Udyog whitepaper

April 2013

EPCG Scheme (Export Promotion Capital Goods)

Recently there have been significant changes in the EPCG scheme. In February 2013 the post-export variant was introduced; and in April 2013 a new zero duty EPCG scheme was announced as part of the annual supplement to the 2009-14 Foreign Trade Policy. We shall look at the latest version of the EPCG scheme, from the standpoint of central excise and customs duties.

What is EPCG

The export promotion capital goods (EPCG) scheme is a scheme under the Foreign Trade Policy that enables import of capital goods against an authorization issued by the Directorate General of Foreign Trade (DGFT) under the Ministry of Commerce. The different variants of this authorisation enable import of the said capital goods for use in manufacture of goods or provision of services for export -

- at zero import duty,
- at concessional import duty (in earlier versions of the scheme), or
- on payment of duty against which post-export duty remission scrip will be issued upon completion of export obligation.

In the earlier version of the scheme (which is still operative for those who hold authorisations taken before 18 April 2013), the rate of duty was zero for specified sectors, and 3% for others. In the new scheme, available from 18 April 2013, EPCG in its duty-exemption avatar is a complete waiver of import duties. In other words, for new applicants there is now only either zero duty EPCG or post-export EPCG. Both are conditional on completion of the stipulated export obligation. Waiver of CVD is optional: the importer can choose to pay it and have his export obligation correspondingly reduced by excluding it from the calculation of duty saved.

The three extant variants of the EPCG scheme now are -

i. Pre-export zero duty / 3% duty EPCG. For applicants after 18 April 2013 this is available only in the zero duty version;
ii. EPCG for annual requirement: in this variant, a status holder who has export performance in the preceding two years gets an annual entitlement of duty-free EPCG imports up to 50% of the value of exports made, whether of goods or services or even deemed export as defined in chapter 8 of the Foreign Trade Policy. In physical exports, the 50% is worked out on the FOB value, and for deemed exports it is worked out at 50% of the FOR value. A status holder refers to an exporter recognised as export house / trading house / star trading house/ premier trading house by the DGFT or by the Development Commissioner of an SEZ.
iii. Post-export duty credit EPCG scheme: in this variant of the EPCG scheme, customs duties are paid on import of capital goods, and thereafter freely transferable duty credit scrips are issued. The export obligation is less in this (see below).

How the post-export EPCG scheme works

In post-export EPCG, the importer is issued an authorisation, against which he makes import of capital goods, <u>on which he pays the full customs duties</u>. He then proceeds to fulfil the export obligation. For this variant of the EPCG scheme, the export obligation is fixed at a lower level, i.e., at 85% of the specific export obligation that would have been normally fixed by taking into account the customs duties on the imported goods. <u>Upon fulfilling the export obligation, the authorisation-holder is issued with duty remission scrips of a value equivalent to the import duty paid.</u> These can be used for duty-free imports. They are freely transferable.

If the export obligation is not completed, duty credit scrip can be issued for exemption of duty in proportion to the proportion of export obligation that has been completed. There can thus be a series of such scrips, issued as the export transactions progress.

Customs duty notifications

The zero duty or concessional duty promise of an EPCG authorisation is operationalized by customs duty exemptions, exempting customs duty on eligible capital goods imported against an EPCG authorisation. For each version of the EPCG scheme under different issues of the Foreign Trade Policy there is a separate notification. These remain extant, even well after the period of export obligation under the respective licence / authorisation is over, presumably to facilitate legal action against defaulters. Thus, the extant customs duty exemption notifications pertaining to various versions of the EPCG scheme are:
160/1992-Customs dated 20 April 1992,
307/1992-Customs dated 28 December 1992,
122/1993-Customs dated 14 May 1993 (for services sector)
110/1995-Customs dated 5 June 1995 (15% duty), under the EXIM Policy 1992-97,
111/1995-Customs dated 5 June 1995 (nil BCD and 10% additional duty), under EXIM Policy 1992-97
130/1995-Customs dated 25 August 1995 (nil duty for components imported for manufacture of capital goods for EPCG holder), under EXIM Policy 1992-97
28/1997-Customs dated 1 April 1997 (10% duty), under EXIM Policy 1997-2002
29/1997-Customs dated 1 April 1997 (nil BCD and 10% additional duty), under EXIM Policy 1997-2002
44/2002-Customs dated 19 April 2002 (5% duty), under EXIM Policy 1997-2002
55/2003-Customs dated 1 April 2003 (5% duty), under EXIM Policy 2002-2007
97/2004-Customs dated 17 September 2004 (5% duty), under Foreign Trade Policy (FTP) 2004-2009
64/2008-Customs dated 9 May 2008 (3% duty), under FTP 2004-2009
136/2008-Customs dated 24 December 2008 (3% duty for Common Service Providers), under FTP 2004-2009
100/2009-Customs dated 11 September 2009 (3% duty for Common Service Providers), under FTP 2004-2009
101/2009-Customs dated 11 September 2009 (nil duty for Common Service Providers), under FTP 2009-14
102/2009-Customs dated 11 September 2009 (nil duty EPCG), under FTP 2009-2014
103/2009-Customs dated 11 September 2009 (3% EPCG), under FTP 2009-2014
5/2013-Customs dated 18 February 2013 (nil duty post export EPCG), under FTP 2009-2014
6/2013-Customs dated 18 February 2013 (3% duty post export EPCG), under FTP 2009-2014

The latest versions of the EPCG are covered by notifications 22/2013-Customs dated 18 April 2013 (new zero duty EPCG), and 23/2013-Customs (new post-export EPCG) under FTP 2009-14;

Who is eligible for the EPCG scheme?

The following categories of persons are eligible for the EPCG scheme:

- Manufacturer-exporters
- Manufacturers tied to supporting vendor(s)
- Merchant exporters tied to supporting manufacturer(s) (whose names are to be entered in the EPCG authorisation)
- Retailers who have minimum area of 1000 sq metres
- Exporters of service
- Common service provider (CSP) in towns of export excellence, who provide service to exporters.

What can be imported / domestically sourced

The following can be imported under the EPCG scheme, subject to the definitions and conditions in the note given below the list:

- Capital goods (including such goods in CKD or SKD condition, and computer software systems), for pre-production, production and post-production,
- Spares (including reconditioned or refurbished spares),
- Tools,
- Moulds, dies, jigs, fixtures,
- Refractory for initial lining.

The same items can also be sourced domestically against an EPCG authorisation, in which case the supplier is entitled to the benefit of deemed export under the Policy. The specific export obligation is 10% less in domestic sourcing than in import.

Cars are no longer allowed for import under EPCG; but are allowed under the Served from India scheme.

Note to list of eligible items

<u>Capital goods definition</u>

It may be noticed that the eligible items for import are specified as capital goods 'for pre-production, production or post-production', which seems to leave some ambiguity regarding capital goods for provision of services. However, the definition of 'capital goods' in the Policy specifically includes such goods used in the services sector. Therefore we may read 'production' as including production of services.

'Capital goods' are defined in paragraph 9.12 of the Foreign Trade Policy as follows:

"Capital Goods" means any plant, machinery, equipment or accessories required for manufacture or production, either directly or indirectly, of goods or for rendering services, including those required for replacement, modernisation, technological upgradation or expansion. It includes packaging machinery and equipment, refractories for initial lining, refrigeration equipment, power generating sets, machine tools, catalysts for initial charge plus one subsequent charge, equipment and instruments for testing, research and development, quality and pollution control. Capital goods may be for use in manufacturing, mining, agriculture, aquaculture, animal husbandry, floriculture, horticulture, pisciculture, poultry, sericulture and viticulture as well as for use in services sector.

<u>Capital goods must be new</u>: Second hand capital goods are not allowed under the EPCG scheme, except for spares (see below).

Spares, tools, moulds, dies, jigs, fixtures: (ia) These are allowed duty-free import at 50% of the normal export obligation up to a value that is 10% of the value of the plant and machinery imported under the EPCG scheme (CIF in both cases). If the plant and machinery was not imported under EPCG, then the 10% ceiling for spares etc is worked out on the basis of the book value of the plant and machinery. (ii) Over and above the 10% ceiling, *spares* are allowed duty-free import with full export obligation. (iii) Second hand *spares*, refurbished or reconditioned, are allowed to be imported under the EPCG scheme.

Actual user condition

The capital goods imported under the EPCG scheme are subject to actual user condition in the Foreign Trade Policy as well as in the customs exemption notifications. They must be used by the importer (or his supporting manufacturer) and not sold or transferred or disposed of in any way till the export obligation under the scheme is completed. Further, in the case of specified sectors [listed at under the section “Export Obligation”], the imported items are not allowed to be transferred for five years even if the export obligation has been completed; however, transfer to group companies is permitted, under intimation to the Regional Authority of the DGFT and to the jurisdictional central excise authorities.

Other schemes

The benefit of zero duty EPCG scheme is not available to persons who have, in the same year, availed benefit of the Status Holder Incentive Scheme, unless they surrender or refund the same with interest.

Availment of benefit of drawback, advance authorisation, DFRC or DFIA or other incentive schemes is, however, permitted for the same export consignments.

Procedure for import

Registration & bond

The EPCG authorisation has to be registered with the Commissioner of Customs at one of these designated ports for import under the scheme, and the importer has to furnish a bond binding himself to fulfil the export obligation and the other conditions of the exemption. If the importer is a Common Service Provider in a 'Town of Export Excellence' (as specified in the FTP), he has to furnish a bank guarantee in addition to the bond. The bank guarantee must cover 100% of the duty saved. It can be given by the Common Service Provider or any of his users or a combination thereof.

Redeeming the bond

The bond is redeemed by presentation of a certificate from the DGFT that the export obligation has been discharged. (This is commonly referred to as EODC – export obligation discharge certificate.)

Nexus certificate

In the case of EPCG for annual requirement, the authorisation (scrip) must indicate the product to be exported. At the time of import of capital goods under the authorisation, the importer must furnish to the customs authorities a nexus certificate from an independent chartered engineer showing nexus of the capital goods to the export product; and a copy of the same has to be given to the DGFT Regional Authority with copy of the bill of entry within 30 days of import. The format of this certificate is given as Appendix 32A to the Handbook of Procedures. It, inter alia, requires a flow chart of the process and identification of where exactly in this process the imported capital goods will be used.

Time-limit for using EPCG scrip

An EPCG authorisation is valid for 18 months from the date of issue, to provide customs duty exemption for the imported capital goods.

Designated ports

Import under the scheme is allowed only through designated ports. These ports are listed in the relevant customs exemption notifications. Under notifications 22/2013-Customs (exemption for import against the new zero duty EPCG scrip)and 23/2013-Customs (exemption for import against zero duty post-export EPCG scrip), the designated ports are listed as follows:

1. Seaports: Bedi (including Rozi-Jamnagar), Chennai, Cochin, Dahej, Dharamtar, Haldia (Haldia Dock

complex of Kolkata port) Kakinada, Kandla, Kattupalli (Tamilnadu), Kolkata, Krishnapatnam,

Ennore (Tamilnadu) and Karaikal (Union territory of Puducherry), Magdalla, Mangalore,

Marmagoa, Muldwarka, Mumbai, Mundhra, Nagapattinam, Nhava Sheva, Okha, Paradeep,

Pipavav, Porbander, Sikka, Tuticorin, Visakhapatnam and Vadinar.

2. Airports: Ahmedabad, Bangalore, Bhubaneswar, Chennai, Cochin, Coimbatore, Dabolim (Goa), Delhi,

Hyderabad, Indore, Jaipur, Kolkata, Lucknow (Amausi), Mumbai, Nagpur, Rajasansi

(Amritsar), Srinagar, Trivandrum, Varanasi and Visakhapatnam.

3. Inland Container Depots: Agra, Ahmedabad, Anaparthy (Andhra Pradesh), Babarpur, Bangalore, Bhadohi, Bhatinda, Bhilwara, Bhiwadi, Bhusawal, Chettipalayam (Tamilnadu), Chheharata (Amritsar), Coimbatore, Dadri, Dappar (Dera Bassi), Daulatabad (Wanjarwadi and Maliwada), Delhi, Dhannad Rau (District Indore), Dighi (Pune), Durgapur (Export Promotion Industrial Park), Faridabad, Garhi Harsaru, Gauhati, Guntur, Hyderabad, Irugur Village (Tamilnadu), Irungattukottai (SIPCOT Industrial Park, Kattrambakkam Village, Sriperumbudur Taluk, Kanchipuram District,

Tamilnadu), Jaipur, Jallandhar, Jamshedpur, Jodhpur, Kanpur, Karur, Kheda (Pithampur, District Dhar), Kota, Kundli, Loni (District Ghaziabad), Ludhiana, Madurai, Malanpur, Mandideep (District Raisen), Marripalem Village (in Edlapadu Taluk of District Guntur), Miraj, Moradabad, Nagpur, Nasik, Patli (Gurgaon), Pimpri (Pune), Pitampur (Indore), Pondicherry, Raipur, Rewari, Rudrapur (Nainital), Salem, Singanalur, Surat, Surajpur, Talegaon (District Pune), Thudiyalur (Tamilnadu), Tirupur, Tondiarpet (TNPM) in Chennai, Tuticorin, Udaipur, Vadodara, Varanasi, Veerapandi (Tamilnadu) and Waluj (Aurangabad).

4. Land Customs Stations:Agartala, Amritsar Rail Cargo, Attari Road, Changrabandha, Dawki, Ghojadanga, Hilli, Jogbani, Mahadipur, Nepalganj Road, Nautanva (Sonauli), Petrapole, Ranaghat, Raxaul, Singhabad and Sutarkhandi.

However the Commissioner of Customs may, by special order or public notice, and subject to conditions that he may specify, allow the import through any other port in his jurisdiction.

Installation certificate

The capital goods imported under EPCG must be installed in the factory or premises of the importer within six months from the date of import. An installation certificate evidencing this has to be obtained from the jurisdictional Deputy Commissioner / Assistant Commissioner of Central Excise and furnished to the Deputy Commissioner / Assistant Commissioner of Customs at the port of import. If the importer is not registered with central excise, or is a service provider, a certificate from an independent chartered engineer will suffice

Export obligation

How EO is fixed

Export obligation under the new zero duty EPCG scheme is six times the duty saved on the import, or such higher sum as may be fixed by the DGFT under paragraph 5.10 of the Foreign Trade Policy. Export obligation calculated in this manner must be over and above the average level of exports achieved in the preceding three licensing years for the same and similar products (not including exports under EPCG). However this stipulation of maintaining average level of exports does not (with some exceptions) apply to export of goods relating to handicrafts, handloom, cottage & tiny sector, agriculture, aquaculture (including fisheries) & pisciculture, animal husbandry, floriculture, horticulture, poultry, viticulture, sericulture, carpets, coir or jute. Within these sectors, the exceptions requiring maintenance of average level of exports are import of fishing trawlers, boats, ships and other similar items.

For import of spares, tools, moulds, dies, jigs, fixtures and refractory for initial lining, the export obligation is 50% of the normal export obligation upto a value that is 10% of the value of the plant and machinery imported under the EPCG scheme (CIF in both cases). If the plant and machinery was not imported under EPCG, then the 10% ceiling for spares etc is worked out on the basis of the book value of the plant and machinery. Over and above this 10% ceiling the export obligation is fixed as for machinery.

For post-export EPCG credit scrips, the specific export obligation of the person who imports capital goods under exemption is 85% of the normal export obligation. Average EO, however, remains unchanged.

For capital goods sourced domestically, the specific export obligation for the value of goods so sourced is reduced by 10 per cent.

For units located in Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, and Jammu & Kashmir, the specific EO shall be 25% f the normal EO; however there will be no change in average EO.

How to compute and show EO fulfilment

Export obligation is fulfilled by export of goods manufactured by or services rendered by the authorisation holder. This includes goods manufactured by a supporting manufacturer of a merchant exporter.

Common service provider has to show completion of export obligation through the shipping bills of its users. For this purpose the Regional Authority of the DGFT must be informed about the users prior to the export. The shipping bills must contain the EPCG reference of the CSP.

The following are included for EO fulfilment:

- Physical exports, including exports under advance authorisation, DFRC, DFIA, drawback scheme, or incentive schemes under chapter 3 of the Foreign Trade Policy.
- Supply of ITA-1 items to the DTA, if the realisation is in free foreign exchange;
- Deemed exports under paragraph 8.2 (a), (b), (d), (f) and (j) of the Foreign Trade Policy, namely,
    - supply of goods against advance authorisation (including advance authorisation for annual requirement);
    - supply of goods to EOU/ STP/ EHTP/ BTP;
    - supply of goods to projects financed by the IBRD and IDA, International Fund for Agricultural Development, Asian Development Bank, OPEC Fund, yen credit channelized through Japan International Cooperative Agency for development, or Swedish International Development Agency under international competitive bidding, where the legal agreements provide for tender evaluation without including customs duty component;
    - supply and installation of goods under turnkey contract to projects financed as above, where the bids may have been invited and evaluated on the basis of Delivered Duty Paid (DDP) prices for goods manufactured abroad;
    - supply of goods to any project or purpose in respect of which notification 12/2012-Customs allows import of goods at zero customs duty subject to the conditions specified therein;
    - supply of goods to nuclear power projects through competitive bidding (as opposed to international competitive bidding): this covers only the items specified in list 33, serial number 511 of notification 12/2012-Customs, for setting up a nuclear power project.

- Royalty payments received by the EPCG authorisation holder in freely convertible currency and foreign exchange received for R&D services;
- Payment received in rupee terms for port handling services.

Block years for EO fulfilment

The export obligation is to be completed in two blocks: 50% of it is to be completed within the first to fourth year, and the remaining 50% is to be completed in the fifth and sixth years. Excess in the first block can be set off against the next block.

Incentive for early fulfilment of EO

If an importer completes 75% of the export obligation (both specific and average) in half the time allowed, the remaining export obligation is waived.

Sourcing capital goods indigenously

EPCG scrip can be used for domestic sourcing

Capital goods can be obtained from indigenous sources against the EPCG authorisation, by either purchase or lease. In the case of lease, the bill of entry (if the goods are imported) or the commercial invoice (if the goods are indigenous) must be jointly signed by the EPCG holder and the leasing company.

To encourage domestic sourcing of capital goods, the specific export obligation is reduced by 10% for the value of such goods. The supplier is entitled to the benefits of deemed export under chapter 8 of the Foreign Trade Policy, which consists of deemed export drawback and terminal excise duty refund.

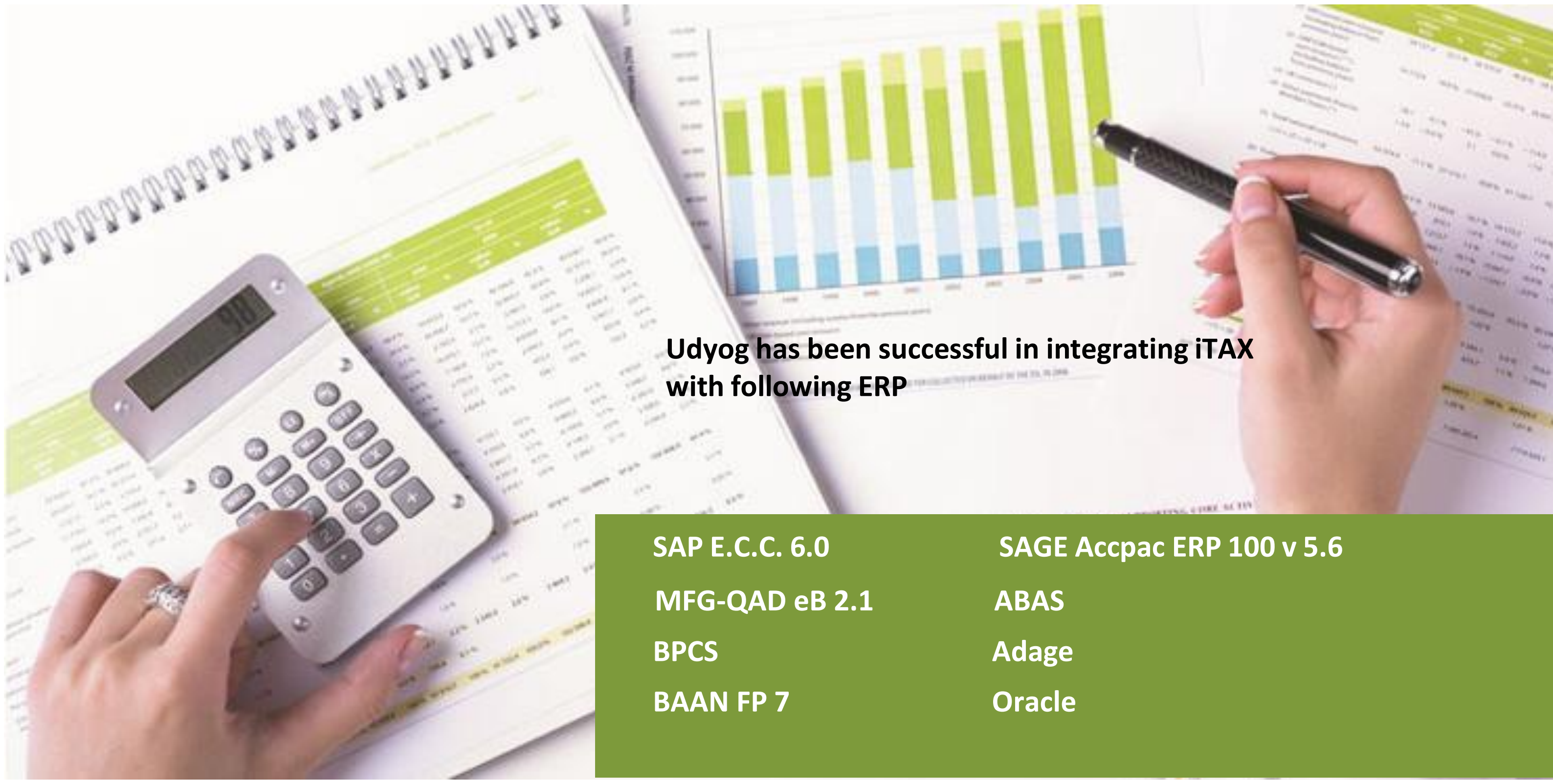
As an alternative to terminal excise duty refund for the supplier, the scrip holder may avail Cenvat credit of excise duty paid, or may claim the terminal excise duty refund himself upon obtaining a disclaimer from the supplier in the prescribed format.

Excise exemption for post-export EPCG

The exemption from excise duty for supply to a post-export zero duty EPCG authorisation holder is available under notification 2/2013-CE dated 18 February 2013, which exempts basic as well as additional duties of excise for such supplies, subject to certain conditions and procedure. (Similar exemption for the 3% EPCG variant is available under notification 3/2013-CE.) Under this notification, the holder of the scrip, including a transferee-holder, is required to

- present the scrip to the customs authorities at the port at which the scrip is registered, with a letter or pro forma invoice of the proposed domestic supplier of capital goods, which indicates details of the goods and also the central excise office having jurisdiction over the said supplier.
- If the scrip is valid (which is for 18 months from issue), the officer will debit the amount of duty exempted, note it in his records, and send written communication of this to the said central excise office.
- The holder of the scrip will present the scrip to the central excise officer with an undertaking to pay any short-debited amount with interest.
- Thereupon the central excise officer will validate the customs officer's debit of duty amount on the scrip, make an entry in his own records, and return the scrip to its holder. The manufacturer-supplier of the goods will retain a copy of the scrip (so debited) for his record.

[*This piece highlights the main features of the scheme. For full information, the reader must peruse all the notifications mentioned above, as well as chapter 5 of the Foreign Trade Policy and of the Handbook of Procedures, along with the relevant Aayaat Niryaat Forms and Appendices.*]



Udyog has been successful in integrating iTAX with following ERP

SAP E.C.C. 6.0	SAGE Accpac ERP 100 v 5.6
MFG-QAD eB 2.1	ABAS
BPCS	Adage
BAAN FP 7	Oracle

Updated and written by **Radha Arun,**
Consultant to Udyog Software (India) Ltd.

Visit www.udyogsoftware.com
Call us on - 022-67993535

sales@udyogsoftware.com | www.udyogsoftware.com

Udyog Software (India) Ltd
www.udyogsoftware.com
Phone: 022-67993535
Email: sales@udyogsoftware.com