Pre-Budget Memorandum 2016-17

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Annexure I

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Petroleum Federation of India

PRE-BUDGET MEMORANDUM FY 2016-17: SUGGESTIONS

Direct Taxes

Corporate Tax

1. Deduction under Section 35AD of the Income Tax Act

Background

i) Under section 35AD of Income Tax Act, 100% deduction in respect of capital expenditure incurred (other than land, goodwill and financial instrument) prior to commencement of operation of the specified business is allowed to the assessee engaged in laying & operating a cross-country Natural Gas/Crude/Petroleum pipeline network for distribution.

ii) Section 35AD (1A) provides that where the specified business is of the nature referred in following sub clauses of sub section 8(c) of Sec 35AD -

- i) Setting up and operating a cold chain facility;
- ii) Setting up and operating a warehousing facility for storage of agricultural produce;
- v) building and operating , anywhere in India, a hospital with at least 100 beds for patients;
- vii) Developing and building a housing project under a scheme for affordable housing framed by Central Government or a State Govt, as the case may be, notified by the Board in this behalf in accordance with the guidelines as may be prescribed;
- viii) Production of fertilizer in India

and the operation has commenced on or after 01.04.2012, deduction of an amount equal to one and one half times of expenditure(i.e. 150%) under sec 35 AD (1) shall be allowed.

Similar deduction of 150% should be allowed to the specified business of laying and operating a cross country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network covered under sub clause (iii) of subsection

8(c) of Section 35AD of the Act as natural gas pipeline industry is in the infrastructure sector.

Section 70 provides that in case of loss under any head of income (other than head of Capital gain), assessee is entitled to set off such loss from any other source of income under the same head. Therefore loss from one business can be set off from profits of other businesses.

However section 73A provides that loss computed under sec 35AD will be set off only against profits & gains of Specified Business and Specified Business inter alia includes business of laying and operating a cross-country natural gas (laid after 01.04.2007) or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network. This restricts the claim for adjustment of loss from profits of other income which is allowed otherwise in all other cases. This discrimination needs to be removed.

Further Section 72A needs to be amended suitably so that in case of amalgamation or demerger of a company accumulated loss in specified business (u/s 35AD) of amalgamating company or demerged company shall, where such loss of specified business (u/s 35AD) is directly relatable to the undertakings transferred to the resulting company, be allowed to be carried forward and set off in the hands of the resulting company

Suggestion

i) A deduction of 150% should be allowed u/s 35AD to the specified business of laying and operating a cross country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network covered under sub clause (iii) of subsection 8(c) of Section 35AD of the Act as allowed to the other specified businesses mentioned above.

ii) In the initial 3 to 4 years there may be no profit in Specified Business of an assessee. Therefore section 73A appears to be restrictive and unfair to the assessee. It is suggested to allow set off of loss under section 35AD against profits of any other business carried on by the assesse as provided under section 70 of the Act.

iii) Section 72A needs to be amended so that carried forward loss of specified business (u/s 35AD) of a demerged company or amalgamating company is allowed to be carried forward and set off in the hands of the resulting company in case of demerger or amalgamation.

2. **Section 35 (2AB) - Weighted Deduction on R&D Activities for Bio-fuels**

Background

The Finance bill 1997 introduced sub section (2AB) in Section 35 of Income Tax Act 1961 allowing a deduction of 200% of the expenditure to encourage Research & Development (R&D) initiatives by the Industry and to make R&D an attractive proposition. Though, such expenditure needs to be approved by the prescribed authority (Secretary, DSIR).

Suggestion

It is suggested that any expenditure incurred on Bio- Fuel activities should also qualify for a deduction of 200% under Section 35(2AB) in order to promote investment/ R&D initiatives for renewable/ non-conventional energy sources.

3. **Benefit of Section 80IA to be extended to 'Gas projects'**

Background

In order to cater the nation's energy requirement for industry, CGD, Power sector, Refineries etc., India is in need of Natural Gas. In Union Budget speech of 2012-13, Oil and Gas / LNG storage facilities and oil and gas pipelines have been recognized as 'Infrastructure' and declared eligible for Viability Gap Funding (VGF) under PPP. Similar eligibility should be given to PSUs like IOCL for undertaking oil and gas pipelines projects for captive use.

The definition of Infrastructure facility under explanation to section 80-IA(4) read with Circular no. 793/2000 dated 23.06.2000 include a port including structures at port for storage, loading and unloading etc. upon fulfillment of conditions. Natural Gas is imported in liquefied form for which storage and/or unloading facility is built at the port.

Suggestion

In order to promote import of LNG, LNG facility at port location may also be included in the definition of "Industrial Infrastructure" in section 80-IA of Income Tax Act 1961.

4. **Deductions in respect of Exploration & Production Business**

100% Deduction u/s 80IB in respect E&P business is allowed to an undertaking for a period of 7 years in case such undertaking-

i) is located in any part of India and has begun or begins production of Mineral oil on or after the 1st day of April 1997.

(provided that the provisions of this clause shall not apply to blocks licensed under a contract awarded after 31st day of March,2011under NELP dated 10.02.1999 announced by Govt. of India or in pursuance of any law for the time being in force or by the Central or state Govt. in any manner).

ii) is engaged in commercial production of natural gas in blocks licensed under the NELP-VIII and begins commercial production of natural gas on or after 01.04.2009;

iii) is engaged in commercial production of natural gas in blocks licensed under IV round of bidding for award of exploration contracts for coal bed methane blocks and begins commercial production of natural gas on or after01.04.2009.

Suggestion

i) Amendment should be made u/s 80IB to include natural gas within the definition of mineral oil for the purpose of admissibility of tax holiday for production of natural gas from all blocks (including CBM) retrospectively ;

ii) Tax Holiday u/s 80IB for E&P undertaking should be allowed for a period of 10 years out of 15 years from date of commencement of commercial production in line with deduction u/s 80IA.

Indirect Taxes

Central Sales Tax

5. **Include Natural Gas and LNG as 'Declared Goods' under CST Act**

(i) Under Chapter IV (Section 14) of Central Sales Tax (CST) Act, 1956 which deals with the 'Goods of special importance in inter-state trade or commerce', most of the fuels such as Coal, Crude Oil, Liquefied Petroleum Gas for domestic use (LPG) have been notified as "Declared Goods' on which Sales Tax of more than 5% cannot be levied/charged in any State irrespective of where the product is sold.

(ii) However, Natural Gas and LNG, which are clean fuels, have not been notified as "Declared Goods" under section 14 of the CST Act. As a result, there is no uniformity of VAT/ Sales Tax in the different states (e.g. Natural Gas is subjected to VAT in Gujarat 15.5%, Andhra Pradesh 14.5% and Tamil Nadu 5%). Many State Governments have levied very high rates of VAT/ Sales Tax on Natural Gas, thereby increasing the delivered price of Natural Gas to customers at unaffordable level. Further, in case of fertilizer sector, high level of Sales Tax only increases extent of subsidies from Government of India. There is, therefore, an urgent need to bring down the Sales Tax/VAT rates to uniform and affordable levels.

(iii) Natural Gas is the feed-stock for vital industries such as fertilizer and source of fuel for power sector. Natural Gas is a clean gas and termed as energy of the future. Importance of Natural Gas in the country is likely to increase due to increase in production of Natural Gas in the coming years. Further, its importance in Inter-State trade is also likely to increase due to the national natural gas grid.

(iv) Recognizing the shortage of Gas, Government has encouraged import of LNG. Since Natural Gas and LNG fall in the same logical category as Crude Oil and Coal, they must have the same level of taxation as applied to Crude Oil.

Suggestion

In view of above, it would be justified to notify Natural Gas and LNG as 'Declared Goods'.

6. **ATF to be given status of declared goods under CST Act**

Background

As the Govt. is keen to promote domestic tourism being a key determinant in attracting international tourists and business into India, the Aviation industry plays a vital role in this regard. It is well recognized that the prices of ATF is a major concern for the Aviation industry being a key cost component in the operation of Airlines.

As regards availability, there is surplus ATF available in India after meeting the entire demand of all the Airlines including Civil, Defence and International customers. India is net exporter of ATF. In 2013-14, India's export of ATF was 7343 TMT (Source- DGFT website). ATF is presently exported by M/s RIL and M/s MRPL. The availability of ATF in the country

will further improve after commissioning of Paradip Refinery of IOCL and may result into higher export of ATF.

However, inspite of domestic availability of ATF, the levy of higher rate of VAT on sale of ATF (largely in the range of 20% to 29%) by most of the State Govts. making such domestic fuel costlier and ultimately resulting in higher prices which leading to import of ATF by the end users. As the basic Custom duty (exempted vide Notification No. 119/2008-Customs dated 31.10.2008) and SAD rate on import of ATF is Nil and also imported product does not attract any Sales Tax/VAT, therefore, cost of imported ATF is become cheaper than domestic ATF due to higher rates of sales taxes on domestic ATF.

Suggestion

Considering the national importance of ATF and to protect the domestic production, it is recommended that ATF be declared as item of special importance under Section 14 of Central Sales Tax Act, 1956 so as to restrict the levy of Sales tax/VAT by State Govt. up to maximum ceiling of 5% or alternatively Customs Duty and SAD duty rates may be restored on import of ATF. The proposal should be examined in the background of Govt. policy of 'Make in India' to boost up the domestic production.

7. **Requirement of special tax treatment for sale of Natural Gas under CST Act, 1956.**

Presently, the domestic gas is available in the state of Gujarat, Maharashtra, Andhra Pradesh, Rajasthan, Tamil Nadu and in a very little quantity in Tripura and Assam. LNG import is possible in the coastal areas like Andhra Pradesh, Kerala, Maharashtra, Gujarat, Tamil Nadu, Orissa and Bengal. The Demand of Natural Gas however exists all across the country to meet the requirement of various sectors like power, fertilizer, City Gas Distribution (for transport and domestic use), Petrochemical, LPG, Steel Industry etc.

To cater this demand, aggregation of the domestic and imported Natural Gas is essential and has to be comingled and transported in the cross country common pipeline network. In the larger public interest, Domestic Natural Gas is presently supplied to the consumers as per allocation and directives given by the Government. The price of domestic gas is also controlled by the Government whereas the imported gas is procured at significantly higher price based on international exchange indices.

The gas produced/available (produced in KG D6) on east coast in AP largely belongs to M/s RIL and the Gas available on west coast largely (produced by ONGC or imported) belongs to GAIL. Gas available from different sources is invariably comingled or needs to be swapped on account of various factors such as:

For co-mingling

i. Cross country pipelines are connected to multiple sources
ii. PNGRB guidelines for common access of pipelines to all suppliers
iii. Nature of commodity requiring economical and safe transportation through pipeline.
iv. Not viable to have pipeline Infrastructure for each source separately

For swapping

i. Connectivity of the consumers to the source of Gas and corresponding contractual arrangement between parties involved
ii. Affordability of the consumers
iii. MOP&NG directions for larger public interest
iv. Optimisation of facilities related to transportation of Natural Gas.

For efficient and equitable distribution of gas from the different sources to the different States, Central Government has issued the guideline for Gas swapping vide MOP&NG order no. (L-12011/10/2011-GP). Even pooling of gas from different sources (pooling of high priced imported gas with low priced domestic gas) is required to supply of gas at reasonable price to different consumers across various sectors. The concept of gas pooling is being actively pursued by MOP&NG also for the most optimal utilisation of Natural Gas.

Till the time Commingling, swapping or pooling of Natural Gas takes place among the gas sources in the same state and Gas belonging to same suppliers, there were no tax implications as it was possible to demonstrate physical movement. However, as a result of extension of the above requirements among the sources located in different states (i.e. AP/ Maharashtra & Gujarat) or gas belonging to different suppliers (i.e. GAIL, RIL etc.), the tax implications are becoming unmanageable.

As per section 3 of CST Act, 1956, sale or purchase of goods is deemed to be in the course of inter-state trade or commerce if the sale or purchase occasions the movement of goods from one state to another. Since the requirement of section 3 stipulates physical movement of goods, it is difficult to comply with this requirement due to reasons explained above

Due to above trends, it has also become difficult to demonstrate physical movement of Gas emanating from each source corresponding to its final delivery/sale to consumers. Since tax treatment under existing VAT/CST

laws is largely dependent on physical movement of goods, it is very challenging to ascertain real tax liability under these circumstances.

Suggestion

With a view to develop cost effective and revenue neutral mechanism for Gas swapping in terms of MOP&NG guidelines as well as to resolve the issues emerging from comingling and pooling of gas, there is a need to make special tax provisions under Central Sales Tax Act, 1956 for facilitating Natural Gas trading such as:

i. Inter-state swapping of Natural Gas between different suppliers is not treated as 'Sale' liable to tax under CST/VAT laws.
ii. Inter-state sale or stock transfer of Natural Gas is allowed based on the contractual movement/ allocation made by the Gas aggregator in common Gas Pipeline Network.
iii. It would be better to exclude gas from the provisions of CST Act, under Section 6(1) of the CST from the levy of CST Act as the rate of tax is only 2% against Form 'C' and the loss of revenue would be marginal compared to the benefits derived by creating a national market for gas.

8. Inclusion of Goods required for Natural Gas Pipeline Network in the category of Goods eligible for concessional CST against form C

Under Section 8(1)(b) read with section 8(3) and 8(4) of CST Act, the concessional VAT of 2% is applicable on inter-state sale of goods used for certain specified purposes against issuance of form C. The goods used for telecommunication network were specified for the purpose w.e.f. 13.05.2002. Laying of cross country pipelines including connecting gas source to ultimate consumers is a priority in the course of developing National Gas Grid announced in the last budget. As the goods required for use in Natural Gas pipeline network are still not covered, Natural gas transmission companies(like GAIL) are not able to issue form C for purchase of goods for pipeline network at concessional tax of 2%.

Since PNGRB regulated tariff is applicable to the pipeline network being expanded by GAIL across the country, it will in the interest of the consumers in particular, if the capital cost of the pipeline is reduced. Eligibility of pipeline transmission projects for inter-statement procurement of goods against form C will enable reduction in project cost which will ultimately benefit the consumers.

Suggestion

Considering the importance of Natural Gas transmission pipeline network for building a national gas grid, it is suggested that the goods required for Natural Gas pipeline network should be included in eligible category of goods under section 8(1)(b) read with section 8(3) of CST Act. This will reduce the capital

cost of Pipe-Line network projects which are capital intensive and have long gestation period. This will ultimately be in the benefit of the consumers. It will benefit the pipeline companies and incentivize the investment in this sector by way of reduction in capital cost.

CUSTOM DUTY

9. Full exemption to be granted on Liquid and Gas pipelines projects covered under chapter 98

Background

Liquid (crude oil & petroleum products) and Natural gas pipeline projects have been notified as Project imports under Chapter heading 98.01 at Entry no.33 of Notification no.42/96-Cus, dated 23.07.96 as amended. Further, vide entry no.510 of the Notfn No.12/2012-Cus, dated 17.03.12 as amended, all goods under chapter heading 98.01 are leviable to 5% customs duty.

Considering that these projects are capital intensive in nature and important for country's energy security, there is a need to grant exemption from levy of customs duty on these projects.

Suggestion

It is suggested that present customs duty being levied at 5% should be reduced to Nil on Liquid as well as Gas pipelines projects covered under chapter 98.01.

10. Zero Customs Duty on Imported equipments, machinery and other material required for substantial expansion of refining capacity

Oil Companies in India have made strategic plans to expand refining capacity to achieve the ambitious targets set out for the next 5 years. They are in the process of implementing integrated refinery expansion projects at their Refineries which envisages expansion of the Refining capacity. Such projects result in substantial expansion of refining capacity (i.e. expansion of more than 25% of their existing capacity). The critical component of the project is as good as setting up of New Refinery with additional capacity and hence the project should be considered for Customs Duty concession/exemption. Further. Massive investments are also planned to upgrade the refineries in order to supply fuels meeting the EURO V/VI environmental norms.

Suggestion

In view of the foregoing, request to issue appropriate Notification under Section 25 of the Customs Act, 1962 to grant exemption by notifying Zero

Customs Duty on imported equipments, machinery and other material required for such projects having substantial expansion of Refining capacity as also for upgrading refineries for meeting environmental norms.

11. **Exemption from payment of Custom Duty on import of Liquefied Natural Gas (LNG).**

LNG is a clean fuel and mainly used in fertilizer and Power sector. Recognizing the shortage of Gas, Government has encouraged import of LNG. Since LNG falls in the same logical category as Crude Oil, they must have the same level of taxation as applied to Crude Oil.

Since custom duty on crude oil has already been made zero, import of LNG presently attracting 5% Custom duty should also be exempt. Through Finance Act 2012, Govt. has exempted levy of Custom duty on import of LNG for Power Sector. However, this exemption should be extended to other sectors also.

Suggestion

Request to grant exemption from payment of Custom Duty on import of Liquefied Natural Gas (LNG) for domestic use.

12. **Customs Duty on Styrene Butadiene Rubber (SBR) under CEPA with South Korea and ASEAN**

Background

Synthetic rubber industry is a key sector of manufacturing and plays a vital role in the country's industrial growth. It plays a complimentary role to natural rubber in Indian rubber industry. The sector supports the vibrant automotive industry with supply of critical raw materials to the tyre industry.

Annual demand for synthetic rubber in India is 650,000 MT and is expected to grow at the rate of 12% per annum. However, benefit of such healthy growth in demand is not being realized by domestic manufacturing sector. While domestic capacities for SBR, PBR and Butyl Rubber are being added, 80% of demand is still met through import. Value of synthetic rubber import exceeds U$ 1.2 billion.

Indian Synthetic Rubber Private Limited (ISRPL), a Joint Venture of Indian Oil Corporation Limited (50%), TSRC Corporation, Taiwan (30%) and Marubeni Corporation, Japan (20%), has implemented and commissioned the Nation's first State of Art Styrene Butadiene Rubber (SBR) plant at Panipat, Haryana based on Butadiene available from Indian Oil's Panipat Naphtha Cracker Complex. Completed at an estimated cost of Rs 958 crore, ISRPL's SBR

project was dedicated to the Nation on 29th November 2013. The project is designed to produce 120,000 MT per annum of high quality Styrene Butadiene Rubber which is currently imported for manufacture of automotive tyres and other applications. This prestigious project is considered as a path breaking venture of national importance since the entire domestic demand is currently met through imports.

There is a Comprehensive Economic Partnership Agreement (CEPA) with South Korea and ASEAN under which the effective Customs Duty on imports from South Korea and ASEAN have been reduced to zero percent. Consequent to this elimination of Duties, the imports from South Korea and ASEAN have surged from 30% to 70-80% thereby restricting the operations of new domestic capacities to about 20% in previous year.

Such low capacity utilization constrains the Refinery & Petrochemical Complexes in the Country to downgrade the available valuable feedstock like Butadiene for alternate use as fuels while the country continues to import Styrene Butadiene Rubber to meet its domestic demand which could have otherwise been produced within the country thereby leading to loss of precious foreign exchange upto USD 500 million per annum.

Suggestion

In view of the above, it is submitted that the Government may kindly consider a review of India-Korea CEPA and India-ASEAN FTA and exclusion of Styrene Butadiene Rubber falling under tariff heading 4002 from all tariff concessions. Alternatively, Govt. should impose Safeguard Duties on import of Styrene Butadiene Rubber under FTA with South Korea & ASEAN. Unless duty protection to ISRPL is considered by the Government of India, survival of this strategic national "Make in India" project would be at stake.

Excise Duty

13. Oil Industries Development Cess [OID]

(i) Oil Industry Development (OID) Cess is levied on Crude Oil produced as a duty of excise under The Oil Industries (Development) Act 1974. OID Cess on crude oil produced from Nomination blocks and pre-NELP Exploratory blocks is presently leviable at Rs. 4,500/MT. However, in case of pre-NELP discovered blocks (e.g. PMT and Ravva), OID Cess is payable as mentioned in respective PSC i.e. Rs. 900/MT whereas OID Cess is exempted in case of NELP blocks.

(ii) OID Cess was last revised from Rs. 2,500/MT to Rs. 4,500/MT w.e.f. 17 Mar'12, when the price of Indian basket of crude was in the range of US$ 110/bbl. Subsequently, crude prices have reduced considerably. During current year FY'16, the average price of Indian basket of crude is US$ 57.83/bbl (till 28 Aug'15) and presently it is hovering around US$ 47/bbl.

(iii) It is pertinent to mention that existing rate of OID Cess of Rs. 4,500/MT works out to the order of US$ 9.52/bbl (considering exchange rate of Rs. 63/$ and BMT factor of 7.5 bbl/MT). It is also pertinent to mention that at current level of crude prices and cost of production, the economic viability of many of the schemes/projects already approved by ONGC is in jeopardy. Therefore, at current level of crude prices, there is an urgent need for review of present applicable rate of OID Cess of Rs. 4,500/MT (equivalent to US$ 9.52/bbl).

(iv) In view of foregoing, it is submitted that at present level of crude price, upstream oil companies are not in a position to absorb presently applicable OID Cess and there is an urgent need for review of the existing rate of OID Cess. It is therefore suggested that keeping in view the volatility in crude prices, it would be prudent that OID Cess may be levied at ad-valorem basis, say @ 8% to 10% on realized price.

Cenvat credit on OIDB Cess on crude.

Since cess is a duty of excise, CENVAT credit should be extended for this cess also.

14. Removal of National Calamity Contingent Duty on Crude Oil @ RS.50/MT

As the Nation was facing a severe drought during 2003, the National Calamity Contingent Duty (NCCD) of Rs.50 per metric tonne was imposed on domestic and imported crude oil, amongst various other goods, in the Union Budget for 2003-04 in order to augment the fund available with the Govt. to provide support to the relief work in the areas affected by natural calamity. It was mentioned in the Finance Bill, 2003 that this new levy will be limited to one year only. Though the Govt. said it was only for one year, they kept on extending it year after year. This levy has put an additional burden on the Oil Refining Companies.

As an interim measure, NCCD should be at least exempted on crude oil imported against Advance Authorisation. Currently, crude oil imported suffers NCCD even if imported under Advance Authorisation. An appropriate Notification could be issued under Section 134 of Finance Act, 2003 read with Section 25 of the Customs Act, 1962 exempting NCCD on crude oil imported against Advance Authorisation.

Suggestion

It is suggested that this additional burden of NCCD imposed on the Oil Refineries may be withdrawn.

15. **Extension of 100% Excise duty exemption to North East Refineries**

Background

The North East Refineries are located in that area mostly on socio political considerations as even today the north eastern petroleum products demand is insufficient to absorb production of these refineries. Due to limited demand, limited crude availability, sub-economic size, high manpower, locational disadvantages and social obligations, it is necessary that these refineries operate and upgrade their units so that they may eventually be in a position to run their own operations economically.

Notification No. 3/2002-CE dated 29.1.2002 was issued in respect of Digboi Refinery followed by Notifications No. 21/2002-CE dated 1.3.2002 & 29/2002-CE dated 13.5.2002, giving 50% of excise duties relief to products produced by all the refineries in the North East keeping in view their economic viability.

In fact, the Standing Committee on Petroleum and Natural Gas in its Sixth Report (2010-11) on Action Taken by the Government on the recommendations contained in the Twenty-Third Report (14th Lok Sabha) on "Oil Refineries-A Critique" has also reiterated to grant 100% excise duty concession to all the refineries in the North East region, till they become profitable.

Suggestion

It is essential that the excise duty concession may be enhanced from 50% to 100% for the long-term sustenance and viability of the North East refineries.

16. **Exemption from Excise, Customs, Service tax etc. for Product Pipeline project from Raxual to Amlekhgunj, Nepal**

Background

The estimated cost of the Project is Rs.275 crore. As per the MOU dated 24.08.2015 signed between Govt of India & Govt of Nepal, Rs. 200 Crore is to be spent by IOCL and Rs.75 crore is to be spent by Nepal Oil Corporation (NOC) for the above project.

It is estimated that out of Rs.200 crore to be spent by IOCL, Rs. 140 Crore would be spent for facilities to be set up in Nepal. In the above referred MOU, the Government of Nepal has ensured to exempt taxes, duties including VAT etc in connection with the project.

Suggestion

It is proposed to provide for exemption of Excise Duty, Customs Duty, Service tax etc on all purchases and services applicable for this project from the Government of India.

Service Tax

17. Scheme for refund of Service Tax incurred on Services consumed by Upstream sector (Exploration & Production of Oil & Gas)

In order to ensure energy security for the economy, the Govt. of India has accorded high priority to the prospecting for and extraction, production of crude, Petroleum oil and Natural gas by formulation of the NELP. The Government has committed itself to exempt from taxation, the activities undertaken under NELP in order to ensure that the entire expenditure incurred by the successful bidders goes towards exploration and production not towards funding Govt. taxes.

In line with the said commitment, the Government has issued appropriate exemption notifications under Customs exempting specified goods imported for petroleum operations. Similarly goods which could be imported at 'nil' rates of customs duty for petroleum operations could also be purchased from indigenous manufacturers thru international competitive bidding, at 'nil' rates of excise duty. The Indigenous manufacturer supplying the said goods against ICB is entitled to full credit of CENVAT on inputs used in relation to the manufacture of the said goods supplied against ICB for petroleum operations. Thus the indigenous manufacturer does not suffer loss of input credit on inputs used for manufacture of goods supplied to E&P entities for use in petroleum operations. Thus, there are no stranded taxes both in the case of imported and indigenous goods used in Petroleum operations.

However the current policy of the Government subjecting the services consumed by the said E & P entities to service tax, drains away a substantial part of the funds committed for exploration, thus reducing the funds available for actually carrying out exploration activities. 'Crude oil' as well as 'Natural Gas' produced under NELP Contracts is not liable to duties of Excise under the Central Excise Act, 1944. Hence, service tax incurred by E & P entities in exploration and production of Crude oil/ Natural Gas end up as "stranded costs", since the said entities cannot take CENVAT CREDIT of service tax incurred on services consumed for exploration

and production of crude oil and/or natural gas.

Since the said levy of service tax is against the spirit of the commitment of Govt. of India in its NELP, there is a need for refund of the service taxes paid on the critical services consumed by the E&P sector.

Suggestion

E&P sector requests that the Government formulate a scheme for "refund of service tax paid by E&P entities" on the services consumed for exploration as well as production purposes.

In the alternative, services provided to E&P companies which are essential for petroleum operations may be "Zero rated", so that there is no stranding of taxes at the hands of service providers.

18. **Exemption of Service tax on deputation of manpower to Government Departments.**

It is a practice of Oil Industry that officers on regular basis with requisite experience are deputed to Government Deparments like PPAC, PCRA, DGHC and Center for High Technology under the control of MOP&NG and the actual costs to the sponsoring Oil PSUs are recovered from them. Keeping in mind that the objective and the purpose of these departments is to assist MOP&NG, we suggest, any deputation to Government or local authorities should be a part of negative list under section 66 D.

Representation to such effect already submitted and duly acknowledged on 14.08.2010 by CBEC.

Goods & Services Tax (GST):

Department of Revenue (DOR) to Recommend to Include Petroleum Products under GST.

While commenting on "First Discussion Paper on GST" Department of Revenue (DoR), Govt of India also recommended that petroleum products including Crude oil and Natural Gas should be under GST which is reproduced herein under:

Quote

Keeping crude petroleum and natural gas out of the GST net would imply that the credit on capital goods and input services going into exploration and extraction would not be available resulting in cascading.

Diesel, ATF and motor spirit are derived from a common input, viz., crude petroleum along with other refined products such as naphtha, lubricating oil base stock, etc. Leaving diesel, ATF and motor spirit out of the purview of GST would make it extremely difficult for refineries to apportion the credit on capital goods, input services and inputs. These products are principal inputs for many services such as aviation, road transport, railways, cab operators etc. As such, these may be levied to GST and in select cases credit of GST paid on these items may be disallowed in order to minimize the possibility of misuse.

Unquote

i. **Recommendation on GST**

a. The Constitutional Amendment Bill should not exclude Crude Oil, MS, HSD, ATF and Natural Gas from the ambit of GST as this would result in substantial stranding of taxes to be absorbed by the Oil & Gas sector. This is due to the fact that inputs, input services to the sector would be subject to GST, the rates of which would be higher than prevailing rates under the current tax regime, but the benefit of input credit would not be available to the excluded products.

b. In case it is decided to exclude certain petroleum products (crude oil, Petrol, Diesel, Natural Gas, ATF) from the ambit of GST, the same should not be in the Constitutional Amendment Bill as it would be extremely difficult to bring these commodities back into GST at an appropriate time in the future, because the same would require another constitutional amendment.

c. The amendment to the Constitution could be confined to empowering Centre and the States for levy of GST on all goods and services. By virtue of this power, the Parliament and State Legislature can decide through taxation laws as to which goods and services should be included or excluded from GST.

d. As envisaged under the Constitutional Amendment Bill, if some petroleum products are excluded from the purview of GST, till the time such products are brought under GST, necessary provision needs to be made under GST law and the existing laws so as to avail full input tax credit and to avoid any stranding of taxes at the hands of the oil companies.

e. To ensure revenue neutrality of States on the implementation of GST, the issue can be addressed as recommended by the 13th Finance Commission,

by allowing the States to levy additional tax, if necessary, without input tax credit on these products in addition to GST, while bringing them within the ambit of GST.

f. Being mined products, Crude Oil and Natural Gas do not attract Excise duty. However, Crude Oil is leviable to OID Cess (Rs. 4500/MT which is about 18% of realized crude price considering Crude price at USD 60/bbl and exchange rate of Rs.55/USD), Royalty (10% to 20%) and NCCD (Rs.50 per MT). Hence, Crude Oil and Natural Gas should be brought under GST and OID Cess & NCCD are to be subsumed under GST so as to avoid additional burden of stranded cost on E&P companies.

As per the first discussion paper presented by the Empowered Committee Of State Finance Ministers and the Constitutional Amendment bill introduced in the Parliament, the basket of petroleum products i.e. Crude oil, MS,HSD and ATF are to be kept outside GST. The Central and state Taxes will continued to be levied at the prevailing rates on these products.

Suggestion:

1. The GST constitutional amendment bill should not specifically exclude Crude, MS, HSD, ATF and natural gas from GST. The bill should only empower State and Centre to tax both goods and services. This is necessary because if the bill is passed in present form, it would need another constitutional amendment to include this product in future which will be difficult.

2. We recommend that the petroleum products should be included in the Goods and Services Tax (GST).

3. Such inclusion would reduce the cascading effect of taxes on the sensitive petroleum products resulting in reduction of price and consequently ease inflation.

4. Inclusion would help to rationalize the indirect taxes structure of the petroleum industry.

5. Inclusion of petroleum products under GST would also avoid complications in credit mechanism. We insist that both Crude and petroleum products viz - Petrol, Diesel and ATF may be included together under GST , i.e. Crude oil should not be included in seclusion while keeping Petrol ,Diesel and ATF out of GST would increase the under recoveries of Input tax credit thereby increasing cost to a considerable extent.

6. Presently, in view of the economic viability of NE refineries, the Govt. has granted 50% excise duty exemption to all the products produced by NE refineries which is further being taken up for 100% duty exemption by Oil refining sector. However, it is not clear whether the benefit would continue to be available on all the products of NE refineries or the same would only be available on products not covered under GST. It is essential that the excise duty concession may be allowed and enhanced from 50% to 100% for the long-term sustenance and viability of the North East refineries.

Clarifications

Income Tax

1. Additional Depreciation under Section 32(1) (iia)

Background

Section 32(1)(iia) of Income Tax Act, 1961 provides that any new plant and machinery which has been acquired and installed after 31 March 2005 by an assessee, engaged in the business of manufacturing or production of any article or things, is eligible for additional depreciation.

The Assessing authority has been disallowing such additional depreciation on new machinery installed during the year on the ground that, both acquisition and installation should be in the same financial year to claim additional depreciation. Therefore, a case where the erection and construction of machinery is covered in more than a year and transferred from construction work in progress is being disputed for allowing additional depreciation.

It is to submit that nowhere in the section it is stated that new plant and machinery should be acquired and installed in the same year.

A huge investment is required for establishing a new grass root refinery which takes almost three to four years to complete. IOC's mega refinery project at Paradip, which is now at completion stage, was taken up for execution in 2008. Apart from new grass root refinery projects, for other large and complex projects also (which cover supply, construction/ erection, testing & commissioning), it may not be practically possible to acquire and install/ put to use the new plant and machinery in the same financial year.

In order to meet constant growth and expansion of business, IOCL makes substantial investments in new Plant & Machinery and the same is duly eligible for additional depreciation of 20% under section 32(1)(iia) of the Act. Financial impact of tax on additional depreciation may vary from year to year depending upon the capital investment undertaken. The tax impact for 2011-12 & 2012-13 was around Rs.1110 Crs and Rs.240 Crs respectively. This impact would rise substantially due to commissioning of our Paradip Refinery in the coming financial year.

It would be noted from the FM's Budget speech (para 162 & 168) for the year 2005-06 that the condition for enhancement in capacity was done away with and the incentive for additional depreciation was introduced to encourage investments and to ensure equity among all sections of corporate tax payers.

Suggestion

It is requested that suitable clarification may be issued to the field formations so as to avoid any confusion and unnecessary litigations. The section must be interpreted keeping in view the intent and purpose for which it was introduced.

2. **Deduction under Section 35AD to crude oil pipelines**

Background

Section 35AD provides benefit of 100% deduction in respect of whole of any expenditure of capital nature incurred for laying and operating a cross country natural gas or crude or petroleum oil pipeline network subject to the conditions, interalia, that such pipeline network to be approved by PNGRB and has common carrier capacity as per PNGRB regulations.

However, crude oil pipelines has been excluded from the ambit of common carrier for PNGRB approval under Section 2(j)(ii) of the PNGRB Act, 2006. Thus, we are unable to avail the above benefit on the laying & operation of crude oil pipelines.

Suggestion

It is requested that conditions under Section 35AD is to be amended suitably to remove the requirement of approval of PNGRB for crude oil Pipelines.

3. **Deduction under Section 80IB(9) on Refining business**

Background

Section 80-IB(9) allows deduction of 100% of profits for a period of 7 consecutive assessment years to an undertaking which begins refining of mineral oil between 01.10.1998 to 31.03.2012.

IOC's 15 MMTPA capacity mega refinery project at Paradip, Orissa is at an advance state of construction. The above project of IOC was prescribed for the benefit of section 80-IB(9) vide Notification No. 66/2008 dated 30.05.2008. It was initially envisaged that the project would be completed and commissioned before 31.03.2012. However, the completion of this project has been delayed due to various reasons beyond the control of IOC.

This issue was also taken up by MOP&NG with MOF in last year's Union Budget proposals for the oil industry, wherein it was requested to extend

the sunset clause from 31.03.2012 to 31.03.2017. However, the request was not acceded.

Non-availability of such benefit under section 80-IB(9) will affect the economics of the project adversely.

Suggestion

As substantial commitments and expenditure have already been incurred and the delay in the project completion is due to unavoidable circumstances which are beyond the control of the company, it is suggested that the benefit of section 80-IB(9) may be reintroduced for the said project by allowing for project completion date from 31.03.2012 to 30.03.2017.

4. Section 42 - Deduction in case of business of prospecting of mineral oil

Background

Under section 42(1)(a) of the Income Tax Act, deduction for expenditure by way of infructuous or abortive exploration expenses is available in respect of any area surrendered prior to the beginning of commercial production.

As a result of requirement of surrender of the area prior to the beginning of commercial production, the tax payer is not able to avail deduction from taxable income, of expenses on account of abortive exploration expenses in the year when the expenses are incurred. Though, as per the accounting practices, the aforesaid expenses are required to be charged off in the books of accounts.

Further, on reading of section 42 along with the Model Production Sharing Contract, it is not clear whether tax payer is eligible to claim deduction for exploration expenses (including survey expenditure) and drilling expense in the year of incurrence against other business income even though no commercial production has been started.

Moreover, in the event of a farm-in, payment is made towards expenditure incurred on exploration operations in the past (i.e. past costs) along with a premium. The tax authorities deny the deduction by taking a view that, exploration expenses have been incurred by earlier participant (i.e. the seller) and not by buyer of the participating interest and therefore, in section 42 the acquisition costs in India are not deductible.

Suggestion

In section 42(1)(a), words "in respect of any area surrendered" may be deleted for allowing the deduction of expenses in the year of occurrence. It may also be clarified by inserting proviso in Section 42 that tax payer will be eligible to claim deduction for exploration drilling expenses (including survey expenditure) in the year of incurrence against other business income irrespective of fact that commercial production has started or not.

Further non allowable of deduction for farm in cost (past cost plus premium), reduces the activity in this market and is clearly against the interests of expediting exploration. This is despite the fact that income arising out of farming out any interest in the block is taxable in the hands of assignor under Section 42(2). Thus, it is suggested that Section 42 is amended suitably to add a provision for deduction of acquisition (farm-in) expense.

5. **Clarification that eligible profit under Section 80-IB(9) includes Govt. Subsidy and discount on LPG/SKO from upstream companies**

Background

Government of India dismantled the administered price mechanism for petroleum products namely Petrol, Diesel, LPG and SKO w.e.f. April 2002 and the prices were to be based on rates prevailing in international market.

The increase in input cost normally leads to increase in selling price of output. However, due to volatile behavior of prices of petroleum products in international market, in spite of deregulating these products, Govt. of India did not permit Oil marketing companies (OMCs) to fix the selling price in line with the prices prevailing in International market.

As per the Government's directives, OMCs are required to sale SKO meant for public distribution system (PDS) and large quantity of LPG used for domestic consumption, to the consumers at the price fixed by the MoP&NG, Govt. of India.

The selling price of such products is lower than even the raw material cost which resulting into operating losses for the OMCs. Under these circumstances, the MoP&NG, Govt. of India provides subsidy from time to time to recoup products under recovery. Similarly, OMCs are also allowed subsidy and discount on purchase of SKO/LPG from upstream Companies.

Assessing authorities took the view that Govt. subsidy and discount cannot be said to be derived from the business of Refining of mineral oil and

therefore such income is being disputed for eligibility of deduction under section 80IB(9). The financial implication on such issue is around Rs.180 Crores per year.

Suggestion

Govt. subsidy and discount received by the PSUs are nothing but recovery of part of sale price of products sold to customers at discounted price. Therefore, subsidy and discount should be considered as derived from the business of undertaking refining mineral oil.

It may be further noted that section 80-IB(9) uses words "Profit derived from the business of undertaking" as against "Profit derived from an undertaking" as used in section 80HH. Therefore, scope of section 80-IB(9) is wider than section 80HH. The following judicial authorities have also upheld the aforesaid view:

CIT v. Eltek SGS P. Ltd. 300 ITR 6

ACIT v. Maxcare Laboratories Ltd 92 ITD 11 (Cuttack)

In view of the above, for removal of doubts, it may be clarified that subsidy and discount received by public sector undertakings on purchase of SKO/LPG from upstream companies will be regarded as income derived from the business of undertaking and will be eligible for deduction under Section 80-IB(9).

6. Clarification that loss on Sale of Oil bonds is a revenue loss

Background

As per the Government's directives petrol, diesel, SKO through Public Distribution System (PDS) and LPG for domestic use are sold to the consumers at the price fixed by the Govt. of India. The selling prices of such products are lower than the cost and therefore, resulting into operating losses. To compensate these operating losses suffered by OMCs, the GOI issues Special Oil Bonds to the OMCs. Entire amount is offered to tax on receipt of intimation for issue of such special oil bonds by GOI. The Special Oil Bonds issued by GOI have long redemption period ranging from 7 to 17 years. The bonds are issued only in the paper format bearing specified rate of interest and no cash is getting transferred in this regard. Further these special oil bonds do not have any statutory liquidity ratio status thus Banks and Financial Institution are unwilling to buy such bonds and therefore, market demand of these bonds are limited.

GOI Special bonds so received are shown under current asset (current investment) and valued at cost or market price whichever is lower in line

with valuation of stock-in-trade. Accordingly the provision for diminution in bonds value i.e. investment is added back in the computation of total income. Loss incurred at the time of sale of such GOI special Bonds are claimed as revenue loss. However, the Assessing authority is of the view that loss on sale of GOI special Oil Bonds is capital loss as the same is incurred on sale of investment.

GOI Special bonds are based on the scheme as framed by GOI. IOCL has not suo-moto invested in it. Further, had GOI given cash compensation in time or allowed IOCL to charge price and not the subsidized rate, the borrowings would have been reduced to the great extent. GOI Special Bonds are sold primarily to meet the working capital and/ or curb the borrowings.

Suggestion

It is suggested that a suitable clarification to be issued in this regard that Loss incurred at the time of sale of such GOI special Bonds are to be allowed as revenue loss.

7. **Clarification in Section 92BA or in Section 40A(2)(b)(v) to exclude transaction between PSUs**

Background

The transaction of purchase/sale of Crude Oil from M/s ONGC/OIL to IOCL is effected at the prevailing international prices. However, to compensate the loss suffered by IOCL on sale of regulated products, viz., SKO (PDS) and LPG (Domestic), a scheme has been formulated by Government of India through Petroleum Planning & Analysis Cell (PPAC), MoP&NG, under which discount is received by IOCL on Crude Oil/Products purchased from ONGC/GAIL/ OIL/CPCL. The discount thus given by ONGC/GAIL/OIL/CPCL result in reduction of purchase cost, reduction in loss or increase profit on one hand and on another hand it result in reduction of sales of respective companies thus reducing their profit or increase loss.

Companies are required to evaluate international and specified domestic transaction on Arm's Length Price under transfer pricing provisions.

Section 40A(2)(b)(v)

"a company, firm, association of persons or Hindu undivided family of which a director, partner or member, as the case may be, has a substantial interest in the business or profession of the assessee; or any director, partner or member of such company, firm, association or family or any relative of such director, partner or member;"

On plain reading of section 40A(2)(b)(v), the transaction between ONGC and IOCL and with other PSUs including oil marketing companies get covered under provision of transfer pricing. Disallowance is warranted for all transaction not within the Arm's Length Price.

Suggestion

Since, Para 4(c) of Accounting Standard 18 excludes above public sector undertaking from the definition of related party. Hence, suitable explanation / clarification may be issued in Section 92BA or in Section 40A(2)(b)(v) to exclude the above transaction.

Custom Duty

8. **Clarification on non leviability of customs duty on LPG used for non-domestic purposes in locations storing both imported and indigenous LPG in common tankages as long as there is adequate quantity of indigenous LPG in the tanks.**

With effect from 02/05/2005 Customs duty on import of LPG/Butane/ Propane for Domestic PDS purposes has been made 'Nil' vide Notification No. 37/2005 dtd. 02/05/2005. LPG is also produced by our own refineries. At port locations LPG indigenously produced as well as imported is stored in common storage tanks in commingled condition since irrespective of the source, the BIS specification of the product is same. Though LPG is primarily used only for domestic PDS purposes, some minor quantity of LPG is also required for Non domestic purposes. Differential Excise duty is duly deposited for such use by our refineries. LPG plants are duty paid locations and there is no mandatory requirement of maintaining stock records as per FIFO basis for receipts and dispatches.

Customs authorities however have initiated proceedings under the Customs Act on the ground that on the basis of FIFO system some portion of the Imported LPG is also being used for non-domestic purposes and the exemption extended for imports is not applicable, therefore appropriate Custom duty should also be paid for such use inspite of Excise duty having been deposited.

Appropriate clarification should be issued to confirm that since the locations storing LPG are duty paid locations storing imported as well as indigenous LPG in common tankages, there should be no requirement to pay any Customs duty for LPG used for non-domestic purposes as long as there is sufficient indigenous product available at the given time for such use on

which appropriate Excise duty is paid. A representation on this issue is already pending with the CBEC.

9. **Advance Authorisation benefit should be allowed for NCCD paid on crude oil imports.**

All the duties paid under Customs act on import should be allowed under Advance authorization.

10. **Amendment under S. No. 356 of Customs Notification No. 12/2012-Cus dated March 17, 2012 to allow Customs Duty exemption on import of specified goods for petroleum operations in nominated blocks irrespective of date of issuance / renewal PEL / ML.**

(i) Currently, ONGC has 86 Blocks awarded to it under New Exploration Licensing Policy (NELP) of Government of India. S. No. 359 of Customs Notification No. 12/2012-Cus dated March 17, 2012 provides exemption from Customs Duty on import of specified goods (as per List-13 of Notification) required for petroleum operation under NELP blocks, subject to the conditions prescribed.

(ii) Similarly, ONGC has 347 blocks allotted to it on nomination basis where Petroleum Exploration License (PEL) or Mining Lease (ML) have been issued or renewed after April 01, 1999. S.No. 356 of said Notification No. 12/2012-Cus dated March 17, 2012 provides exemption from Customs Duty on import of specified goods (as per List-13) required for petroleum operation undertaken under PEL or ML, as the case may be, issued or renewed after the April 01, 1999 and granted by the Government of India or any State Government to the Oil and Natural Gas Corporation Limited (ONGC) or Oil India Limited (OIL) on nomination basis, subject to the conditions prescribed.

(iii) On domestic sourcing of specified goods under procedure of International Competitive Bidding (ICB) for petroleum operation for NELP Blocks as well as for eligible PEL/ML area, Excise Duty is exempted in terms of Excise Notification 12/2012-Ex dated March 17, 2012, S. No. 336.

(iv) Therefore, the import of specified goods required for petroleum operation in 86 NELP blocks and 347 nominated blocks (referred as Eligible Blocks herein-after) as indicated above are exempted from payment of Customs Duty and also from payment of the Excise Duty if such goods are purchased against ICB.

(v) In addition to aforesaid blocks (86 + 347), ONGC has 54 blocks issued to it on nomination basis where PEL or ML have been issued or renewed prior to April 01, 1999 (referred as Non-Eligible Blocks herein-after). Consequently, the import of specified goods required for petroleum

operations in these 54 nominated blocks are subject to levy of Customs Duty and also Excise Duty.

(vi) It is pertinent to mention here that there is no significant financial implication to Govt. as far as duties on such Non-eligible Blocks are concerned. However, due to non-availability of exemption from payment of Custom Duty in respect of the Non-Eligible Blocks, ONGC is facing acute operational difficulties, additional cost and compliance issues.

(vii) ONGC has to follow different methodology for purchase of specified goods, hiring of Rigs, and other equipment for Eligible Blocks and Non-Eligible Blocks. This makes evaluation process complicated and at time it has been noticed that the bidders try to take advantage of the situation by inflating their rates while quoting for Eligible Blocks where Customs Duty exemption is available. Further, inviting separate tenders for Eligible Blocks and Non-Eligible Blocks ONGC loses volume discount, in addition to cumbersome and time consuming process of tender finalization.

(viii) ONGC has to maintain separate inventory of specified goods in respect of Eligible Blocks and Non-Eligible Blocks. This leads to higher inventory carrying cost and is also a drain on valuable foreign exchange.

(ix) ONGC has to hire costly equipment like drilling rigs, logging equipment etc. separately for Eligible Blocks as well as Non-Eligible Blocks. Due to this ONGC loses operational flexibility leading to project delays as well as idle time of hiring costly equipment.

(x) In case of emergency/exigencies, it is practically not possible to utilize the duty free specified goods purchased / hired for Eligible Blocks, in our operations in Non-Eligible Blocks.

(xi) The above difficulties are being faced by only two National Oil Companies i.e. ONGC and OIL, who were allotted blocks prior to April 01, 1999 on nomination basis.

(xii) In view of the above, there is need of an amendment under S. No. 356 of Customs Notification No. 12/2012-Cus dated March 17, 2012 so as to allow exemption on import of specified goods required for petroleum operations undertaken under Petroleum Exploration Licenses or Mining Leases, as the case may be, issued or renewed by the Government of India or any State Government irrespective of its date of issue or renew.

Suggestion

A suitable amendment under S. No. 356 of Customs Notification No. 12/2012-Cus dated March 17, 2012 so as to provide exemption on import of specified goods required for petroleum operations undertaken under Petroleum Exploration Licenses or Mining Leases, as the case may be, issued or renewed by the Government of India or any State Government irrespective of its date of issue or renew.

11. **For the Ease of doing Business, Entry No 356, 358 and 359 of Notification No. 12/2012-Cus dated 17/3/2012 should be merged into single entry. This will obviate the requirement of obtaining multiple Certificate from DG Hydrocarbon (DGH) at the time of import and at each movement from nominated blocks to NELP/Pre-NELP Blocks or vice versa for petroleum operation.**

(i) ONGC, a National Oil Company is having 401 Blocks allotted on nomination basis and 86 Blocks allotted under New Exploration and Licensing Policy (NELP) for exploration and production of hydrocarbons in addition to few Pre-NELP Blocks. Normally, ONGC charter hires Drilling Rigs, Offshore Vessel or other capital equipment for Petroleum operation in both nominated as well as NELP blocks on long term contract of 3 to 5 years.

(ii) **Entry No 356, 358 and 359 of Notification No. 12/2012-Cus dated 17/3/2012 provide customs duty exemption:**

Vide S. No. 356 of notification No. 12/2012-Cus, dated 17/3/2012, the exemption from customs duty is available on import of specified goods (List 13 annexed with notification) in connection with petroleum operations undertaken under Mining Lease issued/renewed after 01.04.1999 and granted by the Government of India or any State Government to the Oil and Natural Gas Corporation or Oil India Limited on nomination basis, subject submission of certificate from DGH and other conditions prescribed.

Vide S. No. 358 of notification No. 12/2012-Cus, dated 17/3/2012, the exemption from customs duty is available on import of specified goods (List 13 annexed with notification) in connection with petroleum operations undertaken under specified contracts subject submission of certificate from DGH and other conditions prescribed.

Vide S. No. 359 of notification No. 12/2012-Cus, dated 17/3/2012, the specified goods (List 13 annexed with notification) required in connection with petroleum explorations undertaken under specified contracts under the New Exploration Licensing Policy are exempt from

basic customs duty as well as CVD, subject submission of certificate from DGH and other conditions prescribed.

(iii) We submit that the objective of exemption granted under Sl. Nos. 356, 358 or 359 of Notification 12/2012-Cus is to exempt the import of specified goods in connection with petroleum operations from customs duty. Whether the goods are essential for such use is certified by the DGH. The conditions prescribed under these three Serial Nos. are similar. The List of specified goods allowed to be imported is similar for Sl. Nos. 356, 358 and 359. Conditions Nos. 41, 43 & 44 under Sl. Nos. 356, 358 & 359 respectively are also similar.

Therefore, all these three Sl. Nos. 356, 358 & 359 should be merged into one so that once the conditions are all fulfilled for availing of exemption at the time of import, the specified goods can move for petroleum operation from eligible Nominated Blocks to a NELP/Pre NELP oil field or vice-versa without the requirement of obtaining certificate subject to the condition that there is no change in Licensee/Contractor or sub-contractor or both. This will obviate the delay in movement of highly costly equipment, substantial saving in cost by effective utilization of Drilling Rigs/equipment, and also saving in compliance cost.

In case if there is change in Licensee/Contractor or sub-contractor or both, the condition of Notification No 28/2013-cus dated 16/05/2013 would be required to be fulfilled.

Suggestion:

Amendment under Customs Notification No. 12/2012-Cus dated 17.03.2015 so as to merge Sl. No. 356, 358 & 359 for common exemption on import of goods specified under List-13 (of such notification) which are required in connection with petroleum operations undertaken under PEL, ML, specified contracts or NELP.

12. **Enlarging the List-13 & 14 (of Sl. No. 356, 358, 359 and 360 of Notification No. 12/2012-Cus) of goods that could be imported, duty free, by the Upstream sector for petroleum operation**

(i) The NELP and CBM Policy and the contracts executed by the Government of India with contractors for exploration and production of Petroleum and CBM under these policies **allow contractors to claim customs duty exemption for all goods imported into the country for the use in operations related to the exploration, development and production of petroleum. Said exemption is also available to ONGC and OIL for nominated blocks where PEL/ML issued or renewed after 1.4.1999.**

(ii) The Government vide its notification No. 12/2012 dated 17.3.2012 has allowed the grant of exemption on imports of goods detailed under List 13 and 14.

(iii) However, the **list of items provided in the notification is not exhaustive and does not cover all goods required to be imported for the purpose of the operations.**

(iv) The following modifications are required in **List 13 of notification No. 12/12 customs dated 17.03.2012** issued by Ministry of Finance:

- In serial No. 1 - the word **"All"** may be added before the words other types of survey. Further, **Software and Hardware required for seismic survey, data processing and interpretation related to E&P Activities may also be added.**

- In serial No.5 - the words **"Requisite Vehicles"** may be added before the words for specialized services. Further the words **"Including Equipment for riser less building, LWD / MWD tools"** may be added after the words down hole equipment. This is required to bring clarity of the items covered under this item.

- In serial No. 6 -the words **"Thread Protectors and Fittings"** may be added in the end since these are the integral part of pipes/tubing/casings.

- The serial No. 9 should be recast to state : **Subsea / Floating / Fixed Process, Production and well platforms and onshore facilities for storage/ production / processing of oil, gas and water injection including items forming part of the platforms / onshore facilities and equipment / raw materials required like process equipment, turbines, pumps, generators, compressors, prime movers, water makers, filters and filtering equipment, all types of instrumentation items, control systems, electrical equipments / items, oil improvement, construction equipment, telemetry, telecommunication, tele-control security, access control and other material required for petroleum operations.** The said recasting is required to cover all types of offshore and onshore facilities and equipment/ material required for petroleum operations.

- In serial No. 10 - the word **"Jumpers"** should be added before the words and trunk. The words **"All types of"** should be added before the words - coatings and wrappings. After the word wrapping, the words should be added - **"Pipeline Fittings, Flanges, Connection systems and Associated items, Paintings and Insulations"**. The said

change is required to cover all the material required for pipelines both offshore and onshore.

- In serial No. 11 - the word **"Operation"** should be added before the words - of platforms.

- In serial No. 13 - the word **"Related"** should be added after the word safety. This modification is required to ensure that all types of fire and gas detection, fighting and suppression systems are covered.

- In serial No. 15 - the words **"and assemblies"** should be added before the words including high pressure.

- In serial No. 16 - the words **"all types of"** should be added before communication equipment. This is important to cover all communication equipments.

- In serial No. 17 - the word EPIRV should be read as **"EPIRB"**.

- In serial No. 19 - the words **"all types of transponders including"** should be added before the words X-band radar. This is required to include all types of transponders.

- In serial No. 21 - after the word panels, the words should be added - **"Flow meters, sand detectors, DTS, MLS, artificial lift equipment including surface and sub-surface equipment"**. This would help in covering all equipments based on latest technology.

- In serial No. 23 - the words **"all types of"** should be added before data tapes. The word **"cartridges/ media"** should be added before the words operational and maintenance. This is required to include new types of data storage, media using new technologies.

- One new serial 25 should be added to state: **"All types of material, equipments, instruments required for deep water projects and associated facilities like control system equipment and materials umbilical, hydraulic oils, connectors, clamps, sub-sea structures, assemblies, control modules, tempers, testing and calibration systems, simulators, intervention vessels, instrumented, safety systems."**

- Serial 26 to state as: **"All types of pre-fabricated structures like manifolds, PLEMS, PLET, decks, jackets, boat landings, buildings, flare / vent boom, subsea modules."**

The following modifications are required in **list 14 of notification No. 12/12- customs dated 17.03.2012** issued by Ministry of Finance:

- In serial No. 1 - the words **"and Aeromagnetic Survey"** should be added before the words equipment and accessories. The word **"Geotechnical"** should be added before the words and Geochemical. Further the word **"CBM"** should be added before the word activities. It is important to note that Aeromagnetic Survey is required in CBM for mapping the different formations having susceptibility to magnetism. Formation such as dolerite can be mapped using aeromagnetic surveys. Similarly, Geotechnical Surveys are also used for mapping of CBM.

- In serial No. 2 - after the words drilling rigs, the words **"Air Drilling with air package consisting of compressors and boosters"** should be added. It is important to note that coal is susceptible to formation damaged during drilling operations; therefore, air drilling is used worldwide to minimize formation damage during drilling.

- In serial No. 3 - the words **"and laboratory"** should be added before the words equipment, directional drilling. The words **"including all types of software"** should be added before the words solids control, fishing. It is important to note that laboratory equipment for measuring gas content and carrying out various analyses on coal samples are required. Further, softwares are required for interpretations of well tests, reservoir simulation, carrying out geological and other modeling.

- In serial No. 4 - the words **"core drilling rods, core barrels"** should be added before the words production tubing. It needs to be appreciated that core drilling rods and barrels are required for taking core samples during core hole drilling operations.

- In serial No. 5 - the words **"DTH hammers"** should be incorporated before the words including nozzles. DTH hammers are required for carrying out air drilling operations.

- In serial No. 6 - the term **"POL"** should be added before the words used in coal bed Methane. It is important to note that lubricants, oil and grease are required in the equipment used in CBM operations.

- In serial No. 7 - the words turbines, pump generators should read as: **"turbines, all types of pump generators, all types of electrical, electronic and instrumentation equipment"**. These equipments are used in gas and water measurement and handling in CBM operation.

- Serial No. 8 should read as: **"Line pipes for flow line and trunk pipelines including weight coating, wrapping and all types of**

fittings." It is important to note that fittings are required for pipe jointing, bends, hot taping etc.

- Serial No. 9 should read as: "Tanks and vessels used for coal bed Methane operations, water, mud, chemicals and related materials.

13. **Request for clarification to the effect that upto 20% of goods imported and cleared for home consumption for petroleum operation (Exploration & Exploitation of Hydrocarbons) on payment of a Nil or concessional rate of customs duty, but remain unused and declared scrap shall be allowed to be disposed of on payment of customs duty on the sale value of scrap.**

(i) Oil and Exploration Companies import various oil field equipment, spares, consumables, drill pipes, etc for petroleum operation in the oil field allotted on a nomination basis, as well as in NELP Blocks.

(ii) Material such as line pipes, line/marine pipes etc is imported against the contract/purchase order on an estimated basis.

(iii) Occasionally, after actual utilization of the goods, a small percentage of the imported consignment remains unused. The leftover / excessive goods are utilized in any other eligible project to the extent possible. However, sometime these pipes being of a particular specification cannot be utilized and remain unused. Hence, such goods need to be disposed of as a scrap.

(iv) Due to ambiguity in the applicability of customs duty, the rate of customs duty etc, old materials lie in store and occupy valuable space.

Recommendation

Request for clarification to the effect that upto 20% of goods imported and cleared for home consumption for petroleum operation (Exploration & Exploitation of Hydrocarbons) on payment of a Nil or concessional rate of customs duty, but remain unused and declared scrap shall be allowed to be disposed of on payment of customs duty on the sale value of scrap

Excise Duty

14. **Exemption of excise duty for captive consumption of petroleum products as fuel or otherwise and supplies to Defence / Fertilizer units should be covered in Rule 6(6) of Cenvat credit Rules, 2004 i.e. Rule 6(6) of CCR, 2004 to be made applicable to supplies against end used based exemptions.**

Presently Rule 6 of Cenvat Credit Rule, 2004 provides for exception to sub rule (1), (2), (3) & (4) for supplies effected to following:

(i) cleared to a unit in a special economic zone or to a developer of a special economic zone for their authorised operations; or

(ii) cleared to a hundred per cent. export-oriented undertaking; or

(iii) cleared to a unit in an Electronic Hardware Technology Park or Software Technology Park; or

(iv) supplied to the United Nations or an international organization for their official use or supplied to projects funded by them, on which exemption of duty is available under notification of the Government of India in the Ministry of Finance (Department of Revenue) No. 108/95-Central Excise, dated the 28th August, 1995, number G.S.R. 602(E), dated the 28th August, 1995; or

(iv-a) supplied for the use of foreign diplomatic missions or consular missions or career consular offices or diplomatic agents in terms of the provisions of Notification No. [12/2012-Central Excise, dated the 17th March, 2012, number G.S.R. 163(E), dated the 17th March, 2012]; or]

(v) cleared for export under bond in terms of the provisions of the Central Excise Rules, 2002; or

(vi) gold or silver falling within Chapter 71 of the said First Schedule, arising in the course of manufacture of copper or [zinc by smelting; or]

(vii) all goods which are exempt from the duties of customs leviable under the First Schedule to the Customs Tariff Act, 1975 (51 of 1975) and the additional duty leviable under sub-section (1) of section 3 of the said Customs Tariff Act when imported into India and are supplied, –

(a) against International Competitive Bidding; or
(b) to a power project from which power supply has been tied up through tariff based competitive bidding; or
(c) to a power project awarded to a developer through tariff based competitive bidding,

in terms of Notification No. [12/2012-Central Excise, dated the 17th March, 2012];

(viii) supplies made for setting up of solar power generation projects or facilities.

Supplies made to Defence are covered by notification no 64/95 dated March 16, 1995 as amended at nil rate of duty. Notification no 83/92-CE dated 16/09/1992, covers inputs captively consumed for the manufacture of final products cleared to units as covered under notification no 64/95 and exempt from the levy of whole of the duty of excise. Hence, supplies to Defence should also be covered under Rule 6(6) of Cenvat credit Rules, 2004.

Exempted goods as defined in CCR, 2004 are "exempt from the whole of the duty of excise leviable thereon, and includes goods which are chargeable to "NIL" rate of duty. Duty of excise is levied on the goods manufactured and payable by the manufacturer. There may be instances where same goods are cleared on payment of duty and cleared without duty as exempted by notification to specified class of customers. Hence exemption by way of notification as applicable to manufacturer only needs to be covered under Rule 6 (1) to (3).

15. Exemption on 10% Ethanol Blended Petrol for the period 12.12.08 to 23.12.2008

Background

Ministry of Petroleum & Natural Gas (MoPNG) vide letter No. P-45018/28/2000-cc (Vol.II) dated 29.10.08 directed PSU Oil Marketing Companies (OMCs) to implement marketing of Petrol (MS) blended with 10% Ethanol i.e. blend of 90% of MS and 10% of Ethanol in two storage locations namely Desur (Belgaum) in Karnataka and Aonla (Bareilly) in U.P. as a pilot project basis. Based on the directions of the Govt, IOCL & BPCL started blending of 10% Ethanol Blended Petrol (EBP) at these storage locations effective 12.12.2008.

Since at the relevant time exemption from excise duty was not available on 10% EBP, IOCL vide letter dated 11.11.2008 sought necessary exemption notification in line exemption available to 5% EBP, based on which CBEC issued Notification no. 61/2008-CE, 62-2008-CE, 63-2008-CE and 64-2008-CE, all dated 24.12.08 exempting 10% EBP from levy of excise duty with prospective effect.

Since the notifications were issued on 24.12.2008 with prospective effect, whereas as per the direction of the Govt., PSU OMCs were constrained to implement 10% EBP w.e.f. 12.12.2008, therefore, demand was raised on OMCs for the intervening period starting from 12.12.08 to 23.12.08 being not covered under the said exemption notifications, which is presently under litigation before CESTAT.

In this regards, Industry made a joint representation to Govt. vide letter dated 10.02.2009 seeking issuance of exemption Notification with retrospective effect from 12.12.08 to 23.12.08 followed by various representation and requests. Further, MoPNG vide letter dated 09.07.2010 also recommended the case for issuance of retrospective notification to CBEC. However, issuance of suitable exemption Notification is still awaited for intervening period from 12.12.08 to 23.12.08.

Suggestion

Considering that implementation of 10% EBP was as per directives of Govt. and exemption was issued from 24.12.2008 accepting these facts, therefore, it is imperative that necessary exemption notification is issued with retrospective effect to cover the period starting from 12.12.2008 to 23.12.2008 to avoid further litigation and any adverse fall out on the OMCs.

Further, it is worth mentioning that at the time of 5% EBP implementation, a suitable exemption notification no. 25/2006-CX (NT) dated 20.11.2006 was issued by the CBEC for the intervening period from 01.07.2004 to 03.08.2004.

16. Reduction in Excise duty from existing 12.5% to 7.5% on Cryogenic Containers (High Vaccum)

One of the IOCL's divisions is engaged in manufacturing of Cryogenic Containers (High Vacuum Containers for storing and transportation of Liquid Nitrogen). Presently the product attracts an Excise Duty of 12.50%. These containers are used for Artificial Insemination of High Breed Cattles and used by Animal Husbandry Departments across the country. It contributes to the Rural Employment and Milk Production by the marginal Rural Population.

If this excise rate is reduced the product will be cheaper and will become affordable to the rural marginal farmers and improve their livelihood.

Suggestion

It is suggested to reduce the excise duty on Cryogenic Containers from existing 12.5% to 7.5%

17. Allowance of Storage Loss on Lubricating Oils and Other Specialty Oils

Background:

IOCL's Lube Oil Blending Plants manufactures more than 300 Grades of lubricating oil in Automotive and Industrial categories. Most of the grades in Automotive and some in Industrial Categories are packed in different packages to suit the market requirement ranging from 20 ml Pouches to 20 litre containers for sale in Retail trade and 50 Litre containers and Barrels for sale to the bulk customers. This requiring handling of the lubricating oil at different stages viz. manufacture, storing, handling, packing, loading,

movement of these product packs within the Lubricating Oil Base Stock (LOBS).

Since there are some breakages, damages are bound to happen due to movement of the product causing leakage of the product. Despite best efforts, losses do occur due to such leakages for the reasons beyond our control. Certain losses are also due to remnant product in the containers since lubricating oil characteristically is a highly viscous product. Considering various factors, the CBEC in their letter F. No. 11-A / 6/ 70/ CX.8 dated 30.04.1971, fixed the limit of 0.1% for storage loss allowance for LOBS.

Suggestion

It is felt that this condonation percentage should equally apply to finished lubricating oils also since LOBS content in each grade of lubricating oil is in the range of 90% and 95%. However, department is not allowing such condonation to finished lubricating and specialty oils alleging that the CBEC's clarification is only applicable to LOBS. Hence, it is suggested that necessary notification/circular to be issued for fixing of condonable loss percentage for lubricating and specialty oils in line with the aforesaid CBEC's letter dated 30.04.1971.

18. **Introduction of Specific rate of excise duty for Aviation Turbine Fuel (ATF):**

Background

ATF is falling under ITC (HS) code 2710.19.20 of the Central Excise Tariff Act and presently chargeable at 8% ad-valorem rate of excise duty.

Generally ATF is received at AFSs through intermediate storage locations (Depot/Terminal) instead of directly from Refinery. At the point of removal, the excise duty is paid on destination assessable value by following the principle of Normal Transaction Value under Section 4 of the Central Excise Act read with Rule 7 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000. In case of further stock transfers by the intermediate storage locations, the duty payable is again determined based on the value applicable to the final receiving locations i.e. AFSs which result in payment of differential duty. This creates problem in re-ascertaining the correct transaction value for payment of differential excise duty at Refinery.

The extension of same rule for payment of duty on account of further stock transfer of products from one depot to another depot, makes the compliance of valuation rule very difficult for the oil companies.

The adoption of the provisional assessment would be complicated and not a pragmatic solution due to untenable and unending exercise to trace the original duty paying documents for finalization of the provisional assessment both for the department and the oil industry.

Suggestion

Like other petroleum products viz MS and HSD, for ATF also specific rate of duty should be introduced in place of ad valorem duty. This would ensure correct payment of duty at the initial clearance stage itself and will eliminate complexities and difficulties in re-determination of duty on further stock transfers which sometime result in avoidable litigation.

19. Amendment in procedure for supplies against Served from India Scheme (SFIS)

Background

There are major Airlines customers who are holding SFIS scrips issued by DGFT, involving huge amounts. These airlines have approached IOCL to issue duty free Aviation Turbine Fuel (ATF) against the SFIS scrips. The present procedures prescribed under SFIS require IOCL to Supply the ATF directly to the airlines only at the refinery level. Since it is not feasible to change the present logistics arrangements wherein ATF is routed through intermediate storage locations as well as Aviation Fuel Stations (AFS) in comingled condition, it is not possible to extend the SFIS benefit to these customers. The airlines are not in a position to utilize the SFIS benefits since the major portion of the duty payment is done by the airlines on purchases of fuel.

Suggestion

Since airlines customers do not have the necessary expertise/ infrastructure to handle the ATF procured from Refinery, its transportation to the AFS and fuelling to the aircrafts, amendment in the existing law is required either by way of permitting the transfer of SFIS scrip to the OMCs for utilizing against their duty payments or by amendment in the procedure prescribed under Central Excise law to enable the debit of duty to the scrip on sale of ATF to airlines at the AFS instead of the debit before the clearance of product from the refinery to the customer.

20. Payment of duty at refinery to be made at quantity at 15 degree

In order to eliminate litigations, it is suggested that duty shall be levied at quantity at 15 degree on all removals from refinery.

21. Permitting Mixed Bonding in Intermediate storage tanks for ATF and Bunkering Fuels:

After withdrawal of the warehousing provision the board has permitted establishment of the intermediate storage locations for storing of Bonded ATF. However, no mixed bonding of the bonded and duty paid ATF is permitted in such intermediate storage locations. This puts enormous operational constraints particularly in places where there are limitations on the availability of the storage tanks.

Mixed bonding of Bonded and Duty paid is permitted at AFS. The same facility should also be extended to the intermediate storage tanks. Segregation of the duty paid and bonded ATF can be maintained through accounting records.

22. Excise Duty on Transit Loss on ATF

With the withdrawal of warehousing provision vide notification no. 17/2004-CE dated: 04.09.2004 no movement from the refineries can be done without payment of duty. However in terms of circular date: 4th January 2005 the duty has to be paid on the quantity at the time of clearance from the refinery, and therefore duty has to be paid on the quantities lost in transit or storage after its clearance from the refinery.

Further as regards the clearance of ATF to be ultimately supplied to foreign Going Aircraft it was specified that though ATF can be removed for an export warehouse without payment of duty but no condonation will be allowed as regards the storage losses suffered during the storage of ATF either at Intermediately Storage Location or at Export Warehouse. Such losses are treated as diversion for home consumption and duty leviable along with interest at the rate of 24%.

These losses occur because of the peculiar nature of petroleum products which expands with the rise in temperature and contracts with the fall in temperature and which are beyond our control and occur purely because of natural causes.

Allowance should be given for the quantities lost in transit or storage as prescribed by the Govt. of India despite the fact that they are removed under export warehouse procedure.

23. Dispute on rate of excise duty on intermingling loss of SKO in pipeline transportation

Oil Companies have been using the pipeline for transportation of multiple products i.e. MS, HSD and SKO from its Refinery to various pipeline head depots /installations. Each parcel of HSD, SKO and MS individually is called a batch. The sequence of the products is MS then SKO then HSD then SKO. Since all the products packed inside the pipeline move at very high velocity and pressure, some co-mingling / intermixing of batches is unavoidable at the boundary of the continuous batches and this intermixing of two adjoining product inside a pipeline is called an INTERFACE. The interfaces between MS-SKO or HSD-SKO are generally upgraded to MS or HSD respectively.

After removal of warehousing facility for petroleum products w.e.f. 06.09.2004, the Board Circular no 796/29/2004 CX dated 04.09.2004 states that the excise duty is liable to be paid by the refineries at the time of removal. Rule 4(1) of Central Excise Rule 2002 states that no excisable goods on which any duty is payable, shall be removed without payment of duty from a place where they are produced or manufactured or from a warehouse.

Thus the applicable duty on MS, HSD, SKO-PDS manufactured by the Refinery needs to be discharged at the factory gate on clearance through the pipeline (here the applicable duty rate on SKO PDS is nil) after removal of the warehousing facility for petroleum products.

The Department however disputed the practice followed by Refineries based on Board Circular No 637/27/2002-CX dated 22.04.2002 and issued a Show Cause Notice demanding the higher of the two duties i.e. duty payable on SKO not used for the intended purpose and duty payable on surge/gain in MS or HSD against the loss quantity of SKO PDS. This Circular is no more valid as post removal of the warehousing provision with effect from 2.9.2004, duty is to be discharged at the point of removal.

Based on a reading of the Board Circular, it is clear that the benefit of nil duty/concessional duty cannot be extended against loss of SKO PDS as this is not utilized for the intended purpose. Accordingly, Refineries have been paying the applicable duty on SKO against the loss quantity of SKO PDS, which was also recognized in the first part of the Circular. The Board clarification on the second part on the payment of the higher of the two duties i.e. duty payable on SKO not used for intended purpose and duty payable on surge/gain in MS or HSD against the loss quantity of SKO PDS contradicts the Central Excise Provision after withdrawal of warehousing provision for petroleum products, which itself created the basis for litigation.

Furthermore, in a recent case, BPCL vs CCE Coimbatore 2013-TIOL-1215-CESTAT - MAD, CESTAT has criticized the approach of the Department on imposing duty liability based on a Circular issued by the CBEC, without explaining the legal provisions under which duty liability arose.

In view of the above, withdrawal of the Circular is required or appropriate clarification may be issued

24. Service tax on transportation of goods by Rail to destinations situated in Jammu & Kashmir

Background

In order to cater the requirement of petroleum products of the State of J&K, IOCL, transfer the petroleum products from its Refineries situated outside J&K like Panipat, Mathura, Koyali (Vadodara) etc. to our Depot situated in J&K States through the Rail transportation.

Till March, 2013, transportation of Petroleum Products falling under chapter heading 2710 and 2711 of the first schedule to the Central Excise Tariff Act 1985 (5 of 1986), through Rail was exempted from Service tax as per S. No. 20(a) of Notification No. 25/2012-Service Tax dated 20.06.2012.

The said exemption was withdrawn w.e.f 01.04.2013 vide Notification No.3/2013-ST dated 01.03.2013 and Railways have started charging service tax on the transportation of these Petroleum Products falling under chapter heading 2710 and 2711.

Though, said exemption was withdrawn but in terms of Rule 10 of the Place of Provision of Service Rules, 2012 (the Rules), for the service of transportation of goods other than by way of mail or courier the place of provision of service is the place of destination of the goods.

Thus, in case of transportation of goods by Rail from a place outside the J&K state to a destination situated in J&K State, the place of provision will be J&K State, which is outside the taxable territory under Service Tax law and accordingly no service tax is payable.

Despite of non-applicability of Service Tax as mentioned above, Railways are charging Service tax on IOCL on movement of petroleum products from outside J&K State to a destination situated in J&K.

The issue was taken up with the Railway Board for not to charging Service tax on such movements. However, Railway authority are of the view that the subject matter needs to be taken up with CBEC (MoF) for seeking

necessary clarification on applicability of service tax on movement of petroleum products from outside J&K to a location situated in J&K.

Suggestion

In view of the above, we request you to kindly issue necessary clarification on non-applicability of Service Tax on transportation of goods by rail from outside J&K State to a destination situated in J&K State.

25. **Extension of service tax abatement on transportation through Time charter Vessels**

Background

Oil Marketing Companies (OMCs) transport the petroleum products either through Voyage Charter vessels (point to point transportation and/or per MT basis) or through the Time Chartered vessels (payment made on per day basis) but both are essentially transportation contract. However, Service tax under voyage charter is leviable after granting 50% abatement on consideration vide Notification No 26/2012-ST, dated 20.06.2012 subject to specified condition whereas no such abatement is available on payment of service tax while engaging vessels under time charter. Since tax rate or taxation should be neutral on type of transaction on similar matter, hence, both types of transportation contracts should be taxed on same rate specially when Service tax levy on the basis of positive list concept has been done away with and concept of service levy on the basis of negative list have been introduced with effect from 01.07.2012. Estimated financial impact per annum on IOCL on the subject issue works out to Rs. 20 Crores.

Suggestion

It is suggested that Time charter of the vessel to be considered only as transportation of product through vessels and 50% abatement may be provided through issuance of suitable clarification or Notification as deemed fit.

26. **Rebate of Service tax on Rupee export of ATF and bunker fuels to foreign going Vessels and aircrafts:**

Background:
As per Notification 41/2012 dated 29.06.2012- Rebate of service tax paid on services used for export of goods -

Point No 4. " Where any rebate of service tax paid on the specified services has been allowed to an exporter on export of goods but the sale proceeds in respect of said goods are not received by or on behalf of the exporter, in India, within the period allowed by the Reserve Bank of India under section 8 of the Foreign Exchange Management Act, 1999 (42 of 1999), including any extension of such period, such rebate shall be deemed never to have been allowed and may be recovered under the provisions of the said Act and the rules made there under;"

Similar provision is in vogue in Rule 16A of the duty drawback rules. It is has been observed that the Central Excise / Customs authorities at many places are rejecting the service tax refund claims / duty draw back claims on the ground that the realization of the exports proceed is not in foreign currency in accordance with FEMA.

Suggestion:

Clarification may be issued confirming non applicability of FEMA requirement with reference to realization in foreign currency in case of deemed exports to countries where rupee export is permitted.

Cenvat Credit Rules:

27. **Extension of Cenvat Credit to Crude Oil and Product Pipelines attached to Refineries-**

(Liquid as well as Gas Pipelines) originating from or terminating in the Refinery premises. This is required to avail Cenvat credit of duty in respect to purchases for pipelines.

Background

Under Rule 3(1) of the Cenvat Credit Rules, 2004, credit of excise duty, additional duty, service tax, etc. paid on any input, Capital goods and input services is available to a Manufacturer of final products or Provider of taxable service

In the existing business model of IOCL {Crude Pipeline -> Refinery -> Product Pipeline -> Marketing}, Refinery qualifies as manufacturer for Central Excise purposes as all processes integral and ancillary to the production of petroleum products takes place in refinery. Cenvat credit on inputs, capital goods as well as on input services is, accordingly, available to Refineries.

Since Pipelines do not undertake any distinct manufacturing activity, no pipeline installation is separately registered under the Central Excise. 'Transportation of Goods by Pipeline' as such is a taxable service. However,

for Pipeline to avail of all sorts of Cenvat credits, it is essential that the services are provided to other person. Since IOCL is not providing pipeline services to other person, Cenvat credit cannot be availed.

For availment of Cenvat credits of duty paid on inputs and capital goods through Refineries, it is provided that:-

- Goods must be used within factory in relation to the manufacture of final products
- Goods must be received in the factory of production

Typically, pipeline system can be construed consisting of two parts:-

i. Installation / office and the end pipeline portion located inside the refinery premises
ii. Installations and major portion pipeline length located outside the refinery premises

Though pipelines traverse long distances outside the Refinery's defined boundary under Central Excise, for Cenvat credit purpose Pipelines should be considered within the factory as one end of the pipeline is within the factory premises. This has been decided in many judicial pronouncements some of which are discussed below:-

a. 'Pepsi Co India' engaged in the manufacture of aerated water had installed a pipeline for drawing water from a well located 200 meters away from the factory premises.

   Decision by Tribunal Chennai: Pipeline connected the well with the factory premises, extended inside and were used within the factory, credit could be availed.

b. J K Udaipur Udyog engaged in manufacture of Cement and used ropeway for transferring crushed limestone from mines located 5.8 KM away from the factory.

   Decision by Tribunal Delhi: Ropeway outside the factory was an extension of the ropeway within the factory, credit could be availed.

c. Jaypee Bela Plant used pipeline for transferring water from a reservoir to the factory.

   Decision by Tribunal Delhi: When one end of the pipeline is within the factory premises, the length of the pipeline is immaterial as long as it is used for transportation of raw material for use in the manufacture of goods within factory.

d. Birla Corp used ropeway for transferring limestone from mines located 4.2 KM away from the factory.

Decision by the Supreme Court: Approving the tribunal judgments in cases at 1 & 2 above, held that credit of duty on spares of ropeways would be allowed.

Cenvat credit of excise duty on capital goods is as such available if the goods are received and also used in the factory premises. Pipelines are not just confined to the Refinery premises but spread length and breadth of the country. Through judicial pronouncements, as stated above, it has been established that if the one end of the pipeline / ropeway is inside the factory premises and the pipeline is used to bring raw material / feedstock for the factory, duty paid on the capital goods used for the pipeline is Cenvatable.

However, the issues pertaining to availing Cenvat credit in respect of long distant pipelines across the country has not yet been put to judicial scrutiny and litigation on this point cannot be ruled out.

Suggestion

Accordingly, in order to avoid litigation, it is suggested that the definition of 'Factory' is amended so as to include in it all connected crude oil and product pipelines.

Alternatively, necessary provisions need to be made in the CENVAT Credit Rules, covering all such pipelines as part of the manufacturing unit for the purpose of eligibility of Cenvat Credit.

28. Duty Credit on MS, HSD and LDO brought to refinery for reprocessing

Background

As per Rule 16 of the Central Excise Rules, 2002, if the goods on which duty is paid at the time of removal thereof are brought back into the factory for being re-made, refined, re-conditioned or for any other reason, the assessee shall be entitled to take CENVAT credit of the duty paid as if such goods are received as inputs under the CENVAT Credit Rules. These goods can be cleared again on payment of applicable duty after subjecting them to manufacturing process.

After clearance on payment of duty sometimes petroleum products become off-spec. and have to be brought back to the Refinery for re-processing so as to make them marketable. In case of products such as MS, HSD and LDO which are non-Cenvatable, Refinery is not eligible to get any CENVAT credit and duty has to be paid again at the time of their clearance after re-processing, resulting in double payment of duty.

Suggestion

It is suggested that non-Cenvatable products like MS, HSD and LDO when received in the Refinery for re-processing should either be exemp from payment of duty at the time of clearance after re-processing or Cenvat Credit should be allowed on these products at the time of receipt in the Refinery by suitably amending the definition of 'Input' contained in the Cenvat Credit Rules'2004 for re-processing of such products in the refinery.

29. **Definition of "Input Services" should include setting up of factory**

Background

The CBEC vide notification No. 3/2011-CE(NT) dated 1.3.2011 (effective from 1.4.2011) amend the definition of input services and remove the word Setting up from definition of service tax.

A company like Indian Oil Corporation limited which business totally depend upon continuous running of refineries and setting up of new refinery to meet the demand. A refinery takes very long time to fully set up and come in operation stage like our grass root Paradeep refinery

Now, if law restrict to take credit of CENVAT on the services which are used during the setting up of factory then it would become injustice to assesses, as these services are being ultimately directly or indirectly used in manufacture of product after commencing refinery/plant.

Suggestion

CBEC is requested to include the word setting up in the definition of "Input Services" of Cenvat Credit Rule 2004, as prior to 01.04.2011.

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Annexure II

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PRE-BUDGET MEMORANDUM FY 2016-17: SUGGESTIONS

Direct Taxes

I) Corporate Tax

(1) Corporate Social Responsibility Expenditure

Background

Corporate social responsibility expenditures have become part of business operations a company, particularly in case of PSU. Further New Companies Act 2013 also provides for mandatory CSR expenses to the extent of 2% of average Net profit of a company in last 3 preceding year. In order to promote development of the country, CSR expenses need to be promoted. Under CSR various development programmes like development of schools for poor children, roads & bridges in rural areas, financial assistance to NGOs engaged in helping poor by providing employment are carried out.

Suggestion

In view of mandatory nature of CSR expenses under new Companies Act, 2013, it is suggested to insert an amendment under Income Tax Act allowing deduction of CSR expenditure.

(2) Eligibility of Prior period expenses in the year in which the expenses is debited in books of accounts

Background

In a large organization, Prior period expenditures are bound to occur as it is not possible to book all expenditure in the previous year to which these expenditure belong to. Presently such expenditure is not allowed in the financial year in which it is actually debited. Hence the only option is to file revised return or litigate the matter with the appropriate appellate authority to allow such expenditure in the year to which it relates. It causes not only undue hardship to the taxpayer but also unnecessary paperwork for the department with no benefit to either party.

Suggestion

It is therefore suggested that such expenditure may be allowed in the year in which it is debited in the books of accounts provided it is otherwise allowable.

(3) **Income Computation and Disclosure Standards (ICDS)**

As per the Hon'ble Finance Minister's speech in Parliament, last year, India would converge its Accounting Standards with IFRS and in Phase-1, it will be effective F.Y. 2016-17 for large listed Corporates. Considering that it will impact tax collections, the Government of India had notified Income Computation & Disclosure Standards (ICDS), under Section 145 of the Act. On a careful perusal of these ICDS, the theme has been to advance the Income & defer the expenditure. While this would certainly improve tax collection, it is also of fact that the same is revenue neutral, over the period. In the process of advancing the tax collection, in our view, the enforcement of ICDS would only increase the cost of tax compliance and litigation.

The effective tax rate, as a result of these ICDS could only raise substantially from the proposed tax rate of 25%. Further, this would lead to spate of disallowances and consequent litigations. It is imperative that as much as exemptions are removed/rationalized, the proposals that have the effect of increasing the tax rate should also be removed/rationalized and avoided especially, if it has the effect of only advancing the tax collection, which otherwise is certain. Therefore, it is recommended that ICDS be totally de-notified or deferred till a broad consensus is reached among the tax payers and Department.

If implementation of ICDS is unavoidable, ICDS-IX, dealing with "Borrowing Costs" requires modification with reference to computation of borrowing costs eligible for capitalization out of funds borrowed generally as the current wording of the Standard conflicts with the provisions contained in Section 36(1)((iii) of the Income Tax Act, 1961.

(4) **Section 43B**

Section 43B allows certain expenditure only upon payment. Primarily, taxes and welfare expenditure on employees fall under this section. Effective 01/04/2002, a new clause (f) was inserted to permit deduction of any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee, only upon payment. Large Corporates set up dedicated funds for 'Leave Encashment' and basis the actuarial valuation, contributes an amount equivalent to the liability to the said fund. In such cases, employer no longer retains the said funds in the business operations. However, Assessing Officers deny the expenditure on the pretext of 43B(f) as contribution to the fund is not considered by them to be equivalent to payment to employees. In this manner, a genuine business expenditure gets disallowed and the claim of expenditure is deferred. To mitigate the hardship, it is proposed that an Explanation be

inserted in Section 43B to the effect that payment to the fund would be equivalent to payment to employees.

(5) AS-15 Vs. Section 36(1)

Under the Companies Act, P&L Accounts of the Company have to be in compliance with certain mandatory accounting standards, one of which is AS-15(Revised). As per the Standard, it is mandatory to provide for long term employee benefits such as post- retirement medical benefits, death benefit, leave encashment etc., based on actuarial valuation. While the Books cannot reflect true and fair view unless complied with the Accounting Standards, the Assessing Officer treats these expenditure as a contingent liability and disallows deduction, primarily because of Section 36(1) that permits only few of the chosen retirement benefits, namely, PF, Gratuity and Pension.

Considering the genuineness of the Business Expenditure and disallowance by the Assessing Officer leads only to delaying the deduction under Income Tax Act, suitable amendments are to be brought in Section 36(1) of the Act, permitting the deduction while transferring of the money to the welfare fund namely, 'Post-Retirement Medical Benefit Fund' and 'Death Benefit Fund' in addition to PF & Gratuity, currently specified in the said section.

(6) Section 14 Vs. Rule 8D

Disallowance towards expenditure incurred in relation to exempt income is provided in Section 14 of the Income Tax Act, 1961. In March 2008, Rule 8D was inserted in the Income Tax Rules which provides for the method of determining the amount of expenditure in relation to exempt income, in case, the Assessing Officer is not satisfied with the correctness of the claim of the assessee and also includes cases where the assessee claims that no expenditure has been incurred in respect of the exempt income. Rule 8D of the Income Tax Rules is interpreted by the Assessing Officers in a manner wherein huge amounts get disallowed and in some cases disallowance exceeds even the exempt income. To avoid litigation, it is suggested to amend Rule 8D to provide for the following:

a. Any disallowance shall be in relation to exempt income, actually earned / realized during the year

b. In case of an investment is made out of borrowed capital, no sooner the loan is re-paid, such investment should be treated as investments made out of own funds and therefore shall be kept out of the ambit of Rule 8D for the purpose of computing the cost of Notional Interest.

c. Wherever amount invested in a previous year is less than or equal to the Book profit, added by Depreciation, such investments shall be treated as investments made out of own funds and therefore shall be kept out of the ambit of Rule 8D for the purpose of computing the cost of Notional Interest.

d. As long as Investments as of end of the financial year has not exceeded Share Capital together with Reserves & Surplus of the Company, such investments shall be construed to have been made out of own funds and therefore shall be kept out of the ambit of Rule 8D for the purpose of computing the cost of Notional Interest.

e. Any Interest expenditure during the year shall be net of Interest Income during the year.

f. Any disallowance U/s Rule 8D should have upper Ceiling and cannot be unlimited.

(7) **Dividend Distribution Tax (DDT) - Section 115O**

Section 115O of the Income Tax Act provides for payment of tax on distributed dividends by companies. Since majority of shares in PSUs is held by the Govt. of India, and as and when dividend is declared on such shares, it becomes the property of the Govt., enjoying constitutional immunity of taxes, income tax should not be again levied thereon. Therefore, it is suggested that Section 115O shall not be made applicable to PSUs, to the extent of dividend, payable on shares held in the name of President, Government of India.

(8) **Exemption Limits for various allowances - Section 10(14) / Rule 2BB**

The Exemption limits for various allowances (eg: Children's Education Allowance, Hostel Allowance etc.) mentioned in Rule 2BB r.w.s. 10(14) was fixed in 1995. We wish to recommend that the same needs to be revised keeping in view the cost inflation. It may be noted that the said Rule was amended last year only in case of Transportation allowance.

(9) **Perquisite Tax**

After the abolition of Fringe Benefit Tax vide Finance (No.2) Act 2009, Perquisite tax in the hands of employees was reintroduced vide Notification No. 94/2009 dt. 18/12/2009 from FY 2009-2010 by inserting new Rule 3 basis which, few perquisites like Free food and non-alcoholic beverages, is taxable if the cost per meal per employee exceeds Rs. 50/- and Gift from employer is taxable if the value exceeds Rs. 5000 p.a etc. We wish to recommend that, the threshold limit for perquisite value to be taxed in the hands of employees, needs to be revised keeping in view the cost inflation.

(10) **Leave Salary - Section 10(10AA)**

With implementation of successive pay commission recommendations, the leave salary of both Public and Private Sector employees has substantially increased. Whereas, a threshold exemption u/s 10(10AA) fixed at Rs.3 lakhs in the year 2002 hasn't undergone any revision over the years. Accordingly, it is suggested to revise the limit from Rs.3 lakhs to Rs.10 lakhs.

(11) Contribution to Superannuation Fund - Section 17(2)(vii)

As per existing provisions U/s 17(2)(vii), any contribution to an approved superannuation fund by the employer to the extent it exceeds Rs. 1 lakh is perquisite. This amount should be revised to Rs.2 lakhs or 10% of the Salary, whichever is higher. Salary for this purpose shall be defined as Basic + Dearness Allowance.

(12) Transfer pricing - Section 92BA

In Finance Act 2012, Section 92BA has been inserted so as to include specified domestic transaction under the purview of 'Transfer Pricing Provisions'. Considering that transactions between PSU Oil Companies for exchange of products are anyway concluded at arm's length and such products are exchanged on tonne to tonne basis, it is suggested that entire Inter - PSU Oil Company Agreements shall be excluded from the purview of Department's scrutiny of 'arm's length'.

(13) Time-limit for NOC for TDS

Under existing Income tax provisions, there are no time limits defined for disposal of application, seeking No Objection Certificate for remittance of TDS u/s 195/197 of the Act. As per the Provisions of section 195 and as per Rule 37BB, any payment made to Non-residents requires payer to obtain a No Objection Certificate from Assessing officer or a Certificate from a Chartered Accountant in Form 15CB before making payment to the concerned party. In order to avoid inordinate delay in obtaining these certificates, it is suggested that an outer limit of say, 30 days shall be fixed for issuance of such certificates, failing which the rate sought in the Application shall be deemed to have been approved. Further a clarification may also be issued on Rule 37BB, so as to exempt the Trade payments for imports made from Non-resident parties, wherever they do not have any Permanent Establishment in India. This will reduce the administrative difficulty with regard to the volume of transactions involved vs. tedious compliance procedures as per New Rule 37BB.

(14) Interest u/s 244A

Currently, interest u/s 234B/234C charged on the Assessee is 1% per month whereas interest u/s 244A payable to Assessee is 0.5%. It is suggested to bring parity in the rates and further the rate be linked to any 'reference rate' thereby making it dynamic.

(15) Tax credit u/s 115JAA

Tax Credit in respect of tax paid on deemed income u/s 115JAA has been allowed to be carried forward for set off to future years but such carry forward shall not be allowed beyond the 10th assessment year. Considering that economic growth hasn't picked up the momentum yet, such restriction on carry forward be extended to 15 years (in place of 10 years, now).

(16) Cost of Assets imported from outside India - Section 43A

Section 43A permits adjustment to 'cost of Assets' imported from outside India. The background to the introduction of this section was devaluation of rupee done during 1966-67, which, but for introduction of this section would have led to disallowance of exchange rate differential, impacting large number of Corporate Assessees. Over the last 5 decades, funding of capital projects have undergone sea change and External Commercial Borrowing is one of the major sources of low-cost funding of large projects wherein Assets acquired need not be imported from outside India and it could be Indian Assets as well. The Hon'ble Prime Minister's theme of 'Make in India', would get a huge fillip if necessary amendment is made in the section to allow capitalization of exchange rate differential arising out of loan borrowed in foreign currency even if the Asset is indigenous. This would also enable keeping the effective tax rate at 25%, intended to be achieved over the 4 years.

(17) TDS Credit be allowed irrespective of the assessment year

Background

Section 199 of Income Tax Act read with Rule 37BA provides that credit of TDS will be allowed for tax deducted at source and paid to central govt. for the assessment year for which such income is assessable.

Practical difficulty is faced when income is accounted by deductee say in FY 2012-13 whereas the deductor has credited/paid the amount and deducted tax thereon in FY 2013-14. As a result of this, TDS certificates (Form 16A) issued by the deductor would reflect in 26AS statement of deductee in FY 2013-14 whereas income was booked and offered to tax in FY 2012-13. Based on section 199 of the Act, Assessing Officer can deny the claim of TDS credit in FY 2013-14 on the plea that income was not booked and offered to tax in FY 2013-14.

Suggestion

Necessary amendment in Rule 37BA under section 199 may be made that TDS credit to be allowed as per 26AS irrespective of the assessment year to which it pertains to.

II) International Taxation

(18) a) Place of effective management (POEM) of a Company

Background

Before amendment, Section 6 (3) of the Act provided that a company is resident in India in any previous year, if it is an Indian Company; or

during that year, the control and management of its affairs is situated wholly in India.

However the concept of residential status of a company has been changed by Finance Act 2015, as per the amendment a company will be said to be resident, if it is an Indian company or its places of effective management (POEM) is in India at any time during the year.

Place of effective management means a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as whole are, in substance made.

The amendment has caused confusion in determination of place of effective management of a company incorporated out-side India and controlled by Indian holding company. It the above amendment will hamper the Global business by Indian Companies which are carrying out their business out-side India through a Subsidiary Company incorporated outside India but controlled from India. The above provision is stringent and in case of POEM of a of a foreign Company is in India it will be required to pay tax and file an Income Tax return in India like an Indian Company.

Suggestion

It is suggested that earlier provision under section 6 (3) should be restored and a company should be treated as resident in India if it is an Indian Company; or during that year, the control and management of its affairs is situated wholly in India.

INDIRECT TAXES

I. Service Tax

(19) Change in Rule 6(3) of Service Tax Rules 1994 to Cover 'Write Off"

After implementation of Point of Taxation rules payment of service tax has been changed from receipt basis to accrual basis and is required to be deposited irrespective of receipt of payment from service recipient.

Rule 6(3) of Service Tax Rules 1994 as introduced w.e.f.01.04.2011 provides that:

"Where an assessee has issued an invoice, or received any payment, against a service to be provided which is not so provided by him either wholly or where the amount of invoice is renegotiated due to deficient provision of service, or any terms contained in a contract, the assessee may take credit of such excess service tax paid by him, if the assesse -

a) has refunded the payment or part thereof, so received for the service provided to the person from whom it was received ; or

b) has issued a credit note for the value of the service not so provided to the person to whom such an invoice has been issued."

In case, the service recipient does not make the payment towards the service and the amount is required to be written off, the above situation is not covered in the provisions under Rule 6(3) of Service Tax Rules 1994 as no credit note is normally issued in such circumstances. However, a condition may be added that whenever the amount so written off is realized from the customers, service tax would be payable on receipt basis.

It is pertinent to mention that under rule 4(7) Cenvat Credit Rules'2004 effective from 1st April 2011, Cenvat credit taken after receipt of the Invoice is required to be reversed if payment is not released within three months of the date of Invoice. The customer would certainly not have taken the benefit of Cenvat credit in such cases.

Suggestion:

In view of above, it should be provided in service tax rules by way of suitable amendment that credit of service tax already paid by the service provider will be available in line with the provisions under rule 6(3) of the service Tax rules in case the outstanding dues for the services rendered are not received and are required to be written off. In case the amount is received at a later date, service tax may be deposited on receipt basis.

It will remove the hardship of the service providers as they become out of pocket in respect of service tax on value of services not realized from customers.

(20) Complex reverse charge mechanism under Service Tax law

Background

In the budget of 2012 various services have been covered under Reverse Charge mechanism like works contract services, manpower deployment services, security services, rent a cab services, services provided to Govt, services rendered by directors to the company.

Present Reverse Charge Mechanism is very complex. First, in case of a service provided who is resident in India only few specified services are under reverse charge method (what deptt. calls "partial reverse charge method"). Second, % of liability for the service recipient under reverse charge mechanism varies accordingly to the legal status of the service provider e.g. whether service provider is an incorporated entity or not. Third, abatement provisions also vary

according to the nature of service. Further these abatement provisions are not absolute but are conditional. Fourth, though conditions for abatement provisions are to be fulfilled by the service provider, deptt. expects that while discharging liability under reverse charge mechanism, service recipient will check and verify whether those conditions have been fulfilled or not. This has led to a situation of complex compliance and reporting mechanism for services falling under reverse charge method.

The definition of Works Contract appears to be vague considering various slabs of abatement like 40%, 60% and 70%. Moreover, in terms of Explanation II to Notification No. 30/2012-ST dated 20.06.2012; the service recipient has the option to choose a valuation method independent of the valuation adopted by the service provider. It is felt that these different valuation procedures would create un-necessary disputes with the department due to lack of clarity in the provision of law.

Suggestion

It is suggested that instead of joint liability, partly on service provider and partly on service recipient under reverse charge mechanism, there should be only one person liable for 100% payment of service tax. To make compliance and reporting easy both for the service provider and recipient, it is suggested that suitable amendments in legal provisions be made enabling service recipient to deduct amount of service tax from the total amount of Bills and Invoices etc. irrespective of the legal status of the service provider and deposit the same with the Govt.

(21) Availment of balance Education & SHE cess available on as on 28.02.2015

Background

In the Union Budget 2015-16, education cess leviable under Section 91 read with Section 93 of the Finance Act, 2004 and secondary and higher education cess leviable under Section 136 read with Section 138 of the Finance Act, 2007 on excise duty has been abolished with effect from 01.03.2015. Thus, no education cess and secondary and higher education cess is leviable with effect from 01.03.2015 on the excise duty paid on the final products cleared from the factory gate.

In this regard, CBEC vide Notification No. 12/2015-C.E. (N.T) dated 30.04.2015, clarified that education cess and secondary and higher education cess paid on inputs/capital goods and input services received on or after 01.03.2015 can be utilized against payment of basic excise duty. However, there is no clarification on the following issues:

Utilization of Cenvat credit of cess paid on inputs / capital goods / input services received prior to 01.03.2015 but invoices received only after

28.02.2015 and in respect of Cenvat credit of cess remaining unutilized as on 28.02.2015.

The above would in turn result in non-utilization of Cenvat credit attributable to cess paid on inputs / services resulting in incremental cost of production.

Suggestion

It is suggested that necessary instructions to be issued regarding treatment of unutilized Cenvat credit on account of education cess and secondary & higher education cess paid on inputs/capital goods / input services received prior to 28.02.2015 for which invoices were received after 01.03.2015 and in respect of Cenvat credit of cess unutilized as on 28.02.2015.

(22) **Clarification that commission agent service is covered input service definition**

Background

In order to facilitate their sales, Companies are engaging service of Commissioner agents. These agents are paid commission based on the sales made to the Customers on principal's behalf. CBEC vide circular No. 943/04/2011 -CX dated 29.04.2011, clarified that credit of service tax paid on account of sale commission is admissible as input service. However, many of the field formation based on the decision in the case of Cadila Healthcare are denying the credit of Service Tax paid on Commission agent service that such services are not in the nature of sales promotion thus not covered under definition of input services. The definition of input service under rule 2 (l) of Cenvat Credit Rules is inclusive definition with certain specified exclusions and service of Commission agent is not covered under exclusions.

Suggestion

CBEC may issue suitable clarification / Notification that services of Commission agents covered under Business auxiliary services is an eligible service for credit under the definition of input services.

(23) **Clarification on fine or a penalty for violation of law / contractual obligation**

As per guidance note 2.3.1, it has been clarified that fines and penalties which are legal consequences of a person's actions are not in the nature of consideration for an activity. Similarly, any amount collected towards fine or penalty for violation of contract (Liquidated damages recovered for delay in

completion or price reduction clause due to delay in delivery of product) should also be treated as legal consequences of person's action and hence are not in the nature of consideration for an activity.

Movement of petroleum products is governed by Essential Commodity Act. To enforce Essential Commodity Act, various control orders issued by Central Government, such as:

1. Petroleum Act, 1934, Rule 2002;
2. Essential Commodity Act 1955
3. HSD & LDO (Restriction on use) Order, 1974
4. LPG (Restriction on use), Order 1974
5. LPG (Regulation of supply and Distribution) Order, 2000
6. Motor Spirit & HSD (Regulation of supply and Distribution) Order 1998
7. Petroleum Product (Supply & Distribution Order 1972
8. Explosive Act, 1884

To enforce such orders, penalties are levied which in no way are consideration for an activity.

It is suggested that to amend definition of service to include following in exclusion list.

(d) Amount collected towards fine or penalty for violation of all Control orders issued by Central Government relating to petroleum products.
(e) Amount collected towards fine or penalty for (Liquidated damages recovered for delay in completion or price reduction on account of delay in delivery of goods / service)

(24) <u>Clarification to the effect that, contributions made to Corporate Social Reposibilty (SR) projects is not a consideration for ley of Service Tax.</u>

India is a Socialist Republic and one of the functions of Govt. is to carry out welfare activities. Therefore, Govt. collects various taxes for implementation of such welfare measures. Under CSR Project, PSU also implements/ carries out various welfare activities on behalf of GoI.

As per the directives of Department of Public Enterprises, Government of India, large public sector undertakings are required to spend 2% of its net profit towards various welfare measures under the Corporate Social Responsibility project. Accordingly, large PSUs like ONGC are making contribution for welfare activities which is primarily the function of Govt. It can be seen that, such welfare activities are being funded by Govt. from Consolidated Fund of India. Therefore the contribution made by PSUs to welfare activities is on behalf of Govt. of India.

Hence, the contribution made by PSUs under CSR project should be treated on

par with expenditure made by the Govt. of India and should be excluded from the levy of service Tax.

Suggestion:

Request to issue Clarification to the effect that Contributions made to Corporate Social Responsibility (CSR) Projects is not leviable to service Tax

(25) **Denial of whole Cenvat credit of Service Tax on the LSTK contract on the ground that the part of the Cenvat credit relates to civil construction activities.**

Typically, an EPC contract is awarded for construction of a major project by the Employer to the EPC contractor. Under the capacity expansion projects which are undertaken at the Refinery, lump sum or LSTK contracts are awarded which includes both mechanical and civil construction.

It is practically difficult to determine the portion of mechanical and civil jobs involved in such works contract.

It is requested that CBEC may specify that in case of LSTK contact, where the value of civil construction is not specified in a LSTK contract, an ad hoc specified ratio of the total contract value will be construed towards civil construction services and only proportionately CENVAT credit pertaining to ad hoc ratio will be only disallowed.

II. **Cenvat Credit Rules**

(26) **Resolution of problem in credit distribution under Input service distribution scheme after 01.04.2012**

Rule 7 of Cenvat Credit Rules'2004 providing for Manner of Distribution of credit by Input service Distributor has been substantially modified w.e.f 01.04.2012 and w.e.f. 01.04.2014 (Not. No. 05/2014 Dated 24.2.2014) whereby the methodology of distribution has been substantially changed.

The amended rules inter-alia provides that credit of service tax attributable to service used in more than one unit shall be distributed pro rata **on the basis of the turnover during the relevant period of the units to the sum total of the turnover of ALL units irrespective of the fact whether service relates or not**.. Turnover means the sum total of the value of -

a. All excisable goods cleared during the relevant period including exempted goods, dutiable goods and excisable goods exported.
b. Export turnover of services and value of all other services
c. All inputs removed as such under rule 3(5) of Cenvat credit rules under an Invoice.

It may be appreciated that it would be very difficult for an undertaking having multiple locations to calculate turnover (which may be different from the turnover of books of accounts) based on above definition every time when credit distribution has to be made

The amended provision has made distribution both difficult and restrictive for the following reasons:

- **In case of a company having multiple units (say 10 units) will have to distribute its credit related to even 2-3 units to all 10 units including units which are not related for the service/activity.**
- The methodology of distribution prescribed in the rules is very cumbersome and complicated.

It appears from the rules that input services used at the administrative offices of ISD located away from the manufacturing/service providing units is not permissible which may not be the intention of the government.

Suggestion:

It is suggested that Rule 7(d) may be amended to state "credit of service tax attributable to service used by more than one unit shall be distributed pro rata on the basis of the turnover of such units, which are operational in the current year, during the said relevant period"; for, the above seems to be the intention of the Govt.

(27) **Transfer of Cenvat Credit by a large tax payer unit from one registered unit to another**

As per the erstwhile Cenvat Credit As per rule 12(A)(4) of the Cenvat Credit Rules, a large taxpayer unit was allowed to transfer Cenvat Credit from one registered premises to another registered premises, however w.e.f. 10.07.2014, the said facility has been withdrawn.

It may be appreciated that the concept of Large Taxpayer unit was introduced to facilitate large businesses and render single-window services to them. The facility of inter-unit transfer of Cenvat Credit was also one of the main feature of LTU concept.

Suggestion:

It is suggested that Rule 12A may be suitably amended so as to restore the provision of inter-unit transfer of Cenvat Credit by a Large Taxpayer Unit.

III. Excise Duty

(28) Non-applicability of unjust enrichment for captive consumption, provisional assessment, pre-deposit etc.

In Chapter 7, Para 6.7.2, Kelkar Committee has recommended that the provisions of unjust enrichment should not be applied for refunds consequent to the finalization of provisional assessments, pre-deposit of duty and goods captively consumed. This was not implemented in any of the subsequent budgets. There is a pressing need to implement atleast in the current budget in line with the recommendations and also for consequential refunds where duty was paid suo moto under protest or duty was recovered by adjustment of refund, pending initiation of adjudication/appeal proceedings.

(29) Exemption to the supply of goods under International Competitive Bidding contracts

- Customs Notification No. 12/ 2012 and Excise Notification No 12/2012 provide an exemption from the supply of goods effected under International Competitive Bidding (ICB) for specified purposes, subject to the fulfillment of specified conditions.
- The term ICB is not defined under the Customs or Excise Notifications, Act, Rules. Thus, it is a very subjective area of interpretation as to whether the supplies of goods are made under ICB or not?
- Generally, when international players are permitted to bid on a contract and a suitable advertisement is issued to this regard in a national/international newspaper etc, this should be sufficient to construe that the supply of goods is effected under the ICB.
- However, in the absence of any guidelines on this matter, Field Formation are denying the benefit of exemption of supply of goods under ICB stating various reasons such as:
  - ✓ A proper advertisement was not issued in a national or international newspaper etc or even if the advertisement is issued, the term ICB is not mentioned in advertisement
  - ✓ Proper procedure of Request for Proposal and Bidding was not followed
  - ✓ Selection of respective participants was not done in the specified manner
  - ✓ Contract was issued to local vendor even though the foreign vendors were only eliminated at the bidding stage
  - ✓ Extension of contract awarded in continuance of an earlier contract issued under ICB cannot be construed as supply of goods made under ICB

- The intention of the legislature seems to allow the benefit when the foreign players are competing with Indian players. Thus, the bid inviting/permitting to tender/bid by a foreign and Indian player should be construed as ICB and thus, the benefit of exemption should be extended to all such contracts.
- It is requested that a Circular is issued by the CBEC to clarify the necessary conditions to be fulfilled for a contract to be construed as ICB compliant contract.