

Most Immediate

F.No. 19/4/2007-FT(ST)
Government of India
Ministry of Commerce & Industry
(Department of Commerce)

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Udyog Bhavan, New Delhi
Dated the 1st July, 2008

Office Memorandum

Subject:- Inputs for 13th Finance Commission

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The undersigned is directed to refer to communications from Chairman and Secretary, Finance Commission on the subject mentioned above and to forward herewith the views of the Department of Commerce.

1. Reimbursement of State level taxes/duties levied on exports:

Exports have been one of the prime contributors as growth engine for sustained economic development in India. Export growth of India in last 5 years has been remarkable. In 2007-08, our merchandise exports have exceeded US \$ 155 billion whereas it was a little over US \$ 63 billion in 2004. This means our exports are not just double of what they were 4 years ago, but 2½ times of that. The average cumulative annual growth rate (CAGR) of exports at 23%, year on year, was way ahead of the average growth rate of international trade.

Our total merchandise trade was US \$ 400 billion last year, accounting for nearly 1.5% of world trade. If the trade in services is added to this, our commercial engagement with the world would be in the region of US \$ 525 billion. Our total trade in goods and services is now equivalent to almost 50% of our GDP.

Government has committed to an ambitious target of achieving a 5% share in world trade by the year 2020. In practical terms, this means a four-fold increase in our percentage share in the next 12 years. Considering that world trade is itself increasing, this would translate into an eight-fold increase in absolute terms. It means we would have to ensure an average annual growth rate of 25% consistently for the next 12 years. This target seems to be achievable based on the macroeconomic indicators such as growth in GDP, the growing % of trade, in particular the exports, to GDP etc. For the current year 2008-09, Government has fixed a target of US \$ 200 billion.

Exports are not just about earning foreign exchange but about boosting our manufacturing sector, creating large scale economic activity and generating fresh employment opportunities. On the issue of employment, as per an estimate, during the last 4 years increased trade activity has created 136 lakh new jobs.

The present sustained growth in exports have been accomplished in the face of appreciation of the rupee (by more than 12% in the last year alone), high interest rates, spiralling oil prices, withdrawal of some GSP benefits to India by other

countries and general international economic slowdown in some of our major trade markets.

Government of India firmly believes that Goods and services are to be exported and not the levies and duties. In the Indian Context, there are not only Central Levies and taxes but also a plethora of taxes levied by the State Governments, which are Non-VATable.. Agreement on Subsidies and Counter-vailing Measures (ASCM) in WTO also provides for exemption / re-imburement of all such Indirect taxes which have been incurred in the manufacture of the exported products. Though the Central Indirect Taxes such as Customs duty, Excise Duty etc. on inputs are being re-imbursed on the exported goods by way of Duty Exemption schemes such as Advance Authorisation Scheme, Duty Free Import Authorisation Scheme etc and Duty Remission schemes such as Duty Drawback Scheme, Duty Entitlement Passbook Scheme (DEPB) etc, Indirect taxes levied by State Governments however remain un-rebated, in particular for the units operating in DTA. Some of these duties/levies having significant impact on the cost of the export products are Central Sales tax (@2% since 2008), Electricity Duty, Sales Tax on Petroleum Products, Octroi, Mandi Tax, Entry Tax etc. Even VAT, which has been exempted on exports by only a few States, a large proportion of VAT refund remains delayed thereby increasing the cost of funds for the exporters.

There have been a large number of representations from the stake holders viz., trade bodies, associations, EPCs, exporting community on the increase in cost of their product, due to a large number of State Taxes and levies, which remain un-rebated. State-wise list of such un-rebated taxes and levies are listed at Annexure-I. Cumulative effect of these taxes / levies range from 3% to 12% of the FOB value, based on the product and its State of origin. [1% to 9% for electricity duty, CST, Sales Tax on Petroleum Products as per NCAER Report and the rest on account of Mandi Tax / Fee, Entry Taxes, and Octroi, Municipal levies and other taxes and cesses]

Relief from these State Indirect taxes is a legitimate goal which is tune with the commitment of Government of India that 'only goods and services are exported, not the levies and duties', and would in any case be self-limiting as CST is abolished and as the country moves towards GST.

GOI has constituted a High Powered Committee for suggesting modalities for operationalisation of GST w.e.f. 2010. With the introduction of GST, it is expected that all taxes, whether levied by Central or State Governments, would be subsumed in the GST. Since GST would not take into consideration the local duties / cesses / fees, the need for re-imburement of these non-VATable State Taxes / duties / cesses / fees would continue even after 2010 and our export competitiveness would suffer as a result of these levies.

Financial implication on rebate of State Cumulative non-VATable Indirect Taxes will vary with the coverage of the scheme. As per a rough estimate, Average rate for such rebate on exports would be 3.01 % i.e., 2.74% (for the components of electricity duty, Sales Tax on petroleum products and Central Sales Tax @ 2%) + 0.27 % (approx. for the component of Octroi, Mandi Tax, turnover tax, entry tax etc). After 2010, when CST will be completely withdrawn, the surrogate average rate will be 1.89%. With the present export growth rate of 23%, India's merchandise export turnover will be \$234 billion (Rs 9828 billion approx) by 2010 and \$660 billion (Rs 27720 billion approx) at the terminal year of the Thirteenth Finance Commission award. Hence financial implication on rebating of these un-

rebated State Indirect taxes will be around Rs 18500 crores for exports of \$234 billion and Rs52390 crores for exports of \$660 billion.

The Finance Commission is, therefore, requested to evolve a Scheme whereby the unremitted State Taxes are refunded to the exporters. Since most State Governments are unwilling/ unable to refund these taxes, it would be in order to allow the Central Government to reimburse these State Taxes/Duties paid by the exporters and recover the same from out of the payments due to the States as per the devolution formula approved by the Finance Commission. An appropriate provision for this may be incorporated in the final recommendations of the Finance Commission.

2. Reimbursement of amounts spent for welfare of plantation workers:

Plantations crops such as tea, coffee, rubber and cardamom are mostly grown in Kerala, Tamil Nadu, Karnataka, Assam and West Bengal. There are other States who are minor players in plantation crops. The activities in plantation sector are perennial in nature and thus provide round the year employment to the workers. Being an agro-processing activity, it promotes a lot many ancillary activities. The sector has contributed significantly to the finances of the Union, States and local bodies. It is employing over one million workers.

Tea

Tea industry is the oldest industry in the country. India is the largest producer and consumer of the tea in the world accounting for 28 per cent of world production and 14 per cent of the world trade. Export of tea is around 20 per cent of the domestic production. The production of tea has risen from 845.97 million kgs in 2002-03 to 945.27 million kgs in 2007-08, whereas the domestic consumption has risen from 693 million kgs to 786 million kgs during the same period. While the import of the tea has decreased from 22.49 million kgs to 16.75 million kgs. The volume of exports has fallen from 184.40 million kgs to 155.59 million kgs in the same period.

Coffee

Coffee is primarily cultivated in about 3.83 lakh hectares in India, principally cultivated in Karnataka, Kerala and Tamil Nadu. The production had risen to above 3 lakh tones in 2001-02 and 2002-03. However, thereafter it stagnated to around 2.75 lakh tons in 2007-08. Due to crop loss an account of heavy rainfall in 2007-08, production has come down to 2.62 lakh tons. Exports have increased from 2.13 lakh tones in 2001-02 to 2.49 lakh tones during 2006-07. During 2007-08 the exports have been fallen to 2.23 lakh tons.

Rubber

Rubber is primarily cultivated in Kerala and in the Kanyakumari district of Tamil Nadu. Total area under rubber cultivation is nearly 6.15 lakh hectares. The rubber economy is primarily domestic centric with insignificant export. The

production has gone up to 825000 tonnes (provisional) in 2007-08 from 631400 tonnes in 2001-02.

The tea industry in India dates back to the 19th century. The life of a plant is, on an average, 60 years. The viability of the industry has been severely affected recently and there is a steep decline in the profitability of the industry. All is not well in the tea industry is further revealed from the declining Indian share in global trade. Lower share imply that Indian tea is losing out to competitors. It is a reflection on the health of the industry. In the early 1970's India's share in the global trade for tea was 33.4%. It has been steadily declining to 31.3% in 1975, 27.7% in 1980, 22.1% in 1990, and 14.4% in 1995. Presently it is around 10% (2007-08). Though the magnitude of the problem is small yet the symptom is indicative of some deeper malice undermining the competitiveness of the Indian tea industry in comparison to green field plantation countries such as Kenya, South Africa etc.

The coffee industry in India employs 10 lakh workers, out of which 5 lakh workers are employed in coffee farms and the remaining are in other coffee related activities. The unique feature of employment of workers in coffee farms is that the coffee farms are situated in the bio sensitive and remote regions located in the western and eastern ghats of South India and the workers employed are uneducated, unskilled and belong to the weaker section of the society.

In rubber, 89% of the area of the plantations are small holdings and workers employed in the sector are not provided with any welfare measures by any agencies except the Rubber Board. The welfare measures include Housing Subsidy Schemes, Medical Stipend Scheme, Merit Award Scheme and Group Insurance cum Deposit Schemes. The large sector plantations are covered under Plantation Labour Act 1951 and the welfare measures envisaged under the Act like drinking water, road and electricity are provided by the employers.

The Plantation industry comprising tea, coffee and rubber etc., is functioning under the regulatory environment of Plantation Labour Act, 1951, the Tea Act, Coffee Act, and the Rubber Act. The respective Acts primarily deal with promotional and developmental aspects of these commodities.

The Plantation Labour Act is a Central Act enacted by the Union Government but is administered by the respective States where the plantations are located. The Plantation Labour Act is primarily a welfare legislation enacted to ensure welfare facilities to make a person a satisfied worker with most of the aspects of the daily living taken care of by the plantation estate/employer. The Act, in Chapter-III, prescribes detailed provisions in respect of health care of the workmen. This includes arrangements for drinking water, conservancy and medical facilities. In addition to health care, the Act also provides for welfare facilities like canteens, crèches, recreational/ educational facilities and housing.

Hence, every employer has to provide the facilities as provided for under the Act. Unlike other industrial labour, given the nature of the Act, there is considerable financial pressure on the plantation employers. While the average capital expenditure per hectare is Rs. 716.31, the recurring expenditure comes to Rs. 7098.16 per hectare. It is estimated that the social costs incurred by plantation owners would amount to between Rs. 8 to 14 per kg. In an age of global competitiveness, this additional burden on the plantation owners only in India renders the products globally uncompetitive. At the same time, it is to be noted that the State Governments are getting allocation for the plantation workers based on the total population in the State. However, the State Governments, citing the provisions of the Plantation Labour Act do not spend any money for the welfare of the plantation labour. Benefits of housing, drinking water, electricity, schools, roads and other social amenities in the plantations are left to the plantation owners and the State Governments have abdicated their entire responsibility. At the same time, the local bodies collect various amounts of taxes/ cess from the plantations. In view of the difficult situation faced by many plantation owners, the quality of the social services provided have also deteriorated in recent years. The State Governments have abdicated their responsibility for providing social services to the plantation labour on the ground that they cannot fund the construction of private roads within plantations nor can they provide housing/ drinking water facilities as the land is either owned/leased to the plantation owners and is not in the name of the plantation labour. It is, therefore, suggested that the Finance Commission may either direct the State Governments to ensure that social service amenities are provided to the plantation labour by their respective State Governments or in the alternative earmark an appropriate provision for this to the Central Government, Department of Commerce, based on the plantation population in the country and the Central Government would then, through the respective Commodity Boards provide the funds to the plantations for the social amenities like housing, roads, schools, water supply etc. since the total number of plantation workers is estimated at about 17 lakhs, it is estimated that during a five-year period, a total amount of Rs. 4000 crores should be earmarked for the Central Government (Department of Commerce) so as to provide the facilities like housing, roads, water supply, electricity to the plantation workers and their families.

3. Provision of Funds for creation of export related infrastructure:-

Department of Commerce has been mandated to provide conducive environment for facilitating Export and Import from the country. At National level, the Central Government has taken major initiatives to develop infrastructure. National Highway network, railways, major ports, airports and national waterways are being developed and maintained by the Central Government either directly or through organisations under it. However, there is a critical need to focus on infrastructure specifically catering to facilitating exports.

Special Economic Zones, Export Clusters and manufacturing/ processing/packing units engaged mainly in exports located in the various States require state-of-the-art infrastructure including power, water, sanitation etc. and

also roads/connectivity to the main national infrastructure grid. The States which could provide these infrastructure supports have seen exponential growth of their industry and other allied sectors. However, in respect of many other States, such a support has not been made available due to a number of reasons. It is a fact that many States do not provide adequate support to exports as they do not derive any direct fiscal benefits as most of these export clusters do not pay taxes. Even if these clusters provide employment, they do not appear to be a prime mover in motivating States for improving the infrastructure for exports. On the other hand, exports have directly contributed to value addition in manufacturing, sustainability of traditional handicrafts, deceleration in migration to urban areas, growth in wages, migration of key technology to the country and increased comfort in terms of foreign exchange reserves.

Under the ASIDE Scheme of the Ministry of Commerce & Industry, launched in 2002, funding for infrastructure directly linked with exports has been taken up. A sum of Rs.2050 crores have been spent in the 10th Plan and it is proposed to spend a further a sum of Rs.3600 crores in the 11th Plan. But it is felt that there will still be a huge gap in the availability of infrastructure for exports.

With a view to developing infrastructure for exports, various Ministries handling infrastructure have been sensitised on the need to improve infrastructure specifically with reference to improving infrastructure used by industries and services for exports. With a serious gap in the general infrastructure in the country, it is not clear how the various Ministries would be approaching the issue of deficit in infrastructure for exports.

The Thirteenth Finance Commission, while making devolution under its award, should favourably consider the objective of creating infrastructure and specifically filling up gaps in infrastructure for exports. Towards this in view, it will be appropriate if the Thirteenth Finance Commission sets apart funds to be utilised by the States for providing and strengthening infrastructure for exports. A sum of Rs.20000 crores will be required for the purpose for the five years of the award period of the Thirteenth Finance Commission. The States Government should be requested to focus its efforts for creating infrastructure in select clusters which have potential for exports. The States must develop infrastructure on a PPP mode using these funds.

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ANNEXURE -

S.No	Name of the States	Unrebated State Indirect Taxes / Levies								
		Central Sales Tax (CST)	Electricity Duty	Sales Tax on Petroleum Products	Entry Tax	Octroi	Turnover Tax	Surcharge, if any	Mandi Tax	Others, if any
1	Andhra Pradesh	3% with C form otherwise local VAT rate will apply (seller VAT will apply)	25 paise per unit (but case is running in the court)	Petrol : 33%, Diesel: 22.25% and Lubricants: 12.50%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Cess is levied on marine products @0.25% on FOB
2	Assam	3%	Not Applicable	Petrol : 20%; Diesel : 12%; Others : 4 to 20%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
3	Bihar	3%	6% on Energy Drawn	Petrol: 27% Diesel: 22%	8%	Not Applicable	Not Applicable	Not Applicable	8%	-
4	Chattisgarh	3%	On generation as well as consumption (details awaited)	Petrol: 25% Diesel: 25%	1%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-

5	Delhi	3% (otherwise local VAT rate will apply)	5%	Petrol: 20% Diesel: 12.5% (Vatable)	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
6	Goa	3%	40 paise per unit	Petrol: 25% Diesel: 23%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
7	Gujarat	3%	40 paise per unit	Petrol: 26% Diesel: 24%	Not Applicable	0.25% to 10%	Not Applicable	Not Applicable	Not Applicable	-
8	Haryana	3%	38 paise per unit 5 paise per unit (Municipal Corpn. Tax)	Diesel (12%) Petrol (20%)	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Available	Toll tax : Rs.1500-2000 per truck for inward and outward movement
9	Himachal Pradesh	1% on Manufacturers & 3% on Traders against Form C	0.01% per unit (Municipal Corpn. Tax)	Petrol: 25% Diesel: 14%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
10	Jammu & Kashmir	3%	22% on the price of energy	Petrol: 20% Diesel: 12%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Toll Tax : Rs.40/- per quintal

11	Jharkhand	3%	7 paise per unit	Petrol: 20% Diesel: 20%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
12	Karnataka	3%	5%	Petrol: 28% Diesel: 20%	Petro Products : 5% Capital Goods : 2%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
13	Kerala	3%	8% of the energy charge; Electric Cess 10 paise per unit	Petrol: 26.04% Diesel: 22.42%	High Court of Kerala had held that Kerala Tax on Entry of Goods into local areas 1994 is unconstitutional. The matter is pending before the Supreme Court	Not Applicable	In respect of foreign liquor @10% at every point of sale	Not Applicable	Not Applicable	-
14	Madhya Pradesh	3%	8% and Electric Cess 10 paise per unit	Petrol: 28.75% Diesel: 28.75%	Average 6.5% including cess	Not Applicable	Not Applicable	Not Applicable	2.2%	-

15	Maharashtra	3%	30 paise per unit	Petrol: 29% for Mumbai, Thane & Navi Mumbai & for others 30% Diesel: 34% for Mumbai, Thane & Navi Mumbai & for others 31%	Not Applicable	5.5 to 7%	1%	Not Applicable	Not Applicable	-
16	Manipur	3%	Not available	Petrol: 20% Diesel: 12.5%	Not Applicable	Yes	Not Applicable	Not Applicable	Not Applicable	-
17	Meghalaya	3%	Not available	Petrol: 20% Diesel: 12.5%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
18	Mizoram	3%	Not Applicable	Petrol: 20% Diesel: 12%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
19	Nagaland	3%	Not available	Petrol: 20% Diesel: 12%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
20	Orissa	3%	8% on Energy Drawn	Petrol: 20% Diesel: 20%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	1% - 12%	-
21	Punjab	3%	10%	Petrol: 27.5% Diesel: 8.8%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Available	Purchase Tax

22	Rajasthan	3%	40 paise per unit	Petrol: 28% Diesel: 20%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	1.6%	Toll Tax : Rs.1000 per container
23	Sikkim	3%	Not Applicable	Petrol: 20% Diesel: 12.5%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
24	Tamil Nadu	3%	5% on net energy charges	Petrol: 30% Diesel: 25%	Selected products like Electrical goods, Iron Aluminium products, LDPE & HDPE etc. are subject to entry tax ranging from 4% to 30%. Set off is given on entry tax paid on raw material.	Not Applicable	Rs.1000/- every half year (Corporation of Chennai)	Not Applicable	Not Applicable	9% Stamp Duty and Registration Fee on Land Purchase for Industrial purpose
25	Tripura	3%	Not available	Petrol: 20% Diesel: 12.5%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-

26	Utter Pradesh	3%	9 paise per unit	Petrol: 25% Diesel: 21%	2%	Not Applicable	Not Applicable	Not Applicable	Mandi samiti tax - 1% on leather; different for other products	Development Tax for units having turnover of more than Rs.50.00 lacs. Tax is levied @1%
27	Uttranchal	3%	Not Applicable	Petrol: 25% Diesel: 21%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	-
28	West Bengal	3%	13.30% Energy Drawn	Petrol: 25% Diesel: 17%	Not Applicable	Not Applicable	Not Applicable	Not Applicable	Not Applicable	1% Marketing Committee Fee