

SEZ unit cannot remove capital goods under the EPCG scheme without exiting from SEZ scheme – CESTAT

21 September 2023



Summary

The Customs, Excise and Service Tax Appellate Tribunal (CESTAT) Ahmedabad Bench has held that an active Special Economic Zone (SEZ) unit cannot remove capital goods under the Export Promotion Capital Goods (EPCG) scheme. The CESTAT observed that the legislative provisions clearly specified that the EPCG scheme could only be utilised at the time of exit from the SEZ, and the same cannot be allowed to be freely availed at any time. The CESTAT further stated that the SEZ unit can remove capital goods only with the one-time approval of the Development Commissioner (DC) once the SEZ ceases to exist. Consequently, the CESTAT dismissed the appeal and upheld the Commissioner's (Appeals) order.

Facts of the case

- ISGEC Heavy Engineering Ltd. (the appellant) is engaged in manufacturing heavy machinery (Chapter 84 of the Customs Tariff Act, 1985). It filed a bill of entry (BoE) for import capital goods, namely a plate bending machine consisting of three rollers, mobile control panel, air cooler, the CNC control unit and all related complete items and accessories for their sister concern, M/s ISGEC Heavy Engineering Ltd, located in the domestic tariff area (DTA) under the Export Promotion Capital Goods (EPCG) scheme, authorised by an EPCG license issued to M/s ISGEC Heavy Engg. Ltd.
- The goods were initially imported into a special economic zone (SEZ) unit from Switzerland by another entity. The value of these capital goods was assessed, and accordingly, the total duty exemption was granted.
- The clearance of the said capital goods under the EPCG scheme was allowed under provisional assessment as per the provisions of SEZ Act/Rules. The customs department contended that as the clearance under the EPCG was supposed to be allowed only at the time of the SEZ exit since the appellant had not exited from the SEZ and did not

have the necessary permission from the Development Commissioner, they were not eligible to clear the capital goods under the EPCG scheme.

- Consequently, the customs department sought to rework the value of the goods and demanded the payment of the applicable customs duties.
- After following due legal procedures, the lower authority finalised the assessment, ordered the payment of the said duties, and appropriated the amount already paid.
- On appeal, the order of the specified officer was upheld by the Commissioner (Appeals).
- Being aggrieved with the impugned order of the Commissioner (Appeals), the appellant has filed an instant appeal before the CESTAT Ahmedabad Bench.

Issues before CESTAT Ahmedabad:

- Is the appellant's SEZ unit legally permitted to sell capital goods to its DTA buyer under an EPCG authorisation without exiting from the SEZ?
- Whether the demand for customs duty and interest by the customs authorities is legally valid?

Appellant's contentions:

- The appellant asserted that their SEZ unit had the legal right to sell the goods to their DTA unit under the EPCG authorisation. They argued that SEZ laws explicitly allow the sale of capital goods from SEZ units to the DTA, provided applicable duties are paid.
- They relied on legal precedents and customs circulars to support their interpretation of SEZ laws, which allows DTA buyers to avail exemptions when importing goods from SEZs. The appellant contended that SEZ laws should be liberally interpreted to promote economic growth, and no restrictions should be imposed on the benefits provided.
- The appellant argued that Rule 74 of the SEZ Rules did not explicitly limit EPCG benefits to the time of the SEZ unit exit.
- The appellant submitted that DTA buyers could obtain EPCG authorisation for capital goods procurement, and they had not violated SEZ law in this regard.
- The appellant insisted that customs duty and interest should not be demanded from either the SEZ unit or the DTA buyer, as the latter has fulfilled its export obligation (EO) and criticised the impugned order for lacking reasoning and violating principles of natural justice.

CESTAT Ahmedabad's observations and ruling (Custom Appeal No. 12023 of 2018 vide order dated 11 September 2023):

- **Interpretation of relevant SEZ provisions:** Rule 74(4) of the Special Economic Zone Rules, 2006 (SEZ Rules), provides that capital goods are allowed to be removed in DTA after use in a SEZ on the payment of duty and the depreciated value counted from the date of commencement of production. This is a special provision for the exiting units through which the Development Commissioner has been allowed to

permit the unit as a one-time option to exit from the SEZ on payment of duty on capital goods into the prevailing EPCG scheme under the Foreign Trade Policy subject to the eligibility criteria under the EPCG Scheme. Thus, the CESTAT stated that the EPCG scheme is intended to be available only at the time of exit from the SEZ, and attempting to utilise the EPCG scheme outside of the exit process goes against the legislative intent.

- **One-time option:** Basis Rule 74(4) of the SEZ Rules, the CESTAT stated that it is clear that the clearance of capital goods under the EPCG scheme is a one-time option given while exiting from the SEZ. When the legislature has made a special provision by mentioning a particular export promotion scheme to be availed only at the time of exit, the same cannot be allowed to be freely availed at any time under a provision in which there is no prescription of capital goods to be cleared under the EPCG scheme.
- **Statutory interpretation principle:** The CESTAT emphasised on the principle of statutory interpretation, which explained that adherence to a prescribed method or condition in a statute implies the prohibition of alternative methods. It emphasised the strict adherence to explicit legislative mandates when transitioning between different schemes for capital goods and also laid the importance of complying with international trade rules and agreements.
- **CESTAT upheld Commissioner's (Appeals) order:** The CESTAT stated that in the present instance, the

stipulation of one-time availment of the EPCG scheme at the time of the exit cannot be read as permitting availment of the EPCG scheme under Rule 34 of SEZ Rules. Particularly under the expression 'on license' appearing in that rule. Further, the EPCG scheme is not available till the exit from the SEZ unit and nor has the appellant produced any such mandate or opinion from administrative authorities like the Development Commissioner approving such availment by the customs. Therefore, the CESTAT upheld the Commissioner's (Appeals) order.

Our comments

Rule 74 of the SEZ Rules specifically provides that the Development Commissioner may permit a SEZ Unit, as a one-time option, to exit from a special economic zone on payment of duty on capital goods under the prevailing Export Promotion Capital Goods scheme under the Foreign Trade Policy, subject to the unit satisfying the eligibility criteria under that scheme.

Thus, the CESAT has emphasised the principle that a specific method prescribed by law prohibits alternative actions, even if not explicitly prohibited, and held that SEZ units could clear capital goods under the EPCG scheme only at the time of exit from the SEZ and cannot be availed normally for clearing capital goods under Rule 34 of the SEZ Rules.

The decision is likely to open a pandora's box for other assessees with similar transactions and is expected to come under the Revenue's scanner.

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