

Fiscal and Non-fiscal Issues Concerning Textiles

I. FISCAL DUTIES

(a) Excise Duty and Service Tax

(i) Man-made Fibres

Present Position: Mandatory excise duty of 4 percent on all man-made fibres.

Proposal: Excise duty on all man-made fibres may be abolished.

Justification: Among major textile producing countries, man-made fibre based textile products have the lowest share in our industry. Uncompetitive fibre prices in the domestic market are the primary reason for this. Removal of duties would encourage increased utilisation of man-made fibres and this will help in correcting the mismatch in the pattern of fibre consumption between the domestic and global textile industries.

(ii) Accumulated Cenvat Credit

Present Position: Cenvat credit continues to accumulate with T&C units.

Proposal: Refund all accumulated cenvat credit of T&C units. Rule 5 of the Cenvat Credit rules has to be amended suitably in order to facilitate refund of accumulated cenvat credit in T&C units.

Justification: Since most of the textile and clothing units are in the optional route for excise duty, cenvat credit accumulated by them cannot be utilized. In the case of cotton textile products, excise duty has now been reduced to zero and for man-made fibre products to 4%. Huge cenvat credits were accumulating with manufacturers of man-made fibre products even earlier, since fibres had mandatory duty. With reduction in excise duty for textile products, the possibility of using such credit for payment of excise duty has reduced further for man-made fibre products and the problem has also spread to producers of cotton textiles. Accumulated cenvat credit for some of the units in the textiles industry runs into crores, eroding their working capital substantially.

(iii) Textile Machinery, Components and Spares

Present Position: 4-8% excise duty on machinery and 8% on all components and spares.

Proposal: Reduce duty to 4% for all textile machinery, components and spares.

Justification: We have a nascent textile machinery industry which is currently in a position to cater to only 30% of the machinery requirements of our textile industry. For garments, there are practically no domestic machinery supplies. For machines which are currently at 4% duty, there is an inverted duty structure, since their components and spares attract 8% duty. Stipulating a rate of 4% across the board for machines, components and spares will remove this anomaly and assist in the growth of the machinery industry.

(iv) Liquid Fuels such as furnace oil and diesel used for captive power generation by T&C units

Present Position: Subject to 14% excise duty

Proposal: Exempt all liquid fuels used for captive power generation by T&C units, from excise duty.

Justification: There is tremendous power shortage in major States producing textiles. Therefore captive power generation is the only alternative to sustain production. With current fuel prices, captively generated power is more than twice as expensive as grid power. Removal of duties will make captive power generation more viable.

(v) Terminal Excise Duty

Present position: Excise duty is collected when domestic machines are sold against EPCG licenses and subsequently refunded when funds are received from Government.

Proposal: Excise duty on machinery procured from the domestic market against EPCG licenses may be exempted.

Justification: The present procedure only results in avoidable delay.

(vi) Service Tax

Present Position: Service Tax on many of the pre production services is taken into account while calculating drawback rates. Many post production services have been notified for refund of service tax to exporters.

Proposal: Exempt T&C industry from all service taxes

Justification: Services being taken into account for drawback calculations and services notified for refund do not cover all the services. In the case of refund, even service taxes on the notified services are not always getting refunded

because of procedural complications. There is delay in reimbursements even where refunds are available. Exemption is viable, feasible and therefore desirable.

(b) Customs Duty

(i) Man-made Fibres

Present Position: Basic customs duty of 5% charged.

Proposal: Abolish customs duty on all man-made fibres.

Justification: Prices of man-made fibres in India are higher than global prices, since domestic producers sell mostly at import parity prices. Abolition of customs duty would make imports more viable and will encourage domestic producers to reduce prices and thus make man-made fibre based textile products more competitive in global markets. This will help in establishing a larger base for man-made fibre textiles and clothing industry in the country. Charging customs duty on man-made fibres is an anomaly, when cotton is allowed for import at zero duty.

(ii) Liquid Fuels such as furnace oil and diesel used for captive power generation by T&C units

Present Position: 10% basic customs duty.

Proposal: Abolish customs duty on all liquid fuels used for captive power generation by T&C units.

Justification: There is tremendous power shortage in major States producing textiles. Therefore captive power generation is the only alternative to sustain production. With current fuel prices, captively generated power is more than twice as expensive as grid power. Removal of duties will make captive power generation more viable.

(iii) Textile Machinery

Present Position: Basic Customs Duties ranging from 5% to 10% are applicable.

Proposal: Abolish customs duty on all machinery for textiles and clothing, except for spindles.

Justification: Currently domestic textile machinery industry is able to supply machinery of contemporary technology only in the case of spindles. Until domestic industry is able to produce machinery of acceptable quality at

affordable prices, customs duty on other textile machinery needs to be abolished in order to ensure proper supply of technology to the textile industry.

(iv) Special Additional duty

Present Position: A special additional duty of 4 percent is charged on fibres and many other products, towards state duties levied on similar domestic products.

Proposal: Exempt fibres and all inputs for T&C industry from SAD.

Justification: Though SAD is cenvatable, this facility is practically not available to T&C units, since they are in the exemption route for excise duty.

(c) Corporate Tax

(i) Minimum Alternate Tax

Present Position: 11.33% of book profit is charged, even if company has not made profits and generated enough cash.

Proposal: Provide exemption for T&C industry

Justification: Most T&C units are now making losses or negligible profits and therefore will not be able to use MAT credit entitlement.

(ii) Dividend Distribution Tax

Present Position: 16.995% is charged (15% tax + 10% SC+3% EC)

Proposal: Exempt T&C Industry

Justification: With global recession and slowdown in domestic economy, financial position of T&C units is extremely weak and dividend distribution tax would further erode the financial position of the units.

(iii) Fringe Benefit Tax

Present Position: Roughly around 7% of income is paid as FBT by T&C units

Proposal: Exempt T&C units from FBT

Justification: Sluggish markets necessitate extra marketing efforts including foreign travels. FBT makes such efforts costlier and adds to the losses of the units.

(iv) **Surcharge**

Present Position: 10% for all Corporate Taxes

Proposal: Exempt T&C industry

Justification: In the present financial position of T&C units, this exemption will help their efforts for survival.

II. BANKING

(i) **Rescheduling of Term Loans**

Present Position: Rescheduling being allowed at discretion of banks on case-to-case basis mostly for less than one year, even when allowed.

Proposal:

- (a) Rescheduling of loans may be allowed for all T&C units by permitting deferment on repayment of principal amounts for 8 quarters on condition that the interest will continue to be paid during this period. RBI may issue the necessary directions in this regard.
- (b) A two year extension may be allowed for the repayment period for term loans, in order to accommodate the rescheduling as per (a) above.
- (c) Under TUFS, extension of repayment period may be permitted beyond the currently stipulated 10 year period, in order to accommodate the rescheduling.

Justification: Banks are overcautious in case-to-case examination of proposals for rescheduling. Unless a mandatory directive is given, rescheduling will only happen in very few cases and for very short periods. In the absence of rescheduling, most term loans in the T&C industry would turn into NPAs, creating serious problems both for the industry and for the banking sector.

(ii) **Interest Subvention for Export Credit**

Present Position: 2% subvention available upto 30th September 2009.

Proposal: 4% subvention to be allowed until March 2010.

Justification: Interest rates in India are higher than those in most competing countries. 4% subvention had been announced in 2007 for the period upto 31st

March 2009. This was withdrawn from 1st October 2008. Subsequently 2% subvention was reintroduced in the stimulus package for the period upto 31st March 2009 and later extended to 30th September 2009. The entire 4% interest subvention needs to be reinstated w.e.f. 1st October 2008 and continued upto 31st March 2010 in order to arrest the current decline in exports in the context of the global economic slowdown.

(iii) Working Capital for Cotton

Present Position: Interest rate = PLR
Margin Money = 25%
Duration of Loan = 3-6 Months

Proposal: Interest rate = 7%
Margin Money = 10%
Duration of Loan = 9 Months

Justification: The over 40% increase in MSPs introduced for the current cotton year has pushed up domestic cotton prices and deceleration in profitability has seriously affected the ability of Indian mills to buy cotton. In this context, these facilities are necessary for mills for purchasing and stocking of cotton. This will ensure prompt cotton purchase and higher consumption and will, therefore, be helpful to farmers also.

(iv) Corporate Debt Restructuring

Present Position: The benefit of reduction in PLR is not fully passed on by banks to the units seeking CDR. Other benefits are also denied in most cases.

Proposal: The CDR Cell should take a liberal approach to the proposals submitted to them after assessing the techno-feasibility report of the unit. They should give concessions based on the sustainable debt of the individual units and take a pragmatic approach with regard to interest rates and infusion of funds by promoters.

Justification: RBI guidelines require promoters to contribute 15% of the sacrifice made by the banks; but banks are pressurizing the promoters to bring in 20-30% of sacrifice amount as promoters' contribution. Banks are also insisting on pledging of 30% of the share capital by the promoters. These measures adopted by the banks are extremely harsh and practically negate the benefits of CDR.

(v) Delayed Government Dues

Present Position: Accumulated cenvat credit and delays in payment of TUFs assistance, refund of TED, rebate of excise on exports etc. are eating into the scarce working capital of T&C units.

Proposal: Banks may be asked to consider all delayed dues from government as receivables for assessment of working capital for T&C units.

Justification: There is no uncertainty in payments due from government. The problem is only of delay. Treating such delayed payments as receivables will improve the working capital position of the units and reduce the adverse impact of the delays to some extent.

III. OTHERS

(i) Export Incentives for Cotton

Present Position: 5% incentive under Vishesh Krishi and Gram Udyog Yojana (VKGUY) effective from 1st April 2008 to 30th June 2009.

Proposal: Withdraw the incentive w.e.f. from 1st April 2008.

Justification: Cotton is a primary raw material for the textile value chain. Stock-to-use ratio for cotton in India is less than half of global standards which means that we have no exportable surplus. In this situation, there is no justification for incentivising exports. Export incentive has pushed up cotton prices in the domestic market making our cotton textiles even more uncompetitive in global markets. It also transfers the benefits of the progress made by our cotton sector to the textile industries of our competitors.

(ii) TUFS Assistance

Present Position: Currently, full interest is recovered by banks and then TUFS assistance is disbursed, when funds are received from Government.

Proposal: Exempt instead of refunding

Justification: There has been a backlog of around one year in disbursement of TUFS assistance, since sufficient funds are not allocated by government. Since Government has decided to extend this interest compensation, doing it through exemption route rather than refund route would make it more effective and useful.

(iii) Wind Turbine Generators

Present Position: Allowed only within 25% limit stipulated for other expenses under TUFS.

Proposal: Permit without restriction

Justification: Power shortage is a major problem in most textiles producing States. In States where wind energy is available, this can be an effective alternative. This needs to be encouraged by extending TUFs assistance to wind energy generators used by T&C industry, without restrictions.

(iv) Hank Yarn Obligation

Present Position: 40% of yarn production to be packed on hanks by all spinning mills, except in the case of hosiery yarn and export production.

Proposal: Abolish Hank Yarn Obligation

Justification: With drastic reduction in handloom fabric production, there is a decline in demand. Hank yarn obligation forces mills to produce excess hank yarn, without any guarantee that they will be able to sell it. Mills will pack yarn on hanks to cater to available demand, for commercial reasons. Forcing mills to produce hank yarn beyond the available demand does not help anybody and harms spinners seriously. Reduction of Hank Yarn Obligation from 50% to 40% a few years back has had no impact on the market. So will be the case if the obligation is abolished.

(v) MSP for Cotton

Present Position: More than 40% increase in MSP for cotton year 2008-09 has pushed the cotton economy to a crisis.

Proposal: Withdraw MSP for Cotton or dispose of procured cotton promptly at international prices.

Justification: Unlike food items, cotton is an industrial raw material. In recent years, market prices have been providing sufficient remuneration to cotton farmers. Unreasonable increase in MSPs has created problems this year for everybody in the cotton economy including cotton farmers who have not been able to sell even half of the cotton at the declared MSPs. MSPs have resulted in our cotton textile products being out-priced in global markets in a situation where international markets are already in turmoil. If it is considered necessary to provide subsidies to cotton farmers, this should be from Government funds. Cross subsidy through the textile industry will be against the interest of the economy as a whole.

(vi) Drawback Rates

Present Position: Reduced substantially in September 2008.

Proposal: Restore pre reduction rates. Take fuel duties into account for calculation of Draw Back rates.

Justification: Drawback rates and DEPB rates were reduced together in September 2008. As part of the stimulus package, DEPB rates were completely restored. For the same reason, drawback rates should also be restored in full. Restoration of DEPB Rates was not based on examination of any fresh cost data; restoration of drawback rates should also be on similar lines. Current drawback rates and other export incentives for textile exports are substantially lower when compared with what is available in our major competing countries and this is affecting our export performance significantly. Fuel duties and infrastructural disabilities also need to be taken into account while determining Draw Back rates. In the T&C industry, most exporters use Draw Back rather than DEPB.

(vii) State Level Duties

Present Position: Not refunded to exporters either by Central Government or by State Governments.

Proposal: May be refunded by Central Government

Justification: CST, electricity duty, mandi tax, entry tax and other local as well as state level duties and taxes amount to 4-6% of FOB value of export in various textiles producing States. All taxes are admittedly refundable to exporters. Until GST is established, it is not practicable for State Governments to refund these taxes and duties because of the involvement of multiple States in textile value chain. Therefore, the only feasible alternative is that the Central Government should refund these and then reduce the amounts from the allocation to State Governments from the central pool, if necessary.
