

Did Adani Group Evade ₹1,000 Crore Taxes?

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The corporate conglomerate headed by Gautam Adani has been accused by the Directorate of Revenue Intelligence of having allegedly evaded taxes and laundered money to the tune of around ₹1,000 crore while trading in cut and polished diamonds and gold jewellery. The DRI has claimed that companies in the Adani Group misused export incentives and indulged in high-velocity circular trading through a complex web of front companies located in different parts of the world. The government seems strangely reticent about filing a review petition in the Supreme Court that could protect its revenue interests.

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For more than a decade now, the Directorate of Revenue Intelligence (DRI) has been investigating how a clutch of companies in the Adani Group led by Gautam Adani allegedly evaded taxes and laundered money while trading in cut and polished diamonds and gold jewellery. The DRI, which is an investigative wing of the Department of Revenue in the Ministry of Finance, has issued a number of show-cause notices to firms in the group alleging evasion of taxes to the tune of roughly ₹1,000 crore. Adani is considered to be close to Prime Minister Narendra Modi.

While the allegations against the Adani Group have meandered through various tribunals and courts of law, questions are being raised as to whether the Ministry of Finance is deliberately dragging its feet in moving a review petition before the Supreme Court that could safeguard its revenue interests. Four detailed questionnaires were sent by the *Economic & Political Weekly* (EPW) to (i) Finance Minister Arun Jaitley and five of his senior officials; (ii) the Minister of State for Commerce and Industry Nirjala Sitharaman and the Director General of Foreign Trade; (iii) Law Minister Ravi Shankar Prasad; and (iv) Adani himself. These questionnaires were emailed and also sent by regular post on 18 November 2016. Whereas spokespersons of Adani and the law minister responded, Jaitley, Sitharaman and officials in their respective ministries did not answer the questions more than a month and a half after these were sent to them.

Here is the story in a nutshell. A set of firms in the Adani Group apparently misused various export-incentive schemes through a complex web of front companies located in different parts of the world. These shell companies, which indulged in high-velocity “circular trading”

among related corporate entities, were also used to launder money, the DRI has claimed. All the corporate entities were directly or indirectly controlled by, or associated with, Adani Enterprises Limited (AEL), a flagship firm of the Adani Group which was called Adani Exports Limited before 2007. The DRI has alleged that AEL flagrantly misdeclared the freight on board (FOB, also called free on board) values of cut and polished diamonds (CPD) and gold jewellery.

The investigative agency has also claimed that group companies and their associates indulged in circular trading to “artificially” inflate exports and “fraudulently” avail of financial benefits from various export promotion schemes initiated by the Directorate General of Foreign Trade (DGFT) in the Ministry of Commerce and Industry (MCI). Such schemes included the Incremental Export Promotion Scheme introduced by the DGFT in 2003–04 under which came the Target Plus Scheme (TPS) introduced in the Foreign Trade Policy 2004–09. Responding to the EPW’s questionnaire, a spokesperson of the Adani Group denied these allegations. Copies of the various show-cause notices issued by the DRI to group companies are with the EPW and material from these notices has been drawn for this article.

Misuse of Export Promotion Schemes

Among the different export promotion schemes initiated by the MCI, a particular scheme sought to provide certain corporate entities exporting goods or services called “trading houses” to avail of benefits that are proportionate to the quantum of exports achieved. Trading houses are ranked on the basis of their total annual exports and the highest exporters are designated “star trading houses.” For 2003–04, the DGFT announced a scheme called the Duty Free Credit Entitlement (DFCE) scheme.

Under the DFCE, certain benefits were provided to trading houses recognised by the government as star trading houses or “status holders.” Specific exporters were recognised as status holders “on the basis of the FOB/NFE (net foreign

exchange) value of goods and services ... as well as on the basis of services rendered by the service provider during the preceding three licensing years or the preceding licensing year, at the option of the exporter.” Under the DFCE scheme, a status holder would receive financial benefits equal to 10% of the total incremental exports achieved in 2003–04 over the exports in the previous financial year, that is, 2002–03, provided the incremental growth was at least 25%.

AEL and its group/associate companies had earlier been exporting various commodities from foodgrain to textiles. The Adani Group had a relatively small export turnover of just over ₹400 crore in 2002–03. The DRI has claimed that after the announcement of the DFCE scheme, AEL formed a consortium with different corporate entities to “artificially inflate” its exports to take advantage of the scheme. These five group companies were Hinduja Exports Private Limited (HEPL), Aditya Corpex Private Limited (ACPL), Bagadiya Brothers Private Limited (BBPL), Jayant Agro Organics Limited (JAOL) and Midex Overseas Limited (MOL). It is further alleged that in addition to these five Indian companies, AEL directly and indirectly managed and controlled 45 overseas corporate entities.

In 2003–04, the total export turnover of AEL suddenly jumped more than 11 times, to be precise, by 1,181%. The turnover of HEPL rose by as much as 160 times (16,624%), ACPL's by over 150 times (15,819%) while that of MOL rose more than seven times (765%) in these two years (Table 1).

Besides the DFCE, other export promotion schemes that were introduced by the DGFT included the TPS in September 2004 which offered incentives to status holders varying between 5% and 15% of the incremental growth in the turnover of exports (Table 2). Initially, studded gold jewellery and CPD were permitted to be included while calculating the FOB figure and therefore, towards claiming incentives under the TPS.

Table 1: Rise in Export Turnover of Adani Group Companies between 2002–03 and 2003–04 (₹ crore)

	Adani Exports	Hinduja Exports	Aditya Corpex	Midex Overseas	Adani Group (Total)
2002–03	377.44	4.15	2.68	28.26	412.53
2003–04	4,838.53	694.07	426.63	244.60	6,203.83
% increase	1,181.93	16,624.58	15,819.03	765.53	1,403.85

Source: <https://indiankanon.org/doc/1510260/>.

DGFT Notifications

On 31 March 2007, the DRI issued a show-cause notice pointing out that there had been a sudden and unprecedented increase in the Adani Group's export turnover of CPD, gold jewellery, rough diamonds and third party exports (all of which could be included at that time in calculating the figure of “incremental” growth of exports for availing benefits from the DGFT) between 2003–04 and 2004–05. According to the notice, the bulk of these exports took place after September 2004 when the TPS was introduced.

The following year, the group's exports came crashing down. In 2005–06, the total exports of the Adani Group were barely a third of that achieved in the previous year. Exports of CPD and articles of gold came down sharply. Why? Simply because the benefits were withdrawn after the government realised that the export promotion schemes were being misused. As the MIC became aware of the misuse of the Incremental Export Promotion Scheme, some amendments were made to the EXIM policy. In January 2004, the DGFT issued a number of notifications clarifying that exports of precious metals in any form, including plain jewellery and rough, uncut and semi-polished diamonds and third-party exports would not be permitted for inclusion in calculating the FOB figure.

The amendments were opposed by AEL and other exporters. They contended that the notifications were seeking to withdraw benefits already given to exporters. On 7 February 2004, AEL filed a petition in the Gujarat High Court challenging the validity of the notifications issued on 28 January that year. On 23 July, the court (in *Adani Exports Limited v Union of India (UOI)*) ruled against AEL and others upholding the validity of the

Table 2: Incentives under the Target Plus Scheme

Percentage Incremental Growth	Duty Credit Entitlement (% of incremental growth)
20% and above but below 25%	5%
25% or above but below 100%	10%
100% and above	15% (of 100%)

Source: DGFT.

notifications. AEL then filed a special leave petition (SLP) in the Supreme Court. The DGFT also filed an SLP against the order of the high court. Appeals were also filed by other firms and the government in similar cases against the orders of various high courts—such appeals included ones filed by Kanak Exports, the UOI and the DGFT challenging an order of the Bombay High Court.

The EXIM policy was later further amended (through notifications issued on 23 February 2005 and 20 February 2006) to exclude studded gold jewellery and certain categories of products (diamonds and other precious, semi-precious stones) from the list of items entitled to receive export benefits under the TPS.

Findings by Supreme Court

In October 2015, the Supreme Court upheld the appeals filed by the DGFT and the UOI, dismissing the appeals filed by others. It was pointed out that there had been a spectacular rise in the turnover of two firms, Rajesh Exports and Kanak Exports, between 2002–03 and 2003–04 (Table 3). The more than 2,000% rise in

Table 3: Exports of Relevant Exporters

Name of Firm	Turnover 2002–03 (₹ crore)	Turnover 2003–04 (₹ crore)	% Growth	Share of Gold Coins and Plain Jewellery in Total Exports (%)
Rajesh Exports, Bengaluru	112	2,372	2,017	100
Kanak Exports, Mumbai	27	1,070	3,816	100

Source: <http://www.advocatekhoj.com/library/judgments/announcement.php?WID=6714>.

exports came entirely in the form of gold coins and jewellery. For Adani Exports, over 80% of its export turnover came from diamonds and supplies from status holders. In other words, the Adani Group would not have met the minimum turnover and growth criteria that had been laid down in the EXIM policy and the amended DFCE scheme (Table 4, p 37).

It is evident from Figure 1 (p 37) that the export turnover of AEL rose sharply from ₹377 crore in 2002–03 to ₹4,657 crore the following year and further to ₹10,808 crore in 2004–05. This sudden spurt in turnover occurred during the period AEL availed of benefits from the DFCE scheme and the TPS. Subsequently, when in 2004 the DGFT issued

notifications clarifying that the particular items would not be eligible for export incentives under the DFCE scheme (in 2004) and the TPS (in 2005 and 2006), AEL's export turnover collapsed. The Supreme Court pertinently observed that there was a 1,135% surge in AEL's exports during 2003–04, whereas the company's exports had declined in the preceding six years.

The division bench of the apex court comprising Justices A K Sikri and Rohinton F Nariman used very harsh language to highlight how the firms “misused” benefits by “fraudulently” inflating export turnover, citing “conclusive” evidence of how AEL increased its exports of rough diamonds despite the fact that India is not a rough diamond producing country. The order reads,

The same set of diamonds were rotating and these never entered the Indian domestic territory or to the end consumers abroad. The value of such exports in the past two years may exceed ₹15,000 crore ... Many of these exporters exported to their own counterparts in Dubai and Sharjah. The jewellery attracted a 5% import duty at Dubai, the consignments were declared as jewellery in India but were declared as scrap in Dubai to avoid the import duty. (*DGFT and Another v Kanak Exports and Another* 2015)

Setting aside the direction of the Bombay High Court granting the exporters benefits of incentive schemes that had

accrued in the past, the Supreme Court bench concluded,

It was pernicious and blatant misuse of the provisions of the Scheme and periscope viewing thereof establishes the same. Thus, the impugned decision reflected in the notifications dated 21 and 23 April 2004, did not take away any vested right of these exporters and amendments were necessitated by overwhelming public interest/considerations to prevent the misuse of the Scheme. Therefore, we are of the opinion that even when (the) impugned Notification issued under Section 5 could not be retrospective in nature, such retrospectivity has not deprived the writ petitioners/exporters of their right inasmuch as no right had accrued in favour of such persons under the scheme. This Court, or for that matter the High Court in exercise of its writ jurisdiction, cannot come to the aid of such petitioners/exporters who, without making actual exports, play with the provisions of the Scheme and try to take undue advantage thereof.

DRI Investigations against Adani Group Firms

The network of the Adani Group is worth mapping. Adani Enterprises Limited (which was earlier Adani Exports Limited or AEL) is a public limited company in which Gautam Adani and his brothers Rajesh Adani and Vasant Adani are directors. With Samir Vora (Gautam Adani's brother-in-law) at the helm of affairs, ACPL and HEPL (partnership firms that were taken over by the Adani Group) played the role of the proverbial knights on the chessboard while MOL, JAOL and

BBPL were the pawns. Pursuant to these MOUs, Deven Mehta (director, HEPL) was appointed as the authorised signatory for BBPL and JAOL while Saurin Shah and Vishwas Shah (employees of AEL) were appointed as signatories for MOL. The alleged “collusion” among the firms and their representatives resulted in accrual of benefits to HEPL and ACPL under the TPS and to the signatories of AEL who allegedly gained between 2% and 2.5 % of the FOB value in an unauthorised manner, the DRI has claimed in its show-cause notice (Table 5).

The DRI has alleged that the import and export operations of all six companies were handled by Vora. The DRI went on to claim that total exports of CPD by the Indian companies in the Adani Group in 2004–05 were worth \$1,643.02 million, out of which goods worth \$1,314.19 million (or 79.98% of the total) were exported to eight specific companies situated in the United Arab Emirates (UAE), Hong Kong and Singapore. Similarly, during 2004–05, out of the total imports worth \$1,641.68 million, imports worth \$1,304.13 million (79.44%) were from only seven companies in the countries mentioned. Similar patterns emerged for 2005–06 as well. Two Hong Kong-based companies, Kwality Diamonds and Seven Stars and four UAE-based companies, Excel Global, Jewel Trade, Crown Diamonds and KVK Diamonds, acted as suppliers and buyers of the CPD and from AEL and its group companies. In addition, eight companies—Wingate Trading, Sphere Trading, Global Enterprises, Top Rich (all in Hong Kong), Planica Exports Private Limited, Emperor Exports Private Limited, Gracious Exports Private Limited and Orchid Overseas Private Limited (in Singapore)—were all incorporated after September 2004 after the introduction of the TPS. Wingate Trading, Sphere Trading, Top Rich and PNJ Trading stopped their business activities in 2005. This, according to the DRI, suggests a clear link between the way in which trading malpractices took place and the timing of the DGFT notifications.

Further, the proprietor of three companies, namely, Wingate Trading, Sphere Trading and PNJ Trading, was one

Figure 1: Export Turnover of Adani Exports Limited (1997–2006)

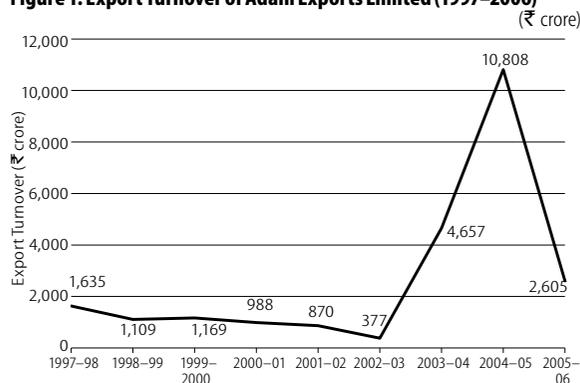


Table 4: Export Turnover of Adani Exports Limited, Ahmedabad, during 2003–04

	Exports (₹ crore)
Total	4,657
(I) Rough, and re-exported polished diamonds	2,475
(II) Supplies taken from status holders not meeting the minimum turnover and growth criteria	1,316
Share of categories (I) and (II) in the total exports	81.4%

Source: <http://www.advocatekhaj.com/library/judgments/announcement.php?WID=6714>.

Nishaben Vijay Gandhi. While PNJ Trading exported CPD to Indian firms from Hong Kong, Wingate and Sphere imported CPD from the same set of Indian companies. These transactions took place among the firms at profit margins varying between 5% and 10% and would return full circle at a remarkable velocity. According to the DRI, goods imported were often exported out of India on the same day! Theoretically, the same goods could have been exported more than 100 times in a year and in terms of the

Table 5: Export of CPD by Adani Group Companies

Year	AEL	ACPL	HEPL	MOL	JAOL	BBPL	Total
2002-03	20.31	0.00	0.00	0.00	0.00		20.31
2003-04	1,465.27	0.00	94.23	0.00	0.00	0.00	1,559.23
2004-05	5,626.67	662.31	1,064.15	329.34	201.79	162.78	8,047.04
2005-06 (up to Jan 2006)	1,193.64	1,311.27	2,258.80	849.86	544.37	296.26	6,454.20

AEL—Adani Enterprises Limited (earlier Adani Exports Limited); HEPL—Hinduja Exports Private Limited; ACPL—Aditya Corpex Private Limited; BBPL—Bagadiya Brothers Private Limited; JAOL—Jayant Agro Organics Limited; and MOL—Midex Overseas Limited.

Source: Show-cause notice issued by the DRI.

various slabs of incentives under the TPS, an unscrupulous exporter could have earned a phenomenal ₹1,500 for every ₹100 invested, the DRI has calculated.

The story was no different in Singapore. There was a common set of five directors shared across AEL's trading partners. Email messages reproduced in the DRI's show-cause notice that were retrieved by the Directorate of Forensic Sciences indicated that AEL controlled and managed its trading partners in Dubai, Hong Kong and Singapore.

Circular Trading of Studded Gold Jewellery

In 2009, the DRI issued a fresh set of two show-cause notices alleging that AEL and its associate companies, HEPL, ACPL and MOL, that had allegedly availed of extraordinary benefits under the TPS, also indulged in fraudulent "circular trading" by importing gold bars of 995 purity from the UAE and then exporting the goods in the form of crude studded gold jewellery purity back to the UAE. The jewellery was subsequently melted down and imported back to India in the form of gold bars to boost the group's export turnover. What is remarkable is the rate at which these activities took place: between September 2004 and February 2005, the firms in the Adani Group exported over 59,500 kilograms (kg) of what is supposed to be

studded jewellery valued at over ₹3,843 crore (\$861.40 million).

The entire trading operations involving first, import of gold jewellery into the UAE and export of gold bars from the UAE; second, receipt of funds for the exports into accounts of dummy exporters of the gold bars; and finally, payments of funds from the accounts of dummy importers of studded gold jewellery, were controlled and managed by the employees of Adani Global FZE, Dubai, which is a subsidiary of Adani Exports and GA International.

Adani Global FZE, Dubai is a company owned and managed by Vinod Shantilal Shah, also known as Vinod Shantilal Adani, the older brother of Gautam Adani.

Interestingly, these export orders comprised gold bangles weighing anywhere between 100 grams (g) and 240 g and pendants weighing over 70 g each. Studded jewellery of such dimensions, using gold with 995 purity, is rare in the jewellery business due to the inability of pure gold to hold precious stones. This has been argued by the DRI. The lengths of the production cycle and the export cycle of this jewellery were unbelievably short: more than 100 kg of the goods were manufactured within two to three days of the receipt of gold by the workers and the goods were then promptly exported. In particular instances, the export consignments each weighed as much as 500 kg, which is reportedly unusual. Moreover, the Indian firms charged an exorbitant 7% as "making charges" to artificially inflate the value of the goods exported, the DRI has alleged.

The investigation also unearthed that Adani Global FZE had insured itself against the risk of storage and transport of the jewellery and gold bars. This insurance policy was bought from Oman Insurance Company, Dubai. The fact that Adani Global FZE obtained an insurance policy covering not only itself but other

importers and exporters in these operations, which included the refinery where the gold scrap was melted down and converted into gold bars, speaks of the "dubious" nature of these transactions, the DRI has alleged. At the time when Adani Global FZE bought the insurance policy, it had neither imported any gold jewellery nor exported gold bars. Further, after the DGFT issued notifications amending the EXIM policy in February 2005, the companies abruptly stopped exporting studded gold jewellery. The value of export incentives obtained by the Adani Group companies in this specific instance was more than ₹575 crore (\$130.68 million).

Abuse of the DFCE Scheme

Permission for setting up private or public bonded warehouses was obtained by AEL from the customs department in July 2003 after the introduction of the Incremental Export Promotion Scheme. This, in effect, meant that goods imported, stored, manipulated and exported from these warehouses would be exempt from payment of customs duty. In accordance with the TPS, AEL imported CPD and re-exported the same after value addition of 5%. This has been shown in the company's books of accounts. The Adani Group firms obtained DFCE certificates from the DGFT and utilised these for importing gold and silver without paying duty, that is, by claiming exemption from payment of duty under the Incremental Export Promotion Scheme. In its application to the DGFT, AEL also acknowledged that it did not take into account the re-export of imported goods while computing the value of exports.

The DRI notice issued seeks to establish that exports of CPD made by AEL were squarely covered as re-export of imported CPD. Further, these imported gold bars, after conversion into 100 g bars, were sold in the open market. Hence, the gold and silver bars imported without payment of duty under the DFCE scheme cannot be accounted as inputs for the CPD exported by AEL and would be liable for payment of customs duty. The DRI has alleged that this was done intentionally in circumvention of the July 2004 order of the Gujarat High Court prohibiting the inclusion of gold exports in the DFCE. This order of the

Gujarat High Court was upheld by the Supreme Court in the case of Kanak Exports. The DRI notice proposed confiscation of the seized 250 gold bars (of 1 kg each) imported by AEL and confiscation of around 25,000 kg of gold bars and 31,000 kg of silver bars together valued at more than ₹4,000 crore.

Artificial Value Addition

There are a few thousand instances of circular trading that have been detailed in the DRI's notices. The firms claimed value addition of 5%–10% in their official books of account although all that was done was to sort, sieve and clean the diamonds by boiling them in water. Such activities do not involve great technical expertise and, if the DRI is to be believed, raise doubts about the genuineness of the transactions that have been recorded. The imports and exports of diamonds took place in small dingy rooms measuring 10 feet (ft) by 12 ft inside the bonded warehouse where manufacturing activities are disallowed, the DRI has alleged.

After the DRI issued show-cause notices, in an adjudication order issued in January 2013, the commissioner of customs, import (Mumbai) held that:

- (i) No processing was carried out by any of the six notices to achieve value addition of 5%–10%.
- (ii) The notices have not shown how simple processes of boiling, sieving and assortment, if carried out, can result in value addition of 5%–10%.
- (iii) The FOB value declared in the shipping bills by simply adding 5%–10% of the CIF (cost, insurance and freight) value is artificial and hence, the export value declared should be rejected under Section 14 of the Customs Act, 1962.

The commissioner then imposed a penalty of ₹25 crore on AEL and penalties of ₹2 crore each on the five other companies. Additionally, it imposed heavy penalties on the directors of all six companies, including Gautam Adani's brother Rajesh Adani and brother-in-law Samir Vora. The commissioner upheld the charges made in the DRI's notices that tax benefits to the tune of ₹1,000 crore had been fraudulently obtained by the Adani Group companies.

To recapitulate, the DRI had from 2007 onwards alleged that the companies had misdeclared the FOB value of export goods in contravention of the Foreign Trade (Development and Regulation) Act, 1992 and Foreign Trade (Regulation) Rules, 1993; that the group through its directors had entered into a "conspiracy" with people and entities based in Singapore, Dubai and Hong Kong to undertake "dubious" imports and exports of diamonds to take undue benefits of the TPS; entered into MOUs with group companies for claiming incremental exports; misdeclared value addition of 5%–10% by assortment, boiling, sieving and repacking without any manufacturing/processing or change in the form of the cut and polished diamonds; and failed to declare details of commission payable in shipping bills. It was estimated that benefits worth ₹679.62 crore were claimed by AEL and its associate companies in 2004–05 and an additional ₹218.16 crore were claimed in 2005–06.

The Reversal: CESTAT Order

A development then took place that shocked the DRI. The order of the commissioner of customs was set aside by the Mumbai bench of the Customs, Excise and Service Tax Appellate Tribunal (CESTAT), Western Zone. By an order dated 9 April 2015 which was issued more than four months later on 26 August that year, CESTAT members Anil Choudhary and P S Pruthi summarily dropped all the charges against the Adani Group. The tribunal chose to accept the FOB value declared by the companies and disagreed with the DRI's claim that there had been circular trading. The CESTAT disagreed with the commissioner that "no process" had been carried out in the bonded warehouse since the diamonds were sorted, sieved and boiled. It disagreed with the commissioner that these "processes" could not have added value to the extent of 5%. The tribunal was of the view that the "transaction values" of the CPD were "genuine" and that foreign exchange had been "fully realised" through the sales proceeds. The allegedly fraudulent intentions with which the value of exports were misdeclared

and artificially inflated as well as the claims of circular trading were all effectively ignored by the CESTAT.

The tribunal ignored the evidence that the DRI had adduced to its show-cause notices to indicate circular trading. One such piece of evidence was an email exchange between different employees of group companies, including Adani Global. The first names of these employees were Asha, Mary, Rakesh, Tejal and another employee was S M Shah. According to the DRI, these email exchanges indicate that the same set of diamonds would be imported, exported, imported again and re-exported from and to India, Dubai and Singapore in a cyclical manner.

The CESTAT also chose to ignore a letter dated 26 May 2015 written by the additional DGFT to the joint secretary (drawback), Central Board of Excise and Customs in the Finance Ministry which stated,

there are cases of circular trading and many other types of mischief reported under the Target Plus Scheme ... Such petitioners do not become eligible for such shipping bill claims as per the judgment of the Supreme Court. So, any claims arising on account of such shipping bills may be disallowed. Therefore, (the) Department of Revenue and (the) DRI are requested to give the complete list of exporters along with details of Shipping Bills who have misused under both the schemes (the DFCE and/or the Target Plus Scheme).

Officials in the Income Tax Department and the Enforcement Directorate (who spoke to the lead author of this article on the condition that they will not be identified) said that no investigations had been conducted nor action initiated by their respective departments. A senior customs officer based in Mundra port (through which many of the consignments of diamonds were imported and exported and which is part of the Adani Group) said a number of disputes relating to alleged misuse of export benefits were pending with the DGFT. "The Adani cases are among the many hundred revenue-sensitive matters on which DGFT has not taken a decision and this is because there is no audit of, or accountability in, the proceedings of the DGFT," said this person.

A senior official of DGFT, who too spoke to the lead author of this article on

the condition of anonymity, explained, the best course of action will be to ensure that no benefits are given under the TPS scheme and the benefits that have already been availed of under the DFCE scheme (for exports in 2003–04) be declared *void ab initio*. Since the exports of CPD have been held to be fraudulent by the Supreme Court in the Kanak Exports case, the benefits under the DFCE already issued to AEL should also be disentitled. It is unfortunate that there are no clear guidelines for expeditious action in such cases of fraud.

A Systemic Problem

On 31 March 2016, the Reserve Bank of India (RBI) relaxed the rules applicable to importers of rough cut and polished diamonds. It permitted banks to approve a “clean credit” facility extended by foreign suppliers to Indian importers of CPD beyond the stipulated 180-day period. Clean credit refers to the credit facility extended by foreign suppliers to Indian importers without imposing the requirement of the need to furnish a letter of credit or a fixed deposit to serve as an underlying guarantee.

While it is contended that this move is intended to ease operational difficulties faced by importers, experts monitoring the diamonds trade suggest that this could be an invitation to fresh trouble. One such person said that these provisions can be easily abused by importers to launder money, that it is quite easy to create an offshore corporate entity that could import goods from an Indian exporter and delay remittances, or worse still, default on payment. This expert apprehended that such malpractices could undermine the financial positions of banks. On one side, the trading firm’s books of accounts would show higher receivables as a part of its balance sheet which may serve as a premise to obtain more credit from Indian banks even as the unscrupulous trader would by then have encashed the proceeds from the sale of the diamonds in, say, Hong Kong, to move the assets out of India.

The systemic nature of such fraud is worth noting. A report by the Financial Action Task Force, released in October 2013, titled “Money Laundering and Terrorist Financing through Trade in Diamonds” stated that India, which accounts for more than 90% of the total

business of CPD in the world, has seen instances of companies grossly overvaluing the goods they exported. The report explained how such activities are conducted and operationalised to transfer sums of foreign exchange outside India, giving examples of diamonds round-tripping back to India at inflated prices.

In its judgment in the Kanak Exports case, the Supreme Court highlighted another instance of mis-utilisation of export incentives relating to Reliance Industries Limited (RIL) and its group company IPCL (formerly India Petrochemicals Corporation Limited). The Court said that RIL and IPCL “manipulated” export turnover to maximise export benefit entitlements under the DFCE scheme and the TPS. It held that IPCL had artificially inflated its export performance in 2003–04 and was hence not eligible for benefits under the DFCE scheme. The Court observed that goods worth ₹2,127.18 crore manufactured by RIL were exported in the name of its group company IPCL to claim extra benefits under the DFCE scheme. A DRI report had earlier stated that RIL lowered its export turnover for 2003–04 by a similar amount to show that it had achieved a rate of growth of exports above 100% (between 2003–04 and 2004–05) to claim TPS benefits at the rate of 15%. The Supreme Court upheld the DRI’s contention in this instance.

Conclusions

The DRI filed an appeal against the CESTAT order in the Supreme Court which was disposed of on 12 April 2016. The Ministry of Finance now has to file a review petition against this decision. The question that remains unanswered: what has dissuaded the ministry from filing this review petition even though more than nine months have gone by?

According to a Delhi-based lawyer familiar with the case who (like the others) spoke to the EPW on condition of anonymity, “the entire argument of the DRI is premised on a DGFT notification which was upheld by the Supreme Court in 2015 in the Kanak Exports judgment.” The advocate added that this case is of great significance since it is first relating to circular trading which has reached

the doors of the country’s apex court. He said that if the revenue department fails to convince the Supreme Court about its case against the Adani Group through its review petition, the “consequences could well be disastrous for the government as this could affect all circular trading cases that are in the pipeline.”

A questionnaire was sent by the EPW to Ravi Shankar Prasad, Union Minister of Law and Justice, seeking to enquire if his ministry would recommend a review of the Supreme Court’s decision on the DRI’s appeal against the CESTAT order. A response came from Saurabh Kumar, additional private secretary to the minister, who said the questions should be sent to the finance ministry and the MCI.

As already stated, a detailed questionnaire sent on 18 November 2016 to Finance Minister Arun Jaitley, copies of which were marked to the revenue secretary, the chairman, Central Board of Excise and Customs, the chairman, Central Board of Direct Taxes, the director, Enforcement Directorate and the Director General, DRI, were not replied to. On the same day, another questionnaire was sent to Minister of State for Industry and Commerce Nirmala Sitharaman and the director general, Foreign Trade, which also went unanswered.

In response to the EPW’s questionnaire, Jatin Jalundhwala, Chief Legal Officer for the Adani Group stated that the CESTAT had dealt with all the allegations made by the DRI, including those relating to circular trading and the relationships with overseas buyers and suppliers, and had set these aside. He stated that the CESTAT had held that all the exports and imports of CPD by the Adani Group were “genuine” and “thus, (the) FOB value of CPD exported cannot be re-determined.” Jalundhwala added that the Supreme Court by dismissing the appeal filed by the customs department also “affirmed the validity/genuineness of transactions of imports and exports ...”

REFERENCE

Financial Action Task Force (2013): “Money Laundering and Terrorist Financing through Trade in Diamonds,” *FATF Report*, October, <http://www.fatf-gafi.org/media/fatf/documents/reports/ML-TF-through-trade-in-diamonds.pdf>.