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B.Com Honours | Semester V | Calicut University

Indirect Tax Laws and Practice

Course Code: COM5EJ314 (7) • Module 1 Notes

MODULE I: INTRODUCTION TO INDIRECT TAXES & CUSTOMS LAW

FOUNDATIONS OF CONSUMPTION TAXATION, SHIFTING MECHANICS & CUSTOMS ARCHITECTURE

MODULE OVERVIEW

Indirect taxation constitutes the dominant fiscal pillar of modern state revenue, mobilizing transaction-based resources across production, import, distribution, and consumption chains. Unlike direct taxes that extract a portion of earned income, indirect taxes are embedded within the market price of goods and services, shifting the ultimate financial incidence to the end consumer. This module delivers an in-depth foundation in the law and practice of indirect taxation: the core conceptual features of indirect taxes, their vital distinction from direct taxes, their merits and demerits in national fiscal policy, an overview of the historic transition to the Goods and Services Tax (GST), and the comprehensive legal architecture of **Customs Duty under the Customs Act, 1962**. It explores the scope and territorial jurisdiction of customs law, essential statutory definitions (goods, customs area, dutiable goods, importer, exporter, coastal goods, and territorial waters), and the precise legal doctrine governing the **taxable event** in cross-border import and export trade.

Concepts & Features

Shiftability of burden, impact vs incidence, embedded pricing, universal coverage, regressive incidence, and fiscal merits.

GST Introduction

Destination-based consumption model, elimination of cascading barriers, 101st Amendment, and the unified dual architecture.

Customs Architecture

Customs Act 1962, territorial waters (12 NM), Indian customs waters (200 NM), key statutory definitions, and the taxable event.

1. Concept and Essential Features of Indirect Taxes

In fiscal jurisprudence, an **indirect tax** is a compulsory financial levy imposed upon the manufacture, import, sale, or supply of commodities and services, where the legal liability (impact) is placed on the commercial producer, supplier, or trader, but the ultimate monetary burden (incidence) is systematically shifted forward to the final consumer through embedded market pricing.

1. **Statutory Levy** → Government imposes legal tax liability (impact) on the manufacturer, importer, or registered supplier.
2. **Forward Shifting** → The registered supplier adds the statutory tax onto the commercial invoice, billing the buyer.
3. **Intermediate Credit** → Wholesalers and retailers offset input taxes, passing only incremental value-added tax downstream.
4. **Final Absorption** — The end consumer pays the gross retail price including tax and absorbs the ultimate incidence completely.

THE SIX DEFINING CHARACTERISTICS OF INDIRECT TAXES

CORE CHARACTERISTICS

1. Separation of Impact and Incidence

The person who pays the tax to the government treasury (the taxable person) and the person who actually bears the money cost (the consumer) are two distinct entities. The tax burden is passed through commercial contracts.

2. Commodity & Transaction Centric

Indirect taxes are not linked to the personal status or income wealth of the taxpayer. They are triggered strictly by commercial events: the physical import of cargo, the manufacture of goods, or the supply of services.

3. Hidden / Embedded Pricing

Indirect taxes are usually bundled into the retail Maximum Retail Price (MRP) (e.g., "*Inclusive of all taxes*"). Consumers pay the tax unconsciously during daily transactions, minimizing direct taxpayer resistance.

4. Universal Population Coverage

Unlike direct income tax which exempts the majority of citizens due to basic exemption limits, indirect taxes capture every human being who consumes goods, including daily-wage laborers, tourists, and students.

5. Regressive Distributive Profile

Because an indirect tax levies the exact same rupee charge on a commodity regardless of who buys it, it consumes a significantly higher proportion of a poor person's income than of a wealthy person's income.

6. Potent Regulatory Tool (Pigouvian Tax)

Governments utilize punitive indirect taxes (excise duties, sin cesses) to suppress socially harmful demerit goods (tobacco, alcohol, luxury sports cars, fossil fuels) and encourage merit goods through zero-rating.

2. Types of Indirect Taxes: Merits and Demerits in Fiscal Policy

In modern comparative public finance, indirect taxes are structured across several distinct operational models:

TAXONOMY OF INDIRECT TAX INSTRUMENTS

TAX TYPES

Tax Type	Operational Mechanism & Taxable Base	Practical Examples & Indian Context
Goods & Services Tax (GST) / Value Added Tax (VAT)	Multi-stage, comprehensive destination tax levied on value addition at each stage of supply, with full input tax credit offsetting previous taxes.	**Dual GST in India:** Central GST (CGST), State GST (SGST), and Integrated GST (IGST) levied on supplies of goods and services since July 1, 2017.
Customs Duties	Levied on the international movement of goods across sovereign national borders (import duties on inflows, export duties on outflows).	Governed by the **Customs Act, 1962** and Customs Tariff Act, 1975 to regulate foreign trade, protect domestic infant industry, and raise revenue.
Excise Duties	Levied on the physical manufacture or production of goods within the domestic borders of the country.	Retained in India post-GST on **five petroleum products** (crude, diesel, petrol, ATF, natural gas) and tobacco products.
Stamp Duty & Registration Fees	Levied on the execution of legal documents, deeds, commercial instruments, and real estate property transfers.	Major revenue source for **State Governments** under Entry 63 of the State List.

COMPREHENSIVE EVALUATION: MERITS VS. DEMERITS OF INDIRECT TAXATION

POLICY EVALUATION

Macroeconomic & Fiscal Merits

• **Vast Revenue Buoyancy:** Generates massive, predictable revenue flows that expand automatically with rising consumer spending and GDP growth.
• **Administrative Convenience:** Collected from registered businesses in large lump sums at transaction points, rather than auditing millions of individuals.
• **Broadened Tax Net:** Reaches the extensive informal sector, black money earners, and non-filers who evade direct income taxes.
• **Difficult to Evade:** Embedded in invoice billing; avoidance requires unrecorded black cash dealing.
• **Steering Public Consumption:** Effectively curbs demerit consumption of harmful goods via sin taxes.

Critical Demerits & Distortions

• **Regressive Nature:** Imposes a disproportionate economic sacrifice on low-income citizens who spend nearly all earnings on basic consumption.
• **Cost-Push Inflation:** Directly inflates the wholesale and retail prices of goods, increasing living costs and production expenses.
• **Absence of Civic Consciousness:** Concealed in prices; taxpayers do not realize the quantum paid, reducing democratic scrutiny of public expenditures.
• **Risk of Cascading:** Unless accompanied by comprehensive input tax credits, leads to tax on tax, inflating prices across supply chains.

3. Introduction to the Goods and Services Tax (GST)

Prior to 2017, India's indirect tax system was crippled by a fragmented labyrinth of overlapping Central and State taxes (Central Excise, Service Tax, State VAT, Central Sales Tax, Entry Tax, Octroi, Luxury Tax). This multiplicity caused severe economic distortions:

The Paradigm Shift: July 1, 2017 (101st Constitutional Amendment Act)

On July 1, 2017, India implemented the **Goods and Services Tax (GST)** under the constitutional motto "*One Nation, One Tax, One Market*". GST is a comprehensive, multi-stage, **destination-based consumption tax** levied on every value addition across the supply chain, designed with three foundational pillars:

1. **Destination Principle:** The tax revenue accrues to the State where the goods or services are ultimately consumed, rather than the State where they were manufactured.
2. **Seamless Input Tax Credit (ITC):** Credit for taxes paid on inputs is available at every stage of the supply chain, completely eradicating cascading tax on tax.
3. **Cooperative Federalism:** Administered under the joint authority of the Centre and the States through the constitutional **GST Council (Article 279A)**.

4. Introduction to Customs Duty & Scope of Customs Law

Customs Duty is an indirect tax levied by the Central Government on goods imported into, or exported from, India. Anchored constitutionally to **Entry 83 of the Union List (List I, Seventh Schedule)**, customs law governs cross-border merchandise trade:

THE DUAL LEGISLATIVE ARCHITECTURE OF INDIAN CUSTOMS LAW

CUSTOMS STATUTES

1. The Customs Act, 1962 (Machinery Statute)

• The substantive and procedural act governing the civil administration of customs.
• Outlines provisions for: levy and assessment of duties, prohibited imports/exports, appointment of customs ports and airports, clearance procedures for home consumption and warehousing, baggage rules, search, seizure, confiscation of smuggled goods, and prosecution.

2. The Customs Tariff Act, 1975 (Tariff Rates Statute)

• Specifies the statutory classification of all goods and the applicable rates of customs duties.
• **First Schedule (Import Tariff):** Standard and preferential import duty rates based on the international 8-digit **Harmonized System of Nomenclature (HSN)**.
• **Second Schedule (Export Tariff):** Specific export duties levied on select raw materials (iron ore, leather) to protect domestic supply.

Territorial Jurisdiction and Maritime Zones under Customs Law

Customs law exercises jurisdiction not only over the physical landmass of India, but extends across designated maritime zones governed by the **Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976**:

THE MARITIME ZONES OF INDIA UNDER CUSTOMS JURISDICTION MARITIME ZONES

Maritime Zone	Geographical Extent from Baseline	Scope of Customs Authority & Legal Enforcement
Territorial Waters of India (TWI)	Extends up to **12 nautical miles (NM)** into the sea from the appropriate baseline (1 NM = 1.852 km; 12 NM ≈ 22.2 km).	**Sovereign Territory of India:** India exercises absolute sovereignty over the water, seabed, and airspace. The moment an import vessel enters 12 NM, the importation process commences.
Contiguous Zone	Extends from the outer limit of territorial waters up to **24 nautical miles** from the baseline.	India exercises preventive control to prevent and punish infringement of customs, fiscal, immigration, or sanitary regulations within its territory or territorial sea.
Indian Customs Waters (ICW)	Extends up to the outer limit of the Exclusive Economic Zone: **200 nautical miles** from the baseline.	**Full Anti-Smuggling Enforcement:** Under Section 106 of the Customs Act, customs officers have the absolute power to stop, board, search, and seize any vessel suspected of carrying contraband within 200 NM.

5. Essential Statutory Definitions under the Customs Act, 1962

The interpretation and application of customs law depend upon precise statutory definitions codified under **Section 2 of the Customs Act, 1962**:

CORE STATUTORY DEFINITIONS UNDER SECTION 2 OF THE CUSTOMS ACT, 1962

CUSTOMS DEFINITIONS

Statutory Term & Section	Statutory Definition under the Act	Legal Scope & Practical Significance
"Goods" [Section 2(22)]	Includes: (a) vessels, aircrafts, and vehicles; (b) stores; (c) baggage; (d) currency and negotiable instruments; and (e) any other kind of movable property.	Extremely broad definition. Covers not only commercial merchandise, but also intangible computer software, electricity, blueprints, and international currency brought into the country.
"Customs Area" [Section 2(11)]	The area of a customs station or a warehouse and includes any area in which imported goods or export goods are ordinarily kept before clearance by customs authorities.	Includes sea wharves, airport cargo sheds, container freight stations, and bonded warehouses. Goods within a customs area remain under customs control and have not yet cleared the barrier.
"Customs Station" [Section 2(13)]	Any customs port, customs airport, international courier terminal, foreign post office, or land customs station.	Designated statutory entry and exit checkpoints where international conveyances must call and cargo must be unloaded.
"Dutiable Goods" [Section 2(14)]	Any goods which are chargeable to duty and on which duty has not been paid.	Goods listed in the Customs Tariff Act that have not yet undergone duty payment or been granted statutory full exemption.
"Imported Goods" [Section 2(25)]	Any goods brought into India from a place outside India but **does NOT include goods which have been cleared for home consumption**.	Once the proper customs officer passes the clearance order and duty is paid, the goods lose their character as "imported goods" and mix with the domestic mass.
"Importer" [Section 2(26)]	In relation to any goods at any time between their importation and the time when they are cleared for home consumption, includes **any owner, beneficial owner, or any person holding himself out to be the importer**.	Ensures that holding agents, consignees, freight forwarders, and end buyers cannot evade liability by transferring shipping documents while cargo is on the high seas.
"Coastal Goods" [Section 2(7)]	Goods transported in a vessel from one port in India to another port in India.	Subject to simplified coastal shipping manifests under Chapter XII to prevent illegal diversion of domestic goods onto the high seas.

6. The Taxable Event in Customs Law: Importation vs. Exportation

The "taxable event" is the specific commercial or legal occurrence that triggers the accrual of tax liability. In customs jurisprudence, defining the exact moment when the taxable event occurs is critical for determining the applicable rate of duty and exchange rate:

THE TAXABLE EVENT IN IMPORTATION: JUDICIAL DOCTRINE & LANDMARK RULINGS

TAXABLE EVENT

The Commencement of Importation

• **Commencement:** Importation commences the exact moment the carrying vessel enters the **Territorial Waters of India (12 NM)**.
• However, customs duty is NOT levied at the 12 NM line, because the goods are still aboard the ship and not yet landed.

The Completion of Importation (Taxable Event)

• In the landmark ruling **Kiran Spinning Mills v. Collector of Customs (1999)**, the Supreme Court of India established that **the taxable event occurs when the goods cross the customs barrier of India and intertwine with the general mass of goods in the country**.
• If goods are stored in a bonded warehouse, the taxable event crystallizes on the date the **Bill of Entry for Ex-Bond Clearance for Home Consumption** is presented.

7. Comprehensive Worked Numerical Problems and Practical Applications

WORKED NUMERICAL PROBLEM 1: MARITIME JURISDICTIONAL ASSESSMENT FOR CUSTOMS ENFORCEMENT

JURISDICTIONAL CASE

Context: A foreign cargo vessel, *MV Ocean Trader*, carrying undeclared electronic microchips, is intercepted by the Indian Coast Guard and Customs patrol at different maritime points off the coast of Mumbai. Evaluate the legality of customs enforcement actions at each position:

Interception Position	Maritime Zone Classification	Customs Authority & Enforcement Powers
Position A: 8 Nautical Miles from baseline	**Territorial Waters of India (TWI)** (Within 12 NM limit)	**Absolute Sovereignty:** The vessel is physically within India. Customs officers possess full authority to board, inspect manifests, arrest crew for smuggling, and seize the ship and cargo under Section 115.
Position B: 18 Nautical Miles from baseline	**Contiguous Zone of India** (Between 12 NM and 24 NM)	**Fiscal Preventive Enforcement:** Customs officers have statutory authority to stop and search the vessel to prevent evasion of customs laws within India's territory.
Position C: 85 Nautical Miles from baseline	**Indian Customs Waters (ICW)** (Within 200 NM EEZ limit)	**Anti-Smuggling Powers:** Under Section 106, customs officers can stop, chase, board, search, and seize any vessel within Indian Customs Waters (200 NM) if suspected of carrying contraband.
Position D: 250 Nautical Miles from baseline	**International High Seas** (Beyond 200 NM EEZ)	**Zero Customs Jurisdiction:** Beyond 200 NM, Indian customs has zero boarding authority, except under the international maritime law doctrine of **Hot Pursuit** commencing inside Indian waters.

WORKED NUMERICAL PROBLEM 2: DETERMINATION OF RELEVANT DATE FOR CUSTOMS DUTY RATE & EXCHANGE RATE

RATE DETERMINATION

Context: Apex Tech Ltd. imports industrial servers from Germany. Trace the statutory applicable date for determining: (A) The Rate of Basic Customs Duty, and (B) The Foreign Exchange Conversion Rate under Section 14 and Section 15 of the Customs Act, 1962:

Supply Chain Milestone	Milestone Date	Statutory Legal Significance under Section 14 & 15
Vessel Enters Territorial Waters (12 NM)	February 10, 2026	Importation commences; no duty determination yet.
Importer files Advance Bill of Entry	February 14, 2026	**Applicable Date for Exchange Rate (Section 14):** The exchange rate notified by CBIC on the date the Bill of Entry is presented applies (e.g., 1 EUR = ₹92.50).
Vessel arrives; Entry Inwards granted	February 20, 2026	**Applicable Date for Duty Rate (Section 15):** Under Section 15(1)(a), if Bill of Entry is filed before Entry Inwards, the rate of duty applicable is the rate in force on the **date Entry Inwards is granted** (or date of presentation, whichever is later).
Goods cleared for Home Consumption	February 24, 2026	Goods clear customs barrier; cease to be "imported goods".

8. Prohibited, Restricted, and Canalized Goods under Customs Law (Section 11)

Under **Section 11 of the Customs Act, 1962**, the Central Government possesses the absolute sovereign authority to prohibit or restrict the import or export of goods of any specified description by notification in the Official Gazette. Cross-border trade is categorized into three regulatory tiers:

STATUTORY CLASSIFICATION: PROHIBITED VS. RESTRICTED VS. CANALIZED GOODS

TRADE CONTROLS

Regulatory Category	Statutory Meaning & Legal Threshold	Product Examples & Regulatory Regime
Prohibited Goods [Section 2(33)]	Goods whose import or export is completely forbidden by law under the Customs Act or any other statute. Bringing them into Indian waters is illegal per se.	• Counterfeit currency notes and coins. • Narcotic drugs, psychotropic substances, and chemical weapons. • Goods infringing registered trademarks, patents, and geographical indications. • Tiger skins, ivory, and wild animal trophies under CITES.
Restricted Goods	Goods whose import or export is permitted, but strictly subject to prior statutory conditions, specific import licenses, or compliance standards.	• Drones and specialized communication transmitters (WPC license). • Genetically modified seeds and live livestock (sanitary permits). • Military arms, ammunition, and dual-use aerospace technologies.
Canalized Goods	Goods whose import or export is reserved exclusively for designated State Trading Enterprises (STEs) to stabilize national food or energy security.	• Petroleum crude (IOCL, BPCL, HPCL). • Food grains and fertilizers during domestic supply crises (FCI, STC, MMTC).

STATUTORY GROUNDS FOR IMPOSING PROHIBITIONS UNDER SECTION 11(2)

SECTION 11 GROUNDS

Sovereignty & Public Safety

The security of India, maintenance of public order, prevention of civil disturbance, and suppression of international terrorism, sabotage, or piracy.

Public Health & Morality

Preventing the entry of obscene literature, protection of human, animal, or plant life from contagious epidemics, and hazardous chemical waste containment.

Economic & Intellectual Rights

Protection of domestic industrial patents, copyrights, trademarks, prevention of counterfeit goods, and conservation of exhaustible national mineral resources.

Anti-Smuggling & Forex Security

Prevention of illegal cross-border outflow of gold, precious gemstones, foreign exchange reserves, and ancient national antiquities.

9. Customs Station Infrastructure: Ports, Airports, Dry Ports (ICDs), and Land Stations

International cargo cannot enter or leave India at any random coastal beach or airstrip. Under **Section 7 and Section 8 of the Customs Act**, conveyances carrying international cargo can only arrive at officially notified **Customs Stations**:

TYPOLOGY OF CUSTOMS ENTRY STATIONS UNDER THE CUSTOMS ACT, 1962

CUSTOMS INFRASTRUCTURE

Customs Station Category	Operational Function & Facilities	Key Examples in India
Customs Sea Ports [Section 7(1)(a)]	Deepwater maritime harbors appointed for the unloading of imported sea cargo and loading of export sea cargo. Equipped with container berths and bonded wharves.	Jawaharlal Nehru Port (JNPT / Nhava Sheva), Chennai Port, Cochin Port, Deendayal Port (Kandla), Mundra Port, Visakhapatnam Port.
Customs Airports [Section 7(1)(a)]	Notified international civil airports equipped with dedicated Air Cargo Complexes (ACC) for rapid transit of high-value, time-sensitive shipments.	Indira Gandhi International Airport (Delhi ACC), Chhatrapati Shivaji Maharaj Airport (Mumbai ACC), Kempegowda Airport (Bengaluru ACC).
Inland Container Depots (ICD) **The "Dry Ports"** **[Section 7(1)(aa)]**	Full-fledged customs clearance stations located in landlocked interior industrial centers, connected to gateway maritime ports by bonded rail corridors.	**ICD Tughlakabad (Delhi)**, ICD Whitefield (Bengaluru), ICD Sanand (Gujarat), ICD Dadri (UP). Exporters clear customs locally without traveling to coastal ports!
Land Customs Stations (LCS) **[Section 7(1)(b)]**	Notified international border checkpoints on international land borders for road, bus, and freight rail traffic with neighboring nations.	• **Attari-Wagah** (India-Pakistan Border) • **Petrapole** (India-Bangladesh Border, West Bengal) • **Raxaul** (India-Nepal Border, Bihar)

Synthesis: The Gateway to Modern Indirect Tax Governance

Indirect taxation represents a sophisticated convergence of domestic consumption regulation and international trade governance. While the Goods and Services Tax (GST) harmonizes domestic multi-stage value addition under the cooperative banner of cooperative federalism, Customs law safeguards the sovereign economic border of the nation. Governed by the timeless machinery of the Customs Act, 1962, customs authorities control territorial and maritime waters, enforcing statutory valuation, curbing international smuggling, and collecting border revenues. Together, GST and Customs Duty form the indissoluble dual pillars that power the fiscal sovereignty of modern India.