

A PRE-BUDGET MEMORANDUM  
FOR THE  
CONSIDERATION  
OF THE UNION GOVT.

FINANCIAL YEAR  
2007-2008

*Presented by*  
**Indian Dairy Association**  
*Sector-IV, R.K.Puram, New Delhi-110022*

# CONTENTS

	Page No.
<b>Section I : Indian Dairy Industry : A Profile</b>	<b>1</b>
<b>Section II : Direct Taxes</b>	<b>3</b>
2.1 Income tax on Dairy Cooperatives	3
2.2 Income tax exemption under Section 36	3
2.3 Income tax exemption under Section 80P	3
2.4 Income Tax on Indian Dairy Association	3
2.5 Service Tax	4
<b>Section III : Custom &amp; Excise Duty</b>	<b>5</b>
3.1 Exemption of Excise Duty on Dairy Equipments and Machinery	5
3.2 Exemption from Central Excise Duty of Stainless Steel and Aluminium Cans etc.	6
3.3 Duty free import of bacteriofuges and UHT	6
3.4 Reduction in duty on packaging material and packaging machinery	7
3.5 Excise duty on Lactose and Casein	7
3.6 Exemption of molasses used in feed industry from central excise	7
<b>Section IV : Export Promotion of Milk Products</b>	<b>10</b>
4.1 Vishist Krishi Upaj Yojana	10
4.2 Duty drawback through REP	10
<b>Section V : Incentives to dairy industry</b>	<b>11</b>
5.1 Credit on concessional rates to dairy industry	11
5.2 Establishment of Fodder Banks	11
<b>Section VI : Reduction in VAT on milk products</b>	<b>12</b>
6.1 VAT on ghee	12
6.2 VAT on items not mentioned in the notification	12

## **SECTION I : INDIAN DAIRY INDUSTRY — A PROFILE**

India is the world largest milk producer since 1998-99. According to estimates of the Central Statistical Organisation (CSO), the value of output from livestock at current prices was about Rs. 173,350 crores in 2004-05. Milk accounted for 68% of this output. It was higher than paddy (Rs. 70,462 crores) and wheat (Rs. 48,052 crores). In terms of value of output, milk is now the single largest agricultural commodity in India.

Dairying is a secondary occupation for about 69 percent of India's milk producers. It contributes close to a third of the gross income of rural households and in the case of those without land, nearly half of their gross income. Women constitute about 70 percent of the labour force in livestock farming. Based on the small holder milk production system, domestic per capita availability of milk was around 229 grams per day in 2004-05.

An estimated 70 million rural milch animal households - of which about 75 percent are landless, marginal or small farmers-were mainly responsible for producing an estimated 88 million tons of milk in 2004-05. Most of the rural milch owning households own only one to three animals and it is estimated that around 15 percent households own more than 4 milch animals.

The landless, marginal and small farmers own only 30 percent of the land holdings i.e. land holdings of less than 2 hectares, but 60 percent of female bovines. The distribution of rural income, as reflected in the Gini Coefficient (a measure of inequality) is very low for the dairy sector in India, indicating that as the ownership of livestock is more evenly distributed with landless labourers and marginal farmers, the progress in this sector will result in a more balanced development of the rural economy.

These livestock keepers are constrained by poor animal health and veterinary services, lack of feed and fodder, water, milk handling, chilling, etc. Besides, there have been lack of infrastructure facilities such as good roads and access to markets, etc. The livestock keepers also lack access to advanced technologies as well as proper institutional support system. The result is that both the production and productivity remain well below its potentials. Thus the losses and wastages continue to remain high. Adapted breeds and local feed resources although available, but need proven technology supports in its preservation and processing. Such support would substantially improve production and productivity, which would result in higher income for the livestock keepers.

One of the problems faced by India is unemployment, despite the rapid growth rate. The problem is more acute in rural educated and marginally educated youths, who have no

alternative but to migrate to urban areas. Due to automation in various core sectors, the employment opportunities have dwindled considerably whereas the service sector has its own limitations, especially the high investment cost per job created. In this context, the dairy industry offers a plausible opportunity of creation of self-employment with minimum investment. There is a scope for doubling the present milk production, which can be achieved with marginal investment, Such a step would not only enhance milk production and productivity, but also would create millions of additional jobs.

Dairying is, in fact, a supplementary activity of the marginal farmers and the landless labourers. It is therefore suggested that dairy and such other animal farming be included within the legal framework of 'agriculture and agriculture products'. This would enable the marginal farmers and the landless agriculture labourers to benefit from the various government incentives.

Milk is no more a luxury, but essential nutritional requirements of human being. The children largely depend on milk for nutrition. Higher milk production therefore will also increase the health status of the farmers and people at large. Due to several inherent reasons, the cost of milk production is high. One of the important reasons is low animal productivity. Because of high cost, the milk and milk products are not affordable to poor strata of the society. Milk is a perishable commodity. Hence, its conversion to products, such as, milk powder, butter and cheese, etc. is necessary. Considering these factors, it is reasonable that at par with agriculture produce, the milk products be also exempted from any excise duty, sales tax and such other taxes. This gesture of the government would go a long way in accelerating the growth of the Indian dairy industry.

The conversion of excess milk to milk-products is a necessity. The basic principle here is evaporation of water which changes its physical form only, whereas there is no change whatsoever in its chemical composition. One of the reasons of higher cost of milk and milk products is the cost of packaging. To safeguard the quality and safety for human consumption, packaging of milk and milk product is necessary. The milk product manufacturing therefore should be construed as 'processing milk for preservation' and it should be exempted from all the taxes and duties like excise, central sales tax and octroi etc.

To enhance milk production during the next five years as well as to address the issues referred in the foregoing paras, there is an imperative need of policy support from the government on the following core areas:

- Clean and quality milk production, processing and packaging
- Boost the exports of milk and milk products
- Enhance milk production and milch animal productivity

## **SECTION II : DIRECT TAXES**

### **2.1 Income Tax on Dairy Cooperatives**

The village level primary dairy cooperative societies are exempt from payment of income tax. However, the district and state level dairy cooperatives (state cooperative dairy federation) are levied income tax @ 35% as against companies who are charged income tax at 25% only. Traditionally the rate of income tax were lower for cooperative institution in comparison to companies. However, in the last budget when the income tax on companies was reduced to 25% a similar concession was not levied to state level cooperative societies.

**Recommendations: The state level dairy cooperative societies (state cooperative dairy federation) should also be exempted from payment of income tax.**

### **2.2 Income Tax Exemption under Section 36**

Specific deduction under Section 36 be allowed for expenditure incurred on Animal Husbandry, providing veterinary services, expenditure incurred on Artificial Insemination for the members of primary milk supplying societies.

### **2.3 Income Tax Exemption under Section 80P**

The whole of the amount of profits and gains of Federal Co-operative Societies engaged in collecting and supplying milk from primary societies be exempt from income tax.

### **2.4 Income tax on Indian Dairy Association (IDA)**

The IDA is not at present exempted from payment of income tax. IDA is a national level body of dairy professionals, research workers, educationists, farmers organisation and industry. It is a professional body engaged in scientific development. The IDA, as an institution, has been providing a common forum to knit the dairy fraternity together and thus, over the years, it has emerged as the reigning czarina of information for the dairy sector. Other than student and individual members, there are institutional members from the cooperatives, multinationals, corporate bodies, private institutions, educational institutions, government and public sector units. The IDA functions very closely with the dairy producers, professionals & planners, scientists & educationists, institutions and organisations associated with the development of dairying in India. IDA is not engaged in any commercial activity.

**Recommendation: IDA should be exempted from income tax under section 10 of the Income Tax Act.**

## **2.5 Service Tax**

It is reported that Government of India has decided to charge service tax on road transport on 30% component of the road freight bill. It has been further stated that certain industries including milk will be totally exempted from service tax. The definition of milk should be enlarged to include skim milk powder, whole milk powder and white butter which are used for reconstitution of liquid milk for the purpose of total exemption from service tax on road transport.

**Recommendation: The definition of milk should be enlarged to include SMP, WMP and White Butter and exempted from Service Tax.**

## **SECTION III : CUSTOM AND EXCISE DUTY**

### **3.1 Exemption of Excise Duty on Dairy Equipments and Machinery**

The quality of raw milk in India is quite poor and the initial bacterial count runs into millions. This is due to unhygienic milking, storage, handling etc. Also, the temperatures all over the country are quite higher during most part of the year which spoils the milk faster. It is therefore very essential to boost clean milk production and hygienic milk handling by adopting milking by machines, use of aluminium or SS milk cans, use of bulk milk coolers etc. However, due to excise, sales tax, octroi the prices of those equipment become exorbitant.

The taxes and duties amount to almost 35 to 40% of the basic prices. e.g. 16% Central Excise + 15.3% Sales Tax + 4% Octroi = 35.3% in Maharashtra. The heavy burden of taxes & duties reduces the use of those equipment and thus the quality of milk remains poor in MS cans, non chilled etc.

In its pre-budget Memorandum for the year 2004-05 and 2005-06, the Indian Dairy Association had requested the Government of India to exempt milking machines, bulk milk coolers and aluminum and SS milk cans and other dairy equipments required from clean milk production as well as processing of milk and milk products. However, such an exemption has been granted only on milking machines for clean milk production and a very few items for milk processing. We have, therefore, reviewed the central excise manual and custom tariffs, and surprised to find that the major items of dairy machinery are classified under the different categories other than 84.34. Therefore, in the event of exemption relief provided only to the items classified under 84.34, most of the essential items required for establishing a dairy plant would be left out! Consequently, we thought it appropriate to list the essential item that are required for establishing a dairy plant showing corresponding category of excise manual and custom tariffs. The list referred above is enclosed. It is suggested that a separate category should be created for "Dairy Equipment and Machinery" under central excise duties and custom tariffs. Besides, the "Dairy Equipment and Machinery", all the essential items for clean milk production should be exempted from central excise and custom tariffs.

The dairy industry is happy on removal of the excise duty on milking machines and dairy machinery with respect to tariff heading 84.34. However, this category does not include most of the equipment used for collection and processing of milk as they fall in the categories classified under other chapters/headings of the excise duty schedule and are not eligible for excise duty exemption. Details of these equipments are annexed.

**Recommendation : A separate category, as per the list appended, should be created for “Dairy Equipment and Machinery” under central excise duties exempted from central excise duty.**

### **3.2 Exemption from Central Excise Duty of Stainless Steel and Alluminium Cans etc.**

Stainless Steel Cans, Collection trays, Sample bottles, SS Plungers and Alluminium Cans are used for milk collection and transportation. Due to increase in the prices of the raw materials the prices of those item are very high. This affects their purchases by the milk handlers and they opt for the cheaper plastic cans, MS galvanized cans etc. which deteriorate the quality of raw milk.

The Stainless Steel 304 quality & Aluminium Alloy raw material prices have increased steeply during the last one year. As of date, SS 304 have increased by 115% & Aluminium Alloy prices have increased by 40%. The raw material for these cans attracts 16% excise duty. The product details with excise heading no. are given below:

Product	Central Excise Chapter Sub Heading No.	Rate of Excise Duty
Aluminium Milk can with lid in 5L to 50L capacities	76121010	16%
Aluminium milk can spares	76161000	16%
Stainless Steel Milk cans with lid in 5L to 50L capacities	73102110	16%
S.S. Milk can spares	73170019	16%
Stainless Steel milk testing equipments for societies	73170019	16%
Bulk Milk cooler	84342000	Exempted

**Recommendation : It is recommended that SS and Aluminium Cans, and other milk handling equipment should be exempted from central excise duty totally.**

### **3.3 Duty Free Import of Bactofuges and UHT Plants**

Presently, Bactofuges and UHT plants attract customs duty of 25% ad-valorem duty of 16% and surcharge of 4%. Bactofuges are mainly required for improving the quality of milk but due to their high cost and additional import duties, their use is very limited in our country. If the cost is reduced by way of exemption of import duty, the use of these machines will result in producing better quality of milk. Similarly, import of UHT plants may also be allowed duty free.

**Recommendation : Exempt Bactofuges and UHT plants from paying any Import Duty.**

### **3.4 Reduction in duty on packaging material and packaging machinery**

Almost 46% of the milk produced is consumed as liquid milk. However, only 14% of the milk is processed and packed. This leaves major portion of liquid milk open for adulteration, unhygienic handling and distribution. Therefore, it is essential that only the pasteurised and packed or machine vended milk should be distributed. However, the huge costs of pouch filling machines, milk vending machines and polyethylene films prevent it. The adulterated milk poses major health hazards to the public. The cost of the packing and vending machines and packing materials can be reduced by exempting them from Central Excise Duty and CST.

**Recommendation : Exempt Pouch Filling Machines, Bulk Milk Vending, Aseptic Packing Machines, Polyethylene Film from Central Excise.**

### **3.4 Excise duty on lactose and casein**

Presently excise duty on lactose and casein is 16%. The excise duty may be exempted so that more and more dairy units can come forward and produce these items.

### **3.5 Exemption of molasses used in feed industry from central excise**

Molasses is used as a source of carbohydrate in the cattle feed. The molasses used by the cattle feed industry attract central excise duty at the rate of Rs. 500 per MT of molasses. The organised feed industry consumes around 3 lakh MT of molasses annually which is meagre as compared to total production of 60 lakh MT produced annually. The molasses used for the manufacture of animal feed were free from excise duty till 1995-96. The levy on excise duty has increased the animal feed cost by 60-75% per MT. The farmer is unable to bear this burden and hence many farmers have discontinued using compound feed. This ultimately results in low milk production and affects the poor and marginal farmers. Refund of central excise duty on molasses may be allowed in case molasses is used by the cattle feed industry. This will result in increasing the use of compound cattle feed and will improve the productivity of animals.

## **SECTION IV : Export Promotion of milk products**

### **4.1 Vishisht Krishi Upaj Yojana**

**(DGFT Policy Circular No. 14 (RE-2005)/2004-2009 dated 4th July, 2005**

Under the recently announced scheme to promote export of agricultural products, the export of milk products are eligible for interest free export credit of 5% value of their export. This scheme has not made much dent in the export of milk products and it is felt that the quantum of incentive is not adequate and it should, therefore, be increased.

**Recommendation: The incentive of interest free credit on export of milk products should be raised to 10% of the value of the export.**

### **4.2 Duty drawback through REP**

The Government of India provides Duty Drawback on products and goods exported by Indian manufacturers and merchant exporters on agro and milk products at varying rates. Although, skimmed milk powder, full cream milk powder and casein are made from milk, the duty drawback benefit of 14 percent is allowed on casein alone. This has put SMP and WMP in a disadvantageous position in the export market. Casein export by the Union Government is treated as an integral part of country's economic endeavor, whereas milk powders are treated as activity, although the latter from the major exportable commodity from India. Production of SMP and WMP require stringent quality requirement from milk production stage upto packaging needing extra efforts and initiatives and expenditure to achieve a quality matching with international specifications.

India can take advantage of the current decline in world milk production especially in the Europe, Oceania and North America, which have traditionally been the major exporting countries for SMP, WMP, cheese and butter oil. Exports of dairy products can be greatly boosted from India provided the Union Government extends the kind of incentives such as duty drawback @ 14 percent for dairy product export as for casein. The exporters of skimmed milk powder and full cream milk powder can multiply their export turn over many a times with uniform rates of export incentives. The price realized by exports is not always remunerative and lack of incentives for exports will become a big limiting factor. It may be stated that inspite of GATT agreement, EU is giving subsidy of more than US\$ 550 per MT on SMP, US\$ 850 per MT on FCMP, US\$ 1200 per MT on butter and butter oil. In EU, US and Pacific region, milk producers subsidies are thus being replaced by processor subsidies which are ultimately passed on to milk producers making it difficult for the Indian dairy plants to compete with those countries in the international market.

**Recommendation : Duty drawback through rep @ 14% may be given to export of all dairy products viz. ghee, SMP, WMP, butter, etc. in addition to casein.**

## **SECTION V : Incentive to Dairy Industry**

### **5.1 Credit on concessional rates to dairy industry**

Today the farmers and agro-sector are placed on high priority by the Union Government. It would be prudent to review the policies of the Governments to find out reasons as to why dairy sector is not developing as fast in India as in other countries. Multiplicity of taxation on dairy projects detracts corporate investors and entrepreneurs to get into this area. The role of dairy sector in export market is very dismal. India's contribution to milk products export trade is less than 0.5 percent, although we are the biggest milk producers in the world. A continuous upgradation of technology, products and management practices would ensure a reasonable share of Indian dairy products in global trade. In many States, a variety of taxes are imposed on dairy commodities which adversely affect the economic interest of farmers directly as their produce would not fetch the same price as paid to farmers of other States where taxation is minimal. Moreover, price differential between fresh and processed foods is very high detracting the consumers to buy processed products.

**Recommendation : It is recommended that besides reducing multiplicity of taxation on dairy produce, loans on concessional rate at 4% should be made available for establishing dairy industries under the industrial investment promotion scheme for 15 years.**

### **5.2 Establishment of Fodder Banks**

Fodder is the major feed input for the dairy industry, but it is not available to many farmers. There are some areas where there is plenty of fodder production whereas in a number of areas there is acute shortage. It is therefore suggested that on the lines of 'Grain Banks' a government-supported initiative be taken up to establish 'Fodder Banks' and schemes for fodder procurement with support price. This will also help fodder producer farmers as well as farmers from drought-prone and fodder—deficient areas. Besides, in case of draughts, cyclones and other calamities it can save cattle population from dying of hunger.

**Recommendation : Fodder Banks should be created in all drought prone areas of the country through Dairy Cooperatives. GOI should provide seed capital and revolving fund to dairy cooperative for this activity.**

## **SECTION VI : Reduction in VAT on milk products**

### **6.1 VAT on Ghee**

Most of the states have levied on ghee VAT on 12.5%. As against VAT on edible oils @ 4.0%. Ghee is a commonly used oil in India by all sections of the community. VAT of 12.5% has put unnecessarily burden on the consumers. Ghee should be treated like any other oil and put under the category of 4.0% VAT instead of 12.5% VAT.

### **6.2 VAT on items not mentioned in the notification**

In the notification on VAT issued by Government of National Capital Territory of Delhi, a number of milk products have not been listed. There is a general clause in the notification that items not listed in the schedule, would be charged at 12.5%. Consequently, dairy items like Shrikhand, packed sweets, etc. are being charged at 12.5%. It is suggested that all dairy products should be put in the schedule with a note that any item not listed would be charged at 0% of VAT. It is reported that in many states a number of milk products are being charged high rate of VAT. It is suggested that Pasteurised and Sterilised Milk (packed or vended) and all dairy products (cream, butter, butterspread, cheeses and spreads, milk powders: SMP, full cream, milk powder, dairy whitener, infant milk food, dahi, yoghurt, ice cream, lassi and traditional milk based products and all the dairy equipment and accessories) should be classified under Schedule I attracting 0% VAT.

## **Machinery for Dairy Industry**

<b>1.0</b>	<b>Milk Procurement &amp; Reception</b>	Chapter	Rate of Duty (Present)
1.1	Village level milk chilling plant	84.18	16%
1.2	Milk chiller	84.18	16%
1.3	Road milk tanker	87.05	16%
1.4	Milk tanker weigh scale	84.23	16%
1.5	Milk weigh scale and bowl	84.23	16%
1.6	Milk cans	73.09	16%
1.7	Milk dump tank	73.09	16%
<b>2.0</b>	<b>Milk Processing &amp; Pasteurization</b>		
2.1	Milk pasteurizer	84.19	16%
2.2	Milk clarifier	84.21	16%
2.3	Milk transfer pump	84.13	16%
2.4	Cream separator	84.21	16%
2.5	Cream pasteurizer	84.19	16%
2.6	Cream storage tank	73.09	16%
2.7	CIP System	84.51/84.19	16%
2.8	Milk Silo	73.09	16%
2.9	Pasteurized Milk Storage Tanks	84.34	16%
2.10	Pasteurized Milk Transfer Pump	84.13	16%
<b>3.0</b>	<b>Milk Packaging &amp; Distribution</b>		
3.1	Milk packing-pouch form, fill & seal machine	84.22	16%
3.2	Milk Vending Machine	84.76	16%
3.3	Milk Silo with Agitator	84.79	16%
3.4	Bottling plant-bottle washer eraze Washer Tetra Pack	84.72	16%
<b>4.0</b>	<b>Ghee Making</b>		
4.1.1	Cream Transfer Pump	84.73	16%
4.1.2	Ghee Kettle	84.79	16%
4.1.3	Ghee Settling Tank	84.22	16%
4.1.4	Ghee packaging machine	84.22	16%
4.1.5	Ghee clarifier	84.21	16%
4.1.6	Cream tank without agitator	73.09	16%

<b>4.2</b>	<b>Butter Making</b>		
4.2.1	Butter churn without agitator	73.09	16%
4.2.2	Butter packing machine	84.22	16%
4.2.3	Positive Displacement Pump	84.13	16%
<b>4.3</b>	<b>Lactose Making</b>		
4.3.1	Separator	84.21	16%
4.3.2	Evaporator	84.19	16%
4.3.3	Dryer	84.19	16%
4.3.4	Packing Machine	84.22	16%
<b>4.4</b>	<b>Yoghurt/Curd Making</b>		
4.4.1	Standardization Tank	73.09	16%
4.4.2	Transfer Pump	84.13	16%
4.4.3	Culture Tank	73.09	16%
4.4.4	Transfer Pump	84.13	16%
4.4.5	Packaging Machine	84.22	16%
<b>4.5</b>	<b>Milk Powder Making</b>		
4.5.1	Multiple Effect Evaporator	84.19	16%
4.5.2	Spray Dryer	84.19	16%
4.5.3	Powder Conveying System	84.79	16%
4.5.4	Powder Milk Silo	73.09	16%
4.5.5	Fluid Bed Dryer	84.19	16%
4.5.6	High Pressure Pump	84.13	16%
4.5.7	Powder Packing Machine	84.22	16%