

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

FINANCIAL YEAR  
2008-2009

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## **SECTION — I**

### **INDIAN DAIRY INDUSTRY — A PROFILE**

1. Dairying in India is an integral part of the total farming system. Symbiotic relationship exists between agriculture and dairy farming. The agricultural by-products provide feed and fodder for the cattle, whereas cattle provide necessary draught power for various agricultural operations. Dairying in India is unique in more than one respect. It ranks first with its 185 million cattle and 95 million buffaloes accounting for about 51 percent of Asia and about 19 percent of world bovine population. We maintain 57 percent of the world's buffalo population. According to estimates of the Central Statistical Organisation (CSO), the value of output from the livestock at current prices was about Rs. 173350 crores in 2005-06. Milk accounted for 68 per cent of this output. It was higher than paddy (Rs. 70462 crores) and wheat (Rs. 48052 crores). In terms of value of output, milk is now the single largest agriculture commodity in India.
2. Dairying contributes close to the third of gross income of rural households and in the case of those without land, nearly half of their gross income. An estimated 70 million rural households, of which about three-fourth are landless, marginal or small farmers are engaged in milk production. The distribution of rural income, as reflected in the gini coefficient (the measure of inequality) is very low for the dairy sector in India, indicating that the ownership and the income is more evenly distributed and the progress in this sector will result in a more balanced development of rural economy.
3. Milk production has shown rapid growth of 4-5 per cent per annum during the last 35 years, now reaching a level of about 100 million tonnes. It has to be realised that unless milk group maintains a growth of five per cent, it would not be possible for the livestock sector to achieve the target growth of 6-7 per cent and unless livestock sector maintains growth of six per cent, the agriculture shall not have the growth of four per cent, since livestock accounts for 28-30 per cent of GDP of agriculture.
4. India has already entered in the international market in milk products, exporting 59,746 MT of milk products during 2005-06. Under the WTO regime, Indian exports will have to adhere to stringent quality and food safety standards. The dairy industry will have to upgrade itself to the international level. The international dairy industry is, however, highly protected through domestic support and export subsidies and does not provide an easy market access. A number of trade barriers are applied to deprive the developing countries from sharing the markets of developed nations.

5. Indian Dairy sector, however, could not make significant inroads in the global market due to several impediments. The quality of milk is a matter of concern which is now being addressed by all concerned. Most of the Dairy units are seriously looking into the improvement of sanitary and hygienic conditions by adopting ISO certification as well as HACCP programmes. The Sanitary and Phyto-Sanitary (SPS) measures are becoming mandatory for export and serious efforts have to be made to achieve the international standards of quality.
6. In recent times India has made considerable progress in dairy equipment manufacture as well . It is, however ,still confined to certain categories such as road tankers, storage tanks, Bulk milk coolers, small homogenizers, milk pasteurizers, milk vending machine and liquid milk packaging system etc. Equipment for packaging of butter, cheese, paneer and other traditional products needs attention with an eye on the industry's need for small and large-scale operations.
7. Milk is, an 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 similar other taxes. This gesture of the government would go a long way in accelerating the growth of the Indian dairy industry.
8. 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.
9. To enhance milk production 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:
  - i) Enhance milk production and milch animal productivity
  - ii) Clean and quality milk production, processing and packaging
  - iii) Boost the exports of milk and milk products

## **SECTION — II**

### **DIRECT TAXES**

#### **II.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 are levied income tax @ 35%. Basically, the primary cooperative societies at the village level form a milk union at the district level to process their milk in a plant owned by themselves. Similarly, the district level milk unions of the milk producers cooperatives federate into a state level milk marketing federation so that their products can be marketed in an efficient manner. Though, all the three levels of the cooperatives are part of the same farmers' setup, the district level milk unions which directly cater to the needs of the farmers need a very special consideration and need to be exempted from the payment of income tax.

**Recommendations: The District Dairy Cooperative Milk Unions should be exempted from payment of income tax.**

#### **II.2 Income tax on Indian Dairy Association (IDA) under Section 10**

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 organisations and industry. It is a professional body engaged in scientific dairy development. The IDA, as an institution, has been providing a common forum to knit the dairy fraternity together and thus, over the years, 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, 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. It has established technology missions on "Technology & Engineering", "Quality Systems", "Milk Production and Farmers Issues" and "Trade & Marketing", to collate and disseminate knowledge on these aspects of dairying to the various stakeholders so that the benefits of advanced technology, available by way of research, ultimately reach the poor milk producers who as stated in the foregoing paragraphs, are small and marginal farmers and landless labourers belonging to the weaker sections of the society.

IDA is not engaged in any commercial activity.

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

## **SECTION — III**

### **CUSTOM AND EXCISE DUTY**

#### **III.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 the fact that milk is a very quickly perishable commodity and due to unhygienic milking, storage, handling etc. The temperature all over the country is quite high 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 Aluminum or Stainless Steel (SS) milk cans, use of bulk milk coolers etc. However, due to excise, sales tax, octroi etc. the prices of these equipment become exorbitant.

China has emerged as a major manufacturer of dairy equipment and machinery and its prices are much lower than those of Indian manufacturers. The material used for manufacture of equipments in China is not the same as universally used and does not appear to have been evaluated from food safety angle. This raw material being cheaper than the stainless steel being used in India and elsewhere, the prices of Chinese equipments are cheaper than Indian manufacturers. It is, therefore important to protect the domestic production and the need to make domestic dairy equipment production cost competitive by removing the excise duty.

Taxes and duties amount to almost 35 to 40% of the basic prices of machinery. 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 these equipment and thus the quality of milk remains poor.

In its pre-budget Memorandum for the last three years, the Indian Dairy Association (IDA) had requested the Government of India to exempt milking machines, bulk milk coolers and aluminum & SS milk cans and other dairy equipments required for clean milk production as well as processing of milk and milk products from the purview of Excise Duty. 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, 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 find that the major items of dairy machinery are classified under 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 have listed the essential items that are required for establishing a dairy plant showing corresponding category of excise manual and custom tariffs. It is requested 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. Details of these equipments are annexed as **Annexure I**.

**Recommendations : A separate category, as per the list annexed, should be created for “Dairy Equipment and Machinery” under Central Excise Custom Tariff and exempted from central excise duty.**

### **III.2 Exemption from Central Excise Duty on Stainless Steel (SS) and Aluminum Milk Cans etc.**

Stainless Steel Cans, Collection trays, Sample bottles, SS Plungers and Aluminum Cans are used for milk collection and transportation. Due to enormous increase in the prices of stainless steel the prices of those items have risen very high. This affects their purchases by the milk handlers and they opt for the cheaper plastic cans, Mild Steel galvanized cans etc. which deteriorate the quality of raw milk.

Hygienically safe and food grade alternatives to stainless steel have nowhere developed/tested or permitted. China is using some cheaper substitute whose food safety has not been verified. The raw material for these cans attracts 16% excise duty. The product details with excise heading Nos. 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 village level societies	73170019	16%

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

### **III.3 Duty Free Import of Bacteria Removing Clarifiers (Custom Code : 84211940)**

The bacteria removing clarifiers are required for improving the quality of milk. These are not manufactured in India. Due to their high cost and additional import duties, their use is very limited in our country. Presently, these machines attract customs duty of 7.5%, counter vailing duty of 16.48% along with cess of 3% and SAD of 4%. If the cost is reduced by way of exemption of these duties/taxes, the use of these machines will result in producing better quality and safe milk. This will ultimately help both the milk producer and the milk consumer who will get a hygienic and safe product.

**Recommendation : Exempt bacteria removing clarifiers from paying any Import Duty.**

### **III.4 Reduction in duty on packaging material and packaging machinery**

Almost 46% of the milk produced in India is consumed as liquid milk. However, only 15% of the milk is processed and packed. This leaves major portion of liquid milk open for adulteration, unhygienic handling and distribution. It is, therefore, 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/VAT.

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

### **III.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 attracts 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 very meager as compared to total production of 60 lakh MT 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%. The farmer is unable to bear this burden and hence many farmers have discontinued using compounded feed. This ultimately results in low milk production and affects the poor and marginal farmers.

**Recommendation: 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**

(Submission in Section IV to be taken up with the Ministry of Commerce)

#### **IV.1 Vishisht Krishi Upaj Yojana**

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

Under the above 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. The hardening of Indian currency against US\$ has further aggravated the situation. This is badly affecting our export of milk products. It is, therefore, felt that the quantum of incentive is not adequate and it should 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.**

#### **IV.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 requirements 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 from India can be greatly boosted provided the Union Government extends incentives such as duty drawback @ 14 percent for dairy product export at par with casein. The exporters of skimmed milk powder and full cream milk powder can multiply their export turn over many 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.

This has further been aggravated by a hardening rupee. It may be stated that despite GATT agreement, EU is giving subsidy of more than US\$ 550 per MT on SMP, US\$ 850 per MT on Full Cream Milk Powder (FCMP, or WMP), 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.**

### **IV.3 Consistency in EXIM Policy on Dairy Products**

As brought out above, despite various constraints, India has become net exporter of milk products for the last couple of years and has started earning a good amount of foreign exchange. The Indian dairy industry has invested huge amounts to upgrade the quality and hygiene systems so that the quality of milk products being exported comes up to the international standards. The industry has, in fact, created a special position for itself in the international dairy market by way of providing consistently good quality products at a price cheaper than the traditional milk products exporters over the last couple of years.

The position thus achieved, however, can be sustained only if there is a consistency in the EXIM policy. For example, the ban on export of SMP imposed during February 2007 was totally unexpected and has caused great damage to the country's export potential because even the confirmed export orders could not be accomplished due to the suddenness and surprise effect of the ban order. This has greatly tarnished the image of the country as a reliable supplier of dairy products. It may take a couple of more years for the industry to build up a reputation again in the international market. A consistency in long term trade policy would greatly help to avoid such situations.

**Recommendation: There should be a consistency and transparency in the EXIM policy so that the export potential of the dairy industry is not damaged. The next EXIM policy be announced for at least three years.**

## SECTION V

### Other Essential Initiatives for developing dairying

#### V.1 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 producing 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.**

#### V.2 Rationalization of VAT on Milk Products

Different states have prescribed different rates of VAT on various dairy products as well as on dairy machinery. For example, many states have levied 12.5% VAT on ghee As against VAT on edible oils @ 4.0%. Ghee is a commonly used oil in India by all sections of the society. VAT of 12.5% has put unnecessary burden on the consumers. Ghee needs to be treated like any other edible oil and put under the category of 4.0% VAT instead of 12.5% VAT.

Similarly, 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%. There is a need for a uniform level of VAT on all milk and milk products throughout the country. This will greatly facilitate movement of milk products from surplus to scarcity areas. All dairy products should be put in the schedule with a note that any item not listed would be charged at 0% of VAT.

**Recommendation: It is suggested that Pasteurised and Sterilized 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 or at the most in schedule II - 4% VAT.**

### **V.3. Removal of Development Cess on Liquid Milk**

Some of the states like Haryana have imposed development cess on milk handled by dairies. Instead of development, this cess is acting as a hinderance in the development of dairy industry and the entrepreneurs are facing a lot of hardship on this account.

### **V.4 Mandi Tax, Purchase Tax on milk**

Some states have imposed Mandi Tax and Purchase Tax on milk and milk products.

The basic principle of introducing VAT was to absorb all such taxes in VAT and reduce unnecessary taxation. Continuation or reimposition of these taxes negates the very purpose of VAT.

**Recommendation: Govt. of India may prevail upon all states to remove all taxes other than VAT on milk and milk products to mitigate the hardships faced by dairy industry and allow it to compete with the global players.**

## **Machinery for Dairy Industry**

<b>1.0</b>	<b>Milk Procurement &amp; Reception</b>	Chapter	Rate of Excise Duty (Basic Duty)
1.1	Bulk Milk Cooler (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%

## **4.2 Butter Making**

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%

## **4.3 Lactose Making**

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%

## **4.4 Yoghurt/Curd Making**

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%

## **4.5 Milk Powder Making**

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%