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SEZs in India – Legal and Regulatory Framework

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Cyril S. Shroff

Amarchand & Mangaldas & Suresh A. Shroff & Co.
Peninsula Chambers, Peninsula Corporate Park,
Ganpatrao Kadam Marg, Lower Parel, Mumbai - 400 013.
Tel: (91-22) 2496-4455 Fax:(91-22) 2496-3666
Email: cyril.shroff@amarchand.com

Indian Ground Reality



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- SEZs regulated under
 - The Foreign Trade (Development and Regulation) Act, 1992
 - SEZ Scheme in the EXIM Policy 2002 – 2007
- State Level Acts - Uttar Pradesh and Rajasthan; Karnataka, Maharashtra, Madhya Pradesh - draft legislations
- 14 functioning SEZs and 13 SEZs under implementation
- Past experience with EPZ/STP/EHTP indicates that fiscal incentives alone not sufficient - adequate infrastructure facilities essential

Taxation



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- Direct Tax
 - Tax holiday on income of
 - § SEZ Units
 - § SEZ Developer
 - § Investment income from SEZs
- Indirect Tax
 - Import duty exemption
 - Service tax exemption – provision of services to both SEZ Units and Developers
 - Sales Tax exemptions - Central Sales Tax and State Sales Tax

Issue 1 – Ease of Land Acquisition



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- Land acquired by the State for development of the SEZ
 - Slow process
 - Active government support essential in light of multiple regulators
 - Judicial intervention on acquisition procedure and compensation
- Procedure for acquisition laid out in the Land Acquisition Act (LAA) and in various local Acts
 - Acquisition for Corporate Use or Public Purpose
 - SEZs as public purpose?

Issue 1 - Ease of Land Acquisition



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- Multiple legislations dealing with property rights
- Lack of clear land titles
 - Title insurance concept by the State as a solution
- No nodal authority
- Is a single window clearance possible?

Issue 2 – Foreign Investment



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- Attracting Foreign Investment
 - FDI in India subject to existing sectoral caps, particularly in services and trading activities
 - Minimum capitalization norms
 - Lock in requirements for investment
- Solutions
 - Lowering entry barriers
 - Opening up sectors



Issue 3 – Labour Regulation

- Flexible Labour regime
 - Exit of labour difficult due to stringent regulation
- India's labour regime is seen as pro labour
- Solution
 - Freedom to hire and fire
 - Productivity linked wages
 - Exemption from applicability of labour laws in the SEZs
 - Single Labour Authority
 - Special labour courts for SEZs

Issue 4 – Low Rates of Taxation



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- Current regime comparable internationally – Scope for provision of further tax incentives ?
- Recommendations:
 - Extending tax holiday to other activities - particularly SEZ Units providing services
 - Reduce rates of import duties
 - Exemption on Service Tax and Sales Tax on goods / services by SEZ Units to the DTA

Issue 5 – S. 10A Benefits



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- Tax benefits not available to units formed by splitting up or reconstruction of an undertaking
 - Legislative intent unclear
 - Is benefit disallowed only where the original owner continues to own the split units
- Clearer guidance for “reconstruction” – applies only where the original owner continues to own both parts
 - § Substantially the same person; and
 - § Old undertaking continues in altered form
- Solution under SEZ Bill - New unit not to be formed by transfer to a person with “substantial interest” in previous unit

Highlights of SEZ Bill, 2004



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- Legislates on subjects in the Central and Concurrent List
- Key Features
 - Deemed Foreign Territory
 - § Attendant import / export duty exemptions
 - Provides for a nodal agency – Special Economic Zone Authority
 - § Will ensure the financial and functional autonomy of the Zone
 - » Funding grants by Central Government
 - § Responsible for development of infrastructure
 - § Fixation of user charges

Highlights of SEZ Bill, 2004



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- Opening up insurance business in SEZs for foreign investment
- Constitution of special courts in respect of economic offences within the SEZ
- Exemption of central taxes, duties or cess under 29 Central Legislation

Highlights of SEZ Bill, 2004



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– Fiscal Incentives for SEZs and SEZ Units

§ Exemptions from

- » Custom Duty

- » Central Excise

- » Service tax – services for development of SEZs

- » Sales tax

§ Provision of duty drawbacks

§ Income tax holidays extended

§ Exemption from dividend distribution tax

Highlights of SEZ Bill, 2004



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- Weaknesses
 - Silent on land acquisition / property rights
 - No Labour Regulation Reform

- Status of the Bill
 - Approved by the Cabinet
 - To be tabled before Parliament
 - On the horizon

In Conclusion



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- Key Drivers for the Success of SEZ – Action Points
 - Develop Favourable Regulatory Framework
 - § Tax incentives
 - » Extend Income Tax benefits to more services
 - § Low transaction costs
 - » Exemptions from stamp duty, registration fee etc. within SEZs
 - § Regulatory certainty - Simple procedures / single window clearance
 - § Adequate Infrastructure Facilities
 - § Labour Law Reform



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THANK YOU