



BMR & Associates

Tax and Regulatory

# SEZ POLICY – PRESENT STATUS

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**Conference on**

**EPC Contracts Tax & Legal Imperatives**

18 -19 May 2007 | Hotel Imperial | Janpath | New Delhi | India

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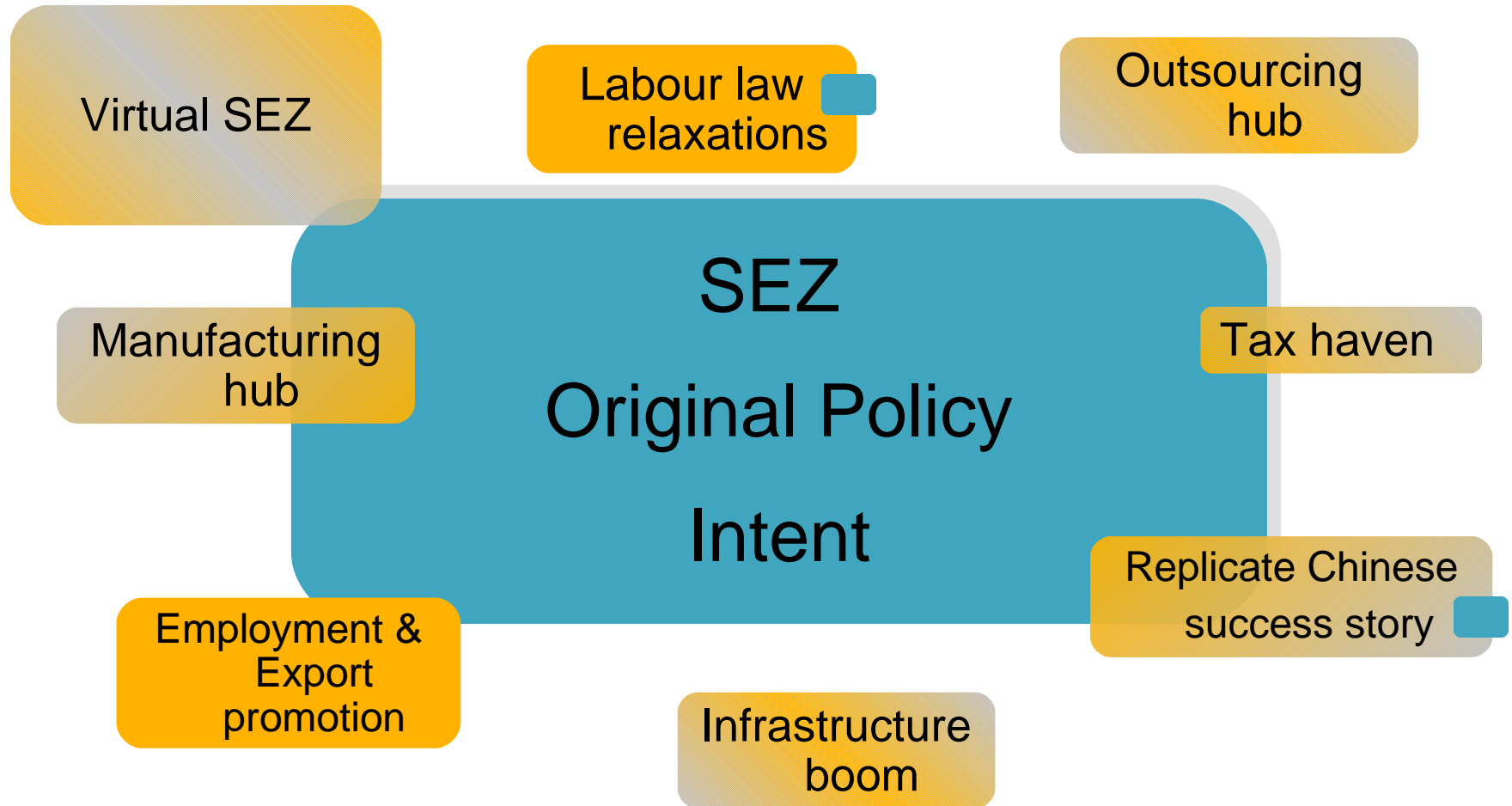
- Global Scenario
- Original Intent
- Ground realities
- SEZ Bandwagon – boon or bane
- Direction of the Policy



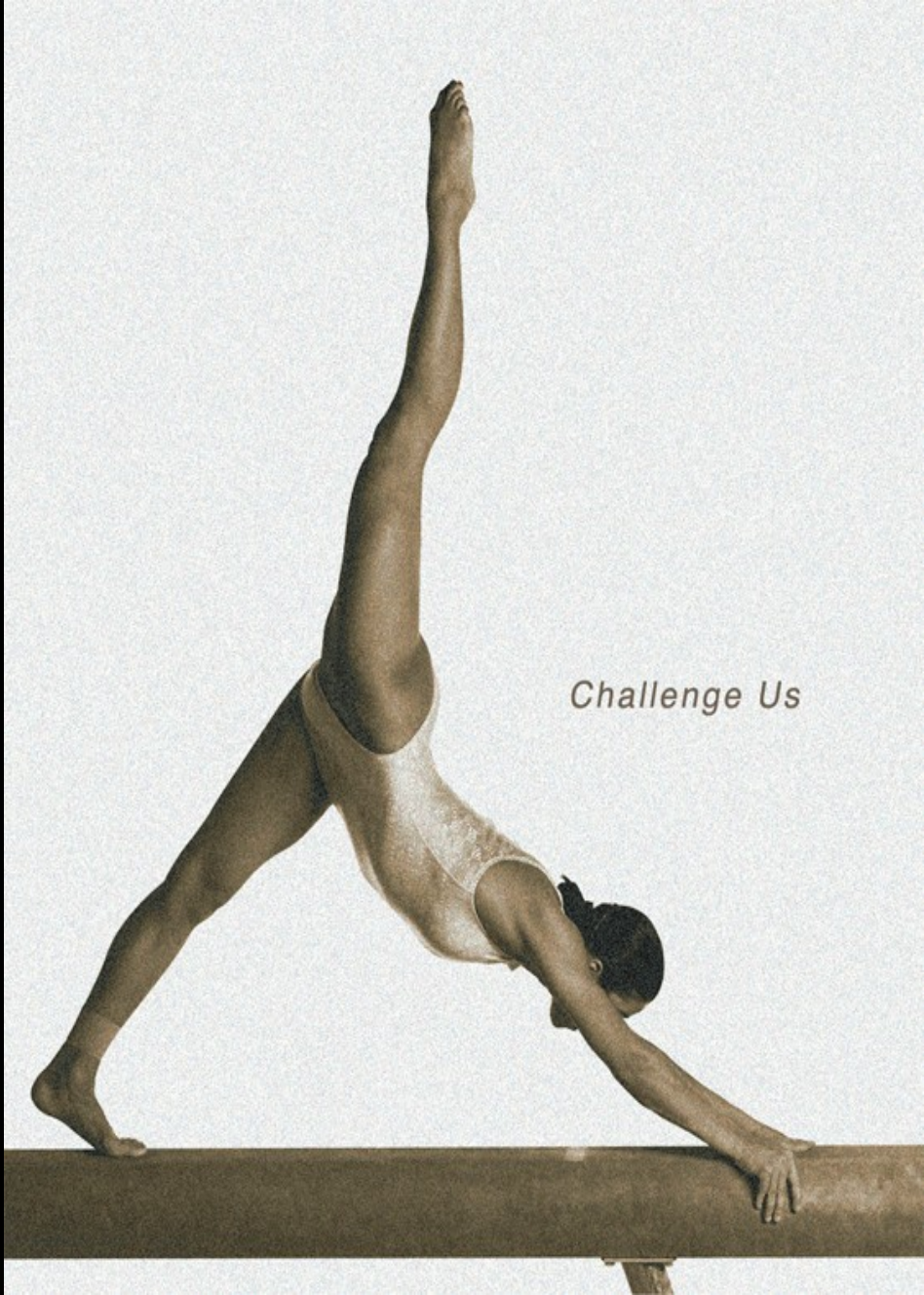
# GLOBAL SCENARIO

- Over 3000 SEZs have been set up in 120 countries the world over
- World's first SEZ set up in Puerto Rico in 1947
- Objective for development of SEZs in each country differed from the other:
  - Mauritius – employment generation
  - South Korea – establishment of the services sector
- SEZ concept has been a driver of economic growth and success in countries like China, Korea, UAE etc

# ORIGINAL INTENT – SEZ POLICY IN INDIA



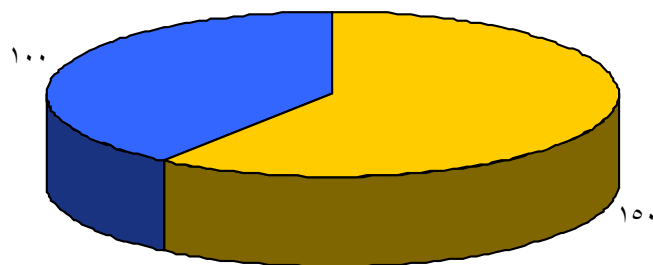
# GROUND REALITIES



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# SEZ APPROVALS AND NOTIFICATIONS

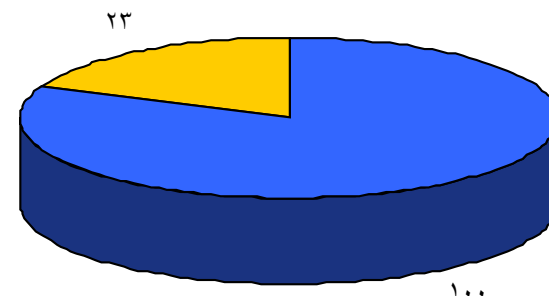
Approvals vs Notifications



■ Formal Approvals ■ Notified SEZs (therefrom till date)

- 250 proposals granted formal approval since introduction of SEZ Act, 2005 (“SEZ Act”)
- Only 100 have been notified till date

Notified vs Functional SEZs



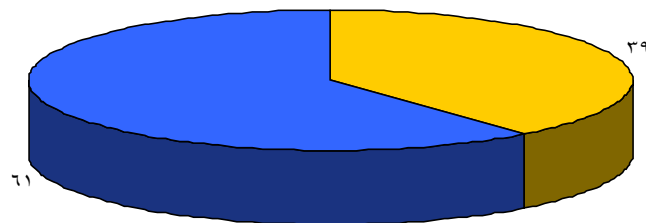
■ Notified SEZs in India ■ Functional SEZs (therefrom)

- There are only 23 functional SEZs in the country (including both pre-Act and new SEZs)

# INDIAN SEZ EXPERIENCE - IT SEZs??

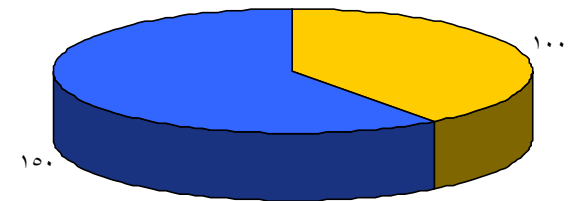
- 250 proposals granted formal approval since introduction of SEZ Act
- Approximately 150 are IT /ITES SEZs
- 170 proposals have been granted in-principle approvals
- Approximately 70 are for IT /ITES sector
- Till date 100 SEZs have been notified approximately 61 are IT /ITES SEZs

Notified SEZs



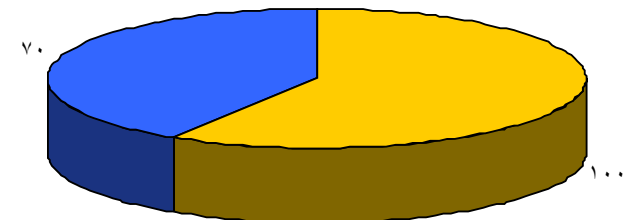
■ Other SEZs ■ IT/ITES SEZs

Formally Approved SEZs



■ Other SEZs ■ IT/ITES SEZs

In principle Approved SEZs



■ Other SEZs ■ IT/ITES SEZs

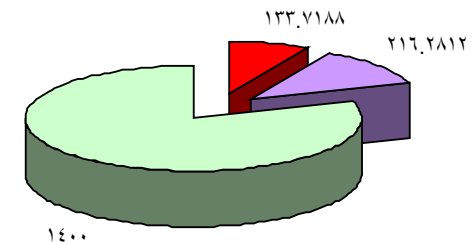
# INDIAN SEZ EXPERIENCE

- Other sectors approved as part of 250 formally approval cases include:

Pharmaceuticals	Textiles	Leather
Footwear	Gems and Jewelry	Biotechnology

- 100 SEZs including TCS, Biocon, Hexaware, Flextronics, Wipro, Infosys, Nokia and Reliance have already been notified
- Total approved SEZ area in India merely stands at a total of 1750 sq kms
- Approximately INR 15000 crores has been invested in new SEZs till date

Division of Total SEZ Area in sq kms (till now)

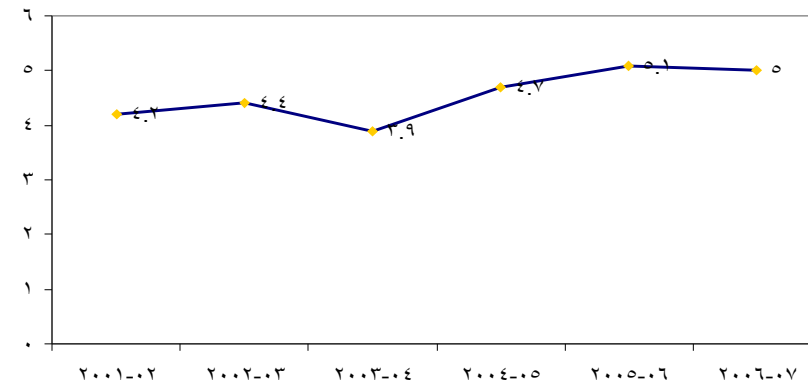


■ Notified area    ■ Formal Approved    ■ In-principle approved

# EXPORTS FROM SEZs

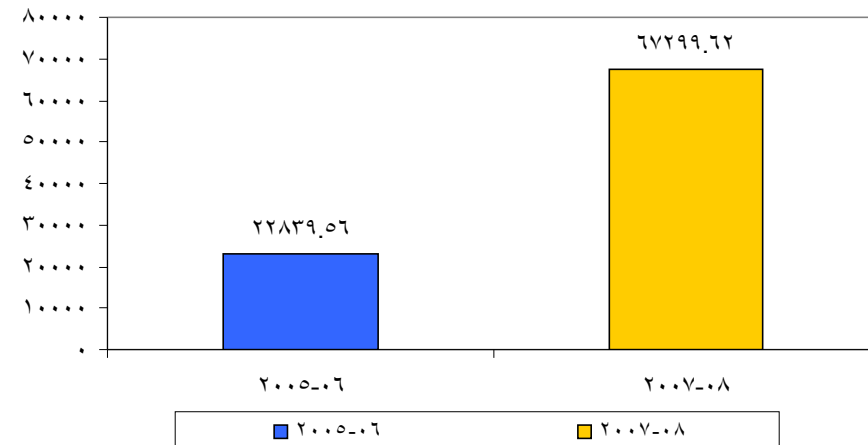
- Stated objective for development of SEZs – augmentation of exports
- SEZs to act as catalyst to increase in India's portion in Global trade
- SEZ exports at a faster pace in comparison to India's overall exports
- Percentage of SEZ exports in India's overall exports remains largely untapped – positioned for higher growth
- In value terms projections for 2007-2008 show that SEZ exports are likely to triple from current levels

Share of SEZ Exports In India's Exports (%)



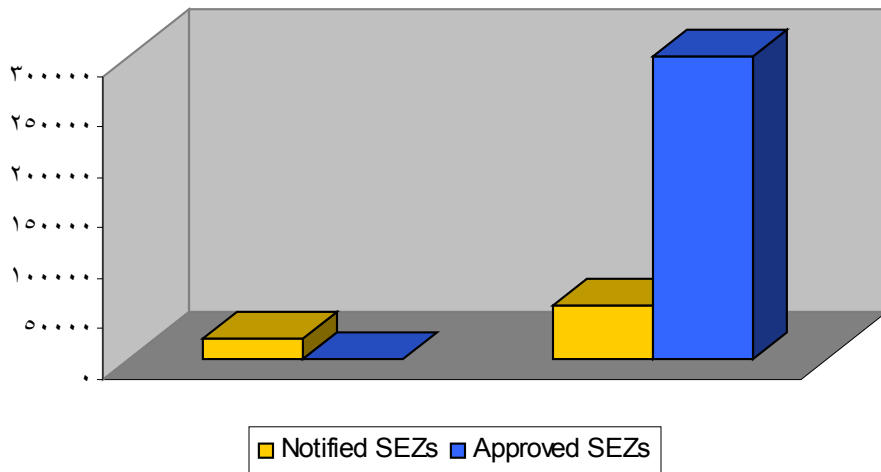
Source – Colliers International India Research, 2007

Total exports Vs Projections (In Crores)

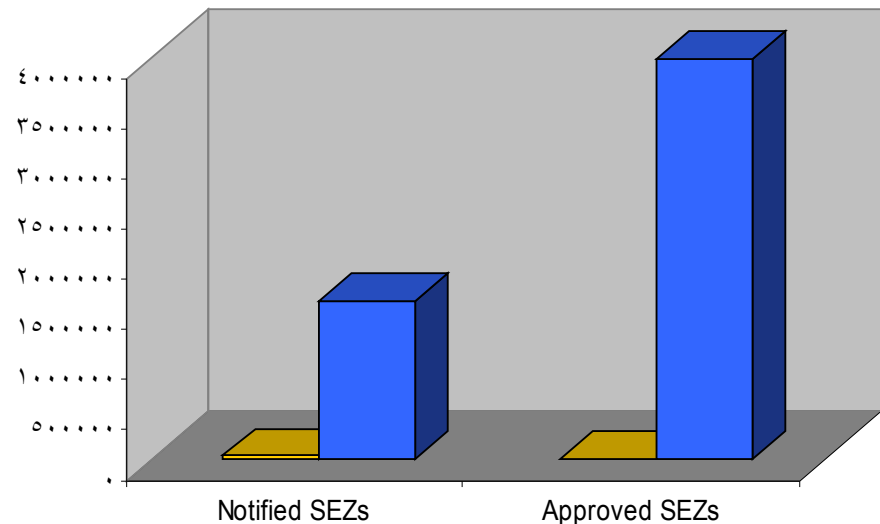


# INVESTMENT AND EMPLOYMENT IN SEZs

Investment In SEZs (In Crores) - Actual figures and projections



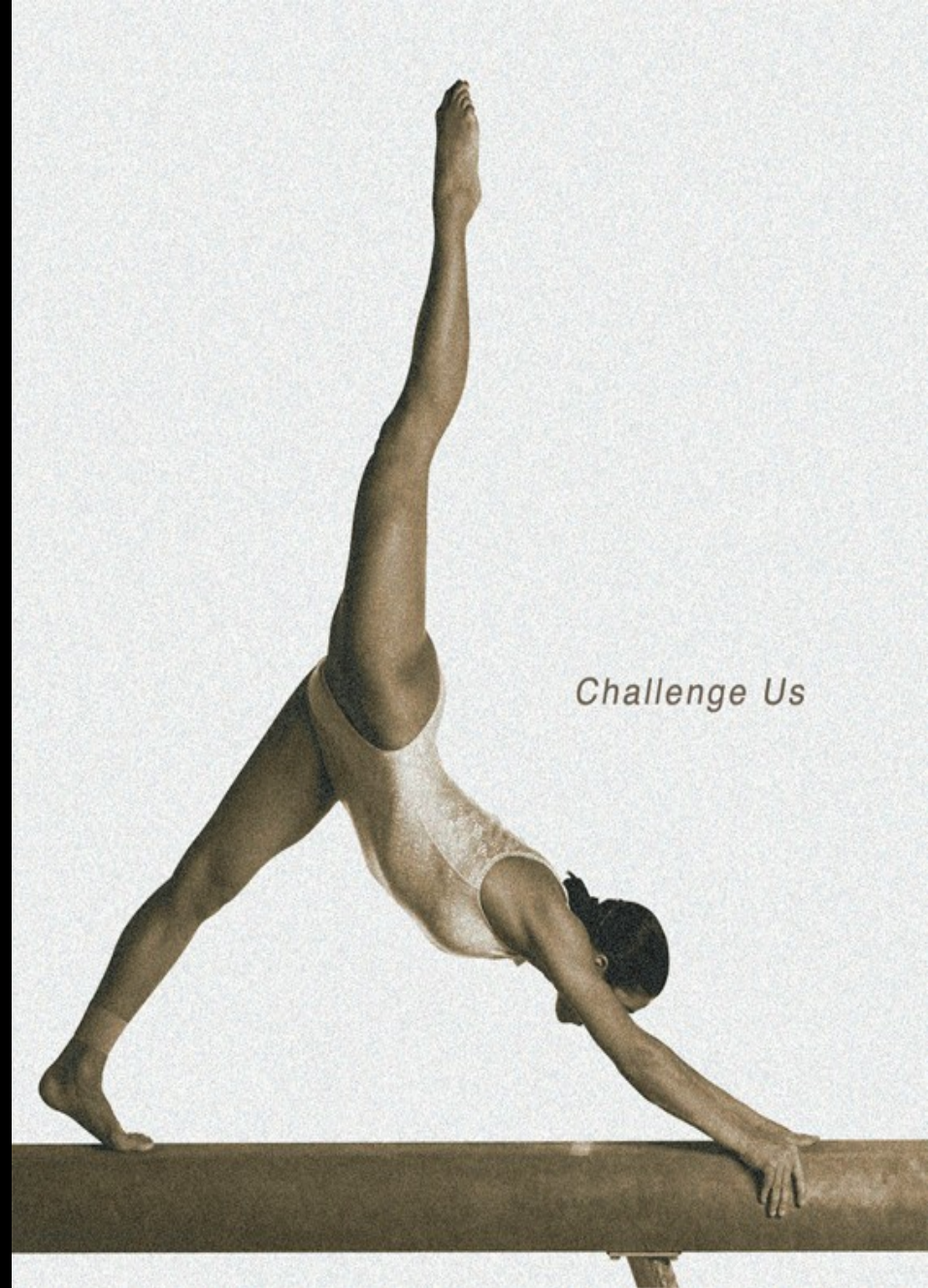
Employment Figures (actuals and projections)



- Upon notification of all formally approved SEZs it is projected that an Investment to the tune of INR 300,000 Crores
- Currently investment of INR 53,561 crores has been made (figures for 63 notified SEZs)

- All notified SEZs becoming functional will generate employment for 1,575,452 persons
- Projections show additional 4 million will be created if all formally approved SEZs became functional

# SEZ BANDWAGON – BOON OR BANE



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# SEZ BANDWAGON

## SEZ Legislative framework

- SEZ Legislation enacted by the Parliament in June, 2005
- SEZ Rules after much delay were notified in February, 2006
- Within a year Government of India released Amendment Rules, 2006 and Amendment Rules 2007
  - Minimum land requirements for development of different types of SEZs revised
  - Minimum processing area requirements rationalized and revised ( 25-35-50%)
  - Directions for provision of specified type of infrastructure ( eg 24/7 – power, AC)
  - Bar on use of previously used plant and machine
  - Empowering the Board of Approvals (“BoA”) to relax contiguity criteria, allow change in categorization of SEZs
  - Reduction of validity period of in-principle approval ( 1 yr, extendable by 1yr at a time)
  - Procedural changes – introduction of new forms, approval letters etc

**Despite extensive legislative framework – Policy continues to be nebulous**

# SEZ BANDWAGON

## Creation of other Regulatory bodies

- Fears of revenue leakage led to Inter-Ministerial tussle between Finance and Commerce Ministry
- Empowered Group of Ministers (“EGoM”) was constituted
- Decisions of EGoM superimposed on the SEZ legislation, like:
  - Moratorium on approvals, Sectoral caps, lifting bans on grant of approval
  - Ceiling on the maximum area for a multi product SEZ
  - Ban on compulsory land acquisition by State Governments
- BoA – nodal agency for granting SEZ approvals though created per the provisions of the SEZ Act – policy level changes superimposed on legislation, viz:
  - Net worth criterion ( 250/1000 cr investment of net worth of group 50/250 crore +)
  - Approval necessary if SEZ Developer changes name and share-holding pattern
  - Guidelines for creation of social infrastructure etc

**Legislative framework is it being hijacked by will of these regulatory bodies**

# SEZ BANDWAGON

## Socio – politico- economic scenario – Effects

- Introduction of SEZ Act – fervour in Industry to file applications to gain SEZ status
  - Approximately 300 application are still pending consideration
  - Constant changes in Policy led to change of plans - Industry Giants to invest in SEZs - Intel's proposed Chip Fabrication SEZ, HPs SEZ in Karnataka
- Politics of SEZs
  - Economics associated with SEZs led to battle-lines being drawn between Commerce Ministry – (advancing SEZ concept) and Finance Ministry – (attempting to roll back exemptions)
  - Empowered Committee of State Finance Ministers on VAT have unanimously agreed that no state level benefits will be given to SEZs for development in non-processing

## Advantage Finance Ministry

# SEZ BANDWAGON

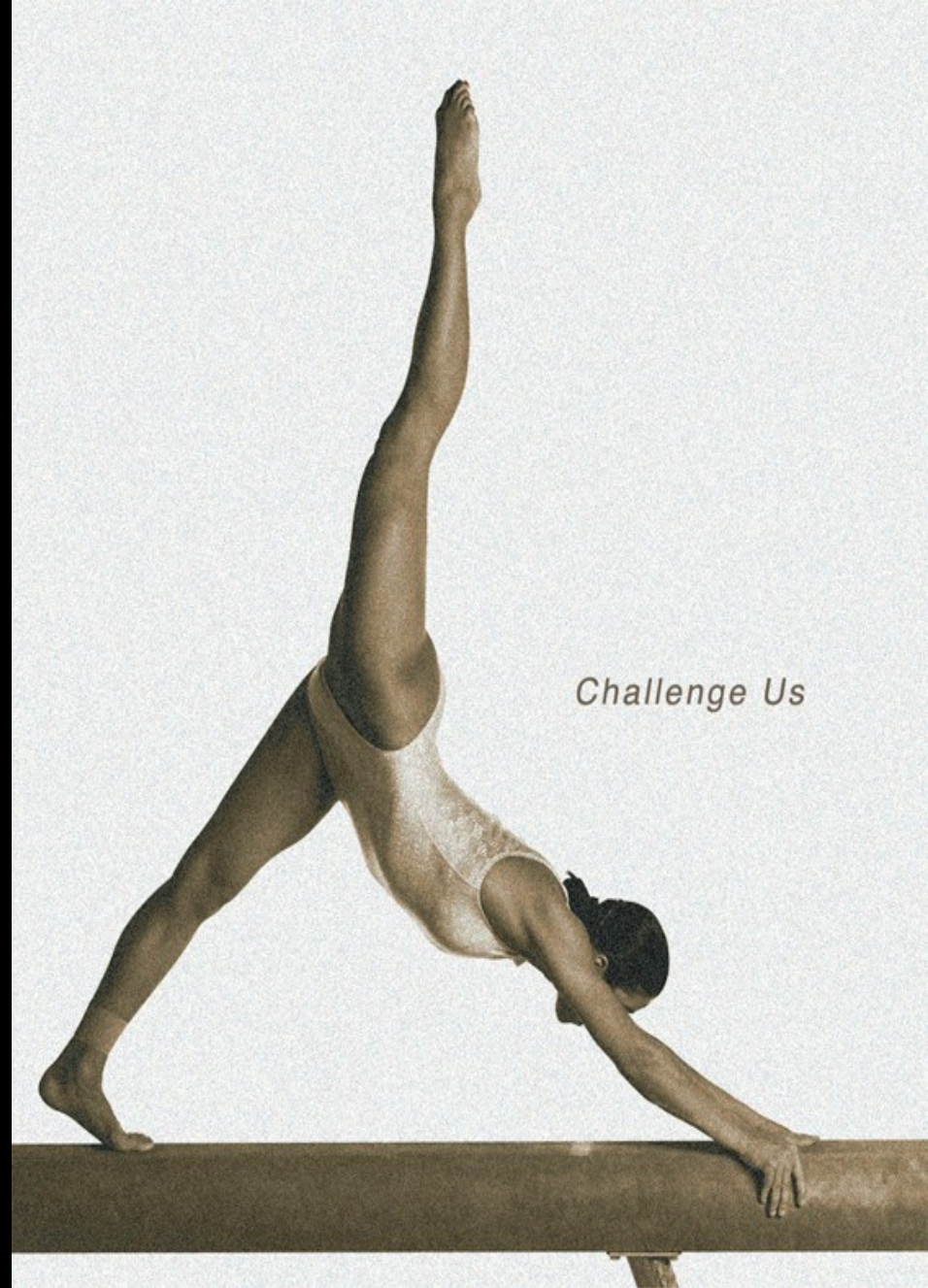
## Socio – politico- economic scenario – Effects

### ➤ Politics of SEZs

- Quantum of investment – Varied States of India all out to woo prospective investors
- Maharashtra and Andhra Pradesh – maximum number of SEZs
- Large scale transfer of lands (industrial, wasteland and agricultural) to large corporates to develop the SEZs
- Uproar by farming community, widespread discontent and violence – against acquisition (Raigad- Reliance SEZ, Nandigram – Saelim Group)
- Claim for adequate compensation to displaced farmers – changes in Rehabilitation and Resettlement Policy (“R&R”), 2003
- Ban on compulsory land acquisition by States for SEZ development
- Comprehensive R&R Bill, 2007 mooted to deal with the compensation packages for displaced farmers for SEZs development
- Group of Ministers (“GoM”) to discuss changes in SEZ related R&R policy and Bill -

## Roadblocks for SEZs continue

# DIRECTION OF SEZ POLICY



# SEZ - DIRECTION

- Yet another Amendment in Rules is imminent to capture the decisions of the EGoM and BoA
- EGoM to clarify date from when ban on compulsory land acquisitions will come into force – Potentially raise legal issues for outstanding agreements entered into by various State Governments eg Saelim Group's SEZ in West Bengal, Reliance – Maha-Mumbai SEZ in Maharashtra etc
- Migration of Growth of existing Units into the SEZ regime with the sunset clause nearing
- Formalization of guidelines for development of infrastructure within the processing and non-processing areas of the SEZ
- R&R Policy / Bill, 2007 to be linked to SEZ development
  - All states should set up rehabilitation councils enjoying statutory backing
  - Those whose lands are acquired should get either jobs or equity shares

# SEZ - DIRECTION

- R&R Policy / Bill, 2007 to be linked to SEZ development (cont)
  - A free house site, proportional to loss, should be allotted to affected family
  - Entire compensation should be disbursed before work on the project begins
  - Councils to conduct environmental and social impact assessment
  - Redressal cell must be set up under rehab & resettlement commissioner
  - R&R Bill requires companies to earmark a percentage of profits or turnover for developing the affected areas
  - Companies should coordinate with the Centre and States in supporting their ongoing rural development plans – Forced CSR

# Annexures



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# SEZ POLICY - EVOLUTION

## Original Intent

- Labour law relaxations
  - Deemed foreign territory
  - Easy hire and fire policy
  - Not to be governed by existing stifling Labour law regime

## Current provisions

- SEZs will be governed by the existing Rules and regulations governing Trade Unions, Industrial and Labour disputes, Employer's Liability, workmen's compensation etc

## Dilution of Intent

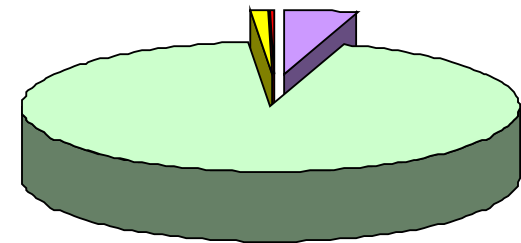
- Passage of the SEZ Bill was stalled owing to political furor against dilution of existing labour law regime
- Bill was passed and subsequent amendment made at the behest of the Communists members of the ruling coalition Government

# CHINA's SEZ MODEL

➤ China adopted the SEZ model in the 1980s. Highlights of Chinese SEZ model are:

- Large in size eg Shenzhen, Xiamen, Shantou etc
- Single window clearance for both application and operation phases
- Flexible labour laws
- Exemption from customs, import duties and licenses on all products and services used for processing of export products
- Delegation of powers in favour of provincial and local governments to manage the zones

Land under SEZs in China and India



■ Total SEZ Land in India ■ Hainan ■ Shenzhen ■ Xiamen

# COMPARISON BETWEEN CHINESE & INDIAN MODEL

## China

- SEZs large in size like Shenzhen (326 sq km), Xiamen (132 sq km) etc
- Locational advantage as SEZs lie strategically close to ports and cities of Hong Kong, Taiwan and Macau
- Vast areas provision for world class infrastructure
- Flexible labour laws

## India

- SEZs vary in size from 10 to 1000 hectares with the Reliance SEZ being the largest at 119 sq km
- Can be set up anywhere. Port based SEZs have been approved but majority SEZs are land locked
- Small areas inadequacy of infrastructure
- Stringent labour law regime

Source – Colliers International India Research, 2007



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