

**GOVERNMENT OF INDIA  
FINANCE  
LOK SABHA**

UNSTARRED QUESTION NO:2230  
ANSWERED ON:06.08.2010  
LOSSES DUE TO TAX RELAXATIONS TO SEZs  
Rama Devi Smt. ;Singh Shri Rajiv Ranjan (Lalan)

**Will the Minister of FINANCE be pleased to state:**

- (a) whether the Government has made any assessment on the quantum of losses incurred due to tax relaxations extended to special Economic Zones (SEZs);
- (b) if so, details thereof and the reaction of the Government in this regard;
- (c) whether Comptroller and Auditor General has made any assessment of the same;
- (d) if so, the details thereof and the reaction of the Government thereto; and
- (e) whether the Government proposes to reconsider the provisions regarding tax relaxation to SEZ units?

**Answer**

MINISTER OF STATE IN THE MINISTRY OF FINANCE(SHRI S.S. PALANIMANICKAM)

(a) & (b) : As per the Receipt Budget, 2010, the estimated revenue foregone during financial year 2008-09 on account of various direct tax deductions given to Special Economic Zone (SEZ) units and SEZ developers is Rs 4459 crores, while the projected revenue forgone on the same account for financial year 2009-10 is Rs.5266 crores. Revenue foregone on account of customs duty exemptions to SEZs has been of the order of Rs.2324 crore (Provisional) for 2008-09 and Rs.3204 crore (Estimated) for 2009-10.

(c) & (d) :The Report of the Comptroller and Auditor General of India (C&AG) for the year ended March, 2007 on Performance Audit on Union Government - Indirect Taxes have, inter alia, raised certain issues relating to Special Economic Zones. These issues mainly relate to achievement of Net Foreign Exchange (NFE) through deemed exports; duty foregone on inputs used in exempt products cleared in DTA; non achievement of NFE positive by certain units; violation of conditions of Letters of Permissions (LOPs); short levy of duty on Domestic tariff Area (DTA) sales, etc. The Special Economic Zones (SEZs) are under obligation to achieve positive Net Foreign Exchange (NFE) earnings over a period of 5 years, failing which penalties are leviable. The SEZ Act, 2005 provides for domestic clearance by units in SEZ on payment of chargeable duties of customs including Anti-dumping, Countervailing and safeguard duties under the Customs tariff Act, 1975 where applicable, as leviable on such goods when imported. In the audit report, the scope of which covered 2061 Special Economic Zone (SEZ) units, C&AG has observed that 22 units in two SEZs had been achieving the prescribed positive Net Foreign Exchange (NFE) mainly through domestic sales. However, as per the latest figures compiled, physical exports from the SEZs are of the order of 84% of their total turnover. During this period, the domestic supplies made by SEZs were about 12% and sales in Domestic Tariff Area, not counted for positive NFE, was about 4%.

(e): The draft Direct Taxes Code (DTC) along with a Discussion Paper were released for public discussion in August, 2009. The Discussion Paper mentioned that profit-linked incentives are inherently inefficient. Essentially, a profit-linked incentive is regressive in nature. Consequently, there is an inbuilt incentive for laundering and shifting of profits to the exempted activity. Since profit is the basis for exemption, there is no incentive for investment and upgradation during the period of tax holiday. Such profit-linked incentives also lead to significant loss of revenue and encourage rent-seeking behaviour. Therefore, the Code proposes to substitute the currently available profit-linked incentives by investment-linked deductions for specified sectors including SEZ developers. Investment-linked incentives are better directed instruments since they are performance based and target the incentive specifically to the capital investment. With regard to the profit-linked incentives available to SEZs, the draft Direct Taxes Code (DTC) proposed the following:

- (i) provision for profit-linked deduction currently available to SEZ developers for the unexpired period for all SEZs which are notified on or before the commencement of DTC;
- (ii) provision for an investment-linked deduction for all SEZ developers notified on or after the date of commencement of the DTC;
- (iii) Minimum Alternate Tax (MAT) and Dividend Distribution Tax (DDT) to be levied on SEZ developers;
- (iv) no protection of the profit-linked deduction available to SEZ units for the unexpired period of the deduction left to them after the date of commencement of the DTC;
- (v) no tax benefits for SEZ units set up on or after the date of commencement of the DTC;and

(vi) MAT on all SEZ units.

A number of inputs were received on the proposals outlined in the draft DTC and Discussion Paper. These inputs have been examined and the major issues on which various stakeholders have given their views have been identified. These issues have been addressed in the form of a Revised Discussion Paper which was released in June, 2010.

The revised Discussion Paper modifies the proposals for SEZ units to also protect the profit-linked deduction for the unexpired period for SEZ units beginning operations before 31.3.2011.