

EY Flash News

Key amendments to Special Economic Zone Rules, 2006

Enabling establishment of non SEZ IT/ITeS businesses in SEZ

Executive summary

EY Alerts cover significant tax news, developments and changes in legislation that affect Indian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor.

The Ministry of Commerce and Industry (MOCI) has announced a long-awaited amendment to the Special Economic Zone (SEZ) Rules, 2006 allowing non SEZ units to set up and operate information technology (IT)/IT enabled services (ITeS) businesses in the demarcated non processing built up area of the SEZ. This amendment will enable SEZ developers to optimally utilize the vacant space in existing SEZs.

The MOCI vide the aforesaid amendment has inserted a new Rule 11B '*Non-processing areas for IT/ITeS SEZ*'^[1] allowing co-existence of SEZ units and non-SEZ IT/ITeS business in the same SEZ premises.

Some of the key features of the amendment are as under:

- ▶ Allowing non SEZ IT/ITeS businesses to operate in the non-processing built up area of the SEZ, subject to obtaining consent from the Board of Approval (BOA).
- ▶ Repayment of proportionate tax benefits availed by the developers on the demarcated non-processing area.
- ▶ Minimum built up processing area to be maintained by the developers depending on category of cities.
- ▶ Control measures in relation to operations of SEZ units and non SEZ IT/ITeS businesses to be put in place.
- ▶ Repayment of tax benefits already availed on common infrastructure that would be accessed by SEZ units and non SEZ IT/ITeS businesses.
- ▶ No tax benefits would be available on continuing basis on the operations and maintenance cost in relation to the common infrastructure.

^[1] G.S.R. 881(E) dated 06th December 2023

Background

- IT/ ITeS SEZs have been facing challenges in capacity utilization due to the COVID-19 pandemic and the Work from Home (WFH) policy adopted by SEZ units. Several representations were made by key industry players and SEZ developers to allow non SEZ IT/ITeS businesses to operate out of SEZ area.
- The MOCI vide notification no. G.S.R. 881(E) dated 6 December 2023 has inserted new Rule 11B 'Non-processing area for IT/ITeS SEZ' enabling co-existence of SEZ units and non SEZ IT/ITeS businesses.

Salient features

1. **Co-existence of SEZ units and non SEZ IT/ITeS businesses:**
 - Prior to this notification, the SEZ regulations did not permit non SEZ IT/ITeS units to operate from a SEZ area on 'as-is' basis.
 - Vide the aforesaid amendment, the MOCI has now enabled non SEZ units engaged in only IT/ ITeS businesses to operate from the demarcated non-processing area of a SEZ.
 - Such non-processing area shall consist of complete floor and part of a floor shall not be allowed to be demarcated as a non-processing area.
 - The BOA on request of developer may permit demarcation of a portion of built-up area of an IT/ITeS SEZ as a non-processing area subject to repayment of taxes.
 - Non SEZ IT/ITeS businesses shall not avail any rights or facilities available to SEZ units and these businesses operating out of the said non-processing area would continue to comply with all other regulations as are applicable to an entity operating in a Domestic Tariff Area.

2. Conditions to be followed by SEZ developers

- SEZ developer would be required to ensure appropriate access control mechanisms are in place for movement of goods and persons in and out of the SEZ premises. This is for both SEZ units and non SEZ IT/ITeS businesses.
- The developer would be required to repay the proportional tax benefits (without interest) corresponding to the built-up area allocated to the non SEZ IT/ITeS businesses.
- For social and commercial infrastructure to be shared by SEZ units and non SEZ IT/ITeS businesses, developer would be required to repay the tax benefits (without interest) availed for creation of such infrastructure.
- The amount to be repaid by developer shall be based on a certificate issued by a Chartered Engineer.
- No tax benefits would be available on the operation and maintenance cost of common infrastructure and facilities.
- The developer would be required to comply with certain minimum area requirements:
 - **Condition 1:** Demarcation of total non-processing area should not result in decreasing the processing area to less than 50% of the total SEZ area.

OR

- **Condition 2:** The minimum built-up processing area should be as under:

Category of cities as per Annexure IV-A of SEZ Rules, 2006	Minimum built up processing area (in sq.mt.)
Category 'A'	50,000
Category 'B'	25,000
Category 'C'	15,000

Comments

- ▶ Enabling non SEZ IT/ITeS businesses to operate out of SEZs is a welcome move and addresses the long-term demand of SEZ developers. This would enable optimum utilization of space available in the SEZs all over India which are currently lying vacant. The amendment will also provide IT/ITeS sector access to state-of-the-art facilities and world class infrastructure available in SEZs.
- ▶ In addition, it would also enable IT/ITeS businesses to revamp their existing operational models and look at consolidation of operations in SEZ.
- ▶ Further, WFH conditions as applicable to the SEZ units shall not apply to these non SEZ IT/ITeS businesses.
- ▶ While the amendment allows non SEZ IT/ITeS businesses to operate from SEZ area, some aspects that still require further clarifications include:
 - ▶ At the time of demarcation of non-processing built up area, whether depreciation benefit would still be available to the SEZ developer.
 - ▶ Whether process of e-scraping of IT assets used by the developer needs to be followed.
 - ▶ Where an existing SEZ unit wishes to operate from non-processing area, process of exit from SEZ scheme and payment of consequential duties.
- ▶ It may also augur well for the stakeholders to look into GST implications for reducing overall cost of demarcation and providing operation & maintenance services.
- ▶ The amendment indicates government's willingness to promote SEZs in the country and give flexibility to operate from SEZ.

Our offices

Ahmedabad

22nd Floor, B Wing, Privilon
Ambli BRT Road, Behind Iskcon
Temple, Off SG Highway
Ahmedabad - 380 059
Tel: + 91 79 6608 3800

Bengaluru

12th & 13th floor
"UB City", Canberra Block
No. 24, Vittal Mallya Road
Bengaluru - 560 001
Tel: + 91 80 6727 5000

Ground Floor, 'A' wing

Divyasree Chambers
11, O'Shaughnessy Road
Langford Gardens
Bengaluru - 560 025
Tel: + 91 80 6727 5000

Chandigarh

Elante offices, Unit No. B-613 & 614
6th Floor, Plot No- 178-178A
Industrial & Business Park, Phase-I
Chandigarh - 160 002
Tel: + 91 172 6717800

Chennai

Tidel Park, 6th & 7th Floor
A Block, No.4, Rajiv Gandhi Salai
Taramani, Chennai - 600 113
Tel: + 91 44 6654 8100

Delhi NCR

Ground Floor
67, Institutional Area
Sector 44, Gurugram - 122 003
Haryana
Tel: +91 124 443 4000

3rd & 6th Floor, Worldmark-1
IGI Airport Hospitality District
Aerocity, New Delhi - 110 037
Tel: + 91 11 4731 8000

4th & 5th Floor, Plot No 2B
Tower 2, Sector 126
Gautam Budh Nagar, U.P.
Noida - 201 304
Tel: + 91 120 671 7000

Hyderabad

THE SKYVIEW 10
18th Floor, "SOUTH LOBBY"
Survey No 83/1, Raidurgam
Hyderabad - 500 032
Tel: + 91 40 6736 2000

Jamshedpur

1st Floor, Fairdeal Complex
Holding No. 7, SB Shop Area
Bistupur, Jamshedpur - 831 001
East Singhbhum Jharkhand
Tel: + 91 657 663 1000

Kochi

9th Floor, ABAD Nucleus
NH-49, Maradu PO
Kochi - 682 304
Tel: + 91 484 433 4000

Kolkata

22 Camac Street
3rd Floor, Block 'C'
Kolkata - 700 016
Tel: + 91 33 6615 3400

Mumbai

14th Floor, The Ruby
29 Senapati Bapat Marg
Dadar (W), Mumbai - 400 028
Tel: + 91 22 6192 0000

5th Floor, Block B-2

Nirlon Knowledge Park
Off. Western Express Highway
Goregaon (E)
Mumbai - 400 063
Tel: + 91 22 6192 0000

Pune

C-401, 4th floor
Panchshil Tech Park, Yerwada
(Near Don Bosco School)
Pune - 411 006
Tel: + 91 20 4912 6000

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