

## The Department of Commerce clarifies on issue of transfer of used capital goods

The Department of Commerce (“DoC”) has earlier today clarified its stand on the issue relating to transfer of used capital goods from a Domestic Tariff Area (“DTA”) to a unit in a Special Economic Zone (“SEZ”) by issuing Instruction No 68 dated October 28, 2010. This Instruction is in furtherance to the earlier Instruction No 11 issued by the DoC in August 2009 wherein the DoC had prescribed guidelines for transferring of used/second hand capital goods from DTA (including from an EOU/EHTP/STP/BTP unit). Instruction No 11 had clarified that SEZ unit could acquire used capital goods in excess of the 20 percent limit (imposed under the Income-tax Law) provided such units forego the income-tax exemption.

In the past, various companies had set up SEZ units by shifting their STP operations with a view of consolidating their operations. These companies had voluntarily forgone their income-tax holiday in respect of the SEZ units which were set up by migrating existing operations in accordance with Instruction No 11 issued by the DoC. Further, various other companies have filed and are in the process of filing application requesting for approvals to set up SEZ units by shifting existing operations.

Recently, some of the Development Commissioners (“DC”) along with the Unit Approval Committees (“UACs”) started taking a view that granting approvals to set up SEZ units by shifting existing operations of a STP unit would be against the basic objectives of the SEZ Regulations. Based on this stand, the UACs rejected applications for setting up SEZ units which involved substantial transfer of assets/operations from existing STPI units to proposed SEZ units. In some cases, approvals granted in the past (including in cases where the companies had actually set up operations in an SEZ pursuant to the said approvals) were also revoked on the same ground.

The DoC, after receiving a number of representations especially from Information Technology/ Information Technology Enabled Services (“IT/ITES”) SEZ units with regard to the above have issued Instruction No 68 dated October 28, 2010. Taking cognizance of the representations, the DoC vide this Instruction has clarified as follows:

- There is no provision in the SEZ Act/ Rules which prevents transfer of used goods from STP units to SEZ units;
- The only deterrence for transfer of such goods is not getting the exemptions under the Income tax Act, 1961 (“Act”) when the value of used goods exceed the threshold of 20 percent of the total capital goods installed by

### HIGHLIGHTS

- ***The DoC has clarified on the issue of transfer of used capital goods from STPI to SEZs***
- ***The DoC has acknowledged that there is no provision in the SEZ Act/ Rules which prevents transfer of used goods from STP units to SEZ units***
- ***Only deterrence to such transfer is unavailability of income tax benefits that too if such goods transferred exceed 20 percent threshold in a year***
- ***The Instruction has indicated the DCs that in case of any doubts, they should refer the case to the DoC and should not take unilateral decisions***

the unit in a year;

- The DoC has reiterated Instruction 11 wherein detailed guidelines have been prescribed for transfer of used/ second hand capital goods from DTA including EOU/EHTP/STP/BTP unit;

The DoC has also mentioned that DCs while considering such requests must take cognizance of the prescribed Instruction (i.e. No 11 and 86) in this regard.

Importantly, in relation to the applications that have been declined by the DCs notwithstanding there being no restriction in the SEZ laws, the DoC has highlighted to all the DCs that in case of any doubts, they should refer the cases to the DoC and should not take unilateral decisions.

## BMR comments

The Instruction issued by the DoC is significant given the difficulties previously approved units and proposed units were facing given the stand taken by a few DCs/UACs. This is likely to provide a huge relief to SEZ developers and units which propose to migrate operations from STP to SEZ by forgoing the income-tax holiday available to SEZ units. While this Instruction does not specifically refer to "migration of business", the intent seems to be clear that such migrations are not prohibited.

While this instruction seems to clarify the doubts on this issue, one would now need to wait and watch whether the DCs/UACs at the ground level accept this interpretation put to rest the controversy surrounding transfer of existing operations and not just capital goods.

To read the Instruction, please [click here](#)

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