

CHAPTER III

EXEMPTIONS UNDER INCOME TAX ACT, 1961

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**SPECIAL PROVISION IN RESPECT OF NEWLY
ESTABLISHED INDUSTRIAL UNDERTAKING
IN FREE TRADE ZONE.**

SECTION 10 - A

**Section 10A Explanatory Notes vide Board Circular
No. 308 dated June 29, 1981 :**

Under the existing provisions, a partial tax holiday is granted to all categories of assessees in respect of profits made by them from an industrial undertaking newly set up in India. Where the industrial undertaking is set up prior to 1-4-1981, the "tax holiday" concession consists of exemption from Income tax upto a specified percentage of the capital employed in the undertaking for five initial assessment years, subject to certain conditions. The percentage specified in this behalf was 7.5 % in the case of a company and 6 % in the case of others. Where an industrial undertaking is set up after 31-3-1981, the assessee who derives profits and gains from the industrial undertaking is entitled to a deduction, in the computation of his taxable income, of 20 % of the profits and gains (25 % in the case of a company) derived from such industrial undertaking for 8 initial assessment years, while in the case of co-operative societies, the tax holiday is granted for a period of 10 initial assessment years.

The Kandla Free Trade Zone was established by the Government of India in 1965, not only as an export promotion venture but also as a pioneering scheme for industrialisation of the under-developed area of Kutch and also for the development of the Kandla Port as a substitute for Karachi; similarly the Santacruz Electronics Export Processing Zone was set up near Bombay to promote rapid growth of the electronics industry as also to encourage setting up of 100 % export oriented industries in the electronics sector. Under the existing provisions assesseees who derive profits and gains from new industrial undertaking set up in these free Trade Zone area are entitled to the benefit of partial tax holiday, investment allowance, export markets development allowance, additional depreciation allowance, deduction in respect of industrial undertakings set up in backward areas (for industrial undertakings situated in the Kandla Free Trade Zone) and other incentives available in the case of all industrial undertakings. A number of countries have set up free trade zones to attract investment for industrial growth by offering substantial tax concessions including a complete tax holiday for a specified number of years.

With a view to encouraging establishment of export oriented industries in free trade zones new section 10A inserted by Finance Act, 1981 w.e.f. 1-4-1981, provides for

complete tax exemption in respect of the profits and gains derived from industrial undertakings set up in these zones for a period of five initial assessment years. The concession will also apply in relation to other free trade zones that may be set up in future and will be available to all taxpayers, including foreign companies and non resident non corporate taxpayers. The proposed "tax holiday" will be in lieu of all other tax concessions e.g. investment allowance the existing Partial tax holiday, concessions available to industries set up in backward areas, etc. It is provided that after the expiry of the tax holiday period there will be no carry forward of any unabsorbed losses, depreciation, development rebate investment allowance, tax holiday deficiency or any other deduction or allowance admissible under the Income tax Act. For the purpose of depreciation, the written-down value of the assets used in the industrial undertakings for the assessment years subsequent to the tax holiday period will be determined as if the depreciation allowable under the existing provisions had actually been claimed and allowed. Some of the existing tax concessions, such as, the deduction available in relation to new industrial units set up in backward areas and small scale undertakings established in rural areas extend over a period exceeding five years. Units availing of the complete tax holiday now enacted will not be intitled to such concessions even after the expiry of the tax holiday period.

**THE PROVISIONS OF NEW SECTION 10 A
MAY BE SUMMARISED AS FOLLOWS :**

Sub-section (1) provides that any profits and gains derived by an assessee from an industrial undertaking to which the section applies will not be included in the total income of the assessee.

Sub-section (2) provides that this section will apply to an industrial undertaking which fulfils certain conditions, namely, that it begins to manufacture or produce articles or things during the previous year relevant to the assessment year 1981-82, or any subsequent assessment year in a free trade zone; it is not formed by the splitting up, or the re-construction, of a business already in existence; and it is not formed by the transfer to a new business of machinery or plant previously used for any purpose. For the purpose of this section, reconditioned imported machinery or plant will be regarded as new. Further, where the total value of the machinery or plant transferred to the new business does not exceed 20 % of the total value of the machinery or plant used in that business, the last mentioned condition will be deemed to have been complied with.

Sub-section (3) provided that the benefit of this section will be available to an industrial undertaking for five

assessment years beginning with the initial assessment year. The sub-section has been amended by the Taxation Laws (Amend. & Misc. Prov.) Act, 1986 w.e.f. 1-4-1987, and enables the taxpayer to choose the period of five years within a time frame of eight years beginning from the year in which production commenced. (see under sub-section(3) supra.)

Sub-section (4) provides that notwithstanding anything contained in any other provision of this Act, in computing the total income of the assessee of the previous year relevant to the assessment year immediately succeeding the last of the relevant assessment years (or of the previous year relevant to any subsequent assessment year), the unabsorbed depreciation allowance, the unabsorbed investment allowance , the unabsorbed development rebate, the unabsorbed capital expenditure on scientific research, the unabsorbed capital expenditure on family planning relating to the relevant assessment years will not be taken into consideration. Similarly unabsorbed business losses or loss under the head "Capital Gain" or the deficiency relating to tax holiday profits relating to the relevant assessment years will not be taken into account. Where the assessee was entitled to a deduction for the relevant assessment years in respect of the profits and gains from newly established industrial undertakings in backward areas or small scale industrial undertakings in rural areas or the tax holiday, no deduction will be admissible in the assessment years subsequent to the relevant assessment

years. Further, in computing the depreciation allowance on any assets in the assessment years following the relevant assessment years the written-down value will be computed as if the assessee had claimed and been allowed the depreciation in accordance with the provisions of the Income tax Act during each one of the relevant assessment years.

Sub-section (5) provides that where any industrial undertaking situated in a free trade zone has begun to manufacture or produce articles or things during any of the previous years relevant to the assessment years 1977-78 to 1980-81, such assessee may, at his option, before the expiry of the time allowed for the furnishing of the return of income for the assessment year 1981-82, furnish to the Income-tax ^{officer} a declaration in writing that the provisions of this section may be made applicable to him for the relevant assessment years other than the assessment year commencing before the assessment year 1981-82, and if he does so, then the provisions of complete tax holiday specified in this section will apply for such assessment years and the provisions of new sub-section (4) will also apply in relation to any assessment year following the relevant assessment years.

EXPLANATION : For the purpose of this section

- i) **FREE TRADE ZONE :** means the Kandla Free Trade zone and the Santacruz Electronics Export Processing Zone and includes any other free trade zone which the central Government may, by notification in the Official Gazette, specify for the purposes of this section.
- ii) **RELEVANT ASSESSMENT YEARS:** means the initial assessment year and four assessment year and four assessment years immediately succeeding the initial assessment year.
- iii) **MANUFACTURE:** includes any -
 - a) process or
 - b) assembling or
 - c) recording of programmes on any disc, tape, perforated media or other information storage device.

This clause has been inserted by the Finance Act, 1987, but is deemed to have been inserted with retrospective effect from 1-4-1981 the date on which section 10 A itself was inserted in the Act. It clarifies that manufacturing activity will include the activities of processing and assembling and also recording of programmes on

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any disc, tape, perforated media or other information storage device. It will be applicable from the assessment year 1981-82.

**TAX EXEMPTION FOR REMUNERATION OF
FOREIGN TECHNICIANS IN INDIA SECTION 10 (6) (VIIA)**

With the primary objectives to encourage development of industries in India, by making it possible for foreign technicians whose specialised experience and knowledge of industry, would be useful for that purpose to be employed by the industrial undertaking in India at reasonable remuneration, section 10 (6) (vii) (a) provides that where an individual who is not citizen of India renders services as a technician while in employment in India, commencing from a date after 31-3-1971, then the remuneration for such services would be exempt from income tax in his hand to the extent of Rs.4,000/- per month for a period of 24 months commencing from the date of his arrival in India.

Remuneration in excess of Rs.4,000/- per month is taxable in the hands of technician but if the employer agrees to pay such tax, the amount of such tax is not to be treated as the income of the foreign technician.

After the initial period of 24 months from the date of his arrival in India, the whole of the remuneration of the technician will be chargeable to tax. However if the employer pays the tax on the whole of the remuneration the perquisite represented by the tax so paid will be exempt from further tax

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in the hands of foreign technician. This latter exemption will be available for a period of 24 months next following the initial period of 24 months as stated above. In other words the total period for which a foreign technician may be employed in India after 31-3-1971, on a tax-free exemption will be 4 years.

In order to earn exemption under this section, it is essential that the foreign technician should have been non-resident in all the 4 financial years immediately preceding the financial year in which the foreign technician arrived in India and his contract of service should have been approved by the Central Government or an application having been made in this behalf within 6 months of the commencement of his service.

The act provides that exemption to the extent of Rs.4,000/- per month for the period of 24 months. The possible reason of giving such exemption for limited period may be that the Indian personnel should acquire new technology within a period of two years and later on the foreign technician should not be in India, and his place should be taken by a domestic person.

It is suggested that the period of foreign technicians should be extended.

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**EXEMPTION FROM INCOME TAX ON INTEREST PAYABLE
BY INDUSTRIAL UNDERTAKINGS ON FOREIGN LOAN**

Section - 10 (15) (B) (C) (F)

Interest paid by a industrial undertakings in India to foreign lenders & would be exempt from income-tax by virtue of section 10 (15) in the undernoted cases:

- i) Interest payable on money borrowed by it under a loan agreement entered into any such financial institution in a foreign company as may be approved in this behalf by the Central Government by a general or special order (Clause-B)
- ii) Interest payable on any moneys borrowed or debit incurred by it in a foreigncountry in respect of the purchase out side India of raw-material or capital plant and machinery, to the extent to which such interest does not exceed the amount of interest calculated at the rate approved by Central Government in this behalf, having regard to the terms of the loan or debts and its repayment. (Clause-C)
- iii) Interest payable on any money borrowed by it in Foreign currency from sources outside India under a loan agreement approved by the Central Government having regard to the need for industrial development

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in India to the extent to which such interest does not exceed the amount of interest calculated at the rate approved by the Central Government in this behalf having regard to the terms of loan and it's repayment.