

## **GST impact on SEZ transactions**

- **CA Madhukar N.Hiregange & CA Mahadev.R**

SEZ schemes are being promoted with an intention to create competitive environment for goods / services exported thereby to increase the foreign exchange inflow into India. The objectives of government for SEZs include allowing tax free procurement of goods and services with support in basic essential infrastructure facility for production of goods or services. Such facilities have led to increase in foreign entities participation in India. Section 7 of SEZ Act 2005 provides for exemption to all goods or services procured from a DTA or foreign suppliers.

According to Section 51 of the SEZ Act 2005, the provisions of SEZ Act would have overriding effect on provisions of any other act including taxation laws. Therefore, tax exemptions were needed to be provided for SEZ transactions in all tax laws. If one were to observe, the central excise duty was not applicable on goods manufactured in SEZ units. State governments provided either refund or exemption on sale of goods by SEZs.

The overriding effect of Section 51 may not be the case in GST. The central government has powers relating to SEZ in article 246 of the constitution whereas GST is levied with article 246A. GST may prevail over SEZ provisions as article 246A provide powers to central / state governments for taxing goods or services notwithstanding anything contained in article 246.

### ***Importation of goods or services by SEZs***

Goods imported by SEZs were exempted from basic customs duty, CVD (levied in lieu of central excise duty) and SAD (levied in lieu of VAT). After introduction of GST, SEZ transactions are liable for IGST. Customs notification no.64/2017 has been issued to exempt import of goods from levy of IGST for SEZ operations. IGST notification no.18/2017 exempts levy of IGST on import of services by SEZs for authorized operations.

### ***Supplies to SEZ from DTA***

Supply of goods or services by or to an SEZ is deemed to be an inter-state supply according to Section 7 of IGST Act 2017. Therefore, the transactions can be subject to IGST even if location of supplier and place of supply are in same state.

Supplies to SEZ are treated as zero rated supply in terms of Section 16 of IGST Act 2017. Therefore, any supplier supplying goods or services cannot charge GST to SEZ. The credit in respect of inputs / input services used in respect of such SEZ supplies would also be eligible for

the supplier which can be utilized for other GST payments. Other option for supplier would be to claim refund of accumulated credits subject to conditions. The pre-requisite for claiming the refund of input tax credits for supplier is execution of letter of undertaking (LUT). Initially, there was need of bank guarantee of upto 15% of tax payable on goods / services expected to be cleared for those who did not fulfill the conditions to execute LUT. However, considering the difficulties, the benefit of LUT has been extended to all exporters including SEZ clearances for exporters with clean track record.

If one were to analyze, Section 16(3) of IGST law requires LUT / bond when supplier opts for refund. However, according to Rule 96A of CGST Rules 2017, LUT/ bond is required for supply of goods or services without payment of GST whether or not refund opted. Rule is overriding the provisions in the act which is generally not accepted in any law.

In terms of Section 16(3) of IGST Act, small suppliers who would not be able to execute LUT for any reasons could explore the option of charging IGST. Such IGST charged needs to be claimed as refund by the suppliers. Supplier may also charge IGST and ask the SEZ unit to claim refund instead if claim of refund is cumbersome for supplier. This option is not clearly envisaged anywhere in law and at the same time, there is no bar either.

SEZs would not be able to procure any goods or services from dealers who have opted for composition scheme. This is because any supplies to SEZ would always be treated as inter-state supply and composition dealers are restricted from making inter-state outward supply. This would put the composition dealers in disadvantage which needs to be addressed.

### ***Exemption only for authorized operations***

For claim of refund towards supplies to SEZ, the supplier has the obligation to prove that the supplies made without GST or with refund option are for authorized operations of SEZ. In service tax, there was a readymade list of approved services for exemption. However, in GST such list is not available. There is no prescribed mechanism to understand what constitutes authorized operations. Department could always question the suppliers for this. Therefore, on a precautionary note, suppliers could request SEZ units to share the list of authorized operations which is issued by Board of Approval at inception of SEZ units. A simple declaration stating that goods / services supplied are for authorized operations could avoid future litigations. Whenever in doubt, suppliers could consider the option of charging GST asking customer to claim refund / credit. Government also needs to provide some clarity on this option as such option is not clearly laid down in law.

### ***Registration issues***

There may be a situation wherein an entity would have both DTA and SEZ units in same campus or same state. Proviso to Rule 8 of CGST Rules 2017 warrants separate registration for DTA and SEZ units in such cases as business verticals. This provision has led to increase in compliance burden as supplies between these distinct persons would be subject to GST even without consideration in terms of Section 7 of CGST / SGST law. In addition to this, all compliance related to return filings, audits, assessments would be separate. Need of LUT would arise for supply of services from a DTA unit to SEZ unit of same entity because of separate registration. Some relaxation could be provided by the government in such cases to make the law more business friendly.

**Conclusion:** GST law being new, lot of practical issues could crop up in initial days as discussed in earlier paragraphs. Assesse should be careful in handling the transactions for which professionals like chartered accountants, advocates or cost accountants could be consulted. Otherwise, due to inadvertent errors assessee could land up in litigations with heavy penalty and waste of time.

Suggestions or feedback can be sent on [madhukar@hiregange.com](mailto:madhukar@hiregange.com) or [mahadev@hiregange.com](mailto:mahadev@hiregange.com).