Whitepaper: GIFT City - International Financial Services Centre – Fiscal Incentives

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Whitepaper

GIFT City - International Financial Services Centre – Fiscal Incentives

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1.0 BACKGROUND

1.1 The Gujarat International Finance Tec-City ("GIFT City") is developed as a planned global financial and IT Services hub. It is a first of its kind in India, designed to be at par or above the globally benchmarked financial centres.

1.2 GIFT City's Master Plan facilitates Multi Services Special Economic Zone ("SEZ") with International Financial Services Centre ("IFSC") status, Domestic Finance Centre and the associated social infrastructure.

1.3 GIFT SEZ Limited has been formed by Gujarat International Finance Tec-City Company Limited ("GIFTCL") for the development of Multi Services SEZ at Gandhinagar with the prime focus being the development of IFSC and allied activities in SEZ.

1.4 The core objectives of developing IFSC in GIFT Multi Services SEZ are as under:

- To realize the vision of the Government of India ("GoI") to emerge as a major economic power by facilitating development of strong base of IFSC in the country.
- Facilitate the implementation of the Government's strategy for the development of a financial hub in the South Asian sub-continent.
- Position the IFSC as a world-class zone for the long-term provision of office / service accommodation and high technological, economical and commercial infrastructure.

1.5 The GIFT City is planned on 886 acres of land with 62 mn sq. ft. of built-up Area which includes office spaces, residential apartments, schools, hospitals, hotels, clubs, retail and various recreational facilities.

1.6 GIFT City has two Zones:

- Domestic Tariff Area (DTA) for business related to India operations; and
- Multi-service Special Economic Zone (SEZ) with IFSC

Total area of 261 acres has been demarcated as SEZ and additional 625 acres has been marked as DTA.

2.0 INTERNATIONAL FINANCIAL SERVICES CENTRE (IFSC)

2.1 IFSCs have been envisioned by the GoI as a special economic zone and a financial centre located within India for providing various financial services to resident and non-resident participants in foreign currency (i.e. other than Indian Rupee).

2.2 GIFT City is the first and only IFSC currently operational in India and was operationalised by the GoI in 2015.

2.3 The IFSC in GIFT City ("GIFT IFSC") seeks to bring back those financial services transactions that are currently carried on outside India by overseas financial institutions and overseas branches/ subsidiaries of Indian financial institutions to the Indian shores.

2.4 GIFT IFSC is intended to provide very competitive cost of operations with very competitive tax regime, single window clearance, relax company law provisions, international arbitration centre with overall facilitation of doing business.

2.5 **Sectors allowed in IFSC:**

The financial institutions defined under the IFSC Authority Act are allowed to setup a unit in the IFSC. The financial institution is defined to mean a unit set up in an IFSC and which is engaged in rendering financial services in respect of any financial product. The list of financial product and services have been provided in the IFSC Authority Act and circulars issued therein. The following key sectors / services are permitted to set up an IFSC unit:

Banking Sector	Insurance Sector	Capital Market	Others
➢ Indian banks ➢ Foreign banks	➢ Indian Insurer ➢ Indian Reinsurer ➢ Indian Broker ➢ Foreign Insurer ➢ Foreign Reinsurer	➢ Stock Exchanges/ Commodity Exchanges ➢ Clearing Corporation ➢ Depository ➢ Stockbrokers, Trading members ➢ Investment Adviser ➢ Portfolio Management services provider ➢ Alternate Investment Fund (AIF) ➢ Mutual Fund ➢ Trustee Companies ➢ Any other intermediary permitted	➢ Aircraft lessors ➢ IT & ITeS ➢ Global in-House Centres ➢ Institution dealing in bullion products ➢ Other services business

3.0 FOREIGN EXCHANGE MANAGEMENT ACT, 1999

3.1 The RBI vide ***Notification dated 2 March 2015*** issued the Foreign Exchange Management (International Financial Services Centre) Regulations, 2015.

3.2 As per the said regulations, any financial institution or branch of a financial institution set up in the IFSC and permitted / recognised as such by the GoI or a Regulatory Authority shall be treated as a person resident outside India. Further, the said regulation gives powers to the Regulatory Authority to determine the activities that can be done by the financial institution or branch of a financial institution set up in IFSC.

3.3 In exercise of the powers, the IFSCA has given various directions / instructions. A few important ones are highlighted below:

- All transactions in IFSCs shall be undertaken in a freely convertible foreign currency and only via bank transfers.

- A financial institution may undertake any capital account transactions permissible under FEMA, excluding acceptance of deposits, with a person resident in India or a person resident outside India or another financial institution in any freely convertible foreign currency.

- A financial institution may undertake current account transactions permissible under FEMA with a person resident in India or with a person resident outside India or with other financial institution in any freely convertible foreign currency.

3.4 New overseas investment rules announced recently also provide for overseas investment by a person resident in India in an IFSC:

- Overseas Investment Rules, 2022 has been extended to include investment in entities located in IFSC by a person resident in India, being an Indian entity or a resident individual, thereby extending the scope of overseas investment to promote investments in IFSC.

- A person resident in India can make Overseas Investment in an entity set up in IFSC as ODI or may make contribution to an investment fund or vehicle set up in an IFSC as OPI subject to conditions specified in rules.

- A recognised stock exchange in the IFSC is treated as a recognised stock exchange outside India for the purpose of these rules.

- Further, the new overseas investment rules / regulations shall not be applicable to any investment made outside India by a financial institution in an IFSC.

4.0 CERTAIN DEVELOPMENTS IN GIFT CITY

4.1 Introduction of International Financial Services Centre Authority

To counter the problem of getting a nod from multiple financial services regulators like the Reserve Bank of India (RBI), Securities & Exchange Board of India (SEBI), Insurance Regulatory Development Authority of India (IRDAI), Pension Fund Regulatory Development Authority of India (PFRDAI) in the IFSC, a unified regulator called the International Financial Services Centre Authority ("IFSCA") was established on 27 April 2020 under the International Financial Services Centres Authority Act, 2019 and is headquartered at GIFT City, Gandhinagar in Gujarat.

The regulatory powers of all above 4 financial services regulators have been vested in IFSCA with respect to regulation of financial institutions, financial services and financial products in the IFSC, making it a unified regulator for the IFSC.

As the dynamic nature of business in the IFSCs requires a high degree of inter-regulatory coordination within the financial sector, the IFSCA has been established as a unified regulator with a holistic vision in order to promote ease of doing business in IFSC and provide world class regulatory environment. It is expected to facilitate a single window clearance.

4.2 Tax incentives to the Units in GIFT CITY and the investors

A host of measures like tax treatment of alternative investment funds, aircraft leasing, steps to encourage foreign offshore funds to relocate to India and setting up of a fintech hub to facilitate provision of services like banking and broking are further aimed at attracting investor interest.

5.0 MINIMUM OWNED FUND REQUIREMENTS

5.1 IFSC Banking Unit (IBU)

The Parent bank shall provide necessary capital for the IBU, subject to a minimum of USD 20 million or such other level of capital that may be specified by the Authority. Such capital shall be maintained at the Parent Bank in the manner as specified by the Authority.

5.2 Net owned fund requirements for the Finance Company/ Finance Unit (other than offshore banking units) is as follows:

Specified Activities undertaken by Finance Company/Unit	Net-Owned Fund required
Entity undertaking one or more non-core activities[1] only without any core activity(ies)	Higher of USD 0.2 million or any such amount as may be required to seek specific registration for a proposed non-core activity under the respective Framework/ Regulation for that particular activity.

Entity undertaking one or more core activities[2] with or without non-core activities, except for Global/Regional Corporate Treasury Centres.	Higher of USD 3 million, minimum regulatory capital for core activities as specified by the Authority; or any such amount as may be required for a non-core activity(ies) under the respective Framework/Regulation for that particular activity
Entity undertaking activities of Global/ Regional Corporate Treasury Centres.	Higher of USD 0.2 million or any such amount as may be required under the relevant regulatory framework specified by the Authority.

[1] Permitted Non-Core Activities for Finance Company/ Finance Unit:

- Merchant Banking
- Authorised person
- Registrar and Share transfer agent
- Trusteeship services
- Investment Advisory services
- Portfolio Management services
- Operating lease of any products, including aircraft lease, ship lease or any other equipment as may be specified by the Authority from time to time
- International Trade Financing Services Platform
- Distribution of Financial Products (including Mutual Funds/ Insurance Products)
- Function as trading and clearing members or professional clearing member of
- exchanges and clearing corporations set up in IFSCs
- Asset Management support services permitted under the Framework for Enabling Ancillary Services as specified by the Authority
- Undertaking to act as facilitators of permissible activities as and when permitted by the Authority

[2] Permitted Core Activities for Finance Company/ Finance Unit:

- Lending in form of loans, commitments, guarantees, securitisation and sale and purchase of portfolios
- Factoring and forfaiting of receivables
- Investments including subscribing, acquiring, holding or transferring securities
- Buying or selling derivatives
- Global/ Regional Corporate Treasury Centres

Similar net worth requirements are specified for other categories of businesses in IFSC. The IFSCA has issued various regulations sector wise for eg. Finance Company, Banking, Fund Management, Insurance Intermediary, etc.

6.0 OPPORTUNITIES / BENEFITS PRESENTED BY GIFT CITY

Key Benefits for entity setting up operations in IFSC

- State-of-the-art infrastructure at par with other global financial centres
- Fiscal incentives in the form of Tax exemptions and concessions — For Instance, Liberal tax regime for 10 years, state subsidies, etc. (*discussed in detail below*)
- Lower operating costs
- International dispute resolution mechanism through Singapore International Arbitration Centre
- Robust regulatory and legal environment
- Integrated ecosystem of banks, insurance, capital markets, law firms and consultancy firms
- A wholly transparent operating environment, complying with global best practices and internationally accepted laws and regulatory processes
- Availability of skilled professionals

Tax Incentives for units in IFSC

A) Income Tax

6.1 Tax holiday for 10 consecutive years out of block of 15 years in respect of income from business carried on in IFSC.

- From the year in which permission under section 23(1)(a) of the Banking Regulation Act, 1949 or permission or registration under the Securities and Exchange Board of India Act, 1992 or permission or registration under the International Financial Services Centres Authority Act, 2019 was obtained.

- CA Certificate in Form 10CCF certifying amount of deduction under this section is obtained for each such year.

6.2 Lower rate of Minimum Alternate Tax (MAT) / Alternate Minimum Tax (AMT) at 9% (Such concessional rate of 9% would not applicable to companies in IFSC opting for new tax regime).

6.3 Pass through status given to any income received by a Category I or II AIF which is regulated under the IFSC Authority Act, 2019.

B) GST

6.4 No GST on services:
(a) received by a unit in IFSC; and
(b) provided by IFSC units to offshore clients.

Tax Incentives for investors investing in IFSC units

A) Income Tax

6.5 No tax on interest paid by IFSC units to non-residents.

6.6 Lower rate of tax deduction at 4% on interest paid to non-resident on Long-term Bonds and Rupee-denominated bonds listed on a recognised stock exchange located in any IFSC.

6.7 No tax on capital gains on transfer of specified securities* listed on IFSC exchanges by a non-resident or by a category III AIF located in IFSC
**Specified securities include Bond, GDR, Foreign currency denominated bond, Rupee-denominated bond of an Indian company, Derivatives, Unit of a Mutual Fund, Unit of a business trust, Unit of Alternative Investment Fund and Foreign currency denominated equity share of a company*

6.8 No tax on income of non-resident by way of transfer of non-deliverable forward contracts or offshore derivative instruments or over-the-counter derivatives entered with offshore banking unit of an IFSC subject to fulfilment of below conditions:

- Non-deliverable forward contract entered into by non-resident with a unit holding valid certificate of registration; and

- Such contract is not entered by the non-resident through or on behalf of its permanent establishment in India.

6.9 No tax on any income received by a non-resident from portfolio of securities or financial products or funds, managed or administered by any portfolio manager on behalf of such non-resident, in an account maintained with an Offshore Banking Unit in any International Financial Services Centre to the extent it does not accrue or arise in India or is not deemed to accrue or arise in India.

6.10 No tax on Income by way of royalty or interest, on account of the lease of an aircraft which is paid by an IFSC to non-resident.

6.11 Concessional tax rates on incomes of Category III AIF located in IFSC:

- No capital gains tax on transfer of specified securities (other than shares in a company resident in India).
- Income received in respect of securities at the rate of 10%. This rate applies only to the extent of income that is attributable to units held by non-residents (not being permanent establishment of the non-resident in India) and calculated in the prescribed manner.
- Short term capital gain on transfer of securities (other than referred in section 111A i.e. STT paid where the rate of 15% will apply) at the rate of 30%.
- Long term capital gain on transfer of securities (other than referred in section 112A) at the rate of 10%.
- Provisions of alternate minimum tax shall not apply to Specified AIFs established in the form of

a trust or a limited liability partnership.

6.12 Eligible Foreign Investors not required to obtain PAN or file return of income, subject to fulfilment of below conditions:-

- Does not have any other income from India or IFSC other than income from transfer of specified capital asset;
- Consideration on transfer of such capital asset is paid or payable in foreign currency; and
- The eligible foreign investor furnishes specified details and documents to the stock broker through whom the transaction is made.

"Eligible foreign investor" means a non-resident who operates in accordance with the SEBI, Circular IMD/HO/FPIC/CIR/P/2017/003 dated 4th January 2017. This circular provides the guidelines for participation / functioning of Eligible Foreign Investors and FPIs in IFSC.

Relaxations under Companies Act

6.13 The Ministry of Corporate Affairs has issued 2 notifications dated 4 January 2017 wherein it has provided various exceptions / modifications / adaptations for both public companies and private companies. Few of the important relaxations are provided below.

- Flexibility to choose the financial year same as that of foreign parent company.
- Convening Extra Ordinary General Meeting by IFSC at any place within or outside India.
- No compulsory rotation of statutory auditors.
- Non applicability of secretarial standards prescribed by the Institute of Company Secretaries of India.
- IFSC firms can make investments through more than two investment companies.
- Regulatory requirement is to hold minimum two board meetings annually.
- Non-applicability of CSR for a period of five years from commencement of business.

Other Incentives

6.14 No Security Transaction Tax (STT), Commodity Transaction Tax (CTT), Stamp Duty in respect of transactions carried out on IFSC exchanges.

Tax Incentives for units in GIFT CITY other than IFSC units

A) Income Tax

6.15 100% tax holiday for 5 consecutive years and 50% tax concession for next 5 consecutive years in respect of income from **business of offshore banking unit i**n a SEZ or from the business referred to in section 6(1) of Banking Regulation Act, 1949 with an undertaking in SEZ/ undertaking develops, operates and maintains SEZ. (Section 80LA)

- From the year in which permission under section 23(1)(a) of the Banking Regulation Act, 1949 or permission or registration under the Securities and Exchange Board of India Act, 1992 or any other relevant law was obtained.

- CA Certificate in Form 10CCF certifying amount of deduction under this section is obtained for each such year.

B) Goods and Service Tax (GST)

6.16 Supplies to SEZ are Zero Rated under IGST Act, 2017

6.17 No GST on services:
(a) received by a unit in SEZ; and
(b) provided by SEZ units to offshore clients.

C) Other Tax benefits

6.18 Duty free import / domestic procurement of goods for development, operation and maintenance of SEZ units.

6.19 Exemption from customs duty for all goods imported in the SEZ used for authorized operations.

6.20 Supply of goods or services from Domestic Tariff Area (DTA) to a unit located in SEZ is regarded as a zero-rated supply (irrespective of the currency in which payment is being made).

6.21 Goods and Services supplied to SEZ regarded as export for customs purpose.

State Subsidies to GIFT City units:

6.22 100% reimbursements of Stamp duty and registration fee.

6.23 100% reimbursements of electricity duty and Re. 1 subsidy on power tariff for a period of 5 years.

6.24 100% of employer contribution of provident fund subsidies in case of female employees.

6.25 75% of employer contribution of provident fund subsidies in case of male employees.

6.26 Lease rental subsidy for every 50 sq. ft. per employee depending on the number of employees.

6.27 Capital subsidy @ 25% of capital expenditure for one-time purchase of Computers, networking and related hardware, subject to a ceiling of Rs. 1 crore.

7.0 CHALLENGES / ISSUES FACED

7.1 Work in Progress for Nearly a Decade

Construction started in 2012, with the idea of having more than a thousand skyscrapers and a million jobs. 10 years since the foundation stone was laid down, the campus is still a work in progress. However, there has been a lot of progress in building up the infrastructure in last two years and a lot of financial institutions have opened their offices in the GIFT City.

7.2 Regulatory Restrictions

Some of the rules and regulations introduced in GIFT City must be measured for efficiency and ease of work against international financial jurisdictions such as the Cayman Islands, Mauritius, Singapore, Luxembourg, etc. Though lot of measures have been taken to liberalise the regulations, formation of IFSCA for single window clearance, etc. Even after these measures the GIFT City has not been upto the mark to attract huge investments. Therefore, these measures need to be relooked and further liberalisation should be considered to match up with the standards of international financial jurisdictions.

7.3 Additional SEZ Approvals

The SEZ Act is applicable to GIFT City. A separate approval from the Development Commissioner SEZ is required for setting up a unit in GIFT City. This approval is required in addition to the general approval required from the IFSCA.

7.4 AIF incorporated in GIFT City may also require an FPI approval for investing in Indian stocks and bonds. This again leads to an additional approval requirement.

8.0 OUR COMMENTS

As discussed above in brief, there are various fiscal incentives and regulatory relaxations offered to the units set-up in GIFT City / GIFT IFSC. The GoI is making all the efforts and taking necessary steps to ensure the ease of doing business and making GIFT CITY an international financial hub which supports various international financial transactions and helps in a big way in bringing an economic reform in India. Many positive initiatives in the right direction have already been taken and now it is a fact that a lot of Indian and foreign financial institutions have already set up their units in GIFT CITY.

Though there are still some minor challenges like multiple approvals from SEZ authority as well as IFSC Authority, even after registering a unit in IFSC an AIF will be required to register as an FPI to invest in Indian capital markets, etc. However, there may not be any major hurdles and the units already registered and operating from GIFT CITY have started enjoying the benefits provided by the GoI and more such units have already filed for registering in the GIFT City.

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