Business Standard

Kick-start likely for finance SEZs in Budget

Finance ministry, regulators to draft regulations based on NIPFP note

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The Union Budget for 2015-16 is likely to kick-start finance special economic zones (SEZs), the first of which is to come up in the Gujarat International Finance Tec-City (GIFT) in Ahmedabad. With only 10 days remaining for the Budget to be presented in Parliament, the finance ministry has sought public comments on far-reaching recommendations, such as tax breaks and lenient regulations for financial firms in these SEZs, made by the National Institute of Public Finance and Policy (NIPFP).

The work on drafting regulations for finance SEZs has already started with consultation with regulators including Securities and Exchange Board of India (Sebi), Reserve Bank of India (RBI) and Forward Markets Commission (FMC).

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LEG-UP FOR FINANCE

National Institute of Public Finance and Policy committee's recommendations for finance SEZs

- Give finance firms in these SEZs tax breaks
- Exempt them from securities transaction tax, commodities transaction tax and service tax
- Set up a separate arbitration system, for dispute resolution with expertise to solve contractual disputes
- Review trade regulations between finance SEZs and mainland
- Make contracts in these zones free from capital control
- Allow complete capital account convertibility in these zones

"To draft the final regulations for financial SEZs, the finance ministry-commissioned concept note would be taken into consideration after feedback from the stakeholders," said a person close to the development.

The ministry posted the NIPFP concept note on Tuesday evening.

In the note, submitted to the ministry on February 6, the think tank recommended full capital convertibility for the rupee and tax breaks for financial firms that set up offices in these zones.

"Free trade zones like Kandla or Seepz (Santacruz Electronics Export Processing Zone) played a role in improving India's engagement with globalisation at a time when there were many restrictions on the current account. There is a possibility that finance SEZs could play a similar role in improving India's engagement with globalisation," said Ajay Shah, member of NIPFP.

So far, regulators of equity, commodities, bond and currency derivative markets have had two consultations to draft regulations for Ahmedabad's GIFT. Foreign banks, stock exchanges and investment managers also took part in these consultations.

Sources indicated firms in these zones could be allowed to set up international exchanges for trading in equities and currencies, and bullion or commodity exchanges; engage in brokerage, investment management, merchant banking, custodian services; and establish clearing and settlement facilities.

The NIPFP report recommends only foreign banks be allowed to set up branches in these zones, not new banks.

"It is difficult to have [domestic] banks in finance SEZs as these would not have access to lender of last resort facilities from RBI," said the concept note.

The note lists three key enablers - law and regulation, dispute resolution, and capital control issues. Regulators are working on a tax structure for financial transactions comparable to international finance centres. These would require doing away with securities transaction tax (STT) and commodities transaction tax (CTT) in these zones.

"Regulations should be principle-based and should be consistent," another source said.

Finance SEZs would help both Indian and foreign companies raise funds. Laws for these, including for litigation, would be separate from those outside these zones. The recommendation is to exempt these from foreign exchange controls. The report also suggests a separate regulator for these.

NIPFP has suggested regulations for finance SEZs be based on the Indian Financial Code (IFC) as suggested by the Financial Sector Legislative Reforms Commission (FSLRC), on a pilot basis. As IFC is yet to be prepared, the committee has recommended enacting a finance SEZ Act.

"The components out of the overall IFC relevant to finance SEZs are: micro-prudential regulation, resolution and trading. This will require implementation work by the Ministry of Finance in setting up a specialised regulator for finance SEZs which will enforce the finance SEZ Act, setting up a bench of the Financial Sector Appellate Tribunal (FSAT) and setting up operations of the Financial Data Management Centre (FDMC)," the report said.

The committee has urged the finance ministry to expand the terms of reference for the task forces on FSAT and FDMC, so that they can have a provision for finance SEZs, too.

Financial services are considered the next driver of economic growth. Even though India has not been able to tap the sector fully because of inadequate norms, advance estimates suggest growth in these services to jump to 13.7 per cent in 2014-15 - the highest among all services - from 7.9 per cent in the previous year.