

Dawn of the EOU Scheme



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"The evening sings in a voice of amber, the dawn is surely coming."

- Al Stewart

(Famous Scottish Singer- Songwriter)

1. In 1980-81, the Export Oriented Unit ("EOU") scheme was introduced in India. This scheme was introduced with the objective of *inter alia* promoting exports from India, earning precious foreign exchange for India and attracting foreign investments into India. This scheme necessitated the registering units (EOUs) to export majority of its finished products outside India. Option was also provided to such units to supply certain quantity of its finished products in India [or domestic tariff area (DTA)]. However, on an overall basis, such EOUs were required to be positive net foreign exchange (NFE) earner for India.

2. For enticing more and more units to setup and operate as an EOU, a host of benefits were provided to such units which *inter alia* included income tax benefits, exemption from payment of customs duty on import of inputs (including consumables) and capital goods, exemption from central excise duty on domestic procurement of inputs and capital goods, speedy clearances, freedom and flexibility to open and operate unit anywhere in India.

3. On its introduction, we saw several units, which were primarily engaged in export of goods outside India, registering themselves as an EOU. However, lately we are seeing that the charm of the EOU scheme has withered away, and a lot of units have either already de-registered themselves from the scheme or are in the process of de-registering. At the same time, even new units are not very keen on operating as an EOU. This article seeks to highlight few reasons which can be attributed to such rampant de-registration of EOUs in India and loss of interest in this scheme.

Withdrawal of Income Tax Benefit

4. One of the major charms of the EOU scheme, right from the start, was the income tax benefit / exemption granted to the EOUs. In this, no income tax was payable on profits derived / earned by an EOU for ten consecutive assessments (or years) under Section 10B of the Income Tax Act, 1961.

5. However, section [10B](#) of the Income Tax Act itself provided a sunset clause i.e., the benefit was slated to come to an end in April 1, 2010. However, the deadline was first extended to April 1, 2011 and then to April 1, 2012. No extension was however granted for period beyond April 1, 2012. Thus, this income tax benefit for EOUs came to an end from April 1, 2012.

6. The withdrawal of this benefit itself led to a number of units to de-bonding / de-registration from the EOU scheme.

No SEIS Benefit

7. In the year 2015, the then existing Foreign Trade Policy, 2009-14 was revised and a new Foreign Trade Policy, 2015-20 (**FTP**) was introduced. In this new policy, the benefit of Services Export from India (**SEIS**) scheme was introduced. This SEIS scheme provided the benefit of duty credit scrips, equivalent to certain specified percentage of FOB value of export, on export of services outside India. These duty credit scrips are capable of being used for payment of basic customs duty (BCD) on import, equal to its face value, and are freely transferable.

8. This benefit however is not available in respect of export of services outside India by an EOU. On the other-hand, this benefit is available in respect of export of services made by a non-EOU / DTA unit. Thus, this scheme was directly disadvantageous to all units registered and exporting services as an EOU.

9. Such non-availability of the SEIS benefit on export of services outside India, when such benefit is being made available to other units in India, is also one strong reason for many units to de-register themselves from the EOU scheme.

No RODTEP benefit

10. Similar to the SEIS benefit, for export of goods, the FTP, 2015-20 had notified the Merchandise Exports from India Scheme (MEIS). This scheme provided the exporter a certain percentage of FOB value of export as transferable duty credit scrips, which could be used for discharge of customs duty (BCD) liability at the time of import. Due to certain objections at the WTO level, this scheme was replaced with a new but similar Remission of Duties and Taxes on Exported Products ("**RODTEP**") Scheme from January, 2021 onwards.

11. This new RODTEP scheme also provides the exporter transferable duty credit scrips on export of goods outside India, as a certain percentage of FOB value of exports. However, to ensure compliance with India's WTO commitments, in RODTEP the principle to calculate the benefit to be made available to an exporter has been changed, as compared to the underlying principle of the earlier MEIS scheme.

12. EOUs were eligible to avail the benefit of duty credit scrips under the earlier MEIS scheme, however in the new RODTEP scheme the benefit is not available to an EOU. All non-EOU / DTA units are eligible to avail this benefit of RODTEP scheme, however EOUs have been dis-allowed this benefit. This is clearly disadvantageous to all units operating as an EOU, and therefore many are de-registering themselves as an EOU.

GST Regime

13. In the new GST regime, the EOUs are facing a lot of technical and legal issues, of which there is no resolution in sight. A lot of ambiguities have crept in, requiring immediate attention of the lawmakers. Few such challenges and ambiguities have been briefly highlighted below:

- a. Prior to the GST regime, on domestic procurement of the inputs and capital goods, outright exemption from payment of central excise duty was available to the EOUs. However, in the GST regime, the benefit of outright exemption from payment of GST on domestic procurement is not available. In the GST regime, the exemption has been made available in form of refund i.e., the supplier to an EOU is required to pay applicable GST and later refund of the same can be obtained (either by the EOU or the supplier) as such supplier qualifies as 'deemed exports' benefit. Such exemption in form of refund has its own disadvantages which broadly entails working capital blockage, increased compliance cost for applying and obtaining such refund and the entire process is time-consuming.
- b. Under the GST regime, on DTA clearance of goods by an EOU, the BCD benefit availed by such EOU on inputs used in the manufacture of finished products cleared in DTA, will have to be surrendered at the time of such DTA clearance. However, no clarity has been given as to the fact that whether this amount will have to be paid along with interest or no interest is payable on this

amount. The language employed in the notification is ambiguous, one part of the notification seems to suggest no interest is payable and another part seems to suggest that interest is payable. Practically, no EOUs as of today are paying any interest on such BCD payment due to lack of clarity. However, most of them are aware that this may turn out of be another cause of litigation between them and the department.

New and Better Customs Warehousing Scheme

14. Recently, the Manufacture and Other Operations in Warehouse (No. 2) Regulations, 2019 ("**Warehouse Manufacturing Regulations**") have been issued which allows a unit to convert any existing premises / new premises into a private customs bonded warehouse, on taking necessary approvals from the customs authorities.

15. All imports into this warehouse are allowed duty free by way of filing a warehousing bill of entry i.e., no customs duty is payable on import of inputs, capital goods and consumables. Using such duty-free items, the unit can manufacture finished goods, which may either be exported outside India or can be supplied in the DTA. No customs duty is payable in case of export of such finished goods outside India; however for finished goods supplied in the DTA, the unit / warehouse is required to pay the customs duties saved on inputs used in the manufacture of such finished goods (without any interest).

16. Therefore, this warehousing scheme offers the same benefit of duty-free imports as are available to an EOU. However, this scheme is better than the existing EOU scheme on the following counts:

- a. As a warehouse there is only one customs authority to deal with; however, as an EOU there are two authorities – customs authority and Development Commissioner (FTP) to deal with (apart from other common authorities such as the GST authority);
- b. As opposed to the EOU scheme, in case of the above warehousing scheme, there is no requirement to be a net positive foreign exchange (NFE) earner;
- c. In case of the above warehousing scheme, as opposed to the EOU scheme, there is clarity that on DTA sale there is no requirement to pay interest on the customs duty to be surrendered on inputs used therein.
- d. In case of the EOU scheme, renewal of licence to operate as an EOU is required every five years. However, in case of the above warehousing scheme, there is no need for any sort of periodic renewal. The licence is valid until the same is either surrendered by the unit or cancelled by the customs authority.

17. The above factors are seemly the few major reasons leading to the recent de-registrations of a number of EOUs and many which are in the pipeline. The Government should either offer new incentives or atleast extend the above few discontinued incentives to the EOUs, to make this scheme more palatable to the existing units and for new units who are considered setting-up and operating as an EOU. Without any positive steps towards this, the EOU scheme is showing all signs of being a minute away for being declared dead.

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