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# *Law of foreign investment and its impact on Indian labour*

Thesis submitted to the Saurashtra University,
Rajkot
For Ph.D. Degree
In Law

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June 2005

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*Dedicated to my father*

*Shri Beniprasad Chaturvedi*

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# Certificate

I, the undersigned, hereby certify that the thesis presented by me represents my original work, which was carried out by me under the guidance and supervision of Dr. B.G. Maniar during the period from 2002 to 2005.

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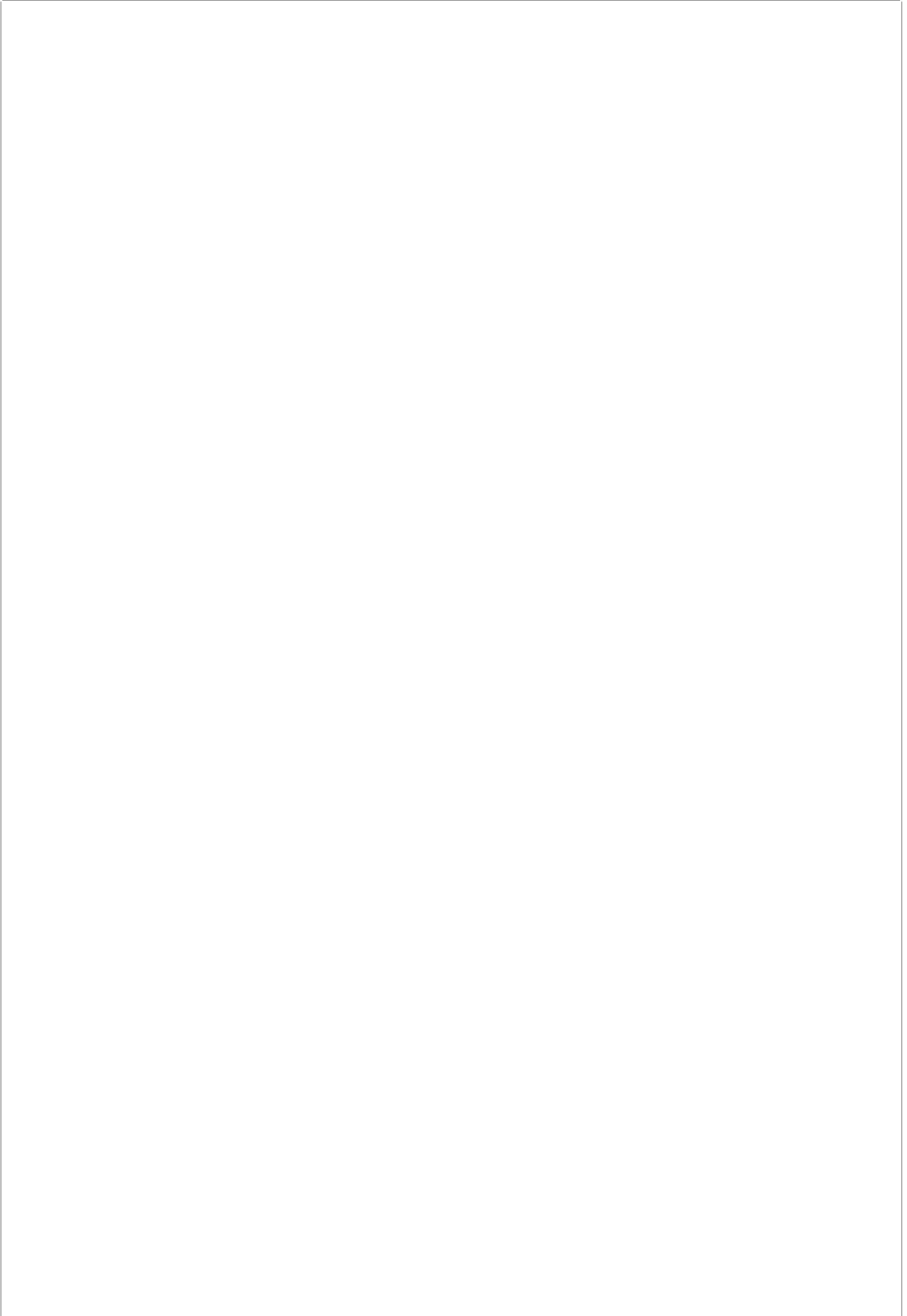

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# CHAPTER 1

# *Foreign Investment*

## 1.1 Historical Perspective

### *1.1.1 British Period*

India was one of the richest countries of the world before the arrival of British. It was regarded, and rightly so, as "Golden Sparrow". The village community of India was self-sufficient. Agriculture was the mainstay of the economy but industry also contributed to a large extent to the economy. Handicrafts, handloom and all other human artistic industries were well developed and which absorbed a large part of the labour force. The internal means of rapid transportation were not yet developed. The land routes and river navigation were used for internal trade and transportation of goods.

The methods of cultivation were ancient and based on experience of centuries, but still due to high fertility of the land, productivity was high. India was home to some of the world's famous crops such as indigo, basmati rice, spices such as cardamom, chilly, etc.

The use of money in the economy was not very wide. Transactions were based on mutual faith and goodwill. Small industries were allied with

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agriculture. Though not very modern, Indian economy was balanced and perfectly so. By the end of 18th century India carved out for itself a high position among the top industrial countries of the world.

The Europeans were attracted by the possibilities of trade in Indian spices. They landed in India primarily for trade. They aimed at making quick profits by selling Indian goods in the European markets. The East India Company set up in 1600 in Britain, came to India for trade but gradually began to dabble into politics. It first acquired the monopoly rights for trade. Later it defeated the Nawab of Bengal in the Battle of Plassey in 1757 and established British rule in India. It set up the first port at Surat followed by similar forts at Hoogly, Mumbai, and Kolkata. With the establishment of forts, the Company acquired political power and patronage. In 1765 the Company acquired the right to collect revenue in Bengal, Bihar and Orissa regions. The Company gradually annexed many territories through persuasion, temptations and deceit.

The following paragraphs describe in brief the economic operations of the East India Company and later British rule and their implications on the Indian Economy.

The East India Company had acquired a license from the Moghul Emperor in 1716, which

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exempted it from paying custom duties on all its imports and exports of goods. As the company's position became strong after 1757, the top officials of the company began to engage themselves in private trade and earned huge profits out of trading operations. The Indian traders suffered huge loses and the customs revenue declined significantly. The Company almost monopolized internal trade through its political power. Indian goods were taxed at several places within the same province. The imported British textiles were taxed at 2.5% *ad valorem*, whereas Indian textiles were subjected to a tax of 15%. Such a discriminatory tax policy harmed the internal trade of India. The age-old handicrafts were destroyed on account of the discriminatory foreign trade policy of the East India Company. Some of them actually got their thumbs severed. The British traders acquired virtual monopoly in Indian markets. The ancient Indian industries were ruined. The nature of foreign trade changed substantially. Industries had a secondary role now compared to agriculture in foreign trade. India became a predominantly agricultural country.

The period between 1757-93 is regarded as the "Plunder of Plassey" in the economic history of India. "The employees of East India Company plundered India's wealth through misuse of political power rather than through genuine trading activities. Among methods used were, exorbitant land revenue and commodity tax, annexation of princely states, monopolizing trade

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of indigo and opium, among others. Since the Company monopolized external as well as internal trade, the wages of artisans were kept at 15-20% lower than acceptable or even sustainable rates. The Indian craftsmen and artisans were forced to sell their products only to the company. The defaulters were punished heavily. When the Company rule ended in 1858, the shareholders of the Company were paid double compensation and the entire burden was borne by the people of India.

The exploitative policies of the Company were continued by the British Government in the name of "Home Charges". These Home Charges included the following:

1. Interest payments on capital borrowed from England,

2. Interest on capital invested in Indian railways,

3. The pension payments to the British officials who served in India and the salaries and perquisites of the British Government,

4. Expenses for the maintenance the Office of the Secretary of State for India and the Office of the Viceroy of India,

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5. Expenses of Indian Army and Navy,

6. The amount of compensation paid by the British Government to the East India Company.

The Home Charges in the year 1898-99 amounted to £16,300,000 and reached a level of £30,000,000 in the year 1924-25. Thus, the flow of wealth continued in one direction bleeding Indian Economy to death.

### *1.1.2 Various parameters*

A. Agricultural Sector:

The ruinous policies of the Company and subsequently of the British Government broke the backbone of Indian prosperity - the self-reliance of villages. The land revenue rates were very high and the revenue policy was exploitative.

The farmers were exploited beyond their endurance. There were different kinds of land settlement systems during 1760 to 1833. The effective tax on land varied from 60 to 100% of the produce of land. The tax was collected by the princely states or by the landlords. After 1850 a large proportion of Indian population turned to agriculture for their livelihood on account of steep decline in the importance of handicraft and their inability to

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provide employment. In short the proportion of population dependent on agriculture rose from 61.1% in 1891 to 73% in 1921. Consequently the per capita availability of land declined from 1.03 acres in 1901 to 0.94 acres in 1941. The peasants became debtors and land ownership pattern changed in the favour of moneylenders. The number of tenants as well as landless labourers increased in all the years of British rule.

All these factors gave a deadly blow to the agricultural productivity in general and the rural population was trapped into a vicious cycle of poverty.

B. Industrial Sector:

India was one of the industrially advanced and self-sufficient countries of the world at the arrival of the British. It had attained noteworthy progress in industry and trade by the end of $18^{th}$ century. But the economic policies of the British ruined the balanced and prospered economy of India. The cotton textile industry was the most important single industry among the Indian industries. The expertise of Indian cloth weavers was world famous. The fine muslin of Dhaka was an excellent example of it. It took six months for a weaver to prepare a piece of muslin 20 yards in length and 36 inches in width. The piece was so delicate that one could pass it

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through a golden ring. Similarly, thin cotton cloth of Chanderi and Kota, the delicate Dhoti of Ahmedabad, the dupatta and the woollens of Punjab and the Kashmiri shawl were well known in the world markets. The silk thread and Jhari cloth industry was well developed in Surat, Tanjore, Trichy, and Varanasi. Nasik, Pune, Hyderabad and Madura were famous for brassware and pieces of art. The shipbuilding industry had developed in ports like Vasai, Goa, Surat and Chittagong.

The plantation industry was a forerunner of different kinds of industrialization in India. The plantations include mainly tea, coffee, rubber and indigo. With the end of monopoly of the East India Company in 1833, the foreign capital began to flow into plantations. The British used their capital and entrepreneurial talents in the new industry and earned huge profits. The poor, helpless Indian labourers had to toil and moil in these industries and yet they received deplorable wages. Their economic condition was pitiable.

Thus, during the British rule the economic progress was in the backward direction mainly on account of scarcity of capital, inadequate banking and other allied services, low productivity of labour, lack of education and training, absence of enterprising entrepreneurs, discriminatory railway rates

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and tariff policies, and above all highly partisan British Government's policies.

C. Service Sector:

The service sector during the British rule comprised of education, transport, banking, etc. As in every country these economic activities assumed great significance to the Indian economy.

The education sector suffered a major decline during the British rule, as the British government had no major interest in developing integrated education system in India. The number of illiterates was on the rise. The literacy rate as mentioned in the census of 1941 was merely 12%. The British education system was conducive to smooth administration and served no other major objective, either vocational or moral. The schools and colleges were set up only to prepare clerks to assist the administration of the Government. No attempt was made to encourage technology and research. The secondary schools and institutions of higher education were established on the pattern of British education System, but they were left to the care of private managements. The medium of instruction was English and this led to the emergence of a new educated class, which had no regard for the dignity of physical labour. Thus, the education policy of

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the British systematically destroyed the sense of dignity of labour among the educated.

The repercussions of the British education policy are felt even today with nation surfeit with an army of clerks, but is in dire shortage of skilled physical labour.

The lone merit of British rule, as considered by many historians, was the establishment of railways as a cheap and efficient means of transport. The first railway in India was set up in 1853 linking Bombay with Thane, and covering a distance of 22 miles. During the decade 1859-69, the railways were set up and managed by private companies with limited liability. Since the arrangement proved to be costly, it was decided in 1870 that the state should the responsibility of setting up new railways. The government laid down 2710 miles of railway track by 1881. The figure rose to 25000 miles by 1900. By the year 1913-14, the railway mileage rose to 35283 miles. The development of railways led to the growth of external trade and development of certain industries. The adverse effects of famines were partially mitigated. But the railway rates policy was discriminatory. It became hindrance to the overall development of the country. As a matter of fact, the main objective of the development of railways by the British was to assist industries in England and to add to the prosperity of England by

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facilitating export of raw material, import of finished goods and internal transport, and serve as a means for transport for the British officials.

The development of roads was of military importance to the British Government, and therefore roads were constructed with a military patronage. It was only in 1855 that the responsibility of construction and maintenance of roads was transferred to the Central Public Works Department. Before this, only the Grant Trunk Road and the Great Deccan road were two important highways constructed in North India. The length of first grade roads in India in 1858 was only 4690 miles, whereas kachcha roads measured about 24715 miles. The need for construction of roads was felt only after the First World War as the use of motor vehicles and trucks increased significantly. The responsibility of development of new roads was laid at the doors of provincial government in 1919. In the year 1913-14 the length of pakka roads was 50075 miles, which increased to 69976 miles in 1943-44. However, the length of kachcha roads was 157287 miles in 1943-44.

The water transport system was considerably well developed even in the pre-British era. The development of roads and railways in India was unsatisfactory till the middle of 19th century, but the internal water transport

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had acquired great significance for passengers and goods as well as for the movements of army personnel and equipment. With the development of railway, this mode of transport gradually lost its importance. The British Government did not give much importance to the construction of canals as a means of internal water transport. The Ganga, the Godavari, and the Krishna canals were constructed, but these were profitable for the transport of goods only. They were not open for passenger traffic as remunerative passenger traffic was not available. Way back in 1938, the National Planning Committee.

The Indian shipbuilding industry also suffered the fate of other industries. In the ancient times, India had acquired fame as a maritime country. The Indian ships and vessels were used for transporting goods to and fro form Iran as well as Arabian, African, and European countries. Shipping was an important basic industry before the British period, in which it was literally shattered.

The revival of Indian shipping industry can be traced to the setting up of the setting up of the Scindia Steam Navigation Company in 1919. When the modern shipping industry began to develop there were 11 shipping companies with a total tonnage of 1.4 lakhs on the eve of Second World War. The tariff policy of the British Government was the

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major cause for underdevelopment of the shipping industry.

The civil aviation in India started with the setting up of Civil Aviation Department by the British Government in the year 1927. The first services were started between Delhi and Karachi. In 1932 Tatas started air services connecting Allahabad, Kolkata, and Colombo. The Imperial Airways introduced services between London and Karachi soon thereafter. After the end of World War II six new companies apart from Tata Company started their business, as air travel got a boost. However these air services were later nationalised.

Banking business started operations on British lines in the reign of the East India Company itself. The British Agency Houses were acting as Company's bankers in Mumbai and Kolkata initially. The Hindustan Bank was set up in 1770 and two other banks, the Bank of Bengal and the Central Bank of India were established in 1785. The Bank of Bombay was set up in 1840 and the Bank of Madras in 1843. The three Presidency Banks were integrated into one bank, namely the Imperial Bank of India in 1921.

The banking industry was decentralised in India till 1860. The development of banking was rather slow during the period of 1865-

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1900. The Swadeshi movement encouraged setting up of a new banking system in the Western India, Uttar Pradesh and Punjab. There were only 22 banks in 1913. Each of these banks had a paid up capital of Rs. 6 lakhs. The period between 1913 to1924 was, however a decade of banking crisis, as 16 banks went into liquidation during that period. The main factors for the banking crisis included inadequacy of capital, imprudent investments, high interest rates, inexperienced management and speculation. The post-war prosperity gave a boost to the development of banking services in general. The number of scheduled banks increased to 25 in 1920, whereas the number of non-scheduled banks went up to 33. The numbers of scheduled and non-scheduled banks in 1930 were 31 and 54 respectively. The Imperial Bank of India was performing the dual functions of a Commercial and a Central Bank of the country till 1934. As Reserve Bank of India was set up in 1935, the responsibility of developing money market and regulation of credit was entrusted to it. It had the monopoly of currency note issue in the country. After the end of the World War II, the number of banks in the country increased rapidly. The number of scheduled banks and the non-scheduled banks were 59 and 119 respectively in 1939.

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D. Situation of Employment:

The British destroyed the ancient industries of India, which were village centric. This led to the downfall of self-sufficient rural economy of the country. The foreign trade policy gave advantage to factory-made imported goods and thus jeopardised the interests of rural artisans and led to their economic disaster. This created large-scale rural unemployment. Though agriculture became more prominent, it was unable to absorb the entire lot of unemployed artisans. This led to their exodus to cities on a limited scale, and thus it augmented urban unemployment.

E. Per capita income:

Dadabhai Navroji has got the honour of being the first person to estimate the per capita income of India in the year 1869. Lord Curzon made a similar attempt in the year 1901 on the event of presenting the budget of the Government. The aggregate national income and per capita income were Rs.675 crores and Rs.30 respectively. The same in 1911-12 were Rs.539 crores and Rs.28 respectively (according to Prof. Balkrishna). According the Prof. Findlay Shiraz, the

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national income and per capital income of India were Rs. 921 crores and Rs.107 respectively in 1921-22. The same as per the Annual Issue of Eastern Economist were Rs.2094 crores, and Rs.72 respectively in the year 1939-40. As per the prices of 1948-49, the national income and per capita income in 1900-01 were Rs.4923 crores and Rs.215, and that in the year 1939-40 were Rs.8568 crores and Rs.280 respectively.

F. Population:

The census was held for the first time in India in the year 1871. The population of India in the year 1901 was 23.6 crores. It rose to 25.2 crores in 1911. Due to famines and diseases like influenza, the death rate was very high prior to 1921 and thus the population declined to 25.1 crores in that year. It was 31.9 crores in 1941. The population increased by a rate of 14% during the decade 1931-40.

Due to lack of education, joint family system, child marriage system, famines, epidemics, and malnutrition and improper medical health facilities, the birth and death rate both were very high in India in the British period. During the decade 1901-10 the birth rate was 49.2 and the death rate was 42.6, the net increase in the population being 6.6. The

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same in 1911-20 were 48.1 and 48.6 respectively, thus recording a decline of 0.5.

G. Poverty:

Poverty in India was mainly due to political factors. The advent of East India Company, the foundation of British rule, and the corresponding adverse economic policies ruined Indian economy and plunged it into a vicious cycle of poverty. With the decline of handicrafts, agriculture became the main economic activity, which also suffered from exploitative taxes of the Government leading the peasants to miserable life. The farmers became debt-ridden due to excessive land revenue and the moneylenders charged exorbitantly high interest rates. Periodic famines and floods hit their backbones. All these factors compelled many of them to sell their lands to zamindars. There was no security of tenure. The peasants were almost in a state of serfdom. The peasants had to bear the burden of home charges paid to England. The exploitative policy of the British Government was largely responsible for the poverty of Indian peasantry.

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H. System of land ownership:

During the pre-British era the Indian system of land ownership was based on tradition. It was a custom that the Hindu kings collected 1/6$^{th}$ of their produce as rent of land, or revenue. The land revenue system improved during the Moghul period. The changes introduced by Raja Todarmal, the finance minister in Akbar's court are well known. He undertook land surveys, made fresh assessment of land in accordance with land fertility and began to collect 1/3$^{rd}$ of the produce of lands as revenue. The provision was also made for collecting rent in cash. Thus land revenue system was liberal. Though many systems prevailed, the common element among them was that the ownership of land was vested in the state and land revenue was treated as rent for the use of land.

The East India Company changed the liberal policies to those aiming at achieving higher revenues for it. The main systems for land settlement popularised by the British were as follows:

I. Tenancy System:

The British systems of land settlement created ripples in the Indian agriculture.

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Under this system the tenants were classified into two types namely permanent tenants and tenants at will. The permanent were relatively in a better position. Sometimes the land acquired for cultivation by the permanent tenant was given to sub-tenants for cultivation. A new class or sub-tenants came in to existence whose economic condition was extremely poor. Very often 50% of the output had to be surrendered as rent by the tenant and yet he had no security of tenure. The amount of rent was not fixed. The Government therefore forced to enact tenancy reforms so as to improve agriculture and condition of peasants. The Bengal Tenancy Act was passed in Bengal in 1859. Another tenancy law was passed in Bengal in 1885 with a view to regulate rent, stopping evacuation of tenants, providing compensation to the tenants for improvements in land, and putting an end to the serfdom of the tenants. These laws were, however partially successful.

II. Zamindari system:

This system was widely popular in Bengal and other adjoining states. In the zamindari system there was no direct relation between the state and the peasant. The zamindari system was of two types – permanent settlement system and

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temporary settlement system. Under the permanent system, land revenue was settled once and for all. There were no changes. This system was introduced in Bengal, Madras and Banaras. About 30% of land was covered under this system at that time. Land revenue was fixed at a level of 10/11th of the rental income. However there was no provision for the security of the tenure. Under the temporary settlement system, land revenue was collected from the Zamindar. The state could make changes in land revenue rates. This system was prevalent in Bengal and Ayodhya. The changes in land revenue however could be affected over a long perid. At the time of each new assessment, the land revenue rates were raised. As a direct result of this settlement, villages were ruined and a new class of tenants came in to existence.

III. Ryotwari system:

The Ryotwari system was introduced by Sir Thomas Munore and revived by the British rule. Under this system, land revenue was determined on the basis of the type of land, its fertility, availability of rain water, and the prevailing prices

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of the produce on land. As along as the peasant paid land revenue, he was considered the owner of the land. There was no intermediary between the government and the peasant. The land revenue was not increased even when the peasant earned more due to the higher productivity of land through his efforts. It was accepted that the peasant stands to gain from increased input of necessary capital and his own labour. This system was introduced in Madras and Bombay regions in the year 1792.

This system was progressive and it ensured ownership rights and security of tenure to the peasant as long as they continued to pay land revenue. However, this system also had certain defects. The sense of belonging to the community was destroyed. The land revenue was arbitrarily determined and it was increased at the time of each new assessment.

IV. Mahalwari system:

This system was unique in its character. Under this system the entire land of a village belonged to the Mahal. The people of the village were the joint owners of land. Their responsibility of

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payment of revenue was both individual and collective. This system was introduced in 1833 during the period of Lord William Bentick in some villages of Agra, Ayodhya, Punjab, Uttar Pradesh, and Madhya Bharat. Although the land was collective property of the village, the government entered into contract with the farmers individually for the payment of land revenue. The Mukhi or some other leader of the village was made responsible for the payment of land revenue. The Mukhi enjoyed a status similar to Zamindar which cerated a new class of intermediaries.

I. Economic condition of workers

The unjust policies of British Government brought hell for the Indian worker class, whether industrial or agricultural. The high rate of population growth and the decline of handicrafts were responsible for lower per capita availability of cultivable land. The per capita availability of land was 1.03 acres in 1901, which declined to 0.94 acres in 1947. The land revenue rates were unduly high and the collection schedules were tight. The conditions of peasants rapidly deteriorated. As the handicrafts and allied industries were ruined, people turned to agriculture in large numbers thereby increasing pressure on land.

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The number of tenants per thousand peasants increased from 291 to 407 in the decade of 1921-31. The number of landless labourers in 1921 was about 210 lakhs. The landless labourers did not get sufficient work to earn livelihood, nor did the tenants have any security of tenure. The zamindars collected exorbitant rent from the tenants, which ranged from 34 to 75% of the total produce. The tenants and landless labourers had little incentive to improve fertility of land. The entire rural population of India was divided into two classes-zamindars and tenants or landless labourers and the seeds of class conflict were sown which influence Indian politics even today.

The land settlement systems introduced by the British created several problems and caused deterioration of social and economic status of tenants. Attempts were made to improve the situation of tenants through different land tenancy legislations such as the Bengal Tenancy Act, 1859, which improved the situation a little bit. These laws classified tenants into permanent and temporary, and were primarily aimed at regulation of rent and protection of the rights of the tenants on the land.

The main factors, which troubled the peasants during the period, were mounting debt, increased pressure on land, and arbitrary

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fixation of land revenue. The responsibility of tenant legislations was shifted to provinces after grant of provincial autonomy in 1937.

The Indian industry suffered dearly during the reign of the East India Company as discussed earlier. The main aim of trade policy of the company was buying goods from India at cheaper rates and selling them at higher prices in England, due to which the company prospered greatly. This prosperity was misused for acquisition of political power and consequent exploitation of Indian artisans and craftsmen through unjust policies.

The Indian goods gave tough competition to English goods as the people of England preferred to buy Indian goods. The problem of maintaining industries and wages of workers arose in England. Hence the company received orders from British Government that only raw silk should be imported from Bengal, which the company was bound to obey. Such orders were issued on March 17, 1869. In a short time from then, England experienced industrial revolution. In order to protect British industries, imports from India were subjected to high tariffs, whereas British exports to India were actively encouraged. This slowed down the growth of Indian industry. The conditions of Indian industrial workers deteriorated. The interests of Indian industries were subordinated to that of

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England. The industrial workers, who became unemployed, turned to agriculture for livelihood. The urban workers migrated to rural areas. Many of these workers had to borrow from moneylenders, as their economic condition was miserable. The moneylenders exploited their condition by charging exorbitant rates of interest. The industrial workers, once in debt, found it difficult to come out of it.

Later half of 19$^{th}$ century saw the rise of trade unions in India. There were 25 strikes during the period 1882-90 in Bombay and Madras presidency. In 1910, the workers formed 'Workers Council' to promote their interests. They gave call for strikes in industries like cotton textiles, iron and steel, jute, etc. and also in Railways. The All India Trade Union Congress was established in 1920. As many as 168 strikes were observed during 1931 and 2.3 lakh industrial workers had joined them. About 24 lakh man-days were lost on account of these strikes. These strikes intensified and in the year 1937 379 strikes were reported with a total participation of 6.79 lakh workers and loss of 89 lakh man-days.

## 1.2 After independence

After independence, India adopted, like many of its contemporary newly independent countries, socialistic pattern for development. This

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development is best described as state led growth. State exercised significant influence in deciding the growth. Only the State had the power to generate necessary resources for building industries of infrastructure, growth engine for other industries. Significant amount of direct intervention by the state in projects requiring heavy investments were the norm rather than the exception during this post-war and post-colonial period. The capital requirements of most economies were so large that no entity other than the state was considered capable of harnessing the required resources. Under-developed international capital markets, significant trade barriers, and the hangover of sovereignty issues, legacy of the colonial period, ensured that most nations planned for economic self-sufficiency. Under-developed domestic capital markets did not create an environment in which this burden could be shared by the private sector in any significant manner especially in capital-intensive long gestation investments.

Some developing countries, notably in East Asia, transited to a liberalised framework three decades early than India, which has been a gradual reformer. Continued reliance on state intervention created a highly regulated economy. The result was the absence of significant levels of competition either from imports or within the domestic economy. Industrial capacity restrictions, prohibitions in foreign trade, high tariff walls, prohibitions on technology transfer, inadequate

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patent protection, restrictive labour laws and administered interest rates severely limited the scope for efficiency enhancing impact of markets. Even though there was a positive result up to 1980, but growth rates in the early reformers in East Asian countries were considerably higher. *See table 1*

**Table 1**
GDP growth (average % per year)

| Country | 1965-80 | 1980-90 | 1990-2000 |
|---|---|---|---|
| China | 6.4 | 9.5 | 10.3 |
| Korea | 9.5 | 9.7 | 5.7 |
| Malaysia | 7.4 | 5.2 | 7.0 |
| Thailand | 7.4 | 7.6 | 4.2 |
| Indonesia | 7.9 | 5.5 | 4.2 |
| India | 3.7 | 5.3 | 6.0 |

Source: World Development Reports, World Bank

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India was not only lagging behind in economic growth, but she could not generate the competitiveness for the domestic manufacturers, India sought self-sufficiency. Isolation of the economy can be gauged from the fact that, India's share in the world exports reduced from 1.85% to 0.42% between 1942 and 1980.

After 1985, the Indian economy was gradually liberalized and restructured. Economic reforms have been characterized by liberalization and simplification of administrative intervention, phased introduction of domestic and import competition, facilitation of participation by the private sector, public sector reform in financial system, the overall result was positive. The economy grew at around 6% with an increase of 4% in per capita income, poverty declined from 44% to 26%, life expectancy increased from 48 years to 64 years. The share of India's exports in the world exports increased from 0.42% to 0.67%. The ratio of external debt to GDP declined from 5.5% in 1990-91 to 2.6% in 2000-01. Profile of external debt became more stable. The ratio of short term external debt to total external debt declined from a peak of 10.2% in the end of March 1991 to 2.8% in the end of December 2000. The level of foreign exchange reserves increased from a level equal to 3 months import in 1990-91 to a level of over 8.5 months of imports since 1993-94. By 2000, India's short term external debt was only 8.5% of foreign exchange reserves, which is much

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lower than 10% in China, 15.5% in Malaysia, 45.6% in Thailand and 112.6% in Argentina. Macro-economic stability and higher degree of openness have also resulted in an increase in inflow of foreign investment in the form of portfolio as well as FDI from a level of $113 million in 1990-91 to $14294 million in 2000-01. Table 1 shows narrowing down of the gaps of growth of GDP between India and other Asian countries.

Decade of 1990s has fared very well in comparison. 6% per annum economic growth was an average. In comparison economic growth in East Asia, except in the case of China and Malaysia was adversely affected by the financial crisis in the second half of the 1990s. The productivity and efficiency of the Indian economy has been a traditional and much analysed concern in India. Usually total factor productivity (TFP) accounts for one-half of economic growth. This was negative during the period 1959-60 to 1979-80, which indicates the structural inefficiency of the Indian economy before introduction of economic reforms.

During the reform period of 1985-2000, annual average growth in the industrial sector increased from 3.9% during the period of 1960-1985 to 7.2%. In contrast annual average growth in the non-agricultural public sector declined from 8.2% to 7.1% of GDP during the compatible periods.

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This period was characterised by increase in TFP, which should be viewed in association with the higher growth rates in non-agricultural private sector. The 1980s are often called the decade of jobless growth in Indian industries. The overhang of employment from 1970s was used more efficiently and the capital intensity of incremental output increased, driven in part by sticky wages and employment policies, but also by technological requirements. Economic liberalisation provided enhanced and cheaper access to imported capital goods, global technology and global enterprises, all of which facilitated improved in overall productivity.

Post-WTO regime of global competition and falling tariff rates forced domestic firms to improve the efficiency and to face the increased competition in the domestic as well as international market. This led to the organisational restructuring, improved managerial practices, and better capacity utilisation. Such changes in macro-environment have benefited the business in general. PSUs on aggregate continued to make losses in the 1990s. Aggregate loss was 4.5% of net sales in 1990-91. This increased to a peak of 6.9% in 1993-94. Reform process has benefited both public and private sector. In the public sector losses persist. Possibly the beneficial changes in the macro environment have not been matched by initiatives within PSUs to increase their competitiveness, perhaps due to complex procedures and their ownership structure.

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Table 2 illustrates the ratio of PAT to net sales for private manufacturing increased to a peak of 9.1% in 1994-95 before declining to 6.2% in 1997-98.

**Table 2**
**Profit After of Tax of PSUs against Private Sector**
(Profit After Tax as % of net sales)

| Year | PSUs | Private |
|---|---|---|
| 1990-91 | -4.5 | 5.7 |
| 1991-92 | -5.3 | 4.9 |
| 1992-93 | -5.4 | 4.9 |
| 1993-94 | -6.9 | 6.6 |
| 1994-95 | -2.3 | 9.1 |
| 1995-96 | -2.4 | 9.0 |
| 1996-97 | -4.3 | 7.0 |
| 1997-98 | -3.9 | 6.2 |

Source: "The lost decade" NCAER study

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An important feature of the globalisation has been the movement of private capital from one country to another so that an economy's growth is not constrained by its own domestic savings. In 1990 there were 40 countries for which the ratio of FDI to Gross Capital Formation was 5% or more. For India in that year, this ratio was only 0.2%. By 2000, the number of countries where the ratio of FDI to GCF was 5% or more had more than doubled to 99, while for India this ratio was only 2.1%. Export orientation and the inflow of private foreign capita have played a significant role in the development of the East Asian Countries. At the peak, the foreign capital flow into Malaysia in 1993 was 17.4% of its GDP, in Thailand in 1995, it was 12.7% of the GDP, whereas in India it has mostly been below 0.5% of its GDP.

Globalisation has enlarged the growth opportunities for developing countries. On average the share of developing economies in aggregate world exports increased from 20.6% in 1988-90 to 29.9% in 2000. Similarly, their share in the world output increased from 17.9% in 1988-90 to 40.4% in 2000. Despite overwhelming evidence that market orientation, competition, greater participation of the private sector, export orientation together with freeing of the resource constraint by FDI inflows, provides a reasonable basis for higher level of economic growth. Strategies are not universally accepted in India. Even today there are endless debates against privatisation and there is always an apprehension

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that FDI will lead to control by external agents. Perhaps this is due to the residual shadows of our colonial past. One should keep in mind that the unlike the present multinationals, East India Company was never intended to invest in India.

The colonial period marked the drain of national resources to fuel the growth in Europe, but this was assisted by the absence of a domestic sovereign authority, unlike today, which could have resisted to such exploitative extraction. In the globalised world, access to private foreign capital does not imply an erosion of sovereignty. Foreign companies seek investment opportunities to enhance their value, but in the process such investment creates jobs, adds badly needed infrastructure and provides a functional business link between economies of the world. Such links and commitments are long term in nature and should be differentiated from the flows of portfolio investments, which can be temporary transfers driven solely by arbitrage opportunities. In the recent East Asian crisis foreign direct investment was the stable element in the external balance. While to some extent FII investments and foreign lending reduced, FDI inflows persisted.

FDI should not be discarded simply because the investors are foreign entities. India's low access to FDI as compared to China, Brazil, Poland and number of South East Asian countries coupled with our lower past growth rates suggests that there is significant economic value in increasing

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our FDI beyond the existing level of 0.5% of the GDP. As a matter of fact, the inadequate level of domestic savings and investment in India requires a more aggressive approach to utilisation of foreign savings. Table 3 illustrates the structure of domestic savings in public as well as private from 1981 to 1991. Savings in the public sector is gradually declining viz. -1%, -0.9%, and –1.7% in the period 1998 to 2000-01. There has been no upward trend in the public savings since 1980s.

**Table 3**

| Country | Period | Public | Private |
|---|---|---|---|
| Indonesia | 1981-88 | 7.7 | 14 |
| Malaysia | 1981-90 | 10.3 | 19.1 |
| Thailand | 1980-85<br>1986-87 | 14.3<br>8.6 | 4.7<br>14.6 |
| Japan | 1981-88 | 5.1 | 15.8 |
| India | 1961-70<br>1971-80<br>1981-90<br>1991-2000 | 2.7<br>3.7<br>3.02<br>1.01 | 9.89<br>13.7<br>16.16<br>22.04 |

Source: World Bank Economic Survey data

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Though a boom in private savings in the 1990s has maintained the investment rate at around 23%, any increase in the investment rate will have to depend on foreign savings. Higher levels of investment will be key for acceleration of the growth rate to a level of 8%, which is estimated to be the minimum required to effectively tackle the problem of poverty. There is considerable evidence to show that an increase in investment levels sharply increases the rate of economic growth. Increase in productivity coupled with an increase in investment explains the acceleration in economic growth particularly in developing countries. Table 4 provides comparative study in this regard.

**Table 4**

**Investment and GDP growth rates**

(Average % per year)

Change in investment rate against change in GDP growth

| Country | 1980-90 | 1990-95 | 1980-90 | 1990-95 |
|---|---|---|---|---|
| China | 11 | 15.5 | 10.2 | 12.8 |
| Malaysia | 2.6 | 16 | 5.2 | 8.7 |
| Indonesia | 7 | 16.3 | 6.1 | 7.6 |
| Thailand | 9.4 | 10.2 | 7.6 | 8.4 |
| Turkey | 5.3 | 2 | 5.3 | 3.2 |

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| | | | | |
|---|---|---|---|---|
| Argentina | -0.3 | 5.7 | -4.7 | 16 |
| India | 6.5 | 5.3 | 5.8 | 4.6 |
| Venezuela | -5.3 | 3.8 | 1.1 | 2.4 |
| Brazil | 0.2 | 3.5 | 2.7 | 2.7 |
| Philippines | -2.1 | 3.2 | 1 | 2.3 |
| Poland | 0.9 | 1.1 | 1.9 | 2.4 |
| Egypt | 2.7 | -1.5 | 5 | 1.3 |

China, Malaysia (1990-95), Indonesia, Thailand, Turkey (1980-90) and Argentina (1990-95) are examples where a sharp increase in the rate of investment had a positive impact on economic growth. India is also benefited with the resultant increase in economic growth as well. The low rates of economic growth in Venezuela, Brazil, Philippines, Egypt, and Poland can be associated with the negative or low rates of change in the investment levels. For further development it has been estimated that India needs to increase its investment rate to 30% of the GDP if it is to grow at 8% per year. However, enhanced savings in public sector coupled with increased usage of foreign savings can bridge the savings-investment gap in a manner consistent with macro-economic stability. FDI is one of such stable potential

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sources of financing particularly in the era of privatisation.

The experience of China, Malaysia, and Brazil indicates that FDI inflows are also associated with increases in productivity and competitiveness. Malaysia whose ratio of FDI to GDP was 4.3% during the period of 1975-1995 is one of the largest exporters of electronics in the world. Brazil has attracted $30 billion of FDI through privatisation of PSUs during the last 10 years. China permits unlimited FDI number of industries particularly for the takeover of sick industries. FDI inflows of around $40 billion per annum over a number of years have enhanced productivity and competitiveness. Competitively priced Chinese exports provide significant import competition worldwide and are a particular source of concern for domestic Indian manufacturers. China's competitiveness has been enhanced by large-scale privatisation of State owned enterprises and rationalisation of the labour force, which began in 1995. More than 30,000 companies have been privatised and about 50 million workers have been laid off since 1997 and given VRS at terms, which are 3/5 times worse than the terms for VRS in India.

We are fortunate that the scale of PSU restructuring is much smaller than in the case of China, though employment in central PSUs is around 1/3 of the total employment in the Central Government, the absolute numbers were only 2.18

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million in 1990-91, which reduced to 1.74 million by 2000-01. What is significant is that barring the organised private sector, employment levels were stagnant in the 1990s. During the period 1991 to 2001, out of 1.6 million jobs added in the organised sector, 1 million or 2/3 were added in the private sector, which indicates that the private sector has become the major source for incremental employment in the organised sector of the economy over the last decade. As against these, unorganised sector provides 10 times more employment. It has traditionally been dominant employer.

In India for economic reforms privatisation and enhanced access to FDI are the next big frontiers. In fact the latter is to some extent linked to implementation of the former. International experience suggests that privatisation enhances inflows of international private capital, hence there is a case for making non-discriminatory rules for FDI inflows. Currently, there are additional restrictions on FDI in the case of disinvestments of PSUs. This is not exceptional. The Queen of England had to use the golden share to stop the takeover of National Power of UK by Southern Utilities of US only 10 years back in the UK. Now, of course London Electricity and Surrey Electricity have been taken over by EDF, France without any public debate. At the best of times privatisation is an emotive subject. However it is instructive that other countries have trodden this path before and have found that economic gains

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from privatisation, justify the pain associated with a break from the past. In a free market economy, and competitive environment, the access to capital for any business entity must bear the test of availability and cost. Here the business entities must be free to determine at their own.

The performance of a very large number of PSUs is disappointing, often owing to reasons beyond their control. Some PSUs have done extremely well, but these are in the monopoly sectors like petroleum, power and telecom, where government determines prices on a cost plus basis. Once these sectors are deregulated, these PSUs are likely to come under severe competitive pressure and may see erosion of their profitability. The policy of Government on disinvestments has evolved over the last decade. It started with the sale of minority shares in 1991-92, which continued with some modification till 1999-2000. During this period Rs. 1863 crores were realised through this method of market sale of shares. This policy changed around 31st March, 2000 and was announced by the Finance Minister in budget speech of 2000-2001. Government established a new Department for Disinvestment, which was objected to emphasize increasingly strategic sales of identified PSUs, in which sale of equity is carried out by Government where the management-control of the entity is handed over to the strategic partner. During the period 1991-2000, the sale of minority shares of PSUs has led to realisation of about Rs. 19,000crore for Government. Most of these shares

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were bought by financial institutions. UTI was one of such institutions, which had picked up substantial quantities of such stock. With the commencement of the policy of strategic sale, there has been a dramatic reversal. The PSU index has increased steadily since then.

Realising the important contribution that private foreign investment can make to the process of economic development, India has introduced many policy reforms to attract them. Restrictive investment regime has been liberalised. In addition, various types of incentives are being offered to attract foreign direct investment. Greater attention is also being paid to make the macro economic environment more conducive to foreign investors. Provisions of infrastructure and other support services are being targeted. Financial sector reforms are being undertaken to facilitate financial flows in various forms.

## 1.3 Industrial structure

Indian economy, like numerous other underdeveloped economies, is agriculturally dominated economy. Though contributing around 25% of the Gross Domestic Product, agriculture employs nearly 70% of the total work force of the country, thus playing important role in demand for other goods and services manufactured in the country. The developed countries on the other hand, are generally industrialised. The people in these countries enjoy higher standards of living.

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India too has adopted the policy of planned industrial development. This increased the possibility of raising the rate of growth by increasing the degree of industrialisation in the economy. According the industrial policy of the Government, the basic industries, the machine tools industries, the consumer goods industries, and services should expand their share in the national economy, thereby reducing dependence on agriculture. Industrialisation is also conceived as a growth engine because it adds to the availability of employment opportunities directly or indirectly. Industrial growth encourages technical knowledge and research activities and also helps to raise productivity of labour and capital as factors of production.

The industrial structure of a country comprises several types of industries. The industries can be classified on various basis such as ownership, technique of production, make up of work force, capital intensity, export orientation, strategic importance, etc.

The most popular and legally important classification of industries is on the basis of scale of production. The industries can be divided into the following four types based on the scale of production:

I. Cottage industries
II. Small scale industries
III. Medium scale industries

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IV. Large scale industries

I. Cottage industries:

The cottage industries are the smallest constituents of the industrial structure based on its scale of operations. The production unit in this category of industries is extremely small, requiring little use of capital. These units function in rural or semi-urban areas. They use family labour and simple tools & techniques. Production is normally carried on in residential premises of the artisans and the use of electricity in the production process is the minimum. The raw material is obtained from the local market. The market of such goods is limited to a particular village or town, or at the most villages in the adjoining area. Though, in recent years, the market for cottage industry's goods has widened but they are still limited in range. These industries provide supplementary employment and incomes to the people in the rural areas. The articles are made out of natural materials such as cane, bamboo, leather, gum, raw cotton, jute, earth, wood, etc. Industries in the cottage category include, handlooms, bamboo products, small iron works, earthen vessels, handicrafts, lock making, ornaments out of precious and non-precious metals, etc.

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## II. Small-scale industries:

Any industrial unit having investment in fixed assets more than Rs. 3 crore is classified as a small-scale undertaking. The small-scale sector in the country occupies great significance by the fact that it employs the largest number of work force just after agriculture and contributes nearly 15% of the country's Gross Domestic Product. The special characteristics of small-scale undertakings are,

(1) Work force of small-scale industries is normally less than 20.

(2) Ownership is mainly on partnership, Hindu Undivided Family, or individual ownership basis.

(3) They are located in specially earmarked industrial zones of medium-size cities and towns or in the outskirts of large cities.

(4) They manufacture mostly non-branded goods.

(5) These industries are based on other large industries. They even act as a link between large industries and

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agriculture. For example the cotton ginning industry, etc.

(6) Most of these industries enjoy one or other form of subsidy or assistance from Government.

(7) The market for most of their produce is local or specific. Some of the small-scale industries are export oriented also.

(8) The main forms of small-scale industries include, cotton ginning, foundries, tools and spare-parts manufacturing, etc.

(9) Research and development expenditure is minimum.

III. Medium-scale industries:

These industries are located mid-way between small-scale and large industries. Many of such industries comprise of expanded small-scale enterprises or subsidiary units of large-scale industries. The following are special characteristics of such industries:

(1) The production process is largely mechanised.

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(2) The goods produced possess a large market.

(3) These industries also carry out research and development on a small scale.

(4) The main forms of medium-scale industries include generic drugs, edible oils, oil engines, food processing and dehydration, etc.

IV. Large-scale industries:

These industries involve heavy investment in fixed assets such as land, buildings, machinery, etc. These industries large amount of formalities before starting up. The important characteristics of these industries are as follows:

(1) The ownership in these industries is more or less on corporate basis.

(2) The set-up and maintenance costs of such industries are very high.

(3) The set-up time is very high compared to other varieties of industries on account of clearances required to be sought from large number of government authorities.

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The process is complex, and the degree of complexity varies across all types of products.

(4) The production is carried out on cyclical basis, that is, every process on the product is specifically accounted and controlled.

(5) The goods manufactured lack substantial variety.

(6) Changes in product lines are difficult and very expensive.

(7) Production is aptly supported by aggressive marketing and sales support.

(8) Employment policies, and the employee structure are more or less static. Prevalent labour laws have greater say in employment policies.

(9) The cost of production of goods manufactured is lower compared to all other scales of industries.

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# CHAPTER 2

# Foreign Investment Policy and Procedure

## 2.1 Entry modes for Foreign Direct Investment

Government wishes to facilitate Foreign Direct Investment (FDI) and investment from Non-Resident Indians (NRIs) including Overseas Corporate Bodies (OCBs) that are predominantly owned by them, to complement and supplement domestic investment. Investment and returns are freely repatriable, except where the approval is subject to specific conditions such as lock-in period on original investment, dividend cap, foreign exchange neutrality, etc. as per the notified sectoral policy. The condition of dividend balancing was applicable to FDI in specified consumer goods, industries stands with drawn for dividends declared after 14th July 2000, the date on which the Press Note No. 7 of 2000 series was issued.

FDI is freely allowed in all sectors including service sector, except where the existing and notified sectoral policy does not permit FDI beyond ceiling. FDI for virtually all items/activities can be brought through the Automatic Route under powers delegated to the Reserve Bank of India, and for the remaining

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items/activities through Government Approval. Government approvals are accorded on the recommendation of the Foreign Investment Promotion Board (FIPB), chaired by the Secretary, Department of Industrial Policy and Promotion (Ministry of Commerce and Industry) with the Union Finance Secretary, Commerce Secretary, and other key Secretaries of the Government as its members.

### 2.1.1 *Entry via automatic route*

(a) New Ventures:

All items/activities for FDI/NRI/OCB investment up to 100% fall under automatic route except those specified:

Whenever any investor chooses to make an application for the FIPB and not to avail of the automatic route, he or she may do so.

Investment in public sector units as also for EOU/EPZ/EHTP/STP units would also qualify for automatic route. Investments under the automatic route shall continue to be governed by the notified sectoral policy and equity caps and RBI will ensure compliance of the same. The National Industrial Classification (NIC) 1987 shall remain

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applicable for description of activities and classification for all matters relating to FDI/NRI/OCB investment:

Areas/sectors/activities hitherto not open to FDI/NRI/OCB investment shall continue to be so unless otherwise decided and notified by Government.

Any change in the sectoral policy/sectoral equity cap shall be notified by the Secretariat of Industrial Assistance (SIA) in the Department of Industrial Policy & Promotion.

(b) Existing Companies:

Besides new companies, automatic route for FDI/NRI/OCB investment is also available to the existing companies proposing to induct foreign equity. For existing companies with an expansion programme, the additional requirements are that

(i) The increase in equity level must result from the expansion of the equity base of the existing company without the acquisition of existing

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shares by NRI/OCB/foreign investors,

(ii) The money to be remitted should be in foreign currency and

(iii) Proposed expansion programme should be in the sector(s) under the automatic route.

Otherwise the proposal would need Government approval through the FIPB. For this the proposal must be supported by a Board Resolution of the existing Indian company.

For existing companies without an expansion programme, the additional requirements for eligibility for automatic route are

(i) That they are engaged in industries under the automatic route,

(ii) The increase in equity level must be from expansion of the equity base and

(iii) The foreign equity must be in foreign currency.

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The earlier SEBI requirement, applicable to public limited companies that shares allotted on preferential basis shall not be transferable in any manner for a period of 5 years from the date of their allotment has now been modified to the extent that not more than 20% of the entire contribution brought in by promoter cumulatively in public or preferential issue shall be locked in.

The automatic route for FDI and/or technology collaboration would not be available for those who have or had any previous joint venture or technology transfer/trade mark agreement in the same or allied field in India.

Equity participation by international financial institutions such as ADB, IFC, CDC, DEG, etc. in domestic companies is permitted through automatic route subject to SEBI/RBI regulations and sector specific cap on FDI.

In a major drive to simplify procedures for foreign direct investment under the automatic route, RBI has given permission to Indian Companies to accept investment under this route without obtaining prior approval from RBI. Investors are required to notify the Regional Office concerned of the RBI of

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receipt of inward remittances within 30 days of issue of shares to Foreign Investors. This facility is also available to NRI/OCB investment.

### 2.1.2 *Entry through Government approval*

For the following categories, Government approval for FDI/NRI/OCB through the FIPB shall be necessary:

(1) All proposals that require an Industrial License, which includes,

(i) The item requiring an Industrial Licence under the Industries (Development & Regulation) Act, 1951;

(ii) Foreign Investment being more than 24% in the equity capital of units manufacturing items reserved for small scale industries; and

(iii) All items which require an Industrial License in terms of the locational policy

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notified by Government under the New Industrial Policy of 1991.

(2) All proposals in which the foreign collaborator has a previous venture/tie up in India. The modalities prescribed in Press Note No. 18 dated 14/12/1998 of 1998 series, shall apply to such cases. However, this shall not apply to investment made by multilateral financial institutions such as ADB, IFC, CDC, DEG, etc. as also investment made in the Information Technology Sector.

(3) All proposals relating to acquisition of shares in an existing Indian company in favour of a foreign/NRI/OCB investor.

(4) All proposals falling outside notified sectoral policy/caps or under sectors in which FDI is not permitted.

Areas/sectors/activities hitherto not open to FDI/NRI/OCB investment shall continue to be so unless otherwise decided and notified by Government.

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Any change in the sectoral policy/sectoral equity cap shall be notified by the Secretariat of Industrial Assistance (SIA) in the Department of Industrial Policy & Promotion.

RBI has granted general permission under Foreign Exchange Management Act (FEMA) in respect of proposals approved by the Government. Indian companies getting foreign investment approval through FIPB route do not require any further clearance from RBI for the purpose of receiving inward remittance and issue of shares to the foreign investors. Such companies are, however, required to notify the Regional Office concerned of the RBI of receipt of inward remittances within 30 days of such receipt and to file the required documents with the concerned Regional Offices of the RBI within 30 days after issue of shares to the foreign investors.

For greater transparency in the approval process, Government has announced guidelines for consideration of FDI proposals by the FIPB.

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### 2.1.3 *Issue and Valuation of shares in case of existing companies*

Allotment of shares on preferential basis shall be as per the requirements of the Companies Act, 1956, which will require special resolution in case of a public limited company.

In case of listed companies, valuation shall be as per the RBI/SEBI guidelines as follows:

The issue price shall be either at:

(i) The average of the weekly high and low of the closing prices of the related shares quoted on the Stock Exchange during the six months preceding the relevant date.

(ii) The average of the weekly high and low of the closing prices of the related shares quoted on the Stock Exchange during the two weeks preceding six months prior to the relevant date.

The stock exchange referred to is the one at which the highest trading volume in respect of the share of the company has been recorded during the preceding six months prior to the relevant date.

The relevant date is the date thirty days prior to the date on which the meeting of the General Body of the shareholders is convened.

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In all other cases a company may issue shares as per the RBI regulation in accordance with the guidelines issued by the erstwhile Controller of Capital Issues.

Other relevant guidelines of SEBI/RBI including the SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 1997, wherever applicable, would need to be followed.

### 2.1.4 *Foreign Investment in the Small-scale Sector*

Under the small-scale policy, equity holding by other units including foreign equity in a small-scale undertaking is permissible up to 24%. However there is no bar on higher equity for holding foreign investment if the unit is willing to give up its small-scale status. In case of foreign investment beyond 24% in a small-scale unit, which manufactures small-scale reserved item (s), an industrial license carrying a mandatory export obligation of 50% would need to be obtained.

### 2.1.5 *Foreign Investment in Trading Activities*

Foreign investment for trading can be approved through the automatic route up to 51% foreign equity, and beyond this by the Government through FIPB. For approval through the automatic route, the requirement would be that it is primarily

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export activities and the undertaking concerned is an export house/trading house/super trading house/star trading house registered under the provisions of the Export and Import policy in force.

### 2.1.6 *Other Modes of Foreign Direct Investments*

1. Global Depositary Receipts (GDR)/American Depositary Receipts (ADR)/Foreign Currency Convertible Bonds (FCCB):

   Foreign investment through GDRs/ADRs/FCCBs is treated as Foreign Direct Investment. Indian companies are allowed to raise equity capital in the international market through the issue of GDRs/ADRs/FCCBs. These are not subject to any ceilings on investment. An applicant company seeking Government's approval in this regard should have a consistent track record for good performance (financial or otherwise) for a minimum period of 3 years. This condition can be relaxed for infrastructure projects such as power generation, telecommunication, petroleum exploration and refining, ports, airports, and roads.

   There is no restriction on the number of GDRs/ADRs/FCCBs to be floated by a company or a group of companies in a

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financial year. A company engaged in the manufacture of items covered under automatic route, whose direct foreign investment after a proposed GDRs/ADRs/FCCBs issue is likely to exceed the percentage limits under the automatic route, or which is implementing a project falling under the Government approval route, would need to obtain prior Government clearance through FIPB before seeking final approval from the Ministry of Finance.

There are no end-use restrictions on GDR/ADR issue proceeds, except for an express ban on investment in real estate and stock markets. The FCCB issue proceeds can be used for general corporate restructuring.

2. Preference Shares:

Foreign investment through preference shares is treated as foreign direct investment. Proposals are processed either through the automatic route or FIPB as the case may be. The following guidelines apply to issue of such shares:

(i) Foreign investment in preference shares is considered as part of share capital and fall outside External Commercial Borrowing (ECB) guidelines/cap.

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(ii) Preference shares to be treated as foreign direct equity for purpose of sectoral caps on foreign equity, where such caps are prescribed, provided they carry a conversion option. If the preference shares are structured without such conversion option, they would fall outside the foreign direct equity cap.

(iii) Duration for conversion shall be as per the maximum limit prescribed under the Companies Act or what has been agreed to in the shareholders agreement whichever is less.

(iv) The dividend rate would not exceed the limit prescribed by the Ministry of Finance.

(v) Issue of Preference Shares should conform to guidelines prescribed by the SEBI and RBI and other statutory requirements.

3. <u>Investment by Non-Resident Indians & Overseas Corporate Bodies:</u>

For all sectors, excluding those falling under Government approval, NRIs (which

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also includes PIOs) and OCBs (an overseas corporate body means a company or other entity owned directly or indirectly to the extent of at least 60% by NRIs) are eligible to bring investment through the automatic route of RBI. All other proposals, which do not fulfil any or, all of the criteria for automatic approval are considered by the Government through the FIPB.

The NRIs and OCBs are allowed to invest in housing and real estate development sector, in which foreign direct investment is not permitted. They are allowed to hold up to 100% equity in civil aviation sector in which otherwise foreign equity only up to 49% is permitted.

## 2.2 Foreign Technology Agreements

With a view to inject the desired level of technological dynamism in Indian industry and for promoting an industrial environment where the acquisition of technological capability receives priority, foreign technology induction is encouraged both through FDI and through foreign technology collaboration agreements. Foreign technology collaborations are permitted either through the automatic route under delegated powers exercised by the RBI, or by the Government. However, cases involving industrial licenses/small scale reserved items do not qualify for automatic approval and would require

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consideration and approval by the Government. Automatic route for technology collaboration would also not be available to those who have, or had any previous technology transfer/trademark agreement in the same or allied field in India. Further, automatic approval for EOU/EHTP/STP units is governed by respective provisions.

### 2.2.1 *Automatic Approval for Foreign Technology Agreements*

The Reserve Bank of India, through its regional offices, accords automatic approval to all industries for foreign technology collaboration agreements subject to:

(i) The lump sum payments not exceeding US $ 2 Million;

(ii) Royalty payable being limited to 5% for domestic sales and 8% for exports, subject to a total payment of 8% on sales over a 10 year period (the royalty limits are net of taxes and calculated according to standard conditions); and

(iii) The period of payment of royalty not exceeding 7 years from the date of commencement of commercial production, or from 10 years from the date of agreement, whichever is earlier.

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Payment of royalty up to 2% for exports and 1% for domestic sales is allowed under automatic route on use of trademarks and brand name of the foreign collaborator without technology transfer. In case of technology transfer, payment of royalty subsumes the payment of royalty for use of trademark and brand name of the foreign collaborator. Royalty on brand name/trade mark shall be paid as a percentage of net sales, viz., gross sales less agents'/dealers' commission, transport cost, including ocean freight, insurance, duties, taxes and other charges, and cost of raw materials, parts, components imported from foreign licensor or its subsidiary/affiliated company. Payment of royalty up to 8% on exports; and 5% on domestic sales by wholly owned subsidiaries (WOS) to offshore parent companies is allowed under the automatic route without any restriction on the duration of royalty payments.

### 2.2.2 *Government Approval Requirements regarding Foreign Technology Agreements*

For the following categories, Government approval would be necessary:

(a) Proposals attracting compulsory licensing

(b) Items of manufacture of reserved for the small scale sector

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(c) Proposals involving any previous joint venture, or technology transfer/trademark agreement in the same or allied field in India. The definition of "same" and "allied" field would be as per 4 digit NIC 1987 code and 3 digit NIC 1987 code.

(d) Extension of foreign technology collaboration agreements (including those cases, which may have received automatic approval in first instance)

(e) Proposals not meeting any or all of the parameters for automatic approval.

The items of foreign technology collaboration, which are eligible for approval through the automatic route, and by the Government are technical know how fees, payment for design and drawing, payment for engineering service and royalty.

Payments for hiring foreign technicians, deputation of Indian technicians abroad, and testing of indigenous raw material, products, indigenously developed technology in foreign countries are governed by separate RBI procedures and rules and are not covered by the foreign technology collaboration approval. Similarly, payments for imports of plant and machinery and raw material are also not covered by the foreign technology collaboration approval. For any of these items, entrepreneurs may contact the RBI.

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## 2.3 Foreign Investment in 100% Export Oriented Units (EOUs)/Export Processing Zones (EPZs)/Special Economic Zones (SEZs)

100% Export Oriented Units (EOUs) and units in the Export Processing Zones (EPZs)/Special Economic Zones (SEZs), enjoy a package of incentives and facilities, which include duty free imports of all types of capital goods, raw materials, and consumables in addition to tax holidays against export.

100% FDI is permitted under automatic route for setting up of industrial park/industrial model town/special economic zone in the country. To encourage investment in this sector, 100% income tax exemption for 10 years within a block of 15 years is also granted for the industrial parks set up during the period 1/4/1997 to 31/3/2006.

### *2.3.1 Automatic Approval for Investment in 100% Export Oriented Units (EOUs)/Export Processing Zones (EPZs)/Special Economic Zones (SEZs)*

The Development Commissioners (DCs) of Export Processing Zones (EPZs)/Free Trade Zones (FTZs)/Special Economic Zones (SEZs) accord automatic approval to projects where

(i) Activity proposed does not attract compulsory licensing or falls in the

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services sector except IT enabled services;

(ii) Location is in conformity with the prescribed parameters;

(iii) Units undertake to achieve exports and value addition norms as prescribed in the Export and Import Policy in force;

(iv) Unit is amenable to bonding by customs authorities; and

(v) Unit has projected the minimum export turnover, as specified in the Handbook of Procedures for Export and Import.

All proposals for FDI/NRI/OCB investments in EOU/EPZ units qualify for approval through automatic route subject to sectoral norms. Proposals not covered under the automatic route would be considered and approved by FIPB.

Conversions of existing Domestic Tariff Area (DTA) units into EOU is also permitted under automatic route, if the DTA unit satisfies the parameters mentioned above and there is no outstanding export obligation under any other Export Oriented Scheme of the Government of India.

FDI up to 100% is allowed through the automatic route for all manufacturing activities in Special

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Economic Zones (SEZs) except for the following activities:

(i) Arms and ammunition, explosives and allied items of defence equipments defence aircraft and warships;

(ii) Atomic substances;

(iii) Narcotics and psychotropic substances and hazardous chemicals;

(iv) Distillation and brewing of alcoholic drinks; and

(v) Cigarettes/cigars and manufactured tobacco substitutes.

For services, norms as notified, would be applicable.

*2.3.2* *Government Approval for Investment in 100% Export Oriented Units (EOUs)/Export Processing Zones (EPZs)/Special Economic Zones (SEZs)*

All proposals, which do not meet any or all of the parameters for automatic approval will be considered and approved by the Board of Approval of EOU/EPZ/SEZ set up in the Department of Commerce.

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## 2.4 Foreign investment in Electronic Hardware Technology Parks (EHTPs) and Software Technology Parks (STPs)

In order to provide impetus to the electronics industry, to enhance its export potential and to develop an efficient electronic component industry, Electronic Hardware Technology Park and Software Technology Park schemes offer a package of incentives and facilities like duty free imports on the lines of EOU scheme, deemed exports benefits and tax holidays.

### *2.4.1 Automatic approval for foreign investment in Electronic Hardware Technology Parks (EHTPs) and Software Technology Parks (STPs)*

The Directors of STPs in respect of STP proposals; and the Designated Officers in respect of EHTP proposals accord automatic approval if:

(i) Items do not attract compulsory licensing;

(ii) Location is in conformity with the prescribed parameters;

(iii) Export obligation laid down in the respective EHTP scheme or STP scheme is fulfilled;

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(iv) Unit is amenable to bonding by the Customs, and all the manufacturing operations are carried out in the same premises and the proposal does not envisage sending out of the bonded area any raw material or intermediate products for any other manufacturing or processing activity.

All proposals for FDI/NRI/OCB investments in EHTP/STP units are eligible for approval through Automatic Route subject to certain parameters.

### 2.4.2 *Government approval for foreign investment in Electronic Hardware Technology Parks (EHTPs) and Software Technology Parks (STPs)*

All proposals which do not meet any or all of the parameters for automatic approval need to be considered and approved by the Government. Government approval for FDI/NRI/OCB investment under EHTP/STP is needed to be obtained through the FIPB.

## 2.5 Approval Procedures

The description of activities seeking all industrial approvals including foreign direct investment are required to be given as per the National Industrial

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Classification of All Economic Activities (NIC), 1987, published by the Central Statistical Organisation, Ministry of Statistics and Programme Implementation, New Delhi.

### 2.5.1 *Procedure for Foreign Direct Investment*

#### 2.5.1.1 *Procedure for approval under automatic route*

The proposals for approval under the automatic route are to be made to the Reserve Bank of India in the FC (RBI) form. In a major drive to simplify procedures for foreign direct investment under the "automatic route", RBI has given permission to Indian Companies to accept investment under this route without obtaining prior approval from Reserve Bank of India. However, investors will have to file the required documents with the concerned Regional Office of the RBI within 30 days after issue of shares to foreign investors. This facility is available to NRI/OCB investment also.

#### 2.5.1.2 *Procedure for Government Approval*

All other proposals for foreign investment in EOU/EPZ/STP/EHTP units, which do not fulfil any or all of the parameters prescribed for automatic approval by Government. All such proposals are considered for approval by the Foreign Investment Promotion Board (FIPB). The FIPB also grants composite approvals involving foreign technological collaborations and setting up

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of Export Oriented Units involving foreign investment/foreign technical collaboration.

Applications to FIPB for approval of foreign investment should be submitted in Form FC-IL. Plain paper applications carrying all relevant details are also accepted. No fee is payable. The following information should form part of the proposals submitted to FIPB:

(i) Whether the applicant has had or has any previous financial/technical collaboration or trademark agreement in India in the same or allied field for which approval has been sought; and

(ii) If so, details thereof and the justification for proposing the new venture/technical collaboration (including trademarks).

The application can be submitted with the EAU of the Secretariat for Industrial Assistance (SIA), Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Udyog Bhavan, New Delhi. Applications can also be submitted with Indian Missions abroad who will forward them to SIA for further processing.

Foreign investment proposals received in the SIA are placed before the Foreign Investment Promotion Board within 15 days of its receipt. The Board has the flexibility of purposeful negotiation

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with the investors and considers the project proposals in totality in order to ensure optimum foreign direct investment into the country. The recommendations of FIPB in respect of project proposals involving a total investment exceeding Rs. 6 billion are considered and approved by the Industry Minister. Projects with a total investment exceeding Rs. 6 billion are submitted to the Cabinet Committee on Economic Affairs (CCEA) for decision.

The decision of the Government in all cases is conveyed by SIA normally within 30 days.

RBI has granted general permission under Foreign Investment Management Act (FEMA) in respect of proposals approved by the Government. Indian companies getting foreign investment approval through FIPB route do not require any further clearance from RBI for the purpose of receiving inward remittance and issue of shares to the foreign investors. Such companies are, however, required to fie the required document with the concerned Regional Office of the RBI within 30 days after issue of shares to the foreign investors.

Similarly, for inward remittance and issue of shares to NRI/OCB up to 100% equity also prior permission of RBI is not required. These companies have to file the required document with the concerned Regional Offices of RBI within 30 days after the issue of shares to NRIs/OCBs.

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### 2.5.2 *Approval Procedure for Foreign Technical Collaboration*

#### 2.5.2.1 *Procedure for Automatic Approval*

Applications for automatic approval for such foreign technology agreements should be submitted in Form FT (RBI) with the concerned Regional Offices of RBI. No fee is payable. Approvals are available within 2 weeks.

#### 2.5.2.2 *Procedure for Government Approval*

All other proposals for foreign technology agreement, not meeting any or all of the parameters for automatic approval, and all cases of extension of existing foreign technical collaboration agreement, are considered for approval, on merits, by the Government. Application in respect of such proposals should be submitted in Form FC-IL to the SIA. No fee is payable. The following information should form part of the proposals submitted to SIA:

(i) Whether the applicant has had or has any previous financial/technical collaboration or trademark agreement in India in the same or allied field for which approval has been sought; and

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(ii) If so, details thereof and the justification for proposing the new venture/technical collaboration (including trademarks).

On consideration of the proposal by the Project Approval Board/FIPB, decisions are normally conveyed within 4 to 6 weeks of filing the application.

### 2.5.3 *Approval Procedure for 100% Export Oriented Units and Unites Set Up in EPZ/FTZ/SEZ*

#### 2.5.3.1 *Procedure for approval for EOUs*

Applications in the prescribed form for 100% EOUs should be submitted to the Development Commissioners (DCs) of the Export Processing Zones (EPZs) concerned for automatic approval and to the SIA for Government approval. The application should be submitted along with a crossed demand draft of Rs. 5000 drawn in favour of "the Pay & Accounts Officer, Department of Industrial Development, Ministry of Commerce & Industry".

Applications in the prescribed form for 100% EOUs should be submitted to the DCs of the EPZs. Whenever, the proposals meet the criteria for automatic approval the DC of the EPZ would issue letters within 2 weeks.

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Proposals not covered by the automatic route shall be forwarded by the DC to the Board of approval for consideration. On consideration of the proposal by the board, the decision would normally by conveyed in six weeks. Such proposals, by foreign/NRI should seek separate approval from the FIPB.

### *2.5.3.2 Procedure for approval for units located in EPZ/FTZ/SEZ*

Applications for setting up units in EPZs/SEZs should be submitted to the concerned DC of the EPZ/SEZ. The application should be submitted along with a crossed demand draft of Rs. 5000 drawn in favour of "the Pay & Accounts Officer, Department of Industrial Development, Ministry of Commerce & Industry".

Proposals not covered by the automatic route shall be forwarded by the DC to the Board of approval for consideration. On consideration of the proposal by the board, the decision would normally by conveyed in six weeks. Such proposals, by foreign/NRI should seek separate approval from the FIPB.

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### *2.5.3.3 Procedure for approval for units located in EHTP/STP*

Applications in the prescribed form for 100% EOUs should be submitted to the concerned Directors of STPs or Designated Officers of EHTPs for automatic approval and to the SIA for Government approval. The application -should be submitted along with a crossed demand draft of Rs. 5000 drawn in favour of "the Pay & Accounts Officer, Department of Industrial Development, Ministry of Commerce & Industry".

Applications in the prescribed form should be should be submitted to the concerned Directors of STPs or Designated Officers of EHTPs for automatic approval. Whenever, the proposals meet the criteria for automatic approval, the approval letters are issued within 2 weeks. All other proposals shall be forwarded to the Inter Ministerial Standing Committee in the Ministry of Information Technology for consideration.

With regard to the proposals requiring government approval should be submitted to the Officer Designated by the Ministry of Information Technology for the purpose. Such applications shall be forwarded by the Officer designated to the Inter Ministerial Standing Committee in the Ministry of Information Technology for consideration. On consideration by the committee, a decision would be normally be conveyed within 6 weeks.

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Such proposals by foreign/NRI/OCB investors shall be treated as above if qualified under automatic approval. For proposals not covered under automatic route, the applicant should seek separate approval of the FIPB.

*2.5.3.4 Procedure for availing Income Tax benefit for the Industrial Park*

For availing 100% tax exemption available under section 80 IA of the Income Tax Act, 1961 for setting up, operating, operating and maintenance of Industrial Park, proposal has to be submitted in IPS-I form to SIA. The proposals, which meet the given criteria, are approved under automatic route. Otherwise, they are considered under non-automatic route by an Empowered Committee. Application for automatic approval has to be submitted in duplicate and for non-automatic approval in six sets. The IPS-I form has to be accompanied with a demand draft of Rs. 6000 drawn in favour of "the Pay & Accounts Officer, Department of Industrial Development, Ministry of Commerce & Industry".

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## 2.6 Investment Promotion and Facilitation

### *2.6.1 Foreign Investment Promotion Board (FIPB)*

The Government has revamped the GIPB and transferred it to the Industry Ministry. The FIPB is the nodal, single window agency for all matters relating to FDI as well as promoting investment into the country. It is chaired by Secretary, Industry (Department of Industrial Policy and Promotion). Its objective is to promote FDI into India by,

(i) Undertaking investment promotion activities in India and abroad,

(ii) Facilitating investment in the country by international companies, non-resident Indians and other foreign investors,

(iii) Purposeful negotiations/discussions with potential,

(iv) Early clearance of proposals submitted to it, and

(v) Review of policy and putting in place appropriate institutional arrangements, transparent rules and procedures and guidelines for investment promotion and approvals.

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After revamping, the FIPB has played a proactive role in promoting and attracting FDI into the country and further facilitating expeditious clearance to the proposals submitted to it. The FIPB has also decided to monitor implementation of mega projects to further facilitate investment and remove bottlenecks and as part of this exercise, to get studies commissioned through professional bodies and undertake other promotional measures.

### 2.6.2 *Foreign Investment Implementation Authority (FIIA)*

Government has set up the Foreign Investment Implementation Authority (FIIA) in the Ministry of Commerce and Industry. The FIIA will facilitate quick translation of Foreign Direct Investment approvals into implementations, provide a pro-active one stop after care service to foreign investors by helping them obtain necessary approvals, sort out operational problems and meet with various Government Agencies to find solutions to problems and maximising opportunities through a partnership approach.

The FIIA shall take steps to:

(i) Understand and address concerns of investors;

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(ii) Understand and address concerns of approving authorities;

(iii) Initiate multi agency consultations; and

(iv) Refer matters not resolved at the FIIA level to high levels on quarterly basis, including cases of projects slippage on account of implementation bottlenecks.

The functions of FIIA are as under:

(i) Expediting various approvals/permissions;

(ii) Fostering partnership between investors and government agencies concerned;

(iii) Resolve difference in perceptions;

(iv) Enhance overall credibility;

(v) Review policy framework and,

(vi) Liase with the Ministry of External Affairs for keeping India's diplomatic missions abroad informed about translation of FDI approvals into actual investment and implementation.

The modalities of functioning of FIIA shall be as under:

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(i) The FIIA shall set up a Fast Track Committee (FTC) to review and monitor mega projects. It will nominate various members of the FTC from representatives of various Ministries/agencies/State Governments at the working level. The representative of the AM concerned shall act as the project coordinator and shall head the FTC. The FTC shall prescribe the time frame within which various approvals/permissions are to be given on a project-to-project basis. FTC shall also flag issues that need to be resolved by FIIA. Based on the inputs provided by FTC, the FIIA will give its recommendations on each project on the basis of which Administrative Ministries/State Government shall take action under their own laws and regulations.

(ii) The FIIA will initiate inter-Ministerial consultations and make appropriate recommendations to the competent authority, i.e. Ministry/Department concerned at the Central Government level and the State Government, as the case may be, on issues requiring public policy intervention.

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(iii) The FIIA will act as a single point interface between the investor and Government agencies including Administrative Ministries/State Governments/Pollution Control Board/DGFT/Regulatory Authorities/Tax Authorities/Company Law Board, etc.

(iv) The FIIA shall meet once every month to review cases involving investment of Rs. 100 crore or more, consider the references received from the FTC, and monitor the functioning of various FTCs. It would also entertain any complaint regarding implementation bottlenecks from FDI approval holders regardless of the quantum of investment.

(v) The FIIA shall also make recommendations from time to time on issue relating of the speedy implementation of various FDI projects and also provide transparency in government functioning with respect to FDI projects.

The Secretariat for Industrial Assistance (SIA) in the Department of Industrial Policy and Promotion shall function as the Secretariat of FIIA.

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### 2.6.3 *Foreign Investment Promotion Council (FIPC)*

Apart form making the policy framework investor-friendly and transparent, promotional measures are also taken to attract Foreign Direct Investment into the country. The Government has constituted a Foreign Investment Promotion Council (FIPC) in the Ministry of Commerce and Industry. This comprises professionals from industry and commerce. It has been set up to have a more target-oriented approach toward Foreign Direct Investment promotion. The basic function of the Council is to identify specific sectors/projects within the country that require Foreign Direct Investment and target specific regions/countries of the world for its mobilisation.

### 2.6.4 *Secretariat for Industrial Assistance (SIA)*

SIA has been set up by the Government of India in the Department of Industrial Policy and Promotion in the Ministry of Commerce and Industry to provide a single window for entrepreneurial assistance, investor facilitation, receiving and processing all applications which require Government approval, conveying Government decisions on applications filed, assisting entrepreneurs and investors in setting up projects,

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(including liaison with other organisations and State Governments) and monitoring implementation of projects. It also notifies all Government Policy relating to investment and technology, and collects and publishes all Government Policy relating to investment and technology, and collects and publishes monthly production data for 209 select industry groups.

As an investor friendly agency, SIA provides information and assistance to Indian and foreign companies in setting up industry and making investments. It guides prospective entrepreneurs and disseminates information and data on a regular basis through its two monthly newsletters the "SIA Newsletter" and the "SIA Statistics" as also through its website. It also assists potential investors in finding joint venture partners and provide complete information on relevant policies and procedures, including those, which are specific to sectors and the State Governments.

The Entrepreneurial Assistance Unit (EAU) of the SIA provides assistance to entrepreneurs on various subjects concerning investment decisions. The unit receives all papers/applications related to industrial approvals and immediately issues a computerised acknowledgement, which also has an identity/reference number. All correspondence with the SIA should quote this number. In case of papers filed by post, the acknowledgement will be sent by post. The Unit extends this facility to all papers/applications relating to IEMs, Industrial

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Licences, Foreign Investment, Foreign Technology Agreements, 100% EOUs, EHTP, STP schemes, etc.

The unit also attends to enquiries from entrepreneurs relating to a wide range of subjects concerning investment decisions. It furnishes clarifications and arranges meetings with nodal officers in concerned Ministries/Organisations. The unit also provides information regarding the current status of applications filed for various industrial approvals.

### 2.6.5 *Investment Promotion and Infrastructure Development (IP & ID) Cell*

In order to give further impetus to facilitation and monitoring of investment, as well as for better coordination of infrastructural requirements for industry, a new cell called the Investment Promotion and Infrastructure Development Cell has been created. The functions of the Cell are:

1) Dissemination of information about investment climate in India;

2) Investment facilitation;

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3) Developing and distributing multimedia presentation material and other publications;

4) Organising Symposiums, Seminars, etc. on investment promotion;

5) Liaison with State Governments regarding investment promotion;

6) Documentation of single window systems followed by various States;

7) Match-making service for investment promotion;

8) Coordination of progress of infrastructure sectors approved for investment/technology transfer, power, telecom, ports, roads, etc.;

9) Facilitating industrial model town projects, industrial parks, etc.

10) Promotion of private investment including foreign investment in the infrastructure sector;

11) Compilation of sectoral policies, strategies and guidelines of infrastructure sectors, both in India and abroad; and

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12) Facilitating preparation of a perspective plan on infrastructure requirements for industry.

### 2.6.6 *Project Monitoring Wing*

Project Monitoring Wing, created within the IP&ID cell in June 1998, has now been functioning under Foreign Investment Implementation Authority Section with effect from 27/7/2001. The functions of Project Monitoring Wing are as follows:

(i) Coordination with Central and State level Ministries/Departments concerned and related agencies for tracking and monitoring approved projects, and compilation and analyses such information;

(ii) Direct contact, wherever necessary, with entrepreneurs and updation of the information on projects, and provision of necessary assistance.

### 2.6.7 *Nodal Officers*

The Department of Industrial Policy and Promotion has identified officers at the Deputy Secretary/Director level as Nodal officers for facilitation of all matters relating to the industrial projects pertaining to a State. For large projects

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involving sizeable amount of FDI, officers have been identified in the Department of Industrial Policy and Promotion and other departments concerned (e.g. the Ministry to which the investment proposal pertains) and the State Government to act as contact officers so that these projects can be implemented within the time schedule. The officers of the Project Monitoring Wing remain in touch with the contact officers.

### 2.6.8 *Focus Windows*

The Department of Industrial Policy and Promotion has opened Country Focus Windows for countries with sizeable investment interest in India. At present, the Focus Window covers countries such as USA, Germany, France, Switzerland, Australia, Japan and Korea. For each focus window a senior officer in the Department provides facilitation and assistance.

## 2.7 Entry routes in India

### 1. As a foreign company

Foreign Company is one, which has been incorporated outside India and conducts business in India. These companies are required to comply with the provisions of the Companies Act, 1956.Foreign Company can set up Liaison, Project and Branch Offices in

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India. Such companies have to register themselves with Registrar of Companies (ROC) within 30 days of setting up a place of business in India. The foreign companies can deal in India in any of the following ways:

(1) By way of liaison offices:

One of the practices for foreign companies to enter the Indian markets is the setting up of a Liaison/Representative office. A Liaison office is not allowed to undertake any business activity in India and cannot therefore, earn any income in India. The role of such offices is, therefore, limited to collecting information about possible market opportunities and providing information about the company and its products to the prospective Indian Customers.

The opening and operation of such offices is regulated by the Foreign Exchange Management Act-1999 (FEMA). Approval from the Reserve Bank of India (RBI) is required for opening such offices. There are certain standard conditions imposed for operations of such offices :

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a) Expenses of such offices are to be met entirely through inward remittances of foreign exchange from the Head Office abroad.

b) Such offices should not undertake any trading or commercial activities and their activities should be limited to collecting and transmitting information between the overseas Head Office and potential Indian customers.

c) Such offices should not charge any commission or receive other income from Indian customers for providing liaison services.

Liaison/representative offices also have to file an annual activity certificate etc. from a Chartered Accountant to RBI.

Permission to set up such offices is initially granted for a period of 3 years and this may be extended from time to time.

(2) By way of project offices:

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Foreign Companies planning to execute specific projects in India can set up temporary project/site offices in India. For the purpose specific approval from the RBI is required for setting up a project office. Such approval is generally accorded in respect of projects of approved by appropriate authorities or where the projects are financed by Indian bank/Financial Institution or a multilateral/ bilateral international financial institution.

(3) By way of branch offices:

Government has allowed foreign companies engaged in manufacturing and trading activities abroad to set up Branch Offices in India for the following purposes:

a) To represent the parent company/ other foreign companies in various matters in India e.g. acting as buying/selling agents in India.

b) To conduct research work in the area in which the parent company is engaged

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c) To undertake export and import trading activities

d) To promote possible technical and financial collaborations between the Indian companies and overseas companies.

e) Rendering professional or consultancy services

f) Rendering services in Information technology and development of software in India.

g) Rendering technical support to the products supplied by the parent/ Group companies.

A branch office is not allowed to carry out manufacturing, processing activities directly/indirectly. Branch Office will have to submit activity certificate from a Chartered Accountant on an annual basis to Reserve Bank of India. For annual remittance of profit Branch Office may submit required documents to authorised Bank. Permission for setting up branch offices is granted by the Reserve Bank of India on a case-to-case basis. RBI

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normally, considers the operating history of the applicant company worldwide and its proposed activities in India for granting the approval.

2. As an Indian company

A foreign company can commence operations in India through incorporation of a company under the provisions of the Indian companies Act, 1956. Foreign equity in such Indian companies can be up to 100% depending on the business plan of the foreign investor, prevailing investment policies of the Government and receipt of requisite approvals. For registration as an Indian company and its incorporation, an application has to be filed with Registrar of Companies (ROC). Once a company has been duly registered and incorporated as an Indian company, it will be subject to same Indian laws and regulations as applicable to other domestic Indian companies.

3. By way of joint venture with Indian partner

Foreign Companies can set up the operations in India by forgoing strategic alliances with Indian partners. Setting up of operations

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through a joint venture may entail the following advantages for a foreign investor

(a) Established distribution/ marketing set up of the Indian partners.

(b) Available financial resource of the Indian partner.

(c) Established contacts of the Indian partner, which help smoothen the process of setting up of operations.

Foreign investments are approved through two routes:

(a) Automatic route:

Indian companies can issue shares under the automatic route up to 100% of their paid capital except for those engaged in certain sector. In certain other sector, the foreign investment is limited to a prescribed percentage ceiling. A company eligible to issue shares under the Automatic Route can receive foreign inward remittance and issue shares without obtaining any prior approval subject to certain reporting requirements.

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(b) Government approval:

All other cases where the automatic route is not applicable require prior specific approval from the Foreign Investment Promotion Board.

4. By wholly owned subsidiary (WOS)

Foreign companies may set up a wholly owned subsidiary, which is an Indian Company with an independent legal status, distinct from the parent foreign company. Under the current foreign investment policy, a wholly owned subsidiary can be established either under the automatic route, if the conditions specified therein are complied with or obtain an approval from the Foreign Investment Promotion Board. Applications for establishment of wholly owned subsidiaries other than those where automatic route is available are approved by the Foreign Investment Promotion Board on a case to case basis, taking into account factors such as credentials of the foreign parent, nature of the industry, export commitments, whether proprietary technology is sought to be protected or sophisticated technology is proposed to be brought in, etc.

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5. By 100% Export Oriented Unit or investment in Export Processing Zones

In order to encourage exports, the Government of India offers special incentives to investors to set up units to manufacture goods for exports. Such units may be set up in Export Processing Zones (EPZs) or may be 100 per cent Export Oriented Units (EOUs) outside EPZs. 100 per cent foreign equity is welcome in EOUs andEPZs.

The EPZs are designed to provide an internationally competitive duty free environment at low cost for export production. Each zone provides basic infrastructure and facilities like developed land, standard design factory buildings, roads, power, water supply and drainage and customs clearance facilities. While EOUs adopt the same regime as an EPZ, it offers a wider option in project location with reference to sourcing of raw materials, port of export, availability of technological skill, existence of an industrial base and the need for a larger area of land for the project. Applications for the approval of EOU/ EPZ units are to be addressed to the Development Commissioners of Export Processing Zones in the case of EPZs and to the SIA in the case of EOUs.

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Additional incentives are offered to units engaged in the field of electronics and software which can be set up under the Electronic Hardware Technology Park or Software Technology Park programmes.

The incentives for EPZs and EOUs are as follows:

- Exemption from customs duty on industrial inputs.
- No import licences required.
- Supplies from the Domestic Tariff Area to EOUs/EPZ units regarded as deemed exports and hence exempt from payment of excise duty.
- Exempted from payment of corporate income tax for ten consecutive years. Export earnings exempt from tax even after the tax holiday is over.

Current budget provides for EPZs being converted into free trade zones from July 1, 1999.

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6. Investment in Special Economic Zones (SEZs)

Special Economic Zone (SEZ) is a specifically delineated duty free enclave and shall be deemed to be foreign territory for the purposes of trade operations and duties and tariffs.

Goods going into the SEZ area from DTA shall be treated as deemed exports and goods coming from the SEZ area into DTA shall be treated as if the goods are being imported.

SEZ units may be set up for manufacture of goods and rendering of services, production, processing, assembling, trading, repair, remaking, reconditioning, re-engineering including making of gold/ silver/platinum jewellery and articles thereof or in connection therewith.

SEZ units may export goods and services including agro-products, partly processed jewellery, sub-assemblies and component. It may also export by-products, rejects, and waste scrap arising out of the production process.

SEZ unit may import without payment of duty all types of goods, including capital goods, as defined in the Policy, whether new or second hand, required by it for its activities or in connection therewith, provided they are not

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prohibited items of imports in the ITC (HS). The units shall also be permitted to import goods required for the approved activity, including capital goods, free of cost or on loan from clients.

SEZ units may procure goods required by it without payment of duty, from bonded warehouses in the DTA set up under the Policy.

SEZ may import, without payment of duty, all types of goods for creating a central facility for use by software development units in SEZ. The central facility for software development can also be accessed by units in the DTA for export of software.

Gem & Jewellery and Jewellery units may also source gold/ silver/ platinum through the nominated agencies.

SEZ units may also import/procure from DTA specified goods without payment of duty and subject to such conditions, as may be notified by the Government, for setting up of units in the Zone.

SEZ unit may, on the basis of a firm contract between the parties, source the capital goods from a domestic/foreign leasing company. In such a case the SEZ unit and the domestic/

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foreign leasing company shall jointly file the documents to enable import/procurement of the capital goods without payment of duty.

SEZ unit shall be a positive net foreign exchange earner. Net Foreign exchange Earning (NFE) shall be calculated cumulatively for a period of five years from the commencement of commercial production.

The performance of SEZ units shall be monitored by a committee comprising of Development Commissioner and Customs. The Committee shall be headed by the Development Commissioner. It will also see that the wastage/manufacturing loss on gold/silver/platinum jewellery and articles are within the overall percentage prescribed. In case of higher wastage/ manufacturing loss, the committee shall satisfy itself of the reasonableness of the same.

All activities of SEZ units, unless otherwise specified, shall be through self certification procedure.

The unit shall execute a legal undertaking with the Development Commissioner concerned and in the event of failure to achieve positive foreign exchange earning it shall be liable to penalty in terms of the legal undertaking or under any other law for the time being in force.

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Applications for setting up of SEZ units, satisfying the conditions mentioned in paragraph 9-A.19 of the Handbook (Vol.1) may be given approval by the concerned Development Commissioner of SEZ. In other cases, approval may be granted by the Board of Approvals (BOA) set up for this purpose.

SEZ unit may sell goods, including by-products, and services in DTA in accordance with the import policy in force, on payment of applicable duty.

DTA sale by service/Trading units shall be subject to achievement of positive NFE cumulatively.

The following supplies affected in DTA by SEZ units will be counted for the purpose of fulfilment of positive NFE:

i. Supplies effected in DTA in terms of paragraph 10.2 of the Policy;

ii. Supplies made to bonded warehouses set up under paragraph 11.14 of the Policy and/or under Section 65 of the Customs Act.

iii. Supplies to other EOU/EPZ/SEZ/EHTP/STP units provided

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that such goods are permissible for procurement by such units in terms of paragraph 9.2 and paragraph 9-A.2 of the Policy.

iv. Supplies against special entitlement of duty free import of goods

v. Supplies of goods to defence and internal security forces, foreign missions/diplomats provided they are entitled for duty free import of such items in terms of general exemption notification issued by the Ministry of Finance.

Supplies from the DTA to SEZ units will be regarded as 'deemed exports' and, besides being eligible for the relevant entitlements under paragraph 10.3 of this Policy, will be eligible for the following:

I. Reimbursement of Central Sales Tax;

II. Exemption from payment of Central Excise Duty on all goods eligible for procurement as per paragraph 9.A.2 of the policy.

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III. Discharge of export performance (EP), if any, on the supplier.

IV. Reimbursement Central Excise Duty, if any, paid on bulk tea procured by EOU/EPZ units so long as levy on bulk tea in this regard is in force.

V. Reimbursement Duty paid on fuels or any other goods procured from DTA as per the rate of drawback notified by the Directorate General of Foreign Trade from the date of such notification.

SEZ units shall, on production of a suitable disclaimer from the DTA suppliers, be eligible for obtaining the entitlements specified in paragraph 10.3 (b) and (c) of the Policy. For the purpose of claiming entitlements at paragraph 10.3 (b), they shall get Brand Rates Fixed by the DGFT wherever All Industry Rates of Drawback are not available. Such supplies would, however, be eligible for entitlements specified in paragraph (I) above.

Supplier of cut and polish diamonds, precious and semi-precious stones, synthetic stones

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and processed pearls from Domestic Tariff Area to the units situated in SEZ shall be eligible for grant of Replenishment Licenses at the rates and for the items prescribed.

An SEZ unit may also export goods manufactured by it through a merchant exporter/ status holder recognised under this Policy or any other EOU/EPZ/SEZ/ EHTP/STP unit.

Transfer of manufactured goods, including partly processed/semi-finished goods from one SEZ unit to another SEZ/EOU/EPZ/ EHTP/STP unit will be allowed.

Goods imported/procured by an SEZ unit may be transferred or given on loan to another SEZ/EOU/EPZ/EHTP/STP unit which shall be duly accounted for, but not counted towards discharge of export performance.

SEZ unit, may subcontract a part of their production or production process through units in the DTA or through other SEZ/EOU/EPZ/EHTP/STP with the permission of Customs authorities. Subcontracting of part of production process may also be permitted abroad with the approval of the Board of Approval.

Subcontracting by SEZ gems and jewellery units shall be subject to following conditions :-

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I. Goods, finished or semi-finished, including studded jewellery, containing quantity and purity equal to the gold/ silver/platinum so taken out, shall be brought back to the Zone within 30 days. Further, no diamond, precious or semi-precious stones shall be allowed to be taken out of the Zone for sub-contracting.

II. Receive plain gold/silver/platinum jewellery from DTA in exchange of gold/silver/platinum of equal quantity and purity.

III. SEZ units shall not be eligible for wastage or manufacturing loss against the jewellery received from DTA after processing as mentioned in (i) and against exchange of gold/silver/platinum as mentioned in (ii).

IV. The DTA unit undertaking job work or supplying jewellery against exchange of gold/silver/platinum shall not be entitled to deemed export benefits.

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V. All units, including gem and jewellery, may sub-contract part of the production or production process through other units in the same SEZ without permission of Customs authorities subject to records being maintained by both the supplying and receiving units.

VI. SEZ units other than gems and jewellery units may be allowed to undertake job-work for export, on behalf of DTA exporter, provided the finished goods are exported direct from SEZ units. For such exports, the DTA units will be entitled for refund of duty paid on the inputs by way of Brand Rate of duty drawback.

VII. Scrap/waste/remnants generated through job work may either be cleared from the job worker's premises on payment of applicable duty or returned to the unit.

SEZ unit may be debonded with the approval of the Development Commissioner. Such debonding shall be subject to payment of applicable Customs and Excise duties on the imported and indigenous capital goods, raw materials etc. and finished goods in stock. In

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case the unit has not achieved positive NFE, the debonding shall be subject to penalty, that may be imposed by the adjudicating authority under Foreign Trade (Development and Regulation) Act, 1992.

SEZ unit may also be permitted by the Development Commissioner, as one time option, to debond on payment of duty on capital goods under the prevailing EPCG Scheme, subject to the unit satisfying the eligibility criteria of that Scheme and standard conditions.

SEZ gem and jewellery units shall be entitled for the following:

I. Export gold/silver/platinum jewellery and articles thereof for holding/ participating in exhibitions abroad with the permission of Development Commissioner.

II. Personal carriage of gold/ silver/ platinum jewellery, precious, semi-precious stones, beads and articles.

III. Export of jewellery, including branded jewellery is also permitted for

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display/sale in the permitted shops set up abroad.

IV. Display/sell in the permitted shops set up abroad or in the show rooms of their distributors/agents.

V. Set up show rooms/retail outlets at the International Airports for sale of plain and studded jewellery to foreign tourists.

Personal carriage of gems and jewellery export parcels by foreign bound passengers and personal carriage of gems and jewellery import parcels by an Indian or foreign national may be permitted as per the conditions prescribed.

Gold/silver/platinum jewellery and articles thereof may be exported by airfreight or through Foreign Post Office or through courier.

Rejects/scrap/waste/remnants arising out of production process or in connection therewith may be sold in the DTA on payment of applicable duty. No duty shall be payable in

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case scrap/waste/ remnants/ rejects are destroyed within the Zone after intimation to the Custom authorities or destroyed outside the SEZ with the permission of Custom authorities.

SEZ will be under the administrative control of the Development Commissioner.

A SEZ may be set up in the public, private, joint sector or by state Government as notified by the Ministry of Commerce and Industry. The existing Export Processing Zones (EPZs) may also be converted into SEZ by the Ministry of Commerce and Industry through issue of a notification.

SEZ units may, on the basis of records maintained by them, and on prior intimation to Customs authority:

I. Supply or sell samples in the DTA for display/market promotion on payment of applicable duties;

II. Remove samples without payment of duty, on furnishing a suitable undertaking to Customs authorities for bringing the good back within a stipulated period;

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III. Export samples, including through courier agencies. Samples made in wax models, silver models and rubber moulds may also be exported.

In case an SEZ unit is unable, for valid reasons, to utilize the goods, including capital goods and spares, it may dispose them in the DTA in accordance with the import policy in force and on payment of applicable duties or export them.

Capital goods and spares that have become obsolete/surplus may either be exported or disposed of in the DTA on payment of applicable duties. The benefit of depreciation, as applicable, will be available in case of disposal in DTA.

No duty shall be payable if the goods are destroyed with the permission of Customs authorities

SEZ unit may be allowed by Customs/Central Excise authorities concerned to donate imported/ indigenously procured computer and computer peripherals, including printer, plotter, scanner, monitor, key-board and storage units without payment of duty, two years after their import/procurement and use by the units, to recognized non-commercial educational institutions, registered charitable

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hospitals, public libraries, public funded research and development establishments, organisations of the Government of India or Government of a State or Union Territory as per Custom/ Central Excise notification issued in this regard.

Developer of SEZ in the Private/Joint/State sector may import/ procure from DTA specified goods without payment of duty and subject to such conditions as may be notified by the Government for the development of SEZ.

SEZ developer shall be eligible for various entitlements as provided for in the Income Tax Act for developing SEZ.

An existing EPZ unit will have the following options:

(a) It can opt for SEZ Scheme under this Chapter. On conversion, its previous obligations as an EPZ unit shall be subsumed by its obligations under the SEZ Scheme. The raw materials, components, consumable and finished goods lying in stock with the unit at the time of conversion shall be taken as its opening balance under the SEZ Scheme. All un-utilised DTA

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sale entitlements of the unit shall cease to exist from the date of conversion as notified by the Ministry of Commerce and Industry

(b) In case an existing EPZ unit decides not to opt for (a) above, it can either convert into an EOU or de-bond. In both the cases, the unit shall physically move out of the SEZ.

## 2.8 Sectoral Investment Policy of Government of India

### 2.8.1 *Biotechnology Sector*

The setting up of a separate Department of Biotechnology (DBT) under the Ministry of Science and Technology in 1986 has given a new impetus to the development of modern biology and biotechnology in India. In more than a decade of its existence, the department has promoted and accelerated the pace of development of biotechnology in the country.

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In India, concerted efforts for over a decade in R&D in the identified areas of modern biology and biotechnology have paid rich dividends. The proven technologies at the laboratory level have been scaled up and demonstrated in field. Patenting of innovations, technology transfer to industries and close interaction with them have given a new direction to biotechnology research.

Necessary guidelines for transgenic plants, recombinant vaccines and drugs have also been evolved. A strong base of indigenous capabilities has been created.

The following are the main opportunities available for investment in the biotechnology sector:

I. Biotechnology industry serves as a research arm to Agritech, and Pharma industry which increases potential for strategic alliances

II. Global trends show that all large pharmaceutical players are putting their money in healthcare for long term benefits. It is expected that nearly half the drugs in the next decade would be biotech products

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III. Tremendous potential in agri business in Indian economy.

IV. Potential therefore for transgenic seeds, bio-fertilizers, etc.

V. Number of small firms is high, knowledge based, research intensive industry, with low capital requirements

**Past consumption of Biotech products in India and future consumption estimates (US $ million)**

| No. | Particulars of Biotech sub-sectors | Actual Consumption 1999 | Future Consumption Estimate 2005 | Future Consumption Estimate 2010 |
|---|---|---|---|---|
| 1. | Human & Animal Health care Products | 670.41 | 821.40 | 1708.49 |
| 2. | Agriculture (including seeds) | 533.79 | 671.62 | 1437.80 |

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| | | | | |
|---|---|---|---|---|
| 3. | Industrial Products | 563.32 | 662.79 | 978.81 |
| 4. | Other Biotech Products | 21.62 | 30.23 | 145.02 |
| Total | | 1789.14 | 2186.04 | 4270.12 |

Source: Confederation of Indian Industry, New Delhi

The field of biotechnology both for new innovations and applications would form a major research and commercial endeavour for socio economic development in this decade.

### 2.8.2 *Information Technology Sector*

A separate Ministry of Information Technology has been established by the Government on October 15, 1999. The IT Ministry will be primarily responsible for all policy legislation relating to information technology, knowledge based industries, internet, e-commerce and IT education and IT - based education and development of electronics, computers and creation of Silicon valleys in India.

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Information Technology Act 2000 has been enacted. This Act provides a legal framework for recognition of electronic contracts, prevention of computer crimes, electronic filling of documents etc. It also amends certain related laws to provide a fully sufficient legal environment for conduct of business in cyberspace. A Cyber Controller would control the digital signature mechanism and the entire law implementation.

The main features of investment policy with regard to information technology sector are as follows:

1. Automatic route for foreign equity up to 100 percent in software and electronics, except aerospace and defence

2. 100 percent foreign investment permitted in units set up exclusively for exports. Such units can be set up under any one of the following schemes, namely Electronic Hardware Technology Parks (EHTPs), Software Technology Parks (STPs), Free-Trade Zones/Export Processing Zones (EPZs) and 100 percent Export Oriented Units (EOUs)

3. A number of states have developed their own IT policy to promote the development of software sector.

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4. Tax holiday up to 2010 for IT units to be set up in Software Technology Parks

5. Tax holiday to R&D for up to 10 years with 125% tax concession

6. IT venture capital fund set up

7. Simplification and liberalisation of Export & Import Policy

According to a recent World Bank study, India is the preferred location for software vendors for its quality and cost. Recognizing the special advantages and opportunities in India, many leading IT multinationals have set up operations in India. India has a strong Unix base, which provides opportunities for the development of products for Internet based applications. Further, India has global connectivity with international dialling facility from over 13,220 locations. Leased/switched high-speed data links from major centres through STPs and VSNL for point-to-point communication are also available. Internet connectivity is provided through several networks. Market openings have emerged across four business sectors – IT services, Software products, IT enabled services and E-business. By March, 2001 end the combined turnover of the IT and software services companies in India would have touched almost US $ 10 billion with exports touching US $ 6.24 billion and profits expected to

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continue and also to increase by more than 30% year on year. The software exports are expected to grow to US$ 50 billion by 2008.

Abundant investment opportunities exist in the following thrust areas in India:

I. Satellite-based Communication

II. Communication Infrastructure

III. Gateways

IV. Wireless

V. Software Development

VI. IT-enabled Services

India has the following advantages software sector

a) Education (100,000 post-graduate professionals in IT required annually by 2004)

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b) IT-enabled education

c) Optic Fibre Cable networks

d) Data Centers & Server Firms

e) 38% of e-commerce start-ups of 1999 in Silicon Valley by Indians

f) 50 portals being launched in India every month

g) 15 out of 23 SEI Level 5 companies worldwide are Indian

h) 170 Indian software companies have already acquired quality certification: ISO 9000/SEI

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i) Large pool of software professionals, proficient in English

j) A software and computing services sector with the highest compounded growth rate globally for the last five years in a row.

k) Economic and political stability.

### 2.8.3 *Oil & Natural Gas Sector*

The Indian government has announced significant policy initiatives to attract foreign investment:

Indian oil and gas fields are open for investment by the domestic private and foreign entrepreneurs under the framework of the New Exploration Licensing Policy (NELP) set out by Government of India in 1998. In the first round of offer under NELP, 24 blocks have been awarded and production-sharing contracts signed. Bids offered in the second round under NELP is being finalised for another 25 blocks including deep-water blocks. The process for the third round of offer of blocks is under preparation. The first round of offer of seven Coal Bed Methane (CBM) blocks has been

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launched in April 2001. FDI is permitted up to:

I. 100% in discovered small sized fields through competitive bidding

II. 60% for unincorporated joint ventures and 51% for incorporated joint ventures in medium sized fields

Refining Industry has been delicensed. The demand for petroleum products is estimated to grow at annual rate of around 6% to reach the level of 370 million tonnes per annum in 2025. The total investment in refining is estimated at around US$ 60 billion by 2025. The investment in marketing infrastructure during the above period is estimated to be around US$ 32 billion. Tremendous opportunity for investment exists in these sectors in the years to come in which the private sector including the foreign companies can set up their own projects or through joint ventures with public sector companies.

The refining sector is open to the joint sector (public-private partnerships) as well as to the private sector for new refineries. FDI participation up to 26% is permitted, with 26% to be held by public sector undertaking and balance 48% to be held by the public. In case of private Indian company, Foreign Direct Investment is permitted up to 100%.

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For petroleum products and pipeline sector, FDI is permitted up to 51%.

Subject to the policy laid down by Government, marketing of transportation fuels (viz. MS, HSD, ATF) can be permitted to a company investing or proposing to invest at least Rs. 2000 crore in exploration, refining, pipelines or terminals in the oil and gas sector of India.

FDI is permitted up to 74% in infrastructure related to marketing and marketing of petroleum products.

FDI upto 100% is permitted for purpose of market study and formulation, and for investment/financing

For actual trading and marketing, minimum 26% Indian equity is required over 5 years Opportunities.

For actual trading and marketing, minimum 26% Indian equity is required over 5 years.

**Expected demand for natural gas in India**

| Year | Demand (MMSCMD) |
|---|---|
| 1999 | 110 |
| 2002 | 151 |

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| | |
|---|---|
| 2007 | 231 |
| 2012 | 313 |
| 2025 | 391 |

MMSCMD = Million Standard Cubic Metres per Day.

The present domestic gas supply is only 65 MMSCDM. The increasing demand supply gap is expected to be met by imports of LNG and pipeline gas.

**Expected/Required infrastructure for natural gas**

| **Particulars** | **1988-99** | **2024-25** |
|---|---|---|
| Product Pipe lines capacity (MMT per annum) | 28.55 | 166 |
| Port Capacity (MMT) | 111 | 361 |

In the refining sector, opportunities exist for investment in public sector oil companies that are

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divesting their equity to the public. Additional refining capacity of over 40 million tonnes per annum has been installed in the last year, there is scope for further installation of 40 million tonnes per annum to meet India's estimated domestic petroleum products demand of 148.9 million tonnes per annum in 2010.

This sector offers the following opportunities for FDI participation:

I. LNG production and marketing/import terminals

II. Regional Gas trade from West, North & South/ South East Asia

III. Development of non-conventional sources like Shale oil, Coal bed methane, Gas hydrates.

IV. Refineries

V. Pipeline network.

### 2.8.4 *Pharma & Chemicals Sector*

The drug policy is aimed at ensuring abundant availability of essential and life saving drugs of quality at reasonable prices, in addition to strengthening the indigenous production base:

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- Control of prices is achieved through the Drug Price Control Order, 1995 wherein 74 bulk drugs are price controlled. The number of drugs under price control is being gradually reduced.

- Industrial licensing has been abolished except for production of products of recombinant DNA technology, bulk drugs requiring in-vivo use of nucleic acids as active principal and specific cell/tissue targeted drug formulations.

- FDI up to 100% is permitted on the automatic route for manufacture of drugs and pharmaceuticals, provided the activity does not attract compulsory licensing or involve use of recombinant DNA technology and specific cell/tissue targeted formulations. FDI proposals for the manufacture of licensable drugs and pharmaceuticals and bulk drugs produced by recombinant DNA technology, and specific cell/tissue targeted formulations will require prior Government approval.

Growth reflected by the Indian pharmaceutical industry in terms of infrastructure development, technology base and the range of production is tremendous. The industry's strength lies in world-class technology, cost effective production of 90 percent of bulk drugs and all required formulation, rich bio-diversity, competitive R&D

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costs and over 20 percent growth rate in exports. With an increasing number of bulk drugs going off patent, and the capability of Indian scientists in process technology, the share of Indian pharma products in world market is expected to rise further.

The technological strengths of India in the pharmaceutical sector are derived form:

I. Production of 90 percent of bulk drugs and almost the entire range of formulations

II. Self reliant technology for production

III. Innovative scientific manpower

IV. Low R&D costs

V. Low cost drug formulating for national health progress

VI. Strength of national laboratories

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VII. Several MNCs conducting clinical trials in India

The well-established Indian chemicals industry produces a wide range of products of including organic and inorganic chemicals, dyestuffs, paints, pesticides and speciality chemicals. The industry has withstood the vagaries of the international market and has continuously augmented its exports.

In the petrochemicals sector India has maintained a 15% growth rate and given the per capita consumption, the scope for further growth is immense. World-class plants have been set up in a record time. India will play an important role in the Asian region.

The chemical sector together accounts for over 10% of the total Indian exports. With its established expertise in the IT sector, with focused attention on R&D and its ability to produce high quality products at globally competitive prices, India will play a crucial role in the knowledge based industries in the coming years.

### 2.8.5 *Power Sector*

The Government's power sector policy seeks to attract significant private sector investment in the Indian power sector. Key initiatives include:

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I. Private sector permitted to set up coal, gas or liquid based thermal projects, hydel projects and wind or solar projects of any size

II. Foreign equity participation upto 100% in the power sector has been brought under automatic route

III. Role of the Central Government is minimal and the State Government and State Electricity Boards (SEBs) are empowered to negotiate directly with developers, facilitating speedy clearances for the investor

IV. Ancillary sectors such as coal have been significantly deregulated

V. The State Electricity Boards of Orissa, Haryana, Andhra Pradesh, Uttar Pradesh, Karnataka and Rajasthan have been unbundled/corporatised. Fourteen States (Orissa, Haryana, Andhra Pradesh, Uttar Pradesh, Delhi, West Bengal, Maharashtra, Karnataka, Himachal Pradesh, Gujarat, Punjab, Arunachal Pradesh, Rajasthan and Tamil Nadu) have constituted/notified

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constitution of State Electricity Regulatory Commission.

Demand of electricity is expected to grow to 570 billion KwH by 2001-02 and to 782 billion KwH by 2006-07. During 10th Plan (2002-2007) & 11th Plan (2007-2012), a total capacity addition of 1,13,000 MW is envisaged, entailing an investment of Rs.5, 750 billion in power generation, transmission and distribution. The installed capacity of power generation in the country as on December 31, 2000 has crossed 1,00,136 MW.

In power generation, a number of projects have been identified as Mega Power Projects. Power Trading Corporation (PTC) has been incorporated, for the purpose of buying power from mega power projects under long-term Power Purchase Agreements (PPAs) and selling the power to the beneficiary states also under long-term PPAs. Transmission projects for power transfer area available for competitive bidding by the Central Transmission Utility (Power Grid) and State Transmission Utilities (SEBs/Grid Corporations). The transmission system projects are being identified for competitive bidding by the Central and State Transmission Utilities.

Liquid Fuel Based Projects using Low Sulphur Heavy Stock (LSHS), Furnace Oil (FO), Heavy Petroleum Stock (HPS), Naphtha, Vacuum Residue, Condensate and Orimulsion are permitted

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by the Government. Import of liquefied natural gas (LNG) is also being considered for setting up large capacity combined cycle power plants.

Attractive investment opportunities are likely to develop in distribution of power as several State governments have agreed to allow the gradual entry of the private sector in distribution.

**Opportunities in non-conventional energy resources**

| **Resource** | **Units** | **Potential** | **Harnessed till July 2000** |
|---|---|---|---|
| Wind Power | MW | 20,000 | 1167.01 |
| Small Hydro Power | MW | 10,000 | 217 |
| Bagasse co-generation | MW | 3,500 | 222 |
| Biomass and gasificati | MW | 17,000 | 34.36 |

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| on | | | |
|---|---|---|---|
| Biogas Plants | Milli on | 12 | 3 |
| Improved Cooking Stoves | Milli on | 120 | 31.35 |
| Solar Photovolt aic Systems | | 20 MW/Sq. km | Only 42 MW |

Areas for FDI participation:

I. Generation, Transmission and Distribution

II. 78% Hydro potential to be harnessed

III. Shelf of generation projects identified

IV. Convergence of Transmission, Telecom and Information Technology

V. Renovation and Modernisation

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VI. Cross Country Grids

VII. Efficiency improvement in generation

VIII. Reduction of T&D losses: Energy Audit / metering

IX. Energy Conservation and Demand Side Management.

### *2.8.6 Roads*

Government initiatives for promotion of this key infrastructure sector include:

I. Automatic route available for foreign equity participation up to 100 per cent (not exceeding Rs.15 billion) for investment in the roads sector.

II. Private parties allowed to develop service and rest areas along the roads entrusted to them.

III. The National Highways Authority of India (NHAI) is permitted to participate in equity in Build Own Transfer (BOT) projects up to 30 percent.

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IV. Investors in identified highway projects permitted to recover investment by way of collection of tolls for specified sections and periods.

V. 10 years of Corporate Tax Holiday to be availed in 20 years of commission of the project.

VI. Investments worth an estimated US$ 34 billion needed, till 2005-06, for the development of National and State Highways. Of this figure, the requirement of private sector investment is US$ 8.3 billion.

Avenues for FDI participation:

I. Construction of highways, bridges, railway-over-bridge, elevated sections in urban areas, interchanges, bypasses, etc.

II. Highway related en route activities like restaurants, motels, and rest/parking areas as may by decided by the implementing agency.

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III. Four-laning of over 15,000 km of National Highways.

Select project opportunities:

I. Chennai-Nellore (US$350 million)

II. Bangalore-Chennai (US$305 million)

III. Surat-Manor (US$180 million), and

IV. Jaipur-Ajmer (US$147 million)

V. Feasibility studies, detailed project preparation & construction supervision

VI. Contracts range between US $ 50-200 million Investors

VII. BOT projects on BOT and Annuity basis

VIII. Participation in bonds and direct borrowings

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IX. State-of-the-art technology deployment

X. Construction equipment import.

### 2.8.7 *Telecom Sector*

Incentives for foreign collaborations coupled with an attractive trade and investment policy have made India an attractive market for telecom equipment suppliers and service providers.

No industrial license is required for setting up manufacturing units for telecom equipment.

In basic cellular, value added services and global mobile personal communications by satellite, FDI is limited to 49% subject to licensing and security requirements and adherence by the companies (who are investing and the companies in which the investment is being made) to the license conditions for foreign equity cap and lock in period for transfer and addition of equity and other license provisions.

For Internet Service Providers with gateways, radio-paging and end-to-end bandwidth, FDI is permitted up to 74% with FDI beyond 49% requiring Government Approval.

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No equity cap is applicable to manufacturing activities

FDI up to 100% is allowed for the following activities in the telecom sector:

I. ISPs not providing gateways (both for satellite and submarine cables);

II. Infrastructure providers providing dark fibre (IP Category 1);

III. Electronic Mail; and

IV. Voice Mail.

FDI up to 100% is allowed subject to the condition that such companies would divest 26% of their equity in favour of the Indian public in 5 years, if these companies are listed in other parts of the world.

The above services would be subject to licensing and security requirements, wherever required/ Proposals for FDI beyond 49% shall be considered by FIPB on case-to-case basis.

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Capital employed as well as dividend income of companies engaged in telecom sector is fully repatriable.

Areas for investment:

1. Internet Services:

   There is no restriction on the number of Internet Service Providers (ISPs). No license fee is payable up to October 31, 2003; thereafter a token license fee of Re 1 per annum is payable. ISPs are free to fix their own tariff. ISPs have been permitted to establish their own international gateways for carrying internet traffic. Internet Service Provider's (ISPs) licenses have been granted to about 380 companies, out of which 80 are already providing internet services.

   120 projects have been cleared for establishment of internet gateways in various parts of the country using satellite and submarine cable landing stations for international gateways for internet. The internet service is, thus, aiming towards fast proliferation of internet within the country and give boost to applications like e-commerce, web-hosting, virtual private networks, etc.

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2. National Long Distance Services:

As per the National Telecom Policy, 1999 (NTP), National Long Distance Service (NLD) has been opened to private sector. The license for NLD shall be granted to an Indian registered company. There will be no restriction on number of operators providing NLD service. A company seeking license for NLD service should have a minimum paid up capital of Rs 250 crores and the promoters of such company should have combined net worth of Rs 2,500 crores. The applicant company shall pay one time entry fee of Rs 100 crores and in addition, four bank guarantees of Rs 100 crores each, which will be released on fulfilment of the network roll obligations. The license shall be initially issued for a period of 20 years, extendable by 10 years. NLD Operator will be allowed to carry inter and intra circle long distance voice and date traffic.

In addition to the above, private participation is also permitted in setting up of infrastructure under NLD policy. Infrastructure providers (IP) has been divided into Category 1, who will provide infrastructure namely towers, buildings, dark fibre etc. and Category II, who will provide end-to-end bandwidth.

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3. Basic Telephone Services:

   Licenses have been issued to private companies for providing basic telephone services as the second operators for 6 circles. 15 circles are to be offered to private operators. Basic service providers are permitted to establish last mile linkages, carry their own long distance traffic (within their service are), provide direct interconnectivity and share infrastructure with other basic service providers. There exists large potential for providing telephone connections (estimated at 75 million by 2005 and 175 million by 2010).

4. Cellular Mobile Services

   Licenses have been awarded to 2 operators in each circle for cellular services. At present, 22 private companies provide cellular services in 18 circles and 4 metro cities. There are 6 slots for cellular services, which are to be offered to private operators.

5. Global Mobile Personal Communication by Satellite (GMPCS)

   There is no restriction on the number of GMPCS licenses and licenses are issued on first-cum-first-served basis. Gateways for GMPCS are to be located in India and operation and maintenance of the same is to

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be with an organisation designated by the Government.

6. Other value added services

As the telecommunications and Information Technology (IT) infrastructure in the country is expanding, there is a surge in demand for a range of value added services. The scheme for value added services have been considerably liberalised. These services include radio paging, public mobile radio trunking, and domestic data using VSATs. Evolving of new services – Tele education, Tele-medicine, Tele-banking, Call Centre – is catching up with the Indian industry and has recently witnessed significant investments from domestic and foreign investors.

### 2.8.8 *Civil Aviation Sector*

The monopoly of public sector air carriers ended with the repealing of the Air Corporation Act, 1953 on March 1, 1994. The government opened Indian skies for private and foreign investment. The following are the main aspects of that policy:

I. Automatic approval for foreign equity participation in airport infrastructure upto 100 percent.

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II. FDI upto 40% permitted subject to no direct or indirect equity participation by foreign airlines.

III. Investment by Non-Resident Indians upto 100 % permitted in domestic air-transport services.

IV. Up to 100% with FDI is allowed in Airports, beyond 74% requiring Government approval.

V. Equity from foreign airlines not allowed in domestic air-transport services either directly or indirectly.

VI. Foreign Financial Institutions allowed holding equity in the domestic air transport sector provided they do not have foreign airlines as their shareholders.

VII. Foreign investors allowed to have representation (upto 33 per cent of total) on Board of Directors of the domestic airline company.

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VIII. Government to consider private sector participation in construction and operation of new airports on a BOT basis.

IX. Minimum fleet size for a scheduled operator raised from the existing 3 aircraft to 5.

X. Management contract with a foreign airline is not permitted.

Opportunities offered by civilian sectors for FDI:

I. Construction of world class international airports in five cities, permitted upto 100% foreign equity investment announced

II. Important private sector aided projects: New airport near Kochi (US$ 85.7 million). Projects for development of new airports at Bangalore and Mumbai with private sector participation are under consideration

III. Other private sector aided airports planned : Ahmedabad airport, Amritsar airport

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upgradation, Chennai cargo complex, new international terminal and second runway for Delhi airport, runway extension and internation block for Jaipur airport

IV. Restructuring & privatisation through long term lease of aircrafts

V. Construction of Green-field airports

VI. Construction of terminal/facilities

VII. Ground handling

### 2.8.9 *Ports Sector*

The Indian Government has announced the following measures to promote foreign investment in the ports sector:

I. Foreign equity upto 100% is now permissible in construction and maintenance of ports and harbours and in projects providing support services to water transport, such as operation and

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maintenance of piers, loading and discharging of vehicles, under the automatic route.

II. FDI up to 51% is allowed on automatic basis in support services like operation and maintenance of piers and loading and discharging of vessels

III. Open tenders will be invited for private sector participation on a BOT basis

IV. Major ports have been permitted to form joint ventures with foreign ports, minor ports and other companies to attract new technology, better management practices, and implementation of development schemes and creation of optional port infrastructure

V. Two tier fiscal benefits has been provided under section 80IA of the IT Act

Opportunities for FDI:

Areas identified for privatisation or investment by the private sector include:

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I. Leasing out of existing port assets

II. Creation of additional assets such by:

a. Construction and operation of container terminals

b. Construction and operation of bulk, break bulk, multipurpose and specialised cargo berths

c. Warehousing, container freight stations, storage facilities and tank farms

d. Cranage and handling equipment

e. Setting up of captive power plants

f. Dry docking and ship repair facilities

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g. Leasing of equipment for port handing and leasing of floating crafts from the private sector

III. Pilotage

IV. Captive facilities for port based industries

V. Consultancies for:

i. efficient O&M practices in port management

ii. training for improved productivity

iii. safe and efficient vessel traffic management system.

### 2.8.10 *Food Processing Sector*

The main features of investment policy for FDI in food processing sector include:

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I. No industrial license required for almost all food and agro processing industries.

II. Automatic approval (including foreign technology agreements within specified norms) is now permitted for FDI upto 100 percent equity of Indian companies, for most products in the food sectors. Exceptions are malted foods, alcoholic beverages such as beer and items reserved exclusively for manufacture by the small-scale sector.

III. Foreign equity ownership of up to 24 percent is allowed in case of units manufacturing items reserved for small-scale sector beyond which a minimum export obligation of 50% of production shall apply.

IV. Food processing industry declared a priority area. New Exim Policy places greater thrust on Agro based Industries - exclusive Agro Export Processing Zones being set up.

V. Agro based 100% Export Oriented Units allowed sale up to 50% in domestic tariff area. Imports of capital goods and raw materials permitted at zero per cent duty.

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VI. Liberal corporate tax policy for exports earnings.

VII. Fruits and vegetables products completely exempt from Central Excise Duty.

VIII. 10 year tax holiday for Industrial Parks (having Food Processing activities) during initial 15 years.

IX. Import of food processing machinery allowed freely with low level of duties. Under Export Promotion Capital Goods (EPCG) Scheme with specific export commotions is only 5%.

X. Quantitative Restrictions on all food products removed. Customs duty on majority of the products at 35%.

XI. New Exim Policy places greater thrust on Agro based Industries - exclusive Agro Export Processing Zones being set up.

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Opportunities for FDI:

I. Need for US $ 28 billion of investment to raise food-processing levels by more than 8-10%

II. Large untapped domestic market of 1000 million which includes
(i) 250 Million upper middle class with growing purchasing power
(ii) 200 million more shift to processed packaged food by 2010

III. Food processing industry growing at the rate of @ 16 to 20%

IV. Locational advantage for exports to Middle East, South East Asia and CIS countries

V. The diverse agro-climatic conditions and a wide ranging and large raw material base suitable for food processing industries.

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Presently, a very small percentage of these products are processed into value added products

VI. Rapid urbanisation, increasing literacy and rising per capita income have all caused rapid growth and changes in the demand pattern, leading to several new opportunities for exploiting the large latent market. An average Indian spends about 50 per cent of household expenditure on food items

VII. Expenditure on mass-based, high volume, low margin basic foods such as wheat, wheat flour and homogenised milk is expected to increase substantially over the next few years

VIII. Popular foods like wheat flour and biscuits, packaged milk, fresh poultry and soft drinks are other areas where a strong growth is forecasted

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### 2.8.11 *Insurance, Banking & Financial Markets*

The main features of FDI policy as to investment in insurance, banking and financial markets include:

1. Direct Investment

   I. Foreign Investment in companies undertaking insurance, private sector banking and non-banking financial services is now under the automatic route

   II. 49 percent FDI allowed in private sector banking

   III. There are 182 branches of Foreign Banks in India and control 5 percent of the Market. Entry Norms for Private Sector Banks eased substantially

   IV. The following investment limits have been specified by the Government for FDI in an Indian company undertaking financial services activities:

      (a) Insurance business – Up to 49%

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(b) Insurance broking – Up to 49%

(c) Banking company – Up to 20% by foreign banking companies or finance companies including multilateral financial institutions

(d) Other specified non-banking financial services activities as per minimum capitalisation norms specified in this regard

2. Portfolio Investment

I. Foreign Institutional Investors (FIIs) registered with SEBI are permitted to invest in aggregate up to 24 percent of the paid-up capital of an Indian company. This 24 percent ceiling may be enhanced to 40 percent by the relevant Indian company, after obtaining prior approval of the Board of Directors and shareholders. Individual FII is permitted to invest up to 10 percent of the paid-up capital of an Indian company

II. NRIs/PIO/OCBs are cumulatively permitted to invest up to 10 percent of the

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paid up capital of an Indian company. This 10 percent ceiling could be enhanced to 24 percent by the relevant Indian company, after obtaining prior shareholder approval. Each NRI/PIO/OCB is permitted to invest up to 5 percent of the paid-up capital of an Indian company

III. The ceiling of 24/40 percent for FIIs is independent of the ceiling of 10/24 percent for NRIs/PIO/OCBs

Investment Incentives:

I. FIIs are subject to Indian taxes on capital gains and income in respect of securities, under a special tax regime.

II. As per the Finance Act, 2000 income of a venture capital company of fund registered with SEBI, is exempt from tax provided such income is derived from investment in a venture capital undertaking:

i. Whose shares are not listed on an Indian stock exchange.

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ii. Which is engaged in the business of providing services, or manufacture of any article or thing, other than those services or articles or thing notified by SEBI.

Opportunities for FDI

I. The Government is encouraging private sector participation in the insurance industry. The opening up of this industry offers tremendous opportunities for insurers, insurance intermediaries and other organisations connected with the industry

II. A broad investor base and a vibrant primary and secondary market provide opportunities for financial intermediaries and service providers

III. A large and rapidly growing consumer market of over 300 million people provide opportunities in retail banking and finance

IV. Increasing globalisation combined with domestic deregulation will create a demand for

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sophisticated financial products as well as innovative financing techniques

V. FII currently handle about a quarter of the Indian market turnover of around Rs.67 crore a day or Rs.2010 crore a month

VI. Internet based trading has made a foray and is growing

VII. Presently, Indian insurance market is one of the least insured markets in the world. It is ranked 57th among 60 countries. Per capita gross premium for a few selected countries are given below:

| Country | Gross Premium (per capita) (US $) |
|---|---|
| Thailand | 30 |
| Taiwan | 407 |
| South Korea | 732 |
| India | 5 |

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VIII. Doubling per capita gross premium can lead to mobilisation of US$ 8-9 billion of funds

IX. In India there are many unmet consumer needs. As the variety of insurance products and services available in other country markets are made available to the Indian consumer post liberalisation, there will be a rapid expansion in the type and level of life of various Insurance Coverage

X. As consumer needs are met, the per capita insurance will go up significantly

XI. Risks will be spread beyond the individual, community, economic sector and geographic area helping both Individuals and Industry.

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## 2.9 Investment by Non-resident Indian (NRI)/Person of Indian Origin (PIO)/Overseas Corporate Bodies (OCB)

### 2.9.1 *Non-resident Indian (NRI)*

"Non-Resident Indian (NRI) means a person resident outside India who is a citizen of India or is a person of Indian origin".

### 2.9.2 *Person of Indian Origin (PIO)*

For the purposes of availing of the facilities of opening and maintenance of bank accounts and investments in shares/securities in India Person of Indian origin means a citizen of any country other than Pakistan or Bangladesh, if

a) he at any time, held an Indian passport; or

b) he or either of his parents for any of his grand parents was a citizen of India by virtue of the constitution of India or Citizenship Act, 1955 (57 of 1995); or

c) the person is a spouse of an Indian citizen or a person referred to in clause (a) or (b)

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For investments in immovable properties, person of Indian origin means an individual (not being a citizen of Pakistan or Bangladesh or Afghanistan or Bhutan or Sri Lanka or Nepal or China or Iran)

- Who at any time, held an Indian passport or

- Who or either of whose father or whose grandfather was a citizen of India by virtue of the Construction of India or the Citizenship Act, 1955 (57 of 1955)

### 2.9.3 *Overseas Corporate Body (OCB)*

Overseas Corporate Bodies (OCBs) are bodies predominantly owned by individuals of Indian nationality or origin resident outside India and include overseas companies, partnership firms, societies and other corporate bodies which are owned, directly or indirectly, to the extent of at least 60% by individuals of Indian nationality or origin resident outside India as also overseas trusts in which at least 60% of the beneficial interest is irrevocably held by such persons. Such ownership interest should be actually held by them and not in the capacity as nominees. The various facilities granted to NRIs are also available with certain exceptions to OCBs so long as the ownership/beneficial interest held in them by NRIs continues to be at least 60%.

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### 2.9.4 *Facilities available to NRIs/OCBs*

NRIs/OCBs are granted the following facilities:

I. Maintenance of bank accounts in India.

II. Investment in securities/shares of, and deposits with Indian firms/ companies.

III. Investments in immovable properties in India.

### 2.9.5 *General permissions granted by RBI*

Reserve Bank has granted general permission to NRIs/PIOs, for undertaking direct investments in Indian companies, under the Automatic Route purchase of shares under Portfolio Investment Scheme, investment in companies and proprietorship/partnership concerns on non-repatriation basis and for remittances of current income. NRIs/PIOs do not have to seek specific permission for approved activities under these schemes.

The Reserve Bank of India has now further simplified financial transactions by NRIs/PIOs by granting general permissions to:

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I. To resident individuals, partnership/proprietorship concerns to avail of interest bearing rupee loans from NRIs/PIOs out of funds remitted by them from abroad or out of funds held in their bank accounts in India, on non-repatriation basis, subject to certain conditions one of them being that the rate of interest on such loans should not exceed Bank Rate plus two percentage points.

II. NRIs/PIOs to transfer by way of gift shares held by them in Indian companies and to transfer by way of gift immovable property held by them in India subject to compliance with other applicable rules/regulations including the provisions of Foreign Contribution Regulations Act, 1976 by the charitable trust/organisation concerned.

III. All domestic public/private sector mutual funds for issue of Units to NRIs/PIOs/OCBs on repatriation as well as non-repatriation basis.

IV. NRIs/PIOs/OCBs to place deposits wit Indian firms, on non-repatriation basis and wit Indian companies including Non-banking financial companies on repatriation and non-repatriation basis.

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V. NRIs/PIOs/OCBs for sale of shares acquired under direct investment Schemes on stock exchanges in India.

NRIs/PIOs/OCBs have been granted General Permission to invest in Government Securities and Treasury Bills.

Taking into account the facilities tat are already available, and the above new measures, NRIs/PIOs will not have to seek specific permission of the Reserve Bank for a whole variety of approved financial/investment transactions. This should considerably reduce paper work and time taken for undertaking such transactions.

After the above changes come into effect, the areas in which facilities available to NRIs/PIOs/OCBs will be the same as available to domestic residents except relating to investment by NRIs/PIOs/OCBs in real estate/agriculture and plantation business Chit Funds, Nidhis or Print Media.

### 2.9.6 *RBI forms for obtaining permission in case of investments not governed in General Permission schemes*

NRIs/OCBs/PIOs do not have to seek specific permission for approved activities covered under

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'General permission' schemes. The activities relating to NRIs/OCBs/PIOs not covered under those schemes either require declaration to RBI or permission from RBI. The activities requiring Declaration/Permission along with corresponding forms are as under;

TS 1 - Transfer of Shares/Debentures by Non-residents to Residents

FNC 1 - Permission to establish a branch office in India by an Overseas Company establishing a Representative Office by Overseas Company for Liaison Activities to open a Project/Site Office in India.

IPI - Company/Individual (declaration) acquiring property

### 2.9.7 *Bank accounts for NRIs/OBCs/PIOs*

NRIs/PIOs/OCBs/ are permitted to open bank accounts in India out of funds remitted from abroad, foreign exchange brought in from abroad or out of funds legitimately due to them in India, with authorised dealer.

Such accounts can be opened wit banks specially authorised by the Reserve Bank in its behalf [Authorised Dealer (AD)].

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There are five types of NRI accounts:

(1) Rupee accounts

(a) Non-Resident (External) Rupee Accounts (NRE Accounts)

NRIs, PIOs, OCBs are eligible to open NRE Accounts. These are rupee denominated accounts. Accounts can be in the form of savings, current, recurring or fixed deposit accounts. Accounts can be opened by remittance of funds in free foreign exchange. Foreign exchange brought in legally, repatriable incomes of the account holder, etc. can be credited to the account. Joint operation with other NRIs/PIOs is permitted. Power of attorney can be granted to residents for operation of accounts.

The deposits can be used for all legitimate purposes. The balance in the account is freely reportable. Interest lying to the credit of NRE accounts is exempt from tax in the hands of the NRI.

Funds held in NRE accounts may be freely transferred to FCNR accounts of the same account holder. Likewise, funds

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held in FCNR accounts may be transferred to NRE accounts of the same account holders.

(b) Ordinary Non-Resident Rupee Accounts (NRO Accounts)

These are Rupee denominated non-reportable accounts and can be in the form of savings, current recurring or fixed deposits. These accounts can be opened jointly with residents in India. When an Indian National/PIO resident in India leaves for taking up employment, etc. outside the country, his bank account in India gets designated as NRO account. The deposits can be used to make all legitimate payments in rupees. Interest income, from NRO accounts is taxable. Interest income, net of taxes is reportable.

(c) Non-resident (Non-reportable) Rupee Deposit Accounts (NRNR Accounts)

NRIs/PIOs/OCBs, other non-resident Individuals/entities are permitted to open these accounts. Accounts can be opened by transfer of freely convertible foreign currency funds from abroad, or from NRE/FCNR accounts. Deposits can be held jointly with a resident. Deposits can

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be for period from 6 months to 3 years, and can be renewed further. Accounts may also be opened by transfer of funds from the existing NRE/FCNR accounts of the non-resident accounts holders.

The principal is non-reportable; interest can be repatriated. There is no income tax on the interest.

(d) Non-Resident (Special) Rupee Accounts with banks in India

NRIs/PIOs presently have the facility of maintaining bank accounts and undertaking financial transactions in India subject to certain exchange control regulations.

In order to simplify the procedures and to provide greater freedom to NRIs/PIOs for putting through financial transactions in India, NRIs and PIOs are now permitted to open bank accounts in India, which will be at par with rupee accounts maintained by residents. They can now open Non-Resident (Special) Rupee Accounts with banks in India which will have the same facilities and restrictions as are applicable to rupee accounts maintained in India by

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residents relating to repatriation of funds held in these accounts and/or income/interest earned on them. The scheme, which has become effective from April 15, 1999 provides that the procedure for opening such accounts is the same as that of domestic accounts of resident individuals.

The existing facilities for NRIs/PIOs to maintain and operate Non-resident(Ordinary) i.e., NRO account, Non-Resident, i.e., FCNR account also continues. The repatriation facilities available under these accounts will continue as before.

(2) Foreign currency accounts

(a) Foreign Currency (Non -Resident) Accounts (Banks) (FCNR (B) Accounts)

NRIs/PIOs/OCBs are permitted to open such accounts in US Dollars, Sterling Pounds, Deutsche Marks, Japanese Yen and Euro. The account may be opened only in the form of term deposit for any of the three maturity periods viz; (a) one year and above but less than two years

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(ii) two years and above but leas than three years and (iii) three years only.

Interest income is tax free in the hands of NRI until he maintains a non-resident status or a resident but not ordinarily resident status under the Indian tax laws.

FCNR (B) accounts can also be utilised for local disbursements including payment for exports from India, repatriation of funds abroad and for making investments in India, as per foreign investment guidelines.

### 2.9.8 *Direct investment opportunities for NRIs/OCBs/PIOs*

NRIs & OCBs can invest in India as under:

I. Investment under Automatic Route with repatriation benefits

II. Investment with Government approval

III. Other investments with repatriation benefits

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IV. Investments up to 100% equity without repatriation benefits

V. Other investments by NRIs/OCBs without repatriation benefits.

1. Automatic route of RBI with repatriation benefits:

   NRIs/OCBs can invest in shares/convertible debentures of Indian companies under the Automatic Route without obtaining Government or RBI permission except for a few sectors where FIPB/SIA permission is necessary, or where the investment can be made only up to a certain percentage of paid up capital.

2. Investment with government approval:

   Investments not eligible under the Automatic Route, are considered by the Foreign Investment Promotion Board (FIPB) a high Powered inter-ministerial body under the chairmanship of Secretary, Department of Industrial Policy & Promotion, SIA, subject to sectoral limits/norms. These investments also enjoy full repatriation benefits.

3. Other investments with repatriation benefits:

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| | | |
|---|---|---|
| | 1. Investment in domestic mutual Funds<br>2. Investment in bonds issued by public sector undertakings<br>3. Purchase of shares of public sector enterprises<br>4. Deposits with companies (for a minimum period of three years)<br>5. Investment in government securities/shares | NRIs/OCBs are permitted to invest in the securities & deposits schemes with repatriation benefits. |
| 4. | Investment up to 100% equity without repatriation benefits: | |
| | 1. Capital contribution to any proprietary or partnership concern | NRIs can invest by way of capital contribution in any proprietary or partnership concern in India provided the firm or the proprietary concern is not engaged |

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| | in any agricultural/plantation activities or real estate business or Print Media on non-repatriation basis subject to the certain conditions. |
| 2. New issues of shares/debentures of indians companies | NRIs/OCBs as been ranted general permission to subscribe to the shares/convertible debentures of an Indian company on non-repatriation basis, and to an Indian company to issue shares or convertible debentures by way of new/rights/bonus issue to NRIs/OCBs on non-repatriation basis provided that the investee company is not engaged in agricultural/plantation activities or real estate business (excluding real estate development i.e. |

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development of property or construction of houses) or chit fund or is not a Nidhi company.

5. Other investments by NRIs/OBCs without repatriation benefits:

1. Investment in non-convertible debentures

2. Money market mutual funds

3. Deposits with companies

4. Commercial papers

*2.9.10 Portfolio investment by NRIs/OBCs/PIOs*

NRIs/OCBs are permitted to make portfolio investment in shares/debentures (convertible and non-convertible) of Indian companies, wit or without repatriation benefit provided the purchase is made through a stock exchange and also through designated branch of an authorised dealer. NRIs/OCBs are required to designate only one

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branch authorised by Reserve Bank for this purpose.

General conditions for purchase with repatriation of non-repatriation rights:

I. Investment in equity shares and convertible debentures is permitted subject to an overall ceiling of (a) 10 per cent of the total paid-up equity capital of the company concerned; and (b) 10 per cent of the total paid-up value of each series of the convertible debentures issued by the company concerned for all NRIs/OCBs taken together both on repatriation and on non-repatriation basis.

II. The purchase of shares and debentures under the scheme is required to be made at the ruling market price.

III. Indian companies listed on recognised stock exchanges in India are however permitted to allow NRIs/OCBs to acquire shares/debentures up to 24% instead of the 10% limit after a resolution in General Body and necessary information to RBI.

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Investment on non-repatriation basis

NRIs/OCBs intending to invest on non-repatriation basis should submit the application in form NRI and NRC respectively, to a designated branch of an authorised dealer. Authorised Dealer will grant general permission to purchase shares/debentures to NRI/OCB subject to the condition that the payment for such investment is received through inward remittance or from the investor's NRE/FCNR/NRO Account.

Securities acquired by NRIs/OCBs under PI scheme on a non-repatriation basis can be sold without any permission on the floor of a stock exchange.

Divided and interest income is fully repatriable

Investment on repatriation basis

NRIs and OCBs intending to invest with repatriation benefits should submit the application to the designated branch of authorised dealer. AD will grant to NRI/IOCB for purchase of shares/debentures subject to the conditions that-

I. The payment is received through an inward remittance in foreign exchange or by debit to the investor's NRE/FCNR account.

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II. Investment made by any single NRI/OCB investor in equity/preference shares and convertible debentures of any listed Indian company does not exceed 5% of its total paid-up equity or preference capital or 5% of the total paid-up value of each series of convertible debentures issued by it.

III. NRIs/OCBs take delivery of the shares/convertible debentures purchased and give delivery of the shares/convertible debentures sold under the Scheme.

NRIs and OCBs can freely sell securities acquired by tem wit repatriation benefits, without any permission, through a stock exchange. Dividend and interest income is also fully reportable.

Investment in the units of domestic mutual funds on non-repatriation/repatriation basis:

Same procedure as indicated in paragraphs for Investment on Non-Repatriation Basis and Repatriation Basis above is applicable. However, approvals already ranted for portfolio investment in shares/debentures of Indian companies will also be valid for purchase of units of domestic mutual funds.

*2.8.11 Investment in real estate*

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All persons, whether resident in India or outside India, who are citizens of Pakistan, Bangladesh, Sri Lanka, Afghanistan, China, Iran, Nepal or Bhutan require prior permission of Reserve Bank for acquiring or transferring any immovable property in India.

A person resident outside India, who has been permitted by Reserve Bank to establish a branch, or office, or place of business in India (excluding a Liaison Office), has general permission of Reserve Bank to acquire immovable property in India, which is necessary for, or incidental to, the activity. However, in such cases a declaration, in prescribed form (IPI), is required to be filed wit the Reserve Bank, within 90 days of the acquisition of immovable property.

An Indian citizen resident outside India does not require any permission to acquire any immovable property in India other than agricultural/plantation property or a farm house.

An Indian citizen resident outside India does not require any permission to transfer any immovable property, to a citizen of India who is resident in India.

An Indian citizen resident outside India does not require any permission to transfer any immovable property other than agricultural or plantation property or farm house, to a person who:

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(a) is a citizen of India resident outside India, or

(b) is a person of Indian origin resident outside India

A person of Indian origin resident outside India does not require any permission to acquire any immovable property other than agricultural land/farm house/plantation property in India by purchase, from out of funds:

i) received in India by way of inward remittance through banking channel from any place outside India, or

ii) held in any non-resident account maintained in accordance with the provisions of the Act and the regulations made by the Reserve Bank under the Act.

A person of Indian origin resident outside India does not require any permission to acquire any immovable property in India other than agricultural land/farm house/plantation property

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by way of gift from a person resident in India or from a person resident outside India who is a citizen of India or from a person of India origin resident outside India.

A person of Indian origin resident outside India does not require any permission to acquire any immovable property in India by way of inheritance from a person resident outside India who had acquired such property in accordance with the provisions of the foreign exchange law in force at the time of acquisition by him or the provisions of these Regulations or from a person resident in India.

A person of Indian origin resident outside India does not require any permission to transfer any immovable property in India other than agricultural land/farm house/plantation property, by way of sale to a person resident in India.

A person of Indian origin resident outside India does not require any permission to transfer agricultural land/farm house/plantation property in India, by way of gift or sale to a person resident in India who is a citizen of India.

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A person of Indian origin resident outside India does not require any permission to transfer residential or commercial property in India by way of gift to a person resident in India or to person resident outside India who is a citizen of India or to a person of India origin resident outside India.

Repatriation outside India, including credit to RFC, NRE or FCNR account, of sale proceeds of any immovable property situated in India, requires prior permission of the Reserve Bank except in circumstances stated.

In the event of sale of immovable property, other than agricultural land/farm house/plantation property in India by a person resident outside India, who is a citizen of India, or a person of Indian origin, the authorised dealer may allow repatriation of the sale proceeds outside India, provided All the following conditions are satisfied:

(i) the immovable property was acquired by the seller in accordance with the provisions of the Exchange Control Rules/Regulations/Law in force at the time of acquisition, or the provisions of the Regulations

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framed under the Foreign Exchange Management Act, 1999;

(ii) the sale takes place after three years from the date of acquisition of such immovable property or from the date of payment of final instalment of consideration for its acquisition, whichever is later;

(iii) the amount to be repatriated does not exceed

(a) the amount paid for acquisition of the immovable property in foreign exchange received through normal banking channels or out of funds held in foreign currency non-resident account or

(b) the foreign currency equivalent, as on the date of payment, of the amount paid where such payment was made from the funds held in non-resident external account for acquisition of the property; and

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(iv) in the case of residential property, the repatriation of sale proceeds is restricted to not more than two such properties.

All requests for acquisition of agricultural land/plantation/property/farm house by any person resident outside India or foreign nationals may be made to the Chief General Manager, Reserve Bank of India, Central Office, Exchange Control, Department, Foreign Investment Division (III), Mumbai - 400 001.

The NRIs/PIOs can freely rent out their immovable property in India without seeking any permission from the Reserve Bank. The rental income being a current account transaction is freely reportable outside India.

For the purposes of transactions, i.e., transfer, sale, purchase, etc., dealing with immovable property in India, a person of Indian origin is defined as under: "an individual (not being a citizen of Pakistan or Bangladesh or Sri Lanka or Afghanistan or China or Iran or Nepal or Bhutan), who

a) at any time, held Indian passport; or

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b) who or either of whose father or whose grandfather was a citizen of India by virtue of the constitution of India or the Citizenship Act, 1955 (57 of 1955)."

### 2.9.12 *PIO card scheme*

The Government has launched a comprehensive Scheme for the Persons of Indian Origin-called the 'PIO Card Scheme'. Under this Scheme, Persons of Indian Origin up to the fourth generation (great grand parents) settled throughout the world, except for a few specified countries, would be eligible. The Card would be issued to eligible applicants through the concerned Indian Embassies/High Commissions/Consulates and for those staying in India on a long-term visa, the concerned Foreigners Regional Registration Officer (Delhi, Mumbai, Calcutta, Chennai) would do the same. The fee for the card, which will have a validity of 20 years, would be US$1000.

In this scheme, unless the context otherwise requires-

"Person of Indian origin" means a foreign citizen (not being a citizen of Pakistan, Bangladesh and other countries as may be specified by the Central Government from time to time) if,

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(i) he/she at any time held an Indian passport; or

(ii) he/she or either of his/her parents or grand parents or great grand parents was born in and permanently resident in India as defined in the Government of India Act, 1935 and other territories that became part of India thereafter provided neither was at any time a citizen of any of the aforesaid countries (as referred to above); or

(iii) he/she is a spouse of a citizen of India or a person of Indian origin covered under (i) or (ii) above.

Besides making their journey back to their roots simpler, easier and smoother, this Scheme entitles the PIOs to a wide range of economic, financial, educational and cultural benefits. The benefits envisaged under the Scheme include:

I. No requirement of visa to visit India;

II. No requirement to register with the Foreigners Registration Officer if continuous stay does not exceed 180 days. If continuous stay exceeds 180 days, then registration is required

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to be done within a period of 30 days of the expiry of 180 days;

III. Parity with Non-Resident Indians in respect of facilities available to the latter in economic, financial, educational fields etc. These facilities ill include:

1) Acquisition, holding, transfer and disposal of immovable properties in India except of agricultural/plantation properties;

2) Admission of children in educational institutions in India under the general category quota for NRIs- including medical/engineering colleges, IITs, IIMs etc.

3) Various housing schemes of Life Insurance Corporation of India, State Governments and other Government agencies;

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IV All future benefits that would be extended to NRIs would also be available to the PIO Card holders;

However, they shall not enjoy political rights in India.

2.9.13 *Facilitation agencies for NRI/OCB/PIO investments*

The main regulatory and facilitation agencies involved in the matters related to NRIs/OCBs investment are Reserve Bank of India (RBI), Securities and Exchange Board of India (SWBI), Authority for Advance Rulings (AAR), Secretariat for Industrial Assistance (SIA), Ministry of Industry; and Office of the Chief Commissioner (Investments & NRIs). Briefly their areas of activities are as under:

1. Reserve bank of India (RBI)

Reserve Bank of India regulates the investment by persons resident outside India. In order to simplify the regulations and procedures they issue 'general permission' from time to time so that no specific permission are required for the activities covered under the 'general permission'. The specific permission as required under

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exchange control manual are granted by Foreign Investment Division-NRI Cell of RBI Mumbai or Exchange Control Department of the concerned Regional office of RBI depending upon the nature of permission required. The permissions are granted in a time bound manner. RBI maintains a comprehensive Website with latest updates, notifications, and forms at www.rbi.org.in.

The RBI has introduced the Banking Ombudsman Scheme since 1995 to provide a mechanism for redressal of grievances relating to customer services offered by Indian Banks. Ombudsmen have been appointed to receive complaints relating to provision of banking services, including complaints from NRIs having accounts in India in relation to their remittances from abroad and other bank related matters.

2. Securities and Exchange Board of India (SEBI)

The Overseas Investor Cell of SEBI provides answers to queries on registration procedures, formalities and other investment related issues pertaining to SEBI to all overseas investors including NRIs through its website at www.sebi.gov.in.

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3. Authority for Advance Rulings (AAR)

The Authority for Advance Rulings enables non-residents to obtain, in advance, a binding ruling on the issues that could arise in determining their Income Tax liabilities. Therefore, time consuming and expensive legal disputes can, thus, be avoided. The Authority is empowered to determine any question of law or of fact as specified in the application made before it in respect of a transaction, which has been undertaken or is proposed to undertaken by a non-resident.

Any non-resident person individual, company, firm, association of persons or other body corporate, can make an application for seeking an advance ruling.

The applicant is entitled to represent his case before the Authority either personally or through an authorised representative.

4. Secretariat for Industrial Assistance (SIA)

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SIA has been set up by the Government of India in the Department of Industrial Policy and Promotion in the Ministry of Industry to provide a single window for entrepreneurial assistance, investor facilitation, receiving and processing all applications which require Government approval, conveying Govt. decisions on applications filed, assisting entrepreneurs and investors in setting up projects, (including liaison with other organisations and State Govt.) and in monitoring implementation of projects. SIA maintains a comprehensive website at http://indmin.nic.in.

5. Indian Investment Centre [Office of the Chief Commissioner (Investments & NRIs)]

The Indian Investment Centre - a service organisation of the government of India advises overseas investors on setting up industrial projects in India by providing information regarding investment opportunities in India, the Government's industrial policy licensing procedures, taxation laws and facilities and incentives available. It also helps them in finding partners in India. The centre also provides escort services to NRIs. For details kindly refer website www.nic.in/iic.

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# CHAPTER 3

# *Laws of Foreign Exchange*

## 3.1 COFEPOSA (Control of Foreign Exchange and Prevention of Smuggling Act), 1974

### *3.1.1 History*

The Control of Foreign Exchange and Prevention of Smuggling Act was passed in the year 1974. During that period smuggling had reached notorious proportions and it was worsening the already fragile foreign exchange situation of the country. To check smuggling and its economic repercussions, the Government decided to give wide powers to custom authorities, and incidentally, this Act was passed. The Act gives the much talked about power of detention on mere suspicion that the concerned person is engaged in smuggling. However, with the implementation of liberal foreign trade policy and highly comfortable foreign exchange position, this Act has lost its significance.

The Act has been provided special protection by its inclusion in Schedule 9 of the Constitution.

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### 3.1.2 *Authority of detention under the Act*

A Government Officer, not below the rank of Joint Secretary in case of Central Government and Secretary in case of State Government, is authorised to order detention of a person (including a foreigner) with a view to prevent him from acting in any manner prejudicial to conservation or augmentation of foreign exchange, or to prevent him from smuggling or abetting smuggling of goods or harbouring persons engaged in smuggling of goods.[1] Where an order of detention is made b State Government office, it should be reported to Central Government within 10 days of such an order.[2]

When an order of detention is made by Central Government, it becomes the "Appropriate Government". The same is the case for State Government. The concerned "Appropriate Government" has to make a reference to Advisory Board formed for the purpose of COFEPOSA and take action as per decision as per the decision of Advisory Board. "Appropriate Government" also has powers to revoke a detention, release a person temporarily, etc.

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### 3.1.3 Other provisions regarding detention

Under Article 22(5) of the Constitution, a person detained under ay law providing for preventive detention, authority making the order must communicate grounds for order to him. However, Article 22(6) provides that facts need not be disclosed if the authority considers it against public interest. The COFEPOSA also provides that such communication should be done within 5 days or under exceptional circumstances, within 15 days of such an order.[3]

Article22 (5) also gives the detenue, the right to make representation. Such representation can be made to Officer who made the order of detention (who is specially authorised by Government for this purpose) as well as to the Advisory Board. The officer making order of detention must consider the representation. The detenue must be informed that he can make representation to the Officer ordering detention as well as the authority who has powers to revoke orders. If this is not informed it is violation of Constitutional right guaranteed under Article 22(5) of the Constitution and hence illegal. The detaining authority as well as the authority that has powers to revoke the detention order have to consider the representation.[4]

In case of the order being made by the State Government, it should consider representation before the case is referred to the Advisory Board.

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The representation can be considered even after matter is referred to Advisory Board. Inordinate delay in consideration of representation of detenue is illegal.[5]

The order of detention can be served on a person anywhere in India in the manner for execution of warrants of arrest under Section 4 of the Code of Criminal Procedure. In case the person is absconding, the Government shall make application to Judicial Magistrate First Class or Metropolitan Magistrate and he shall issue orders in respect of that person and his property as per the provisions of the Code of Criminal Procedure.

The Government is also empowered to issue order in Official Gazette and ask the person to report within prescribed period. If he does not report without sufficient cause, he can be imprisoned for one year plus charged with appropriate fine.[6] The order of detention can also be served on a person who is already in jail, if he is likely to be released on bail and may indulge in smuggling after release.[7] Detention must be made soon after the order is issued.[8]

A person can be detained at any place and under any condition as to maintenance, interviews or communication with others, discipline and punishment for breach of discipline, as the Central

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or State Government may specify. He can be removed from one place to another and from one State to another.[9] The ground for detention should not be vague, non-existent, irrelevant, not concerned or connected with the person or otherwise invalid. In case when the detention is on more than one ground in which some may be vague, irrelevant, etc., then all grounds have to be treated separately.[10]

Even if detention order on one or some other ground is found invalid, detention cannot be set aside, if it can be sustained on remaining grounds. It is presumed that officer making order of detention is satisfied that detention is necessary to conserve foreign exchange or prevent smuggling and no further proof regarding his satisfaction is necessary.[11] Detention order can be issued by State Government officer even if the person or place of detention is outside the State.[12]

A person detained under the Act can be released for a specific period by Central Government or State Government with or without conditions. A bond may be asked from the person being released.[13]

### *3.1.4 The Advisory Board*

The purpose of detention under COFEPOSA is preventive. The detention can be further extended only if Advisory Board reports before three

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months that there is sufficient cause for further detention. Members of such board should have been High Court judges or qualified to be High Court judges. Such boards are to be constituted by Central as well as the State Governments. The Advisory should consist of a Chairman and two other members. [14]The concerned Government is required to make a reference to the Advisory Board within 5 weeks of detention. The Advisory Board will consider material placed before it, hear the person detained, if he so desires, and give report within 11 weeks from detention The person detained will not be provided with lawyer for making representation. [15] If the Advisory Board reports that there is sufficient cause for detention, it may continue detention. Otherwise, the person has to be released. Even if he is detained, maximum detention can be one year from the date of detention. [16] Despite recommendation from the Advisory Board, Government can revoke the order or amend detention order any time.

## 3.2 Foreign Exchange Management Act (FEMA), 1999

### *3.2.1 Objectives*

FEMA is the liberalised version of its predecessor the Foreign Exchange Regulation Act, 1973. FERA was implemented for improving the foreign exchange position and controlling external money

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flow due to long experienced adverse Balance of Payment (BoP). FERA was introduced in 1947, and was later replaced by the 1973 law. FEMA coincides with comfortable BoP situation, adequate exchange reserves and overall high growth foreign trade. The Act aims to facilitate, rather than regulate international trade in view of changed economic conditions post WTO.

FEMA aims at achieving the following objectives:

1. Consolidation of foreign exchange resources

2. Control over transactions directly or indirectly affecting foreign exchange.

3. Control over import and export of the currency and bullion.

4. Facilitate the proper use of available resources of foreign exchange in the interest of the economic development of the country.

5. Prevention of leakage of foreign exchange.

The responsibility of achieving these objectives has been vested with Reserve Bank of India. The Act has been applied to the whole of India including Indian citizens residing abroad and the agencies and branches outside India of the companies registered or incorporated in India.

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### 3.2.2 *Definitions*

Currency:

Currency includes coins, currency notes, bank notes, postal orders, money orders, cheques, drafts, traveller's cheques, letter of credit, bill of exchange and promissory notes.[17] Indian Currency means currency expressed in Indian Rupees, but does not include special bank notes and special rupee notes under section 28A of Reserve Bank of India Act. Foreign currency means any currency other than Indian currency. Thus the definition is wide and includes bill of exchange, Letter of Credit, etc. apart from normal currency.

Rupee trade:

India has rupee trade with Nepal and Bhutan. Rupee trade means trade that payments with respect to trade are made in respect of Indian rupee.

Convertible or Hard Currency:

Currencies, which are freely convertible, i.e. one can exchange these currencies with any other currency without any restriction. These currencies include US Dollars, Euro, Japanese Yen, etc.

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Foreign Exchange:

Foreign exchange means foreign currency and includes,

(a) All deposits, credits, and balances payable in any foreign currency and any drafts, traveller's cheques, letter of credit and bill of exchange expressed or drawn in Indian currency but payable in foreign currency.

(b) It also includes any instrument payable at the option of the drawee or holder or any other party thereto; either in Indian currency or in foreign currency or partly in Indian currency and partly in foreign currency.[18]

Person Resident in India:

Person Resident in India includes the following:

(c) A citizen staying in India at the time after 25th March 1947, except those gone out of India for employment, carrying out business or vocation, or for any other purpose in such circumstances, which would indicate

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his intention to stay outside India for an uncertain period.

(d) A citizen of India who have ceased to be Indian Resident because of above clause; who returns to or stays in India for the purpose of employment, carrying on business or vocation, or for any other purpose in such circumstances which would indicate his intention to stay in India for an uncertain period.

(e) A person who is not a citizen of India, but who has came to India for the purpose of taking employment, carrying out business or vocation in India, staying with his or her spouse-if the is an Indian Resident, or for any other purpose in such circumstances which would indicate his intention to stay in India for an uncertain period. However, if he stays out of India, he will not be deemed to be resident of India during the period he is out of India.

(f) Citizen of India who did not stay in India any time after 25th March 1947; who comes to India for the purpose of taking employment in India, carrying

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out business or vocation in India, staying with his or her spouse-if the is an Indian Resident, or for any other purpose in such circumstances which would indicate his intention to stay in India for an uncertain period.[19]

Broadly speaking, person resident in India includes citizen of India (except those staying abroad for work or business or other purpose) and non-citizen who come to India or stay in India for employment, carrying out business or other purpose or for staying with spouse who is an Indian resident.

Person Resident outside India:

Person Resident outside India means a person who is not resident in India.[20] Following persons will be treated as persons resident outside India:

(g) A citizen of India who has gone out or stays out of India for the purpose of employment, carrying out business or vocation, or for any other purpose which would indicates his intention to stay in out of India for an uncertain period.

(h) A non-citizen who has come to India for visit but not for employment,

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carrying out business or staying for uncertain period.

Non-Resident Indian (NRI):

The term Non-Resident Indian has been defined in Income Tax Act, 1961. According to section 6 of the Act, Non-Resident Indian (whether a citizen of India or not) is a person, who comes on a visit to India and who satisfies the following conditions:

a. He stays in India for 182 days or more during the financial year or

b. Stays in India for a period amounting in all to 365 days in four years preceding the financial year and stays for not less than 182 days in the financial year.

Overseas Corporate Body (OCB):

As per notification of Reserve Bank of India the term OCB means overseas company, partnership firm, society and other corporate body predominantly owned directly or indirectly to the extent of at least 60% by Non-Resident Indians.[21] It also includes trust in which at least 60% beneficial interest is

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irrevocably held by NRIs. The OCBs have to produce certificate from overseas auditors that the ownership interest/beneficial interest of NRIs in OCBs is at least 60%.

Person of Indian Origin (PIO):

Person of Indian Origin has been define by RBI in its various notifications for the purpose of maintenance of bank accounts in India or abroad and making investments in shares, securities, industry, business, real estate, etc. in India. The conditions for being classified as PIO are as follows:

(i) The person should not be a citizen of Pakistan or Bangladesh

(j) He should satisfy any one of the following sub-conditions:
   (i) He was at any time holding Indian passport or was a citizen of India or
   (ii) Anyone of his parents or grandparents was a citizen of India or
   (iii) His spouse- husband or wife - is a person of Indian Origin, though he or she may be non-Indian.[22]

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Reserve Bank:

Reserve Bank means the Reserve Bank of India constituted under sub-section (1) of section 3 of the Reserve Bank of India Act, 1934 (2 of 1934). [23]

Security:

Security means shares, stocks, bonds and debentures, Government securities as defined in the Public Debt Act, 1944 (18 of 1944), savings certificates to which the Government Savings Certificates Act, 1959 (46 of 1959) applies, deposit receipts in respect of deposits of securities and units of the Unit Trust of India established under sub-section (1) of section 3 of the Unit Trust of India Act, 1963 (52 of 1963) or of any mutual fund and includes certificates of title to securities, but does not include bills of exchange or promissory notes other than Government promissory notes or any other instruments which may be notified by the Reserve Bank as security for the purposes of this Act. [24]

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Service:

Service means service of any description which is made available to potential users and includes the provision of facilities in connection with banking, financing, insurance, medical assistance, legal assistance, chit fund, real estate, transport, processing, supply of electrical or other energy, boarding or lodging or both, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal service.[25]

Special Director:

Special Director (Appeals) means an officer appointed under section 18.[26]

Specify:

Specify means to specify by regulations made under this Act and the expression "specified" shall be construed accordingly.[27]

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Transfer:

Transfer includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien. [28]

*3.2.3 Regulation and management of foreign exchange*

*3.2.3.1 Capital Account transactions*

Subject to the provisions of sub-section (2), any person may sell or draw foreign exchange to or from an authorised person for a capital account transaction.

The Reserve Bank may, in consultation with the Central Government, specify

*(a)* any class or classes of capital account transactions which are permissible;

*(b)* the limit up to which foreign exchange shall be admissible for such transactions:

**Provided** that the Reserve Bank shall not impose any restriction on the drawal of foreign exchange for payments due on account of amortization of

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loans or for depreciation of direct investments in the ordinary course of business.

Without prejudice to the generality of the provisions of sub-section (2), the Reserve Bank may, by regulations, prohibit, restrict or regulate the following—

*(a)* transfer or issue of any foreign security by a person resident in India;

*(b)* transfer or issue of any security by a person resident outside India;

*(c)* transfer or issue of any security or foreign security by any branch, office or agency in India of a person resident outside India;

*(d)* any borrowing or lending in foreign exchange in whatever form or by whatever name called;

*(e)* any borrowing or lending in rupees in whatever form or by whatever name called between a person resident in India and a person resident outside India;

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(*f*) deposits between persons resident in India and persons resident outside India;

(*g*) export, import or holding of currency or currency notes;

(*h*) transfer of immovable property outside India, other than a lease not exceeding five years, by a person resident in India;

(*i*) acquisition or transfer of immovable property in India, other than a lease not exceeding five years, by a person resident outside India;

(*j*) giving of a guarantee or surety in respect of any debt, obligation or other liability incurred—

(*i*) by a person resident in India and owed to a person resident outside India; or

(*ii*) by a person resident outside India.

A person resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person when he was

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resident outside India or inherited from a person who was resident outside India.

A person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India.

Without prejudice to the provisions of this section, the Reserve Bank may, by regulation, prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a person resident outside India, for carrying on any activity relating to such branch, office or other place of business. [29]

### *3.2.3.2 Current Account transactions*

Any person may sell or draw foreign exchange to or from an authorised person if such sale or drawal is a current account transaction.

**Provided** that the Central Government may, in public interest and in consultation with the Reserve Bank, impose such reasonable restrictions for current account transactions as may be prescribed. [30]

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### *3.2.3.3 Export of goods and services*

Every exporter of goods shall—

*(a)* furnish to the Reserve Bank or to such other authority a declaration in such form and in such manner as may be specified, containing true and correct material particulars, including the amount representing the full export value or, if the full export value of the goods is not ascertainable at the time of export, the value which the exporter, having regard to the prevailing market conditions, expects to receive on the sale of the goods in a market outside India;

*(b)* furnish to the Reserve Bank such other information as may be required by the Reserve Bank for the purpose of ensuring the realisation of the export proceeds by such exporter.

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The Reserve Bank may, for the purpose of ensuring that the full export value of the goods or such reduced value of the goods as the Reserve Bank determines, having regard to the prevailing market conditions, is received without any delay, direct any exporter to comply with such requirements as it deems fit.

Every exporter of services shall furnish to the Reserve Bank or to such other authorities a declaration in such form and in such manner as may be specified, containing the true and correct material particulars in relation to payment for such services.[31]

*3.2.3.4 Dealing in foreign exchange*

Save as otherwise provided in this Act, rules or regulations made thereunder, or with the general or special permission of the Reserve Bank, no person shall—

*(a)* deal in or transfer any foreign exchange or foreign security to any person not being an authorised person;

*(b)* make any payment to or for the credit of any person resident outside India in any manner;

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(*c*) receive otherwise (than) through an authorised person, any payment by order or on behalf of any person resident outside India in any manner;

*Explanation.*—For the purpose of this clause, where any person in, or resident in, India receives any payment by order or on behalf of any person resident outside India through any other person (including an authorised person) without a corresponding inward remittance from any place outside India, then, such person shall be deemed to have received such payment otherwise than through an authorised person;

(*d*) enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person.

*Explanation.*—For the purpose of this clause, "financial transaction" means making any payment to, or for the credit of any person, or receiving any payment for, by order or on behalf of any person, or drawing, issuing or negotiating any bill of exchange or promissory note, or transferring any security or acknowledging any debt.[32]

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### *3.2.3.5 Holding of foreign exchange*

Save as otherwise provided in this Act, no person resident in India shall acquire, hold, own, possess or transfer any foreign exchange, foreign security or any immovable property situated outside India. [33]

### *3.2.3.6 Realisation and repatriation of foreign exchange*

Save as otherwise provided in this Act, where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realise and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank. [34]

### *3.2.3.7 Exemption from realisation and repatriation in certain cases*

The provisions of sections 4 and 8 shall not apply to the following, namely:—

*(a)* possession of foreign currency or foreign coins by any person up to such limit as the Reserve Bank may specify;

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*(b)* foreign currency account held or operated by such person or class of persons and the limit up to which the Reserve Bank may specify;

*(c)* foreign exchange acquired or received before the 8th day of July, 1947 or any income arising or accruing thereon which is held outside India by any person in pursuance of a general or special permission granted by the Reserve Bank;

*(d)* foreign exchange held by a person resident in India up to such limit as the Reserve Bank may specify, if such foreign exchange was acquired by way of gift or inheritance from a person referred to in clause (*c*), including any income arising therefrom;

*(e)* foreign exchange acquired from employment, business, trade, vocation, services, honorarium, gifts, inheritance or any other legitimate means up to such limit as the Reserve Bank may specify; and

*(f)* such other receipts in foreign exchange as the Reserve Bank may specify. [35]

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### *3.2.4 Authorised person*

### *3.2.4.1 Authorised person*

The Reserve Bank may, on an application made to it in this behalf, authorise any person to be known as authorised person to deal in foreign exchange or in foreign securities, as an authorised dealer, money changer or off-shore banking unit or in any other manner as it deems fit.

An authorisation under this section shall be in writing and shall be subject to the conditions laid down therein.

An authorisation granted under sub-section (1) may be revoked by the Reserve Bank at any time if the Reserve Bank is satisfied that—

*(a)* it is in public interest so to do; or

*(b)* the authorised person has failed to comply with the condition subject to which the authorisation was granted or has contravened any of the provisions of the Act or any rule, regulation, notification, direction or order made thereunder:

**Provided** that no such authorisation shall be revoked on any ground referred to in clause *(b)* unless the authorised person has been given a

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reasonable opportunity of making a representation in the matter.

An authorised person shall, in all his dealings in foreign exchange or foreign security, comply with such general or special directions or orders as the Reserve Bank may, from time to time, think fit to give, and, except with the previous permission of the Reserve Bank, an authorised person shall not engage in any transaction involving any foreign exchange or foreign security which is not in conformity with the terms of his authorisation under this section.

An authorised person shall, before undertaking any transaction in foreign exchange on behalf of any person, require that person to make such declaration and to give such information as will reasonably satisfy him that the transaction will not involve, and is not designed for the purpose of any contravention or evasion of the provisions of this Act or of any rule, regulation, notification, direction or order made thereunder, and where the said person refuses to comply with any such requirement or makes only unsatisfactory compliance therewith, the authorised person shall refuse in writing to undertake the transaction and shall, if he has reason to believe that any such contravention or evasion as aforesaid is contemplated by the person, report the matter to the Reserve Bank.

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Any person, other than an authorised person, who has acquired or purchased foreign exchange for any purpose mentioned in the declaration made by him to authorised person under sub-section (5) does not use it for such purpose or does not surrender it to authorised person within the specified period or uses the foreign exchange so acquired or purchased for any other purpose for which purchase or acquisition of foreign exchange is not permissible under the provisions of the Act or the rules or regulations or direction or order made thereunder shall be deemed to have committed contravention of the provisions of the Act for the purpose of this section. [36]

### *3.2.4.2 Reserve Bank's powers to issue directions to authorised person*

The Reserve Bank may, for the purpose of securing compliance with the provisions of this Act and of any rules, regulations, notifications or directions made thereunder, give to the authorised persons any direction in regard to making of payment or the doing or desist from doing any act relating to foreign exchange or foreign security.

The Reserve Bank may, for the purpose of ensuring the compliance with the provisions of this Act or of any rule, regulation, notification, direction or order made thereunder, direct any authorised person to furnish such information, in such manner, as it deems fit.

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Where any authorised person contravenes any direction given by the Reserve Bank under this Act or fails to file any return as directed by the Reserve Bank, the Reserve Bank may, after giving reasonable opportunity of being heard, impose on the authorised person a penalty which may extend to ten thousand rupees and in the case of continuing contravention with an additional penalty which may extend to two thousand rupees for every day during which such contravention continues. [37]

*3.2.4.3 Reserve Bank's powers to inspect authorised person*

The Reserve Bank may, at any time, cause an inspection to be made, by any officer of the Reserve Bank specially authorised in writing by the Reserve Bank in this behalf, of the business of any authorised person as may appear to it to be necessary or expedient for the purpose of—

*(a)* verifying the correctness of any statement, information or particulars furnished to the Reserve Bank;

*(b)* obtaining any information or particulars which such authorised person has failed to furnish on being called upon to do so;

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*(c)* securing compliance with the provisions of this Act or of any rules, regulations, directions or orders made thereunder.

It shall be the duty of every authorised person, and where such person is a company or a firm, every director, partner or other officer of such company or firm, as the case may be, to produce to any officer making an inspection under sub-section (1), such books, accounts and other documents in his custody or power and to furnish any statement or information relating to the affairs of such person, company or firm as the said officer may require within such time and in such manner as the said officer may direct. [38]

### *3.2.5 Contraventions and penalties*

#### *3.2.5.1 Penalties*

If any person contravenes any provision of this Act, or contravenes any rule, regulation, notification, direction or order issued in exercise of the powers under this Act, or contravenes any condition subject to which an authorisation is issued by the Reserve Bank, he shall, upon adjudication, be liable to a penalty up to thrice the sum involved in such contravention where such amount is quantifiable, or up to two lakh rupees where the amount is not quantifiable, and where such contravention is a continuing one, further

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penalty which may extend to five thousand rupees for every day after the first day during which the contravention continues.

Any Adjudicating Authority adjudging any contravention under sub-section (1), may, if he thinks fit in addition to any penalty which he may impose for such contravention direct that any currency, security or any other money or property in respect of which the contravention has taken place shall be confiscated to the Central Government and further direct that the foreign exchange holdings, if any of the persons committing the contraventions or any part thereof, shall be brought back into India or shall be retained outside India in accordance with the directions made in this behalf.

*Explanation.*—For the purposes of this sub-section, "property" in respect of which contravention has taken place, shall include—

*(a)* deposits in a bank, where the said property is converted into such deposits;

*(b)* Indian currency, where the said property is converted into that currency; and

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*(c)* any other property which has resulted out of the conversion of that property.[39]

### *3.2.5.2 Enforcement of the orders of adjudicating authorities*

Subject to the provisions of sub-section (2) of section 19, if any person fails to make full payment of the penalty imposed on him under section 13 within a period of ninety days from the date on which the notice for payment of such penalty is served on him, he shall be liable to civil imprisonment under this section.

No order for the arrest and detention in civil prison of a defaulter shall be made unless the Adjudicating Authority has issued and served a notice upon the defaulter calling upon him to appear before him on the date specified in the notice and to show cause why he should not be committed to the civil prison, and unless the Adjudicating Authority, for reasons in writing, is satisfied—

*(a)* that the defaulter, with the object or effect of obstructing the recovery of penalty, has after the issue of notice by the Adjudicating Authority, dishonestly transferred, concealed, or removed any part of his property, or

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(*b*) that the defaulter has, or has had since the issuing of notice by the Adjudicating Authority, the means to pay the arrears or some substantial part thereof and refuses or neglects or has refused or neglected to pay the same.

Notwithstanding anything contained in sub-section (1), a warrant for the arrest of the defaulter may be issued by the Adjudicating Authority if the Adjudicating Authority is satisfied, by affidavit or otherwise, that with the object or effect of delaying the execution of the certificate the defaulter is likely to abscond or leave the local limits of the jurisdiction of the Adjudicating Authority.

Where appearance is not made pursuant to a notice issued and served under sub-section (1), the Adjudicating Authority may issue a warrant for the arrest of the defaulter.

A warrant of arrest issued by the Adjudicating Authority under sub-section (3) or sub-section (4) may also be executed by any other Adjudicating Authority within whose jurisdiction the defaulter may for the time being be found.

Every person arrested in pursuance of a warrant of arrest under this section shall be brought before the Adjudicating Authority issuing the warrant as

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soon as practicable and in any event within twenty-four hours of his arrest (exclusive of the time required for the journey):

**Provided** that, if the defaulter pays the amount entered in the warrant of arrest as due and the costs of the arrest to the officer arresting him, such officer shall at once release him.

*Explanation.*—For the purposes of this sub-section, where the defaulter is a Hindu undivided family, the *karta* thereof shall be deemed to be the defaulter.

When a defaulter appears before the Adjudicating Authority pursuant to a notice to show cause or is brought before the Adjudicating Authority under this section, the Adjudicating Authority shall give the defaulter an opportunity showing cause why he should not be committed to the civil prison.

Pending the conclusion of the inquiry, the Adjudicating Authority may, in his discretion, order the defaulter to be detained in the custody of such officer as the Adjudicating Authority may think fit or release him on his furnishing the security to the satisfaction of the Adjudicating Authority for his appearance as and when required.

Upon the conclusion of the inquiry, the Adjudicating Authority may make an order for the

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detention of the defaulter in the civil prison and shall in that event cause him to be arrested if he is not already under arrest:

**Provided** that in order to give a defaulter an opportunity of satisfying the arrears, the Adjudicating Authority may, before making the order of detention, leave the defaulter in the custody of the officer arresting him or of any other officer for a specified period not exceeding fifteen days, or release him on his furnishing security to the satisfaction of the Adjudicating Authority for his appearance at the expiration of the specified period if the arrears are not satisfied.

When the Adjudicating Authority does not make an order of detention under sub-section (9), he shall, if the defaulter is under arrest, direct his release.

Every person detained in the civil prison in execution of the certificate may be so detained,—

*(a)* where the certificate is for a demand of an amount exceeding rupees one crore, up to three years, and

*(b)* in any other case, up to six months:

**Provided** that he shall be released from such detention on the amount mentioned in the warrant

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for his detention being paid to the officer-in-charge of the civil prison.

A defaulter released from detention under this section shall not, merely by reason of his release, be discharged from his liability for the arrears, but he shall not be liable to be arrested under the certificate in execution of which he was detained in the civil prison. [40]

A detention order may be executed at any place in India in the manner provided for the execution of warrant of arrest under the Code of Criminal Procedure, 1973 (2 of 1974).

*3.2.5.3 Power to compound contravention*

Any contravention under section 13 may, on an application made by the person committing such contravention, be compounded within one hundred and eighty days from the date of receipt of application by the Director of Enforcement or such other officers of the Directorate of Enforcement and Officers of the Reserve Bank as may be authorised in this behalf by the Central Government in such manner as may be prescribed.

Where a contravention has been compounded under sub-section (1), no proceeding or further proceeding, as the case may be, shall be initiated or continued, as the case may be, against the person committing such contravention under that

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section, in respect of the contravention so compounded. [41]

### *3.2.6 Adjudication and Appeal*

#### *3.2.6 .1 Appointment of adjudicating authority*

For the purpose of adjudication under section 13, the Central Government may, by an order published in the Official Gazette, appoint as many officers of the Central Government as it may think fit, as the Adjudicating Authorities for holding an inquiry in the manner prescribed after giving the person alleged to have committed contravention under section 13, against whom a complaint has been made under sub-section (3) (hereinafter in this section referred to as the said person) a reasonable opportunity of being heard for the purpose of imposing any penalty:

**Provided** that where the Adjudicating Authority is of opinion that the said person is likely to abscond or is likely to evade in any manner, the payment of penalty, if levied, it may direct the said person to furnish a bond or guarantee for such amount and subject to such conditions as it may deem fit.

The Central Government shall, while appointing the Adjudicating Authorities under sub-section

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(1), also specify in the order published in the Official Gazette, their respective jurisdictions.

No Adjudicating Authority shall hold an enquiry under sub-section (1) except upon a complaint in writing made by any officer authorized by a general or special order by the Central Government.

The said person may appear either in person or take the assistance of a legal practitioner or a chartered accountant of his choice for presenting his case before the Adjudicating Authority.

Every Adjudicating Authority shall have the same powers of a civil court which are conferred on the Appellate Tribunal under sub-section (2) of section 28 and—

*(a)* all proceedings before it shall be deemed to be judicial proceedings within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860);

*(b)* shall be deemed to be a civil court for the purposes of sections 345 and 346 of the Code of Criminal Procedure, 1973 (2 of 1974).

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Every Adjudicating Authority shall deal with the complaint under sub-section (2) as expeditiously as possible and endeavour shall be made to dispose of the complaint finally within one year from the date of receipt of the complaint:

**Provided** that where the complaint cannot be disposed off within the said period, the Adjudicating Authority shall record periodically the reasons in writing for not disposing off the complaint within the said period.[42]

*3.2.6.2 Appeal to special director (appeals)*

The Central Government shall, by notification, appoint one or more Special Directors (Appeals) to hear appeals against the orders of the Adjudicating Authorities under this section and shall also specify in the said notification the matter and places in relation to which the Special Director (Appeals) may exercise jurisdiction.

Any person aggrieved by an order made by the Adjudicating Authority, being an Assistant Director of Enforcement or a Deputy Director of Enforcement, may prefer an appeal to the Special Director (Appeals).

Every appeal under sub-section (1) shall be filed within forty-five days from the date on which the copy of the order made by the Adjudicating

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Authority is received by the aggrieved person and it shall be in such form, verified in such manner and be accompanied by such fee as may be prescribed.

**Provided** that the Special Director (Appeals) may entertain an appeal after the expiry of the said period of forty-five days, if he is satisfied that there was sufficient cause for not filing it within that period.

On receipt of an appeal under sub-section (1), the Special Director (Appeals) may after giving the parties to the appeal an opportunity of being heard, pass such order thereon as he thinks fit confirming, modifying or setting aside the order appealed against.

The Special Director (Appeals) shall send a copy of every order made by him to the parties to appeal and to the concerned Adjudicating Authority.

The Special Director (Appeals) shall have the same powers of a civil court which are conferred on the Appellate Tribunal under sub-section (2) of section 28 and—

*(a)* all proceedings before him shall be deemed to be judicial proceedings within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860);

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*(b)* shall be deemed to be a civil court for the purposes of sections 345 and 346 of the Code of Criminal Procedure, 1973 (2 of 1974). [43]

*3.2.6.3 Establishment of appellate tribunal*

The Central Government shall, by notification, establish an Appellate Tribunal to be known as the Appellate Tribunal for Foreign Exchange to hear appeals against the orders of the Adjudicating Authorities and the Special Director (Appeals) under this Act. [44]

*3.2.6.4 Appeal to appellate tribunal*

Save as provided in sub-section (2), the Central Government or any person aggrieved by an order made by an Adjudicating Authority, other than those referred to in sub-section (1) of section 17, or the Special Director (Appeals), may prefer an appeal to the Appellate Tribunal:

**Provided** that any person appealing against the order of the Adjudicating Authority or the Special Director (Appeals) levying any penalty, shall while filing the appeal, deposit the amount of such penalty with such authority as may be notified by the Central Government:

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**Provided further** that where in any particular case, the Appellate Tribunal is of the opinion that the deposit of such penalty would cause undue hardship to such person, the Appellate Tribunal may dispense with such deposit subject to such conditions as it may deem fit to impose so as to safeguard the realisation of penalty.

Every appeal under sub-section (1) shall be filed within a period of forty-five days from the date on which a copy of the order made by the Adjudicating Authority or the Special Director (Appeals) is received by the aggrieved person or by the Central Government and it shall be in such form, verified in such manner and be accompanied by such fee as may be prescribed:

**Provided** that the Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days if it is satisfied that there was sufficient cause for not filing it within that period.

On receipt of an appeal under sub-section (1), the Appellate Tribunal may, after giving the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed against.

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The Appellate Tribunal shall send a copy of every order made by it to the parties to the appeal and to the concerned Adjudicating Authority or the Special Director (Appeals), as the case may be.

The appeal filed before the Appellate Tribunal under sub-section (1) shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the appeal finally within one hundred and eighty days from the date of receipt of the appeal:

**Provided** that where any appeal could not be disposed of within the said period of one hundred and eighty days, the Appellate Tribunal shall record its reasons in writing for not disposing of the appeal within the said period.

The Appellate Tribunal may, for the purpose of examining the legality, propriety or correctness of any order made by the Adjudicating Authority under section 16 in relation to any proceeding, on its own motion or otherwise, call for the records of such proceedings and make such order in the case as it thinks fit. [45]

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*3.2.6.5 Composition of appellate tribunal*

The Appellate Tribunal shall consist of a Chairperson and such number of Members as the Central Government may deem fit.

Subject to the provisions of this Act,—

*(a)* the jurisdiction of the Appellate Tribunal may be exercised by Benches thereof;

*(b)* a Bench may be constituted by the Chairperson with one or more Members as the Chairperson may deem fit;

*(c)* the Benches of the Appellate Tribunal shall ordinarily sit at New Delhi and at such other places as the Central Government may, in consultation with the Chairperson, notify;

*(d)* the Central Government shall notify the areas in relation to which each Bench of the Appellate Tribunal may exercise jurisdiction.

Notwithstanding anything contained in sub-section (2), the Chairperson may transfer a Member from one Bench to another Bench.

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If at any stage of the hearing of any case or matter it appears to the Chairperson or a Member that the case or matter is of such a nature that it ought to be heard by a Bench consisting of two Members, the case or matter may be transferred by the Chairperson or, as the case may be, referred to him for transfer, to such Bench as the Chairperson may deem fit. [46]

### *3.2.6.6 Qualifications for appointment of Chairperson, Member and Special Director (appeals)*

A person shall not be qualified for appointment as the Chairperson or a Member unless he—

*(a)* in the case of Chairperson, is or has been, or is qualified to be, a Judge of a High Court; and

*(b)* in the case of a Member, is or has been, or is qualified to be, a District Judge.

A person shall not be qualified for appointment as a Special Director (Appeals) unless he—

*(a)* has been a member of the Indian Legal Service and has held a post in Grade I of that Service; or

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*(b)* has been a member of the Indian Revenue Service and has held a post equivalent to a Joint Secretary to the Government of India.[47]

*3.2.6.7 Term of office*

The Chairperson and every other Member shall hold office as such for a term of five years from the date on which he enters upon his office:

**Provided** that no Chairperson or other Member shall hold office as such after he has attained,—

*(a)* in the case of the Chairperson, the age of sixty-five years;

*(b)* in the case of any other Member, the age of sixty-two years.[48]

*3.2.6.8 Terms and conditions of service*

The salary and allowances payable to and the other terms and conditions of service of the Chairperson, other Members and the Special Director (Appeals) shall be such as may be prescribed :

**Provided** that neither the salary and allowances nor the other terms and conditions of service of

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the Chairperson or a Member shall be varied to his disadvantage after appointment. [49]

### 3.2.6.9 Vacancies

If, for reason other than temporary absence, any vacancy occurs in the office of the Chairperson or a Member, the Central Government shall appoint another person in accordance with the provisions of this Act to fill the vacancy and the proceedings may be continued before the Appellate Tribunal from the stage at which the vacancy is filled. [50]

### 3.2.6.10 Registration and removal

The Chairperson or a Member may, by notice in writing under his hand addressed to the Central Government, resign his office :

**Provided** that the Chairperson or a Member shall, unless he is permitted by the Central Government to relinquish his office sooner, continue to hold office until the expiry of three months from the date of receipt of such notice or until a person duly appointed as his successor enters upon his office or until the expiry of term of office, whichever is the earliest.

The Chairperson or a Member shall not be removed from his office except by an order by the Central Government on the ground of proved

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misbehaviour or incapacity after an enquiry made by such person as the President may appoint for this purpose in which the Chairperson or a Member concerned has been informed of the charges against him and given a reasonable opportunity of being heard in respect of such charges. [51]

*3.2.6.11 Member to act as Chairperson in certain circumstances*

In the event of the occurrence of any vacancy in the office of the Chairperson by reason of his death, resignation or otherwise, the senior-most Member shall act as the Chairperson until the date on which a new Chairperson, appointed in accordance with the provisions of this Act to fill such vacancy, enters upon his office.

When the Chairperson is unable to discharge his functions owing to absence, illness or any other cause, the senior-most Member shall discharge the functions of the Chairperson until the date on which the Chairperson resumes his duties. [52]

*3.2.6.12 Staff of appellate tribunal and Special Director (appeals)*

The Central Government shall provide the Appellate Tribunal and the Special Director

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(Appeals) with such officers and employees as it may deem fit.

The officers and employees of the Appellate Tribunal and office of the Special Director (Appeals) shall discharge their functions under the general superintendence of the Chairperson and the Special Director (Appeals), as the case may be.

The salaries and allowances and other conditions of service of the officers and employees of the Appellate Tribunal and office of the Special Director (Appeals) shall be such as may be prescribed.[53]

*3.2.6.13 Procedure and powers of appellate tribunal and Special Director (appeals)*

The Appellate Tribunal and the Special Director (Appeals) shall not be bound by the procedure laid down by the Code of Civil Procedure, 1908 (5 of 1908) but shall be guided by the principles of natural justice and, subject to the other provisions of this Act, the Appellate Tribunal and the Special Director (Appeals) shall have powers to regulate its own procedure.

The Appellate Tribunal and the Special Director (Appeals) shall have, for the purposes of discharging its functions under this Act, the same powers as are vested in a civil court under the

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Code of Civil Procedure, 1908 (5 of 1908); while trying a suit, in respect of the following matters, namely:—

i. summoning and enforcing the attendance of any person and examining him on oath;

ii. requiring the discovery and production of documents;

iii. receiving evidence on affidavits;

iv. subject to the provisions of sections 123 and 124 of the Indian Evidence Act, 1872 (1 of 1872) requisitioning any public record or document or copy of such record or document from any office;

v. issuing commissions for the examination of witnesses or documents;

vi. reviewing its decisions;

vii. dismissing a representation of default or deciding it *ex parte*;

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viii. setting aside any order of dismissal of any representation for default or any order passed by it *ex parte*; and

ix. any other matter which may be prescribed by the Central Government.

An order made by the Appellate Tribunal or the Special Director (Appeals) under this Act shall be executable by the Appellate Tribunal or the Special Director (Appeals) as a decree of civil court and, for this purpose, the Appellate Tribunal and the Special Director (Appeals) shall have all the powers of a civil court.

Notwithstanding anything contained in sub-section (3), the Appellate Tribunal or the Special Director (Appeals) may transmit any order made by it to a civil court having local jurisdiction and such civil court shall execute the order as if it were a decree made by that court.

All proceedings before the Appellate Tribunal and the Special Director (Appeals) shall be deemed to be judicial proceedings within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860) and the Appellate Tribunal shall be deemed to be a civil court for the purposes of sections 345 and 346 of the Code of Criminal Procedure, 1973 (2 of 1974).[54]

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### *3.2.6.14 Distribution of business amongst benches*

Where Benches are constituted, the Chairperson may, from time to time, by notification, make provisions as to the distribution of the business of the Appellate Tribunal amongst the Benches and also provide for the matters, which may be dealt with by each Bench. [55]

### *3.2.6.15 Power of chairperson to transfer cases*

On the application of any of the parties and after notice to the parties, and after hearing such of them as he may desire to be heard, or on his own motion without such notice, the Chairperson may transfer any case pending before one Bench, for disposal, to any other Bench. [56]

### *3.2.6.16 Decision to be by majority*

If the Members of a Bench consisting of two Members differ in opinion on any point, they shall state the point or points on which they differ, and make a reference to the Chairperson who shall either hear the point or points himself or refer the case for hearing on such point or points by one or

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more of the other Members of the Appellate Tribunal and such point or points shall be decided according to the opinion of the majority of the Members of the Appellate Tribunal who have heard the case, including those who first heard it.[57]

*3.2.6.17 Right of appellant to take assistance of legal practitioner or chartered accountant and of Government, to appoint presenting officers*

A person preferring an appeal to the Appellate Tribunal or the Special Director (Appeals) under this Act may either appear in person or take the assistance of a legal practitioner or a chartered accountant of his choice to present his case before the Appellate Tribunal or the Special Director (Appeals), as the case may be.

The Central Government may authorise one or more legal practitioners or chartered accountants or any of its officers to act as presenting officers and every person so authorised may present the case with respect to any appeal before the Appellate Tribunal or the Special Director (Appeals), as the case may be.[58]

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### *3.2.6.18 Members, etc. to be public servants*

The Chairperson, Members and other officers and employees of the Appellate Tribunal, the Special Director (Appeals) and the Adjudicating Authority shall be deemed to be public servants within the meaning of section 21 of the Indian Penal Code (45 of 1860). [59]

### *3.2.6.19 Civil court not to have jurisdiction*

No civil court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which an Adjudicating Authority or the Appellate Tribunal or the Special Director (Appeals) is empowered by or under this Act to determine and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act. [60]

### *3.2.6.20 Appeal to High Court.*

Any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the High Court within sixty days from the date of communication of the decision or order of the Appellate Tribunal to him on any question of law arising out of such order :

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**Provided** that the High Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

*Explanation.*—In this section "High Court" means—

(*a*) the High Court within the jurisdiction of which the aggrieved party ordinarily resides or carries on business or personally works for gain; and

(*b*) where the Central Government is the aggrieved party, the High Court within the jurisdiction of which the respondent, or in a case where there are more than one respondent, any of the respondents, ordinarily resides or carries on business or personally works for gain.[61]

### 3.2.7. *Directorate of enforcement*

#### 3.2.7.1 *Directorate*

The Central Government shall establish a Directorate of Enforcement with a Director and such other officers or class of officers as it thinks fit, who shall be called officers of Enforcement, for the purposes of this Act.

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Without prejudice to the provisions of sub-section (1), the Central Government may authorise the Director of Enforcement or an Additional Director of Enforcement or a Special Director of Enforcement or a Deputy Director of Enforcement to appoint officers of Enforcement below the rank of an Assistant Director of Enforcement. [62]

Subject to such conditions and limitations as the Central Government may impose, an officer of Enforcement may exercise the powers and discharge the duties conferred or imposed on him under this Act.

### 3.2.7.2 *Power of search and seizure, etc.*

The Director of Enforcement and other officers of Enforcement, not below the rank of an Assistant Director, shall take up for investigation the contravention referred to in section 13.

Without prejudice to the provisions of sub-section (1), the Central Government may also, by notification, authorise any officer or class of officers in the Central Government, State Government or the Reserve Bank, not below the rank of an Under Secretary to the Government of India to investigate any contravention referred to in section 13.

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The officers referred to in sub-section (1) shall exercise the like powers which are conferred on income-tax authorities under the Income-tax Act, 1961 (43 of 1961) and shall exercise such powers, subject to such limitations laid down under that Act. [63]

*3.2.7.3 Empowering other officers*

The Central Government may, by order and subject to such conditions and limitations as it thinks fit to impose, authorise any officer of customs or any central excise officer or any police officer or any other officer of the Central Government or a State Government to exercise such of the powers and discharge such of the duties of the Director of Enforcement or any other officer of Enforcement under this Act as may be stated in the order.

The officers referred to in sub-section (1) shall exercise the like powers, which are conferred on the income-tax authorities under the Income-tax Act, 1961 (43 of 1961), subject to such conditions and limitations as the Central Government may impose. [64]

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### 3.2.8. *Miscellaneous provisions*

### 3.2.8.1 *Presumption as to documents in certain cases*

Where any document—

I. is produced or furnished by any person or has been seized from the custody or control of any person, in either case, under this Act or under any other law; or

II. has been received from any place outside India (duly authenticated by such authority or person and in such manner as may be prescribed) in the course of investigation of any contravention under this Act alleged to have been committed by any person,

and such document is tendered in any proceeding under this Act in evidence against him, or against him and any other person who is proceeded against jointly with him, the court or the Adjudicating Authority, as the case may be, shall—

(b) presume, unless the contrary is proved, that the signature and every other part of such document which purports to be in the handwriting of any particular person or which the court may reasonably assume to have been signed by, or to be in the handwriting of, any particular person, is in

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that person's handwriting, and in the case of a document executed or attested, that it was executed or attested by the person by whom it purports to have been so executed or attested;

(c) admit the document in evidence notwithstanding that it is not duly stamped, if such document is otherwise admissible in evidence;

(d) in a case falling under clause (*i*), also presume, unless the contrary is proved, the truth of the contents of such document.[65]

*3.2.8.2 Suspension of operation of this Act*

If the Central Government is satisfied that circumstances have arisen rendering it necessary that any permission granted or restriction imposed by this Act should cease to be granted or imposed, or if it considers necessary or expedient so to do in public interest, the Central Government may, by notification, suspend or relax to such extent either indefinitely or for such period as may be notified, the operation of all or any of the provisions of this Act.

Where the operation of any provision of this Act has under sub-section (1) been suspended or

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relaxed indefinitely, such suspension or relaxation may, at any time while this Act remains in force, be removed by the Central Government by notification.

Every notification issued under this section shall be laid, as soon as may be after it is issued, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the notification or both Houses agree that the notification should not be issued, the notification shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that notification. [66]

### *3.2.8.3 Power of Central Government to give directions*

For the purposes of this Act, the Central Government may, from time to time, give to the Reserve Bank such general or special directions as it thinks fit, and the Reserve Bank shall, in the discharge of its functions under this Act, comply with any such directions. [67]

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### *3.2.8.4 Contravention by companies*

Where a person committing a contravention of any of the provisions of this Act or of any rule, direction or order made thereunder is a company, every person who, at the time the contravention was committed, was in charge of, and was responsible to, the company for the conduct of the business of the company as well as the company, shall be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly:

**Provided** that nothing contained in this sub-section shall render any such person liable to punishment if he proves that the contravention took place without his knowledge or that he exercised due diligence to prevent such contravention.

Notwithstanding anything contained in sub-section (1), where a contravention of any of the provisions of this Act or of any rule, direction or order made thereunder has been committed by a company and it is proved that the contravention has taken place with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of

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the contravention and shall be liable to be proceeded against and punished accordingly.

*Explanation.*—For the purposes of this section—

*(i)* "company" means any body corporate and includes a firm or other association of individuals; and

*(ii)* "director", in relation to a firm, means a partner in the firm. [68]

*3.2.8.5 Death or insolvency in certain cases*

Any right, obligation, liability, proceeding or appeal arising in relation to the provisions of section 13 shall not abate by reason of death or insolvency of the person liable under that section and upon such death or insolvency such rights and obligations shall devolve on the legal representative of such person or the official receiver or the official assignee, as the case may be:

**Provided** that a legal representative of the deceased shall be liable only to the extent of the inheritance or estate of the deceased. [69]

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### *3.2.8.6 Bar of legal proceedings*

No suit, prosecution or other legal proceeding shall lie against the Central Government or the Reserve Bank or any officer of that Government or of the Reserve Bank or any other person exercising any power or discharging any functions or performing any duties under this Act, for anything in good faith done or intended to be done under this Act or any rule, regulation, notification, direction or order made thereunder. [70]

### *3.2.8.7 Removal of difficulties*

If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order, do anything not inconsistent with the provisions of this Act for the purpose of removing the difficulty:

**Provided** that no such order shall be made under this section after the expiry of two years from the commencement of this Act.

Every order made under this section shall be laid, as soon as may be after it is made, before each House of Parliament. [71]

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### *3.2.8.8 Power to make rules*

The Central Government may, by notification, make rules to carry out the provisions of this Act.

Without prejudice to the generality of the foregoing power, such rules may provide for,—

*(a)* the imposition of reasonable restrictions on current account transactions under section 5;

*(b)* the manner in which the contravention may be compounded under sub-section (1) of section 15;

*(c)* the manner of holding an inquiry by the Adjudicating Authority under sub-section (1) of section 16;

*(d)* the form of appeal and fee for filing such appeal under sections 17 and 19;

*(e)* the salary and allowances payable to and the other terms and conditions of service of the Chairperson and other Members of the Appellate Tribunal and the Special Director (Appeals) under section 23;

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(*f*) the salaries and allowances and other conditions of service of the officers and employees of the Appellate Tribunal and the office of the Special Director (Appeals) under sub-section (3) of section 27;

(*g*) the additional matters in respect of which the Appellate Tribunal and the Special Director (Appeals) may exercise the powers of a civil court under clause (*i*) of sub-section (2) of section 28;

(*h*) the authority or person and the manner in which any document may be authenticated under clause (*ii*) of section 39; and

(*i*) any other matter which is required to be, or may be, prescribed.[72]

*3.2.8.9 Power to make regulations*

The Reserve Bank may, by notification, make regulations to carry out the provisions of this Act and the rules made thereunder.

Without prejudice to the generality of the foregoing power, such regulations may provide for,—

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(*a*) the permissible classes of capital account transactions, the limits of admissibility of foreign exchange for such transactions, and the prohibition, restriction or regulation of certain capital account transactions under section 6;

(*b*) the manner and the form in which the declaration is to be furnished under clause (*a*) of sub-section (1) of section 7;

(*c*) the period within which and the manner of repatriation of foreign exchange under section 8;

(*d*) the limit up to which any person may possess foreign currency or foreign coins under clause (*a*) of section 9;

(*e*) the class of persons and the limit up to which foreign currency account may be held or operated under clause (*b*) of section 9;

(*f*) the limit up to which foreign exchange acquired may be exempted under clause (*d*) of section 9;

(*g*) the limit up to which foreign exchange acquired may be retained under clause (*e*) of section 9;

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*(h)* any other matter which is required to be, or may be, specified.[73]

*3.2.8.10 Rules and regulations to be laid before Parliament.*

Every rule and regulation made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or regulation, or both Houses agree that the rule or regulation should not be made, the rule or regulation shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule or regulation.[74]

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### *3.2.8.11 Repeal and saving*

The Foreign Exchange Regulation Act, 1973 (46 of 1973) is hereby repealed and the Appellate Board constituted under sub-section (1) of section 52 of the said Act (hereinafter referred to as the repealed Act) shall stand dissolved.

On the dissolution of the said Appellate Board, the person appointed as Chairman of the Appellate Board and every other person appointed as Member and holding office as such immediately before such date shall vacate their respective offices and no such Chairman or other person shall be entitled to claim any compensation for the premature termination of the term of his office or of any contract of service.

Notwithstanding anything contained in any other law for the time being in force, no court shall take cognisance of an offence under the repealed Act and no adjudicating officer shall take notice of any contravention under section 51 of the repealed Act after the expiry of a period of two years from the date of the commencement of this Act.

Subject to the provisions of sub-section (3) all offences committed under the repealed Act shall continue to be governed by the provisions of the repealed Act as if that Act had not been repealed.

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Notwithstanding such repeal,—

*(a)* anything done or any action taken or purported to have been done or taken including any rule, notification, inspection, order or notice made or issued or any appointment, confirmation or declaration made or any licence, permission, authorization or exemption granted or any document or instrument executed or any direction given under the Act hereby repealed shall, in so far as it is not inconsistent with the provisions of this Act, be deemed to have been done or taken under the corresponding provisions of this Act;

*(b)* any appeal preferred to the Appellate Board under sub-section (2) of section 52 of the repealed Act but not disposed of before the commencement of this Act shall stand transferred to and shall be disposed of by the Appellate Tribunal constituted under this Act;

*(c)* every appeal from any decision or order of the Appellate Board under sub-section (3) or sub-section (4) of section 52 of the repealed Act shall, if not filed before the commencement of this Act, be filed before the High Court within a period of sixty days of such commencement :

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**Provided** that the High Court may entertain such appeal after the expiry of the said period of sixty days if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period.

Save as otherwise provided in sub-section (3), the mention of particular matters in sub-sections (2), (4) and (5) shall not be held to prejudice or affect the general application of section 6 of the General Clauses Act, 1897 (10 of 1897) with regard to the effect of repeal.[75]

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*End Notes:*

1. Section 3
2. Section 3(2)
3. Section 3(3)
4. Kamleshkumar Patel v/s Union of India, 1995
5. TA Abdul Rehman v/s State of Kerala, 1991
6. Section 7
7. Abdul Sathari Ibrahim Manik v/s Union of India, AIR 1992 SC 1900
8. KPM Bashir v/s State of Karnataka, AIR 1993 SC 1353
9. Section 5
10. Section 5A
11. Section 5A(b)
12. Section 6
13. Section 12(3)
14. Section 8(e)

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15. Section 10

16. Proviso to Section 10

17. Section 2(f)

18. Section 2(i)

19. Section 2(p)

20. Section 2(q)

21. RBI notification no.114/92 dated 27th April 1992

22. RBI notification no.114/92, 66/86, 85/89, 23/92 as amended on 26th April 1993

23. Section 2 (z)

24. Section 2 (za)

25. Section 2 (zb)

26. Section 2 (zc)

27. Section 2 (zd)

28. Section 2 (ze)

29. Section 6

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30. Section 5

31. Section 7

32. Section 3

33. Section 4

34. Section 8

35. Section 9

36. Section 10

37. Section 11

38. Section 12

39. Section 13

40. Section 14

41. Section 15

42. Section 16

43. Section 17

44. Section 18

45. Section 19

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| | | |
|---|---|---|
| 46. | Section | 20 |
| 47. | Section | 21 |
| 48. | Section | 22 |
| 49. | Section | 23 |
| 50. | Section | 24 |
| 51. | Section | 25 |
| 52. | Section | 26 |
| 53. | Section | 27 |
| 54. | Section | 28 |
| 55. | Section | 29 |
| 56. | Section | 30 |
| 57. | Section | 31 |
| 58. | Section | 32 |
| 59. | Section | 33 |
| 60. | Section | 34 |
| 61. | Section | 35 |

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62. Section 36

63. Section 37

64. Section 38

65. Section 39

66. Section 40

67. Section 41

68. Section 42

69. Section 43

70. Section 44

71. Section 45

72. Section 46

73. Section 47

74. Section 48

75. Section 49

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# CHAPTER 4

# *Foreign Trade Impact Analysis*

## 4.1 Foreign Trade Policy

Each and every policy swing in some sense reflects the Government's particular types of responses to the foreign exchange crisis in the respective periods. Though, many factors may have been at work causing the policy swing. The point of emphasis is the undercurrent of the Balance of Payment crisis in shaping the country's attitude and policy towards foreign investment. Changes in policy frameworks in India dealing with private financial and investment inflows can be studied in four phases.

1. Cautious welcome policy from independence to the emergence of crisis in the late sixties.

2. Selective and restrictive policy from 1967 to the end of oil crisis in 1979.

3. Partial liberalisation policy from 1980 to 1990

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4. Gradual opening up of the economy from 1990

India's foreign trade policy has been historically based on certain presumptions:

(1) Foreign exchange scarcity

(2) Poor Balance of Payment situation

(3) Provision of foreign exchange only for purposes of national importance or inevitability

Industrialisation and self-sufficiency in food production and other essential commodities were the objectives of India's trade and business policies in the period after independence. It was feared that dependence on other, more powerful countries for imports of essential commodities would lead to political dependence on them as well. Nearly a decade before independence, in 1938, the National Planning Committee was set up by the Indian National Congress under the chairmanship of future Prime Minister Jawaharlal Nehru. This committee viewed that "in the context of the modern world, no country can be politically and economically independent, even within the framework of international independence, unless it is highly industrialised and has developed its power resources to the utmost. Nor can it achieve or maintain high standards of living and liquidate poverty without the aid of modern technology in

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almost every sphere of life. An industrially backward country will continually upset the world equilibrium and encourage the aggressive tendencies of more developed countries. Even if it retains its political independence, this will be nominal only and economic control will tend to pass to others. The objective for the country as a whole was the attainment, as far as possible, of national self-sufficiency, international trade was certainly not excluded, but we were anxious to avoid being drawn into the whirlpool of economic imperialism."

This thinking was supported by the First Five Year Plan as: "Control and regulation of exports and imports, and in the case of certain select commodities state trading, are necessary not only from the point of view of utilising to the best advantage the limited foreign exchange resources available but also for securing an allocation of the productive resources of the country inline with the targets defined in the Plan."

Thus, a system of wide government control over production, investment, technology and locational choice, prices and foreign trade was instituted in the mid-1950s. In the following years this development strategy based on import-substituting industrialisation and the system of controls that were implemented failed to produce rapid growth, self reliance, and eradication of poverty, but instead led to lacklustre growth, an internationally uncompetitive infrastructure, a perpetually

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precarious balance of payments, and above all, rampant rent seeking and the corruption of social, economic and political systems.

## 4.2 The Planning Era

India adopted its Constitution on 26th January 1950, and within just three months, i.e. in March the Planning Commission was established as an advisory body with no executive functions. There had been a broad consensus on the need for planning for national development even during the struggle for independence from Britain. Indeed, soon after the National Planning Commission was established in 1938, a group of private businessmen produced the Bombay Plan. Even the colonial government had put together development plans for post-war India. The adoption of the Constitution, however, gave a particular impetus to planning.

The objectives of national planning were laid down in the Directive Principles of State Policy. They suggested that, "the state should strive to secure a social order in which justice – economic, social and political – shall inform all the institutions of national life" and "to minimise inequality in income, status and facilities and opportunities, amongst individuals and groups." Further, the state was required to ensure "that ownership and control of the material resources of the community are so distributed as best to

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subscribe common good; that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment." The government was also supposed to protect the right to work, education, and to public assistance in case of unemployment, disability, or sickness. It is evident that these principles envisaged a dominant role for the state in achieving an egalitarian society through state intervention in economic activity. Besides the goal of poverty alleviation, the three broad objectives of the Indian development strategy are economic growth, self-reliance, and social justice. Even though the state was assigned a dominant role in developing the economy, leaders across the political spectrum recognised to varying degrees that India had a mixed economy with a significant private sector, and more importantly, that the private sector had a political role in ensuring social stability in the functioning of the democratic framework of the constitution.

Indian economic policy and planning had a significant socialistic bias inspired from the erstwhile USSR (United Soviet Socialist Republic). Although Soviet planning operated with totalitarian political control of the society and state ownership of the means of production, India's mixed economy and democratic policy ruled out planning by command. Instead, the policy framework had to create incentives for the private sector to conform to the priorities of the plan. In designing such a framework, the Indian

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policy makers opted in most cases for direct, discretionary, non-market, quantitative controls over indirect, rule-based, market-mediated controls operating through price mechanism. Unfortunately, this choice adversely affected economic growth, efficiency and equity.

Almost throughout the entire planning period agriculture has dominated the economy. Agriculture accounted for nearly 60% of Gross Domestic Product and provided employment to 70% of the total work force in the year1950. Its share drastically to around 20% in 2001-02, but it still provides employment to more than 60% of the total work force. This fact implies that the Indian industrialisation strategy failed to generate significant productive employment opportunities outside agriculture for rapidly growing work force. No significant redistribution of land emerged from the land reform legislation of the 1950s. Concentration of land ownership, however, has not meant that a large proportion of farms are operated on a large scale. In 1982, only 20% of the farm area was operated in land holdings exceeding 10 hectares. Early planners showed some enthusiasm for cooperative farming. The National Commission on Agriculture, in the year 1976, concluded that under Indian conditions, small peasant-owned farms cultivated mainly with family labour should be the preferred form of organisation of production rather than large Soviet-style collective farms or large capitalist farms cultivated with mechanisation in some regions and the emergence

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of large capital farms, particularly in the fast growing agricultural regions of Punjab and western Uttar Pradesh, small owner-operated farms, however continue to be the dominant mode of operation.

Agriculture has also been under state intervention, though has been different than in the case of industries. In agriculture, the state has made substantial investments in irrigation, fertilizer production, and infrastructure. Other state interventions affected the prices that farmers paid for their inputs and received for their outputs. Prices paid for the part of output that was purchased by the government for its subsidised distribution were regulated. There were some quantitative restrictions, such as the ban on interstate movement of food grains on private account, but these were abandoned early on. Policies that placed quantitative restrictions on millions of individual producers were obviously infeasible, although access to subsidised credit is an exception. Remarkably, India has maintained a constant trend growth in agricultural output of about 3% per year over nearly four decades despite slow growth in cultivated area. This trend reflects the superiority of the largely market-mediated interventions in agriculture, unlike the discretionary interventions in industry.

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## 4.3 Planning and industrial development

The Industrial Policy Resolution of 1948 divided the industrial structure of India in three broad constituents:

(1) Industries to be developed exclusively by the public sector. These included key and strategically important industries like railways, defence equipments, etc.

(2) Industries reserved for the private sector, which included mostly industries producing consumer goods, and non-essential items.

(3) Industries open for either sectors, but with greater regulation for units established by private sector.

The development of key industries, such as railways, telecom, electricity generation and defence equipments were vested in the hands of public sector. Industries producing key industrial raw materials and equipments, such as steel, petroleum and heavy machinery, electric generators, etc. were also reserved for the public sector. The rationale behind the resolution was that by controlling the apex of the industrial structure – that is, the infrastructure and industries supplying key inputs – the state could cause the development of all industries, in the private and

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public sectors, to follow socially desirable directions. Goods and services produced and supplied by the public sector could be priced appropriately for generating surpluses to be used for investment in the public sector and to finance other public expenditure. Also, the state hoped to promote the development of backward regions through location of public sector projects. Finally, the public sector was to be made role model for the private sector firms to follow with respect to the wages and conditions of the workers. But this policy of investment in government public sector undertakings at the cost of infrastructure development did not bring desired results. A major share of investment in the five-year plans was allocated to the public sector undertakings. Yet, the enterprises created by this investment and others acquired through nationalisation performed poorly in supplying key services and inputs at reasonable price and thus defeated their objectives. The public sector, on the other hand, acted as a break on private sector development, rather than promoting and channelling it in socially desired directions.

The main reasons cited for the under-performance of the public sector include,

(1) Incorrect policy decisions regarding location of units,

(2) Adoption of backward technology,

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(3) Unnecessary employment orientation,

(4) Inefficient price mechanism and pricing policies,

(5) Politicisation of operations,

(6) Inefficient organisation and management,

(7) Waste in use of resources,

(8) Mounting losses.

The necks of private sector firms were tightened in the form of industrial licensing and exchange control to make them follow the planned pattern. The broad features of such restrictive policy instruments remained essentially unchanged from the late 1950s to the reforms of 1990s, though their severity waxed and waned. The system was meant to achieve several goals.

(1) To make capacity created in the private sector consistent with plan targets.

(2) To locate the private sector firms in such a way that they do not overload the infrastructure, particularly in cities and other areas

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to which they would naturally gravitate. The system induced plant owners to move to backward regions with potential for development.

(3) To promote the objective of self-reliance. This implied promoting domestically available technology, equipment and raw materials against imports.

(4) To prevent concentration of economic power in the hands of few.

Given the perennial shortage of foreign exchange for imports of equipment at the time of investment and for imports of raw materials and spares during the lifetime of the plant.

Similarly, an industrial license was required to invest in capacity creation if the quantity of investment or the value of equipment imports exceeded specified limits. For importation of equipment, a capita-goods license was needed. If foreign collaboration was involved, a separate clearance was required. In particular, foreign equity participation was limited to below 50%, with some exceptions. If foreign technology imports involving royalty payments were to be undertaken, yet another clearance was mandated. If part of the equity was to be obtained by selling

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shares in domestic capital market, permission of the controller of capital issue had to be taken. Even the investment projects of public enterprises required many of these permits, in addition to clearances from the ministry or department in charge of the enterprise and from other relevant ministries. In sum, several hurdles had to be crossed before a single rupee was spent on any project in the private as well as public sector. Even though success in obtaining all the required clearances was by not means assured, entrepreneurs had to expend considerable time and resources pursuing them.

The licensing system was adopted to evaluate proposed projects and to disprove those schemes which were not expected to materialise the goals of planning and which may dislocate country's scarce resources. The criteria for evaluation of applications were sufficiently broad that the licensing authorities had substantial discretion in granting or denying a license. The licensing bureaucrats and their political bosses were under constant pressure from interested parties. It should cause no surprise that the exercise of their discretionary power led to their corruption and the politicisation of decisions. Obviously, a private entrepreneur would apply for a license in a project only if he expected it to be profitable. The license could be denied, of course, if the project was deemed socially unworthy. But licensing authorities could not induce a private sector entrepreneur to apply for a license and invest in a

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socially worthy project if he did not find it privately profitable. The grant of license did not necessary mean that the capacity licensed came on stream, and even if it did, that it became operational at the time specified in the application. Since the processing of license application often took so long and restrictive conditions were often attached to accepted applications, it was possible that the project for which a license was granted would not longer be profitable from the applicant's perspective and hence he would choose not to implement it. Further, given that license were granted only to the extent of capacity expansion called for in the relevant five-year plant, firms had a built-in incentive to take out a license and then fail to invest, essentially to foreclose competition by preventing firms from getting it. An information system to keep track of the licenses granted and their implementation did not exist, so the ink between capacity increases targeted in the plan and their actual realisation through licensing was tenuous. In the final analysis, the procedure for license granting became ad hoc and followed rules of thumb rather than any economic rationale. It degenerated into an exercise in dispensing political and other kinds of patronage and a source of rents for personal and political use rather than a guidance mechanism for directing private sector to conform to the plans.

The comparison of development of Indian economy with other developing countries during the planning period reveals that Indian

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performance is relatively poor. India's average annual rate of growth of per capita GNP from 1965 to 1990 is the lowest among the five comparable economies viz. India, China, Brazil, Mexico and Korea. In 1965, India's manufacturing industry was more than five times the size that of Korea in terms of value added at current US dollars. But by 1990 Korea's manufacturing industry had grown to exceed that of India, and its manufactured exports were nearly five times that of India. Only China, which also followed an inward-oriented development strategy until recently, had a greater share of the labour force in agriculture than India. *Table 1*

**Table 1**

Selected indicators for India and other developing countries

| **Indicator** | *India* | *China* | *Brazil* | *Mexico* | *Korea* |
|---|---|---|---|---|---|
| Population in mid 1990 (millions) | 850 | 1134 | 150 | 86 | 43 |
| GNP per capita, in 1990 (US$) | 350 | 370 | 2680 | 2490 | 5400 |
| Average annual GNP growth rate (%) | 1.9 | 5.8 | 3.3 | 2.8 | 7.1 |

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| | | | | | |
|---|---|---|---|---|---|
| Inflation rate 1980-90 (%) | 7.9 | 5.8 | 284.3 | 70.3 | |
| Share in GDP of agriculture (%) | 31 | 27 | 10 | 9 | 9 |
| Value added in manufacturing, 1989 (US$ billion) | 44 | 146 | 121 | 51 | 66 |
| Gross domestic investment as % of GDP | 23 | 39 | 22 | 20 | 37 |
| Gross domestic savings as % of GDP | 20 | 43 | 23 | 19 | 37 |
| **Social indicators** | | | | | |
| Life expectancy, 1990 | 59 | 70 | 66 | 70 | 71 |
| Total fertility rate, 1990 | 4.0 | 2.5 | 3.2 | 3.3 | 1.8 |
| Labour force | 63 | 74 | 29 | 23 | 18 |

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| | | | | | |
|---|---|---|---|---|---|
| in agriculture (%) | | | | | |
| Merchandise exports, 1990 (US$ billion) | 18 | 62 | 31 | 27 | 65 |
| Manufactured exports, 1990 (US$ billion) | 13 | 45 | 16 | 21 | 61 |
| Merchandise imports, 1990 (US$ billion) | 24 | 53 | 22 | 28 | 70 |
| Aggregate net resource flow, 1990 (US$ billion) | 3.6 | 10.1 | 1.2 | 8.4 | -0.2 |
| Total outstanding external debt, 1990 (US$ billion) | 70.1 | 52.6 | 116.2 | 96.8 | 34.0 |
| Total outstanding debt service/exports (%) | 29 | 10 | 21 | 28 | 11 |

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| | | | | | |
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| Overall central government surplus, 1990 (% of GNP) | -7.3 | NA | -16.6 | 0.8 | -0.7 |

*Source:* Human Development Report, 1992

## 4.4 Phases of change in foreign trade regimes

Prominent economists J. Bhagwati and A. Krueger, in their competitive analysis of the impact of foreign trade regimes on economic development in a number of countries, defined a set of analytical phases in which an exchange control regime may be found. According to their hypothesis, all countries pass through these five phases. These phases are as discussed below:

*Phase 1:*

During this phase, quantitative restrictions (QRs) on international transactions are imposed, generally in response to unsustainable balance of payments deficit, and then, after a period are intensified. The period during which reliance upon QRs for containing balance of payment is deficit is an important feature of Phase 1.

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*Phase 2:*

While QRs continue to be intense, various measures are undertaken to offset some of the undesired results of the system. Heightened tariffs, surcharges on imports, rebates for exports, special tourist exchange rates, and other price interventions are used. However, QRs continue to be relied upon as the primary means for controlling the balance of payments deficit.

*Phase 3:*

An attempt is made to systematize the changes introduced during phase 2. This phase often starts with a foreign exchange rate change and may be accompanied by removal of some of the surcharges and other special measures imposed during phase 2 and by reduced reliance upon QRs. Phase 3 may end up being little more than a tidying-up operation, in which case the chances are high that the country will re-enter phase 2. The country may also move beyond the tidying and signal the beginning of withdrawal from reliance upon QRs, in which case enters phase 4.

*Phase 4:*

If the response to changes introduced in phase 3 is encouraging enough for the continuation and extension of liberalisation, the country is said to enter phase 4. A favourable response in the form

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of increased foreign exchange earnings would encourage gradual relaxation of QRs or increased foreign exchange allocations, thus reduced premiums, under the same administrative system.

*Phase 5:*

The exchange regime is fully liberalised. There is full convertibility on current account, and QRs are not longer employed as a means of regulating balance of payments situation.

## 4.5 Analytical phases of foreign trade policy in India

*Phase IV (1950 to1956)*

This period was relatively stable than the following years in terms of balance of payment position and overall economic progress. The export earnings sufficed import payments, though the exports earnings were stagnant. The machinery import control inherited from the World War II period was not used in any systematic way to impose Quantitative Restrictions.

*Phase I (1956 to 1962)*

The implementation of heavy industry-oriented Second Five-Year Plan gave rise to severe balance of payments crisis in 1957. Instead of adopting appropriate macro-economic policies including

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making exchange rate adjustments, the government imposed a regime of Quantitative Restrictions on imports. The QRs and the industrial licensing system were both selective rather than across-the-board. Besides containing the demand for foreign exchange, the selectivity of QRs served the objective of the development of particular industries through import substitution. The QR regime was used to provide automatic and custom-made protection to any domestic activity that substituted imports. Foreign aid flows increased substantially from less than 0.5% of net national product in the pre-1956 period to over 3 % in 1960-61.

*Phase II (1962 to 1966)*

The QR regime initiated in 1957 continued during this period. This measure was accompanied with export subsidization in 1962, primarily to offset the penalties that the QR regime was in effect imposing on exports. Two exogenous events in the period had major consequences: The Indo-Pakistan war of 1965 and the consequent suspension of foreign aid and a major drought in the agricultural year 1965-66, which affected traditional exports severely and increased the need of food imports. Increasing use was made of import duties, in part to mop up the premia on imports that license receivers were realising. Export subsidisation and increasing import duties could be viewed as a de facto devaluation of the exchange rate although

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unlike in de jure devaluation, the impact was selective. Some efforts to loosen up the industrial licensing system were made toward the end of the period. By early 1966, the combined effects of the drought and suspension of aid caused import premia to rise to unprecedented levels. The donors of bilateral and multilateral external aid made resumption of the large-scale aid and access to short-term credit conditional on the liberalisation of the economy.

*Phase IIII (1966 to 1968)*

The first step in the liberalisation was the devaluation of the rupee by 57.5% announced in June 1966. Since this was also accompanied by elimination of export subsidies and reduction of import duties, the net devaluation after allowing for these changes was on average less than the gross devaluation of 57.5% and varied among commodities. According to Bhagwati and Srinivasan, the total net devaluation on the trade account was 21.6% of exports and 42.3% for the imports. On the current account, the total net devaluation was 22.3% for receipts and 44.8% for payments. In 1966-67 another disastrous drought followed that of 1965-66. The two severe droughts in succession resulted in price increases, adverse effects on traditional exports, and an industrial recession induced by shortage of agro-based raw materials. Economic liberalisation, of which devaluation was a major component, was stalled in

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part for economic reasons related to drought. More importantly, the economic difficulties were accentuated by political problems; the fact that devaluation was seen as capitalisation to pressure from donors of external aid made liberalisation politically suspect, not only among the opposition but also within the ruling Congress party led by the newly installed and politically insecure Prime Minister Indira Gandhi. The 1967 general election saw considerable erosion of support, the external aid promised at the time of devaluation, which was meant to ease the short–run costs of adjustment to a liberalised economy did not materialise. Under the circumstances, it was not surprising that the hesitant step towards liberalisation introduced with devaluation were soon abandoned.

*Phase II (1968 to 1975)*

This period marked one of the most restrictive phases of India's foreign and trade policy. With the abandonment of liberalisation, import premia rose, though not as high as immediately before devaluation. Export subsidies were reinstated and augmented. Industrial licensing reverted to its severely restrictive mode. The economy experienced several exogenous shocks during the period. First, the Bangladesh War of 1971 and the refugee inflow that preceded it created severe economic strains. Second, adverse weather conditions during the 1972-1975 period led to stagnant agricultural output and double-digit

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inflation for two years in a row in 1972-73 and 1973-74. Third, the Breton Woods system of fixed exchange rate parties collapsed in 1971 and 1975 the pound depreciated against the US$ and other major currencies, leading to a gradual and modern depreciation of rupee against the US$ in that period. This depreciation of the rupee provided across-the-board incentives for exports and import substitution. But with the linked to a basket of currencies, its vicarious devaluation was halted. Fourth, in 1973 the first oil shock occurred.

The period was marked by increasingly restrictive and complex import policy. Scarcity of foreign exchange became even more acute, and a new set of restrictive measures was introduced every year. Import allocation criteria became more complex and subject to marginal conditions. Tariff rates were gradually escalated to absorb partially the increasing import premia generated by tighter Quantitative Restrictions.

*Phase III (1975 to 1985):*

Foreign exchange availability improved dramatically during the early part of the period 1975-1985. Net reserves of foreign exchange went up from a low of US$ 758 million to a high of US$ 7579 million in 1979-80. This change in phenomenon was cause partly by the dramatic increase in remittances from Indians working in West Asia. The decline in public investment and

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the slowing of industrial growth after the mid-1960s also contributed to reducing pressure in the balance of payments. With dramatic increase in the output of wheat, and to a smaller extent of rice, during the green revolution, the public stock of food grains mounted and imports of food grains ceased. The net result was the relaxation in the severity of QRs. Import allocation rules were made simpler and most non-competing essential imports were liberalised. Protective quotas, however, remained intact and domestic industry continued to be completely shielded from import competition. Interestingly, the second oil shock in 1979 did not lead to a tightening of the QR regime, partly because of the substantial increase in the worker remittances and partly because of the fortuitous discover and development of significant offshore oil deposits in the Arabian Sea. Output of crude oil more than doubled, from 8.4 million tons in 1975-76 to 21.1 million tons in 1982-83.

In April 1985, in a significant departure, the government announced that the import and export policy was to cover a period of three years rather than six months or a year as in the past. This innovation was meant to bring some stability to the policy and thereby reduce the uncertainty about year-to-year changes that exporters and importers faced. Yet the government could not resist introducing changes frequently. Until 1988, there were 250 public notices regarding changes in the policy. The subsequent policy statement for the period 1988-1991, announced in April 1988,

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candidly recognised that changes have to be announced within the three-year period and stated, "it is proposed to issue a revised version of the import and export policy at the beginning of each year." Though the complexity of the scheme of QRs had not diminished substantially, the two three-year policies did represent some major simplifications. In particular the number of items in the category of Open General License, a license to import but with the quantitative restrictions, for capital goods had increased from nil in 1975 to over 1100 items in the 1988-91 policy. Similarly, many intermediate goods were put in the OGL category. Though, these items constituted non-competitive imports. Therefore, lifting QRs on their import had little effect on import competition with domestic production. Also, the import of some items formally in the OGL category was restricted on other grounds. For example, the value of equipment imports had to conform to licensed investment capacity. Although tires had been in the OGL category since 1978, no imports took place, in part because actual users such as car and truck manufacturing firms were under phased manufacturing programmes through which they were under an obligation to replace imports by domestic substitutes over time in a progressive manner. The share of the value of imports covered by OGL in total imports appeared to be modest.

*Phase IV (1991 to 2004)*

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The year 1991 ushered a new era in Indian economy. In July 1991, the newly installed minority government of P.V. Narsimha Rao announced a set of major economic reforms. In announcing the reforms to the Indian Parliament, the then Finance Minister Dr. Manmohan Singh declared that "Let the world hear it loud and clear. India is now wide-awake. The emergence of India as a major power in the world is an idea whose time has come." The proximate reason for these policy changes was a crisis in the economy that was both acute and different from anything experienced in the post-independence era – a drastic fall in the foreign exchange reserves to a level not even enough to pay for three weeks of imports, a near default in the colossal external debt of over US$ 71 billion, and a fiscal deficit of nearly 9% of GDP. But the deeper reason for the changes was the realisation that India's economic development strategy since 1950 and the regulatory framework created to implement it had failed miserably. The policy reforms were further extended in scope and coverage in 1992.

The pillars of the 1991 reforms were,

(1) Currency devaluation,

(2) Abolition of import licensing replacement of cash subsidies for exports, initially by

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the so-called exim scrips (free saleable rights to imports linked to exports) and later by partial convertibility of rupee under which exporters could sell 60% of their foreign exchange receipts at a market determined exchange rate,

(3) Abolition of industrial licensing except for investment in eighteen industries and for locational reasons in cases of industries with potential of pollution creation,

(4) Relaxation of restrictions on large industrial houses under the Monopolies and Restrictive Trade Practices Act,

(5) Easing of entry requirements (including equity participation) for foreign direct investment, and

(6) Allowance of private investment in some industries hitherto reserved for public sector investment.

A National Renewal Fund for assisting workers employed in public sector undertakings, which would have to be scaled down, or closed altogether was established, although without the support of political barons of the labour aristocracy in the organised sector such scaling down was difficult. The government contemplated reform of the financial sector, which is largely left to be implemented.

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These reforms were systematic and went beyond liberalising the more irksome controls at the margin that earlier economic liberalisations attempted. Besides, the authorities apparently realised that the benefits from reforming one sector would be limited if other related sectors are not reformed. The needed reforms are conceived as package of mutually supporting and consistent elements that call for coordinated action in several areas. The elimination of import licensing and the introduction of partial convertibility of rupee are suggestive of entering of Indian economy in phase IV. Since the reforms have been in place only since July 1991, a period of recession and break-up of the Soviet Union with whom India had barter trade relations, the effect of reforms could only be seen after the year 1994-95.

### 4.6 Structure of pre-1991 exchange control mechanism

The pre-1991 exchange control mechanism divided imports into three broad categories:

(1) Consumer goods,

(2) Capital goods,

(3) Intermediate goods, which included raw materials, components, spares and other supplies.

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Consumer goods imports, other than those canalised and imported by state agencies such as food grains, edible oils, sugar, and certain drugs and medicines) were not permitted. Other imports were divided into the following licensing categories:

(1) Non-permissible,

(2) Limited permissible,

(3) Automatic permissible, and

(4) Items covered under Open General License (OGL).

The allocation of permissible imports by sector of use (private and public), by type of good (consumer, capital, and intermediate), by industry, and by firm within industries was carried out by elaborate administrative machinery. For example, Volume 1 of the 1988-1991 policy statement relating only to import policy consists of 387 pages, divided into twenty-three chapters and seventeen appendices. Broadly speaking, the complex system of import control persisted through 1951 to 1991 period. Though, some categories were introduced and some were disposed, but more or less the character and spirit of the import control machinery remained the same. The OGL category of imports gained a lot of importance: the 1988-91 statement listed 66 items,

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the import of which were canalised through public sector agencies, ranging from paraffin wax to steel, petroleum products, fertilisers and fatty acids.

The import control regime inevitably led to a lower effective exchange rate for exports than for imports on the average and for each industry. The scheme of export subsidisation, initiated in 1962 in an attempt to redress this bias against exports, was extremely complex with little or no economic logic to support its complexity. Subsidies took essentially two major forms:

(1) Direct subsidies through fiscal measures, and

(2) Indirect subsidies to import entitlement schemes that entitled to scarce and restricted imports.

Some other relatively minor promotional activities included budgetary allocations for market development.

Referring to the specific subsidy schemes, it is worth mentioning that analogous to the category of non-permissible and restricted imports, there were also non-permissible and restricted exports. As of 1988, there were 172 such products, 67 of which could simply not be exported. An important difference, however, was that exports of items not on this list could be made without a license, while

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a license was required for any item other than personal baggage.

In the matter of export assistance, fiscal measures were tax drawback schemes, which included refunds of indirect taxes including import duties on inputs used exports; exemptions from sales taxes; cash compensation schemes, and rail freight concessions. Import replenishment licences, previously called import entitlement certificates, allowed the exporter to import certain restricted raw materials and components. Whereas under the import entitlement certificate scheme the value of the entitlement equalled twice the import content, under the import replenishment license scheme the value of license was supposed to equal the actual import content of exports. Between July 1991 and February 1992 such licenses were called exim scrips.

Import entitlements, as a proportion of the FOB values varied widely across different products. Since it was virtually impossible to assess the actual import content, such variation was more a reflection of arbitrary assignment by policy makers than of variation of actual import contents. There were 58 pages in Appendix 17 and its annexes to the 1988-1991-policy statement on import replenishment license. For example wheat bran exporters were given import replenishment licenses at the rate of 3 % and permitted to import under those licenses only silk and nylon bolting cloth. Unlike actual user licenses, import

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replenishment licenses could be sold and transferred subject to certain conditions. Exporters were registered and classified under various categories such as manufacturer exporter, merchant exporter, export house and deemed exporter.

The compensatory cash support scheme was initially introduced to compensate for taxes not refunded under the duty drawback scheme and for any excess of short-run marginal cost of production over FOB realisation. It was later extended to compensate for a host of factors, including losses incurred on exports when domestic demand was inadequate to use installed capacity fully. The rates of compensatory cash support also varied significantly across products with no apparent rationale. The rationale of most of the export assistance schemes was that Indian exporters should be compensated for the excess costs they incurred compared to their competitors because of other distortions in the Indian economy. Since these excess costs were hard to quantify, there was no way to establish that the local assistance received under various incentive schemes to which a potential exporter was entitled was more or less than necessary to induce him to export. The bureaucratic requirements to be met in order to claim assistance available under these schemes were complex, time consuming, and costly. Small-scale exporters often did not find it worthwhile to claim the incentive schemes to which they were entitled. As is the case of import

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controls, export incentives were made complex without any functional need for such complexity. By eliminating import licensing and introducing partial convertibility of the rupee, the 1992 reforms eliminated at one stroke the maze of complexity and variance in incentives across commodities of the import replenishment and compensatory cash support schemes

## 4.7 Performance of foreign trade

Since the purpose of the import control regime was to confine imports to certain essential consumer goods, raw materials, and investment goods needed for domestic production and exports, it is not surprising that changes in the commodity composition India's imports reflected this. For example, food grains and edible oil accounted for about 16% of total imports in 1960-61 and about 1% in 1990-91. Imports of gems, which were negligible accounted for US$ 2.079 million or nearly 8% of imports in 1990-91, reflected the fact that gems and jewellery exports at $1.667 million comprised nearly a sixth of total exports. The share of crude petroleum, oils and lubricants in total imports rose from about 6% in 1960-61 to a high of roughly 40% in 1980-81 only to fall to about 23% in 1990-91, reflecting in part, the rise and fall of petroleum prices and in part the rapid growth of domestic crude output from the Bombay High Field. *Table 2*

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**Table 2**

India's merchandise imports, 1950-51 to 1990-91 (US$ million at current prices)

| Item | 1950-51 | 1960-61 | 1970-71 | 1980-81 | 1990-91 |
|---|---|---|---|---|---|
| Food grains | NA | 378.4 | 271.8 | 483 | 533 |
| Petroleum and its by-products | 116.4 | 144 | 181.2 | 6669 | 5726 |
| Fertilizers | 25.9 | 22.3 | 100.9 | 210 | 338 |
| Other raw materials | NA | 10.8 | 32.4 | 529 | 1766 |
| Iron and steel | 42 | 257.3 | 196.1 | 1080 | 1231 |
| Non-ferrous metals | 59.4 | 99.4 | 159.2 | 605 | 618 |
| Metals ores and scraps | 0.9 | 7.0 | 14.6 | NA | NA |
| Edible oils | NA | 7.4 | 30.6 | 865 | 180 |

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| | | | | | |
|---|---|---|---|---|---|
| Non-edible oils | NA | 2.7 | 20.7 | NA | NA |
| Oilseeds | 4.8 | 24.4 | 8.5 | NA | NA |
| Cotton (raw) | 211.6 | 171.7 | 131.8 | NA | NA |
| Other fibres | NA | 18.8 | 37.2 | NA | NA |
| Cashew nuts (raw) | 6 | 20.2 | 39.2 | NA | NA |
| Diamonds | NA | 0.7 | 25.2 | 528 | 2079 |
| Pulp and paper | 22.2 | 39.5 | 49.8 | NA | NA |
| Chemicals | NA | 157.7 | 155.5 | NA | NA |
| Precision instruments | 14 | 22.9 | 32.5 | NA | NA |
| Machinery | 192 | 547.3 | 437.5 | NA | NA |
| Transport equipments | 73.4 | 152 | 88.5 | NA | NA |
| Other imports | NA | 306.9 | 165.5 | 9452 | 19994 |

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| | | | | | |
|---|---|---|---|---|---|
| **Total imports** | **1365.4** | **2393.4** | **2178.9** | **15892** | **26427** |

In terms of exports, the share of Indian exports in global trade has declined steadily from around 2% in 1950 to less than 0.5% in 1990. Since world export grew rapidly between 1950 and 1973 and somewhat more slowly thereafter, India's exports grew in absolute terms in spite of a declining share. But the dramatic fall in share reflects the fact that other countries were able to take greater advantage of growing world trade. *Table3*

**Table 3**

India's share in world exports, 1950-1990 as a % of global trade

| Year | Rate |
|---|---|
| 1950 | 2.0 |
| 1955 | 1.5 |
| 1960 | 1.2 |
| 1965 | 1.0 |
| 1966 | 0.9 |

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| | |
|---|---|
| 1967 | 0.6 |
| 1970 | 0.5 |
| 1973 | 0.5 |
| 1975 | 0.6 |
| 1977 | 0.5 |
| 1978 | 0.5 |
| 1979 | 0.4 |
| 1980 | 0.4 |
| 1981 | 0.5 |
| 1982 | 0.5 |
| 1983 | 0.5 |
| 1984 | 0.5 |
| 1985 | 0.5 |
| 1986 | 0.5 |
| 1988 | 0.4 |
| 1989 | 0.5 |

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| | |
|---|---|
| 1990 | 0.5 |

A crude index of terms based on indexes of unit value of exports and imports shows no distinct trend but significant fluctuations. The volume of Indian trade grew at an average annual rate of 3.0% during 1965-1980 and 6.5% during 1980-1990. Indian export growth was faster than that of the world and that of low-income developing countries. *Table 4*

**Table 4**

Unit value and volume indexes of exports and imports and India's terms of trade from 1951-52 to 1991-92

| Year | Exports | | Imports | | Terms of Trade |
|---|---|---|---|---|---|
| | Volume index | Unit Value index in US$ | Volume index | Unit value index in US$ | |
| 1950-51 | 73 | 99 | 50 | 187 | 53 |
| 1951- | 58 | 145 | 63 | 123 | 118 |

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| 52 | | | | | |
|---|---|---|---|---|---|
| 1952-53 | 65 | 102 | 47 | 121 | 84 |
| 1953-54 | 65 | 93 | 44 | 112 | 83 |
| 1954-55 | 68 | 99 | 52 | 109 | 91 |
| 1955-56 | 75 | 91 | 55 | 106 | 86 |
| 1956-57 | 71 | 96 | 65 | 110 | 87 |
| 1957-58 | 77 | 96 | 74 | 120 | 80 |
| 1958-59 | 70 | 94 | 66 | 112 | 84 |
| 1959-60 | 75 | 94 | 73 | 104 | 90 |
| 1960-61 | 70 | 104 | 85 | 107 | 97 |
| 1961-62 | 74 | 104 | 80 | 110 | 95 |

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| | | | | | |
|---|---|---|---|---|---|
| 1965-66 | 87 | 107 | 102 | 117 | 91 |
| 1966-67 | 84 | 102 | 99 | 106 | 96 |
| 1967-68 | 86 | 102 | 110 | 96 | 106 |
| 1968-69 | 100 | 100 | 100 | 100 | 100 |
| 1969-70 | 100 | 104 | 84 | 100 | 104 |
| 1970-71 | 106 | 106 | 87 | 100 | 106 |
| 1971-72 | 107 | 109 | 105 | 94 | 116 |
| 1972-73 | 120 | 117 | 99 | 94 | 124 |
| 1973-74 | 125 | 141 | 114 | 133 | 106 |
| 1974-75 | 133 | 172 | 100 | 225 | 76 |
| 1975-76 | 147 | 171 | 99 | 243 | 70 |

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| | | | | | |
|---|---|---|---|---|---|
| 1976-77 | 174 | 176 | 97 | 233 | 76 |
| 1977-78 | 168 | 207 | 130 | 218 | 95 |
| 1978-79 | 180 | 214 | 140 | 238 | 90 |
| 1979-80 | 199 | 219 | 135 | 334 | 66 |
| 1980-81 | 194 | 241 | 199 | 322 | 75 |
| 1981-82 | 101 | 100 | 101 | 93.3 | 107.6 |
| 1982-83 | 97 | 98 | 94 | 92.3 | 106.2 |
| 1983-84 | 97 | 101.1 | 101 | 88.1 | 114.8 |
| 1984-85 | 103 | 98.5 | 95 | 87.1 | 113.1 |
| 1985-86 | 106 | 97.7 | 119 | 85.2 | 115 |
| 1986-87 | 118 | 97.1 | 124 | 80.3 | 121 |

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| | | | | | |
|---|---|---|---|---|---|
| 1987-88 | 135 | 106 | 116 | 93.6 | 114 |
| 1988-89 | 154 | 107.8 | 130 | 93.8 | 115 |
| 1990-91 | 178 | 110.3 | 135 | 99.2 | 111 |
| 1991-92 | 186 | 115.2 | 140 | 106 | 100 |

The composition of India's exports has, as expected, moderately away from primary products to manufactured goods, whose share rose from about 45% in 1950-51 to 79% in 1990-91. In recent years, however, primary exports have been virtually stagnant, and manufactured products have accounted for almost the entire growth in total products. Among manufactured products, just four items namely, leather, gems, garments, and textiles account for most of the growth in recent years. In contrast, the growth of engineering goods, which rose by 20% per year in value terms between 1950-51 and 1975-76 and between 1970-71 and 1978-79, declined between 1980-91 and 1985-86. From the low point of US$ 780 million in 1985-85, the value of engineering goods exports grew at an average annual rate of 20.5% during the

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period 1985-90. Chemical exports also showed a similar trend.

**Table 5**

India's merchandise exports, 1950-51 to 1970-71 (US$ million at current prices)

| Items | 1950-51 | 1960-61 | 1970-71 |
|---|---|---|---|
| **Agricultural products** | 328.8 | 420.7 | 519.3 |
| Tea | 168.9 | 259.6 | 197.7 |
| Oil cakes | 0.1 | 30 | 73.9 |
| Coffee | 1.8 | 15.2 | 35.5 |
| Sugar | 0.8 | 5.1 | 56.8 |
| Spices | 53.4 | 34.9 | 51.8 |
| Fish | 5.2 | 9.7 | 41.7 |
| Cashew | 18.0 | 39.7 | 69.4 |

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| | | | |
|---|---|---|---|
| Vegetable oils | 53 | 17.9 | 9.4 |
| Essential oils | 26.6 | 8.6 | 5.1 |
| Raw materials | 78.3 | 135.4 | 252.7 |
| Raw cotton | 10.4 | 18.2 | 18.6 |
| **Unmanufactured** | | | |
| Tobacco | 29.6 | 22.4 | 41.9 |
| Iron ore | 0.5 | 35.8 | 152.9 |
| Mica | 21.0 | 21.2 | 20.7 |
| Manganese | 16.8 | 29.5 | 18.6 |
| Silver | NA | NA | NA |
| **Manufactured items** | 568.8 | 571.7 | 976.3 |
| Jute manufactures | 239.0 | 283.8 | 253.9 |
| Cotton textiles mill made | 225.4 | 110.8 | 90 |
| Handloom | 22.8 | 10 | 10.4 |
| Coir | 22.8 | 18.2 | 17.3 |

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| | | | |
|---|---|---|---|
| manufactures | | | |
| Clothing | 0.8 | 1.8 | 40.3 |
| Cotton yarn and thread | 4.2 | 9.3 | 29.6 |
| Leather and leather manufactures | 54.5 | 56.6 | 108.8 |
| Gems | NA | 0.3 | 55.8 |
| Other handicrafts | NA | NA | 37.3 |
| Iron and steel | 3.3 | 20.3 | 121.6 |
| Engineering goods | 1.2 | 37.8 | 155.3 |
| Chemicals | 17.9 | 7.2 | 39.2 |
| Mineral fuels | NA | 15.6 | 16.8 |
| Other | 285.4 | 258.7 | 298.6 |
| **Total** | **1261.3** | **1386.5** | **2046.9** |

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**Table 6**

India's merchandise exports, 1980-81 and 1990-91 (US$ million at current prices)

| **Items** | **1980-81** | **1990-91** |
|---|---|---|
| **Primary exports** | 3400 | 3740 |
| Fish | 270 | 535 |
| Rice | 284 | 245 |
| Cashews | 178 | 249 |
| Coffee | 271 | 141 |
| Tea | 539 | 599 |
| Spices | 141 | 130 |
| Iron ore | 384 | 585 |
| Other primary | 1333 | 1257 |
| **Manufactured exports** | 5067 | 14383 |

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| | | |
|---|---|---|
| Chemicals | 298 | 1781 |
| Leather and leather goods | 478 | 1422 |
| Textiles | 1292 | 1705 |
| Garments | 717 | 2252 |
| Gems and jewellery | 783 | 2903 |
| Engineering goods | 1010 | 1978 |
| Petroleum products | 10 | 522 |
| Other manufactures | 479 | 1819 |
| **Total** | **8467** | **18123** |

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**Table 7**

Composition of India's export growth in the period 1980-81 to 1990-91

| **Item** | **Average annual value** (US$ million at current prices) | | | **Contribution to growth (%)** |
|---|---|---|---|---|
| | **1980-81 to 1985-86** | **1985-86 to 1990-91** | **Increase** | |
| Manufactured exports | 5296 | 10837 | 5542 | 97 |
| Consumption goods | 3408 | 6514 | 2106 | 55 |
| Leather | 502 | 1046 | 544 | 10 |
| Gems (gross) | 1097 | 2551 | 1454 | 26 |
| Garments | 757 | 1612 | 855 | 15 |
| Textiles | 1052 | 1305 | 253 | 4 |
| Investment goods | 860 | 1518 | 658 | 12 |
| Intermediate | 1028 | 2805 | 1777 | 31 |

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| goods | | | | |
|---|---|---|---|---|
| Chemicals | 382 | 1138 | 756 | 13 |
| Petroleum products | 238 | 421 | 183 | 3 |
| Other | 407 | 1247 | 839 | 15 |
| **Primary exports** | 3144 | 3287 | 143 | 3 |
| Fish | 340 | 442 | 102 | 2 |
| Rice | 210 | 227 | 17 | 0 |
| Cashews | 165 | 231 | 66 | 1 |
| Coffee | 185 | 195 | 9 | 0 |
| Tea | 497 | 493 | -4 | 0 |
| Spices | 145 | 181 | 37 | 1 |
| Iron ore | 408 | 490 | 83 | 1 |
| Other primary exports | 1195 | 1028 | -167 | -3 |
| **Total exports** | **8440** | **14124** | **5685** | **100** |

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The export of gems has grown rapidly since the early 1970s. This export is heavily dependent, however on imports of uncut small gems, the cost of which is determined in large part by South African monopoly De Beers. The exports of garments and textiles are governed by India's quotas under the multifiber arrangement. India lagged behind in utilisation of its quotas against its competitors. The recent growth of India's garment exports reflects better use of quotas and higher prices realised on an average. Since the removal of quota systems by January 2005, the garment exports have seen considerable growth and are expected to double their present level by the year 2009.

## 4.8 Changing pattern of exports

India's central banking authority, Reserve Bank of India in its Report on Currency and Finance, 2002-03 said that since the initiation of economic reforms, India's outward orientation has increased considerably. The destination pattern of Indian exports has remarkably changed whereby the importance of developing countries as an export market has considerably increased. There is, however, some concern that India has not been able to fully utilise its potential in international trade. In contrast to the dramatic changes in exports of East Asia, India's experience has seemingly fallen short of expectation. India's share in global trade did not rise as impressively

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and the commodity structure of India's exports remained almost unchanged until the mid-1990s. Moreover, unlike the East Asian countries where industry has been the major driver of exports growth, the contribution of industrial exports in India has been comparatively low. This could perhaps be attributed to small-scale industry reservations, high transaction costs and inflexible labour laws besides other structural bottlenecks. The linkages between trade and foreign investment in India indicate that FDI has been much less important in driving India's export growth, except in information technology. The labour cost in India, however, is one of the lowest among its competitor countries. Moreover, given the exports structure of India, the potential for higher exports of manufactures, especially to the developed countries, is high.

It is important to note that despite significant liberalisation of imports with reduction in tariffs, phasing out of quantitative restrictions and allowing bullion imports through the formal channel, the country's current account deficit has remained modest during the 1990s. Besides, the overall balance of payments has been in surplus for most of the years and consequently the country's foreign exchange reserves have increased significantly. This suggests that tariff reductions could be carried out faster than envisaged earlier, without posing any significant risk to the balance of payments.

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The overall trade balance at the end of fiscal 2002-03, according to foreign trade statistics released by the federal Commerce ministry, shows a widening trade gap of US$ (-) 7.68 bn against US $ (-) 6.95 bn in fiscal 2001-02. Exports during 2002-03 stood at US$ 51.70 bn signifying 18.05 percent growth over previous comparable figure of US$ 43.79 bn. Imports during 2002-03 stood at US$ 59.38 bn against US$50.74 bn in fiscal 2001-02 signifying 17.03 percent increase.

In the first 11 months (April, 2003-February, 2004) of the fiscal 2003-04, India's exports were up 14.75 percent where as imports witnessed a marked growth of as high as 26.33 percent leading to a deficit trade balance of over US$ 15.52 billion. In rupee terms the deficit stands at Rs 71993.86 crore. Oil imports during this 11-month period stood at US$ 18.77 bn signifying 17.80 percent increase over the comparable period's US$ 15.93 bn. Non-oil imports during this period are estimated at US$ 49.82 bn- up 29.88 percent higher than US$ 38.36 bn for the comparable period of fiscal 2002-03.

In its 2003 Country report on India, the Institute of International Finance, Inc, (IIF) said that a revival in agriculture made possible by abundant rainfall is fuelling an economic recovery and containing inflation. The high level of official foreign exchange reserves and favourable agricultural performance provide considerable support to the economy and guard against financial

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instability over the near-term. In its report 'Capital flow to emerging market economies' IIF said that though the current account surplus of the Asia/Pacific region is likely to show a decline in 2004, as the pace of import growth, particularly for services, outstrips that of exports, stronger activity in trading partner countries should allow double-digit export growth to continue in China, India, Korea, and Thailand.

To fine tune the 2002-07 EXIM Policy so as to consolidate & accelerate incremental growth rate of exports and make India a manufacturing hub for producing quality goods & services, India's Directorate General of Foreign Trade (DGFT) has announced on January 28, 2004 a series of measures. The Indian government expects that these EXIM facilitation initiatives coupled with the ballooning foreign exchange reserves, upgradation of India's international credit rating and the increasing confidence of the international markets in the Indian economy will not only enhance international competitiveness and acceptability of Indian exports but also lead to focused international investment in areas of India's core competence.

The export facilitation measures like allowing Capital Goods (CG) imports, based on a Chartered Engineer's certificate for establishing nexus with the export product under Export Promotion Capital Goods (EPCG) scheme without the need for an examination by an Expert Committee and

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permitting exports of alternate products and services made by Group Companies for the purpose of discharge of export obligation under EPCG scheme are aimed at creating additional export markets, enhance operational efficiency of the exporting community, remove procedural impediments and help expand the manufacturing base in the country.

Re-determination of Export Obligation of the past EPCG licences on the principle of 8 times the duty saved instead of 5 times the CIF value will go a long way in correcting the distortion of the past EPCG licence holders vis-à-vis the licensees under the present liberalised Policy. Facility of clubbing of EPCG licences for discharge of export obligation and import of spare refractories, catalyst and consumables under EPCG has also been allowed.

To offset the high power costs faced by the manufacturing industry, duty free fuel will be allowed to be imported with actual user condition under Duty Free Replenishment Certificate (DFRC) scheme. The extension of new benefits relating to Advance Licence for intermediate supplies under Duty Free Replenishment Certificate (DFRC) scheme, facility of grant of export obligation period extension and revalidation facility for Advance Licence for annual requirements being availed by Status Holders, reduction in payment of composition fee for extension of Export Obligation & linking it to

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duty saved amount and re-introduction of Advance Licence for free of cost material will go a long way in meeting the demands of the industry.

Besides, some of the procedural bottlenecks relating to 'deemed exports' benefits have been removed through procedural simplifications. Deemed export benefits for items attracting Zero percent basic Customs duty shall be granted. Deemed export facility shall also be extended to Fertiliser & Refinery projects spilled over from 8th and 9th Plan periods. To reduce transaction costs, fixation of Drawback brand rates for deemed exports has been decentralised and delegated to DGFT regional offices.

Equity base of the Export Credit & Guarantee Corporation (ECGC) is being raised from Rs 500 crores to Rs 800 crores to help the Indian exporters in better risk management.

In addition, to underwrite high value projects being implemented by Indian companies abroad, a National Export Insurance Account is being created for ECGC. Details are being worked out in consultation with Ministry of Finance.

A Gold Card Scheme for credit worthy exporters with good track record is also being finalised by RBI to enable them to obtain export credit without difficulty. This would ensure easy availability of export credit to Indian exporters at best terms and enhance the competitiveness of Indian goods and services.

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To promote export related infrastructure, rupee payments received for Port handling services shall be counted for discharge of export obligation under EPCG scheme. Import of Prototypes shall be also allowed to Actual Users for R & D purposes without any limit (presently restricted to 10 Nos. per annum). Annual ceiling on export of Gifts has been raised from Rs 1-5 lakh.

In a significant move, the government has also liberalised the import of Gold and Silver. This will provide freedom to procure inputs by jewellery exporters and add to the cost competitiveness of the Indian jewellery exports. Non-tariff barriers applicable on imports for export production have also been rationalised for food & textile items.

Increased focus has also been made on procedural simplification by introducing E-Commerce initiatives like Digital Signature, Electronic Fund Transfer & Message exchange with community partners like Customs, Banks etc. All these will not only reduce transaction costs for the exporting community but also impart greater transparency and reduce discretion while availing various benefits under the EXIM Policy.

Changes in EXIM to make it in line with overall reforms *See appendix*

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# CHAPTER 5

## Statistical Profile

The investment pattern and magnitude of foreign in investment in India has gone through wide changes in the past three decades. This changing pattern reflects the growing investor confidence in the country.

The chief indicator of strengthening of India's foreign exchange situation is the capital account of balance of payments. This account reveals that foreign investment inflows have risen from $366 million during the 1970s to $39317 during 1980s. This figure jumped to $76985 million in 1990s. Foreign investments, which are non-debts creating inflows, were 5.95% of the total capital inflows in seventies. During eighties also they were just 5.7% of the total inflows, though there was increase in the absolute amount. However, the post liberalisation period shows remarkable improvement in the share of foreign investment in total inflows. They contributed 42.7% of the total capital inflows. Foreign investment inflows were just 1.5% of the total capital flows in 1991. They rose to 117.5% of capital inflows during 1995-95 (other capital being –75.2%). They declined to 51.2% in 1996-97. An improvement to 54.8% was made in 1997-98 but in 1998-99 with FDI declining considerably and portfolio investment becoming negative, non-debt creating inflows stood at 28.6% of the total flows. The investor's confidence seems to have improved in 1999-2001

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and 2000-2001. After the East Asian crisis, portfolio investment showed remarkable improvement. It was 29% of the total flows in 1999-2000. There was again a fall in the share of FDI in 1999-2000. The sluggish growth of the economy seems to be a factor behind this fall. In 2000-01 the net capital inflows amounted to $ 9.02 billion as compared with $10.44 billion in 1999-2000. The reduction was mainly due to the bunching of repayment of commercial borrowing and significant net outflows under banking capital.

The relative importance of debt creating inflows comprising of external assistance, external commercial borrowings, short-term credit, rupee debt servicing, and non-resident Indian deposits has considerably declined over the past three decades. The share of debt creating inflows has declined from 139.85% during seventies to 99.65% during first half of eighties and 89.4% during the latter half of eighties. They were 51.4% of the total capital inflows during 1990s. There was a steady decline in their share from 83.3% to 21.2% during 1990-91 and 1993-94. This remarkable change within the debt creating inflows during the last three decades has bee, the declining share of external assistance from 107.5% during 1970s to 48.3% during the first half and 31.5% during the second half of 1980s. They further declined to 27.3% during 1990s. Short-term credits have been –3.5% of the total capital inflows during the 1990s and rupee debt servicing has been 15.7% of the total capital inflows during the same period. The share of NRI deposits increased from 13.9% during 1970s to 28% during 1980s. During 1990s the

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contribution of NRI deposits in the total capital inflows has declined to 20%. *Table 1*

**Composition of Capital Account inflows in India**

| Type of inflow | Period | | |
|---|---|---|---|
| | **1970s** | **1980s** | **1990s** |
| Debt creating inflows | 139.8% | 89.4% | 53.5% |
| Non-debt creating inflows | 5.9% | 5.7% | 42.7% |
| Other inflows | -45.8% | 4.9% | 4.7% |

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**Merchandised Trade**
**(In US$ million)**

| Year | Export | Import | Balance |
|---|---|---|---|
| 1990-91 | 18145 | 24073 | -5927 |
| 1991-92 | 17865 (-1.54) | 19411 (-19.36) | -1545 |
| 1992-93 | 18537 (3.76) | 21882 (12.72) | -3344 |
| 1993-94 | 22238 (19.96) | 23306 (6.50) | -1068 |
| 1994-95 | 26331 (18.40) | 28654 (22.94) | -2324 |
| 1995-96 | 31795 (20.75) | 36675 (27.99) | -4880 |
| 1996-97 | 33470 (5.26) | 39132 (6.70) | -5663 |
| 1997-98 | 35006 (4.58) | 41484 (6.01) | -6478 |

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| | | | |
|---|---|---|---|
| 1998-99 | 33219 (5.10) | 42389 (2.18) | -9170 |
| 1999-2000 | 36822 (10.84) | 49738 (17.33) | -12916 |
| 2000-01 | 44560 (21.0) | 50536 (1.7) | -5976 |
| 2001-02 | 43827 (-1.65) | 51413 (1.74) | -7587 |
| 2002-03 | 52719 (20.29) | 61412 (19.45) | -8693 |
| 2003-04 | 63843 (21.10) | 78150 (27.25) | -14307 |
| 2004-05 (P) (April '04-February '05) | 68798 | 93628 | -23830 |

P : Provisional
Crore : 10 million
Source: Reserve Bank of India

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## India's Exports and Imports in 2004-05
## (In US$ million)

| APRIL 2004 - FEBRUARY 2005 | |
|---|---|
| **EXPORTS** | |
| 2003-04 | 54946.43 |
| 2004-05 | 69798.26 |
| % growth | 27.03 |
| **IMPORTS** | |
| 2003-04 | 68675.59 |
| 2004-05 | 93628.82 |
| % growth | 36.33 |
| **TRADE BALANCE** | |
| 2003-04 | -13729.16 |
| 2004-05 | -23830.56 |
| | |

Source : Federal Ministry of Commerce, Govt. of India

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**Regions wise distribution of India's foreign trade (In US$ million)**

| Regional and Principal Countries | 1999-2000 | 2000-2001 | % change over previous year |
|---|---|---|---|
| **I EUROPE** | 13718.66 | 13446.85 | -1.98 |
| **ECM Countries** | 10531.43 | 9791.10 | -7.03 |
| Belgium | 3681.27 | 2860.54 | -22.29 |
| Denmark | 135.42 | 110.74 | -18.22 |
| France | 718.23 | 628.56 | -12.49 |
| FRG | 1841.55 | 1735.47 | -5.76 |
| Greece | 26.90 | 21.97 | -18.30 |
| Ireland | 55.68 | 71.50 | 28.40 |
| Italy | 734.62 | 713.88 | -2.82 |

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| | | | |
|---|---|---|---|
| Luxembourg | 2.54 | 5.22 | 105.35 |
| Netherlands | 470.90 | 382.71 | -18.73 |
| Portugal | 9.74 | 11.81 | 21.31 |
| Spain | 139.88 | 140.83 | 0.67 |
| United Kingdom | 2714.69 | 3107.85 | 14.48 |
| **EFTA Countries** | 3088.44 | 3654.37 | 18.32 |
| Finland | 138.76 | 207.21 | 49.32 |
| Sweden | 238.90 | 236.85 | -0.86 |
| Switzerland | 2599.98 | 3095.19 | 19.05 |
| Rest of Europe | 98.79 | 1.38 | 98.60 |
| **II. ASIA & OCEANIA** | 23521.71 | 13649.61 | -41.97 |

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| | | | |
|---|---|---|---|
| **ESCAP** | 13847.98 | 10746.37 | -22.40 |
| Bangladesh | 78.15 | 78.26 | 0.14 |
| Nepal | 188.62 | 220.35 | 16.82 |
| Sri Lanka | 44.23 | 46.34 | 4.78 |
| Australia | 1081.56 | 1045.18 | -3.36 |
| China | 1286.70 | 1467.97 | 14.09 |
| Hongkong | 817.90 | 821.43 | 0.43 |
| Indonesia | 958.79 | 902.54 | -5.87 |
| Japan | 2535.80 | 1820.80 | -28.20 |
| Korea, Republic of | 1273.34 | 778.34 | -38.87 |
| Malaysia | 2024.03 | 1132.96 | -44.02 |
| Singapore | 1534.41 | 1434.13 | -654 |

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| | | | |
|---|---|---|---|
| Thailand | 327.77 | 314.37 | -4.0 |
| Others | 9673.73 | 2903.24 | -69.99 |
| Saudi Arabia | 3017.48 | 623.45 | -79.34 |
| United Arab Emirates | 2334.25 | 644.14 | -72.32 |
| Israel | 581.94 | 432.38 | -25.70 |
| **III. AFRICA** | 6611.38 | 2043.12 | -69.10 |
| Egypt | 443.87 | 38.68 | -91.29 |
| Nigeria | 2928.39 | 61.50 | -97.90 |
| South Africa | 2012.15 | 1003.05 | -50.15 |
| **IV. AMERICA** | 4878.36 | 3912.21 | -19.80 |
| **North** | 3944.46 | 3190.62 | -19.11 |

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| | | | |
|---|---|---|---|
| Canada | 380.51 | 386.14 | 1.48 |
| U.S.A | 3563.96 | 2804.48 | -21.31 |
| **South** | 829.57 | 642.76 | -22.52 |
| Brazil | 330.89 | 143.96 | -56.49 |
| **OTHER CENTRAL & CARIBBEAN** | 104.33 | 78.83 | -24.44 |
| **V. EAST EUROPE** | 986.70 | 843.78 | -14.49 |
| C.I.S | 800.84 | 676.02 | -15.59 |
| Russia | 623.18 | 513.19 | -17.65 |
| Rest of CIS Countries | 177.65 | 162.83 | -8.34 |
| Other East European Countries | 185.87 | 167.76 | -9.74 |

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| | | | |
|---|---|---|---|
| Fomer RPA Countries | 71.23 | 64.46 | -9.51 |
| Rest of the Countries | 102.60 | 97.49 | -4.99 |
| **GRAND TOTAL** | **49738.08** | **49639.15** | **-0.20** |
| **Source:** Federal Ministry of Commerce, Government of India | | | |

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## Composition of Exports
## (In US$ million)

| Commodity Group | 2000-01 (P) | 1999-2000 | 1998-99 |
|---|---|---|---|
| **1.Primary Products** | **7161** | **6524** | **6928** |
| **Agr. & Allied Products** | **6003** | **5608** | **6034** |
| Tea | 432 | 412 | 538 |
| Coffee | 260 | 331 | 411 |
| Rice | 641 | 721 | 1493 |
| Oil Meal | 448 | 378 | 462 |
| Marine Products | 1394 | 1183 | 1038 |
| **Ores and minerals** | **1158** | **916** | **893** |
| **2. Manufactured** | **34511** | **29714** | **25791** |

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| **Goods** | | | |
|---|---|---|---|
| **Leather & Manufrs** | **1951** | **1590** | **1661** |
| **Chemicals& related products** | **5890** | **4707** | **4009** |
| Basic Chemicals, Pharmaceuticals & Cosmetics | 3664 | 3088 | 2655 |
| Plastic&Linoleums | 909 | 604 | 472 |
| Rubber, Glass, Paints & Enamels etc. | 945 | 694 | 631 |
| Residual chemicals and Allied Products | 371 | 321 | 252 |
| **Engineering Goods** | **6862** | **5152** | **4464** |
| **Textiles** | **10758** | **9126** | **8303** |
| Cotton Yarn, | 3500 | 3090 | 2772 |

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| Fabrics,Made-ups etc. | | | |
|---|---|---|---|
| Ready-made garments | 5575 | 4765 | 4365 |
| Manmade Yarn, fabrics, Made-ups etc | 1058 | 811 | 700 |
| **Gems& Jewellery** | **7390** | **7502** | **5929** |
| **Handicrafts** | **668** | **669** | **633** |
| **Carpets** | **582** | **645** | **544** |
| Handmade | 447 | 499 | 409 |
| Millmade | 110 | 113 | 102 |
| Silk | 24 | 34 | 32 |
| **3.Petroleum, Crude & Products** | **1819** | **30** | **89** |

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| **4.Others** | **837** | **554** | **410** |
|---|---|---|---|
| **Total Exports (1-4)** | **44328** | **36822** | **33219** |

P: Provisional
**Source:** Reserve Bank of India, DGCI&S

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**Composition of Imports (In US$ million)**

| Commodity Group | 2000-01 (P) | 1999-2000 | 1998-99 |
|---|---|---|---|
| **Bulk Imports** | **20758** | **19646** | **13230** |
| **Petroleum , Petroleum Products** | **15650** | **12611** | **6399** |
| **Bulk Consumption Good** | **1432** | **2417** | **2524** |
| Cereals, cereal items | 19 | 222 | 288 |
| Edible Oil | 1299 | 1857 | 1804 |
| Pulses | 108 | 82 | 168 |
| Sugar | 7 | 256 | 264 |
| **Other Bulk items** | **3675** | **4618** | **4307** |

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| | | | |
|---|---|---|---|
| Fertilisers | 746 | 1399 | 1076 |
| Non-ferrous Metals | 526 | 547 | 597 |
| Paper,Paperboard &Manufactures incl. Newsprint | 450 | 447 | 465 |
| Crude Rubber incl. Synthetic & reclaimed | 151 | 143 | 145 |
| Pulp & Waste Paper | 279 | 255 | 236 |
| Metalliferrous Ores & Metal Scrap | 750 | 874 | 724 |
| Iron and Steel | 773 | 952 | 1064 |
| **II. Non-Bulk Imports** | **28881** | **30092** | **29159** |
| **Capital Goods** | **8785** | **8965** | **10064** |

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| | | | |
|---|---|---|---|
| Manufactures of Metals | 386 | 405 | 380 |
| Machine Tools | 218 | 261 | 347 |
| Machinery except Electrical & Electronics | 2754 | 2745 | 3045 |
| Electrical Machinery except electronics | 472 | 438 | 421 |
| Electronic Goods incl. Computer Software | 3676 | 2994 | 2386 |
| Transport Equipment | 643 | 1137 | 798 |
| Project Goods | 635 | 986 | 2688 |
| **Mainly Export related Items** | 8054 | 9117 | 7131 |
| Pearls, Precious & Semi-precious stone | 4808 | 5436 | 3760 |

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| | | | |
|---|---|---|---|
| Chemicals-organic and inorganic | 2438 | 2866 | 2684 |
| Textile Yarn, Fabrics | 596 | 538 | 457 |
| Cashew Nuts, Raw | 211 | 277 | 230 |
| **Others** | **12042** | **12009** | **11963** |
| Gold & Silver | 4427 | 4706 | 5072 |
| Artificial Resins & Plastic Materials | 554 | 719 | 676 |
| Professional, Scientific & Optical Goods | 854 | 845 | 820 |
| Coal, Coke,Briquittes | 1103 | 1008 | 980 |
| Medicinal & Pharmaceuticals item | 372 | 373 | 384 |
| Chemical | 329 | 361 | 390 |

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| materials | | | |
|---|---|---|---|
| Non-metallic Mineral Manufactures | 173 | 164 | 160 |
| **Total Imports(I-II)** | **49639** | **49738** | **42389** |

P : Provisional
**Source:** Reserve Bank of India, DGCI&S

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## Chronology of India's removal of quantitative restrictions

| | |
|---|---|
| Total number of tariff lines as on April1, 1996 | 10202 |
| Tariff lines free as on April 1, 1996 | 6161 |
| Tariff lines freed for import during 1996-97 | 488 |
| 1997-98 | 391 |
| Tariff lines freed preferentially for imports from SAARC countries with effect from August 1, 1998 | 1429 |
| 1998-99 | 894 |

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| | |
|---|---|
| 1999-2000 | 714 |
| 2000-01 | 715 |
| Source: India's Federal Commerce minister's Exim Policy ( 2001-02) speech delivered on March 31, 2000. | |

**Forex Reserve**
**(In US$ million)**

| Year | Gold | Foreign Currency Assets | Total |
|---|---|---|---|
| 1990-91 | 3,496 | 2,236 | 5,834 |
| 1991-92 | 3,499 (0.08) | 5,631 (151.83) | 9220 (58.03) |
| 1992-93 | 3,380 (-3.40) | 6,434 (14.26) | 9832 (106.64) |
| 1993-94 | 4,078 (20.65) | 15,068 (134.19) | 19,254 (95.82) |

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| | | | |
|---|---|---|---|
| 1994-95 | 4,370 (7.16) | 20,809 (38.10) | 25,186 (30.80) |
| 1995-96 | 4,561 (4.37) | 17,044 (-18.09) | 21,687 (-13.89) |
| 1996-97 | 4,054 (-11.11) | 22,367 (31.23) | 26,423 (21.83) |
| 1997-98 | 3,391 (-16.35) | 25,975 (16.13) | 29,367 (11.14) |
| 1998-99 | 2,960 (-12.71) | 29,522 (13.65) | 32,490 (10.63) |
| 1999-2000 | 2,974 (0.47) | 35,058 (18.75) | 38,036 (17.06) |
| 2000-01 P | 2,725 (-8.37) | 39,554 (12.82) | 42,281 (11.16) |

Source: Reserve Bank of India

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**India's Merchandise Trade (2004-05)**
**(April 2004 - February 2005)**

| In US$ million | | In Rs crore | |
|---|---|---|---|
| **EXPORTS** | | **EXPORTS** | |
| 2003-04 | 54946.43 | 2003-04 | 252554.14 |
| 2004-05 | 69798.26 | 2004-05 | 314185.17 |
| Growth | 27.03 | Growth | 24.40 |
| **IMPORTS** | | **IMPORTS** | |
| 2003-04 | 68675.59 | 2003-04 | 315829.09 |
| 2004-05 | 93628.82 | 2004-05 | 421376.42 |
| Growth | 36.33 | Growth | 33.42 |
| **TRADE BALANCE** | | **TRADE BALANCE** | |
| 2003-04 | -13729.16 | 2003-04 | -63274.95 |
| 2004-05 | - | 2004- | -107191.25 |

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| 23830.56 05 |
|---|
| **SOURCE**: Federal ministry of Commerce, Government of India |

**India's Balance of Payments (2003-04)**
**India's foreign exchange reserves stand at US$ 142.13 billion as on Mar 18, 2005**

| Item | 2001-02 | 2002-03 | 2003-04 |
|---|---|---|---|
| **A. CURRENT ACCOUNT** | | | |
| **I Merchandise** | **-12703** | **-12910** | **-12703** |
| **II Invisibles (a+b+c)** | **13485** | **17047** | **25425** |
| a) Services | 4577 | 6765 | 10684 |
| b) Transfers | 12509 | 15217 | 19444 |
| c) Income | -3601 | -4935 | -4703 |
| **TOTAL CURRENT ACCOUNT (I+II)** | **782** | **4137** | **8719** |
| **B. CAPITAL ACCOUNT** | | | |
| **1. Foreign Investment (a+b)** | **6692** | **4555** | **14492** |
| a) Foreign Direct Investment | 4741 | 3611 | 3137 |
| i) In India | 6131 | 4660 | 4675 |

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| | | | |
|---|---|---|---|
| ii) Abroad | -1390 | -1049 | -1538 |
| b) Portfolio Investment | 1951 | 944 | 11355 |
| i) In India | 2020 | 979 | 11377 |
| ii) Abroad | -69 | -35 | -22 |
| **2. External Assistance** | **1117** | **-2460** | **-2661** |
| **3. Commercial Borrowings** | **-1567** | **-2344** | **-1576** |
| **4. Short Term Credit, Net** | **-891** | **979** | **1560** |
| **5. Banking Capital** | **5592** | **8412** | **6197** |
| **6. Rupee Debt Service** | **-519** | **-474** | **-376** |
| **5. Other Capital, Net** | **158** | **3455** | **4763** |
| **Total Capital Account (1-5)** | **10573** | **12113** | **22122** |
| **C. ERRORS & OMISSIONS** | **402** | **730** | **580** |
| **D. OVERALL BALANCE [A(5)+B(8)+C]** | **11757** | **16980** | **31421** |
| **E. MONETARY MOVEMENT (i+ii)** | **-11757** | **-16980** | **-31421** |
| i) I.M.F | 0 | 0 | 0 |
| ii) Foreign Exchange Reserve (-/+) | -11757 | -16980 | -31421 |

* Provisional
**Source:** Reserve Bank of India

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## Weighted index of Industrial Production

| Sector | Mining | | Manufacturing | | Electricity | | General | |
|---|---|---|---|---|---|---|---|---|
| (Weights) | (104.73) | | (793.58) | | (101.69) | | (1000.00) | |
| Month | 1997-98 | 1998-99 | 1997-98 | 1998-99 | 1997-98 | 1998-99 | 1997-98 | 1998-99 |
| Apr | 116.6 | 113.0 | 132.3 | 140.2 | 123.9 | 137.5 | 129.8 | 137.1 |
| May* | 119.2 | 119.0 | 134.1 | 140.0 | 128.8 | 140.5 | 132.0 | 137.9 |
| Jun | 114.6 | | 133.4 | | 123.0 | | 130.4 | |
| Jul | 115.6 | | 134.2 | | 128.7 | | 131.7 | |
| Aug | 114.2 | | 134.0 | | 128.8 | | 131.4 | |
| Sep | 113.5 | | 136.4 | | 127.5 | | 133.1 | |
| Oct | 120.7 | | 136.2 | | 129.4 | | 133.9 | |
| Nov | 122.8 | | 138.3 | | 124.5 | | 135.3 | |
| Dec | 128.6 | | 148.9 | | 131.7 | | 145.0 | |
| Jan | 133.5 | | 146.2 | | 142.1 | | 144.5 | |
| Feb | 126.6 | | 149.2 | | 131.3 | | 145.0 | |
| Mar | 141.0 | | 154.6 | | 143.6 | | 152.1 | |
| Average Apr-May | 117.9 | 116.0 | 133.2 | 140.1 | 126.4 | 139.0 | 130.9 | 137.5 |
| | | | | | | | | |
| Growth over the corresponding period of previous year | | | | | | | | |
| May | 3.7 | -0.2 | 2.8 | 4.4 | 4.0 | 9.1 | 3.0 | 4.5 |
| Apr-May | 4.1 | -1.6 | 2.4 | 5.2 | 3.8 | 10 | 2.7 | 5.0 |

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| India's Balance of Payments: April-December 2004 (in US$ million) | | |
|---|---|---|
| | **April-December 2004** | **April-December 2003** |
| **Exports** | 57485 | 44394 |
| **Imports** | 85841 | 58378 |
| **Trade Balance** | -28356 | -13984 |
| **Invisible, Net** | 21005 | 18790 |
| **Current Account** | -7351 | 4806 |
| **Balance** | | |
| **Capital Account** | 20835 | 16544 |
| **Change in Reserves** | -13484 | -21350 |
| (-) Indicates increase | | |
| Source: Reserve Bank of India | | |

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## Domestic Savings in India

| | At current prices (Rs. Crore) | | Rates | |
|---|---|---|---|---|
| | 1995-96 | 1996-97 | 1995-96 | 1996-97 |
| **Gross** | 283003 | 333816 | 25.3 | 26.1 |
| **Net** | 171417 | 206634 | 17 | 18 |

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# INDEX OF INDUSTRIAL PRODUCTION - MONTHWISE (2-DIGIT LEVEL)

**(BASE : 1993-94 = 100)**

## September 97 to January 98

| Industry Code | Description | Weight | Sep'97 | Oct'97 | Nov'97 | Dec'97 | Jan'98 |
|---|---|---|---|---|---|---|---|
| 20-21 | Food Products | 90.83 | 103.6 | 99.0 | 118.9 | 164.5 | 175.1 |
| 22 | Beverages, Tobacco and related Products | 23.82 | 152.6 | 162.0 | 159.0 | 162.0 | 160.9 |
| 23 | Cotton Textiles | 55.18 | 129.5 | 124.7 | 124.7 | 133.6 | 125.3 |
| 24 | Wool, Silk and man-made fibre textiles | 22.58 | 183.1 | 170.8 | 169.6 | 168.1 | 173.3 |
| 25 | Manufacture of Jute and other vegetable fibre Textiles (except cotton) | 5.90 | 116.2 | 115.0 | 120.7 | 120.5 | 115.5 |

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| | | | | | | | |
|---|---|---|---|---|---|---|---|
| 26 | Textile Products (including Wearing Apparel) | 25.37 | 168.9 | 157.4 | 165.2 | 160.6 | 170.7 |
| 27 | Wood and Wood Products; Furniture and Fixtures | 27.01 | 123.2 | 123.0 | 123.1 | 107.7 | 127.7 |
| 28 | Paper & Paper Products and Printing, publishing & Allied Industries | 26.52 | 141.3 | 153.0 | 147.8 | 155.9 | 150.4 |
| 29 | Leather and Leather & Fur Products | 11.39 | 101.1 | 107.1 | 115.9 | 110.7 | 101.2 |
| 30 | Basic Chemicals & Chemical Products(execpt products of Petroleum & Coal) | 140.02 | 145.2 | 142.7 | 140.8 | 145.1 | 145.0 |
| 31 | Rubbler, Plastic, Petroleum and Coal Products | 57.28 | 115.4 | 120.4 | 126.6 | 131.1 | 126.6 |
| 32 | Non-Metallic Mineral Products | 43.97 | 150.0 | 169.6 | 153.7 | 193.0 | 163.8 |
| 33 | Basic Metal and Alloy Industries | 74.53 | 139.8 | 145.9 | 141.5 | 148.8 | 150.8 |
| 34 | Metal Products and Parts(except Machinery and | 28.10 | 113.6 | 118.7 | 118.5 | 126.5 | 132.4 |

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| | | | | | | | |
|---|---|---|---|---|---|---|---|
| | Equipment ) | | | | | | |
| 35-36 | Machinery and Equipment other than Transport equipment | 95.65 | 150.8 | 148.0 | 153.6 | 160.5 | 137.3 |
| 37 | Transport Equipment and Parts | 39.84 | 151.0 | 138.8 | 144.8 | 146.3 | 150.0 |
| 38 | Other Manufacturing Industries | 25.59 | 121.5 | 116.8 | 112.8 | 116.9 | 117.0 |
| 1 | Mining & Quarrying | 104.73 | 113.5 | 120.7 | 122.8 | 128.6 | 133.5 |
| 2-3 | Manufacturing | 793.58 | 136.4 | 136.2 | 138.3 | 148.9 | 146.2 |
| 4 | Electricity | 101.69 | 127.5 | 129.4 | 124.5 | 131.7 | 142.1 |
| | General | 1000.00 | 133.1 | 133.9 | 135.3 | 145.0 | 144.5 |

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## February 98 to May 98

| Industry Code | Description | Weight | Feb'98 | Mar'98 | Apr'98 | May'98 |
|---|---|---|---|---|---|---|
| 20-21 | Food Products | 90.83 | 176.5 | 182.4 | 147.6 | 115.4 |
| 22 | Beverages, Tobacco and related Products | 23.82 | 158.9 | 177.6 | 169.5 | 173.0 |
| 23 | Cotton Textiles | 55.18 | 119.9 | 129.7 | 119.1 | 121.0 |
| 24 | Wool, Silk and man-made fibre textiles | 22.58 | 161.5 | 165.7 | 164.0 | 166.7 |
| 25 | Manufacture of Jute and other vegetable fibre Textiles (except cotton) | 5.90 | 109.3 | 122.9 | 118.1 | 98.3 |
| 26 | Textile Products (including Wearing Apparel) | 25.37 | 153.2 | 168.3 | 155.3 | 161.6 |

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| | | | | | | |
|---|---|---|---|---|---|---|
| 27 | Wood and Wood Products; Furniture and Fixtures | 27.01 | 135.4 | 121.0 | 135.0 | 136.7 |
| 28 | Paper & Paper Products and Printing, publishing & Allied Industries | 26.52 | 154.8 | 152.8 | 154.0 | 157.1 |
| 29 | Leather and Leather & Fur Products | 11.39 | 115.6 | 119.0 | 112.9 | 115.2 |
| 30 | Basic Chemicals & Chemical Products(execpt products of Petroleum & Coal) | 140.02 | 139.0 | 146.5 | 140.4 | 149.1 |
| 31 | Rubbler, Plastic, Petroleum and Coal Products | 57.28 | 129.1 | 129.1 | 124.3 | 131.2 |
| 32 | Non-Metallic Mineral Products | 43.97 | 198.9 | 203.4 | 158.5 | 164.4 |

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| | | | | | | |
|---|---|---|---|---|---|---|
| 33 | Basic Metal and Alloy Industries | 74.53 | 144.1 | 154.8 | 131.1 | 136.3 |
| 34 | Metal Products and Parts(except Machinery and Equipment ) | 28.10 | 138.4 | 133.0 | 140.5 | 133.1 |
| 35-36 | Machinery and Equipment other than Transport equipment | 95.65 | 156.1 | 159.2 | 129.9 | 131.5 |
| 37 | Transport Equipment and Parts | 39.84 | 158.8 | 166.6 | 166.5 | 169.3 |
| 38 | Other Manufacturing Industries | 25.59 | 125.1 | 131.5 | 130.8 | 132.8 |
| 1 | Mining & Quarrying | 104.73 | 126.6 | 141.0 | 113.0 | 119.0 |
| 2-3 | Manufacturing | 793.58 | 149.2 | 154.6 | 140.2 | 140.0 |

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| 4 | Electricity | 101.69 | 131.3 | 143.6 | 137.5 | 140.5 |
|---|---|---|---|---|---|---|
| | General | 1000.0 | 145.0 | 152.1 | 137.1 | 137.9 |
| | | | | | | |

## Sector-wise absorption of labour

| | |
|---|---|
| Agriculture | 62 per cent |
| Manufacturing & construction | 16 per cent |
| Services | 10 per cent |
| Sundry / miscellaneous jobs | 12 per cent |

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## Trends in Labour Force Participation Rates (Per Thousand of Population)

| Period | Male | | Female | |
|---|---|---|---|---|
| | Rural | Urban | Rural | Urban |
| 1977-78 | 879 | 746 | 515 | 257 |
| 1987-88 | 824 | 710 | 478 | 211 |
| 1993-94 | 804 | 684 | 455 | 204 |
| 1977-78 | 990 | 990 | 619 | 324 |
| 1987-88 | 988 | 987 | 603 | 301 |
| 1993-94 | 990 | 986 | 600 | 300 |
| 1977-78 | 963 | 940 | 538 | 291 |
| 1987-88 | 964 | 933 | 538 | 275 |
| 1993-94 | 968 | 937 | 543 | 283 |
| 1977-78 | 667 | 517 | 221 | 130 |
| 1987-88 | 670 | 482 | 220 | 123 |
| 1993-94 | 699 | 443 | 241 | 114 |
| 1977-78 | 904 | 831 | 517 | 269 |
| 1987-88 | 879 | 810 | 496 | 239 |
| 1993-94 | 877 | 811 | 491 | 238 |

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## Projections of Work opportunities 1997-2002

| Sector | GDP Growth (% p.a.) | Work Opportunities (Million) | |
|---|---|---|---|
| | 1997-02 | 1997 | 2002 |
| Agriculture | 3.9 | 238.32 | 262.48 |
| Mining & Quarrying | 7.2 | 2.87 | 3.54 |
| Manufacturing | 8.2 | 43.56 | 48.22 |
| Electricity | 9.3 | 1.54 | 1.93 |
| Construction | 4.9 | 14.74 | 17.03 |
| Wholesale & Retail Trade | 6.7 | 34.78 | 41.67 |
| Transport, Storage & Communication | 7.3 | 11.96 | 14.57 |
| Financing, Real Estate, Insurance and Business Services | 8.5 | 4.55 | 5.68 |
| Community, Social and Personal Service | 7.1 | 38.98 | 46.41 |
| All Sectors | 6.5 | 391.30 | 441.52 |

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## Population, Labour Force and Employment (Million)

| Criteria | 1978 | 1983 | 1994 | 8th Plan | 9th Plan | 10th Plan |
|---|---|---|---|---|---|---|
| | | | | | | |
| Population (c) | 637.6 | 718.2 (2.19) | 895.0 (2.12) | 951.2 (1.89) | 1028.9 (1.58) | 1112.9 (1.58) |
| Labour Force | 255.8 | 286.6 (2.09) | 368.5 (2.42) | 374.2 | 423.4 | 478.8 |
| Employment | 249.1 | 281.2 (2.23) | 361.5 (2.42) | 367.2 | 416.4 | 474.7 (d) |
| Unemployment | 6.7 | 5.4 | 7.0 | 7.0 | 7.0 | 4.1 (e) |
| Rate (%) | 2.63 | 1.89 | 1.89 | 1.87 | 1.66 | 0.86 (e) |

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Several measures to boost FDI have been announced in 1998-99. Projects for electricity generation, transmission and distribution as also roads and highways, ports and harbours, and vehicular tunnels and bridges have been permitted foreign equity participation up to 100 per cent under the automatic route, provided foreign equity does not exceed Rs. 1500 crore. FDI permissible under Non-Banking Financial Services now includes "Credit Card Business" and "Money Changing Business". Regarding equity participation in private sector banks, multilateral financial institutions have been allowed to contribute equity to the extent of the shortfall in NRI holdings within the overall permissible limit of 40 per cent. The Government has also decided to permit FDI up to 49 per cent of the total equity, subject to license, in companies providing Global Mobile Personal Communication by Satellite (GMPCS) services. Also, minimum capitalisation norms earlier required for pure financial consultancy services have been relaxed.

India's balance of payment (BoP) in fiscal year 2003-04 witnessed an impressive positive growth of 85.04 percent year-on-year basis. In terms of US$ the balance of payments in fiscal 2003-04 stood at US$ 31.42 billion compared with US$ 16.98 bn in the previous fiscal. For the same period the BoP in Rupee terms stood at Rs 143925 cr against Rs 82016 cr in fiscal 2002-03. According to the federal Commerce ministry's provisional report, India's merchandise trade

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deficit in terms of balance of payment during fiscal 2003-04 widened by 29.40 percent to US$ 16.70 bn from US$ 12.91 bn a year back. Net earnings from invisibles were up 49.17 percent at US$ 25.42 bn from US$ 17.04 bn in the previous fiscal (2002-03). There was an impressive over 110.89 percent growth in Current Account balance with a surplus at US$ 8.71 bn in 2003-04 from US$ 4.13 bn in the previous fiscal. Foreign direct investment in 2003-04 was lower at US$ 3.13 bn compared with US$ 3.61 bn in the comparable period of fiscal 2002-03. The overall balance of payment at the end of fiscal 2003-04 stood at US$ 31.42 bn compared with US$ 16.98 bn in fiscal 2002-03.

The overall trade balance at the end of fiscal 2003-04, according to foreign trade statistics released by the federal Commerce ministry, shows a widening trade gap of US$ (-)14.30 bn against US $ (-) 8.69 bn in fiscal 2002-03. Exports during 2003-04 stood at US$ 63.84 bn signifying 21.10 percent growth over previous comparable figure of US$ 52.71 bn. Imports during 2003-04 stood at US$ 78.15 bn against US$61.41 bn in fiscal 2002-03 signifying 27.25 percent increase.

Meanwhile, for India, fiscal 2004-05 took off on a disappointing note. The provisional merchandise trade figures for 2004-05 show abnormal widening of trade deficit. In the first 11 months (April, 2004-February, 2005) of the fiscal 2004-05, India's exports were up 27.30 percent where as imports witnessed a marked growth of as high as about 36.33 percent leading to a deficit trade balance of over US$ 23.83

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billion. In rupee terms the deficit stands at Rs 107191.25 crore. Oil imports during this 11-month period stood at US$ 26.65 bn signifying 44.45 percent increase over the comparable period's US$ 18.45 bn in 2003-04. Non-oil imports during this period are estimated at US$ 66.97 bn- up 33.36 percent higher than US$ 50.22 bn for the comparable period of fiscal 2003-04.

In terms of balance of payment in 2004-05, India's foreign trade in first nine months stood at a hopping deficit of US$ 28.35 bn signifying 11.30 percent increase over previous comparable period in fiscal 2003-04 when deficit stood at US$ 13.98 bn.

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# CHAPTER 6

## *Impact of Foreign Investment*

The era of 1990s has been an era of structural reforms where much emphasis has been on privatisation and deregulation of domestic economies, especially in the socialist and developing countries. It is well known that under the era of planning, both centrally planned as well mixed economies, had adopted a system of rules and regulations, often highly complicated and cumbersome, for the growth of their domestic industrial economies. Behind this, the basic idea was to encourage, first, the public sector, and secondly, to have a guided growth of the private sector where especially, the foreign private investment was discouraged, this being the result of its dominating role in the pre-independence era in most of newly emerging economies where it had encouraged a colonial pattern of development. So, under the planned era, it was the public sector, which got the maximum attention and next to it was the local private sector, which found good opportunity to grow especially when strict trade regulations discouraged the import of foreign goods. As the time passed this system got more and more entrenched; which, in other words, means that far more strict rules and regulations were followed for conducting business and

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industry. This naturally provided all time boost to public sector and far larger resources began to flow into it than into private sector.

The above model very well fits into the growth of Indian economy during the past seven plans, which had gradually led to a lead place for the public sector, most of units under it were generally in perpetual red. On the other hand, the adoption of highly controlled and regulated economy had discouraged the flow of foreign private investment. As a result of these developments, the country was forced to borrow heavily from the international and other institutional lenders. It was also the growing deficit in balance of payments; as a consequence of pursuing aggressive trade policies that more and more help had to be sought from foreign lenders. In fact, this situation was at its worst couple of years, when the country had virtually lost its financial credibility and no global financial institution was prepared to lend money to bail our economy out of highly critical foreign exchange position. It was at this stage that the government had to pledge part of its gold reserves to raise the urgently needed credit.

It is interesting to find that while the earlier strategy of the planned development of this country for the public as well as the private sector was basically in favour of more and more employment generation rather than production, the recent strategy of structural reforms however puts all out emphasis on raising production and

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especially productivity as well expansion in trade rather than employment. Thus, employment, which has been the high priority issue in our planned strategy during the four decades preceding 1990, now suddenly becomes far less important issue under the new regime of privatisation and deregulation of the economy and bidding farewell to the public sector. The model of structural reforms borrowed from the Western Capitalist economies starts with the basic assumptions that the country already has full employment. Thus what is needed is redistribution of such employment in those areas of production, which promise higher output and productivity. Such type of approach is hardly suitable for a developing economy where employment happens to be the basic issue and this is all the more so for a highly densely populated economy like India where every year a very large number of young people enter the labour market. The fast growing backlog of unemployment becomes obvious enough from scanning the registers of employment exchange which of course, as is well know, does not reflect the situation in the rural areas which house over 2/3 of India's population.

That the recent situation in India's employment vis a vis population growth has been getting worse is supported form the study made by Rajendra Prasad Singh. It states, "Available facts that emerging realities make the labour scenario to appear bleak. The growth rate of labour force is continuing to overtake population growth rate as well as growth

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rate of employment opportunities. Growth rate of population during the decade 1991-01 was 2.1% per annum; the growth rate of labour force over the same period was 2.5% per annum.

Thus the employment situation being grim the basic question that arises is, can these structural reforms and privatisation move provide solution to this problem. First of all as under the structural reforms, the emphasis being on higher productivity, which, it is well known, could largely result from change in the existing mode of production, that is adopting new technology as well affecting a large number of changes in the whole scenario of production. We are straightaway confronted with these two issues, one is growing demand for skilled manpower capable of handling new equipment as well ensuring its well maintenance and the other is that such mode of production is generally going to be capital intensive and labour saving. Thus, in other words, means that the scope for generating more employment is reducing.

The impact of MNCs on employment generation in India has generated lot of controversy and that is not without any doubt. The main arguments put forth by the opponents of New Economic Policy are that the technology transfers which will take place alongwith the MNCs will be highly sophisticated and capital intensive, which may not lead to generation of employment in the economy. In order to compete with world-class

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manufacturing, cheap labour is seldom a major competitive advantage. Experience, market share, and technology innovations are greater determinants of cost than cheap labour. A study by Rudder Dutt brings out the fact that NEP by its programme of technological upgradation and import has led to decline in employment elasticities. He quotes Bhattacharya and Mitra that on the basis of the data obtained from 1981 and 1991 censuses, the study revealed that employment elasticity (measured as a ration of employment growth rate to income growth rate) has varied widely across sectors. For the economy as a whole, employment elasticity was 0.45. For the primary sector it was 0.74, but, for the manufacturing it was as low as 0.19. For trade and commerce it was 0.37. However, for service sector it was 0.65 and for construction it was 1.12. The rate of unemployment, which was 3.1% in 1990-91 shot up to 5.5% in 1993-94. This is cause of serious concern for the policy makers. The implication of the fall in gainful employment in the organised sector from 9% of total employment in 1992 to 8.7% in 1994 is again alarming. The argument put forth by the proponents that there shall be an increase in unemployment in the short period, but as the economy picks up this problem will be solved. But we have seen that growth has failed to trickle down so is the growth of employment. The deleterious influence of foreign investment in particular on the job market in India has been and is bound to be in future more and more marked and palpable. The emerging employment profile of the

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country is indeed disturbing under the political policy dispensation.

After looking at the positive and negative implications of the operations of MNCs one comes to the conclusion that under the present world perspective of globalisation our industry and trade will have to develop competitiveness, particularly with respect to quality, reliability, and cost in order to become a viable source-base for international markets. This will require the willingness to forego various internal and external protective devices afforded by laws of industrial licensing, monopoly control, etc. Ushering in competition by dismantling these barriers would invariably change the strategic focus to product design and marketing areas. There is a strong need to develop manufacturing excellence in order to deliver a sustained level of economic growth in future. The world economy has become so competitive that we have to import and keep pace with the highly developed industries as regards technology development is concerned. There is a wide gap between the manufacturing sector of the developed countries as against developing countries. In order to bridge this gap we have to get the assistance of foreign collaborators. Moreover, technology is advancing so fast that a resource starved country like India cannot devote much of its resources for research and development. The only implication, which should be taken care of, is that policy on foreign investment should be approached from a

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bargaining perspective rather than one of uncritical welcome.

Employment implications no doubt are serious and we have to restructure our indigenous plan strategy to meet this challenge. Merely creating more job opportunities through labour-intensive technologies or under the slogan of "Swadeshi" will not serve our purpose. We have not been able to obtain comparative advantage in many industries even after decades of investment concentration in these lines. In fact our leading experts today are all concerned with traditional and primary sector activities. At least, it is now time that we concentrate our attention on improving the productivity and in reducing the capital-output ratio therein. All this requires massive investment as well as knowledge improvement.

Another word of caution is regard to direction of investment. Most of the MNCs have entered into areas, which cater to elite consumptive patterns. Here role of the government role becomes all the more important to monitor such investment in accordance to our national priorities. Some incentives to MNCs can be given so that they should divert their efforts to priority areas.

Between 1972 and 1992 the 500 largest MNCs monitored by Fortune magazine laid off 4.4 million workers. Manufacturers are increasingly replacing labourers with machines. A study by

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Prof. Michael Hammer at MIT shows that re-engineering of a company's production can typically result in a 40% reduction in jobs. The objectives seem to be to lay off the workers and to reduce wage levels. More and more part time, temporary and self-employed workers are appearing in the job market even in the North America. MNCs are taking advantage of both low wages and state-of-the-art technology without sharing any of the productivity gains with their workers. For example, between 1975 and 1984 output per worker in electronics firms located in Mexico grew form 63% and 83% of US productivity levels for that industry. Over the same period wages paid to Mexican electronics workers fell from 24% to 15% of US levels. As Bruce Campbell explains "the problem is not wage difference, per se, but rather the existence in some jurisdictions of structures and institutions which prevent wages from rising in a generally positive relationship with productivity.

In a world of high unemployment, foot loose capital and widely divergent working conditions, free trade puts downward pressure on labour standards and pay scales everywhere. In less developed countries workers are forced to endure inhuman working conditions because their governments want to attract foreign investment.

The economy is expanding but it is hardly creating any new jobs. Most of the existing industrial units are shedding, excess labour, and in order to be

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competitive are resorting to sophisticated machinery and automation. The NSS data also shows that the growth of employment has come down from 2% per year in the period 1983 to 1993-94 to less than 1%. Urgent action will have to be taken to promote the generation of more employment in the country. Otherwise it will result in a serious problem of law and order.

There is a reduction in the proportion of the workforce to the total population in both urban and rural areas. Out of 1000 persons, 418 were part of the workforce on 1/1/1994. But now only 395 persons are part of the workforce. There is a beneficial rise in the student population ratio indicating a rising participation in secondary and higher education level.

The growth of employment should not be compared with growth of population and it must be viewed in the context of growth rate of workforce.

The growth of employment has declined sharply from 2.43% in 1987-88 to mere 0.98% in 1999-2000 but the growth of Labour Force Participation Rate has declined form 2.29% to 1.03% during the same period. The growth of GNP has gone up from 5.25% to 6.60% during the same period.

The number of persons employed in agriculture has declined from 68.5% in 1983 to 64.5% in 1993-94 and further to 59.9% in 1999-2000. Employment in sectors like construction, trade,

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financial services, and transport, storage and communication has grown faster than average along with the growth of GNP.

High rate of unemployment among the educated youth is a very serious problem.

The percentage of young unemployed persons having studied upto secondary level and above has come down from 20.7% to 14.8%. But the unemployment rate among the youth as a whole has gone up and unemployment rate among technically qualified persons is almost constant.

As in June 2000, there were 958 Employment Exchanges in the country and the job seekers registered with these exchanges were 406.98 lakh. Between January-June 2000, 26.64 lakh were registered for new jobs, while Employment Exchanges were able to provide jobs to only 80,000 persons.

During the last few years there has been considerable talk of downsizing either through voluntary retirement schemes or through retrenchment. This is true of both public and private sector organisations. In public sector Banks 99,452 have opted for VRS. This accounts for 11% of its staff. Staff accounts for 65-70% of total costs in public sector banks. National Textile Mill has introduced VRS in six units in Tamil Nadu. During the last one-year, 15,000 jobs have been cut between March 2000 and June 2001.

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About 1,200 employees of the Taj Group of Hotels have opted for VRS. Oberoi Welcome Group of Hotels have downsized by about 1,800. ITDC may offload another 1500 after privatisation. Automobile companies are downsizing in order to remain competitive. Telco got downsized by 9,375 workers, Bajaj Auto by about 4,785 workers have all cut the jobs. During the last one-year, 10,000 persons in the IT sector have lost their jobs. The software sector is too feeling the impact of the slow down. Indian Railways are the world's second largest rail transport system. Not only will there be recruitment in the Railways but it is considering proposals to cut 30,000 jobs every year. This is only glimpse of the grave situation.

The proportion of self-employed has come down form 58.9% in 1977-78 to 52.9% and the number of casual workers has gone up substantially from 27.2% to 33.2%. Organised sector employment grew relatively slow at 1.20% per annum during the 1983-94 period and has further slided down to only 0.53% between 1994 and 1999. Since ther is a general preference for all jobs in organised sector, this trend is of great concern. 44% of the labour force in 1999-2000 was illiterate and 33% had schooling upto secondary education and above. Only 5% of the workforce had the necessary vocational skills. There is therefore large-scale unemployment and at the same time shortage of skill. The fact of being employed is obviously no guarantee for escaping poverty because of the

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underemployment. It is estimated that 6.5% of the total employed (397 million in 1999-2000) i.e. around 25.74 million is underemployed.

The Task Force appointed by Planning Commission has recommended acceleration of the rate of growth of GDP, with particular emphasis on sectors that ensure spread of income, pursuing appropriate sectoral policies in individual sectors which are important for employment generation; implementing focussed special programmes for creating additional employment for vulnerable groups that may not be sufficiently benefited by the more general policies for generating economic growth; pursuing suitable policies for education and skill development, which would upgrade the quality of labour force, the policy and legal environment governing the labour market that encourages labour absorption; accelerated GDP growth to a range between 8% and 9% (continuation with GDP growth of about 6.5% will not help) to help achieve our objective of generating additional employment. The Task Force has further recommended lowering of import tariffs to ensure competition and increasing efficiency; allow agro companies to buy, develop and cultivate and sell degraded and wastelands after detailed delimitations and taking these lands out of purview of tenancy law; freedom of conversion of rural land into urban use; active involvement of large industrial units MNCs in food-processing; dereservation and increasing FDI in the SSI sector, expediting grant of necessary

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permission for setting up of good quality hotels, switchover to, switch over to modern retailing; emergence of modern and large transport companies; and removing present bias against large construction firms. Central Government should completely withdraw from the delivery of vocational training and labour reforms should be undertaken.

Recommendations of the Task Force were criticized by the Swadeshi Jagran Manch, Bharatiya Mazdoor Sangh, Khadi and Village Industries Board.

Therefore, in order to undertake a review of these recommendations Planning Commission has now set up another expert committee headed by Planning Commission Member S.P. Gupta. New committee is considering an agricultural driven job creation to be placed in the broad policy framework of second-generation reforms. IT is understood that using the latest census figures the committee has observed that unemployment is much higher at an estimated 10%. If the total work force is 400 million, the unemployed will account for 40 million. The new emphasis may be on some of the sectors in agriculture as watershed development, minor irrigation, fruit processing and many other diversified activities in agriculture and creating jobs in the small and medium sectors of industries.

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Advisory Panel set up by the Commission constituted to Review the constitution has emphasised on the growth of the small and unorganised industrial sectors. Their emphasis is not on creating jobs but on creating conditions that will enable a larger number of people to undertake activities on a self-employment basis as sustained agricultural growth, on both farm and non-farm employment, setting up of primary processing of agricultural products, development of rural community assets, encouraging activities like horticulture, floriculture, sericulture.

According to the panel, rural activities can create an additional 80 million jobs. All these estimates are based on various specific studies by the International Commission on Peace and Food, NDDB, NCAER, etc. These estimates therefore have a sound basis.

We discussed the subject with many social activists working in rural areas who have carried out a number of experiments, some of which have been successful. Their experiences can be good guide for future models of employment growth.

If we consider the general trend of employment in different countries in South Asia, we find some common features such as slow down of economic growth and growth in employment, casualisation of employment, non-declining share of informal sector in total employment, stable or rising

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unemployment, increasing incidence of long term unemployment, declining labour force participation and low level of education and skills of labour force. Casual workers are increasing in both rural and urban sectors.

The major contributors to employment in 1999-2000 were agriculture (60%), manufacturing (12%), trade (9%), community, social and personal services (8%). In manufacturing sector large and medium scale units together have contributed to 14% of employment while 86% of employment is in the small-scale industries. Owing to persistent pursuit of market development and increasing emphasis on efficiency of production activities, the large and medium scale industries have adopted capital intensive techniques which has resulted in the displacement of labour.

A GDP growth of about 4.80% was achieved in 1983 to 1986-87 but the employment growth during this period approximately was 1.54%. From 1993-94 to 1999-2000, the average GDP growth was 6.6 to 6.5%. During this period, employment grew by a mere 0.98%.

Employment has been continuously growing in the small-scale sector and this has gone up from 12.53 million in 1990-91 to 18.56 million having cumulative annual growth in employment of 4.19%.

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There were 33.7 lakh small units in 2000-01 (as against 19.4 lakh in 1990-91) with total production of Rs. 6,39,024 crore employing about 18 million persons and exporting goods worth Rs. 59,978 crore.

A number of Committees have been appointed to study the difficulties and problems that small-scale industries are facing, the latest being the S.P. Gupta Committee. The committee made recommendations regarding enhancing the availability of credit, improvement in technology, and the marketing of products. The small entrepreneurs have been complaining of harassment by inspectors and the rigidity of labour laws. While the large corporate sector employed a total number of 67.4 lakh persons, the small-scale sector employed 171.6 lakh persons in 1999-2000, which has gone up to 177 lakh in 2000.

Except a few industries like garments or leather goods, which are labour intensive, most of the manufacturing industries are highly mechanised employing few workers. In comparison the service sector is much more labour intensive.

In manufacturing companies labour intensity, the highest being in Tata Steel, with labour costs of 15.3% of total sales. Compared to manufacturing companies, hotels have more than 22% of costs as wages or salaries. Infotech companies have 42% of costs as wages. The service sector accounted for 49% of our GDP. The services sector includes

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trade, hotels and restaurants, banking, transport, communications, insurance.

The efforts of the Government will have to be in creation of a congenial atmosphere for the services sector to grow.

Urban informal sector comprises very small units producing and distributing goods and services, and mostly consists of largely independent self-employed persons. This sector is also heterogeneous, and comprises of small modern manufacturing and sevice enterprises and consists of street vendors, shoe shiners, hawkers, rickshaw pullers, rag pickers, small commercial enterprises, repair shops, road side dhadbas, paan shops, bakeries, food processing units, leather goods manufacturers, etc.

Though unorganised sector has provided much additional employment in recent years, this sector has been neglected by the policy makers. No special efforts have been made to promote its growth. Most of the workers and entrepreneurs in this sector operate at low economic levels and are not wanted by the urban society. The municipal authorities remove them very often from their places of work, their work-places are demolished and goods confiscated.

In a residential zone, processing and manufacturing activity is not allowed to be carried on, whereby large number of undertakings had to

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be closed down. Activities like IT industry, which do not pollute or create noise, may be allowed in residential areas. Without such liberal provisions, small entrepreneurs will find it hard to start any new business and survive.

We cannot depend on industrialisation alone for creating new jobs. One has to turn to the rural sector and give emphasis on agriculture, and allied occupations including agri-business and processing.

The scheme based on the study by Dr. M.S. Swaminathan which spelled out strategy for creation of 100 million jobs and incorporated in 8th Plan needs to be revived and reworked to eradicate poverty and unemployment in India.

Some non-Government organisations in Maharashtra have made successful experiments in utilizing community common water resources and its equitable distribution among the rural communities. The Green Revolution which took place, comparatively in a small area of the country seems to have become unsustainable. NGOs advocate and practice water management on a scientific basis, organic farming, and low capital-intensive agro-processing, and organise training programmes resulting in reverse migration from cities to villages in some cases. Similar experiments have been carried out by Anna Hazare and Gram Gaurav Pratishthan in

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Maharashtra, Forest Revival and Water Harvesting by Tarun Bharat Sangh in Rajasthan, and by Water Conservation Mission in Andhra Pradesh.

Agriculture productivity can be improved by use of fertilisers, soil health care, realignment of cropping patterns, water management including drainage, integrated horticulture, floriculture, medicinal plant production, production of seeds and planting materials, animal husbandry programmes, integrated programme for intensive aquaculture, s3ericulture, wasteland development, soil conservation, water conservation and tank rehabilitation, compost preparation, vermiculture and organic farming, establishment of agro-industrial complexes, development of rural infrastructure. These improvements in agriculture will create jobs on a large scale.

The forestry sector holds large potential for creation of employment. There is a large potential for agro-forestry on private agricultural holdings and also the private sector plantations on Government lands lying barren or wastelands. In addition to generating employment it will improve soil conservation, environmental protection, raw material supply for industries, ground water replenishments.

The overall budgetary allocations under the State sector for various programmes are not commensurate with the size and magnitude of the problem of maintenance and sustenance of forest

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wealth. The forest provide nutrition, food security in lean seasons, source of supplementary income and range of household items from fodder to fuel wood, medicinal plants and so on.

A new thrust for creation of employment can be by way of encouraging large-scale investment in forestry and promotion of agro-forestry on agricultural land. The survey and settlement records in many states carried out during 1960s and 1970s categorised vast expanses of fallow land owned by the States as having bushy forest growth and therefore these came under the control of the State Revenue Departments and cannot be leased and Forest Conservation Act applied to them. Though very often these lands do not have any canopy cover but some undergrowth of bushes in some areas which is deemed to be forest lands. When the State is unable to fully look after areas which is deemed to be forest lands and which are under direct control of the State, there is perhaps need to review the provisions of the Act. Permitting private activities and initiatives will ensure that the areas would have canopy cover for medium term conferring benefits of soil and moisture conservation, groundwater recharging, arresting of monsoon and biosphere improvement benefiting surrounding agricultural land.

It has been reported that China has been able to bring down the people dependent on land from 70% to 45%. The Township, Village and Private enterprises has become the most dynamic sector

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accounting for 40% of the countries total industrial employment. It is worthwhile to study the organisation of these organisations, the types of products manufactures by these units and marketed by them.

For promoting growth of employment, special skills have to be developed, and for this, training programmes have to be organised at different levels.

In rural areas there is a dominance of casual workers and self-employed persons who are in large numbers. Therefore, one has to take advantage of the opportunities. Both in urban and rural areas, there may not be an impressive rise in wage employment but there will probably enough scope for self-employment.

There was no Ministry or Department responsible for executing plans for employment promotion. Ministry of Labour deals with employment, as far as questions in Parliaments are concerned. It collects information from different departments and prepares replies to questions to be answered in the Parliament.

The obvious choice seems to be the Ministry of Labour. Unless there is someone responsible, there will be no initiative, no diligent execution and no monitoring.

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There is general awareness that the travel and tourism industry has great potential in the country for generating jobs. This is particularly so because a large part of the potential in the country has remained untapped. If it is promoted there will be resultant spin-offs like revitalisation of arts and crafts, including performing arts.

The specific components of development which are underway as per Tenth Plan include infrastructure development, product development and diversification, promotion of entrepreneurship and self employment, human resources development, promotion and marketing thrust with public and private partnership with the Government working as facilitator. Specific development initiatives include development of Mega tourism resorts, targeted approach towards development of tourism circuits, and promotion and marketing initiatives.

Promotion of domestic tourism has mostly been taken up by the State Governments based on their own resources. Development of low-end sector of the travel and tourism industry has been largely in the hands of small entrepreneurs, and mostly confined to places of pilgrimage and other commercial or industrial centres.

The developments in the field of telecommunications, the Internet revolution and associated IT enabled technological developments are bringing about rapid, informative and

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significant changes in different aspects of human life. In all sectors of human existence and activity, healthcare communication, trade, manufacturing services, entertainment, education, research and so on. Information technology has been in the forefront of profound changes.

Estimated number of IT professionals in the country is 5,22,000, of which nearly 1,70,000 are in the IT enabled services, and 2,20,000 in user organisations. The present level of about 1,06,000 personnel employed in the IT enabled services is likely grow to ten times by 2008. Domestic sector also offers a large potential for all such services with improvement in the infrastructure like assured electricity, better communication links, etc.

The health care sector is another area, which offers considerable potential for the creation of sustained jobs throughout the length and breadth of the country. The country would need more than 1.5 lakh paramedical professionals by the year 2007 over and above the projected availability of 17.76 lakh persons in 2002. Besides the Government approach for catering to the health needs of the rural population would suggest pooling of medical practitioners including from alternative forms of medicine. Similarly, in areas where there is an acute shortage of doctors, qualified nurses and midwives can be permitted to render simple primary health services.

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With increasing affluence leading to changes in the lifestyle and the health and the health concerns associated with this stress and strain of urban life, there is also going to be a large increase in the requirement for medical services in the urban areas. This is further compounded by the increase in employment in sectors like psychiatric counselling, fitness professionals and nutritionists.

The manpower available in the health care sector in the rural areas in the country shows a huge shortfall in the personnel levels of which run to over 1.6 lakh medical and paramedical personnel. There is a considerable scope for absorption of medical and paramedical personnel for catering to the backlog and expanding requirements of this sector.

## 6.1 Impact of FDI

The global context for development has changed over the last three decades. These changes affect not only the role of FDI in the host countries, but also the government policies on FDI. The following paragraphs describe the roles of FDI and their relative importance in the changed global scenario.

1. Enhancing the technology, skill and knowledge base

   Firms in developing countries have to become proficient and technically efficient in order to

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compete in the international market. Technology is not sold like physical products, in fully embodied forms. It has important tacit elements that need effort to master. It often faces an uncertain environment where the skills, information, networks and credit needed are not readily available. Enterprises have to interact intensively with other agents. All these features mean that technology development faces extensive coordination problems, externalities, missing markets and cumulative effects. More importantly, firms may face learning problems. The diffusion of technologies even in industrially advanced countries poses challenges. In developing countries, it is generally far more difficult. Mastering new technology is not just once-for-all task. It is a process that requires continuous upgrading and deepening of all kinds of intellectual capital, as well supporting networks and institutions. Without this, countries can remain at the bottom of the technology ladder where the competitive edge lays in simple assembly or processing based on cheap labour. Once wages starts rising they lose this edge. Thus, they master the simpler elements of technology, they have to move into more advanced technological capabilities. As technologies change, they have to upgrade their own capabilities to remain competitive. As they gain competence in simple activities, they have to move to advance ones. This process of technology

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development involves high costs, risks of market and institutional failures, and the ability of governments to overcome them, create new markets and strengthen institutions. This is where the huge size and capabilities of a multinational companies come into picture. Free and easy access to technologies developed by these companies can be of a great help to sustainable development of domestic enterprises

Foreign companies transfer technology in two ways:

(1) Through internal transfer to affiliate enterprises in various countries

(2) Through external transfer to enterprises on payment of royalty or in the form of a joint venture

Internal transfer, as the name indicates, takes the form of direct investment and is, by definition, the preserve of MNCs. It is difficult to measure and compare directly the amount of technology transferred in this manner. It can be measured by payments for royalties and license fees in the form of repatriation of profit.

Rising costs or quick movement of technology may compel an enterprise to purchase technology from another firm, which

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is called external transfer of technology. This mode is more prominent in countries with closed economy. This mode of transfer takes a variety of forms: minority joint ventures, franchising, capital goods sales, licenses, technical assistance, subcontracting or original equipment-manufacturing arrangements. MNCs are not the only source of such transfer of technology, but they are a force to reckon in high technology activities and in providing entire "packages", i.e. technology together with management, marketing, etc.

The use of new technology by the recipient is the only one of its of technology transfer arrangements. The other benefit is the diffusion of technology and skills within the host economy. Many forms of diffusion are not priced or paid for in markets. They are externalities, which arise involuntarily or are deliberately undertaken to overcome information problems. Firms diffuse technology and skills to suppliers, customers and institutions with which they have direct dealings. Globalisation gives such collaboration an international dimension: supply contracts extend over national boundaries, and suppliers follow their customers overseas.

Except certain compulsions the firms acquire raw material locally because of proximity,

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lower transaction costs, close monitoring and greater flexibility in changing specifications and developing new inputs. These firms also, thus, invest in helping local suppliers upgrade their technology. Foreign enterprises can also have direct linkages with a variety of local institutions as well as firms. These include local technology institutions such as standards and quality control agencies, research institutes and universities, vocational training centres, financial intermediaries, infrastructure providers and so on. The most relevant ones are those providing technical skill and inputs. The scale of host country's Research and Development, thus, goes higher.

MNCs invest significantly in training often more than local counterparts. They also often bring in training materials and techniques to supplement training offered locally. Their awareness of the importance of skill formation sometimes, leads them to foster new training institutions.

Apart from providing a competitive stimulus, MNCs can have spill over benefits. Local competitors can learn from their technological or managerial practices, attract their employees or gain access to their technical knowledge.

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MNCs undertake large R&D projects. The developing countries having adequate technically qualified workforce have large benefits from such projects. Also, when the production base in a country is very large and such that requires localisation, MNCs have to undertake R&D in such countries. For example, India with its large array of engineers and science graduates has become a major destination for undertaking R&D for MNCs especially in software, biotechnology and automobile sectors. This has facilitated to make India a manufacturing centre for global firms.

Thus, technology flows across economies occurs in two ways – embodied and disembodied. Its effective transfer and subsequent development may depend on the channels of transfer and, increasingly on local abilities to use it. With a growing reliance on information and rapid change, the abilities needed have become more varied and skill intensive. As a result of technological progress, the channels for transferring technology have expanded and often become cheaper, though at the advanced end of the spectrum, access may have become more difficult. The cost of innovation, the spread of international production and policy liberalisation have increased the role of foreign enterprises in all aspects of technology. As commercial enterprises,

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MNCs in principle do not have an interest in transferring knowledge to and supportive innovation in foreign affiliates beyond what is needed for the production process or product at hand. Developing countries, therefore cannot expect that by simply opening their doors to FDI, MNCs will transform their technological base. Deficiency in technological learning and transfer in developing countries can mean that markets do not create technological dynamism at best, they can lead to a better use of static endowments but not to the continuous upgrading that competing in the new context requires. In these circumstances, the government of the host country therefore requires to play a crucial role, i.e. to promote local learning, development of skills, etc.

2. Boosting the domestic financial resources

It is an established fact that investment is a key factor in economic growth. Countries that devote a high proportion of output to investment, may sustain more rapid growth. In a closed economy, with no access to foreign savings, investment is financed solely from the domestic savings. In most countries with superior investment performance, foreign savings normally play a complimentary role in the provision of financial resources for development. They

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permit domestic investment in a country to exceed its own savings. But in developing countries, they always lag behind in their own savings as well as foreign investment. Here, they play the crucial role for the development of the economy. FDI has come to play a growing role during the 1990s within international flows of capital. The impact of FDI on investment in host country depends on its conditions. Therefore it will be different in countries with abundant countries and other forms of capital than in countries without enough capital relative to their investment needs or demand. It is also dependent on the financial and other aspect of behaviour of foreign affiliates viz. their mode of entry, the activities they undertake, their source of finance, and the ways in which they affect the domestic economy.

3. Building competitiveness of domestic firms

The greatest potential of MNCs lies in difficult, technology intensive, and marketing intensive products where they have the largest ownership advantages over other firms. They can promote exports best in the complex or branded products. They have access to established brand names, warehouses, transport facilities and marketing links.

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The entry of MNCs in different sectors of the industry leads to increased competition in the respective sectors. The domestic industries are at loggerheads with some of the best technologies, marketing techniques, administrative skills of the world. The effects of this competition are usually beneficial for the industry as a whole. Increased competition encourages both productive efficiency and a more efficient allocation of resources. Concerns are raised that strong MNCs out-compete their domestic counterparts, or at least force the local firms to merge. Thus increasing economic concentration and market domination. But these effects are not seen very largely in India, except some popular cases like those in the beverage industry.

4. Generating employment opportunities

National labour markets are becoming increasingly interdependent. Maintaining or increasing employment or its quality in a particular country requires that its labour market must be responsive not only to changes related to development and growth within the country, but also to changing conditions worldwide. At the same time, globalisation through international production creates scope for MNCs and foreign firms to

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play a role in the generation and upgrading of employment and the building up of skills in the host countries. The role and impact of MNCs activities in these respects can vary, however, according to the type or motivation of FDI, the industries in which MNCs invest, the strategies they adopt, in host country conditions. They also depend significantly on the policies of host countries on FDI for increasing employment quantity, improving employment quality and strengthening human resource capabilities and minimising any negative effect that FDI may have in these respects.

The quantity and quality of employment generated within a firm regardless of whether it is MNC or not depends mainly upon the industry group to which it belongs, the production activities in which it is engaged and its size. MNCs like other enterprises, combine labour and other factors of production to generate goods and services. There are some factors that suggest that the behaviour, practice and role of MNCs with respect to employment and skills upgrading may differ in some respects from those of the other, which includes larger size and greater technological sophistication, the competitive pressures under which they operate and their ability to deliver goods and services.

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Foreign Direct Investment generates employment opportunities in host countries directly and indirectly. Foreign affiliates of MNCs employ people in their mines, plantations, manufacturing plants and service establishments. This may be the direct employment. They also cause employment to be created in enterprises that are suppliers, sub-contractors or service providers to them. These include domestic firms as well as foreign affiliates of MNCs, some of which may be established because of associated investments attracted to the country by the demand for their products or services from original investors. This may be termed as indirect employment.

Because of their size, technological sophistication and origin, principally in developed countries, MNCs are often considered better employers than domestic firms. MNCs also provide excellent training facilities to their employees, which plays important role in boosting their overall employability. They invest in human capital, which is most essentially in country like India with large resources of human capital.

The working conditions at MNCs work complexes are observed to be better than their domestic counterparts. This makes them more efficient and increases their productivity.

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## 6.2 Impact of FDI and economic reforms on overall employment situation in the country

Economic reforms may have given a boost to industrial productivity and brought in foreign investment in capital-intensive areas. But the boom has not created jobs. This was not unexpected. According to a report by the Washington-based Institute of Policy Studies (IPS), the combined sales of the world's top 200 MNCs is now greater than the combined GDP of all but the world's nine largest national economies. Yet, the total direct employment generated by these multinationals is a mere 18.8 millions-one-hundredth of one per cent of the global workforce.

India's Ninth Five-Year Plan projects generation of 54 million new jobs during the Plan period (1997-2002). But performance has always fallen short of target in the past, and few believe that the current Plan will be able to meet its target.

India's labour force is growing at a rate of 2.5 per cent annually, but employment is growing at only 2.3 per cent. Thus, the country is faced with the challenge of not only absorbing new entrants to the job market (estimated at seven million people every year), but also clearing the backlog.

Sixty per cent of India's workforce is self-employed, many of who remain very poor. Nearly 30 per cent are casual workers (i.e. they work only when they are able to get jobs and remain unpaid for the rest of the days). Only about 10 per cent

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are regular employees, of which two-fifths are employed by the public sector.

More than 90 per cent of the labour force is employed in the "unorganised sector", i.e. sectors which don't provide with the social security and other benefits of employment in the "organised sector."

In the rural areas, agricultural workers form the bulk of the unorganised sector. In urban India, contract and sub-contract as well as migratory agricultural labourers make up most of the unorganised labour force.

Unorganised sector is made up of jobs in which the Minimum Wage Act is either not, or only marginally, implemented. The absence of unions in the unorganised sector does not provide any opportunity for collective bargaining.

Over 70 per cent of the labour force in all sector combined (organised and unorganised) is either illiterate or educated below the primary level.

The Ninth Plan projects a decline in the population growth rate to 1.59 per cent per annum by the end of the Ninth Plan, from over 2 per cent in the last three decades. However, it expects the growth rate of the labour force to reach a peak level of 2.54 per cent per annum over this period; the highest it has ever been and is ever likely to attain. This is because of the change in age structure, with the

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highest growth occurring in the 15-19 years age group in the Ninth Plan period.

The addition to the labour force during the Plan period is estimated to be 53 millions on the "usual status" concept. The acceleration in the economy's growth rate to 7 per cent per annum, with special emphasis on the agriculture sector, is expected to help in creating 54 million work opportunities over the period. This would lead to a reduction in the open unemployment rate from 1.9 per cent in 1996-97 to 1.47 per cent in the Plan's terminal year, that is, by about a million persons - from 7.5 million to 6.63 million.

In other words, if the economy maintains an annual growth of 7 per cent, it would be just sufficient to absorb the new additions to the labour force. If the economy could grow at around 8 per cent per annum during the Plan period, the incidence of open unemployment could be brought down by two million persons, thus attaining near full employment by the end of the Plan period, according to the Plan.

However, there appears to be some confusion about the figure of open unemployment. The unemployment figure given in the executive summary of the Ninth Plan, gives the figure of open unemployment at 7.5 million while the annual report of the Labour Ministry, for 1995-96, puts the figure for 1995 at 18.7 million. An internal government paper prepared in 1997 put

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the unemployment figure at the beginning of the Eighth Plan at 17 millions and at 18.7 million at the end of 1994-95. Perhaps the Planning Commission referred to the current figure while the Labour Ministry figure referred to the accumulated unemployment backlog.

*Underemployment*

Open unemployment is not a true indicator of the gravity of the unemployment problem in an economy such as India, characterised as it is by large-scale underemployment and poor employment quality in the unorganised sector, which accounts for over 90 per cent of the total employment. The organised sector contributes only about 9 per cent to the total employment.

Underemployment in various segments of the labour force is quite high. For instance, though open unemployment was only 2 per cent in 1993-94, the incidence of under-employment and unemployment taken together was as much as 10 per cent that year. This, in spite of the fact that the incidence of underemployment was reduced substantially in the decade ending 1993-94.

According to the Planning Commission, the States which face the prospect of increased unemployment in the post-Ninth Plan period (2002- 2007) are Bihar, Rajasthan, Uttar Pradesh, Kerala and Punjab.

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## 6.3 Sector-wise analysis of impact of FDI and economic reforms

I have identified the following as the factors of impact of liberalisation laws and policies

1. Rapid changes in technology and their consequences and ramifications

2. The effects that these changes were likely to have on the nature and structure of industry, on methods and places of production, on employment and the skills necessary to retain employability and mobility, and

3. The responses that are necessary to acquire and retain economic efficiency and international competitiveness

The context makes a special mention of the need to attain and retain the degree of international competitiveness that our economy needs in the era of globalisation. Competitiveness should not be regarded as the need of any single sector of our society or economy. Competitiveness does not depend on merely technology, credit, inputs and managerial skills, but also on the contribution that labour makes. The commitment of the workforce to quality and productivity must be high. This commitment and the new work culture that it calls for can be created only when workers feel that

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they are receiving fair wages, a fair share of profits and incentives, and the respect or consideration due to partners.

Our Constitution describes our State as a sovereign, secular, democratic and socialist republic. The fundamental rights guaranteed by the Constitution include the right against exploitation. The Directive Principles are not justiceable in a court of law, but they are both for the guidance of the state and a covenant with the people. There is another state of factors. The new concepts of Human Rights, and the conventions and standards that have emerged from the United Nations and the International Labour Organisation, which are valid in the present context of labour reforms.

### 6.3.1 *Textiles sector*

The textile industry in the mill sector has been plagued by sickness and industrial unrest. One of the major events that showed the extent of unrest among workers was the strike of textile workers in Bombay, which commenced in January 1982, and continued for more than a year. With the structural transformation in the mill sector, and the competition faced from powerlooms, the textile industry in the mill sector began to face increasing sickness. The other reasons for sickness were comparatively low productivity, lack of modernisation, increase in cost of inputs, etc. The growing incidence of sickness is reflected by the increase in the number of closures, which

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increased from 123 in the year 1992-93 to 349 in 1999-2000. Globalisation has also had adverse effects on the already sick textile industry as imports have increased and textile products from other countries are available in abundance at cheaper rates.

The pathetic condition of workers in the decentralised sector also deserves mention. The wage levels in this sector are also on lower side. It is estimated that more than 2.50 lakh textile workers have been affected adversely due to closure and curtailment of activities. Powerlooms were considered to be viable propositions. But due to the vast expansion of capacity they are also becoming uneconomical, which calls for massive rationalisation in production techniques.

### 6.3.2 *Steel sector*

India has continued to be the 10th largest steel producing country in the world during 1999-2000, and has consolidated its position in world steel production in ensuing years. This sector directly provides employment to over 5 lakh people. The global steel industry has witnessed major ups and downs in the last few decades, especially over the past few years. It is in this global context that the Indian steel industry will have to identify its future role. With the coming of liberalisation, the steel industry, especially in the public sector, has now to face up, not only to domestic competition but also to global competition in terms of product

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range, quality and price. The factors affecting production and productivity are labour, material, technology and capital. The most important factor for the improvement of productivity is the workforce. High productivity is necessary for the survival of the industry.

### 6.3.3 Plantation Sector

The total number of workers employed by all tea plantations has risen from 7.31 lakh in 1967 to 11.38 lakh in 1999-2000. The number of workers employed in coffee plantations has since risen from 2.6 lakh in 1967 to 5.35 lakh in 1999-2000. In the year 1999-2000 the total employment in rubber plantations has risen from 1.22 lakh in 1967 to 3.48 lakh. In the year 1999-2000 the total cardamom plantations were employing 30,000 workers. Plantation operations are carried out in open fields. Employment depends upon the intensity of operations and crop availability. The industry can be described as seasonal. Because of the humid conditions workers are often exposed to malaria. Every plantation is required to provide medical facilities such as dispensaries for the workers and their families. The things have improved in these regards, but more attention has to be devoted to make the facilities adequate and satisfactory. The minimum wages fixed for agricultural workers apply to plantation workers as well. The workers are mostly paid the minimum wages fixed by the State Governments for agricultural workers. In Kerala, wages are fixed

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through negotiated settlements or under conciliation settlements. The plantation industry is at present facing a severe crisis. The prices of coffee have come down almost by 50%. The average rubber has come down from Rs. 47.50 kg in 1995-96 to Rs. 27 per kg in 1998-99. In 2000 the price stood at Rs. 28.5 kg, which was about Rs. 14.35 below the cost of production. Tea plantations have faced similar conditions. Russia was one of the biggest consumers of Indian tea, but exports of tea to Russia have come down drastically. The import duty on Sri Lankan tea under the Indo-Sri Lanka trade agreement has been brought down to 7.5%. As a result the prices of indigenous tea, particularly, from the Nilgiris have also come down. Producers are losing about Rs. 17 per kg.

Competitiveness and low costs of production have to be achieved through increased productivity, improved quality, uniqueness, and so on. The workers/unions will also have to accept the crucial role that productivity and productivity norms play in ensuring the competitiveness necessary for the survival of the industry.

The Government therefore, urgently needs to examine measures that can be taken to ensure the viability of the industry without adversely affecting the interests of the workforce employed in the industry. There is a strong case for reducing the tax burden on the industry.

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### *6.3.4 Chemicals Sector*

The overall existing employment in the chemical industry is rated around 4.5 million. The industry generates additional indirect employment to nearly 12 million workers in transport, distribution, sales, packaging, exports, etc. It is expected that despite the ongoing restructuring the chemical industry will continue to offer high job opportunities.

India's main competitive strength lies in speciality chemicals. It appears that in the future one of the main competitors of India would be China. 60% of synthetic detergents is produced in the small scale sector. The small-scale industries account for more than 50% of the total dyestuffs production. In drugs and pharmaceuticals, the small-scale units account for 40% of the total production with more than 11,000 manufacturing units. The small-scale industries in the drugs and pharmaceuticals sector provide employment to more than 1,70,000 workers directly plastic processing industry to 1,65,000 persons directly. The share of the small-scale industries in the production of rubber products is 30%. In the surface coating, i.e. paints, varnishes, etc. there are 20,000 small-scale units producing around 50% of the total production. The toiletries, cosmetics an agarbatti industry has more than 15,000 units in the small-scale sector.

The chemical industry carries out many hazardous processes and operations. Workers in chemical factories are often exposed to dangerous

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chemicals, fumes and gases. There is an imperative need for periodical medical check-ups for early identification of occupational health hazards as well as technological upgradation of safety norms.

### 6.3.5 Mining Sector

The mineral extraction and processing is the base of industrialisation in any part of the world. At the time of independence, a total number of 3,21,537 people were employed the coal mining industry. In the year 1999-2000, the coal industry employed about 5,50,000 workers. The nationalisation of the industry brought about considerable change in the lives of the workers engaged in coal mining. They now get the wages settled through negotiations. The housing satisfaction percentage terms has increased form 21.71% to 75.05%. There is considerable increase in the number of hospitals. The number of schools and colleges too has increased.

### 6.3.6 Coal Sector

Globalisation has had an adverse impact on the coal industry in India. Low ash cooking coal required for making steel is not available in the country to the extent that is required. The western coastal states like Gujarat, Maharashtra, Karnataka, and Kerala that do not produce coal, or where surface transportation cost to consumption

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centres is very high, find imported coal much cheaper. The cost of production of coal in India is very high. The labour cost of Indian coal is as high as 50% of the total cost of production, whereas it is only 20% in some of the other coal producing countries in the world.

In the year 1947, non-coal mines employed 85,726 persons in about 1,074 non-coal mines. According to 1998 figures, the non-coal mine industry including oil employed about 195,000 persons. The frequency of accidents in mines in India in terms of fatal and serious accidents calculated on the basis of per 1000 persons employed is not worse than in any other country, but it is perhaps the highest in terms of million tonnes of minerals produced.

### 6.3.7 *Construction Sector*

Construction industry covers a wide field of activities and provides employment for workers of various levels of skills. Much of the work in this field goes on under conditions that are often very strenuous and hazardous. Construction industry is the second largest economic activity in India. Construction has accounted for about 40% of the investment in the country during last 45 years. An estimated 14.6 million persons were directly employed in construction work in 1995-96. A recent study gives estimates and projections on employment in the industry for the period 1995-96 to 2004-05 according to which total employment

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in the industry is expected to increase to 32.6 million in 2004-05 from 14.6 million in 1995-96. While in 1995-96, unskilled workers comprised 73.08% of the workforce; in 2004-

05 it is likely to be 55.08%. Comparatively, the percentage of skilled workers is likely to increase from 15.35 to 27.62. For the existing workforce of 14.6 million, and against an annual increase of 1.2 million employees in construction, the average rate of formal training is around 10,000 persons per year since 1989 in 15 construction trades and 8 manufacturing skills. There are constraints on the modernisation of construction activity. These are inherent in the technology itself, and due to the social linkages of technology. Due to the scope for easy entry, small firms with scant resources and limited technical capabilities proliferate. Sub-contracting and low wages justify the continued use of archaic methods of construction. Low wages produce poverty on the one hand, and low productivity on the other. Workers are exploited because they are illiterate, socially backward, unskilled, unorganised, uninformed and poor. The industry functions at low productivity because the technology it employs is among the 'most backward in the world'.

Some laws are of direct relevance to construction labour, namely

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(1) Contract Labour (Regulation and Abolition) Act, 1970;

(2) Inter-State Migrant Labour (Regulation of Employment Conditions of Service) Act, 1979;

(3) Building and Construction Workers (Regulation of Employment and Conditions of Service) Act, 1996;

(4) Building and other Construction Workers Welfare Cess Act, 1996.

The problem is that the laws are not implemented in the construction industry. Construction labour does not get the benefits of the ESI Act, but is covered by the Workmen Compensation Act, 1923. While the Employee's Provident Fund Act, 1952 applies to the construction industry both the employer and employees are normally prefer to avoid implementing the Act for their own reasons. While the Maternity Benefit Act, 1961 applies; the number of beneficiaries is likely to be limited due to the intermittent nature of employment. The industry does employ a sizeable number of women workers, although largely as unskilled labour. It is estimated that the percentage of women in the construction industry is around 30 to 40.

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The importance of adequate infrastructure, generation and effective allocation of capital and labour, technology and the creation of skill has remained intact for sustained economic development. These factors determine how well each economy uses its endowments and adds to them. They also affect flexibility and dynamism of the country in responding to the changing economic situation.

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# CHAPTER 7

## Conclusion & Suggestions

India used its import policy for the healthy development of local industries. A good number of restrictions were put on the import of industrial goods, and the effort was to encourage the production of these goods indigenously.

Levying higher tariffs and a total or partial physical ban on imports of such products gave a much- needed sheltered market for Indian goods. But as years went by, industries acquired experience in manufacturing and turned out quality products. During the Second and Third Five Year Plans, the emphasis was on the development of capital goods industries. Encouragement was given to import technical know-how and to enter in to foreign collaborations to undertake manufacture of capital equipment locally. This gave a fillip to industrial development.

The Government gave encouragement to industries to import parts and components required for indigenous production. Actual users of imported raw materials or products were given preference over the category of established importers, i.e. traders. Items that were scarce were channelised through the State Trading Corporation, Mines and

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Minerals Trading Corporation and such other Government bodies. Imports were strictly controlled by the import policy announced every year by the Government of India.

Custom tariffs were raised in some cases to 200 to 300% on imported products. This gave protection to local industries. The Government also followed a policy of low tariffs on import of raw materials, parts and components compared to those on finished products. This encouraged Indian industries to manufacture or assemble final products in India.

To provide the financial infrastructure necessary for industry, the Government of India established various financial institutions namely,

(1) The Industrial Finance Corporation of India (IFCI) in 1948,

(2) Industrial Credit and Investment Corporation of India (ICICI) in 1955,

(3) Industrial Development Bank of India (IDBI) in 1964,

(4) Industrial Reconstruction Corporation of India (IRCI) in 1971

(5) Unit Trust of India (UTI) in 1963, and

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(6) Life Insurance Corporation of India (LIC) in 1956.

For financial assistance to small enterprises, Finance Corporations were established in all states on the basis of an Act passed by the Parliament in 1951. The National Small Industries Corporation was established at the Centre and a Small Industries Development Bank was established in 1989.

Regulations under the Foreign Exchange Regulation Act, restricted foreign investment in a company to 40%. This ensured that much of the control in companies with foreign collaboration remained in the hands of Indians.

Encouragement to small-scale industry by providing a number of support measures covered industrial extension services, factory space in industrial estates, credit facilities at concessional rates of interest, low margins for technical entrepreneurs, supply of scarce raw materials through special quotas and import licenses, training facilities, subsidised power tariffs and exemption of electricity duties, machinery on hire purchase basis, assistance for marketing, incentives for setting up units in backward areas, differential central excise levies for the small-scale sector, creation of institutions to help small enterprises, and training in entrepreneurship development.

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The Central and State Governments made huge investments in providing such infrastructure facilities like power generation and distribution, roads, communications, creation of port facilities, etc. Various State Governments made developed plots of land or industrial estates available to entrepreneurs.

To cater to the growing needs of industries during the last fifty years, the Government set up several large number of Industrial Training Institutes all over the country. It also set up Indian Institute of Technology, Management Institutes and Engineering Colleges to train persons with higher management and technical skills.

The Government of India set up 48 national laboratories to undertake applied research in chemistry, physics, electronics, botany, etc.

The Central Government and the State Government followed a policy of encouraging industries in backward areas. The Central Government selected a few backward districts and offered 25% capital subsidy for industries set up in these areas. Various State Governments also offered similar capital incentives, exemption from sales tax levy, subsidies on power rates, cheap developed land, sales tax loans and other facilities.

In the Industrial Policy Resolutions of 1948 and 1950, a very important role was assigned to the public sector, power, telephones, communications,

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atomic energy, defence industries and some areas were reserved for the public sector. Industries like life insurance, civil aviation, banks were nationalised and were included in the public sector.

The policy of the British Government was against encouraging industrial development in India.

There were many hurdles placed in the way of growth of Indian industry. In 1951, the Industrial (Development and Regulation) Act was passed by the Parliament. The main provisions of the Act were that all existing undertakings at the commencement of the Act, except those owned by the Central Government were required to register with the designated authority. No one except the Central Government would be permitted to set up any new undertaking "except under and in accordance with a license issued by the Central Government. Such a license or permission prescribed a variety of conditions, such as, location, minimum standards in respect of size and techniques to be used. Such licences were also required in cases of 'substantial expansion'. The industries to be brought under regulation were divided in to two parts, Part I and Part II in accordance with the schedule to the Act. In regard to the industries listed in Part I of the schedule, the Central Government could issue necessary directions in respect of quality, production prices, etc., and could transfer industries specified in one part to another. The IDR Act resulted in more or

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less complete control by the bureaucracy on the industrial development of the country.

A new industrial policy was announced in 1956. The policy divided industries into three categories. All basic and strategic industries were to be set up in the public sector. In category B of industries, private enterprise could participate along with public enterprises and was called the joint sector. All remaining industries falling in category C were left to be developed by the private sector.

The Industrial Policy of 1956, for the first time, emphasised the role of small industries in providing employment, equitable distribution of national income and the effective mobilisation of resources.

In April 1964, the Government of India appointed a Monopolies Inquiry Commission. The Commission drafted a law to control monopolies and recommended the setting up of a permanent Monopolies and Restrictive Trade Practices Commission. An Act was passed and a Monopolies Commission was appointed by the Government in 1969.

In July 1969, an Industrial Licensing Policy Committee was appointed to examine the shortcomings in licensing policy. Following the report of the Industrial Licensing Policy Inquiry Committee, a number of new restrictions were put

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on the large industrial houses in the industrial licensing policy announced in February 1970.

The Foreign Exchange and Regulation Act was amended in 1973. This brought a great change in foreign investment policy of the Government of India. Foreign firms were not allowed more than 40% of equity. FERA companies were subject to many restrictions, and were not allowed to participate in certain industries. They were also not allowed to expand and take up production of new products.

The Policy Statement of 1973 drew up a list of Appendix 1 industries to be started by large business houses so that the competitive effort of small industries was not affected. A Secretariat for Industrial Assistance (SIA) was set up in November 1973, and all industrial licenses, capital goods, import licenses, terms of foreign collaboration were brought under the SIA.

The thrust of the Industrial Policy Statement of December 1977 was on effective promotion of Cottage and Small Industries widely dispersed in rural areas and small towns. The focal point of development of small-scale industries was taken away from the big cities to districts. The concept of District Industries Centres was introduced.

Within the SSI sector, a new concept of tiny sector was introduced. This tiny sector was to be given special attention and extended help.

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The policy statement considerably expanded the list of reserved items for exclusive manufacture in the small-scale sector. This concept recommended by the Karve Committee was introduced in 1967 with 47 products. The list of such reserved items was 504 till 1977. The new policy expanded this list to 807.

After 1980, an era of liberalisation started. The trend was to dilute the strict licensing system and allow more freedom. The steps taken included: re-endorsement of licenses (1984), automatic re-endorsement of licensed capacities (1988), broad banding and selective delicensing (1985-86) extended to 25 industries, exemption from licensing for all new units and those having an investment of Rs. 2.5 crores in fixed assets, investment of foreign equity upto 40% freely and removal of locational restrictions and investment ceiling for small industries (1990).

The enactment of the IDR Act acted as a great deterrent to the growth of industries in the country. The bureaucracy acquired unprecedented powers over industrial activities. A number of other Acts acted as obstacles and retarded the industrial development of the country. Despite industrial licensing, an entrepreneur had to obtain clearance form many agencies. Thus, when the Government of India announced the new economic policy in July 1991, Indian industries were not competitive in the world market. Our industries

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were suddenly required to face international competition. Many of these industries allowed their foreign collaborators to take over. Those who remain in the field are trying to downsize. It is becoming increasingly difficult not only to face competition in the world, but also competition at home with the products of multinationals.

The broad features of the economic reforms initiated in early 1990s are as follows:

(i) The Government opened major sectors of the economy to the private sector.

(ii) Foreign investment was invited in all these sectors.

(iii) All restrictions on the entry of the private sector into the field of infrastructure and strategic industries were removed.

(iv) There is more freedom for financial institutions

(v) By the cuts in Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR) over a period of years, more funds have been made available by the RBI to the banks. Banks can also approach capital markets for raising funds.

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(vi) Private capital and foreign investment in such areas as construction of roads, ports, airports, telephone services, etc.

(vii) The Government wants to reduce its investment in the public sector undertakings.

(viii) Import restrictions have been reduced.

(ix) Subsidies are being cut, tax rates are being reduced and the entire fiscal system is being streamlined.

(x) The Controller of Capital Issues stands abolished.

The post-reform growth has been at least marginally better than the average growth rate achieved during the pre-reform period.

The wide fluctuations in our national income growth have been curbed in the nineties.

The industrial sector has been very badly affected during the last few years and the slowdown and loss of production and employment in this sector has, in turn, led to lower demand for consumer goods which has resulted in a general levelling down of all production activities. The implementation of the new economic policy has hit this sector hardest.

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The inflation rate as estimated by the consumer price index for industrial workers remained below 4% till July 2001 and rose to 5.2% in December 2001. The liberalisation policy can certainly take some credit for keeping prices under control.

It has been observed that the strength of India's external sector management has turned out to be among the most noteworthy successes of the structural reforms undertaken since 1991.

The Government was interested in augmenting the country's foreign 1991 does not reoccur. On 31st March 2005, these resources touched 138 billion dollars.

In the global context too, India's indebtedness position has improved over the years. In terms of absolute levels of debt, it ranked as the third largest debtor country after Mexico and Brazil in 1991. Now, it is the tenth largest debtor country. For the first time the World Bank has classified India as a less indebted country.

Indian exports have remained stagnant at around 5% of the GNP for almost a decade. If exports remain stagnant, the overall economic growth of the country is likely to be affected.

Diversification and the broad base of Indian manufacture are not reflected in our exports. This means that only a few manufactured products enter the export market. This is one reason why exports

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are not growing. The new economic policy has not succeeded in promoting exports as a sustainable basis and improving our international competitiveness.

The rupee depreciated significantly even after its devaluation in 1991. In the last ten years, the rupee went down from Rs. 18-20 per US$ to Rs 43-44 per US$ now.

Foreign collaborators first increased their shares from 40% to 51%, and then took over the entire management of the company. This trend was accepted by some companies like TVS motor company, which bought out the share of its multinational partner Suzuki.

In recent years, there is a substantial amount of growth in Mergers and Acquisitions activities in India. It implies that takeovers or acquisitions are the dominant feature Mergers and Acquisitions activity in India. It appears that foreign companies are not interested in mergers because mergers generally take place between equals while acquisitions involve buying existing firms. They are, therefore, interested in acquiring Indian companies and eliminating Indian management.

Another method of takeover that foreign companies are employing is to convert their joint ventures in India with a local partner into Wholly Owned Subsidiary (WOS). During the last decade the trend has been very much in evidence.

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In the absence of a generalised improvement of economic activity and the growing competition from cheap imported goods and goods produced locally by MNCs in India, the Indian entrepreneurship has, as a consequence, gone into a state of stupor and indecisiveness. More and more Indian entrepreneurs seem to be feeling that it is difficult to survive against the multinationals whose resources cannot be matched.

Thus, the new economic policy seems to be resulting in the closure or disappearance of many Indian companies, especially those engaged in consumer goods industry. Some may say this is survival of the fittest, and consumers now get a better product. But in the process, India seems to be losing the indigenous breed of entrepreneurs and innovators who once played an important role in developing Indian industry.

It appears that the days of importing technology and collaborating with a foreign company are over. Since foreign companies can export their goods freely to India, manufacturing in India is probably a second consideration for such a company. Nearness to the market and volume of sales are important considerations, and on that count, if a foreign company decides to undertake manufacturing in India, the company prefers to go it alone with 100% foreign equity without joining hands with any Indian manufacturer.

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Coming to the changed form of economic and labour laws as a part of the overall liberalisation policy, and their implications on employment the example of China, the champion of globalisation induced economic growth, is noteworthy. The Central Labour Law was applicable to the whole territory of the People's Republic of China, and there were no areas or zones or industries or enterprises that were exempted from these laws. The implementation of the law can be circumvented by foul means but the very presence of such umbrella statute can be beneficial to the workers.

The establishment of a venture in China is not as simple an affair as per general perception. There are detailed regulations laid down to regulate employment plans, recruitment, the signing of labour contracts with individual employees, the signing of collective contracts with Trade Unions in the enterprise, conditions for retrenchment, responsibility to provide basic living allowance, etc. to the laid off and retrenched, etc. We can refer to the Shanghai Municipal Regulations of Labour and Personnel Management in Foreign Invested Enterprises. They make, *inter alia,* the following provisions:

(i) The foreign invested enterprises must set up and institutionalise relevant regulations according to the law in order to secure labour rights for and labour responsibilities of its staff or workers.

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(ii) Lists methods or procedures for recruitment of staff

(iii) The foreign invested enterprise can determine its own organisation structure and personnel system in accordance with the need of production and business operation.

(iv) The foreign invested enterprise must conclude the labour contract with its recruited employees according to the law, and on the basis of equality, self-willingness, coordination and consistency. The labour contract must be in accordance with relevant laws and regulations of the People's Republic of China.

(v) The labour contract, when concluded, is a legal document and binding upon both parties.

(vi) Lays down the conditions under which an employee can be terminated.

Labour disputes between the foreign invested enterprise and its employees may be settled through consultations between the concerned parties. Should the consultation fail, the concerned parties may apply to the labour dispute mediation

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committee of the enterprise for mediation and should this mediation fail, the parties concerned may approach labour dispute arbitration committee for arbitration. Either party that is not satisfied with the order of the arbitration may bring the case to the people's court of the district or country where the enterprise is located.

According to the National Labour Law, the Chairman of the Mediation Committee in an enterprise is a representative of the Trade Union. The Arbitrator is a representative official of the Government. In general 10% of the disputes fail to get resolved at the levels of the Mediation Committee and arbitration, and go to the People's Court.

Enterprises of any kind have to fulfil certain stipulated conditions before firing or laying off or retrenching. It is clear that the law does not contemplate or permit "hire and fire". With the transition to the Socialist Market economy, the concept of jobs has changed. The basic changes that come about where jobs are strictly contractual, and the lay-off or retrenchment has resulted in increased disputes.

The Trade Union Law in China makes no mention of strikes. It neither mentions them as legal instrument in the hands of the workers, nor prohibits them. There is only one trade union in China, the ACFTU. Globalisation, and the

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consequent downsizing of its enterprises have also affected Chinese economy.

Chinese Government offers the following Social Security Schemes:

1. Old Age Pension Scheme
2. Medical Insurance
3. Workers Injury Scheme
4. Maternity Benefits
5. Unemployment Insurance

The leaders of the Trade Unions have themselves identified the main problems they are encountering as:

1. Conflicts have increased and become increasingly complicated because of the strategic reform of state owned enterprises and the burgeoning development of non-public sectors.

2. Rampant violation of the Labour Law by preventing the workers from joining Trade Unions.

3. Illegally hiring workers without signing contracts.

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4. Forcing workers to work extreme hours.

5. Skimping on salaries.

6. Non-payment of wages on dates stipulated by law.

7. Refusal by some enterprises to buy their workers insurances for unemployment, industrial accidents and endowments.

8. Failure by enterprises to offer working protection facilities.

9. Frisking of women workers at factories.

10. Inadequate immunisation.

It will be erroneous to think that flexible labour laws are the main reason for China's progress. I would also like to place on record arguments and observations that have been put forward to explain why China has made spectacular progress in globalisation and the post-globalisation scenario, as compared to the tardy progress that India has made.

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1. China followed a policy of market economy since 1978. India introduced the new economic policy only in July 1991.

2. China did not follow the standard policy prescriptions laid down by the World Bank and IMF for developing economies blindly.

3. China followed a policy of competition rather than ownership for higher productivity.

4. China did not give too much importance to balanced regional development.

5. China gave a lot of importance to provide excellent infrastructure of international standard in Shanghai, Shenzen and Guangdong provinces and attracted foreign enterprises over there.

6. Overseas, Chinese played a very important role in attracting foreign investments.

7. China followed proper sequence of reforms. China, instead of initiating reforms with foreign trade and exchange rate liberalisation, started with agriculture. Then, China introduced export orientation for Township and Village enterprises. Then, special economic zones were opened which offered foreign investors excellent infrastructure, special fiscal and financial

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incentives and flexible labour relations by their innovative contract system.

8. A new policy was first tried in small region, and after gaining experience of such a policy and the difficulties encountered, this policy with modifications was introduced in a wider area.

9. The administration in China is completely decentralised. Local municipal corporations can also take a decision regarding foreign exchange up to a limit. The laws are simple.

10. China allowed its companies to grow. Chinese companies are much bigger in size than Indian companies. In India because of our different ideas of monopolies, industrial licensing, etc., Indian companies were never allowed to grow in the license permit system and even the largest companies in India are pigmies as compared to global players. As a result, they cannot effectively compete.

It is not merely the flexible labour laws, but because of all these factors that foreign investment is attracted to China and China has been able to achieve phenomenal progress.

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During the first few years of economic reform in India, there was a general growth in all sectors of the economy. But since 1996-97, the industrial growth has slowed down, and that has affected almost all sectors of industries. Year 2003-04 proved to be a turn-around for this trend witnessing sustained industrial growth, which is likely to improve in 2004-05. There are some signs of recover in the intermediate and consumer durable goods industry, the performance of the capital goods sector has, though, not been encouraging.

The Government policy during 1990s aimed at attracting foreign investment of all varieties. But in this process, and in the wave of globalisation and the pressures from international bodies like IMF, etc. it seems that some of the vital sectors of the economy did not receive adequate attention. The list of such sectors is long - spanning from plantation to small-scale and medium scale industrial units. Agriculture has also taken a backseat in overall development process. During the decade after economic liberalisation, most of the state governments in their budget have reduced the share of investment and allocation to the rural sector. Since investment is made in agriculture and rural areas, agricultural production has been adversely affected. Agriculture which is still the mainstay of the Indian economy and which provides employment to almost 60% of our population does not appear to have got the thrust it deserves.

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Agriculture and allied activities still contribute about 25% of GDP and increase of even 5% in its output would make an incremental contribution of 1.3% to real growth of GDP.

It will be interesting to note that while food grain production is stagnating, procurement operations have increased. While food procurement is rising, PDS sales are falling. Supply demand mismatch is leading to building up of huge food stocks. At current levels of annual PDS sales, food stocks can as well last for next four years.

With the entry in to the WTO, it is doubtful whether there will be any encouragement to ancillary industries.

The SSI units, which are producing independent products of their own, are in deep difficulties because of the large-scale imports from other countries.

The following are some trends in employment, unemployment rates, and industrial distribution of total workers:

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1. Overall employment is estimated to have grown at around 1.01% per annum in 1990s compared to 1.55% per annum in 1980s.

2. The number of unemployed in 1997 is more than the number employed in organised sector.

3. About 7% to 8% of the workforce in the organised sector is protected while 92 to 93% is unprotected, unorganised and vulnerable.

4. There is a trend in growth of causal labour in the total workforce during all these years. The proportion of self-employed has come down from 58.9%in 1977-78 to 52.9% in 1999-2000. But the number of casual workers has gone up substantially from 27.2% to 33.2%.

5. Employment is not growing in the organised sector.

6. Forty four percent of the labour force in 1999-2000 was illiterate. Only 5% of the workforce had necessary vocational skills.

7. It is not enough to cerate employment opportunities. The quality of jobs is equally important.

Because of global competition most of the companies want to reduce costs and be competitive. The first casualty is the number of

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workers employed, and since 1992 many Indian companies have resorted to downsizing by introducing Voluntary Retirement Schemes.

The task force has recommended the following recommendations:

1. Accelerating the rate of growth of GDP, with particular emphasis on sectors likely to ensure the spread of income to the low-income segments of the labour force.

2. Pursuing appropriate sectoral policies in individual sectors, which are particularly important for employment generation. These sector level policies must be broadly consistent with the overall objective of accelerating GDP growth.

3. Implementing focussed special programmes for creating additional employment and enhancing income generation from existing activities aimed at helping vulnerable groups that may not be sufficiently benefited by the more general growth promoting policies.

4. Pursuing suitable policies for education and skill development, which would upgrade the quality of the labour force and make it capable of supporting a growth process which generates high quality jobs.

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5. Ensuring that the policy and legal environment governing the labour market encourages labour absorption, especially in the organised sector.

The report of the Task Force has evoked considerable criticism. A review of industrial relations in the pre-reform decade reveals that as against 402.1 million days lost during that decade, the number of man days lost declined to 210 million during 1991 to 2000, i.e. in the post reforms period. But more man-days have been lost in lockouts than in strikes.

A large number of workers have lost their jobs as a result of VRS, retrenchment and closures both in the organised and unorganised sector. The exact number is not available. According to our information, no data on this subject has been compiled by any state government.

The following observations are noteworthy with regard to the change in industrial relations scenario:

1. It is increasingly noticed that trade unions do not normally give a call for strike because they are afraid that a strike may lead to closure of the unit.

2. Service sector workers feel they have become outsiders and are becoming

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increasingly disinterested in trade union activities.

3. There is a trend to resolve major disputes through negotiations at bipartite level. The nature of disputes or demands is changing.

4. The attitude of Government, especially of the Central Government, towards workers and employers seems to have undergone a change. Now, permissions for closure or retrenchment are more easily granted.

5. The Conciliation Machinery is more eager to consider problems of employers and today consider issues like increase in productivity, cost reduction, financial difficulties of the employer, competition, market fluctuations, etc.

6. The industrial relations machinery is not seriously pursuing recovery proceedings against employers who could not pay heavy dues of workers, if the financial position of the employer is very bad.

7. The labour adjudication machinery is more willing to entertain concerns of industry.

Globalisation is affecting collective bargaining. Earlier in the public sector, the emphasis was on greater parity across sectors and reducing the gap between the lowest and the highest paid

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employees. Now the gap is widening. Over 100 out of 240 public sector companies have not had any pay revision since 1992.

The incidence of industrial conflict seems to be on the decline. Most long drawn strikes in the private sector do not seem to have borne results from the workers' point of view. Even resistance to privatisation from trade unions is not deterring the government any longer.

Since 1991, a number of reforms have been introduced in the financial sector and a good number of structural and organisational changes have taken place at frequent intervals. They expose the inadequacy of the present institutional and regulatory systems.

On 1st January, the World Trade Organisation came into existence. India was a signatory to the agreement, and as a result we became a member of the WTO. The results of this are felt far and wide on the Indian industry. In some industries like chemicals, plantation, household goods, toys, etc. products have been imported in a big way and are out-pricing Indian products. More and more of such goods are likely to come into India and if Indian manufacturers are not able to compete with them on price and quality, they will have to pull their shutters down. This is a real threat to Indian industry, and therefore to employment.

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Many countries are dumping their goods in Indian markets at a cheap price. There is urgent need to revamp the set-up responsible for this purpose, including augmentation of manpower and capabilities to enable prompt action for the benefit of domestic industries.

In the new regime, we have to encourage foreign investment and give them treatment on par with local investors. A large number of multinationals have entered the field of low technology; high volume products and this will close an area of opportunity to small entrepreneurs.

Since imports are freely available, one may not be interested in manufacturing such products inside the country. Thus, one avenue for SSI units will be permanently closed.

The migration of workers across international boundaries is one of the most striking aspects of the globalisation of the world economy, with a major impact on well over 100 countries.

Increased internationalisation of production, trade and finance is expected to exert additional pressure in the countries of origin and destinations for larger flow of skilled or unskilled labour in the immediate decades to come.

In such a context, it is imperative that attempts are made to examine the implications of the contemporary migration flows so as to evolve a

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more purposeful migration policy framework aimed at the maximisation of benefits from migration in the wider context of economic development.

Since independence, India has faced two kinds of labour migration:

1. Migration of technically and professionally qualified workforce to industrialised economies, and

2. Migration of skilled workers and low-end white-collar workers to the Middle-East countries.

The basic characteristics of the labour-flows from India to the industrialised countries are:

1. Such outflows are made up almost entirely of permanent migration.

2. A large proportion of these migrants are persons with professional expertise, technical qualifications or other skills.

3. The destinations have been the United States, Canada, and the United Kingdom, and in recent times some countries in Europe.

The oil prices of 1973-74 and 1979 saw an enormous growth in the demand for foreign labour

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in the oil exporting states of the Gulf. This sudden spurt in the demand for labour was met by drawing labour from labour surplus economies like India.

The oil glut in the early 1980s resulted in a reduction of development expenditure in most Middle East States. This had adverse impact on the demand for labour.

There has been a clear shift in the pattern of labour demand in the Middle East – a shift away from several categories of unskilled and semi-skilled labour towards service, operations, and maintenance workers requiring high skills – thus, generating new opportunities for labour exporting countries.

Apart form providing a 'safety valve' for the massive unemployment problems at home, migration to the Middle East would continue to be an important source of foreign exchange.

The employment of Indian workers helps to earn foreign exchange and leads to augmentation of the foreign exchange reserves of the country.

The closure of industrial units and bankruptcies are a normal feature in the developed economies all over the world. Developed economies with their well-established social security systems, easily take care of workers displaced by such closures. Developing economies, with their limited investible resources and relatively limited

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alternative employment opportunities, however, cannot, easily afford their productive assets and labour force turning non-operational. Industrial sickness and its resultant consequences have, therefore, to be handled carefully to see that its adverse impacts fall least on workers and society.

The major issue that emerges is how the industrial units, which are sick, or closed or under liquidation, need to be dealt within India, particularly the displaced workers and locked assets of these units.

There is evidence to indicate that both real wages and productivity of labour have registered an increase during 1990s. This growth is visible in all segments of the workforce, even among casual workers.

In spite of impressive increase in labour productivity in 1990s, India's labour productivity is lowest amongst 47 countries covered by the World Competitive Year Book 2000.

The Economic Survey of 2001-02 claims that poverty reached an all time low of 26% in 1999-2000. According to the latest estimates in the Economic Survey, the number of poor people in the country stands at 260 million.

There is some evidence to show that growth has favoured urban India, the organised sector, the richer states and the property owners as against

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rural India, the unorganised sector, the poorer states and the wage earners. The period of growth during 1980s and 1990s has also been the period of growing inequalities.

The capital market is an important indicator of the economy. The present state of the market only indicates the uncertainty and loss of confidence of the entrepreneurs about the future prospects of Indian economy.

Though a number of changes have taken place in the Indian economy, bureaucratic systems and procedures seem to retain their role.

India was the second largest economic power, next only to China, in the entire Asia-Pacific region at the time of independence. The position continued till the end of 1970s. Thereafter, first Japan, and then other tigers in the region have overtaken India.

India's share in both FDI and foreign trade are well below 1% of the world's total. In this sense, India is a marginal player in the globalisation process. But India is reputed to have a middle class whose size is equal to that of the whole of Europe.

South Asian countries, including India, continue to fare badly in terms of productivity and competitiveness and because of the underdevelopment of infrastructure. The

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arguments for liberalisation and privatisation should be seen in this context. The Government can probably release its energies from routine commercial activities and focus more on education, health, transport and telecommunications and other key concerns of infrastructure.

The events of September 11, 2001 and its aftermath have resulted in a sharp deterioration in confidence across the globe, which has contributed to a downward revision in the IMF's projection of world growth 2.4% from 3.5% a few months ago.

The growth of G7 countries is expected to slide down. Whereas China's industrial production-growth has been forging ahead, India's growth-rate of manufacturing is stagnating.

The IMF, in its World Economic Outlook has said that India, Russia and China are reasonably insulated from world turmoil as they are relying more on their huge domestic demand.

As a result of the new economic policy, inflation is under control. We have been able to accumulate enough foreign exchange reserves. Indian companies have access to global financial markets. India's external debt position has improved. Some industries like Information Technology have made impressive progress, taking advantage of global economic integration. Foreign investment is coming to India both in portfolio investment as

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well as in industrial projects. Indian consumers have increased access to all types and a large variety of international brands of goods in the market.

One has to accept the fact that we have travelled quite some distance along the road to full-scale globalisation. It is technology that has made globalisation possible. It has generated new hopes and given rise to new dangers and temptations. Its impact can already be seen in many fields of human activity. Old mindsets may prove a handicap in responding to the new situations and factors that have emerged.

Industry is not an end in itself. It is a social activity undertaken to meet the needs of society. All economic activity is the result of independent interests, and cooperation among the various factors that together constitute the cycle of economic activity. Globalisation has not altered this fundamental. It has underlined its importance for communities that choose to enter the arena of competition.

In a regime of competition, this means that every nation has to acquire and retain sufficient competitiveness to be able to survive and prosper in the world markets. This competitiveness cannot be acquired without harmonious relations or at least peaceful relations in industry. The first requisite for the employers and employees today, therefore, is to develop a mindset that looks upon

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each other as partners, to develop a work culture that new technology and the context of globalisation demand.

It is an overstatement to say that labour laws are the only cause of our unsatisfactory economic development. There are other factors that affect the efficiency of industry like managerial skills, integrity and honesty, efficient and reliable infrastructure, etc. If there are many causes, and one deals only with one, and ignores all other, one cannot overcome the disease or hope for cure. All these reasons make it necessary for us to place labour laws in perspective, as a part of what we look at.

This does not mean that we do not believe in the need for important changes both in laws and in attitudes. It has to be conceded that the worker has a stake in the viability and growth of the undertaking, and an attendant responsibility as well as right. Wages have to be looked upon as incomes that are earned through hard work, and not merely monetary payment but also a balance of responsibilities and rights.

The individual worker' attitude to work has to include,

(a) Pride in maximising his own productivity to repay his debt to society, and

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(b) Pride in his commitment to excellence, as reflected in the quality of work.

It was observed many workers in private and public undertakings work only 4 to 5 hours a day. This is not only true for Government or administrative offices, but true for factory workers as well.

The prevailing situation in the country is that should cause deep concern and distress. We must be concerned at the moral culpability of "short charging" or working less and accepting the same payment. The loss in time and output caused by the underutilisation of resources, and the atmosphere that we create with the resultant fall in efficiency even during working hours, further compounds loss of output.

Our reputation abroad shows that our workers are capable of creating and maintaining highest levels of work culture. The question is why is it that we do not create and maintain such high standards of work culture in our own country. This matter deserves concern and reflection. The author feels that each of the partners involved should seriously reflect on how he/she can contribute to the transformation our work culture.

We must make a few observations on the contribution that managements can make to improve our work culture. Industrial relations relate to relations between management and

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workforce employed in the undertaking. In the ultimate analysis industrial relations are a branch of human relations. Human beings like to be treated as human beings. It is imperative then, that old perceptions and mindsets about the workforce have therefore to change, and new methods have to be identified and pursued to elicit cooperation and respect.

In the ultimate analysis, the level of work culture in any undertaking will depend on the level of realisation of identity, of interest, or in the least, the sense of belonging, and the sense of independence. The systematic arrangements that will help us to maintain a high level of work culture include:

(i) Fair wages,

(ii) Equitable profit sharing,

(iii) Effective organs of participatory management at all levels, and

(iv) Opportunities to interact.

There seemed to be a considerable difference in the application and efficiency of workers who were on probation, whose status was temporary and the attitude to work that one could see in those who had been confirmed as permanent employees.

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It must be accepted that one needs to find measures to correct this discrepancy.

Over manned organisations are also a cause of poor work culture. It lowers normal levels of work efficiency and the work hours per employee.

The work environment also plays a role in promoting good work culture good work culture. A vibrant work environment will result in greater output.

We have the maximum number of holidays. A study reveals that three out of every seven days are holidays for an average Government servant. All commercial and industrial activities are connected with various departments of the Government and if the Government offices are closed, many economic activities in the country also come to a standstill. The State Governments and the Central Government should have a uniform policy on holidays, only 3 national holidays be gazetted, viz. Independence Day, Republic Day and Gandhi Jayanti. Two more days may be added to be determined by each state according to its own tradition and apart from these each person must be allowed to avail 10 restricted holidays in a year. Government holidays should be delinked from holidays under the Negotiable Instruments Act, In case of the option of a five-day week, if a holiday occurs during the week, Saturday should be a working day, and the movement of quality circles should be encouraged. This will enable

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workers to take interest in their work and contribute to the improvement in the overall work culture in the organisation.

The attitude of hours of work should not be rigid. The total number of hours per day should not be more than nine, and hours of work per week should not be more than 48. But within these limits, there may be flexibility, and compensation for overtime.

Most of those who demand the right to hire and fire also want to bring about a fundamental change in the nature of perception of employment. They want all employment to be on the basis of contracts for stipulated periods. This introduces a basic or fundamental change in the current system in vogue in most kind of employments. While we understand that non-permanent jobs or temporary assignments can be on contract for specified periods, we are accustomed to look upon employment against permanent jobs as permanent service. Attempt to change the basis of tenure in all jobs (permanent as well as non-permanent) to contractual, and for stipulated periods, involves a basic change in attitudes and notions. If transforming the basis of all employment is a social necessity because it has become an economic necessity for industrial or commercial enterprises, then, it is equally necessary to create social acceptability for the change, and the social institutions that can take care of the consequences.

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A fundamental change of this kind has to be preceded by,

1. The evolution of a socially accepted consensus on the new perception of jobs.

2. The evolution of a system of constant upgradation of employability through training in a wide spectrum of multiple skills.

3. The setting up of a system of social security that includes unemployment insurance and provisions for medical facilities.

4. The institution of a mandatory system of two contracts

   (i) an individual contract, and

   (ii) a collective contract with the workers' union.

There are weighty considerations that should temper the demand for an immediate switchover to the contract system and to unrestricted rights of hire and fire.

Most developed countries where the majority of jobs are contracts have elaborate and effective systems of social security. China, which can be cited as an example, too has requirements at least

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for two or three years of transition or unemployment. In India, we do not have such legal provisions or practices. We are convinced that social justice as well as the benefit of the economic returns that accrue from a moderately assured workforce, demand the establishment of a socially acceptable link between transition to a contract based employment system and the establishment of a viable social security system to which the entire vulnerable workforce has access.

The mindset that was rooted in the faith in the power and resilience of private initiative and industry to take over the role of State in economic matters was shaken by September 11, 2001 and the crash of Enron have altered the scenario in many ways. The centrality of the state in ensuring security – security against forces of disintegration and terrorism, and social security – has had to be acknowledged again.

The danger of such social national hazards is reflected in the State of the Union address that President Bush delivered to the American Congress on the 29th of January 2002. It may be useful to quote what the President said on social security:

> "Americans who have lost their jobs need our help, and I support extending unemployment benefits and direct assistance for health care coverage. My economic security plan can be summed up in one word: jobs. Good jobs

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> must be the aim of welfare reform. The goal is to reduce depending on government. Economic security can vanish in an instant. I ask Congress to give uninsured workers credits to help by health-coverage. A good job should lead to security in retirement. Employees who have worked hard and served all their lives should not have to risk losing everything when the company fail. Retirement security also depends upon keeping the commitments of social security."

We need not point out that these are as necessary in our country as in America. Those who look to America, as a model should see the need for policies oriented to creations of jobs and the provision of basic social security.

The new mindset that the new context calls for must be reflected in all attitudes and activities in industrial relations or employer-employee relationships. All efforts must therefore be made to promote bilateralism based on mutual interests and universally accepted fundamental rights and norms. The legal system should therefore promote bilateralism. Where differences persist the law must enable contending views to be settled through mediation and arbitration, including compulsory arbitration where the disputes may lead to disruption of social life affecting public health, sanitation, drinking water supply, medical facilities and transport, and cause suffering to

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large sections of people who are unrelated to the disputes.

Process of adjudication must be quick, expeditious and inexpensive. They should not involve delays that cripple worker. Workers should be encouraged to organise themselves with the awareness that struggles on the basis of extraneous issues may divide and weaken them.

The ILO declaration on Fundamental Principles and Rights at Work, adopted by the International Labour Conference in June 1998, declares *inter alia* that all Member States whether they have ratified the relevant conventions or not have an obligation to respect, to promote and to realise the principles concerning the fundamental rights which are the subject of those conventions. These principles include:

1) Freedom of association and the effective recognition of the right to collective bargaining,

2) Elimination of all forms of forced or compulsory labour,

3) Effective abolition of child labour, and

4) Elimination of discrimination in respect of employment and occupation.

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The primary goal of the ILO today is to promote opportunities for women and men to obtain decent and productive work in conditions of freedom, equity, security and human dignity. The goal is not just the creation of jobs, but the creation of jobs, of acceptable quality.

This convention was ratified by India at a time when unemployment levels are high. One therefore has to presume, that the Government is now committed to pursue an active policy designed to promote full, productive and freely chosen employment.

From the commitments of the Government of India, it can be deduced that the following rights of workers have been recognised as inaliable, and must therefore, accrue to every worker under any system of labour laws and labour policy. These are:

(1) Right to work of one's choice

(2) Right against discrimination

(3) Prohibition of child labour

(4) Just and humane conditions of work

(5) Right to social security

(6) Protection of wages including right to guaranteed wages

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(7) Right to redress of grievances

(8) Right to organised and form trade unions

(9) Right to collective bargaining, and

(10) Right to participation in management.

Ever since the country accepted regime of economic reforms by the Narsimha Rao Government in the early 1990s, the need for reforms in labour laws has been increasingly felt. Industry has been demanding necessary changes in labour laws to tackle the growing challenges from competitors abroad. The country's labour laws do not possess the flexibility needed to operate successfully in the right direction especially in the present competitive scenario. In fact, Public Sector Undertakings (PSUs) do not have the freedom to retrench labour or close down a particular section in the company in response to changing market conditions without the permission of the Government. Not only this, labour also specify the service rules that govern employment and which cannot be changed. This makes it difficult to deploy workers to different activities whenever required. The liberalized market-oriented set up of today needs industry to be flexible enough to compete in new and competitive environment.

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Reforms in labour laws occupy a key role in enhancing competitiveness of domestic industries. While reforms in various sectors like taxation, financial market, infrastructure have moved ahead rapidly, labour reforms have not progressed with the desired pace due to various reasons. Ignoring the long terms benefits of a flexible labour structure, successive governments have failed to pursue labour law reforms. Those who are opposed to the reforms in the labour policy need to realize that existing labour laws have become outdated. Excessive job security has affected workers' productivity as well as efficiency. It has impaired discipline in every critical sector of the workforce. Trade unionism has become bane of several industries. Cast-iron guarantees for a lifetime job security have led to irresponsible behaviour on part of workers and trade union leaders. However, the proposed changes in the labour laws by Second national Labour Commission make sense in the altered economic situation following globalisation and liberalization. On one hand, the labour reforms would extend the labour flexibility that Indian industry urgently needs, and on the other hand, pave way for increased Foreign Direct Investment.

It is said that the labour laws should be amended to bring them in line with the practices in other nations. The existing laws only apply to the organized sector that constitutes only 8% of the total labour force in the country. It is noticeable that the remaining 92% of the labour population

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derives no benefit from these laws. The changes in the existing labour laws must be welcomed, but stifling labour laws would jeopardize the interest of the working class. Also, labour reforms would be realistic and meaningful if the interest of both the organized and the unorganised labours is taken care of. This in mind, the Union Government has set up the Second Labour Commission. It suggested means for the rationalization of the existing laws relating to labour in the organized sector and umbrella legislation to ensure protection to workers in the unorganised sector.

India is a founder member of the International Labour Organisation. The constitution of the ILO aims at universal and lasting peace based on social justice. The ILO is considered to be one of the specialized agencies under the United Nations. The organisation, however, has a unique character because of its tripartite composition. At every level in the ILO, governments are associated with social partners, i.e. workers and employers.

The Government of India holds a permanent seat in the Governing Body of the ILO. India has been regularly attending the sessions of the International Labour Conference since its establishment. The most important activity of the ILC is to set international standards in the form of ILO conventions and recommendations. The ILO conventions are open to ratifications by Member States, whereas recommendations are in the form of guidelines to member states for incorporating

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them in policies and programmes. India has ratified 38 ILO conventions so far. India has so far ratified three out of eight ILO core conventions. The ratified conventions are No. 29 concerning forced labour, No. 100 concerning equal remuneration and No. 111 concerning discrimination in employment and occupation. We are also in the process of completing ratification formalities in respect of convention no. 105 concerning abolition of forced labour. Active involvement of the Government delegation in coordination with other developing countries resulted in the ILC unanimously adopting the ILO convention no. 182, as well as the recommendation no. 190 concerning prohibition and immediate action for elimination of worst forms of child labour. Tripartite consultations with a view to ratify the above convention are in progress. However, convention 138 concerning minimum age for admission to employment and work could not be ratified by India so far because there was no omnibus provision in our laws and regulations fixing minimum age for admission to employment and work. The Government is considering enacting a central legislation fixing minimum age for entry for employment and work, which will not be less than 14 years of age. Considering the size of the unorganised and informal sector in the country, there will be initial difficulties in enforcing and achieving full compliance with the proposed legislation. Ratification of the minimum age convention would be considered when it is realised that we have achieved satisfactory compliance of

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the proposed legislation. The guarantees provided for workers under ILO Convention 87 concerning freedom of association and protection of right to organise and Convention 98 concerning right to organise and collective bargaining are available by and large to all workers in the country through Constitutional provisions, laws and regulations. However, it has not been possible for India to ratify these two conventions because of technical problem relating to trade union rights of the government employees.

It is surely a startling and at the same time worrisome fact that India, though attracting nearly one-fourth of the global portfolio investment by Foreign Institutional Investors (FIIs), it attracts merely 3% of the global FDI.

FII inflows to India in the last quarter previous fiscal and first quarter of current fiscal have exceeded US$ 8 billion. FDI inflows have been less than one-third of that amount. Very often arguments are made that this is not so good. Instead of having so much portfolio investment, Indian should have been attracting more FDI. However, contrary to this common belief, research suggests that attracting FII investment is a sign of good health of the economy, and attracting more FDI is a sigh of bad health of the economy. In contrast to the commonly held unfavourable view of FII flows, evidenced suggests that countries with good institutions and markets attract more

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FII, while countries with poor laws and institutions attract more FDI.

FDI is problematic for foreign investors because it means bringing to the country managerial capacity. In contrast FII is easy. Only money needs to be invested for earning returns. No effort is required to build organisational capacity for operating in that market. But if a country does not have a well-developed stock market, foreign investment has limited choices. In the well-developed markets of Europe, for instance, the share of FII in total capital inflow is high. In contrast, in the countries of Africa, FDI is the dominant form of foreign investment flows. However, too many investors do not venture into poor countries so the total foreign private follows are small.

In the poor countries of Africa, often the share goes in to the primary and extraction sector – such as mining and oil is very high. In rich OECD countries the share of FDI in total capital flows is low at barely 12%. As countries develop, the total capital flowing to them goes up with the increase in per capita income. However, the share of FDI in it goes down. Foreigners learn to trust their markets and institutions and do not feel the need to go there physically to earn returns. That is why economists in Latin America have been getting concerned about the rise in the share of FDI in total flows. The share of portfolio investment has collapsed and this is seen to be a loss of

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confidence in their markets and institutions. In the light of the above evidence, it is not surprising that the share of FII in total capital flows to China is very low. It is an indication of the bad accounting, bad corporate governance, market design problems, and the fundamental inconsistency between communism and the stock market. India should not be embarrassed about attracting portfolio flows. This in fact reflects its success in building sound companies and a well-designed equity market. It is a sign of good health. But what about the impact on economy? In the conventional argument, there are two reasons why FDI is preferred to portfolio investment. First, it is believed that FDI will stay in India in the event of a currency crisis, and second it is believed that FDI has a greater impact on growth. The dominant view is that FDI is bolted down as it involves investment in physical plants and equipment and these are very hard to get rid of.

Studies of currency crisis usually compare the stability of FDI with that of debt, particularly short-term debt, and in a comparison with short-term debt, FDI has indeed been found to be more stable. But that does not mean FDI cannot move. Latin American economist, Ricardon Hausmann, has argued that there are important mistakes that flow from problems of measurement. In a country's balance of payment, FDI inflows are defined as the increase in the equity position of a non-resident owner who holds more than 10% of the share of a firm. It also includes the loans

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received by local company from the parent owner. About 20% of FDI takes the form of loans from the parent company.

Moreover, since the firm is merely a set of assets that are owned – in other words, financed - creditors and shareholders, we must not think of FDI as the firm and its assets. Instead, it is just one of the sources of financial for the firm. FDI is not bolted down, machines are. At the time of crisis, the foreign company can either sell its equity or take a loan against physical assets and take money out of the country. Indeed, economists Graham Bird and Ramkishen Rajen have found that despite the bulk of capital inflows in to Malaysia being FDI, there was a currency crisis.

The argument that FDI raises the growth rate of the country is also not able to find absolute support. FDI is not found to raise growth when it goes into the primary sector. The impact is ambiguous in the case of services. When it comes to manufacturing, cross-country evidence does suggest that FDI raises growth. But, here again, growth can remain limited to the specific industry in which the FDI is made. Worse, it may even remain limited to the specific industry in which the FDI is made. The spillover effect of technology, management and corporate governance that is often expected to accompany FDI is not automatic. The growth impact of FDI is thus not automatic. It is only countries that have good institutions, skilled labour, openness to trade and

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well-developed financial markets that gain from FDI. In the absence of these, even if a country attracts FDI, its usefulness is limited.

The message for India is clear: instead of trying to increase FDI flows artificially, and restrict FII flows artificially, India should focus on improving markets, institutions and the regulatory framework to encourage investment – whether domestic or foreign. Domestic investment is largely responsible for the growth in any economy. Whether foreign investment comes or not should be a slide show. Policies should focus on creating a healthy well-functioning market and world-class infrastructure.

The reforms undertaken in last one decade have attempted to reverse the Government intervention to facilitate private, foreign direct investment and market orientation of Indian economy. Many legislative reforms have also been undertaken to create a climate conducive for investment. However, private efforts on investment are still getting disrupted because of inadequacies in the legal framework.

The Constitution of India provides individualistic powers to the executive, legislative and judicial branches. The recent history reveals that Indian judiciary has promptly risen to the occasion wherever the legislative or executive has failed in its role.

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To make Indian economy totally market oriented, we need several institutional and legal reforms. Although the reform process requires a lot of amendments in the legal framework, there is an urgency to make changes in the following Acts.

1. Labour laws

Labour laws legislations and industrial relations are put under concurrent list in Schedule VII of the Constitution. The legal regime governing industrial relations in India is complex with over 50 major laws covering labour welfare and dispute settlement. Notable statute is the Industrial Disputes Act which is hindering the productivity of the organised sector. Under Chapter V of the Act, the firm is required to get prior permission of the Government, in case of retrenchment and closure. Besides other provisions make employers very difficult to go for modernisation and technology upgradation. The impact of these laws on any foreign company is naturally on the same line as on Indian companies. It is important to emphasise reforms in this area urgently. The Raghavan Committee on Competition Law and Policy which submitted its report on 22$^{nd}$ May 2000 has recommended that the Industrial Disputes Act, 1947 and the connected statutes need to be amended quickly to provide for an easy exit to the non-viable, ill-managed and inefficient units

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subject to their legal obligations in respect of their liabilities.

2. The Land Acquisition Act:

Land Acquisition Act is the basis for all land acquisition procedures and for payment of compensation. Although Article 31(2) of Indian Constitution ensures that no law regarding compulsory acquisition for public purposes shall be questioned in any court, there are a lot of court cases and stay orders due to misinterpretation of certain terms in the Act. Hence, streamlining of the land acquisition procedures is very important with clear-cut definitions in the Act.

3. The Urban Land (Ceiling and Regulations) Act

The Urban Land (Ceiling and Regulations) Act was enacted mainly to counterbalance the impact of ceiling on agricultural land. The Act had many provisions which acted as negative features and were major obstacles to investment in real estates. To do away with these obstacles this Act was repealed with effect from 11/1/1999. This had immediate application in Punjab, Haryana, Delhi and all Union Territories. With regard to all other States where this Act is applicable separate

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resolutions by State legislatures are necessary to repeal it. Till date, it has been repealed only in some States including Tamil Nadu, Gujarat, Rajasthan and Uttar Pradesh. Urgent steps should be taken to repeal this Act in all other States where it continues to be applicable.

4. The Agricultural Land Ceiling Act

The Agricultural Land Ceiling Act was mainly enacted to abolish the Zamindari system and to protect small farmers. The liberalisation policies announced recently is mainly confined to foreign trade sector, industrial sector, and in financial and related sectors, but not in agricultural sector. While in the industrial sector, ceiling on investment limit under MRTP Act was removed, the agricultural sector still continues with Land Ceiling Act. Similarly, the reforms permitted non-resident Indian investment, but absentee cultivation of holdings in agriculture is not permitted. The Indian Constitution places the subject of land under the State list. So changes that are required in these laws require legislations in the States. It would be necessary to amend the relevant provisions of land reforms legislations and in tenancy laws to legalise hiring of land and consolidation of holdings for large-scale investment.

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The new Agricultural Policy announced in July 2000 proposes to promote private sector participation in the agriculture sector through contract farming and leasing arrangements. This is intended to allow accelerated technology transfer, capital inflow and assured markets for crop production, especially of oil seeds, cotton and horticultural crops.

5. Rent Control Acts

The Rent Control Acts were introduced as temporary measure to regulate the rent and also to prevent landlords from unscrupulous eviction. It is a state subject under the constitution which empowers the state governments to legislate on this subject. The provisions of Rent Control Act do not attract investment in the construction and real estate business. The Central Government has formulated model rent control law apart form creating a climate for reforms on rent control laws. Based on this model, the Delhi Rent Act, 1955 was passed and got the assent of the President. While the earlier Act was considered pro-tenant, the model is being considered pro-landlords. Such controversy over the Act is delaying the implementation of the Act. Speedy implementation of the Act is very important for attracting investment in real estate sector.

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6. The Companies Act

The Companies Act is one of the most voluminous pieces of legislation comprising over 650 sections and 15 schedules. Following liberalisation, some of the provisions of the Act were modified to attract foreign investment. Still there are many sections relating to incorporation of companies, on share capital, procedures on public issue, registration and on remuneration procedures which are felt as unnecessary and require amendment. The Companies (Second Amendment) Bill, 1999 is under the consideration of Parliament now. The fundamental objectives of this Bill are to improve the quality of corporate governance, investor protection and deletion of some of the redundant provisions of the Companies Act of 1956.

7. The Indian Electricity Act, 1910 and the Electricity (Supply) Act, 1948

The Indian Constitution puts electricity as one of the sectors under concurrent list. The core legislation in this sector comprise of the Indian Electricity Act, 1910 and the Electricity (Supply) Act, 1948. The existing provisions of the electricity sector prevent intervention of Central Government at the

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state level. The government must make necessary amendments to ensure timely implementation of the power projects. The Electricity Regulation Commission Act, 1998 has been enacted for the constitution of Central and State Electricity Regulatory Commissions with the power to fix tariffs. But many states have not yet constituted State Electricity Regulatory Commissions. A draft Electricity Bill, 2000 is now under the consideration of the Central Government. It proposes to replace all the existing Acts of 1910, 1948 and 1998.

8. Major Port Trust Act and the Indian Ports Act

The Major Port Trust Act and the Indian Ports Act are viewed as being strongly biased in favour of regulation rather than autonomy. To enable the privatisation to succeed, many amendments are required. Besides, there are plethora of legal provisions in the form of regulations and also Dock bye-laws. These need to be amended. The Major Port Trusts Act has been amended in May 2000 allowing major ports to enter in to joint ventures with minor ports, foreign ports and foreign or domestic companies. However this amendment does not extend to minor ports.

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9. The National Highway Act

The National Highway Act is primarily intended to enable development and maintenance of national highways. Necessary amendments are made to permit private investors to collect toll from users. However, the amendments do not clearly define the rules governing the toll rate.

10. The Indian Telegraphs Act

The telecommunication sector is covered by Indian Telegraphs Act, Indian Wireless Telegraph Act and the Telegraph Regulatory Authority of India Ordinance. Although the Indian Telegraph Act is got to be replaced and a new law is to be enacted, the Act does not come in the way of implementing the New Telecom Policy.

11. The Indian Patents Act

The Indian Patents Act requires a lot of changes to accommodate the changes that are enshrined in the TRIPS Agreement of WTO. It would be necessary for India to pass the Patent Bill immediately to avoid discrepancies within the sectors as well amongst the players. By the Patents (Amendment) Act, 1999 Patent Act was amended to provide for Exclusive Marketing

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Rights and mailbox facilities to foreign pharmaceuticals and agro-chemical companies. The Patents (Second Amendment) Bill, 1999, now passed by the Parliament provides for, inter alia, a uniform

term of twenty years for all categories of invention.

12. Central Excise Act, Salts Act, 1944, and Customs Act, 1962

Valuation under these taxes becomes one of the most important aspects, which increases arbitration and court cases. Legal reforms in these areas are necessary for efficient imposition of these Acts.

The keys to effective and balanced economic growth are equity, participation, self-reliance, sustainability and holistic approach to community life. The key purpose should be to create and environment in which people can expand and make best use of their competence and capabilities.

It has been unfortunately observed that under the pressure of globalisation, governments are reducing expenditure on education and health, thus retarding the growth of human capital. Redistributing resources to the poor by improving

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their health, education, and nutrition is very crucial because it enhances their capabilities to lead more fruitful lives. We need action plan in three directions namely,

(i) Poverty reduction,
(ii) Employment generation, and
(iii) Social integration.

India merely spends 1.5% of GDP in health compared to average of 9% investment in health by other economies. We need to focus on social sector reforms like a widespread of literacy, expansion of vocational training programmes and change in outlook of industries through increased training of HRD activities. Market mechanism should maximise employment rather than profit and state plans should fill up infrastructural gaps.

We need to spread education as widely as possible among citizens. In order to lead India towards knowledge society we need to literate half of the population, as the human capital is the most precious form of capital. If we cannot afford education, we cannot afford to remain a civilised society. These economic reforms must ensure the right to work and decent living to all.

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# Appendix

## Details of changes made in the Foreign Trade Policy

### *Changes in chapter 2 – FTP General Provisions Regarding Imports and Exports*

The following paras have been added / amended / deleted as under

PARA 2.5 – Exemption from Policy / Procedure

Second sub-para, second sentence amended "Such request may be considered only after consulting Advance Licensing Committee (ALC) if the request is in respect of a provision of Chapter-4 (excluding any provision relating to Gem & Jewellery sector) and EPCG Committee if the request is in respect of a provision of Chapter-5 of the Policy/ Procedure". The words in bold are added.

Second sub-para, third sentence amended "However, any such request in respect of a provision other than Chapter-4, Chapter-5 and

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Gem & Jewellery sector as given above may be considered only after consulting Policy Relaxation Committee." The words in bold are added.

Remarks : Clarity provided with reference to operational issues.

PARA 2.45 – Electronic Data Interchange

In an attempt to speed up transactions, reduce physical interface and impart transparency in activities related to exports, digitally signed electronic applications with payment through the electronic fund transfer would be encouraged. Such applications shall be cleared within 24 hours and the applicant shall be required to furnish only 50% of the fee mentioned in Appendix- 29 of Handbook (Vol.1).

PARA 2.45.1 – Trade Facilitation through EDI Initiatives

It is endeavour of the Government to work towards greater simplification, standardization and harmonization of trade documents using international best practices. As a step in this direction DGFT shall move towards an automated environment for electronic filing, retrieval and authentication of documents based on agreed protocols and message exchange with other community partners including Customs and Banks.

PARA 2.45.2 - DGCI&S Commercial Trade Data

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To enable the users to make commercial decisions in a more professional manner, DGCI&S trade data shall be made available with a minimum time lag in a query based structured format on a commercial criteria.

Remarks : Needs speedy implementation. All other departments should also move fast.

PARA 2.45.3 - Fiscal Incentives to promote EDI Initiatives adoption

With a view to promote the use of Information Technology, DGFT will provide fiscal incentives to the user community. The details are enumerated in the Handbook (Vol.I).

Remarks : Nothing but reduction of processing fees already promised earlier.

PARA 2.46 - Regularization of EO default and settlement of customs duty and interest through Settlement Commission

Remarks : DGFT still has a say and can levy fiscal penalty in respect of EO shortfall in value terms. This should be seriously noted.

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PARA 2.47 – Easing of documentation requirements

Pending the finalization of Single Common Document (SCD) for international trade, the government departments dealing with exports and imports will honour the permission/ licence/ certificate issued by the other government departments based on the verification of the export documents like shipping bill, bank realization certificate, packing list, bill of lading etc and will not insist upon fresh submission of these documents

Remarks : Why this deletion? This para is needed.

PARA 2.48.1 – Remission of Service Tax in DTA – Heading amended

Amended "For all goods and services which are exported from units in Domestic Tariff Area (DTA) and units in EOU/EHTP/STP/BTP remission of service tax levied shall be allowed." The words in bold are added.

PARA 2.48.2 – Exemption from Service Tax in SEZ – Heading amended

Amended. "Units in SEZ shall be exempted from service tax." "EOU/EHTP/STP/BTP" deleted.

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Remarks : It seems MoF does not agree to extend exemption of service tax to EOUs/EHTPs/STPs/BTPs

PARA 2.49.3 - Web chat

The office of the Director General of Foreign Trade has opened a chat window on its website for interacting with the trade and industry to reply to queries on the Foreign Trade Policy. This web based interface would be held from 3.00 pm to 5.00 pm on the second Wednesday of every month.

A new para added in the end.

The Government is committed to resolving all outstanding problems and disputes pertaining to the past policy periods through the Grievance Redressal Committee set up on 27.10.2004, for condoning delays, regularizing breaches by exporters in bonafide cases, resolving disputes over entitlements, granting extensions for utilization of licences etc

*Chapter 2 – HB General Provisions Regarding Imports and Exports*

The following paras have been added / amended / deleted as under:

PARA 2.9.1 – IEC Format and Statement

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In first sub-para instead of "Appendix 3A", "Appendix 18B" has been substituted.

Second sub-para "A consolidated statement of IEC numbers issued by the licensing authority shall be sent to the offices of the Exchange Control Department of the RBI as given in Appendix-18D as per the statement given in Appendix-18C." Instead of "Appendix 30", "Appendix 18D" has been substituted and instead of "Appendix 3B", "Appendix 18C" has been substituted.

Remarks : There is no Exchange Control Department in the RBI now. It is now Foreign Exchange Department.

PARA 2.11 – Imports under Indo-US Memorandum of Understanding

Instead of "Appendix 7", "Aayaat Niryaat Form" has been substituted. Instead of "Annexure to Appendix 7", "Appendix 31" has been substituted.

Remarks : A consolidated and comprehensive new form called 'Aayaat Niryaat Form" to be referred.

PARA 2.12.4 – Validity of Import licence/certificate/permission/CCPs

Last sentence added "The original validity of export licence for restricted items shall be 12

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months from the date of issuance unless otherwise specified."

Remarks : Special provision for export licence for restricted items.

PARA 2.13.3 – Revalidaiton of Import licence/certificate/permission

Second sub para instead of "Appendix 10G", "Aayaat Niryaat Form" has been substituted.

PARA 2.14 – Duplicate Copies of Export-Import Licence/Certification/Permission/CCP

Instead of "Appendix 11", "Appendix 24" has been substituted.

PARA 2.20 – Execution of Bank Guarantee/Legal Undertaking for Advance Licence and EPCG

In the table, for sr. no. 5 and 6, percentage of BG has been reduced from 25% to 15% of duty saved on excise and education cess, if applicable.

Remarks : Good provision. BG limited to 15% of duty saved (excise + education cess). No interest to be taken into account for calculation of BG.

Third sub-para, instead of "25% bank guarantee", "15% bank guarantee" is substituted

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Earlier fourth sub-para deleted "In all the above cases, the licencee is required to furnish declaration to the effect that they have not been penalized under the Customs Act, Excise Act, Foreign Trade (Development & Regulation) Act, 1992 and FEMA/FERA."

Earlier fifth sub-para, now fourth – instead of "Appendix 23", "Appendix 26" has been substituted

PARA 2.21.1 – Preferential

(a) – Generalized System of Preferences (GSP)
Instead of "Appendix 35", "Appendix 4A" has been substituted

(b) – Global System of Trade Preferences (GSTP)

(c) – SAARC Preferential Trading Agreement (SAPTA)

Instead of "Appendix 35A", "Appendix 4B" has been substituted

(d) – Bangkok Agreement
Instead of "Appendix 35A", "Appendix 4B" has been substituted

(e) – India- Sri Lanka Free Trade Agreement (ISLFTA)

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(f) – India Afghanistan Preferential Trade Agreement

(g) – Indo-Thailand Framework Agreement for Free Trade Area

First sentence amended as "India and Thailand have signed the protocol to implement Early Harvest Scheme under India- Thailand Free Trade Agreement on 1st September 2004.The tariff preferences for imports on the items of Early Harvest Scheme would be available only to those products, which satisfy the Rules of Origin Criteria, which have been notified by Department of Revenue, Ministry of Finance, vide notification No.101/2004-Customs dated 31st August 2004."

Remarks : Tariff reduction for agreed items are as under :

| Period | Tariff reduction on applied MFN tariff rates as of 1st January 2004 |
|---|---|
| 1.9.2004 – 31.8.2005 | 50% |
| 1.9.2005 – 31.8.2006 | 75% |
| 1.9.2006 | 100% |

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PARA 2.21.2 – Non-Preferential

Instead of "Appendix 35B", "Appendix 4C" has been substituted

Fourth sub-para amended "Any of the agencies desirous of enlistment in Appendix–4C may submit their application as per Annexure I to Appendix 4C to the concerned Licensing Authority under whose Jurisdiction the applicant falls as given in Appendix 1."

PARA 2.27 – Import/Export of Samples

Value limit of duty fee import of samples for gems and jewellery sector has been increased from Rs. 1 lakh to Rs. 3 lakhs.

Remarks : Limit extended to Rs. 3 lakhs for G & J sector.

PARA 2.59.3

This para has been deleted. However, in the case of foreign agencies accredited by a nodal agency in the parent country desirous of enlistment in Appendix-28-A, the following documents may be forwarded to the office of DGFT:

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a) A copy of the valid accreditation certificate of the foreign agency as also mentioning whether the accreditation agency is a member of IAF( International Accreditation Forum),

b) Details of the Indian partner/agency/branch operating in India on behalf of the parent company,

c) List of foreign and Indian agencies granted certification,

d) An undertaking to the effect that "in case of any liability arising out of certification, the parent company and its partner/agency/ branch in India would be liable to Indian laws in Indian courts".

PARA 2.15 – Duplicate copies of Export/Import Licence/Certification/Permission/CCPs

Duplicate copy of freely transferable licence/ certificate/ permissions, may be issued against an application accompanied by the following documents:

a. An application with a fee equivalent to 10% of duty saved or duty credit.

b. A copy of FIR reporting the loss.

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c. A copy of the original affidavit on notorised stamp paper.

d. Indemnity bond on a stamp paper undertaking to indemnify the revenue loss to the Government which may be caused on account of issue of duplicate licenses covering the duty saved/ duty credit amount.

Remarks : How to calculate duty saved amount may be a problem but since DFRCs are granted with same value addition of 25% - this may be justified.

*Chapter 3 – FTP Promotional Measures*

The following paras have been added / amended/ deleted as under

PARA 3.5.2 – Status Category

In the note given under this para have been amended as under:

i) Note No. 1 amended as under:

Manufacturer exporters in the Small Scale Industry/Tiny Sector/Cottage Sector, Units registered with KVICs/KVIBs, Units located in

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North Eastern States, Sikkim and J&K, Units exporting handloom/ handicrafts/hand knotted or silk carpets, exporters exporting to countries in Latin America/CIS/sub-Saharan Africa as listed in Appendix-9, units having ISO 9000 (series)/ ISO 14000 (series) /WHOGMP/HACCP/SEI CMM level-II and above status granted by agencies listed in Appendix-6, exports of services and exports of agro products shall be entitled for double weightage of exports made for grant of Star Export House status.

- The word 'Units' has been replaced by the words in bold.
- The words 'Appendix-17C' have been replaced by the words 'Appendix-9'
- The words 'Appendix-28A' have been replaced by the words 'Appendix-6'

Remarks : For double weightage, merchant exporters exporting products of SSI may not be considered. Needs clarification.

ii) New Note No. 4 has been added

"In case the recognition is claimed based upon the current year's export performance, same shall be considered only in case the exporter has export performance during any one of the preceding three years as well."

Remarks : Status cannot be claimed purely on current year's basis.

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*Vishesh krishi upaj yojana (special agricultural produce scheme)*

PARA 3.8.1 – Objective

The objective of the scheme is to promote export of fruits, vegetables, flowers, minor forest produce, dairy, poultry and their value added products, by incentivising exporters of such products.
The words in bold are added

PARA 3.8.2 – Entitlement

The para amended as under:
"Exporters of such products shall be entitled for duty credit scrip equivalent to 5% of the FOB value of exports for each licencing year commencing from 1st April, 2004. However, dairy, poultry and their value added products shall qualify for benefits in respect of the exports made on or after 1st April 2005. The scrip and the items imported against it would be freely transferable."

PARA 3.8.2.1 – Entitlement

Under the Scheme, export of all items as given in Appendix-37A of Handbook (Vol.1) shall qualify

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for export benefits as per Para 3.8.2 above. ** Items which are restricted or prohibited for export under Schedule-2 of the Export Policy in the ITC (HS) Classification of Export and Import items shall not be eligible for any benefits under Para 3.8.2.

- The words 'Chapter 6, 7, 8, 9 (excluding 0901, 0902 & 0903), 20 under the ITC (HS) Classification of Export and Import items, 2004-2009 and Minor Forest Produce (to be notified separately)' have been replaced by the words in bold.

- ** The words 'However, items appearing as 'Others' at the 8 digit level in the ITC (HS) in the aforesaid Chapters shall not be eligible for any benefits under Para 3.8.2. In addition,' have been deleted

PARA 3.8.2.2

Following exports shall not be taken into account for duty credit entitlement under the scheme:

(a) Export of imported goods covered under Para 2.35 of the Foreign Trade Policy or exports made through transshipment.

(b) Deemed exports (even when payments are received in Free Foreign Exchange and payment is made from EEFC account).

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Remarks : Procedural details notified.

PARA 3.8.3.1 - Imports allowed

The para has been amended as under
"Items listed in Appendix-37B of Handbook of Procedures Vol.I shall not be allowed to be imported under the scheme."

*Chapter 3 – HB Promotional Measures*

The following paras have been added / amended as under

PARA 3.2 - Application for Grant of Status

First sub-para – Alongwith 'grant', 'renewal' added. Instead of '1st March', '31st March' is substituted. Instead of 'Appendix 17", 'Aayaat Niryaat Form' is substituted and instead of 'Appendix 17A', 'Aayaat Niryaat Form' is substituted.

Third sub-para instead of 'Appendix 17", 'Aayaat Niryaat Form' is substituted

PARA 3.2.3 – PARA DELETED

The application for grant of status certificate in the case of non service providers mandates the

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submission of a "Bank Certificate of Export Realisation/ Deemed Exports for Status Certificate" as given in Appendix-17B. However, this provision shall not apply to existing Status Holders who are seeking renewal or upgradation of existing status.

PARA 3.2.5 - Target Plus Scheme

I. For direct as well as third party exports, the Export documents viz Export Order, Invoice, GR form, Bank Realization Certificate should be in the name of applicant only.

Remarks : Any bought out exports will automatically get disqualified.

Point II – First sentence "II. Goods allowed to be imported under this scheme shall have a broad nexus with the products exported and a declaration in this regard shall be made by the applicant in Appendix 17D." The words in bold are deleted. Second sentence added "For the purpose of import entitlements under this scheme, 'broad nexus' would mean goods imported with reference to any of the product groups of the exported goods within the overall value of the entitlement certificate."

Remarks : Very good provision.

Point III – Second sub-para added "Further in order to enable supporting manufacturers, whose

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names appear in the shipping bills, to import directly, Licensing Authority concerned shall endorse the names of such supporting manufacturers on the certificate as co-licensees."

Remarks : Very important provision – this means exporter need not undertake imports. This also means limited transferability.

Point IV - amended

The last date for filing of such applications shall be 31st December.
Earlier it was 31st March.
Point VII – Second sub-para added – "Revalidation of duty credit entitlement certificate shall not be allowed."

Remarks : Enough period to utilize, however, one should not delay the utilization.

Point VIII – Instead of "Appendix 17E", "Aayaat Niryaat Form" is substituted

PARA 3.17.1 - Electronic Data Interchange

The role and functions of EDI are defined in Para 2.45 of the Foreign Trade Policy. The basic purpose of EDI Initiatives is to improve the services for DGFT user community thereby achieving greater transparency of operations and reducing transaction costs by decreasing the processing time for obtaining licences /permission/

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certificate from the DGFT. These EDI initiatives have made our exports competitive in international markets.

The provisions contained above have been transferred from earlier Para 3.17 which now stands deleted. The deleted para is "With a view to reducing transaction time and costs in obtaining licences/permission/certificate from the DGFT, electronic filing and electronic processing of licence application has been introduced."

PARA 3.17.3 – Procedure

Last sentence of first sub-para deleted "Deficiency, if any, shall be communicated online to the applicant. [Earlier Para 3.17.2]

PARA 3.17.4 – Fiscal Incentives for EDI

The following deductions in Application Fee would be admissible for applications signed digitally or/ and where application fee is paid electronically through EFT (electronic fund transfer)

| S. No | Mode of Application | Fee Deduction (as a % of normal application fee) |
|---|---|---|
| 1 | Digitally signed | 25% |
| 2 | Application fee payment | 25% |

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vide EFT

3 Both digitally signed as well as use of EFT for payment of application fee 50%

[Earlier third and fourth sub-paras of Para 3.17.2]

PARA 3.17.6 –

Amended "License issued using DGFT Electronic Application System shall be transmitted electronically to the Customs through EDI Mode. This shall also obviate the need for verification of licences before allowing clearance."
[Earlier Para 3.17.4]

Remarks : Important enabling provision.

PARA 3.1.7.7 – New EDI Initiatives – New Para Added

To further improve the quality of services some new EDI Initiatives are being taken by DGFT.

In order to reduce documentation, a multiple purpose common application form 'Aayaat Niryaat Form' is being introduced.

PARA 3.18 - Served From India Scheme

Point (b) – Instead of "Appendix 36A", "Aayaat Niryaat Form" is substituted

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Point (c) deleted – "Where the applicant is the branch office or the individual units of the service provider, it shall furnish (i) self certified copy of any valid documentary evidence such as tax return etc. where the name of the branch/unit is given and (ii) an authority letter from the Registered Office of a company or head office of a firm, clearly, indicating that the Registered/Head office or its branches and unit(s) have not been declared defaulter or otherwise made in eligible for import/export under any of the provisions of the policy."

Point (e) deleted "The certificate holder intending to procure the item (s) from the indigenous sources/State Trading Enterprises in lieu of direct import has the option to source them against Advance Release Order (ARO) or invalidation letter, as the case may be, which shall be denominated in foreign exchange/Indian Rupees."

Point (g) – Second sentence added "Revalidation of duty credit certificate shall not be allowed." Instead of "Appendix 36B", "Aayaat Niryaat Form" has been substituted

Point (h) – Second sub para deleted "This would be confirmed by the submission of a certificate as per Annexure 1 to Appendix 36 B pertaining to the "Statement of Utilization of Duty Credit Entitlement for Status Providers" to the licencing authority."

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PARA 3.18.1 - Ineligible Remittances and Services –

(a) The following Foreign Exchange remittances shall not be eligible for entitlement under this scheme:

I. Remittances related to Financial Services Sector

1. Raising of all types of foreign currency Loans.
2. Export proceeds realisation of clients.
3. Issuance of Foreign Equity through ADRs /GDRs or other similar instruments.
4. Issuance of foreign currency Bonds.
5. Sale of securities and other financial instruments.
6. Other receivables not connected with the services rendered by the financial institutions.

II. Remittances earned through contract/regular employment abroad (e.g. labour remittances).

(b) Payments received from Export Earners Foreign Currency (EEFC) Account shall not be counted for benefits under the scheme.

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Remarks : Important para for exporters of financial services

PARA 3.19 - Vishesh Krishi Upaj Yojana

The following guidelines would be applicable for exports under this scheme:

(a) For direct as well as third party exports, the Export documents viz Export Order, Invoice, GR form, Bank Realization Certificate should be in the name of applicant only.

(b) The Duty Credit may be used for import of inputs or goods including capital goods, as may be notified, provided the same is freely importable under ITC(HS).

(C) The duty credit certificate would be valid for a period for 24 months.

Detailed guidelines and procedure for the scheme shall be notified.

PARA 3.19.1 – NEW PARA ADDED

A single consolidated application for the duty credit entitlement certificate against exports made through one port shall be filed with the jurisdictional Regional Licensing Authority by the Registered office in case of a company and Head

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Office in case of others. The last date for filing of such application shall be 31st December.

PARA 3.19.2 – NEW PARA ADDED

The application in the 'Aayaat Niryaat Form' shall be accompanied by EP copy of the shipping bill and bank realization certificate as per Appendix-22A.

PARA 3.19.3 – NEW PARA ADDED

For direct as well as third party exports, the Export documents viz Export Order, Invoice, GR form, Bank Realization Certificate should be in the name of applicant only.

PARA 3.19.4 – NEW PARA ADDED

In cases where the applicant applies for the credit entitlement certificate after realization or shipments are made against irrevocable letter of credit or bill of exchange is unconditionally Avalised/ Co-Accepted/ Guaranteed by a bank and the same is confirmed by the exporters bank and certified by the bank in the relevant Bank certificate of export and Realization, the credit entitlement certificate shall be issued with transferable endorsement. In other cases, the credit entitlement certificate shall be initially issued with non-transferable endorsement. Upon realization of export proceeds, such credit entitlement

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certificates can be endorsed as transferable, if the applicant so desires.

PARA 3.19.5 – NEW PARA ADDED

The duty credit certificate shall be issued with a single port of registration and this will be the port from which the exports have been made. However, the applicant may use this duty credit for imports from any other port after obtaining TRA from the port of registration.

PARA 3.19.6 – NEW PARA ADDED

For each duty credit certificate, split certificates subject to a minimum of Rs 5 lakh each and multiples thereof may also be issued. A fee of Rs 1000/- each shall be paid for each split certificate. However, a request for issuance of split certificate(s) shall be made at the time of application only and shall not be considered at a later stage. The split certificate will have the same port of registration for the purposes of imports as appearing in the main certificate.

PARA 3.19.7 – NEW PARA ADDED

The entitlement can be used for import from private/public bonded warehouses subject to the fulfilment of provision of paragraph 2.28 of

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Foreign Trade Policy and the terms and conditions of the notification issued by Department of Revenue from time to time in respect of private/public bonded warehouses.

PARA 3.19.8 – NEW PARA ADDED

The duty credit entitlement certificate shall be valid for a period of 24 months.

Revalidation of duty credit entitlement certificate shall not be allowed.

Remarks : Procedure for VKUY finally introduced.

*Chapter 4 – FTP Duty Exemption Remission Scheme*

PARA 4.1.9A – Provision for BIFR units

Any firm/company registered with BIFR or any firm/ company acquiring a unit, which is under BIFR shall be allowed EOP extension as per the rehabilitation package prepared by the operating agency subject to subsequent approval of BIFR.

However, in cases where the rehabilitation package does not specify the EOP extension period, a time period upto 5 years reckoned from the date of issue of licence would be permitted on

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merits of the case for fulfillment of export obligation.

Similarly, SSI units shall also be entitled for similar facility as per the rehabilitation scheme of the concerned State government. However, in cases where the State rehabilitation scheme does not specify the export obligation extension period, a time period upto 5 years reckoned from the date of issue of licence would be permitted on merits of the case for fulfillment of export obligation.

Remarks : Sick units can get extention of 5 years in Export obligation period, provided they are covered by rehabilitation scheme.

PARA 4.1.10 - Advance Licence for Annual Requirement

The entire para 4.1.10 has been amended as under
'Advance Licence can also be issued on the basis of annual requirement for physical exports, intermediate supplies and / or deemed exports.

One to Five Star Export House shall be entitled for the Advance licence for annual requirement. All other categories of exporters having past export performance (in the preceding two years) shall also be entitled for the Advance Licence for annual requirement.

In addition, a merchant exporter shall also be issued the Advance Licence for Annual Requirement provided they agree to the

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endorsement of the name(s) of the supporting manufacturer(s) on the relevant licence.

The entitlement in terms of CIF value of imports under this scheme shall be upto 300% of the FOB value of physical export and / or FOR value of deemed export in the preceding licensing year or Rs 1 crore, whichever is higher. Such licence shall have value addition as specified in para 4.1.6 of the Foreign Trade Policy.'

The words in bold are added and the word in bold and underlined is amended.

Remarks :
1) Annual advance licence now be claimed by other exporters as well.
2) Value limit for Star Export Houses increased from 200 to 300% of FOB value of exports of preceeding year.

*Chapter 5 FTP Export Promotion Capital Goods Scheme*

The following paras have been added / amended as under

PARA 5.1 - EPCG Scheme

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Provision related to agri units is amended as under :

In the case of agro units, import of capital goods at 5% Customs duty shall be allowed subject to a fulfillment of an export obligation equivalent to 6 times the duty saved (on capital goods imported under the Scheme) over a period of 12 years from the date of issue of licence.

Remarks : Instead of 0% duty, it is now 5% duty and instead of EO at 8 times the duty saved over a period of 8 years, it is now equal to 6 times the duty saved to be fulfilled over a period of 12 years.

Third sub-para added as under :

However for SSI units, import of capital goods at 5% Customs duty shall be allowed subject to a fulfillment of an export obligation equivalent to 6 times the duty saved (on capital goods imported under the Scheme) over a period of 8 years from the date of issue of licence provided the landed CIF value of such imported Capital Goods under the Scheme does not exceed Rs Twenty Five Lakhs and the total investment in plant and machinery after such imports does not exceed the SSI limit.

Remarks : For SSI provision for EO has been amended to 6 times duty saved over a period of 8 years with restrictions imposed hereabove.

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Earlier sixth sub-para deleted “Spares (including refurbished/ reconditioned spares), tools, refractories, catalyst and consumable for the existing and new plant and machinery may also be imported under the EPCG scheme.”

In provision related to import of motor cars, etc., “companies owning/operating golf resorts” has been added.

“Import of Restricted items of imports mentioned under ITC(HS) shall only be allowed to be imported under the Scheme after approval from the Import Licensing Committee.”

Remarks : Any restricted item will require the approval of Import Licensing Committee first. In other words, for restricted item, licence will not be issued on self declaration basis.

EPCG for Retail Sector

To create modern infrastructure in the retail sector, concessional duty benefits under EPCG scheme shall be extended for import of capital goods required by retailers having minimum area of 1000 sq meters. The retailer shall fulfil the export obligation i.e. 8 times the duty saved in 8 years.

Remarks : In line with government’s intention to attract FDI in retail sector.

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Export Obligation –

"The import of capital goods for creating storage and distribution facilities for products manufactured or services rendered for export by the EPCG licence holder would be permitted under the EPCG Scheme."

Storage and Distribution :

1. Air-conditioners for storage of sensitive goods required to be stored under controlled condition

2. Computer controlled inventory equipments

Distribution

1. Fork lifts
2. Vehicles like delivery vans, trucks, etc.

Proper justification would however be required.

"The export obligation under the scheme shall be, over and above, the average level of exports achieved by him in the preceding three licensing years for same and similar products within the overall export obligation period including extended period, if any except for categories mentioned in Handbook (Vol.1)."

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Remarks : Maintenance of average exports continues.

"Payments received against 'Counter Sales' in free foreign exchange through banking channels as per the RBI guidelines shall be counted for fulfillment of export obligation under Para 5.1 C."

Remarks : In line with EPCG for retail sector. However, proper records will have to be maintained (credit card purchases/cash purchases against encashment certificate, etc.)

Benefits to Domestic Supplier

First sub para – Instead of "Advance Licence for deemed exports", "Advance Licence" has been substituted.

Remarks : Due to merging of different categories of licences.

Technological Upgradation of existing EPCG machinery

"The facility for technological upgradation shall be available only once and the minimum imports to be made shall be at least 10% of the existing investment in plant and machinery by the applicant firm."

Remarks :

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1. Restrictive provision - shall complicate the issue.

2. Policy makers should not dictate as these are technical matters.

3. simpler provision should be introduced.

<u>Incentives for Fast Track Companies</u>

"To incentivise fast track companies with a view to accelerate exports under the Scheme, in cases where the licence holder has fulfilled 75% or more of the export obligation under the Scheme (including average level of exports) in half or less than half the original export obligation period specified in the Licence, the remaining export obligation shall be condoned and the Licence redeemed by the licensing authority concerned.

However no benefits under Para 5.12 of Handbook (Vol.I) shall be available in such cases."

*<u>Chapter 5 – HB Export Promotion of Capital Goods</u>*

The following paras have been added / amended as under

PARA 5.3.1 – amended

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"The Licensing Authority concerned shall, on the basis of the nexus certificate from an Independent Chartered Engineer (CEC) submitted by the applicant in Appendix 32A, issue the EPCG licence and thereafter forward a copy of the EPCG licence [along with a copy of the CEC] to the concerned Jurisdictional Central Excise Authority.

'nexus' has been added.
Instead of Annexure I to Appendix 9, "Appendix 32A" has been substituted. The words in bracket are deleted.

PARA 5.3.2 – DELETED

The licence holder (whether registered with Central Excise Authority or not) shall produce to the concerned licensing authority a certificate from the jurisdictional Central Excise authority confirming installation of capital goods at the factory / premises of the licence holder or his supporting manufacture(s)/vendor(s) within six months from the date of completion of imports.

However, service providers, can give a certificate either from the jurisdictional Excise Authority or from an independent chartered engineer confirming installation of movable and immovable capital goods at the premises of the service provider.

Remarks : Very good simplification. Installation Certificate no more required.

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PARA 5.3.4 –

Point (i) "The applicant may also apply for import of spares including refractory, catalyst and such consumables as are required for installation and maintenance of capital Goods imported/to be imported under the EPCG Scheme." Words in bold are added.

Point (iii) deleted "(iii) In case of import of spares for capital goods, the licence holder (whether registered with Central Excise Authority or not) shall produce to the licensing authority a certificate by the jurisdictional central excise authorities confirming the inventory of spares taken in the records of the licence holder within one month of the date of completion of each import."

Last sub-para deleted "However, the service providers, can give a certificate either from the jurisdictional Excise authority or from an independent chartered engineer confirming the inventory of spares taken in record of the licence holder within six months from the date of completion of imports."

Amended Para 5.3.4 (ii)
"Further at the time of final redemption of export obligation licence holder shall submit certificate from the Independent Chartered Engineer confirming the use of spares so imported in the

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installed capital goods on the basis of stock & consumption register maintained by licence holder."

Remarks : No need of submitting central excise certificate. Only Chartered Engineer certificate is enough both for goods and services.

PARA 5.7.3 – Condition for fulfilment of export obligation

Earlier first three sub-paras deleted.

"Exports shall be physical exports. However, deemed exports as specified in paragraph 8.2 (a), (b), (d), (f), (g) & (j) of Policy shall also be counted towards fulfilment of export obligation along with the usual benefits available under paragraph 8.3 of the Policy.

Royalty payments received in freely convertible currency and foreign exchange received for R& D services shall also be counted for discharge under the EPCG scheme.

Payment received in rupee terms for the port handling services in terms of Chapter 9 of the Foreign Trade Policy shall also be counted for export obligation discharge under the Scheme."

The para now reads as under :

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Exports made against the Government of India/EXIM Bank Line of Credit and exports made under Deferred Payment/Suppliers Line of Credit Contract backed by ECGC Cover would also be counted for fulfillment of export obligation under the Scheme.

This para was added vide Public Notice No. 45 dtd. 14.01.2005.

Remarks : Is this a mistake or deliberate omission. If the omission is correct, one cannot fulfill the export obligation against EPCG by deemed exports. Needs immediate clarification.

PARA 5.7.5 –

Amended "Where the manufacturer exporter has obtained licences for the manufacture of the same export product both under EPCG and the Duty Exemption or Diamond Imprest Licence Scheme or made exports under DEPB/Advance Licence/ DFRC/ Replenishment licences, the physical exports or deemed exports for categories mentioned in paragraph 5.7.3 made under these schemes shall also be counted towards the discharge of the export obligation under EPCG scheme.". The words in bold are added.

Remarks :

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1. The word 'drawback' is missing. There should be a provision to include drawback also.
2. This language includes deemed exports, contrary to deletion of sub-paras of 5.7.3

PARA 5.7.6 –

Third sub-para amended as "However, the transfer of capital goods would be permitted [within] the group companies or managed hotels under intimation to the Regional Licencing Authority and the jurisdictional Central Excise Authority in case of manufacturer/merchant exporters and to the Regional Licensing Authority only in the case of Service providers.". The words in bold are added and the word in bracket 'within' is substituted instead of 'to'.

PARA 5.8.4 – Fulfilment of export obligation

Last sub para deleted

"However, wherever Customs duty is to be paid under EPCG scheme, on account of shortfall in export obligation for regularisation for bonafide default, the same shall be paid alongwith interest @15% per annum thereon. This facility shall be available to all pending cases of regularisation of EPCG licences irrespective of the date of its issuance".

PARA 5.8.5 – Maintenance of Average

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Second sentence deleted "However, in case of any shortfall in maintenance of the average exports below the 75% threshold as given in para 5.9 of the Policy, the licence holder shall intimate the regional office of the same at the end of the year of the shortfall giving a valid justification."

Remarks : Relaxation in maintenance of annual average stands deleted.

PARA 5.9.1 – Monitoring of Export obligation

First sentence amended "The licence holder shall submit to the licensing authority by 30th April of every year, report on the progress made in fulfillment of export obligation against the licence issued as well as annual average level of exports achieved.". The words in bold are added.

Remarks : Annual average for extended period continues.

Second sentence amended "The report shall be submitted electronically on the DGFT website." instead of Appendix 9A, the words in bold are substituted.

Remarks : Progress report to be submitted to the RLA by 30th April every year electronically. This report will now also include progress on annual

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average level of exports achieved. Time bound submission of report.

PARA 5.10 – Automatic Reduction / Enhancement up to 10 % of CIF value and pro rata Reduction / Enhancement in Export Obligation

First sentence of second sub para amended "In such cases, the licence holder shall furnish additional fee to cover the excess imports effected in terms of CIF value/duty saved amount to the licensing authority within one month of the excess imports taking place."

Remarks : Time period of one month has been specified for furnishing additional fee to cover excess imports.

PARA 5.11 – Extension of Export Obligation Period

Para amended "The concerned licensing authority, may consider one or more request for grant of extension in export obligation period, on payment of a composition fee of 2% of the total duty saved under the Licence or an enhancement in export obligation imposed to the extent of 10% of the total export obligation imposed under the Licence, as the case may be, at the choice of the exporter, for each year of extension sought. The total extended export obligation period shall not exceed two years from the expiry of the original export obligation period. Exports made on or after the

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date of receipt of application for EO extension shall only qualify for discharge of EO fulfillment under the Scheme

However extension in EO period beyond the two years period available above, may be considered, for an extension upto 3 years with 50% enhanced EO and upto 5 years with 100% enhanced EO in addition to any other provision subject to such undertaking by the licensee. However, in such cases, the licensee shall not be given the benefit of refixation of EO as given in Para 5.4 (i) of the Policy.

Remarks : New relaxation introduced. With such provisions how do you expect early fulfilment? Total period of export obligation will be 8+2+5 = 15 years.

In cases where an enhanced EO is imposed on the licence holder for granting such extension, he shall give an additional BG to the extent of the proportional duty saved to the enhanced EO imposed to the licensing authority concerned in addition to extending the validity of BG/LUT submitted at the time of initial imports. No exemption from BG shall be granted to any category of exporter under this Clause.

The extension in export obligation period shall be subject to such terms and conditions as may be prescribed by the competent authority. Wherever the export obligation period is extended, the licence holder shall be required to maintain

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average export obligation during the extended period as well."

Remarks : BG for everybody for such extension.

PARA 5.12 – Export Obligation Shortfall

Amended "The regional licencing authority may also consider condonation of shortfall upto 5% in the export obligation within the validity of the export obligation period, subject to such terms and conditions as may be prescribed by them."

Remarks : The shortfall can be condoned if it falls under the validity of the EOP.

PARA 5.14 – Regularisation of Bona fide Default
Second sentence added "This facility of payment of interest @15% shall be available to all pending cases of regularisation of EPCG licences irrespective of the date of its issuance"

Remarks : Relaxation for old cases.

PARA 5.16 – Re- Export of Capital goods

Last sentence added "However, in such cases the licence holder shall fulfill the balance export obligation under the Licence from export of alternate products/services or the licence holder shall pay duty equivalent to a proportionate amount of duty saved to the unfulfilled export obligation under the licence"

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Remarks : Totally un-understandable. In fact, there should be a provision for refund of duty collected with certain cuts. Also contrary to the provisions of export obligation period. In normal circumstances, when capital goods are re-exported within three years, drawback is available (Customs Notification No. 36-Cus (NT) Dtd. 26.05.1995), then why this condition? Needs reconsideration.

PARA 5.18.2 – Clubbing of EPCG licences

Instead of "Appendix 9C", "Aayaat Niryaat Form" has been substituted. Conditions (a) and (c) are deleted"

(a) The EPCG licences have been issued during the same licencing year,

(c) The EPCG licences must be for the export of the same product(s) or same services."

Remarks : Now the licences can be clubbed even if they are issued in different licensing years and even if the licences pertain to different products or services.

PARA 5.18.4 –

Last sentence added "However, in cases where the clubbed CIF/duty saved value exceeds Rs 100 crore, no corresponding benefit of increase in export obligation period shall be admissible."

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Remarks : Restrictive provision for big value imports under EPCG.

PARA 5.18.6 –

Amended "No clubbing would be permitted in the case of expired EPCG licences. In case any specific (as against general extensions under Para 5.11) export obligation extension has been given for any EPCG licence, the same licence cannot be considered for clubbing."

Remarks : Restrictive provision.

PARA 5.19 – Refixation of Export obligation

Point (a) - Instead of "Appendix 9D", "Aayaat Niryaat Form" has been substituted.

Point (b) deleted "In case of all EPCG licences where the application is made for re-fixation within two years of its issuance, the export obligation shall be automatically refixed based on 8 times the duty saved on the date of issuance of licence."

Point (c) – amended "For all EPCG licences, the licence holder should have fulfilled the mandated (original or extended, as the case may be) blockwise export obligation at the end of the block in which the application is made. This facility is extended to the applications made in the extended

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export obligation period as well. However, in such cases, extended export obligation period would be treated as the last block for the purpose of EO re-fixation. In all such cases, the refixed export obligation would be computed as under:

(% export obligation unfulfilled) x (8) x (duty saved on the date of issuance of the licence)". The words in bold are added. Earlier example as given in second sentence has been deleted "For example if the licence holder applies in the 3rd-4th year block for an EPCG licence with an export obligation period of 8 years, he should have fulfilled 15% of the original export obligation."

Remarks : This will improve your mathematical ability. But ultimately all this amounts to half-hearted approach which results in more complications.

Point (d) amended "In cases where the remaining original export obligation period (and not the extended export obligation period) of the EPCG licence is less than 2 years on the date of application for refixation, and the mandated (original or extended, as the case may be) blockwise export obligation has been fulfilled, the export obligation would be refixed at two times the duty saved on the date of issuance of licence.". The words in bold are added.

Point (f) - Instead of "Appendix 9D", "Aayaat Niryaat Form" has been substituted.

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PARA 5.22 – New para added
Revalidation of licences issued under EPCG scheme shall not be allowed.

Remarks : Another restriction.

*General remarks:*

1. The government has taken liberal approach in extension of EOP, clubbing provisions and doing away with installation certificate. However, in practice this will ultimately result in non fulfillment of EO within stipulated period.

2. The maintenance of annual average still continues. In the changed scenario, this does not seem practical. Issues like replacement of machineries which are not ultimately adding to installed capacity are still unresolved.

3. When the duty difference is only 10% (CVD being cenvatable), the imposition of penalty of export obligation even when capital goods are re-exported because of defect is un-understandable.

4. With all the extensions of EOP as provided under the FTP, the total period taken into account is 15 years from now. Once duty on capital goods becomes 5% latest by 2007, the

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scheme itself may not have any value. The imposition of additional EO after a period of 8 years therefore seem impractical.

5. Ultimately this is a result of half hearted approach.

*Chapter 6 – FTP Export Oriented Units(EOUs), Electronics Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) and Bio-Technology Parks (BTPs)*

The following paras have been added / amended as under

PARA 6.2 - Export and import of goods

Point (f) – Second sentenced amended as "Units obtaining gold/silver/platinum from the nominated agencies shall export gold/silver/platinum jewellery within 90 days from the date of release". Earlier it was 60 days.

Remarks : More time provided.

PARA 6.6 - Letter of Permission/ Letter of Intent and Legal Undertaking –

Point (a) – First sentence – Alongwith "Development Commissioner", "designated officer" has been added. Earlier sentence

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"Standard format for the extension of LOP is given at Appendix MM" has been deleted.

Investment criteria (d) – Last sentence deleted "Sector-wise investment criteria shall be fixed by BOA."

PARA 6.8 - DTA Sale of finished products/ rejects waste/scrap/ remnants and by-products

Point (d) – First sentence amended as "Unless specifically prohibited in the LOP, rejects within a overall limit of 50% may be sold in the Domestic Tariff Area (DTA) on payment of duties as applicable to sale under paragraph 6.8(a) on prior intimation to the Customs authorities". Words in bold are added.

Point (k) amended as "In case of new EOUs, advance DTA sale will be allowed not exceeding 50% of its estimated exports for the first year except the pharmaceutical units where this will be based on its estimated exports for the first two years."

Remarks : Pharma EOU can get higher DTA sale permission in the initial year. However, subject to adjustment later.

PARA 6.9 - Other Supplies in DTA

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Point (a) – Part of the sentence amended "DFRC under the duty exemption / remission scheme". The words in bold added.

Point (d) – Instead of "warehouses in Free Trade and Warehouse SEZ", "free trade and warehousing zones" has been substituted.

Remarks : Mistake corrected.

PARA 6.11 - Entitlement for supplies from the DTA

Point (c) (iii) – Earlier point deleted. "Reimbursement of Central Excise Duty/ additional excise duty paid on bulk tea procured from licenced auction centres"

Point (c) (v) – amended "CENVAT Credit on service tax paid." Earlier point was "Exemption from payment of service tax."

Remarks : Exemption not acceptable to MoF. CENVAT credit either will have to be utilized for payment of duties on DTA sale or refund will have to be claimed.

PARA 6.12 - Other Entitlements

Point (c) – Earlier point deleted. "An Offshore Banking Unit will extend credit on the same terms and condition as extended to units to SEZ"

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PARA 6.13 - Inter Unit Transfer

Point (b), amended "Capital goods may be transferred or given on loan to other EOU/EHTP/STP/BTP/SEZ units with prior intimation to the concerned Development Commissioner and Customs authorities."

Remarks : Earlier it was permission from DC and intimation to customs authorities. Now it is intimation to both DC and customs authorities.

PARA 6.14 - Sub-Contracting

Point (b) (i) – "For such exports, the DTA units will be entitled for refund of duty paid on the inputs by way of All Industry Rates of drawback/ Brand Rate of duty drawback." Words in bold have been deleted.

Remarks : Since brand rate is fixed only after verification, this deletion is justified.

PARA 6.15 - Sale of Un-utilised Material

Point (c) amended – "In the case of textile sector , disposal of leftover material/fabrics upto 2% of CIF value or quantity of import whichever is lower, on payment of duty on transaction value may be allowed, subject to certification of central excise/custom officers certify that these are leftover items." The word in bold is deleted.

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Remarks : Correctly deleted as the word 'certification' has already been used. No actual change.

PARA 6.16 - Reconditioning Repair and Re-engineering

Last sentence amended "The provisions of paragraphs 6.8, 6.9, 6.10, 6.13, 6.14 of policy and para 6.29 of Handbook shall not, however, apply to such activities." Paras have now been correctly specified. The words '6.15' of policy has been deleted and '6.13' has been added. Instead of 'Chapter 6 of Handbook of Procedures Vol.I, 'Para 6.29 of Handbook of Procedures Vol.I' has been specified.

PARA 6.17 – Replacement / Repair of imported / Indigenous Goods

Point (a) – First sentence amended "The general provisions of the Policy relating to export / import of replacement / repair of goods would also apply equally to EOU/EHTP/STP/BTP units."

Remarks : Correct language used.

PARA 6.18 – Exit from EOU Scheme

Point (e) amended "The unit proposing to exit out of the EOU scheme shall intimate the Development Commissioner and Customs and Central Excise authorities in writing. The unit

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shall assess the duty liability arising out of debonding and submit the details of such assessment to customs and Central Excise authorities. The Customs and Central Excise authorities shall confirm the duty liabilities on priority basis. After payment of duty and clearance of all dues the unit shall obtain "No Dues Certificate" from the Customs and Central Excise authorities. On the basis of No dues certificate so issued by the Customs and Central Excise authorities, the unit shall apply to the Development Commissioner for final debonding. In case there is no proceeding pending under FT(DR) Act 1992, the Development commissioner shall issue final debonding order within a period of 7 working days. During the period between "No dues certificate" issued by the Customs and Central Excise authorities and the final debonding order by the Development Commissioner, the unit shall not be entitled to claim any exemption for procurement of capital goods or input. The unit can however, claim Advance License / DFRC / DEPB / Duty Drawback."

Remarks : Very good provision. This should ease the procedural problems.

Point (f) – In the second sentence "as a DTA unit" has been deleted. It has been correctly deleted to avoid duplication.

PARA 6.19 – Conversion

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Point (a) – "Section 10A" alongwith Section 10B of Income Tax has also been added.

*Chapter 6 – HB Export Oriented Units (EOUs), Electronics Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) and Bio-Technology Parks (BTPs)*

The following paras have been added / Amended as under

PARA 6.7 – Conditions of Import

Point (a) – Last sentence added "The granite sector would also be allowed to take spares upto 5% of the value of the Capital Goods to the quarry site."

Remarks : Earlier only capital goods were permitted. Now spares are also included – logical.

PARA 6.16 – Transfer of Power from one unit to another

Amended "Transfer of power from Captive Power plants (DG Sets) from one unit of EOU/EHTP/STP/BTP to another is permitted as prescribed in sector specific condition in Appendix 14 IC".

Remarks : Subject to specific conditions, transfer of power is permitted. Earlier there were no conditions.

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PARA 6.21.1 – Sub- contracting

Point (d) – Amended "EOUs shall be eligible for wastage as applicable as per para 4.56 of Handbook for sub-contracting and against exchange." Words in bold are added.

Remarks : Wastage norms for gold/silver/platinum as permitted under DES stands extended to sub-contracting.

PARA 6.29.4 – New Para added

"An EOU on the basis of records maintained by them and on prior intimation to customs authorities may send samples to other EOUs for display on returnable basis within a period of 30 days"

Remarks : Time limit fixed for bringing back the samples.

PARA 6.39.10 – Fast Track Clearance Procedure – PARA DELETED

The status holder units shall be eligible for factory stuffing without any permission.

PARA 6.39.11 - Fast Track Clearance Procedure - PARA DELETED

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The clearance of samples and temporary removal of Capital Goods and parts for repair shall be allowed on self-certification basis.

PARA 6.39.12 - Fast Track Clearance Procedure - PARA DELETED

Sub-contracting shall be based on prior intimation of the process and the details of the sub contractor on annual basis to the jurisdictional Assistant Commissioner/Deputy Commissioner of Central Excise. Provisions of Circular 65/2002-Cus in terms of taking samples, retention of samples and the finished goods received from job-worker and period restriction of 30 days shall not be applicable to the Status Holder EOUs.

PARA 6.39.13 - Fast Track Clearance Procedure - PARA DELETED

In respect of the following activities of a status holder EOU, permission will not be required from the Development Commissioner/jurisdictional Central Excise Authorities and instead unit shall be required to send prior intimation :-

(i) import of capital goods (ii) installation of fax machine (iii) laptop from outside the approved premises (iv) DTA Sale of finished products (v) Inter Unit Transfer (vi) Sub-contracting (vii) Participation in Exhibitions (viii) Personal carriage of Gems & jewellery for export promotion

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tours (ix) Replacement/repair of imported indigenous goods (x) Supply of sale of samples (xi) Sale of unutilized material.

Remarks : This deletion is because MoF did not agree to these provisions.

New provisions represented by the industry pertaining to Fast Track which are not so far accepted:

- Video projection systems and video conferencing systems to be allowed w/o prior intimation to Customs and Excise
- Time period for approval of matters like issue of CT 3 / procurement certificate should be specified
- Instead of prior permission prior intimation to jurisdictional authorities for sub-contracting should be allowed

*Chapter 7 – FTP Special Economic Zones*

The following paras have been added / amended as under

NOTE : Fourth sentence amended "The proposed legislation on SEZs to be enacted in the near future would cover the concepts of the developer

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and co- developer , incorporate the provision of virtual SEZs, have fiscal concessions under the Income Tax and Customs Act, provide for Offshore Banking Units (OBUs) etc ." The words in bold are deleted

Remarks : Since SEZ Bill is presented to Parliament, there is no need of this sentence.

PARA 7.8 – DTA Sales and Supplies
Point (c) (iii) amended "Supplies to other EOU/SEZ/ EHTP/ STP/BTP units provided that such goods or services are permissible to be procured/rendered by these units."

Point (c) (vii) - Instead of "Appendix 14-II", "Appendix 14-IC" has been substituted.

PARA 7.9 - Entitlement for Supplies from the DTA

Point (b) (iii). Earlier point deleted. "Reimbursement of Central Excise Duty, paid on bulk tea procured from the licenced auction centres by the Development Commissioner of concerned zone as long as levy on bulk tea in this regard is in force."

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Remarks : This has been properly corrected.

PARA 7.12 - Sub- Contracting

Point (b) (i) – First sentence amended "Goods, finished or semi-finished, including studded jewellery, taken outside the zone for sub-contracting shall be brought back to the unit within 90 days." Earlier it was 30 days.

Point (f) - Instead of "Appendix 14-II", "Chapter 7" has been substituted.

Remarks : This has been properly corrected.

*Chapter 7 – HB Special Economic Zones*

The following para has been deleted as under

PARA 7.17.3 - Entitlement for Supplies from the DTA
Point (c) – Earlier point deleted "Reimbursement of Central Excise Duty, including additional excise duty, if any, paid on bulk tea procured from licenced auction centers by Development Commissioner of concerned Zone so long as levy on bulk tea in this regard is in force. The unit shall submit documentary evidence showing that the tea was procured from licenced auction centers along with the claim."

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Remarks : Because of new provisions of tea exports announced by Public Notice No. 67 Dtd. 02.04.05 and Notification No. 31 Dtd. 02.04.05.

*Chapter 8 – FTP Deemed Exports*

The following paras have been added as under

PARA 8.4.1 - Benefits to the Supplier – NEW PARA ADDED

(i) In respect of supplies made against Advance Licence in terms of paragraphs 8.2(a) of the Policy, the supplier shall be entitled to Advance Licence for intermediate supplies.

[Earlier first sub-para of 8.2 of old HB transferred here with amendments]

(ii) If the supplies are made against Advance Release Order (ARO) or Back to Back Letter of Credit issued against Advance Licence in terms of paragraphs 4.1.11 and 4.1.12 of the Policy, supplier shall be entitled to the benefits listed in paragraphs 8.3(b) and (c) of the Policy, whichever is applicable.

[Earlier second sub-para of 8.2 of old HB transferred here with amendments]

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(iii) If the supplies are made against Advance Release Order (ARO) or Back to Back Letter of Credit issued against DFRC, the supplier shall be entitled to the benefit listed in paragraph 8.3(b) of the Policy. [Earlier third sub-para of 8.2 of old HB transferred here with no changes]

Remarks : Only drawback to be claimed against ARO or Back to Back Letter of Credit.

PARA 8.4.2 – NEW PARA ADDED

In respect of supply of goods to EOU/ EHTP/ STP/BTP in terms of paragraphs 8.2 (b) of the Policy, the supplier shall be entitled to the benefits listed in paragraph 8.3(a),(b)and (c) of the Policy, whichever is applicable.
[Earlier Para 8.2.1 of old HB transferred here with no changes]

PARA 8.4.3 – NEW PARA ADDED

In respect of supplies made under paragraph 8.2(c) of the Policy , the supplier shall be entitled to the benefits listed in paragraph 8.3(a), (b) and (c), of the Policy, whichever is applicable.
[Earlier Para of 8.2.2 of old HB transferred here with no changes]

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PARA 8.4.4 – NEW PARA ADDED

(i) In respect of supplies made under paragraphs 8.2 (d), (f) and (g) of the Policy, the supplier shall be entitled to the benefits listed in paragraphs 8.3(a), (b) and (c),whichever is applicable.
[Earlier Para of 8.2.3 of old HB transferred here with no changes]

(ii) In respect of supplies mentioned in paragraph 8.2(d), supplies to the projects funded by such agencies alone, as may be notified by Department of Economic Affairs, Ministry of Finance, shall be eligible for deemed export benefits. A list of such agencies/ funds is given in Appendix-13 of Handbook (Vol.I).
[Earlier second sub para of 8.4.3 of old HB transferred here with amendments]

(iii) The benefits of deemed exports under para 8.2(f) of the Policy shall be applicable in respect of items, import of which is allowed by the Department of Revenue at zero customs duty subject to fulfillment of conditions specified under Notification No.21/2002-Customs dated 1.3.2002, as amended from time to time.
[Earlier Para of 8.4.5 of old HB transferred here with no changes]

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(iv) Supply of Capital goods and spares upto 10% of the FOR value of the capital goods to the power projects in terms of paragraphs 8.2(g) shall be entitled for deemed export benefits provided the International Competitive Bidding procedures have been followed at Independent Power Producer (IPP)/Engineering and Procurement Contract(EPC) stage. The benefit of deemed exports shall also be available for renovation/ modernization of power plants. The supplier shall be eligible for benefits listed in paragraph 8.3(a) and (b) of the Policy, whichever is applicable. However , supply of goods required for setting up of any mega power projects as specified in S.No. 400 of Department of Revenue Notification No.21/2002-Customs dated 1.3.2002, as amended, shall be eligible for deemed exports benefits as mentioned in paragraph 8.3(a), (b) and (c) of the Policy, whichever is applicable, if such mega power project is –

(a) an inter state thermal power plant of capacity of 1000 MW or more; or

(b) an inter state Hydel power plant of capacity of 500 MW or more.

[Earlier Para of 8.4.6 of old HB transferred here with no changes]

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(v) Supplies under paragraph 8.2(g) of the Policy to the new refineries being set up during the Ninth plan period and spilled over to the Tenth plan period shall be entitled for deemed export benefits in respect of goods mentioned in list 17 specified in S.No.228 of Notification No.21/2002-Customs dated 1.3.2002, as amended from time to time.
[Earlier Para of 8.4.7 of old HB transferred here with no changes]

PARA 8.4.5 – NEW PARA ADDED

In respect of supplies made under paragraph 8.2(e) of the Policy, the supplier shall be eligible for the benefits listed in paragraph 8.3(a) and (b) of the Policy, whichever is applicable. The benefit of deemed exports shall be available in respect of supplies of capital goods and spares to fertilizer plants which are set up or expanded/ revamped/ retrofitted/modernized during the Ninth Plan period. The benefit of deemed exports shall also be available on supplies made to Fertilizer plants, which have started in the 8th /9th Plan periods and spilled over to the 10th Plan period.
[Earlier Para 8.2.4 and 8.4.4 of old HB transferred here with no changes]

PARA 8.4.6 – NEW PARA ADDED

The supplies of goods to projects funded by UN agencies covered under Para 8.2(i) of the Policy

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are eligible for benefits listed in paragraph 8.3(a) and (b) of the Policy, whichever is applicable
[Earlier Para of 8.2.5 of old HB transferred here with no changes]

PARA 8.4.7 – NEW PARA ADDED

In respect of supplies made to nuclear Power Projects under para 8.2(j) of the policy, the supplier would be eligible for benefits given in para 8.3 (a), (b) and (c) of the Policy, whichever is applicable. Supply of only those goods required for setting up any nuclear power project specified in list 43 at S.No.401 of Notification No.21/2002-Customs dated 1.3.2002,as amended from time to time having a capacity of 440 MW or more as certified by an officer not below the rank of Joint Secretary to the Government of India in the Department of Atomic Energy shall be entitled for deemed exports benefits in cases where the procedure of competitive bidding (and not international competitive bidding) has been followed.
[Earlier Para 8.2.6 and 8.4.8 of old HB transferred here with amendments]

PARA 8.5 - Eligibility for refund of terminal excise duty/drawback - NEW PARA ADDED

Supply of goods will be eligible for refund of Terminal Excise Duty in terms of para 8.3 (c) of Policy provided the recipient of the goods does not avail CENVAT credit /rebate on such goods.

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Similarly, supplies will be eligible for deemed export drawback in terms of para 8.3(b) of Policy on the Central Excise paid on inputs /components, provided CENVAT credit facility/rebate has not been availed by the applicant. Such supplies will however be eligible for deemed export drawback on the customs duty paid on the inputs/components.
[Earlier Para of 8.3.1 of old HB transferred here with no changes]

PARA 8.6.1 - Supplies to be made by the main/sub-contractor - NEW PARA ADDED

In all cases of deemed exports, supplies shall be made directly to the designated Projects/ Agencies/ Units/ Advance Licence / EPCG licence holders. The sub-contractor may, however, make the supplies to the main contractor as per paragraph 8.4 of Handbook instead of designated projects/ agencies.
[Earlier Para of 8.3 of old HB transferred here with amendments]

PARA 8.6.2 – NEW PARA ADDED

Supplies made by an Indian sub-contractor of an Indian or foreign main contractor, shall also be eligible for deemed export benefits provided the name of the sub-contractor is indicated either originally or subsequently in the contract, and payment certificate is issued by the project

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authority in the name of the sub-contractor in the form given in Appendix 22C of Handbook (Vol.I). [Earlier first sub para of 8.5 of old HB transferred here with amendments]

*Chapter 8 - HB Deemed Exports*

PARA 8.1 – Policy – No change

PARA 8.2 – Benefits to the Supplier – Deleted.
In respect of supplies made against Advance Licence in terms of paragraphs 8.2(a) of the Policy, the supplier shall be entitled to Advance Licence for intermediate supplies.

(i) If the supplies are made against Advance Release Order (ARO) or Back to Back Letter of Credit issued against Advance Licence, in terms of paragraphs 4.1.11 and 4.1.12 of the Policy, supplier shall be entitled to the benefits listed in paragraphs 8.3(b) and (c) of the Policy, whichever is applicable.

(ii) However, in such cases where Advance Release Order (ARO) or Back to Back Letter of Credit has been issued against DFRC, in terms of paragraphs 4.1.11 and 4.1.12 of the Policy, supplier shall be entitled only to the benefit listed in paragraph 8.3(b) of the Policy.
[Transferred to 8.4.1 of new FTP with amendments]

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PARA 8.2.1 –

In respect of supplies under Paragraph 8.2(a) of the Policy, the procedure for issue of ARO and Back-to-Back Inland Letter of Credit is given in paragraphs 4.14 and 4.15 of the Handbook.
[Earlier Para 8.4(i) of old HB transferred here with amendments]

PARA 8.2.2 -

In respect of supplies under paragraph 8.2(b) of the Policy and DFRC, the deemed export benefits may be claimed from the Development Commissioner or the Licensing Authority concerned. Advance Licence and DFRC shall be claimed from the concerned licensing authority. Such supplies shall be certified by the receiving agencies.
[Earlier Para 8.4.1 of old HB transferred here with amendments]

PARA 8.2.3 -

In respect of supply of capital goods under paragraph 8.2 (c) of the Policy, the supplier shall produce a certificate from the EPCG License holder evidencing supplies/ receipt of the manufactured capital goods.
[Earlier Para 8.4.2 of old HB transferred here with amendments]

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PARA 8.2.4 -

In respect of supplies under categories mentioned in paragraphs 8.2(d),(e),(f),(g), (i) and ( j ) of the Policy, the application for advance licence shall be accompanied with a project authority certificate in Appendix - 27. The payment against such supplies shall be certified by the Project Authority concerned in the prescribed format in Appendix-22C.
[Earlier Para 8.4.3 of old HB transferred here with amendments]

PARA 8.2.5 - Deleted

The supplies of goods to projects funded by UN agencies covered under para 8.2(i) of the Policy are eligible for benefits listed in paragraph 8.3(a) and (b) of the Policy, whichever is applicable.
[Transferred to 8.4.6 of new FTP with no changes]

PARA 8.2.6 – Deleted

In respect of supplies made to Nuclear Power Projects, the supplier would be eligible for benefits given in para 8.3(a), (b) and (c) of the Policy , whichever is applicable.
[Transferred to 8.4.7 of new FTP with amendments]

PARA 8.3 – Deleted

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In all cases of deemed exports, supplies shall be made directly to the designated Projects/ Agencies/ Units/ Advance Licence/EPCG licence holders. The sub-contractor may, however, make the supplies to the main contractor as per paragraph 8.5 instead of designated projects/ agencies.
[Transferred to 8.6.1 of new FTP with amendments]

PARA 8.3.1 – Procedure for claiming deemed exports drawback and terminal excise duty refund / exemption from payment of terminal excise duty

The procedure for claiming benefits under paragraph 8.3 (b) and (c) of the Policy shall be as under:-

(i) An application in the Aayaat Niryaat form along with the documents prescribed therein, shall be made by the supplier to the Regional Licensing Authority concerned. The recipient may also claim the benefits on production of a suitable disclaimer from the supplier along with a self declaration in Appendix 22C of Handbook regarding non-availment of CENVAT credit in addition to the prescribed documents.

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[Earlier first sub - para of 8.6 of old HB transferred here with amendments]

(ii) In case of supplies under paragraph 8.2(a), (b) & (c), the claim shall be filed against receipt of payment through normal banking channel in the form given in Appendix – 22B. Such claims shall be filed within a period of 6 months from the last date of the month of receipt of payment.
[Earlier second sub - para of 8.6 of old HB transferred here with amendments]

(iii) In respect of supplies under paragraph 8.2(b) of the Policy where the supplier wants to claim benefits from the licensing authority, the Licensing Authority while allowing deemed export benefits to the DTA supplier, will endorse a copy of the communication to the concerned Development Commissioner along with the details of invoices against which deemed export benefits have been allowed for confirmation of the transaction involved.
[Earlier third sub - para of 8.6 of old HB transferred here with no changes]

(iv ) In respect of supplies under categories mentioned in Paragraphs 8.2(d )( e )(f ) (g ) (h) ( i ) &( j ) of the Policy, the claim may be filed for the payment received/supplies effected during a particular month/quarter/half year as per the option of the applicant either on the basis of proof

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of supplies effected or payment received. The claim may be filed either against a particular project or all the projects. Such claims shall be filed within a period of 6 months from the end of monthly/quarterly/half yearly period reckoned from the date of receipt of the supplies by the project authority or from the date of receipt of the payment as per the option of the applicant. Such claims may also be filed where part payments have been received.
[Earlier para 8.6.1 of old HB transferred here with amendments]

PARA 8.3.2 – NEW PARA ADDED

For claiming exemption from payment of terminal excise duty, procedure prescribed by the Central Excise Authority shall be followed.
[Earlier para 8.6.2 of old HB transferred here with no changes]

PARA 8.3.3 – NEW PARA ADDED

Where All Industry Rate of Drawback is not available or the same is less than 4/5th of duties actually paid on the materials or components used in the production or manufacture of the said goods, the exporter/ supplier may apply for fixation of brand rate in the application form as given in Aayaat Niryaat form to the regional licensing authority or Development Commissioner as the case may be.

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[Earlier para 8.6.3 of old HB transferred here with amendments]

PARA 8.3.4 – NEW PARA ADDED

The claim application shall be filed along with the application for fixation of brand rate of duty drawback in case brand rate is required to be fixed. The provision of late cut under paragraph 9.3 and supplementary claim under paragraph 9.4 shall also be applicable under this sub-paragraph.
[Earlier para 8.6.4 of old HB transferred here with no changes]

PARA 8.3.5 – NEW PARA ADDED

Regional Licensing Authorities may consider provisional payment to the extent of 75% of the drawback claim in the case of private companies and 90% in the case of Public Sector Undertakings, pending fixation of Brand Rate.
[Earlier para 8.6.5 of old HB transferred here with no changes]

PARA 8.3.6 – NEW PARA ADDED

Subject to the procedure laid down in this Handbook, the Customs and Central Excise Duty Drawback Rules, 1995 shall apply mutatis mutandis to deemed exports.

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[Earlier para 8.6.6 of old HB transferred here with no changes]

PARA 8.4 – Procedures for claiming Deemed Exports Benefits by sub-contractor – Heading amended

In respect of supplies made by sub-contractor to the main contractor under paragraph 8.2 (d)(e) (f) (g)(i) and (j), the main contractor may make payment to the sub-contractor and issue payment certificate in the form given in Appendix-22C as Form 1-C. However, for supplies under paragraph 8.2(d) (e) (f) (g) and (j), the payment certificate from main contractor shall not be insisted for refund of Terminal Excise duty. The deemed exports benefits to the sub-contractor would be available to the extent of goods that are manufactured and supplied by him or outsourced from other manufacturers, for the value as indicated in Appendix 22C of the Handbook.
[Earlier second sub-para of 8.5 of old HB transferred here with amendments]

PARA 8.4 (ii) - Deleted

For the purpose of claiming deemed export benefits, if any, the indigenous supplier shall produce documentary evidence substantiating the realisation of proceeds from the recipient through the normal banking channel in the form given in Appendix-22A as well as a copy of ARO/ Non-

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negotiable copy of Back to Back Inland Letter of Credit.
[However, this provision does not find place any where in the new policy & procedure]

Remarks : Probably a mistake. Needs clarification.

*Chapter 9 – FTP Definitions*

The following paras have been added / amended as under

PARA 9.7 – 'AEZ'

"AEZ" means Agricultural Export Zones notified by DGFT in Appendix 8 of Handbook (Vol 1).". Instead of "Appendix 15", "Appendix 8" is substituted.

PARA 9.41 – 'NFE'

Amended "NFE" means Net Foreign Exchange Earning."
Earlier definition of NFEP was provided as "NFEP" means Net Foreign Exchange Earnings as a percentage of exports".

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