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Amendments by the Finance Act 2011 to levy minimum alternate tax and dividend distribution tax on units operating in special economic zones (SEZs) (including units engaged in development or operation or maintenance of SEZs) held to be constitutionally valid and in public interest

In brief

In a recent ruling by the Karnataka High Court (HC) in the case of Mindtree Ltd[1] (the taxpayer) (being one of the petitioners to the writ petition), the HC upheld an amendment by Finance Act (FA) 2011. Under this amendment, units located or engaged in development, operation or maintenance of special economic zones (SEZs) were made liable to pay minimum alternate tax (MAT) on its book profits and dividend distribution tax (DDT) on dividend distribution to shareholders (if it is a domestic company incorporated under Indian laws).This was held to be constitutionally valid and in the public interest.

Facts

- The government of India announced the SEZ policy in April 2000. Accordingly, the government sought domestic and foreign investment in India for making goods manufactured in the country competitive internationally.

- To overcome practical difficulties faced in the implementation of the SEZ policy and to foster confidence among prospective investors, the government

[1] Mindtree Ltd. *v.* Union of India [2013] 34 taxmann.com 250 (Karnataka)

introduced a well-integrated SEZ Bill which received the President's assent on 23 June 2005.

- Along with the SEZ Act, 2005, the government incorporated a specific provision in relation to SEZ units under the Income-tax Act, 1961 (the Act) through the FA 2005. It was specifically provided that liability in relation to MAT and DDT shall not arise on SEZ units.

- With this background of tax exemptions, investors invested in SEZs through extensive borrowings and incurred substantial costs.

- The government, faced with the problem of an eroded tax-base, withdrew the exemptions related to MAT and DDT, previously available under the FA 2005, by the FA 2011.

  The petitioners contended that withdrawal of the MAT and DDT exemption affected or would affect cash inflows of SEZ units. This was not expected when investment decisions were planned.

- Aggrieved by this amendment, the petitioners moved a writ petition before the HC challenging the constitutional validity of these amendments.

Issue before the HC

- Whether the withdrawal of tax exemptions available to the SEZ units, (concerning MAT and DDT) effective 1 April 2011 (i.e. financial year 2011-12) is constitutionally valid

Tax payer's contentions

- The government had, at the time of instituting the SEZ Act, promised investors that the MAT and DDT liability would not arise on SEZ units. Accordingly, withdrawal of this exemption is opposed to the doctrine of promissory estoppel.

- The withdrawal of this exemption would make exports less competitive in the international market. Therefore, this amendment is against the basic objective of the SEZ Act.

- The Finance Minister has no power to make amendments to the SEZ Act, which comes under the purview of the Ministry of Commerce.

Revenue's contentions

- The tax laws providing exemption to SEZ units from MAT and DDT did not have a sunset provision and as such the impugned amendments are in accordance with the Indian Constitution.

- The amendments are not hit by the doctrine of promissory estoppel.

- The amendments were made to stabilise the country's tax base and were issued in the public interest. The exemption provided to the SEZ units resulted in its erosion.

HC's ruling

- The HC, in accordance with the mechanism of judicial review of laws passed by the Indian Parliament, observed that a finance minister under the Ministry of Finance has complete powers to amend the SEZ Act even though it comes under the Ministry of Commerce. The HC further observed that the said powers are derived from the Rules of the Lok Sabha which specify that "minister" includes any minister and as such the Finance Minister is competent to move a bill seeking amendment to the SEZ Act.

- The HC endorsed the view of the Supreme Court in the case of Madurai District Central Cooperative Bank Ltd[2] that depending upon the exigencies of

[2] Madurai District Central Cooperative Bank Ltd *v.* ITO [1975] 101 ITR 24 (SC)

the financial year, the Parliament of India has the legislative competence to introduce a new charge of tax even by incorporating it in any statute other than the Act.

- The HC observed that the amendment was brought in to set apart the inequality between the SEZ units and non-SEZ units. Furthermore, it observed that no fundamental rights of any of petitioners as bestowed upon them by the Constitution are infringed as a result of the various amendments. It further observed that the social and economic matters of a country are very complicated and they require experimental decisions which may be deregulated again in public interest.
- The HC observed that the doctrine of promissory estoppel does not preclude the Legislature from exercising its legislative powers.
- The amendments made in MAT and DDT provisions are in accordance with the Article 14[3] of the Indian Constitution.

Conclusion

The HC has laid down an important principle that the doctrine of promissory estoppel does not apply to the Legislature and that the Finance Minister has complete authority and power to amend the provisions of the SEZ Act. The HC held that the withdrawal of exemptions related to MAT and DDT is constitutionally valid.

[3] Article - 14. Equality before law:- The State shall not deny to any person equality before the law or the equal protection of the laws within the territory of India Prohibition of discrimination on grounds of religion, race, caste, sex or place of birth

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