

Policy for India's Services Sector

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Abstract

Services sector has been particularly important for India. This paper focuses on the major policy issues for India's services sector. In the beginning, the paper dwells briefly on the importance of services for India in terms of GDP growth, services export growth and openness of the economy; the country-wise exports of services of India; and the important services for India. The paper then directly examines the major policy issues under three major headings: domestic policy issues, domestic regulations and market access issues.

Domestic policy issues cover many areas like FDI, disinvestment, tariff & trade, credit & finance and other general & sector-specific policy issues. FDI related policy measures include putting the FDI policy on the website in a user-friendly way and opening atleast some segments of insurance sector like health insurance. Policies for disinvestment include a listing of PSUs in services sector for disinvestment. Tariff and tax related policy measures include many suggestions like rationalisation of taxes in shipping and telecom sectors, allowing advance tax instead of TDS in some services and a single return for service tax and excise tax which is being administered by the same department. Credit & finance related issues include exempting External Commercial Borrowings (ECBs) from withholding tax for financing export-related activities and overseas acquisition including acquisition of ships. Other general and sector specific issues include among others increasing visibility of India in services, facilitating services exports by setting up joint offices with common facilities, setting up a portal for services, resolving the issue of preconditions in overseas tenders, facilitating international accreditation for Indian health services and skill certifying unskilled labour.

Domestic regulations perform the role of tariffs in regulating services. So the paper underlines the need to list domestic regulations in India which need to be disciplined to help the growth of the services sector and exports, while retaining those domestic regulations which need to be retained at this stage. Some of the policy suggestions related to domestic regulations include addressing restrictions on inter-state movement of goods, resolving the issue of ban on use of logos of accounting firms, removing the unnecessary regulations under Banking Regulations Act and competition policy for services.

Market access issues include domestic regulations, subsidies and other barriers in India's major markets which deny market access for India's services exports. Some examples of such issues are dealt in this paper.

In the Executive Summary and Conclusion, the important reforms which need to be initiated and implemented in the short run are listed. The paper concludes that immediate and time-bound reforms in the services sector could not only help in attaining India's targeted GDP growth rates, but also give a fillip to growth and exports of this services-led-economy.

Foreword

The Economic Division in the Department of Economic Affairs has initiated a working paper series with the objective of improving economic analysis and promoting evidence based policy formulation. The themes to be covered in the series include both macroeconomic and sectoral issues of relevance for national policy, strategy for addressing emerging global and national development concerns, and the agenda for economic policy reforms.

The paper by Dr.H.A.C.Prasad and Mr.R.Sathish on Policy for India's services sector is the first working paper for 2010. This paper examines the major issues concerning India's services sector and gives both general and sector-specific policy suggestions.

Services sector plays a vital role in India for various reasons. The rate of growth of the Services sector GDP has been more than that of overall GDP in the recent time period. Even in 2008-09 when GDP growth was relatively low at 6.7%, service sector growth was 9.7% with its share in GDP at 57.3%. The primary importance of services sector in the growth process of India and most of the states of India has been strongly established in the last two decades. Despite global recession, services exports grew by a respectable 12.4 percent in 2008-09. The openness of the economy reflected by total trade including services as a percentage of GDP shows a remarkable increase from 27.4 percent in 2000-01 to 52.1 percent in 2008-09.

Some services have been particularly important for India. Software is one sector in which India has a brand identity. Tourism and travel related services and transport services are also major items in India's Services exports. Besides these, the potential services which are particularly important for India include many professional services, infrastructure related services and financial services. India also has great potential to be a major outsourcing destination for many services. However, to tap the full potential of the services sector, policy reforms are needed which have been covered in this paper under different headings such as domestic policy issues, domestic regulations, market access. I hope that this interesting and informative paper will contribute to the discussion and debate on the subject and help design policy.



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The views expressed in this paper are those of the authors and do not necessarily reflect the views of the Ministry of Finance or Government of India.

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Policy for India's Services Sector

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Executive Summary and Conclusion

Services sector is particularly important for India for various reasons. The ratcheting up of the trend rate of GDP growth of the economy reaching 9.4 per cent in 2006-07 was to a great extent due to the ratcheting up of the trend growth rate in the services sector of around 10 percent since 2004-05. Even in 2008-09 when GDP growth was relatively lower at 6.7 per cent due to global recession, services growth was at 9.7 per cent with its share in GDP at 57.3 per cent. State wise growth rate of GSDP is also closely associated with higher growth of tertiary sector. The primary importance of services sector in the growth process of India and most of the states of India has been strongly established in the last two decades. India is also moving towards a services dominated export growth. Even in 2008-09 when the merchandise export sector was severely affected by the global recession, services exports grew by a respectable 12.5 percent. The openness of the Economy reflected by total trade including services as a percentage of GDP shows a remarkable increase from 27.4 percent in 2000-01 to 52.1 percent in 2008-09.

2. Some services have been particularly important for India. Software is one sector in which India has a brand identity. Tourism and travel related services and transport services are also major items in India's Services exports. Besides these, the potential services which are particularly important for India include many professional services, infrastructure related services and financial services. India also has great potential to be a major outsourcing destination for many services, though this prospect has been threatened by the recent developments in US & EU limiting outsourcing.

Major Policy Issues

3. The major policy issues in the services sector are 1) the Domestic Policy Issues including FDI, Disinvestment, Tariff & Tax Issues, Credit & Finance related issues and Other Policy Issues – General & Sector Specific; 2)

Domestic Regulations-Sector Specific and General; 3) Market Access Issues due to domestic regulations, subsidies and other barriers; and 4) Other Issues like bilateral, regional and multilateral negotiations and policies of multilateral institutions. This paper focuses only on Domestic Policy issues and Domestic Regulations though a sample of issues under Market Access has also been given. Other issues like bilateral, regional and multilateral negotiations and policies of multilateral institutions have not been dealt here though they are interesting and emerging issues. The list of policies and regulations given here are also not exhaustive, though many important issues in different sectors have been covered.

Domestic Policy Issues

(i) Foreign Direct Investment (FDI)

4. Some important policy issues in the case of FDI in Services sector for India are the following:

- **Opening retail trade**, where FDI is prohibited (except single brand product retailing subject to 51% cap) while there is a large unorganized sector with low tax compliance. Along with allowing FDI in retail in a phased way beginning with metros, the existing mom and pop shops (kirana shops) could be incentivized to modernize and compete effectively with the retail shops foreign or domestic.
- **Raising FDI cap in the insurance sector** from 26% has been in the Government's agenda for long but could not be implemented for various reasons. Given the practical difficulty in raising FDI Cap in the insurance sector as a whole, atleast some segments of the Insurance sector can be opened up further. One such segment is health insurance and FDI cap at least in health insurance can be raised in India on a priority basis as it will also help the export of super-specialty hospital services. There is also a 10 year disinvestment clause in the insurance sector which could be removed. FDI restrictions in reinsurance sector could also be removed and foreign re-insurance companies should be allowed to set up their representative offices and function in India through a network of branches and divisions.
- **In the Banking sector** there is scope for further liberalisation. Though foreign investment (FDI+FII) of 74% is allowed, there are licensing requirements. There is also a limit of ten percent on voting rights in respect of banking companies. While many concerns have to be addressed here particularly in the light of the recent global financial crisis, atleast some segments of this sector could be opened up to foreign investment in areas like rural Banking with the help of mobile technology.
- **FDI in Animation studio** needs to be liberalized as there is good scope for this.

- **In Construction Sector**, though 100% FDI is allowed under automatic route, there are conditions like minimum capitalization norms of US\$10 million for wholly owned subsidiaries and US\$ 5 million for joint venture, minimum area norms under each project – 10 hectares in case of development of services, housing plots and built-up area of 50,000 sq. mts. in case of construction development project and any of the above in case of a combination project. Besides, original investment cannot be repatriated before a period of three years from completion of minimum capitalization. Some of these conditions could be relaxed.
- **For Uplinking News & Current Affairs TV Channel**, foreign investment cap is 26% (FDI+FII) under FIPB route and not automatic route. Besides there are conditions like the portfolio investment in the form of FII/ NRI deposits shall not be “persons acting in concert” with FDI investors, as defined in the SEBI regulations; the Company permitted to uplink the channel to certify the continued compliance of this requirement through the Company Secretary at the end of each financial year; etc. While the foreign investment cap could be raised atleast upto 49% in the case of these services, other conditions mentioned above need to be examined for relaxation.
- **Telecommunications:** In the case of ISP without gateway, the 26% disinvestment clause in 5 years to companies listed in other parts of the world could be relaxed.
- **Air Transport Services:** 49% FDI is allowed (100% for NRI Investment) subject to no direct or indirect participation by foreign airlines thus preventing those with experience from operating in this sector. Ministry of Civil Aviation’s initiative to liberalise this sector needs to be taken to its logical conclusion, while security concerns are also addressed
- **FDI in railways:** FDI is not allowed in railways. FDI upto 26% could be thought of which can help in modernization of railways.
- **Besides the above, the whole FDI policy should be made available in the website in a user friendly way. At present, one has to search in many places and different Press Notes to understand the FDI caps and other regulations for different sectors. This has also been highlighted in the Economic Survey 2009-10 and later in the Budget 2010-11 it has been stated that the Government intends to make the FDI policy user-friendly by consolidating all prior regulations and guidelines into one comprehensive document.**

(ii)Disinvestment

5. There is plenty of scope for disinvestment in the case of Public Sector Units (PSUs) in services sector under both the Central and State governments. Around 27 PSU’s in Services sector can be considered for disinvestment. These include Telecommunications Consultants of India Ltd., PEC Ltd., Engineers India Ltd., Water and Power Consultancy Services,

MSTC Ltd., National Building Construction Corporation, State Trading Corporation of India Ltd., MMTC Ltd. , Shipping Corporation of India Ltd., Balmer Lawrie & Co. Ltd., Mahanagar Telephone Nigam Ltd., Bharat Sanchar Nigam Ltd., Dredging Corporation of India Ltd., Cochin Shipyard Ltd., Goa Shipyard Ltd., Mazagon Dock Ltd., Hindustan Shipyard Ltd., India Trade Promotion Organisation, Indian Railway Catering and Tourism Corporation, Central Warehousing Corporation, IRCON International Ltd., RITES Ltd., Engineering Projects India Ltd., MECON Ltd., Educational Consultants India Ltd., National Research Development Corporation, National Film Development Corporation and Broadcast Engineering Consultants India Ltd. **Among these, SCI, NBCC, EIL, Balmer Lawrie & Company Ltd., Engineering Projects India Limited, STC, were earlier listed for strategic sales. However, in February, 2005, disinvestment through strategic sale of profit making CPSUs were called off as per the NCMP and the above companies continued as CPSUs. Now disinvestment of these companies can be initiated.** In the case of some of the companies there are some labour related issues and one company, namely, National Film Development Corporation is a loss making company. Among the 27 companies, **disinvestment could possibly be initiated immediately in the case of SCI, RITES, Engineers India Ltd., Engineering Projects India Ltd. and ITPO, STC & MMTC. In the case of NBCC and NFDC, there can even be full sale of the companies. In the case of ITPO, exporters and even Exim Bank of India could have a stake.** In the case of the companies, where there are issues related to labour, etc., some percentage of the government shares could be offloaded. The above disinvestments can, not only yield sizeable revenue for the government, but also make these companies more efficient contributing to the growth process.

(iii) Tariff & Tax related.

6. Some important tariff and tax related suggestions in different services which need to be examined and addressed to make Indian services more competitive compared to our competitors are the following:

Shipping Services:

- Strengthening Indian fleet by rationalising the taxes in Shipping Sector: Studies show a positive contribution by the Indian Shipping Industry to the Indian economy with a 1 per cent change in Gross Tonnage (GT) likely to bring about 0.0068 percent change in GDP. While trade has increased, India's Shipping has not kept pace with it. The strength of the Indian fleet is 9.3 million gross tonnage as on 01.04.2009. Out of this, about 4 million GT (or 44 per cent) are likely to be scrapped over the next 5 years due to the completion of commercial life as well as on account of IMO regulation for phasing out single hull tankers coming into force by 2010. This would require an estimated investment of US\$ 4 to 5 billion. Though the Indian

shipping industry has benefited due to the introduction of tonnage tax, Indian flag vessels are gradually diminishing and even Indian owners are increasingly opting to own vessels outside India by paying, virtually zero tax, employing shipboard personnel of any nationality, while accessing India's booming cargo base. Though 100 per cent FDI in shipping has been allowed since the late 90s, no worthwhile foreign investment has taken place due to the high taxes and rigid regulations like manning norms in India. Indian shipping is presently subjected to 12 direct/indirect taxes over and above the tonnage tax that add to its costs thereby increasing the effective tax rate of around 2 per cent under the tonnage regime to around 9 per cent. The 12 taxes are corporate income tax on interest and other income, minimum alternate tax (MAT) on profit on sale of vessels, dividend distribution tax, withholding tax liability on interest paid to foreign lenders, withholding tax liability on charter hire charges paid to foreign ship-owners, seafarer's taxation cost to employer, wealth tax, fringe benefit tax, sales tax/value added tax (VAT) on ship supplies/ spares, lease tax on charter hire charges, customs duty on import of certain categories of ships, stores, spares & bunkers and service tax. This calls for rationalization of the taxes in the shipping sector.

- Some tonnage tax issues: There are some issues related to tonnage tax which need to be addressed like modifying the definition of 'core' activities to treat the incomes arising from book-profit on sale of vessels as core activities under the Tonnage Tax (TT) regime and not subjecting it to MAT as is currently being done. Similarly interest income from compulsory reserves also needs to be treated as arising from 'core activities' of a tonnage tax company.
- Zero rating input services availed by the Indian shipping industry (either imported or domestically procured) as globally, input services for shipping industry are not subject to service tax. These services include brokerage, commission and finance charges, general insurance services including P&I insurance, ship management services; and manpower recruitment and supply agency services.
- Addressing the seafarers' taxation issue as Indian shipping companies face an acute shortage of seafarers, particularly in the officers' category because of drift of personnel from Indian flag ships to Foreign flag under lure of higher 'take home' pay packets, without having to pay tax in India.
- Exemptions from Customs Duty on direct import of repair materials by ship repair units and shipowners for repairs in India on import of vessels under H/S. 89.04, H.S. 89.0510 and H.S. 89.0590; and on capital goods imported for shipbuilding including renewals and replacements of yard facilities from customs duty (as in any yard having both ship building and ship repair facilities, most of the assets are common and the concessions extended to one activity alone may not serve the required purpose).

- Exemptions from Excise duty of 16 per cent on capital goods required for construction of ships as in the case of ship repair.
- Reinstating the exemption from withholding tax of 10 per cent on interest paid to ECBs to acquire ships abroad, withdrawn with effect from 1.06.2001. Similarly withholding tax on in-chartering of foreign vessels could be removed.

Tourism Services:

- Rationalizing the tax structure for tourism as the overall tax impact on tourism is around 30-35 per cent.
- Reduction in taxation on ATF which directly affects airfares. It is better to bring ATF under “Declared goods” which will reduce duty to 4 percent. While state governments are opposing this as it will lower their revenue, there is also concern that the benefits may not be passed on to the consumers. This needs to be sorted out and states convinced of the possible advantages due to increase in business volumes. This is a long term solution and better than the alternative to reduce sales tax on ATF by states ranging from 12 percent to 35 per cent as lower but widely varying rates may not end the problem.
- Rationalising state luxury tax at around 5 per cent which at present varies from 5 percent to 20 per cent in different states with some states charging not on the actual rate but on rack rates (published rate) which affect tourists when the former is lower than the latter.
- Introducing electronic system of tax payment for tourist vehicles with the help of swipe cards.
- Addressing the anomalies in the per seat passenger tax which affects tourist buses not plying with full capacity and penalizes buses carrying more passengers and reducing pollution compared to other vehicles like cars.
- Rationalising the fees for entry to monuments and using the fees for their maintenance. Private sector could also be allowed to maintain monuments and collect fees on the lines of toll taxes.

Entertainment Services:

- Tax credit issue: UK gives 25 percent tax credit for films i.e. 25 percent of expenditure of budget of films is rebated (though subject to a limit). Though this is actually a subsidy, it is disguised as tax credit and is not at all related to the usual taxes which have to be paid. This type of subsidy given by UK and other countries led to investment in film production in these countries. India does not give such benefits and many film producers of India produce films in UK to avail of this benefit and show only a part of their work from India where there is no benefit and taxes are high. The options with India are two. Either, give such tax credits and gain from huge investments along with multiplier effects while usual taxes can continue, or else, raise this issue in

the WTO and other fora as there is an unfair advantage for providers of these services in countries giving subsidies.

Aviation maintenance/repair Services:

- Addressing the issue of sales tax on aircraft parts imported by aircraft service companies. When a service centre imports aircraft parts into India, it is required to first pay an import duty (around 20-25%) and again when it sells these parts to an aircraft operator, a sales tax/VAT (around 10-13%) is applicable. Whereas if an aircraft operator directly imports aircraft parts, no sales tax/VAT is incurred and same import duty is payable only if the parts imported are meant for a private category aircraft. Exemption in sales tax applicable on imported aircraft parts sold by a service centre to aircraft operators and charging import duty only if parts are sold to private operators will help service centres in providing better support to its customers.
- Reducing the import duty for spare parts of Aircraft which is 20-25% for special tools and 30-35% for equipment as aviation repair/ maintenance are affected by it.
- Addressing the issue of turnover tax by Airport Authorities on service centres which are required to pay a turnover tax (currently @ 14%) to airport authorities on their revenue earned from services rendered to aircraft operators on air side of airport in addition to service tax payable to the Income Tax authorities.

Printing and Publishing Services:

- Exemption of customs duty on import of state-of-the art printing and allied machinery and equipment which are not being manufactured in India; on paper and paperboard of 10% (as printed materials can be imported at nil or much lower customs duty due to Bilateral Trade Agreements.)
- Exemption of central excise duty imposed on diaries, registers, labels etc. falling under Chapters 48.20 & 48.21, as both diaries and labels are primarily items of the printing industry and the printers will now be required to maintain separate cumbersome accounting records for (a) the dutiable goods and (b) the exempted goods and unless the concerned authorities are satisfied with the said records, the concerned printers would have to revert to 10% the value of the exempted goods as per provision of CENVAT credit rule, 2004.
- Addressing the Inverted duty issue in printing sector as paper and paperboard has higher duty and printed material has lower duty.

Engineering, Construction & Infrastructure Services:

- Taxing each members share of profits/losses instead of tax as Association of Persons since infrastructure construction contracts are generally executed through a prime contractor or a consortium of companies or established through Joint Ventures (JVs).
- Allowing advance tax instead of TDS as it creates a severe cash flow problem in a business where margins are low.
- Customs and Excise issue: To give a big boost to infrastructure projects, all imports including spares and parts, can be lowered or made duty free.
- Procedural changes: Liberal import of high tech equipment is permitted for infrastructure projects but the procedures require fine-tuning as indicated below:
 - Withdrawing the 5-year restriction on sale of imported equipments as these are expensive, having 10-15 years of useful life, but may be used for only 2-3 years in a project.
 - Allowing member companies of Joint Ventures to import duty exempt goods in their own name instead of in the name of JV, since these have to be held for 5 years as per policy, while a JV may cease after 23 years on completion of a project.
 - Extension of duty under project import to contractor's plant and machinery used for initial setting up of a specified project.
 - Project exporters who have executed projects abroad be allowed to import equipment purchased abroad at lower duty of around 5 percent instead of at 50 percent as at present. The bank guarantee may be waived as the export obligation is already met.
 - Cross border lending/hiring of equipment be allowed with a bank guarantee for the duty for period of lease/hire. Duty may be collected while re-exporting the equipment as per certain norms.
- Need to re-think over the restoration of income tax sops for infrastructure withdrawn w.e.f. 01.04.2007 as infrastructure is now more or less well defined. This includes restoration of 10(23) G of the Income Tax Act under which banks got an exemption on their interest income for financing infrastructure.
- The issue of high stamp duties in some states needs to be addressed.

Healthcare :

Focussed approach to healthcare sector both to increase the welfare of the people and to increase exports of healthcare services is needed. Tax related measures in this context could include the following:

- At the central government level zero customs duty for all equipment/spares to enable hospitals to provide the latest technology as

available in the West; lower excise duty to the indigenous manufacturers of medical equipment, drugs and other consumables; higher depreciation allowance to counter the high rate of obsolescence of technology and to generate internal accrual for replacement.

- At the state level, measures could include exemptions of sales tax and octroi for capital goods items used in hospitals including super specialty hospitals exporting healthcare and research centres.

IT Services & Telecom:

- Addressing the issue of customs bonding as Companies operating under the STP scheme are required to get their premises customs bonded necessitating multiple approvals from DOE-STP and also the Customs and the Excise departments resulting in delay of movement of computer and other equipments from one STP to another.
- Resolving the difference of opinion between the Central Government and State governments on taxability of certain items like SIM cards, recharge coupons, bill plan rental, handsets/modems, IT software, etc. leading to double taxation on the same transaction.
- Need for clarity on applicability of sales tax or service tax on IT Software.

Some other common tax related issues:

- Need for clarity in service tax refund policy on input services as many companies are not able to get refund.
- Transfer Pricing issue. The Budget 2009-10 has proposed the creation of an alternative dispute resolution mechanism within the Income Tax Department for the resolution of transfer pricing disputes. To reduce the impact of judgmental errors in determining transfer price in international transactions, it was proposed in the Budget to empower the CBDT to formulate “safe harbour” rules. These initiatives need to be expedited and taken to their logical conclusion.
- Having a single return for service tax and excise tax administered by same Department.
- Reduction of the TDS rate of 10 percent for professional and technical services sector which is too high.
- Making TDS uniform for all heads of income with exemptions for small incomes upto a certain threshold limit.

(iv) Credit and Finance related issues

7. Some of the important credit and finance related issues for services are the following:

- Addressing the issue of withholding tax on interest paid on ECBs. The requirement of overseas lenders/ investors is that interest due to them be paid without deducting any withholding tax in India. Exemptions could be considered atleast for foreign currency borrowings raised for financing all export related activities and overseas acquisitions.
- Venture capital funding, given the difficulty of arranging security/ collateral especially by first time entrepreneurs, as in the case of software sector in US where more than 20 percent of the investments has been due to venture capital since the 1980ies. The venture industry not only provides the capital to create some of the most innovative and successful companies, but also becomes actively engaged with a company, typically taking a board seat. With a startup, daily interaction with the management team is common. Given the fact that some of the renowned venture capital backed companies include Intel Corporation, Microsoft, Apple, Google and Starbucks Corporation among others, there is a need to focus on Venture Capital for services sector.
- Extending specific dedicated lines of credit focusing on promotion of service exports like construction services, IT related services and education services.

(v) Other policy issues – General

8. There are many other policy issues of a general nature. These include the following:

- Increasing visibility of India in services by showcasing India's services overseas by workshops, buyer-seller meets and positioning people in some major markets for services including by sectors or regions and a sincere effort to reorient our foreign missions to focus on India's commercial interests by placing professionals and experts on services in these missions. Supplier companies must make sure that they appear on the first page of Google and other search engines in response to the relevant key words entered into a search engine.
- Facilitating Measures for promoting services exports including setting up joint offices with common facilities to help professional services as in Hong Kong, devoting some SEZs exclusively for services, facilitating Indian companies to set up subsidiaries in EU as it is difficult to enter EU market, etc.
- Standardization of services on the lines of National Manufacturing standard.
- Setting up an institutional mechanism as lack of a single nodal department/division/institution is one of the weaknesses of the services sector, particularly for domestic policy making. Since, coordinated policy

action is needed, there is a need for a nodal department or division, preferably in the Department of Economic Affairs, Ministry of Finance which can look into all aspects related to services, while the individual departments dealing with some services or some aspects of services can continue their usual work as is being done by them at present.

- Having a preferential system for overseas investors in domestic market and government procurement for services.
- Setting up a portal for services to provide useful information for foreign service providers who intend to do business with India in this sector. This can also help in increasing the visibility of India in terms of its capability.
- Consolidation of the service providers in each sector to face international standards.

(vi) Other policy issues - Sector specific

9. The other policy issues for services which are sector specific in nature are the following:

Telecom Services

- Addressing the issue of multiple levies and duties, licence fee on unrelated activities like revenue from sale of handsets, lack of uniformity in the fee structure across States and services, etc. The fee also needs to be reduced, simplified and rationalized. This can be done by a simple formula of dividing total revenue of telecom department by the total license fee the government is getting out of it. Telecom licences should be disaggregated from spectrum allocation. Spectrum should be auctioned and be freely tradable among companies having a telecom licence.
- Auctioning of 3G Technology immediately which is long overdue and introduction of high speed connectivity in all cities and towns.
- Utilizing USO funds for construction of towers across villages, providing each village with fibre connectivity and providing power at right rates by subsidizing it.

Shipping and related services

- Strengthening Indian fleet and funding as the strength of cargo ownership provides a strong leverage, to build a substantial Indian flag tonnage as well as to moderate freights quoted by foreign owners and provide more stability in the freight costs of Indian charterers. With the overall share of Indian ships carrying Indian cargo (in export-import trade) falling below 12% from as high as 40% a couple of decades ago and the need to scrap around 40% of existing shipping capacity due to IMO regulation, this is all the more

important. The current circumstances also offer a good opportunity to augment the fleet at a time when such assets are readily available at reasonable prices, if cheaper funds are made available. The following measures could be considered for financing ship acquisition:-

- Raising rupee resources by providing tax incentives for investment as in the case of the proposal for power bonds (Vidyut Vikas Patra).
- Relaxing ECB funding norms for the shipping industry by particularly addressing the withholding tax issue.
- Long term shipping contracts and cargo support for Indian flags. The shipping requirements of the PSUs could be channelised and long term contractual cargo support to Indian shipping companies ensured. Such long term contracts would, in turn, enable the Indian companies to invest in Indian flag tonnage and help in the growth of the Indian fleet. Long term contracts and similar cargo support (including coastal cargo cabotage measures), are also now a necessity for securing funding. Most lenders worldwide are now seeking the comfort of contracts backing up ship acquisitions. In the evolving context of India's growing energy demand and consequent dependence on global energy markets, there is an urgent need to own and develop a national "core" fleet in the energy sector, similar to the US Sea Lift Command. The 'brand value' of Indian flag can be improved through policies like first right of refusal and cabotage. The preference for the national flag in the carriage of national cargo can be through directives from the Government. The Directorate General of Shipping needs to be appropriately empowered to enable strict implementation of the chartering guidelines as at present the powers are only implied and not explicit.
- Giving infrastructure status to shipping industry and supporting industries like the shipbuilding and ship repair industry. Presently, those sectors under infrastructure enjoy the benefits/concessions available under sec.80-IA of Income Tax Act, which provides for a deduction equal to 100 percent of the profits and gains derived from the infrastructure for 10 consecutive assessment years.
- Other potential areas to be tapped including promoting ship registry services alongwith a low tax regime, positioning India in logistics services to manage the whole supply chain and ship repair services .

Port Services

- Following a holistic approach for improving the existing infrastructure and services at the ports through modernization of the systems with latest technology. Particularly, the infrastructure facilities at major ports for handling crude oil need to be strengthened through a facilitative policy on single point moorings. The facilities at existing ports with regard to cargo handling, stevedoring, pilotage services, bunker services, warehousing facilities etc.

need to be upgraded. The transshipment of Indian cargo taking place outside the country at present needs to be handled at Indian ports through concerted measures. This would include increasing the drafts available at Indian ports , rationalization of port dues and providing differential levels of tariff for different sizes of vessels or for different cargoes to attract mother ships to berth at Indian ports. The many port charges in India need to be reduced as they are higher than in many other countries due to inefficiency of ports, and inclusion of unrelated costs like pension & other contributions to port labour in port services.

- Providing port services by port based SEZs: These services could include international bunkering facilities, pilotage facilities, supply of spare parts, ship repairs, etc.
- Corporatising port trusts (minus excess land) which can be converted into public listed companies with atleast 49 percent shares held by the general public.

Construction Services & Project Exports

- Using the Standard Contract Document for all domestic civil engineering projects.
- Setting up consortiums to bid effectively for international projects.
- Exploring the opportunity for low-energy buildings using sunlight with the growing emphasis on climate change. Even existing buildings in UK and some other developed countries are being redesigned and modified to be environment friendly.
- Resolving the issue of precondition in most of the overseas tenders floated by clients wherein equipment to be supplied by the contracting company should necessarily be sourced from approved list of suppliers from developed countries and considering the possibility of double guarantee avoidance treaty on the lines of double taxation avoidance treaty as overseas clients insist on Bank Guarantees to be issued under the contract to be routed through a local bank operating in the country of project execution which results in Indian contracting companies being called upon to pay the bank guarantee charges to Indian banks as also to the local overseas banks which issue the final end guarantees to the client, based on the counter guarantees from the Indian Banks.

Healthcare Services

- Need for international accreditation apart from national standardized accreditation. External assessment of healthcare services is being increasingly used to regulate, improve and promote healthcare services all over the world. In many countries, external assessment of healthcare

services is in demand by governments, healthcare professionals, patients and communities. Though the Quality Council of India (QCI), an autonomous body set up by the Government of India, announced the National Accreditation Board for Hospitals and Healthcare Providers (NABH) in order to have standard accreditation and make available accreditation standards at lower costs, international accreditation is a very important step to make the hospitals eligible for the coverage with foreign insurers. For example, the JCI (Joint Commission International) seal would enable Indian hospitals to be accredited with US insurers. This in turn would attract customers from other parts of the world and thereby increase their profitability. A growing number of hospitals in India have turned to accreditation agencies worldwide to both standardize their protocols and project their international quality of health care delivery. International accreditation would also reduce the rigour of undergoing a separate national government evaluation process and help in achieving prerequisite of insurance reimbursements.

- Exploiting the potential of outsourcing health services for UK's NHS as there is huge opportunity and increased interest in UK in using technology and internet based health services from India.
- Tapping the demand for financial and accounting services from India in health sector of developed countries like U.K. and helping companies to get funding for under funded healthcare facilities in US by taking advantage of tax savings provisions in US.
- Negotiating for removal of market access barriers and recognition of technical degrees by other countries, developing India as a regional healthcare hub, tie-ups with some developed countries under CECAs and setting up Health Consultancy Parks which combine both preventive and curative health care with tourism.
- Encouraging stem technology research alongwith monitoring its application by different private hospitals/clinics. The draft Clinical Establishments (Registration & Regulation) Bill, 2007 is particularly relevant in this context. Necessary steps need to be taken to get this passed in Parliament.
- A complete overhauling of the Central Government Health Scheme (CGHS) system and similar systems of state governments, other levels of government and semi-government institutions with outsourcing to private sector in a big way. The space used for the CGHS clinics could then be put to other profitable uses.

Accounting, Auditing, Bookkeeping and Legal Services

- Tie-ups to overcome the weakness of small size of domestic accountancy firms.

- Allowing representative offices of foreign law firms to practice non Indian law in India on a reciprocal basis.
- Tapping outsourcing in niche areas like actuarial and accountancy services as there is good scope for outsourcing actuarial services and accountancy services to India including setting up back offices. But Indian service producers need good training on US tax laws and laws related to insurance, pension etc.

Financial Services

- Mergers and acquisitions including acquisition of small banks by big banks.
- A coordinated policy for setting up bank branches to avoid mushrooming of banks in the same place in cities.
- Operationalising offshore financial centres by removing any hurdles. The report on Implementation Model for free Ports in India has suggested the setting up of offshore Banking units in SEZ's. The report of the High Powered Expert Committee (HPEC) on 'Mumbai: An International Financial Centre' has suggested the setting up of International Financial Centre in Mumbai. These need to be examined and a decision should be taken on their implementation and the time-frame for implementation. Some of the recommendations of the HPEC include the creation of a currency spot market with a minimum transaction size of Rs.10 million, accessible to all financial firms; an Indian rupee settled exchange traded currency derivatives market with trading in futures, options and swaps on currencies, accessible to all; opening up fully to foreign investment in Indian rupee denominated sovereign bonds issued by Government of India; replacement of rules based regulation by principles-based regulation; inclusion of financial services under GST with simultaneous removal of all central and state transaction taxes including the Securities Transaction Tax (STT), stamp duties, etc.; removing existing barriers to entry of private domestic corporate players in some segments of the financial services industry; removing barriers to the entry of foreign financial firms in the provision of International Financial Services (IFS); restricting demands for reciprocal market access only to domestic financial services; reducing the extent of public ownership progressively in Indian financial institutions; improving the Indian legal system in resolving disputes, adjudicating settlements and enforcing financial contracts in real time; and opening up domestic space to permit the entry of well-known international law firms that operate in other International Financial Centres (IFCs) and Global Financial Centres (GFCs) as well as international accounting firms and tax advisory firms as well as specialist management consulting firms focusing on the International Financial Services sector. The recommendation of a well-functioning Bond-Currency-Derivatives (BCD) nexus where all these three separate markets work as a

seamless whole, if adopted with proper checks & balances could help in the speedy transmission of monetary policy including checking inflation with marginal hikes in interest rates and easier access to external funding. IFCs would enable India to shift from exporting its best financial talents permanently, to retaining a hold on such talent in the future by providing greater global mobility.

- Resolving the issue of limit on bank branches and ATMs of foreign banks in India.
- Tapping the huge foreign business by Indian Insurance companies by encouraging them to venture outside India.
- Taking a view on the suggestions of different committees and setting up a specific time frame for the actionable suggestions. Some of the suggestions of the Committee on Financial Sector Reforms (Raghuram Rajan Committee) which could be considered, include warehouse receipts as negotiable instruments for farmers to get credit; steadily opening up investment in the rupee corporate and government bond markets to foreign investors after a clear monetary policy framework is in place; liberalising the Banking Correspondent Regulation so that a wide range of local agents can serve to extend financial services; encouraging the entry of more well-capitalized ARCs (Asset Reconstruction Companies) including ones with foreign backing; and a well functioning bankruptcy code.
- Providing extended banking arrangements by greater coordination among the existing network of banks. Since the Banking system in India is spread far and wide with a concrete network and this is made even stronger by the presence of a number of Regional Rural Banks in the interiors of the country, a paradigm shift will be the creation of a platform wherein the unique services offered by select banks is utilized at select branches through an exchange-sharing basis. This will bring local knowledge to bear on the products that are needed locally, and to have the locus of decision-making close to the banker who is in touch with the client, so that decisions can be taken immediately. The Raghuram Rajan Committee has also suggested the liberalization of the Banking Correspondent Regulation to allow a wide range of local agents to extend financial services. Thus, there is scope for considering expanded reach by working with and through local institutions. However these institutions should be selected through a screening process and with clearly defined limiting role to serve as extension of the banking industry.
- Including climate change related financial schemes/instruments as climate change issues are gaining in importance. These could include developing insurance schemes against climate related risks; structured emission products, carbon funds, European Union Allowances (EUAs) Certified Emission Reductions (CERs) swaps, avoided deforestation/ Reducing Emissions from Deforestation and Forest Degradation (REDD), synthetic portfolios and carbon securitization; SRI (Socially Responsible Investment)

funds, Low-carbon technology stocks, index products; forestry bonds; Carbon venture capital; energy efficiency/green building real estate investment trusts; and hedging Instruments like weather derivative products, catastrophe bonds and insurance products.

Tourism Services

- Facilitating measurers like issue of visas on arrival for select countries, establishing special tourism police force, slum clearance with proper resettlement facilities, stopping begging on a priority basis, etc.
- Promoting services like trade fairs and exhibitions by setting up convention centres. It is really a pity that India does not have a convention centre for international exhibitions in Mumbai, the financial capital of India. Even the annual Gems & Jewellery Expo is organized in an old factory shed. State governments should give land for such convention centres which could even be on a PPP basis. Funds from schemes like ASIDE of Govt. of India could also be given for them.
- Changing urban land use rules to separate land use for hotels from commercial land use and defining transparent rules for setting up of hotels in mixed use locations and the borders between commercial and residential areas.
- Allowing railway passenger services by private sector to important tourist destinations.
- Creating holiday homes by utilizing idle resources with public sector units . Many public sector units have holiday home facilities availed by employees at nominal prices, often unused and not well maintained. A public private partnership mode for more efficient utilisation of these facilities could generate enhanced revenue streams besides continuing to make available the facilities to employees though on a more commercial basis. This could be achieved, for instance, through tie-ups with agencies that offer such facilities on their own, often nationwide This could also include Central/State government guest houses and port guest houses.

IT and related Services

- Addressing the issue of weakness of India in retesting computer software.
- Improving the quality of the new-breed of IT professionals as there is a feeling abroad that the new talent pool in IT is not as efficient as the old pool, particularly when new competitors have emerged.
- Shifting from low-end service to high-end services like programming in the light of competition in Business Process Outsourcing (BPO) from other countries like Ukraine, China, Bolivia, South Africa, etc., and policy in countries like U.K. to employ locals. There is a need to move to systems

software coupled with hardware-software combination alongwith further progress in applications software.

- Need for Data Protection Act as EU and other developed countries are very particular on data protection as half of offshore work does not come to India due to this. This should be on the lines of EU Safe Harbour Decision and EU directives on data protection. The IT Amendment Act includes this issue. This Act needs to be implemented urgently.
- Concluding totalisation agreements with target countries to resolve the social security benefits issue and making necessary changes in domestic laws.

R&D Services and Consultancy Services

- Tapping the potential for R&D services, particularly in healthcare, electronics and biotech. Problems in India are due to lack of local R&D and Intellectual Property Rights (IPRs). While the IPR laws are good, litigation takes a long time and Indian legal system has not understood the IPRs. This needs to be addressed.
- Other policy measures for R&D services could include setting up R&D labs in SEZs, patent funding to reimburse costs of patenting, promoting lab testing services and setting up design, engineering, consultancy parks.
- Need for international accreditation for consultancy institutions/ associations.

Satellite Mapping Services

- Negotiating with US, EC and other developed and developing countries regarding defence restrictions, examining possibilities of sharing some common facilities and data of public sector institutions like ISRO with private sector, consortium bidding and including government institutions like ISRO in the consortium, partnering with other countries for launching and tracking of satellites and tapping the potential to export to all the 42 markets identified.

Education Services

- Replacement of bureaucratic controls on educational institutions by professional regulation, encouraging public-private partnership in education, rating the quality of educational institutions and regulated entry of large quality foreign and rated domestic institutions in higher education.
- Review of the built in space norms and patient load factor norms to be in tune with present day equipment intensive care and modern practices and procedures as some institutions of higher education like medical colleges are

found mainly in some states, with even Delhi having few medical colleges with fewer seats, while the demand is very high for such education.

- Entrance to medical education and jobs in the medical sector should be based only on quality.
- Revamping the system of teaching, curricula, research etc. in the universities and institutions. To begin with, university courses particularly economics, finance & management-related, should be time tuned in consultation with policy makers in these areas and Trade & Industry.
- Phased introduction of education reforms given the fact that state governments are also involved. While states may oppose centralization of selection process for higher education, they could be persuaded to accept common entrance tests for technical education which could be one of the components in the selection and the other components like marks in the qualifying exams may be decided by the states.

Other Services

- Privatization of sewage services. Charges on sewage services can be based on property value as done in UK or some other criteria like, say size of family.
- Training and skill certifying in the case of unskilled labour services before Indian labourers go abroad as done by countries like Philippines, Thailand and Sri Lanka.

Domestic Regulations

10. One major issue in services is the domestic regulations in India. Using the strict definition as indicated in the WTO documents, domestic regulations basically include licensing requirements, licensing procedures, qualification requirements, qualification procedures and technical standards. Since domestic regulations perform the role of tariffs in regulating services, we have to list the domestic regulations in India which need to be disciplined to help growth of the sector and exports, while retaining those domestic regulations which need to be retained at this stage.

11. As per the World Bank & IFC publication "Doing Business 2010" India ranks 133 among 183 countries in the ease of doing business. Though in trading across borders, India was the top reformer in 2006/07, India's poor ranking in most of the sub indicators is mainly due to domestic regulations like licensing and procedural delays. The difference between different cities in India is still sharper. Domestic regulations not only affect manufacturing but also services. An indicative list of some important domestic regulations

in India which need to be examined for suitable policy reforms in different service sectors are given below.

Transport Services

- Restrictions on inter-state movement of goods and coordination issues between government departments in the case of multimodal transportation and need for changes in merchant shipping Act and Multimodal Transportation of Goods Act, 1993. There are also restrictions on free movement of cargo between ICDs, CFSs and Ports.

Construction, Engineering and related services

- Restrictions like minimum capitalization norms, some restrictions on repatriation, minimum area norms and a general umbrella clause that all applicable rules/ bye laws/ regulations of the state government/ municipal/local body concerned have to be complied with.
- Restrictions under the Urban Land Ceiling and Regulation Act. As a result of this Act, construction services firms in India operate at a small scale, and do not exploit economies of scale.

Healthcare Services

- Restrictions on foreigners providing healthcare services: While there is no cap on FDI in health services, foreign individuals are prohibited from providing services for profit and their movement is subject to registration by Medical/Dental/Nursing council of India.

Accountancy Services

- Besides FDI not being allowed in this sector, foreign service providers are not allowed to undertake statutory audit of companies as per the provisions of the Institute of Chartered Accountants of India and the Institute of Company Secretaries of India Acts.
- There is also ban on use of logos of accounting firms which need to be disciplined to facilitate tie-ups and penetrate foreign markets given the potential for exporting these services by the outsourcing mode.
- The accountancy professionals are only allowed to operate either as a partnership firm or as a sole proprietorship firm. Since the Partnership Act of India permits only 20 or less professionals under one firm, this de facto means that the number of partners in Indian accounting firms are limited to 20 or less. Further, the number of statutory audits of companies per partner are restricted to 20. Indian regulations also proscribe inter-disciplinary professional models, i.e. accounting firms are not allowed to hire management professionals to perform consulting/ management services. As a result of the above restrictions, less than 200 firms (or 0.5% of total accountancy firms) have more than 10 partners. Due to their small size,

domestic firms have been less successful in competing with international firms.

Legal Services

- FDI is not permitted and International law firms are not authorized to do advertising and to open offices in India.
- Foreign service providers can neither be appointed as partners nor sign legal documents and represent clients. Bar council is opposed to entry of foreign lawyers/law firms in any manner. With recent developments like outsourcing of administrative work of legal firms of UK and other countries, there is a need to be more open on legal services to at least facilitate overseas firms to outsource legal services to India.

Education Services

- Multiple controls and regulations by central and state governments and statutory bodies as education comes under the concurrent list in India.
- Regulations with respect to establishment of new medical colleges and need to review patient load factors to be in tune with present day equipment intensive patient care and modern practices and procedures of medical education, as mentioned earlier.

Infrastructure services

- Reforming the regulatory framework which include efficient, transparent and standardized bid process/ procurement; clarity in contractual structure/ concessions/ incentives and adoption of equitable contract as under International Federation of Consulting Engineers (FIDIC) or Construction Industry Development Council (CIDC) guidelines; well defined pre-qualification norms; single window regulatory approvals; effective dispute resolution mechanism; harmonized legal definition of infrastructure; and liberalized investment guidelines for debt & equity instruments.

Financial Services

- Many regulations under the Banking Regulation Act which at present has the requirement that banks obtain regulatory approval for a range of routine business matters including opening branches, remuneration to board members and even payment of fees to investment bankers managing equal capital offerings as pointed out by the Raghuram Rajan Committee report.
- In the case of insurance, besides, cap on foreign investment of 26 percent/other restrictions like minimum capitalization norms, funds of policy holders to be retained within the country, compulsory exposure to rural and social sectors and backward classes.

Entertainment services

- Regulations related to cable TV channels like getting license and having an agent in India to downlink channels needs to be examined.

Distribution Services

- FDI not allowed in retail trade except single brand product retailing with 5 percent cap as stated earlier.

Others – General

- Need for a competition policy for 'Services' in India and a regulatory body. While there are regulators for some services like Banking, Insurance, Telecom and Ports, there are no independent regulators for most professional services with de facto regulation taking place through a combination of statutes provided in law and by professional all-India and state councils. There is need for strengthened regulation, to protect the interests of Indian consumers and to get recognition for the qualifications by foreign governments and regulators in sectors like education and healthcare services where regulatory regimes and current enforcement of regulations have resulted in a huge disparity in the quality of services and the abilities of domestic service providers.
- Transfer pricing which is aggressively attacked by India as mentioned earlier.
- Indian laws like prohibiting night shifts for women and laws related to contract labour which affect different services.

Market access issues

12. This is another important issue as domestic regulations and policies in India's major services markets deny market access for India's services exports. Market access barriers can be due to domestic regulations, subsidies or other barriers. However, this paper does not deal with them in detail and gives only some examples under the different categories. These are as follows:

- **Market access barriers due to domestic regulations in the US** include state level licensing and the 'Buy American' provisions in the case of business services and IT services; the requirement of the Office of the Comptroller of the Currency (OCC) and some State banking supervisors to maintain "asset pledges" in addition to the paid up capital they maintain in their home country in the case of financial services; the fragmentation of the insurance market into 56 different jurisdictions and direct discrimination on a number of fronts, such as need for foreign insurance companies to first be licensed in another state before seeking a license in the first state to underwrite risks in one state; difficulty in opening bank branches and

restrictions even after licensing in banking sector; need in some states of US for foreign insurers to buy reinsurance from state-licensed companies before allowing re-insurance premiums to leave the state; restrictions in the case of transport and related services like the reservation of a minimum of 50 percent of government cargo for US registered ships, all cargo provided with loans from the US Exim Bank to be reserved for US registered ships though a 50 percent waiver may be granted, etc; restrictions in the case of construction and related engineering services and urban planning and landscape services, where the “Buy American” legislations passed in many states of US have gone to the ridiculous extent of even insisting on the materials used (i.e. cement) to be of domestic origin for construction of public works projects financed by state funds. The latest protectionist policies in US and other economies like the conditions in U.S. bailout package related to employment of non- U.S. nationals and moves against outsourcing are the new domestic regulations denying market access to other countries.

- **Market Access barriers due to subsidies** include the huge subsidies in the Civil Aviation sector to aircraft in both US and EU; the subsidy programme in shipping providing an operating cost subsidy of \$100 million a year for a period of ten years for US registered ships meeting certain requirements ; etc.

- **Other Market Access barriers** include a 50 percent ad valorem tax on the cost of equipment and non-emergency repairs for US flag vessels done outside US which is an example of tariff barrier on shipping services by the US; the provision of free medical services to all UK citizens under the NHS system which acts as an invisible market entry barrier in healthcare services and possibly even helps the export wing of the NHS.

Conclusion

13. The different suggestions for reforms in the services sector have been given above. Among these suggestions, there are many reforms which need to be initiated and implemented in the short term as given in Box 1. Some policies like opening retail trade, opening insurance sector, liberalizing air transport services, FDI in railways, disinvestment of those PSUs involving labour issues, etc. may need more time. Nevertheless, it is worth making efforts to push these reforms as well.

Box 1 : Policy suggestions for services sector in the short term

FDI

- Opening some segments of insurance sector like health insurance and removing the 10 year disinvestment clause.
- Liberalising foreign investment in rural banking with the help of mobile technology.

- Liberalising FDI in animation sector.
- Relaxing the minimum area norm in construction sector.
- Raising foreign investment cap for uplinking news and current affairs TV channel from 26 per cent to 49 per cent.
- Making available FDI policy in the website in a user friendly way.

Disinvestment

- Initiating disinvestment in atleast 9 PSUs (out of 27), namely, SCI, EIL, RITES, EPIL, ITPO, STC, MMTC, NBCC and NFDC.

Tariff & Tax related

- Addressing the issue of multiple levies & duties in telecom.
- Rationalising taxes in shipping sector.
- Resolving the definitional issues under tonnage tax for shipping.
- Allowing advance tax instead of tax deduction at source (TDS) in some services like engineering and construction.
- Introducing electronic system of tax payment for tourist vehicles.
- Rationalising the entry fees for monuments and privatization of these services.
- Addressing the tax credit issue in the case of films.
- Addressing the issue of Royalty/Turnover tax by Airport authorities on service centres.
- Addressing the inverted duty issue in printing sector.
- Allowing advance tax instead of TDS in Engineering & Construction sector.
- Procedural changes for infrastructure projects.
- Abolishing octroi atleast for capital goods used in hospitals including super speciality hospitals exporting healthcare services and in health-related research centres.
- Resolving the differences in the case of taxability of items like SIM Cards, recharge coupons, IT software, etc.
- Making TDS uniform for all heads of income with exemptions for small incomes upto a certain threshold limit.
- Expediting the measures related to transfer pricing.
- Single return for service tax & excise tax which are being administered by the same Department.
- Reduction of TDS for professional and technical services.

Credit and Finance related issues

- Exempting interest paid to ECBs from withholding tax for financing export related activities and overseas acquisition including of ships.
- Encouraging venture capital in services.
- Operationalising offshore financial centres.

Other policies – General

- Increasing visibility of India in services through trade fairs, buyers-sellers meets and setting up convention centres.
- Facilitating services exports by setting up joint offices with common facilities and devoting some SEZs exclusively for services.
- Standardization of services.
- Institutional mechanism for services by a nodal department/division for services in Ministry of Finance.
- Setting up a portal for services.

Other policies –sector specific

- Speeding up auctioning of 3 G technology.
- Utilising USO funds for construction of towers across villages.
- Strengthening Indian fleet and providing long term contracts for Indian flags.
- Promoting ship repair services.
- Rationalisation of port dues.
- Modernising port infrastructure on priority basis.
- Preparing a standard contract document & setting up consortiums in construction sector.
- Resolving the issue of precondition in most of the overseas tenders wherein equipment to be supplied by the contracting company should necessarily be sourced from an approved list of suppliers from developed countries.
- Exploring the opportunity for low-energy buildings.
- International accreditation for health services.
- Tapping the demand for outsourcing financial & accounting services in healthcare sector.
- Changes in CGHS system with the help of outsourcing to private sector.
- Tapping outsourcing in niche areas like actuarial and accounting services.
- Mergers and acquisitions and coordination policy for setting up bank branches.
- Introducing climate change related financial schemes/instruments.
- Creating holiday homes by utilizing idle resources in public sector units.
- Implementing the IT amendment Act including Data protection.
- Totalisation agreements with target countries and making necessary changes in domestic laws.
- Reviewing built in space norms and patient load factors to be in tune with present day equipment intensive care and modern practices and procedures.
- Revamping the system of teaching, research, etc. in universities/ institutions, phased introduction of education reforms and allowing foreign educational institutions in higher education with proper checks and balances.
- Privatisation of sewage services.
- Skill certifying unskilled labour.

Domestic regulation

- Addressing restrictions on inter-state movement of goods.
- Resolving the issue of ban on use of logs of accounting firms.
- Removing the unnecessary regulations under Banking Regulation Act.
- Competition policy for services and regulatory body for services other than banking, insurance, telecom and ports.

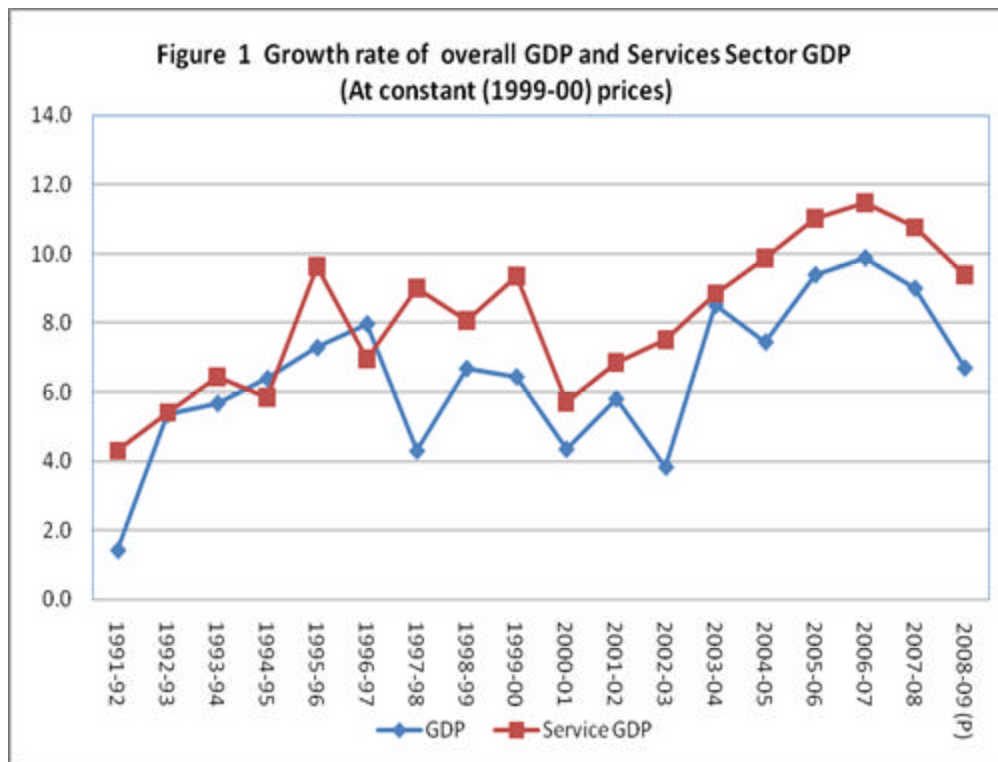
14. Immediate and time-bound reforms in the services sector could not only help in attaining our targeted GDP growth rates, but also give a fillip to growth and exports of this services led economy.

Part 1. Introduction

15. Services sector is particularly important for India. Some major features of India's services sector can be seen under the following heads.

GDP Growth :

16. The ratcheting up of the trend rate of GDP growth of the economy from 6 percent to about 7 percent per year and reaching 9.4 per cent in 2006-07 was to a great extent due to the ratcheting up of the trend growth rate in the major sector i.e. services sector from 6.7 per cent in 1983-93 to 8.2 per cent in 1993-03 and further to around 10 per cent since 2004-05. The CAGR for services at 9 percent is higher than the 5.8 percent for non-services during 2000-01 to 2006-07. The close relationship between GDP growth and Services GDP growth can be seen in the Figure 1. In fact the latter has pulled up the former particularly since 1997-98.



17. State wise growth rate of GSDP is also closely associated with higher growth of tertiary sector. The relative importance of service sector in the growth process has been strongly established in the last two decades as can be seen from Table 1.

Table 1 Correlation of sectoral growth with overall growth across 17 major states

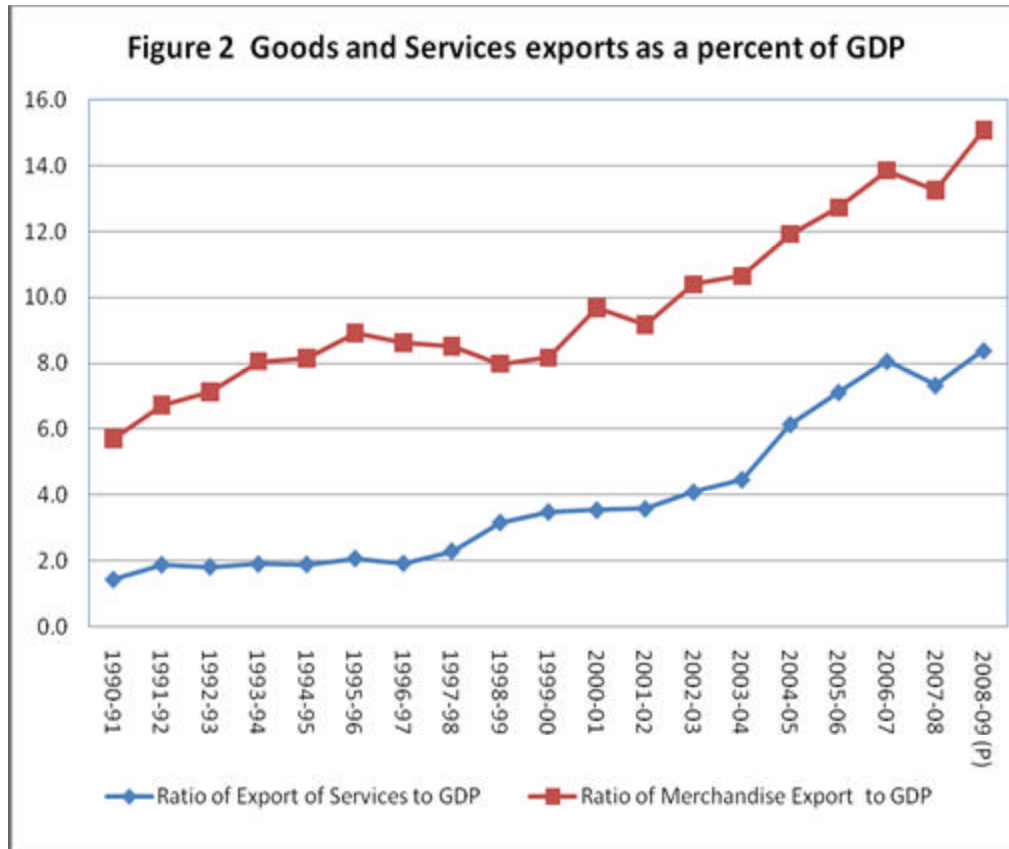
Year	Primary	Secondary	Tertiary
1983-93	0.77	<i>0.54</i>	0.45
1993-99	0.40	0.83	0.94
1999-2004	0.46	0.00	0.82

Note: Figures in bold are significant at 1 per cent level and figures in Italics are significant at 5 per cent level.

The correlation coefficient of overall growth rate of state domestic product (SDP) with sectoral growth rates across seventeen major states shows contrasting picture over three periods. In the first period (1983-1993) the higher growth of SDP was most significantly associated with higher growth of primary sector. In the second period (1993-99) higher growth of SDP was associated with higher growth of both secondary and tertiary sectors. In the last period (1999-2004) higher growth of SDP was associated with only higher growth of tertiary sector. The primary importance of the tertiary sector in the growth process has been strongly established in the last two decades. Further, during 1999-00 to 2004-05, out of 17 major states, except Himachal Pradesh and Jammu & Kashmir, all the other states experienced a growth in tertiary sector which was higher than the overall growth of the respective states.

Services Export Growth:

18. India is also moving to a services dominated export growth with services export growth at 28.0 percent and 22.1 percent respectively for the years 2006-07 and 2007-08. The CAGR for export of services at 28.7 percent is higher than the 19 percent for merchandise exports during 2000-01 to 2006-07. Even in 2008-09 when the world economy was affected by the global recession, India's services exports grew by 12.5 percent. In the second half of 2008-09 export growth of services was less negative at -0.53 percent compared to merchandise export growth of -16.6 percent. However, in the first half of 2009-10, the impact of global recession was visible on India's services export sector as well, with exports declining by 21.4 percent though it was better than the fall of merchandise exports by 28.5 percent. Exports of services are valued at \$ 102 billion compared to \$185.3 billion of merchandise exports in 2008-09, thus forming 55 percent of merchandise exports.



Openness of the Economy:

19. Total trade including services as a percentage of GDP shows a remarkable increase from 27.4 percent in 2000-01 to 52.1 percent in 2008-09. The ratio of services exports to GDP shows an upward movement since 1997-98 which was particularly sharp from 2003-04 to 2006-07 (Figure 2).

Country-wise exports of Services of India :

20. US is the most important destination for India's services exports. However, in US imports of other commercial services in 2003, the share of a NAFTA member like Mexico is nearly double that of India, though its growth rate is only 9.2 percent and the share of a FTA partner like Israel though small is increasing. India's presence is much lesser in EU than in the US. China, Hong Kong and Singapore have higher shares than India in the EU market. However, in the case of UK's imports of total services, other services, travel services and even transportation services, India has relatively higher shares though it is still less than 1 percent. In fact, the pattern of India's exports of services to UK is similar to that of US, rather than EU. The historical and cultural ties between India and UK may also be one of the reasons for this. India has not made any impact in the Japanese market in services which needs to be examined. Thus India's experience

with services sector is not only different from other developing economies (which have yet to develop and market many of these services), but also different with respect to its direction of exports even among the developed countries.

List of Important Services for India:

21. Software is one sector in which India has a brand identity. Tourism and travel related services and transport services are also major items in India's services exports. Besides these, the potential services which are particularly important for India are: professional services, R & D services, consultancy services, printing and publishing services, telecommunication services, maintenance and repairs including ship repair services, construction services, educational services, financial services, entertainment services, satellite mapping services and standardization & quality assurance services. India has a great potential to be an outsourcing destination for many of the above services. This however seems to be threatened by the recent developments in US & EU limiting outsourcing.

Part 2. Major Policy Issues

22. Accelerating growth and exports of services is important for India. For this many policies are needed. The major policy issues can be seen under the following headings:

1) Domestic Policy Issues

- (i) FDI
- (ii) Disinvestment
- (iii) Tariff & tax related
- (iv) Credit and finance related issues
- (v) Other policy issues - General
- (vi) Other policy issues - sector specific

2) Domestic Regulations

- (i) Sector specific
- (ii) General

3) Market access issues

- (i) Due to domestic regulations
- (ii) Due to subsidies
- (iii) Other barriers

4) Other issues like bilateral, regional and multilateral negotiations and policies of multilateral institutions.

23. In this paper, however we have focused only on domestic policy issues and domestic regulations though a sample of issues under market access has also been given. Other issues like bilateral, regional and multilateral negotiations and policies of multilateral institutions have not been dealt here though it is an interesting and emerging issue. The list of policies and regulations are also not exhaustive, but gives some important issues in different sectors. In the case of financial services we have not dealt with details as many recent committees have gone into these details.

1) Domestic Policy Issues

(i) Foreign Direct Investment (FDI):

24. FDI in services formed 22.4 percent of total FDI inflows of \$27.3 bn in 2008-09, as per the Department of Industrial Policy and Promotion (DIPP) which uses a very narrow definition. If all services including telecommunications, housing & real estate, construction, trading, ports, hotel & tourism, information & broadcasting, consultancy services, hospital and diagnostic centres, sea transport, education, air transport and

agricultural services are included, the share will be 61.1 percent. If computer software & hardware are also included (break-up figures for computer hardware and software are not readily available) then the share will be 67.2 percent in 2008-09. Some policy issues in the case of FDI in the different services are the following:

Retail Trade:

25. Opening retail trade, where FDI is prohibited (except single brand product retailing subject to 51 percent cap) while there is a large unorganized sector with low tax compliance. Since farmers also benefit due to modern retail trade, there is a need for opening this sector which can also provide greater market access for India's exports. Along with allowing FDI in retail in a phased way beginning with metros, the existing mom and pop shops (kirana shops) could be incentivised to modernise and compete effectively with the retail shops foreign or domestic.

Insurance:

26. Raising FDI cap in the insurance sector has been in the Government's agenda for long but could not be implemented for various reasons. The FDI cap is at 26 percent, though it is through automatic route, while Indian firms can independently set up firms, foreign firms are allowed entry only through partnerships or joint ventures. If it is difficult to raise the FDI cap in the insurance sector as a whole due to practical difficulties, atleast some segments of the insurance sector could be opened up further. One such segment is health insurance and FDI cap at least in health insurance can be raised in India on a priority basis as it will also help the export of super-specialty hospital services.

27. There is also a 10 year disinvestment clause in the insurance sector which could be removed. The IRDA Act also stipulates that funds of policyholders be retained within the country and there be compulsory exposure to the rural and social sector and backward classes including crop insurance as fixed by IRDA, which the foreign insurance companies find difficulty to fulfill. FDI restrictions in reinsurance sector could also be removed and foreign re-insurance companies could be allowed to set up their representative offices and function in India through a network of branches and divisions, thus creating conditions for the development of a buoyant reinsurance market.

Banking sector:

28. This is another sector where there is scope for further liberalisation. Though foreign investment (FDI+FII) of 74 percent is allowed, there are licensing requirements. There is also a limit of ten percent on voting rights in respect of banking companies. While many concerns have

to be addressed here particularly in the light of the recent global financial crisis, atleast some segments of this sector could be opened up. Liberalising banking services to foreign investment only for rural banking with the help of mobile technology is one such area.

Animation studio:

29. FDI needs to be liberalised as there is good scope for these services.

Construction Sector:

30. In construction including housing commercial premises, resorts, educational institutions recreational facilities, city and regional level infrastructure, townships, while 100 percent FDI is allowed under automatic route, there are the following conditions:

- Minimum capitalization of US\$ 10 million for wholly owned subsidiaries and US\$ 5 million for joint venture. The funds would have to be brought within six months of commencement of business of the company.
- Minimum area to be developed under each project – 10 hectares in case of development of services, housing plots and built-up area of 50,000 sq. mts. in case of construction development project and any of the above in case of a combination project.
- Original investment cannot be repatriated before a period of three years from completion of minimum capitalization.

Some of these conditions could be relaxed

Uplinking Services:

31. For Uplinking News & Current Affairs TV Channel, foreign investment cap is 26% (FDI+FII). This is under FIPB route and not automatic route. Besides there are conditions like the following:

- The portfolio investment in the form of FII/ NRI deposits shall not be “persons acting in concert” with FDI investors, as defined in the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997.
- The Company permitted to uplink the channel shall certify the continued compliance of this requirement through the Company Secretary at the end of each financial year.
- While calculating foreign equity of the applicant company, the foreign holding component, if any, in the equity of the Indian shareholder companies of the applicant company will be duly reckoned on pro-rata basis, so as to arrive at the total foreign holding in the applicant company. However, the indirect FII equity in a company as on 31st march of the year would be taken for the purposes of pro-rata reckoning of foreign holdings.

- FDI for up-linking TV channels will be subject to compliance with the uplinking policy of the Government of India notified by the Ministry of Information & Broadcasting from time to time.

While the foreign investment cap could be raised atleast upto 49 percent in the case of these services, the conditions above need to be examined for relaxation.

Telecommunications:

32. In the case of ISP without gateway, infrastructure provider providing dark fibre, electronic mail and voice mail, 100 percent FDI is allowed with FIPB approval beyond 49 per cent. However, there is the 26 percent disinvestment clause in 5 years, if these companies are listed in other parts of the world. In the case of all other segments of telecom services, FDI cap is at 74 percent with FIPB approval beyond 49 percent. In the case of basic cellular, unified access services, V-sat, etc. and value added services 74 percent cap includes FDI, FII, NRI, FCCBs, ADRs, GDRs, convertible preference shares and proportionate foreign equity in Indian promoters/ investing company. Besides, to ensure that at least one serious resident Indian promoter subscribes reasonable amount of the resident Indian shareholding, such resident Indian promoter shall hold at least 10 percent equity of the licensee company. The disinvestment clause could be relaxed and the other conditions examined for relaxation.

Air Transport Services:

33. In this sector, 49 percent FDI is allowed (100 percent for NRI investment) subject to no direct or indirect participation by foreign airlines. Since this prevents those with experience from operating in this sector, there is a need for liberalisation while taking note of security concerns. The Ministry of Civil Aviation's initiative should be taken to its logical conclusion.

Railways:

34. FDI is not allowed in railways. FDI upto 26 percent could be thought of which can help in modernization of railways.

35. Besides the above, the whole FDI policy should be made available in the website in a user friendly way. At present, one has to search in many places and different Press Notes to understand the FDI caps and other regulations for different sectors. This has also been highlighted in the Economic Survey 2009-10 and later in the Budget 2010-11, It has been stated that the government intends to make the FDI policy user-friendly by consolidating all prior regulations and guidelines into one comprehensive document.

(ii)Disinvestment

36. There is plenty of scope for disinvestment in the case of public sector companies in services sector under both the central and state governments. This will not only yield the necessary resources to lower the fiscal deficit and meet social sector and infrastructure related investments. Besides loss making units, even profit making PSUs can be completely/partially disinvested. A list of some of these companies alongwith related details are given in table 2.

37. Among the PSUs given in table 2, SCI, NBCC, EIL, Balmer Lawrie and Company Ltd., Engineering Projects India Limited, STC, were earlier listed for strategic sales. However, in February, 2005, disinvestment through strategic sale of profit making CPSUs were called off as per the NCMP and the above companies continued as CPSUs. Now disinvestment of these companies could be initiated.

38. In the case of some of the companies there are some labour related issues and one company, namely, National Film Development Corporation is a loss making company. Among the companies given in table 2, disinvestment could possibly be initiated immediately in the case of RITES, SCI, Engineers India Ltd., Engineering Projects India Ltd., STC, MMTC and ITPO. In the case of ITPO, exporters and even Exim Bank of India could have a stake. The price could also be good in the case of many of them. In the case of NBCC and NFDC, there can even be full sale of the companies. In fact NFDC is a loss making company and there is no need for government to be in the films sector. In the case of the companies, where there are issues related to labour, etc., some percentage of the government shares could be offloaded.

39. The above disinvestments can, not only yield sizeable revenue for the government, but also make these companies more efficient, contributing to the growth process.

Table 2: List of PSUs for likely disinvestment

Name of the company	Established in	Administrative control (Ministry)	Activities	Income from operations (Rs. Lakhs)	Net profit/(loss) (Rs. Lakhs)	Authorised capital (Rs.Lakhs)	Paid-up capital (Rs. Lakhs)	Book value**	Number of shares	Government shareholding (%)	Other share holders (%)
Telecommunications Consultants of India Ltd*	1978	Ministry of Communication and IT	Consultant services in telecom sector	64,641.18	939.38	6,000	4,320				
PEC Ltd	1971	Ministry of Commerce and Industry	Turnkey project services	57,264	4,138	12,607	200	6,303.50	2,00,000	100	
Engineers India Ltd*	1970	Ministry of Commerce and Industry	Engineering and technical services	153,246.28	34,453.37		5,615.62	205.14	56,155,849	90.4	9.6
Water and Power Consultancy Services	1969	Union Ministry of Water Resources	Consultancy services in water and power sector	16,406.36	1,514.06	200	200	3277.08	2,00,000	100	
MSTC Ltd	1964	Ministry of Steel	Trading in metal scarp	519,711	9,220		220			90	10
National Building Construction Corporation*	1960	Ministry of Urban Development	Construction and infrastructure projects	204,435.15	15,915.72	12,000	9,000			100	
State Trading Corporation of India Ltd	1956	Department of Commerce	Trading company	16,990	12,400		6,000			91.03	9.97
MMTC Ltd	1956	Ministry of Commerce and Industry	Trading company	42,975.80	20,050	1,000	5,000	205.99	5,00,00,000	99.33	0.67
Shipping Corporation of India Ltd	1961	Ministry of Shipping	Shipping services	416,664	94,067	45,000	42,345	199.51	423,366,715	80.12	19.88
Balmer Lawrie & Co Ltd	1867	Ministry of Petroleum & Natural Gas	Trading and logistics	200,688	10,915		1629	199.42	16,286,337	61.8	38.20

Mahanagar Telephone Nigam Ltd	1986	Ministry of Telecommunication	Telecom services	532,993.30	40,681.80	80,000	63,000			56.25	43.75
Bharat Sanchar Nigam Ltd	2000	Ministry of Telecommunications & IT	Telecom services	3,805,340	300,939	1,750,000	1,250,000				
Dredging Corporation of India Ltd*	2000	Ministry of Shipping	Dredging services	68,497	6,168		2,800	442.42	27,995,802	78.56	21.44
Cochin Shipyard Ltd	1972	Ministry of Shipping	Ship building and repair services	83,378	9,385		23,242			100	
Goa Shipyard Ltd	1957	Ministry of Defence	Ship building and repair services	40,094	6,998		2,910			100	
Mazagon Dock Ltd	1934	Ministry of Shipping	Ship building and repair services	260,981	24,086	20,000	27243			100	
Hindustan Shipyard Ltd	1941	Ministry of shipping, road and highways	Ship building and repair services	48,976.63	1,133.54		28,101.22			87.15	12.85
India Trade Promotion Organisation	1991 (by merging two organizations)	Ministry of commerce	Trade fairs and promotional activities	19,677	6,957	50	25	117408	25,000	100	
Indian Railway Catering and Tourism Corporation		Ministry of railways	Railway catering and tourism services	52,766.38	2,074.91	5,000	2,000	40.72	20,000,000	100	
Central Warehousing Corporation	1957	Ministry of Railways	Warehousing services	77,622.87	13,691.04	10000	6802.1	17861.81	745250	100	

IRCON International Ltd	1976	Ministry of Railways	Railway infrastructure construction and consultancy services	209,311.20	11,379.80	2500	989.8	958.52	9898000	99.729	0.271 (institutions and others)
RITES Ltd	1974	Ministry of Railways	Engineering, infrastructure construction and consultancy services	66,070.23	10,381.66	10,000	4,000	134.72	40,000,000	100	
Engineering Projects India Ltd	1970	Department of Heavy Industries	Engineering turnkey contracts, construction and consultancy services	87,236.04	1,753.18	90940.46	3542.26	188.51	90,94,400	100	
MECON Ltd	1959	Ministry of Steel	Engineering, infrastructure construction and consultancy services	50,415.41	3,331.78	10,400	10,313.84	-22.47	40,138,360	100	
Educational Consultants India Ltd	1981	Ministry of Education and Culture (reconstituted as the Ministry of Human Resource Development in 1985).	Consultancy services in the areas of education and human resources development	4,462.51	270.39	200	125	1257.60	125,000		
National Research Development Corporation	1953	Ministry of Science and Technology	Technology development and advisory services in diverse fields	882.61	30.26	1,000	441.81	2248.87	44,181		

National Film Development Corporation	1975	Ministry of Information and Broadcasting	Developmental activities for promotion of films	3,318.98	-237.56	1400	1,399.98	-17.71	1,399,985		
Broadcast Engineering Consultants India Ltd#	1995		Consultancy services and turnkey jobs in the specialized fields of Broadcast Engineering and Information Technology	9867.84	524.37		136.5				

Note: * 2008-09, # 2006-07, ** Book value is for 2007-08

(iii) Tariff & Tax related.

40. Some important tariff and tax related issues which make Indian services less competitive compared to our competitors and need to be addressed are given below for the different services:

Shipping Services

Strengthening Indian fleet by rationalizing the taxes in shipping sector:

41. The share of Indian carriers in the carriage of overseas sea borne trade in 1982-83 was 40.7 percent, which has seen steady erosion since then and in 2007-08 stood at a mere 9.5 percent. Barring POL & products and other liquids sector, where the share of Indian carriers is 16.4 percent, in other sectors the share of Indian carriers is in single digit @3.7 percent in the carriage of general cargo and @ 6.8 percent in the carriage of dry bulk cargo. According to the TERI report commissioned by the Indian National Ship-owners Association (INSA), there is a clear and positive contribution by the Indian shipping industry to the Indian economy with a 1 percent change in Gross Tonnage (GT) likely to bring about 0.0068 percent change in GDP. While trade has increased, India's shipping has not kept pace with it. The strength of the Indian fleet was 9.3 million GT in 2009. Out of the 9.3 million GT fleet, about 4 million GT are likely to be scrapped over the next 5 years due to the completion of commercial life as well as on account of IMO regulation for phasing out single hull tankers coming into force in 2010. The estimated balance of the existing fleet at the end of next 5 years would be around 5 million GT. Thus 44 percent of the existing fleet will have to be replaced over the next 5 years which involves an estimated investment of US\$ 4 to 5 billion. The Indian shipping industry has benefited due to the introduction of tonnage tax. But the value of Indian flag has gradually diminished and even Indian owners are increasingly opting to own vessels outside India, pay virtually zero tax, employ shipboard personnel of any nationality and access India's booming cargo base. Since the late 90s, 100 percent FDI in shipping has been allowed. But no worthwhile foreign investment has taken place to provide a thrust to the growth of Indian fleet so far. This is despite the fact that several foreign shipping lines have been operating services to and from India and the main reasons for lack of interest were due to the non-availability of level playing field in direct and indirect taxation and rigid regulations like manning norms in India. Greece and Singapore are such maritime nations, which although do not have substantial cargo carriage of their own, have earned the position of world cargo carriers in having policy measures to attract investments. Indian shipping is presently subjected to various direct/indirect taxes that add to its costs thereby increasing the effective tax rate of around 2 percent under the tonnage regime to around 9 percent. Shipping industry is subject to 12 direct and indirect taxes over and above the tonnage tax, thereby, reducing the benefit of lower taxes of 2-3 percent intended to be granted under the tonnage tax regime. The 12 taxes are given in Table 3.

Table 3: Taxes in the Shipping Sector

Direct Taxes	Indirect Taxes
1) Corporate Income Tax on interest and other income	9) Sales Tax/ VAT on ship supplies/ spares
2) Minimum Alternate Tax (MAT) on profit on sale of vessels	10) Lease Tax on charter hire charges
3) Dividend Distribution Tax	11) Customs Duty on import of certain categories of ships, stores, spares & bunkers
4) Withholding Tax on interest paid to foreign lenders	12) Service Tax
5) Withholding Tax on charter hire charges paid to foreign ship-owners	
6) Seafarer's Taxation-cost to employer	
7) Wealth Tax	
8) Fringe Benefit Tax	

42. Recognizing the importance of Indian shipping to the country's trade and economy and with a view to providing a level playing field so that Indian shipping becomes internationally competitive, steps to rationalise the taxes in the shipping sector are needed.

Tonnage tax issues:

43. Modifying the definition of 'core' activities to treat the incomes arising from the following, as core activities covered under the Tonnage Tax (TT) regime;

(i) Book-profit on sale of vessels should not to be subjected to MAT but should be treated as arising from 'core activities' of tonnage tax. Sale/purchase of ships being intrinsic to the industry's core business, major maritime nations like UK, Ireland, Singapore, Netherlands have covered profit/loss on sale of vessels in their TT regime. Profit on sale of ship on forming part of relevant shipping income would attract compulsory transfer of profit to TT reserves, thus leading to further growth in tonnage. So, MAT on sale of ships could be removed.

(ii) Interest income from compulsory reserves needs to be treated as arising from 'core activities' of a tonnage tax company in terms of sub-section (2) of Section 115V-I. While waiting for opportune time to acquire the assets, the interest generated needs to be treated as core income and would further attract provisions of Sec.115VT(1) viz. compulsory transfer to tonnage tax reserve for buying ships. Moreover, Double Taxation Agreements (DTAs) with countries like Belgium, China, Denmark, Germany, Netherlands, Malta, S. Africa, UAE,

USA etc. have treated interest on funds as income from shipping operations. So the interest earned on TT reserves could be treated as income from core activities.

Zero rating input services availed by the Indian shipping industry (either imported or domestically procured)

44. Since globally, input services for shipping industry are not subject to service tax, whether such services are availed domestically or internationally, service tax on import services could be zero-rated. These include the following:

- Brokerage, commission and finance charges
- General insurance services including P&I insurance
- Ship management services; and
- Manpower recruitment and supply agency services

This will place the Indian ship industry on a level playing field as foreign ship owners can obtain these services from foreign service suppliers with no service tax payment.

Seafarers' taxation issue:

45. India has one of the largest pools of seafarers in the world. The industry spends a lot of resources in their training and development. Since the introduction of tonnage tax, the shipping companies have provided approximately 1.5 lakh training mandays annually. However, despite this, Indian shipping companies face an acute shortage of seafarers, particularly in the officers' category because of drift of personnel from Indian flag ships to foreign flags under the lure of higher 'take home' pay packets, without having to pay taxes in India. This needs to be addressed.

Customs duty issues

46. These include the following:

- Exemption from customs duty on direct import of repair materials by shipping companies for repairs in India. As in the case of ship repair units, shipowners could be permitted to import spares and repair equipment directly for carrying out repairs in India without being subject to payment of customs duty.
- Exemption from customs duty on import of certain categories of vessels as per Sec.2(23) and 2(27) of Customs Act. As in the case of other categories of ships (H.S. 89.01), 5 percent customs duty could be removed on import of vessels under H.S. 89.04, H.S. 89.0510 and H.S. 89.0590.
- Exemption of capital goods imported for shipbuilding including renewals and replacements of yard facilities from customs duty. These are presently dutiable under Customs Act. The effective rate of duty is 38.82 percent. In any yard having both ship building and ship repair facilities, most of the assets are common. Hence the concessions extended to one activity alone may not serve the required purpose. So the capital goods imported for ship building could also

be exempted from customs duty. This could help modernisation and upgradation of ship building facilities.

Exempting capital goods required for construction of ships from levy of excise duty as in the case of ship repair:

47. At present excise duty is 16 percent. This will help in modernisation and upgradation of ship building facilities, improving the productivity and achieving a better competitive edge in global bidding. Besides in any yard having both shipbuilding and ship repair facilities, most of the assets are common. Hence the concessions extended to one activity alone may not serve the required purpose. So excise duty could be lowered further for capital goods for growth to pick up.

Reinstating the exemption from withholding tax on interest paid to foreign currency loans to acquire ships abroad:

48. Withholding tax on charter hire paid to foreign shipowners on ships taken on charter, etc. are high at 10 percent compared to either nil or 23 percent in different cases in Singapore. Reinstating the exemption from withholding tax withdrawn with effect from 1.06.2001 on the interest payment of ECB loans could be considered. Similarly withholding tax on in-chartering of foreign vessels could be removed.

Tourism Services

49. Some important tax related issues in the tourism sector include the following:

Rationalizing the tax structure for tourism as the overall tax impact on tourism is around 30-35 percent.

Reduction in taxation on Air Turbine Fuel (ATF) which directly affects airfares. It is better to bring ATF under “Declared goods” which will reduce duty to 4 percent. While state governments are opposing this as it will lower their revenue, there is also concern that the benefits may not be passed on to the consumers. This needs to be sorted out and states convinced of the possible advantages due to increase in business volumes. Since this is a long term solution, this is better than the alternative to reduce sales tax on ATF by states ranging from 12 percent to 35 percent. Besides lowering duties and continuing with widely varying rates may not end the problem.

- State Luxury tax issue – Luxury tax in some states are very high and varies from 5 percent to 20 percent in different states. Some states charge on the actual rate and some on rack rates (published rate). Each state has its own criteria. Since no changes are made in rack rates if there are variations, tourists are affected if the actual rates are lower than the rack rates. State governments need to rationalise luxury tax at around 5 percent.

- Electronic system of tax payment for tourist vehicles with the help of swipe cards should be introduced.
- The per seat passenger tax system for buses needs to be changed. Since this is based on estimated passengers carried, tourist buses not running at full capacity will lose. Further, this not only makes the tax high, but also penalizes the buses carrying more passengers and reducing pollution compared to other vehicles like cars.
- Rationalizing the fees for entry to monuments and using the fees for their maintenance. Private sector could also be allowed to maintain monuments and collect fees on the lines of toll taxes.

Entertainment Services

50. Tax credit issue is an important issue in this sector. Entertainment exports have huge potential as Indian culture (film & music) are becoming a part of mainstream culture in countries like U.K. Gaming, multimedia and animation have scope and even children in UK are trained in Bollywood. UK gives 25 percent tax credit for films i.e. 25 percent of expenditure of budget of films is rebated (though subject to a limit). This is actually a subsidy and not a tax credit. But it is disguised as tax credit. This is not at all related to usual taxes which have to be paid. Germany, Hungary, Los Angeles, Michigan, New Zealand also give similar subsidies. Canada gives 50 percent of labour costs as tax credits. This type of subsidy given by UK led to investment in film production in UK. Similarly with other countries. India does not give such benefits. Many film producers of India produce films in UK to avail of this benefit and show only a part of their work from India where there is no benefit and taxes are high. There is a need to examine if India can give these tax credits as India can gain from huge investments along with multiplier effects while usual taxes can continue. If not, this should be raised in the WTO as there is an unfair advantage for these services in some countries due to the subsidies.

Aviation maintenance/repair services

Addressing the issue of sales tax on aircraft parts imported by aircraft service companies.

51. When a service centre imports aircraft parts into India, it is required to first pay an import duty (around 20-25 percent) and again when it sells these parts to an aircraft operator, a sales tax/VAT (around 10-13 percent) is to be paid. Whereas if an aircraft operator directly imports aircraft parts, no sales tax/VAT is incurred and same import duty is payable only if the parts imported are meant for a private category aircraft. Due to this tax structure it is not viable for a service centre to stock frequently required parts locally in India for supplying to various operators at competitive prices and without having them to go through the importation hassles. Exemption in sales tax applicable on imported aircraft parts sold by a service centre to aircraft operators and charging

import duty only if parts are sold to private operators will help service centres in providing better support to its customers.

Reducing the import duty for spare parts of aircraft

52. Import duty is 20-25 percent for special tools and 30-35 percent for equipment. As aviation repair/ maintenance are affected by these duties, they could be reduced.

Addressing the issue of turnover tax by airport authorities on service centres

53. Service centres are required to pay a turnover tax (currently @ 14 percent) to airport authorities on their revenue earned from services rendered to aircraft operators on air side of airport. This tax is in addition to service tax payable to the Income tax authorities. This issue needs to be addressed.

Printing and publishing services

54. The printing and publishing industry is developing at a very fast pace and India has the advantage of having low cost labour and a large English knowing young population. With 12.5 percent growth per annum, the Indian printing industry is poised to achieve 60 percent growth by the year 2012 and can generate phenomenal increase in employment opportunities. The following could be considered for this sector:-

- Exemption from customs duty on import of state-of-the art printing and allied machinery and equipment which are not being manufactured in India.
- Exemption from customs duty on paper and paperboard. The printers in the country have to pay 10 percent customs duty together with 4 percent CVD and 4 percent special CVD, etc. on paper and paperboard. The total quantum of duty works out to a figure of 19.72 percent on import of paper and paperboard. However, due to bilateral trade agreements, printed materials can be imported at 'nil' or much lower customs duty. To provide the printers in the country a level playing field, coated paper and paperboard covered under chapter 4810 could be exempted from payment of customs duty.
- Exemption from central excise duty @ 8 percent imposed in the Central Budget 2006-07 on diaries, registers, labels etc. falling under chapters 48.20 & 48.21. Both diaries and labels are primarily items of the printing industry. The printers are now required to maintain separate cumbersome accounting records for (a) the dutiable goods and (b) the exempted goods and unless the concerned authorities are satisfied with the said records, the concerned printers would have to revert to 10 percent the value of the exempted goods as per provision of CENVAT credit rule, 2004. Besides, printers are required to purchase a large variety of paper and paperboard in wide range of sizes and substance in small quantities to cater to the varied print requirement. Since the individual quantities are quite small in nature, the purchases have to be made from the traders directly. Thus the small printers will not be able to receive

excisable invoice from the manufacturers and hence would be unable to take credit of excise duty already paid on the various raw material inputs. This needs to be addressed.

- Inverted duty issue: There is also inverted duty in printing sector as paper and paperboard has 19.72 percent duty and printed material has lower duty. This needs to be addressed.

Engineering, construction & infrastructure services

55. Some tax and tariff related issues for these services include the following:

- Taxing each members share of profits/losses instead of tax as Association of Persons (AOPs): In the construction sector, infrastructure construction contracts are generally executed through a prime contractor or a consortium of companies or established through Joint Ventures (JVs). The latter two enable construction companies to pool their expertise and resources. Profit sharing JVs are taxed as AOPs. Instead each member's share of profits/losses could be taxed along with his other business income.
- TDS issue: Construction companies are subject to TDS, which creates a severe cash flow problem. A 2 percent TDS in a business where margins are 4-5 percent is severe. Construction companies with equity capital of Rs.1 crore, may be allowed to pay advance tax as is done by manufacturing companies.
- Customs and excise issue: All imports for infrastructure projects, including spares and parts, could be made duty free. Imports of steel and cement for infrastructure projects could also be lowered. At the same time, excise duties on cement and steel needs to be in the lower excise band.
- Procedural changes: Liberal import of high tech equipment is permitted for infrastructure projects but the procedures require fine-tuning as indicated below:
 - Withdrawing the 5-year restriction on sale of imported equipments as these equipments are expensive, having a 10-15 years of useful life, but may be used for only 2-3 years in a project. Allowing its resale or lease will enable construction companies engaged in similar projects to buy or lease the equipment from other domestic companies.
 - The member companies of joint ventures may be allowed to import duty exempt goods in their own name instead of in the name of JV, as these have to be held for 5 years as per policy, while a JV may cease after 2-3 years on completion of a project.
 - Duty exemption under project import could be extended to a contractor's plant and machinery used for initial setting up of a specified project.
 - Project exporters who have executed projects abroad could be allowed to import equipment purchased abroad at, around 5 percent duty instead of at 50 percent as at present. The bank guarantee could be waived as the export obligation is already met.

- Cross border lending/hiring of equipment could be allowed with a bank guarantee for the duty for the period of the lease/hire. Duty could be collected while re-exporting the equipment at discounted rates based on some norms.
- Need to re-think over the restoration of income tax sops for infrastructure withdrawn w.e.f. 01.04.2007 as infrastructure is now more or less well defined. This includes restoration of 10(23) G of the Income Tax Act under which banks get an exemption on their interest income for financing infrastructure.
- Extending the tax benefits available to IT firms to engineering design offshore firms to help enhance export of engineering design services.
- The issue of high stamp duties in some states needs to be addressed.

Healthcare

56. Focussed approach to healthcare sector both to increase the welfare of the people and to increase exports of healthcare services is needed both at the central and state levels. Tax and tariff related policy measures include the following:

- Zero customs duty for all equipment/spares to enable super-specialty hospitals to provide the latest technology as available in the West.
- Lower excise duty to the indigenous manufacturers of medical equipment, drugs and other consumables.
- Higher Depreciation allowance under Income Tax Act to counter the high rate of obsolescence of technology and to generate internal accrual for replacement.
- Exemptions of sales tax and octroi for capital goods items used in hospitals and research centres.

IT Services & Telecom

57. Some important tax and tariff issues for IT and Telecom services are the following:

- Addressing the issue of tax on packaged software at multiple points. In the Budget 2009-10, the value attributable to the transfer of the right to use packaged software has been exempted from excise duty and CVD subject to certain conditions.
- Issue of customs bonding: Companies operating under the STP scheme are required to get their premises customs bonded (Paras 9.18 and 9.25 of the Handbook of Procedures) necessitating multiple approvals from DOE-STP and also the Customs and the Excise departments. This results in delay of movement of computer and other equipments from one STP to another. This needs to be addressed.
- Difference of opinion between the central and state governments on taxability of certain items such as SIM cards, recharge coupons, bill plan rental, handsets/modems etc. (customer premise equipment-not sold by the assessee but provided in the course of rendition of services), IT software etc. This amounts to double taxation on the same transaction. Further, there isn't enough

clarity on applicability of sales tax or service tax on IT software and the basis thereof. The central government intends to levy service tax on above items, whereas, the state governments are levying sales tax on the same. As per the state governments, the software is goods and liable to sales tax whereas the central government has defined the customized software as a service liable to service tax. A clarification on the applicability of service tax or sales tax on IT software along with the basis thereof needs to be given and ambiguity leading to levy of dual taxes needs to be removed.

Some other common tax related issues

58. Some of these issues are given below:

- Need for clarity in service tax refund policy on input services as many companies are not able to get refund.
- Transfer Pricing (TP) issue: Many MNCs have set up captive companies in India for providing IT/ ITES and other services which are exported out of India. Having regard to the functions performed, assets employed and the risks assumed, an arm's length price is charged by the captive units for the international transactions. The arm's length price determined is invariably disputed in the transfer pricing assessments and substantial demands are being raised. Dispute resolution involves committing substantial financial and managerial resources. Dispute resolution has also become a challenge as the transfer pricing officers continue to follow different methods/ benchmarks for different assessment years. Many MNCs have invoked the Mutual Agreement Procedure to resolve the disputes arising from the TP adjustments. So there is need for clarity in transfer pricing rules and refrain from aggressively attacking transfer pricing. Indian rules need to be explicit on what level of activity a foreign company can conduct in India without creating a taxable presence i.e. a Permanent Establishment (PE). The Budget 2009-10 has proposed the creation of an alternative dispute resolution mechanism within the Income Tax Department for the resolution of transfer pricing disputes. To reduce the impact of judgmental errors in determining transfer price in international transactions, it was proposed in the Budget to empower the CBDT to formulate "safe harbour" rules. These initiatives need to be expedited and taken to their logical conclusion.
- Having a single return for service tax and excise tax which are administered by the same Department
- Reduction of TDS rates: TDS @ 10 percent is too high for professional and technical services sector. Ability to pay TDS @ 10 percent requires a firm to have margins of 30-35 percent which is rare for many service sector companies, whose margins are normally in the range of 8-10 percent. Income tax refunds take 3-4 years (after filing of IT returns) and entail long drawn-out procedures, lengthy correspondence, etc. resulting in wastage of time in non-professional work. So, TDS rates could be reduced for these services.

- Making TDS uniform for all heads of income with exemptions for small incomes upto a certain threshold limit.

(iv) Credit and Finance related issues

Withholding Tax on Interest paid on ECBs:

59. Several sub-segments of the services sector, including shipping, tourism, retailing and healthcare, require significant capital investment and need to raise debt resources to finance asset creation. The present trend of the industries is to resort to External Commercial Borrowing (ECB) whereby the industries can raise low cost funds. However, there are domestic barriers such as withholding tax on the interest paid on such ECBs. Further such ECBs are exposed to risks of fluctuating exchange rates. The requirement of overseas lenders/ investors is that interest due to them be paid without deducting any withholding tax in India. Exemptions could be considered atleast for foreign currency borrowings raised for financing all export related activities and overseas acquisitions.

Working Capital finance:

60. In certain other services segments such as business services, which are primarily cash-flow based rather than asset-based, there is a need to evolve more effective methods for financing working capital, which addresses lenders' risks while also providing necessary funding to services enterprises.

Addressing the difficulty of arranging security/ collateral by getting the support of venture funds:

61. This is an issue that requires to be addressed especially to help first time entrepreneurs, as for instance in the software sector. In the USA and some other developed countries, such support is often rendered through venture funds. The software sector in the USA has been among the few in the industry to attract investments from non-traditional sources like venture capital investments. The venture capital segment of the private equity industry focuses on investing in new companies with high growth potential and accompanying high risk. The venture industry provides the capital to create some of the most innovative and successful companies. But venture capital is more than money. Venture capital partners become actively engaged with a company, typically taking a board seat. With a startup, daily interaction with the management team is common. The entrepreneur's active engagement is critical to the success of the fledgling company. Some of the renowned venture capital backed companies are Intel Corporation, Microsoft, Apple, Google and Starbucks Corporation among others. According to the National Venture Capital Association (NCVA), USA, in the year 2006, venture capital financed companies in the computers and peripherals sector employed nearly 2 million Americans, followed by the industrial/energy industry with 1.3 million American jobs. The computers and peripherals industry was also the leading industry in 2006 with

revenue at US\$ 533.0 billion, followed by the industrial/energy sector with US\$ 302.4 billion revenue. The venture capital investments in the US software and IT services sector has been contributing immensely towards the growth of the sector. According to the National Venture Capital Association (NCVA), share of venture capital investments in the software and IT services sector as a proportion of the total have been hovering over 20 percent since 1980's. During 1980, it stood at 20.3 percent which increased to touch 31.1 percent in 1990 and later in 2008 it dropped to around 23 percent in 2008. The venture capital investments in the sector has not taken much of a beating even in 2008 and 2009 inspite of the worst ever global financial crisis and recession since the Great Depression.

Other issues:

62. These include providing appropriate export financing with reduced transaction costs and considering extension of specific dedicated lines of credit focusing on promotion of service exports like construction services, IT related services and education services.

(v)Other policy issues – General

Increasing Visibility of India in Services:

63. Visibility of India in terms of its capability in services is lacking. There is a need to showcase India's services overseas by workshops, buyer-seller meets and position people in some major markets for services including by sectors or regions and make a sincere effort to reorient Indian foreign missions to focus on India's commercial interests by also placing professionals and experts on services in these missions. Lobbying is another related issue as many contracts can be obtained by intense lobbying. Providing right and quick information is very important as, for example, there is good demand for Indian engineering and architectural services abroad, but finding right companies for tie-ups is not easy as information is lacking. While there is a need to be more visible in services, there is also a need to have a good mechanism to enable global sourcing of services from India particularly by SMEs. The conventional route for discovering new suppliers, via Chambers of Commerce, is being progressively superseded by the use of the Internet. Supplier companies must make sure that they appear on the first page of Google and other search engines in response to the relevant key words entered into a search engine. SMEs typically have very limited resources in carrying out the search and validation process for new suppliers. They need to obtain reassurance in a rapid and cost effective way on factors like validation of supplier companies, credit worthiness of the company, quality assurance, intellectual property protection, effective problem resolution process, visibility and trust of the

company by proper branding/packaging products and services and delivery, and establishing business relationships.

Facilitation and standardization measures for promoting services exports:

64. These include setting up joint offices with common facilities to help professional services as in Hong Kong; devoting some SEZs exclusively for services, facilitating Indian companies to set up subsidiaries in EU as it is difficult to enter EU market; and standardization of services on the lines of National Manufacturing standard.

Institutional set up:

65. There is a need for an institutional set up as lack of a single nodal department/division/institution is one of the weaknesses of the services sector, particularly for domestic policy making. Since, coordinated policy action is needed, there is a need for a nodal department or division, preferably in the Department of Economic Affairs, Ministry of Finance which can look into all aspects related to services, while the individual departments dealing with some services or some aspects of services can continue their usual work as is being done by them at present.

Preferential System:

66. There is a need to examine the issue of preferential system in India in domestic market and government procurement for overseas investors in the case of services as they spend a lot of money investing in India. For example, if IBM invests in China, Chinese government will use IBM items. Similar systems need to be examined by India.

Setting up a portal for services:

67. This is needed to provide useful information for foreign service providers who intend to do business with India in this sector. Besides providing relevant export market information and help service exporters to become known suppliers of quality services, this can also increase the visibility of India in terms of its capability.

Consolidation of the service providers in each sector to face international standards:

68. A World Bank study has pointed out that many Indian services are highly fragmented by international standards. For example, there are 100,000 chartered accountants in India and 43,000 audit firms, with an average of two chartered accountants per firm compared to an average of between 350 and 1500 chartered accountants in the “big four” accounting firms in India. Nearly ninety percent of housing construction companies in India are single owner proprietorships and ninety-five percent of all trucks in India are owned by small fleet operators. In retail distribution, the penetration of supermarkets in India is

only 2 percent compared to 55 percent in Malaysia and 36 percent in Brazil. In many instances, statutory policies have played a role in preventing consolidation.

(vi) Other policy issues - Sector specific

a) Telecom Services

Multiple levies and duties and licence fee issues:

69. There are multiple levies and duties and license fee on unrelated activities like revenue from sale of handsets which needs to be addressed. Besides, license fee of telecom sector varies across states as well as services offered. There should be uniformity in the fee structure across states and services. The fee also needs to be reduced, simplified and rationalized. This can be done by a simple formula of dividing total revenue of telecom department by the total license fee the government is getting out of it. Telecom licences should be disaggregated from spectrum allocation. Spectrum should be auctioned and be freely tradable among companies having a telecom licence. The auction price can be in the form of a fixed price or charge per unit of bandwidth per annum or a combination of the two.

Expediting introduction of 3G Technology:

70. India has moved a great deal in telecom, but the world has moved further. So, major reforms in our telecom sector are needed including immediate introduction of 3G technology and high speed connectivity in all cities and towns. This is all the more important as telecommunications are more robust even in countries like Poland where turnover costs are less. So 3G auction should be held immediately which is long overdue.

Universal Service Obligation (USO) issue:

71. Government of India has collected huge amount by way of USO but not utilized it. These funds could be used for construction of towers across 6 lakh villages, providing each village with fibre connectivity and providing power at right rates by subsidizing it.

b) Shipping and related services:

Strengthening Indian fleet and funding:

72. The strength of cargo ownership provides a strong leverage, to build a substantial Indian flag tonnage as well as to moderate freights quoted by foreign owners and provide more stability in the freight costs of Indian charterers. However, there is no substantial Indian tonnage. This has unfortunately resulted in the overall share of Indian ships carrying Indian cargo (in export-import trade), to fall below 12 percent from as high as 40 percent a couple of decades ago. In fact, the UNCTAD has favoured reserving 40 percent of the national cargo for national fleet. The analysis of the estimates of freight payments for imports

published in the UNCTAD Review of Maritime Transport 2007 also indicates significant variations in the freight cost ratios among the developed, developing and transition economies of the world. As against 5.9 percent freight cost of the total CIF import value in the world trade as a whole in 2005, the share of freight costs in the imports of developing countries at 7.7 percent continues to be higher than those of the developed market economy countries at 4.8 percent. The freight factor of transition economies was at 7.6 percent. Besides moderating the freight rates, the national tonnage has a tremendous potential for increasing the foreign exchange earnings/savings by increasing the share of Indian shipping in India's overseas trade. If the Indian shipping industry's share in India's overseas trade increases to 40 percent, as indicated by UNCTAD, the foreign exchange earnings/savings would proportionately rise to around Rs.40,000 crores. According to a study conducted by the National Council of Applied Economic Research (NCAER), shipping as a single industry is one of the largest contributors to the foreign exchange pool of the country. The Council has also established, on the basis of their analysis of the trade and freight data, that a 5 percent increase in the national shipping tonnage saves or earns an additional 17 percent of the freight bill.

73. As stated earlier, due to IMO regulation, around 40 percent of existing shipping capacity is to be scrapped. The current circumstances also offer a good opportunity to augment the fleet at a time when such assets are readily available at reasonable prices, if cheaper funds are made available. So all out efforts to increase the Indian shipping fleet needs to be done. Besides the measures suggested earlier, the following measures could be considered for financing ship acquisition:-

➤ Raising rupee resources by providing tax incentives for investment as in the case of power bonds: Recognising the need for augmenting the power supply in the country for speedy industrial growth, there was a proposal on issuing "Vidyut Vikas Patra". Similar measures could also be introduced for the shipping industry.

➤ ECB funding: The ECB funding norms need to be suitably relaxed for the shipping industry particularly addressing the withholding tax issue.

Long term shipping contracts and cargo support for Indian flags:

74. The long-term shipping contract is a good method to derive mutual benefits for the owner and the charterer. Indian shipping companies are now well equipped to own and operate ships and compete in the world arena, both in the dry bulk sector, as well as in the wet bulk (crude and petroleum products) sector. The government has a very substantial amount of cargo that it controls, through the PSUs in imports and exports. The government could channelise its shipping requirements of the PSUs and ensure long term contractual cargo support to Indian shipping companies. Such long term contracts would, in turn, enable the Indian companies to invest in Indian flag tonnage and help in the growth of the Indian fleet. Long term contracts and similar cargo support

(including coastal cargo cabotage measures), are also now a necessity for securing funding. Most lenders worldwide are now seeking the comfort of contracts backing up ship acquisitions.

75. In an era of heightened terrorism many nations look at security of critical cargo such as crude oil, coal, fertilisers etc. as a national priority. Accordingly, the control of tonnage for movement of such strategic cargo is consciously built in the national flag. Today's security situation in the country warrants that this aspect also needs to be considered. The essence of energy security is the ability to maintain adequate supplies of energy resources such as coal, crude oil and natural gas at all times at minimum cost. In the evolving context of India's growing energy demand and consequent dependence on global energy markets, there is an urgent need to own and develop a national "core" fleet in the energy sector, similar to the US Sea Lift Command. This core fleet of strategic marine assets can be used in case of national emergency and war time to ensure national security. This core fleet could be deployed in the energy sector with public sector units on long term contracts. This would also indirectly serve as protection against the imperative 2010 phase out of single hull tankers. While the economy benefits in terms of national security, the industry too benefits as long-term contracts lead to lower financing rates, which in turn could be shared with the end users.

76. The 'brand value' of Indian flag can be improved through policies like first right of refusal and cabotage. Indian ownership and Indian flag can be strengthened by making access to Indian cargo via the Indian flag. As Indian trade is booming, ships will be attracted to Indian flag, if there is cargo support. The preference for the national flag in the carriage of national cargo could be through directives from the government as PSUs as well as private sector companies could sideline Indian flag ships or tweak tender conditions to disqualify Indian ships. These issues need to be addressed and the Directorate General of Shipping needs to be appropriately empowered to enable strict implementation of the chartering guidelines as at present the powers are only implied and not explicit.

Infrastructure Status:

77. Shipping industry is the cheapest and largest means of transport in international trade. It is the backbone of any country in trade and commerce. Hence this sector needs to be given the infrastructure status. Being a supporting industry to shipping industry, the shipbuilding and ship repair industry could also be given infrastructure status. Presently, those sectors under infrastructure enjoy the benefits/concessions available under sec.80-IA of Income Tax Act, which provides for a deduction equal to 100 percent of the profits and gains derived from the infrastructure for 10 consecutive assessment years.

Other related services:

78. Ship registry services could be promoted in India. However, this is also related to a low tax regime. India can position itself in logistics services to manage the whole supply chain due to its location. A clear cut plan is needed for this purpose. Ship repair services is another potential area to be tapped where there is need for better marketing and capacity building.

c) Port services:**Better port services and lower port charges:**

79. Since the shipping lines are major port users, the inadequate facilities at various Indian ports seriously affect the operational viability of Indian shipping companies for whom Indian ports are the base ports. It is essential that a holistic approach be followed for improving the existing infrastructure and services at the ports through modernization of the systems with latest technology, capital dredging towards providing drafts at ports and for coordinated development of major and minor ports to exploit the potential of the hinterland on a priority basis. Particularly, the infrastructure facilities at major ports for handling crude oil need to be strengthened through a facilitative policy on single point moorings. The facilities at existing ports with regard to cargo handling, stevedoring, pilotage services, bunker services, warehousing facilities etc. need to be upgraded wherever necessary in order to bring them on par with the leading ports of the world. The transshipment of Indian cargo taking place outside the country at present needs to be handled at Indian ports through concerted measures. This would include increasing the drafts available at Indian ports and rationalization of port dues, providing differential levels of tariff for different sizes of vessels or for different cargoes to attract mother ships to berth at Indian ports. The many port charges in India which are higher than in many other countries is due to inefficiency of ports, and inclusion of unrelated costs like pension & other contributions to port labour in port services. Lower port charges can make our exports more competitive and imports including essential commodities cheaper which is important particularly when supply bottlenecks lead to inflation.

Providing port services by port based SEZs:

80. Services like international bunkering facilities, pilotage facilities, supply of spare parts, ship repairs, etc., could be provided by port based SEZs.

Corporatising port trusts (minus excess land):

81. Port trusts have larger funds and lot of idle land. They could be converted into public listed companies with atleast 49 percent shares held by the general public.

d) Construction services & project exports:

82. Some of the issues for construction services & project exports include the following:

- Using the standard contract document for all domestic civil engineering projects and need for consortiums to bid effectively for international projects.
- Low-energy buildings using sunlight has great demand with the emphasis on climate change. Even the existing buildings in UK and some other developed countries are being redesigned and modified to be environment friendly. This opportunity needs to be explored.
- There is demand for engineering & architectural services. But foreign companies consider that it is not easy to find companies for tie-ups as information is lacking on India's capability and capacity of SMEs is not known abroad.
- Resolving the issue of precondition in most of the overseas tenders floated by clients wherein equipment to be supplied by the contracting company should necessarily be sourced from approved list of suppliers from developed countries; examination of the need to consider double guarantee avoidance treaty on the lines of double taxation avoidance treaty as overseas clients insist on Bank Guarantees (BGs) to be issued under the contract to be routed through a local bank operating in the country of project execution which results in Indian contracting companies being called upon to pay the BG charges to Indian banks as also to the local overseas banks which issue the final end guarantees to the client, based on the counter guarantees from the Indian banks; and reduction of delays in international bidding due to formalities at different levels of the government; and reduction of delays in international bidding due to formalities at different levels of the government.

e) Healthcare Services:

International Accreditation:

83. Responsibilities are divided between centre and states in the case of healthcare services and there is a need for international accreditation system along with national standardized accreditation system. There are various accreditation systems adopted in different countries. USA is the first one to have an accreditation programme as early as in 1950's (Joint Commission Accreditation for Health Organisations (JCAHO)). Canada set up its accreditation (Canadian Council for Health Service Accreditation) in 1958, followed by Australia (Australian Council on Healthcare Standards). There are currently around 40 countries that have set up accreditation programmes for healthcare services. Some countries such as USA have more than one accreditation systems (apart from JCAHO, USA also has American Osteopathic Association's Healthcare Facilities Accreditation Programme (AOA-HFAP), National Committee for Quality Assurance (NCQA) and Accreditation Association for Ambulatory Healthcare (AAAHC)). External assessment of

healthcare services is being increasingly used to regulate, improve and promote healthcare services all over the world. In many countries, external assessment of healthcare services is in demand by governments, healthcare professionals, patients and communities. Various external evaluation models include accreditation, peer review, inspection by external agencies, evaluation and certification, or other frameworks. Such models are evolved to meet changing demands of the customers and regulators, which include public accountability, clinical effectiveness, and improving the quality and safety of services and their outcomes. Though India has witnessed a number of international accreditations, they were either found to be expensive or not tailored for the Indian healthcare industry. The Quality Council of India (QCI), an autonomous body set up by the Government of India, announced the National Accreditation Board for Hospitals and Healthcare Providers (NABH), a not-for-profit initiative to make available accreditation standards at lower costs. Accredited hospitals are also potential winners in attracting medical tourists. International accreditation would be an important step in making the hospitals eligible for the coverage with foreign insurers. For example, the Joint Commission International (JCI) seal would enable Indian hospitals to be accredited with US insurers. This in turn would attract customers from other parts of the world and thereby increase their profitability also. A growing number of hospitals in India have turned to accreditation agencies worldwide to both standardize their protocols and project their international quality of health care delivery. Accreditation also helps continuous improvement of risk management practices in the healthcare organization and thereby helps in risk reduction. International accreditation would also reduce the rigour of undergoing a separate national government evaluation process and help in achieving prerequisite of insurance reimbursements.

Tapping the potential for export of healthcare services:

84. These include the following:

- Monitoring elderly population in UK, US and other developed countries is a potential service, where India can be successful.
- UK Government has allowed 15 percent of NHS to be outsourced to private sector. There is a need to exploit the potential of outsourcing health services for UK's NHS as there is huge opportunity and increased interest in UK in using technology and internet based health services from India. There is potential in UK for Public Private Partnerships (PPPs) in healthcare sector and there are no restrictions on opening hospitals in UK.
- Patients under NHS in UK are allowed to go to Spain and some other countries for medical treatment and not to India. This is because issues like quality regulations and liability laws in case of death of patient, etc., are involved. India needs to address these issues and tap the opportunity.

- There is also demand for financial and accounting services from India in health sector of developed countries like U.K. which needs to be tapped. Helping companies to get funding for under funded healthcare facilities in US by taking advantage of tax savings provisions in US is a trillion dollar business. There is scope for outsourcing this to India if Indians are familiar with US tax laws. The model of using US citizens of Indian origin is successful.
- Negotiating for removal of market access barriers and recognition of technical degrees by other countries, developing India as a regional healthcare hub, tie-ups with some developed countries under Comprehensive Economic Cooperation Agreements (CECAs) and setting up Health Consultancy Parks which combine both preventive and curative health care with tourism are some other suggestions.

Stem Technology Research:

85. Stem technology research should be encouraged by India. But application of stem technology by different private hospitals/clinics needs to be monitored and a decision should be taken regarding their genuineness and also pricing. A standard policy is needed in this regard. The Clinical Establishments (Registration & Regulation) Bill, 2007 approved by the Union Cabinet is particularly relevant in this context.

Reforms in Government healthcare services:

86. The CGHS system and similar systems of state governments and semi-government institutions need a complete overhauling with outsourcing to private sector in a big way. This will not only lead to quality services, but also result in saving of manpower, space and possibly medicines. The space used for the CGHS clinics can be put to other profitable uses.

f) Accounting, Auditing, Bookkeeping and Legal Services:

87. The policy suggestions for these services include the following:

- Tie-ups to overcome the weakness of small size of domestic accountancy firms.
- Overcoming limitations related to licensing and accreditation by meaningful negotiations with other countries and tapping fully the potential of outsourcing many components of these services.
- Allowing representative offices of foreign law firms to practice non Indian law in India on a reciprocal basis.
- Tapping outsourcing in niche areas like actuarial and accountancy services as there is good scope for outsourcing actuarial services and accountancy services to India including setting up back offices. But Indian service producers need good training on US tax laws and laws related to insurance, pension etc. Even para legal services (like Assistant Attorney) has scope if there is practical understanding of US laws.

g) Financial Services:

Mergers and acquisitions:

88. These are needed to strengthen capital base of Indian public and private sector banks and financial institutions (FIs) including acquisition of small banks by big banks. Merging of core competencies of financial institutions with those of commercial banks can also bring in the much needed consolidation in the domestic financial sector.

A coordinated policy for setting up bank branches:

89. This is needed to avoid mushrooming of banks in the same place in cities with the same business shared by all. Mergers and acquisitions could also help in achieving this objective.

Operationalising offshore financial centres by removing any hurdles:

90. The report on Implementation Model for Free Ports in India has suggested the setting up of offshore banking units in SEZ's. The report of the High Powered Expert Committee (HPEC) on 'Mumbai: An International Financial Centre' has suggested the setting up of International Financial Centre in Mumbai. These need to be examined and a decision should be taken for their implementation and the time-frame for implementation. Some of the recommendations of the HPEC include the following:

- The most critical financial market components missing in India are: a properly functioning bond market, a currency market and a derivatives market for currencies and interest rates. These three interlinked markets are termed collectively as the bond-currency-derivatives (BCD) nexus. The HPEC recommends the immediate creation of a currency spot market, with a minimum transaction size of Rs.10 million, accessible to all financial firms. In addition, an INR-settled exchange traded currency derivatives market should be created, with trading in futures, options and swaps on currencies, accessible to all.
- The setting up of the IFC would help in removing the deficiency in India of not having a universe of institutional investors that have the size visibility and capability of those in established IFCs.
- HPEC also recommends opening up fully to foreign investment in INR denominated sovereign bonds issued by Government of India.
- Replacement of rules based regulation by principles-based regulation as suggested by Kelkar Committee report, inclusion of financial services under GST with simultaneous removal of all central and state transaction taxes including the Securities Transaction Tax (STT), stamp duties, etc.
- Inducing greater competition and innovation in the Indian financial system by
 - Removing existing barriers to entry of private domestic corporate players in some segments of the financial services industry.

- Removing barriers to the entry of foreign financial firms in the provision of IFS on the grounds that unilateral liberalization is in India's own interests.
 - Restricting demands for reciprocal market access only to domestic financial services.
 - Reducing the extent of public ownership progressively in Indian financial institutions.
 - Removing existing barriers to friendly or hostile mergers, acquisitions and takeovers in the financial services industry within/across market segments; and
 - Encouraging the emergence of Indian Large Complex Financial Institutions (LCFIs) through market-driven initiatives.
- Improving the performance of the legal system for finance/IFS. HPEC has recommended significant improvements in the Indian legal system in resolving disputes, adjudicating settlements and enforcing financial contracts in real time. If that does not happen the prospects for Mumbai emerging as an IFC, or aspiring to become a GFC, will be irreparably damaged.
- Opening up space for IFS support services infrastructure. Related to improvements in the legal system as they apply to finance and IFS, the HPEC recommends opening up domestic space to permit the entry of well-known international law firms that operate in other IFCs and GFCs as well as international accounting firms and tax advisory firms as well as specialist management consulting firms focusing on the IFS industry. This recommendation is made so that India can catch up quickly with the rest of the world in becoming a competitive provider of IFS through an IFC in Mumbai. It will not do so if it is left to existing domestic law, accounting and tax advisory firms to develop domain knowledge and skill-sets organically – in coping with the demands for IFS related legal, accounting, tax and business advisory services – without being confronted with the pressures of competition and innovation in their market.

91. The recommendation of a well-functioning BCD nexus where all these three separate markets work as a seamless whole, if adopted with proper checks & balances could help in the speedy transmission of monetary policy including checking inflation with marginal hikes in interest rates and easier access to external funding. IFCs would enable India to shift from exporting its best financial talents permanently, to retaining a hold on such talent in the future by providing greater global mobility.

Issue of limit on bank branches and ATMs of foreign banks in India:

92. Though India is going beyond the WTO commitments in the case of bank branches, there is a general feeling abroad that India is limiting branches of foreign banks. There is also difficulty in getting license for ATMs of foreign banks. This issue needs to be examined and corrective steps taken. The Budget 2010-11 has stated that the RBI is considering giving some additional banking licences to private sector players.

Potential for insurance business overseas:

93. There is a need to tap the huge foreign business by Indian insurance companies by encouraging them to venture outside India.

Supply-chain financing:

94. There is a need to focus on effective and market leading supply-chain financing, which is an agreement between a bank, buyers and suppliers in which buyers can utilize bank financing to extend their own payment terms while ensuring that participating suppliers have the liquidity needed to operate and grow.

Suggestions of the Committee on Financial Sector Reforms:

95. Many committees have come up with different suggestions to reform the financial sector. There is a need to take a view on these suggestions and set up a specific time frame for the actionable suggestions. The Committee on Financial Sector Reforms (Raghuram Rajan Committee) which is the latest among them has come out with several suggestions for the financial sector. Some of the suggestions which could be considered are the following:

- Warehouse receipts as negotiable instruments for farmers to get credit.
- Steadily opening up investment in the rupee corporate and government bond markets to foreign investors after a clear monetary policy framework is in place.
- Liberalising the Banking Correspondent Regulation so that a wide range of local agents can serve to extend financial services.
- Encourage the entry of more well-capitalized ARCs (Asset Reconstruction Companies) including ones with foreign backing.
- A well functioning bankruptcy code that neither protects the debtor at the expense of everyone else including employees, as our current system does, nor one that allows secured creditors to drive a well functioning firm into the ground by seizing assets.

Extended Banking Arrangements:

96. The Indian financial services sector has shown resilience amidst the global financial crisis. However, there is a need to set up a strong operational structure that would make the current financial system in the country more robust not only from any external exigencies but also internally. As on March 2009, there were 80 commercial banks (excluding Regional Rural Banks - RRBs); 4 local area banks; 86 RRBs; 1,721 Urban Cooperative Banks; 4 development finance institutions apart from 12,739 Non Banking Financial Companies in the country. With the advent of aggressive private sector banking in the country, it may seem imperative for the smaller banks present in the country to change their existing structure to stay 'alive'. Consolidation of smaller banks or merging with bigger banks is one option. Another option may be

technology infusion, which may enable to bring down the cost of the small banks considerably. However, another possibility is a greater coordination amongst the existing network of banks. It is a matter of fact that the Banking system in India is spread wide and far with a concrete network and this is made even stronger by the presence of a number of Regional Rural Banks in the interiors of the country. A paradigm shift will be the creation of a platform wherein the unique services offered by select banks is utilized at select branches through an exchange-sharing basis. The intent is to bring local knowledge to bear on the products that are needed locally, and to have the locus of decision-making close to the banker who is in touch with the client, so that decisions can be taken immediately. It would also offer an entry point into the banking system, which some Banks can use to eventually grow into large firms. This will also augment the Banks' businesses without incurring operational costs. There is scope for considering expanding reach by working with and through local institutions, selected through a screening process and with clearly defined limiting role to serve as extension of the banking industry. The Raghuram Rajan Committee 2008 recognizes the fact that these small banks have not been able to distinguish themselves in India often due to poor governance structures, excessive government and political will or interference and the unwillingness/inability of the regulator to undertake prompt corrective action. So one of the suggestions of the committee is to liberalize the Banking Correspondent Regulation to enable a wide range of local agents to extend financial services.

Climate change related financial schemes/instruments:

97. Since climate change issues are gaining in importance, financial services sector should also include instruments related to climate change. These include the following:

- Developing insurance schemes against climate related risks. Developing public-private risk transfer programmes i.e. Index based livestock insurance as in the case of Mongolia, catastrophe bond as in the case of Mexico, catastrophe risk insurance facility as in the case of the Caribbean could be examined.
- Carbon markets: Structured emission products, carbon funds, emission price indexes, EUA/CER swaps, voluntary credits, avoided deforestation/REDD, synthetic portfolios, carbon securitization.
- Equities: Portfolio screening, SRI (Socially Responsible Investment) funds, Low-carbon technology stocks, index products.
- Bonds: Portfolio screening, forestry bonds.
- Private Equity/Venture Capital: Carbon venture capital, carbon-driven principal investing.
- Real Estate: Energy efficiency/green building real estate investment trusts.
- Hedging Instruments: Weather derivative products, catastrophe bonds, insurance products.

h) Tourism services:

98. Some of the issues related to tourism services are the following:

- Issue of visas on arrival for select countries.
- Establishing special tourism police force which can help in growth of tourism services as well as provide employment.
- Slum clearance with proper resettlement facilities and stopping begging on a priority basis.
- Promoting services like trade fairs and exhibitions by setting up convention centers. It is really a pity that India does not have a convention centre for international exhibitions in Mumbai, the financial capital of India. Even the annual Gems & Jewellery Expo is organized in an old factory shed. State governments should give land for such convention centres which could even be on a PPP basis. Funds from schemes like Assistance to States for Developing Export Infrastructure and Allied Activities (ASIDE) of government of India could be given for them.
- A holistic approach to promote tourism services is needed. If this is done on mission mode, with focus on providing quality services in tourist places, safety for tourists, security in cities, then the foreign exchange earnings from this service can increase manifold with multiplier linkage effects.
- Changing urban land use rules to separate land use for hotels from commercial land use and defining transparent rules for setting up of hotels in mixed use locations and the borders between commercial and residential areas (subject to provision of internal parking and adequate size roads for access).
- Allowing railway passenger services by private sector to important tourist destinations.
- Creating holiday homes by utilizing idle resources with public sector units. Many public sector units have holiday home facilities availed by employees at nominal prices and these often remain unused and are also not well maintained. A public private partnership for more efficient utilization of these facilities could not only generate enhanced revenue streams but also continue to make available the facility to employees on a more commercial basis. This could be achieved, for instance, through tie-ups with agencies that offer such facilities on their own, often nationwide. This could even include guest houses of central/state governments and port guest houses.

i) IT and related Services:

99. India has a brand equity in IT services. However, the full potential has not been tapped even in this sector. Some issues related to these services are the following:

- Need to address the issue of weakness of India in retesting computer software.
- Need to improve the quality of the new-breed of IT professionals as there is a feeling abroad that the new talent pool in IT is not as efficient as the old pool,

particularly when new competitors have emerged like the low-cost Bolivian competitors in the US market and the new favourites like Poland and Hungary in European market.

- As a result of global recession there is a fall in BPO services exports of India which may be due to the fact that this is low level stuff which youngsters in UK and other countries are pushed into these days by respective governments. This trend is likely to continue in the future. In the light of competition in BPO from countries like Ukraine, China, Bolivia, South Africa, etc., and policy in countries like UK to employ locals, there is a need to examine whether India should shift focus from this low-end service to only high-end services like programming. Policies for IT services should also include steps to move to systems software coupled with hardware-software combination, and further progress in application software.
- Need for Data Protection Act as EU and other developed countries are very particular on data protection as half of offshore work does not come to India due to this. This should be on the lines of EU Safe Harbour Decision and EU directives on data protection. This will help in tapping the EU market, reduce cost and avoid litigation. The IT Amendment Act includes this issue. This Act needs to be modified and implemented urgently.
- Concluding totalisation agreements with target countries to resolve the social security benefits issue and making necessary changes in domestic laws.

j) R&D Services and Consultancy Services:

100. Trade in R&D services has high potential. India has the capacity and reputation as people working in these labs are brilliant and considered to be better than those in countries like China. But there is a need to do enough R&D locally. Healthcare, electronics and biotech are the key areas. Problems in India are also due to IPRs. While the IPR laws are good, litigation takes a long time and Indian legal system has not understood the IPRs. This needs to be addressed.

101. Other policy measures for R&D services could include setting up R&D labs in SEZs, examining the possibility of cheaper loans taking note of the gestation period in R&D services, patent funding to reimburse costs of patenting, promoting lab testing services for use of South Asian countries in India and setting up design, engineering and consultancy parks.

102. In the case of consultancy services, there is a need for international accreditation for consultancy institutions/ associations.

k) Satellite Mapping Services:

103. Negotiating with US, EC and other developed and developing countries regarding defence restrictions; examining possibilities of sharing some common facilities and data of public sector institutions like ISRO with private sector; consortium bidding and including government institutions like ISRO in the consortium; partnering with other countries for launching and tracking of satellites as ISRO is ready for it, though risks have to be lowered; and tapping the potential to export to all the 42 markets identified are some policy suggestions for this sector.

l) Education Services:

104. Some policy issues in the education services are the following:

- Replacement of bureaucratic controls on educational institutions by professional regulation and encouraging public-private partnership in education. Rating the quality of educational institutions (public and private) at all levels of education and education service providers (public and private) is a must as there has been a mushrooming of technical institutions in recent years with low quality of faculty and infrastructure. Entry of registered societies (non-profit) and publicly listed (education) companies in all fields of education, subject to the regulatory framework which ensures quality and reasonable pricing needs to be covered. Regulated entry of large quality foreign and rated domestic institutions should be allowed in higher education.
- Some institutions of higher education like medical colleges are found mainly in some states, with even Delhi having few medical colleges with fewer seats, while the demand is very high for such education. This needs to be addressed on a priority basis by reviewing the built in space norms and patient load factor norms to be in tune with present day equipment intensive care and modern practices and procedures.
- Passing the right to Education Bill ensuring free and compulsory education to children in 6-14 age group. This has now been passed. What is now needed is its proper implementation.
- Targeted and outcome oriented review and reform of elementary education is needed.
- Merit should be given utmost importance in medical education and jobs in the medical sector, as even relatively less qualified doctors cannot be allowed to play with the life of the people.
- There is a need to revamp the system of teaching, curricula, research etc. in the universities and Institutions. To begin with, university courses particularly economics, finance & management-related should be set in consultation with policy makers in these areas and business chambers. A quick study of the courses & pattern of teaching in the different universities in India should be done and in case of any government funding for universities, it should be mandatory to include a policy maker and member of Trade & Industry in deciding the

course & teaching pattern of these subjects. This will help in making university education and research in institutions relevant to present day needs.

- Phased introduction of education reforms may be needed, given the fact that state governments are also involved. While states may oppose centralization of selection process for higher education, they could be persuaded to accept common entrance tests for technical education which could be one of the components in the selection and the other components like marks in the qualifying exams may be decided by the states.

m) Waste, disposal and sewage services:

105. There is a need for privatization of sewage services. Charges on sewage services can be based on property value as done in UK or some other criteria like, say size of family.

n) Unskilled labour Services:

106. Training and skill certifying labour before they go abroad as done by countries like Philippines, Thailand and Sri Lanka can help unskilled labour services.

2) Domestic Regulations:

107. One major issue in services is the domestic regulations in India. Using the strict definition as indicated in the WTO documents, domestic regulations basically include licensing requirements, licensing procedures, qualification requirements, qualification procedures and technical standards. Since domestic regulations perform the role of tariffs in regulating services, we have to list the domestic regulations in India which need to be disciplined to help growth of the sector and exports, while retaining those domestic regulations which need to be retained at this stage. There is also a need to list the burdensome domestic regulations in our major markets which deny market access to us and therefore need to be negotiated at multilateral and bilateral levels.

108. As per the World Bank & IFC publication "Doing Business 2010" India ranks 133 among 183 countries in the ease of doing business with Singapore at 1st rank, China with 89th rank and almost all the countries of South Asia including Pakistan, Bangladesh, Srilanka, Nepal and Bhutan with better ranks than India. This indicator consists of 10 sub indicators, namely, starting a business, dealing with construction permits, employing workers, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts, closing a business. Interestingly in trading across borders, India was the top reformer in 2006/07 (as per Doing Business 2008) though it ranked at 79. It introduced online customs declarations for imports and exports. Arriving ships now submit their cargo manifestos electronically, allowing the clearance to begin even before the ship docks. These reforms helped cut delays for exporters and importers by 7 days. In the case of getting credit and protecting investors, India's rank is fairly good. However in the case of other indicators, India is far behind many other countries. For example, to start a business there are 13 procedures and 33 days are needed and for closing a business 10 years are needed. These are mainly due to domestic regulations like licensing and procedural delays. The difference between different cities in India is still sharper with the time to obtain a business license in India ranging from 159 days in Bhubaneshwar to 522 in Ranchi and the time to register property from 35 days in Hyderabad to 155 in Calcutta. So there is a need to look at the different domestic regulations in India to ease the burden of doing business. These domestic regulations not only affect manufacturing but also services.

109. Some important domestic regulations in India which need to be examined for suitable policy reforms in different service sectors are given below. This is only an indicative list and by no means an exhaustive list.

(i) Domestic regulations: sector specific

110. Some important sector-specific domestic regulations in India are given below:

Transport services

- Restrictions on inter-state movement of goods and coordination issues between government departments in the case of multimodal transportation and need for changes in Merchant Shipping Act and Multimodal Transportation of Goods Act, 1993 to support easy transportation and documentation through different modes of transport.
- Restrictions on free movement of cargo between ICDs, CFSs and Ports.

Construction, engineering and related services

- Restrictions like minimum capitalization norms, some restrictions on repatriation, minimum area norms and a general umbrella clause that all applicable rules/ bye laws/ regulations of the state government/ municipal/ local body concerned have to be complied with.
- Restrictions under the Urban Land Ceiling and Regulation Act (ULCRA). According to this Act, no person is entitled to hold any vacant land, in excess of the ceiling limit stated by the Act. This law in effect prevents anyone from buying a large tract of land to construct houses. The law also vests discretionary powers in state governments to grant exemptions, leading to corruption in the exercise of these powers. Further, the government has the power to acquire the entire surplus vacant land above the ceiling at a nominal price, leading to lengthy disputes and litigation. Consequently, competition in housing construction is not based on costs but on securing access to lands and circumventing the regulatory impediments. This is one of the reasons for construction services firms in India to operate at a small scale, and not exploiting economies of scale.

Healthcare services

- While there is no cap on FDI in health services, foreign individuals are prohibited from providing services for profit and their movement is subject to registration by Medical/Dental/Nursing council of India.

Accountancy services

- While FDI is not allowed in this sector, foreign service providers are not allowed to undertake statutory audit of companies as per the provisions of the Institute of Chartered Accountants of India and the Institute of Company Secretaries of India Acts. There are also different domestic regulations like ban on use of logos of accounting firms which need to be disciplined to facilitate tie-ups and penetrate foreign markets given the potential for exporting these services by the outsourcing mode.
- The accountancy service providers in India are self-regulated through a combination of legal and professional bodies like the Institute of Chartered Accountants of India (ICAI) and the Institute of Cost and Work Accountants of India. The accountancy professionals are only allowed to operate either as a

partnership firm or as a sole proprietorship firm. Since the Partnership Act of India permits only 20 or less professionals under one firm, this de facto means that the number of partners in Indian accounting firms are limited to 20 or less. Further, the number of statutory audits of companies per partner are restricted to 20. Indian regulations also proscribe inter-disciplinary professional models, i.e. accounting firms are not allowed to hire management professionals to perform consulting/ management services. As a consequence of the above restrictions, less than 200 firms (or 0.5 percent of total accountancy firms) have more than 10 partners. As stated by the World Bank study due to their small size, domestic firms have been less successful in competing with international firms in the lucrative consultancy/advisory and non-statutory work markets.

Legal services

- FDI is not permitted and international law firms are not authorized to do advertising and to open offices in India.
- Foreign service providers can neither be appointed as partners nor sign legal documents and represent clients. Bar council is opposed to entry of foreign lawyers/law firms in any manner. Indian advocates are not permitted to enter into profit-sharing arrangements with persons other than Indian advocates. With recent developments like outsourcing of administrative work of legal firms of UK and other countries, there is a need to be more open on legal services to at least facilitate overseas firms to outsource legal services to India. Countries like UK have opened up legal services for other countries including India.

Education services

- Education in India comes under the concurrent list with multiple controls and regulations by central and state governments and statutory bodies.
- Regulations with respect to establishment of new medical colleges, patient load factors which need to be reviewed to be in tune with present day equipment intensive patient care and modern practices and procedures of medical education.

Infrastructure services

- Regulatory framework which needs reforming include the following:
 - Bid/procurement process which needs to be efficient, transparent and standardized.
 - Contractual structure / concessions / incentives where clarity is needed and adoption of equitable contract as under FIDIC or CIDC guidelines.
 - Pre-qualification norms which needs to be defined well.
 - Regulatory approvals which need to be single window approvals.
 - Dispute resolution mechanism, the effectiveness of which needs to be enhanced.
 - The legal definition of infrastructure which needs to be harmonised.
 - Investment guidelines for debt & equity instruments which need to be liberalised.

- A strengthened public private partnership (PPP) initiative can attract private sector investment, particularly in infrastructure if suitable reforms in regulatory framework are adopted as indicated above along with strengthening the viability gap funding mechanism.

Financial services

- There are many regulations under the Banking Regulation Act which at present has the requirement that banks obtain regulatory approval for a range of routine business matters including opening branches, remuneration to board members and even payment of fees to investment bankers managing equal capital offerings as pointed out in the Raghuram Rajan Committee report.
- In the case of insurance, besides cap on foreign investment of 26 percent, restrictions like minimum capitalization norms, funds of policy holders to be retained within the country, compulsory exposure to rural and social sectors and backward classes.

Entertainment services

- Regulations related to cable TV channels like getting license and having an agent in India to downlink channels needs to be examined.
- The issue of valuation of customs duty on DVD including royalties which needs to be addressed.

Distribution services

- The major issue is FDI being not allowed in retail trade except single brand product retailing with 51 per cent cap as stated earlier.

(ii) Domestic Regulations: General

111. Some important domestic regulations of a general nature are given below:

- Restrictions on the operation of domestic firms are still maintained in a number of services sectors and these need to be addressed. For instances, laws in road transport, quantitative restrictions in financial and accountancy services, administrative and regulatory burdens in construction services and overlapping responsibilities with regard to multimodal transport have contributed to creating fragmented and uncompetitive industry structures. Domestic service providers have thus not been able to attain economies of scale to enable them to function more efficiently.
- Need for a competition policy for services in India and a regulatory body. There are regulators for some services like banking, insurance, telecom and ports. While there are no independent regulators for most professional services, de facto regulation takes place through a combination of statutes provided in law and by professional all-India and state councils. These include the Institute of Chartered Accountants of India and the Institute of Cost and Works Accountants of India, the Council of Architecture, the Bar Council of India and the State Bar Councils and the Medical, Dental and Nursing Councils of India. The unevenness of standards in professional, educational, financial and health

services are not only a problem domestically but also legitimize foreign restrictions and, therefore, need to be addressed in order to make a credible case for obtaining foreign recognition. So there is a need for the creation of a credible, all-India accreditation system that could grade different attributes in terms of training and experience in these services. For a variety of other network services, including transport (terminals and infrastructure), and energy services (distribution networks), there is a need for regulators.

- Transfer pricing which is aggressively attacked by India as mentioned earlier.
- Indian laws like prohibiting night shifts for women and laws related to contract labour affect different services. For example under the Factories Act, 1948, section 66B, night work for women (beyond 6 AM -6 PM) is prohibited, though state governments give some exemptions under Shop & Establishment Act, as in the case of BPOs. These laws prohibiting women in night shifts should be removed, but safety norms for women working in the night should be ensured.

2) Market access issues

112. This is another important issue as domestic regulations and policies in India's major services markets deny market access for India's services exports. Market access barriers can be due to domestic regulations, subsidies or other barriers. Some examples are given here under the different categories.

(i) Due to domestic regulations

113. Some examples of market access barriers due to domestic regulations include the following:

- In the case of business services and IT services, in the US, licensing of professional service suppliers is generally regulated at state level. In addition, there are the 'Buy American' provisions.
- In the case of legal services, in US the system and requirements are set by the concerned state bar associations and therefore differ from state to state.
- In the case of communication services, non-US firms and foreign-owned firms wishing to invest in radio telecommunications infrastructure and to provide mobile and satellite services are virtually denied access due to stringent legislation in US. The events of September 11, 2001 have added a new dimension to these market access limitations with US law enforcement agencies imposing strict corporate governance requirements.
- In the case of financial services, the restrictions are the requirement of the Office of the Comptroller of the Currency (OCC) and some state banking supervisors to maintain "asset pledges" in addition to the paid up capital they maintain in their home country. Further, foreign insurance companies seeking to operate in the US market face the fragmentation of the market into 56 different jurisdictions and direct discrimination on a number of fronts, such as

need for foreign insurance companies to first be licensed in another state before seeking a license in the first state to underwrite risks in one state.

- Difficulty in opening bank branches in USA and other developed economies and restrictions even after licensing while it is absent in India.
- Need in some states of US for foreign insurers to buy reinsurance from state-licensed companies before allowing re-insurance premiums to leave the state.
- In the case of transport and related services, in the US there are restrictions in foreign ownership of air carriers, restrictions related to foreign repair stations; various forms of assistance in US to its domestic shipping industry such as the reservation of a minimum of 50 percent of government cargo for US registered ships, all cargo provided with loans from the US Exim Bank to be reserved for US registered ships though a 50 percent waiver may be granted, restrictions in domestic commercial shipping where the US requires shippers operating in internal waters to use ships that were built in the US.
- Discrimination by the Federal Maritime Commission (FMC) between foreign shipping companies and US ships by unilaterally regulating the shipping fees charged by foreign shipping companies; significant restrictions on the use of foreign built vessels in the US coastal trade under Jones Act; prohibition on foreign built vessels for documentation and registration for dredging, towing or salvaging in the US; ensuring terms of shipment favourable to US, while not being liberal in allowing foreign ships to operate in US; the application of restrictive measures to US public procurement contracts which require the goods to be shipped in US-flagged vessels, which charge significantly higher freight rates than other vessels.
- In the case of construction and related engineering services and urban planning and landscape services, “Buy American” or “Buy local” legislations passed in many states of US have gone to the ridiculous extent of even insisting on the materials used (i.e. cement) to be of domestic origin for construction of public works projects financed by state funds.
- In EU, there are restrictions in audio-visual services. For example, France provides that at least 60 percent of movies on television must be made in Europe and that more than 40 percent of the programmes must be broadcast in French.
- In the case of travel services there is the issue of high visa fees for Indian citizens by UK.
- The latest protectionist policies in US and other economies like the conditions in U.S. bailout package related to employment of non-U.S. nationals and moves against outsourcing are the new domestic regulations denying market access to other countries.

(ii)Due to subsidies

114. Subsidies also act as market access barriers. Some examples are also follows:

- In the case of transport & travel services, the huge subsidies in the civil aviation sector to aircraft in both US and EU act as indirect market access barriers.
- There is a subsidy programme providing an operating cost subsidy of \$100 million a year for a period of ten years for US registered ships meeting certain requirements

(iii) Other Barriers

115. There are also some provisions like those related to taxes, protection of titles and provision of some social services which may also act as market access barriers. Some examples are given below:

- In the case of port services there is the issue of Harbour Maintenance Tax (HMT) and Harbour Services Fee in US only on waterborne imports, at an ad valorem rate of 0.125 per cent while it is prohibited for exports.
- In the case of ship repair services, US applies a 50 percent ad valorem tax on the cost of equipment and non-emergency repairs for US flag vessels done outside US. US owned foreign-flag vessels are not subject to the duty and under NAFTA and the Chile and Singapore FTAs, this duty was eliminated. This is a tax or an example of tariff barrier on services by US !
- In the case of legal services in Sweden, under WTO commitments the Swedish title “advokat” is protected. Thus virtually non-citizens cannot use this title. Now under the conditional revised offers (2005) of EU, this has been cleverly reworded as follows: “Admission to the Bar necessary only for the Swedish title “Advokat” which is subject to a residency requirement.” Though foreign lawyers can freely offer legal services when not appearing under the title “advokat”, this protection creates an barrier in the form of Grade A and Grade B lawyers.
- In the case of healthcare services in UK, the provision of free medical services to all UK citizens under the NHS system acts as an invisible market entry barrier. This possibly even helps the export wing of the NHS.

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