

# kcmFlash

## Transaction Advisory

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## IFSCA issues circular widening the scope of activities covered under the ship leasing entity framework!

### Background

In August 2022, the IFSC Authorities introduced a new framework (Circular No. 496 / IFSCA / FC / SLF / 2022-23 / 001) wherein ship leasing entities could operate from the IFSC jurisdiction and hence avail the various benefits of the IFSC. This framework ("prior framework") was an innovative scheme for Indian shipping industry, where the ship leasing entities will enjoy income tax and GST exemption. However, the eligible activities were restricted predominantly to finance and operating lease and keeping the ship operators out. Hence, although the framework made it lucrative to carry out ship leasing activity from India, the ship owners were reluctant to enter the IFSC since they had to source such 'excluded transactions / activities' from offshore jurisdictions. Consequently, a pressing need arose for a more inclusive framework which would be successful in attracting global ship owners and operators to the IFSC. IFSCA has attempted to serve this need by means of amendment to the existing framework vide Circular No. 496 / IFSCA / FC / SLF / 2022-23 / 002 dated March 22<sup>nd</sup>, 2023.

### Highlights and Rationale

Inclusion of voyage charter and contract of affreightments in the permissible activities under ship leasing framework

In the global maritime industry, ship chartering is the most essential activity in order for ship operators to provide maritime transportation

services. Ship chartering transactions may be broadly classified into 3 main categories –

- Voyage charter (includes crew, stores, insurance etc.)
- Time charter (leasing of vessel)
- Bareboat charter (excludes crew, stores, insurance etc.)

From among the above, voyage charter is the most basic form of ship chartering, and one of the more popular methods of ship chartering in the industry.

Further there are also 'contracts of affreightment' which is similar to voyage charters and include commitment for multiple voyages.

In the prior framework, permissible activities included operating lease of vessels, and lease contracts were to be construed as such in light of the principles for classification of leases provided under Ind AS 116. Based on Ind AS 116, contracts like voyage charter contracts and contracts of affreightment were classified as service contracts (i.e., not lease contracts). Hence they were not permitted to be carried out in the IFSC jurisdiction under the prior framework.

Now, the IFSCA has explicitly included voyage charters and contract of affreightment as a permissible activity, under the broad category of ship leasing in the IFSC jurisdiction.

In addition to inclusion of voyage charters, the amendments have also included asset management

support services to all the group entities of the lessor as opposed to the earlier narrow scope which permitted provision of such services only to the lessor, its wholly owned subsidiary (WOS), and the branch of such WOS set up in IFSC.

### Conclusion

The IFSCA's thoughtful approach to industry feedback is evident in the introduction of amendments aimed at establishing India as a global maritime hub. These changes will open up opportunities for a large number of shipping industry players, not just Indian entities but foreign ones as well (a foreign entity can be registered in IFSC). For operators dealing with India, this would be beneficial compared to top jurisdictions like Bahamas, Liberia, Panama, Marshall Islands, Malta, UAE and Singapore, since this enables complete

income tax and GST exemption, with significantly reduced risk of POEM and transfer pricing.

The shipping industry is an industry with a lot of intricacies, many specific to the sector. Hence, a careful analysis will be required for restructuring entities/operations. A thorough analysis will be necessary to navigate transfer pricing implications, GST considerations, cross-border income tax and VAT issues, treaty matters, PE issues, POEM requirements, and related challenges when structuring.

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*For further analysis and discussion, you may please reach out to us.*

## Locations

### Ahmedabad

**Arpit Jain**

Level 11, Tower B,  
Ratnaakar Nine Square,  
Vastrapur,  
Ahmedabad - 380 015

Phone: + 91 79 4910 2200  
[arpit.jain@kcmeha.com](mailto:arpit.jain@kcmeha.com)

### Bengaluru

**Dhaval Trivedi**

FF - 4/1, Rudra Chambers,  
4th main, Between 8<sup>th</sup> & 9<sup>th</sup>  
Cross Rd, Malleshwaram,  
Bengaluru - 560 003

Phone: +91 99983 24622  
[dhaval.trivedi@kcmeha.com](mailto:dhaval.trivedi@kcmeha.com)

### Mumbai

**Bhadresh Vyas**

315, The Summit Business Bay,  
Nr. WEH Metro Station,  
Gundavali, Andheri East,  
Mumbai - 400 069

Phone: +91 22 2612 5834  
[bhadresh.vyas@kcmeha.com](mailto:bhadresh.vyas@kcmeha.com)

### Vadodara

**Milin Mehta**

Meghdhanush,  
Race Course,  
Vadodara - 390 007

Phone: +91 265 2440 400  
[milin.mehta@kcmeha.com](mailto:milin.mehta@kcmeha.com)