CHAPTER-II

SPECIAL ECONOMIC ZONE (SEZ) IN HISTORICAL AND PRESENT SCENARIO

2. Introduction

India was one of the earliest to have Export Processing Zone (EPZs). Following Shannon in Ireland in 1965 and Mayagaez at Puerto Rico in 1965, the first Asian EPZ came up at Kandla in 1965. This was followed by the Santa Cruz Electronics Export Processing Zone (SEEPZ) at Mumbai in 1974. These were succeeded by zones at Noida, Madras, Cochin, Falta and Visakhapatnam. All these were developed by the Central Government. There are other SEZs built by State government and private developers prior to the SEZ Act of June 2005.

During the period of Jawaharlal Nehru’s Prime Ministry, the foreign partnerships had been promoted in particular sectors and foreign investment was encouraged. The first Export Processing Zone (EPZ) was established in 1965 in Kandla, Gujarat. This was a precursor of the Unique Economic Zone in India. The industrial zone of Santa Cruz in Mumbai was launched in 1973.

After the death of Jawaharlal Nehru, Indira Gandhi became Prime Minister of India in 1966. She also did much for the country’s economic development. The Foreign Investment Board was formed in 1968. In 1973, Foreign Exchange Regulation Act (FERA) was enacted. India established the Santa Cruz Electronics Export Processing Zone (SEEPZ) between 1973-74. It was the first totally free zone dedicated to the electronics industry. The doors were opened of India’s economy during the decade of 1980 by Indira Gandhi and later in 1985 by Rajiv Gandhi. From 1984 to 1989, the policy was to permit the middle class to consume more in order to improve domestic demand. This resulted in increased imports and the growth of foreign direct investment. The government tried to raise the level of exports to balance this phenomenon. In 1984, the totally free Zone policy was a new beginning. In 1991, India’s economy opened to link the Indian market with the world leading to the free

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2 L. Lakshmanan, “Evaluation of SEZs: and some issues. The India experiences” RBI staff studies (2009).
flow of commerce and trade. The multilateral financial institutions like the World Bank and International Monetary Fund, while helping developing countries like India, also insisted on the restructuring of the political and administrative machinery.

Following a change in policy regime in this period and the formation of the World Trade Organization (WTO), India became a founding member and chose a technique of capitalist liberalization. There was the introduction of policies since July 1991 especially in the industrial sector. De-reservation of industries for the public sector was first of the most important actions taken by the government as part of the policy changes in the industrial sector where industries such as defense, nuclear power, coal and lignite, the railroads and the oil reserved in the public sector as well as basic industries like iron and steel, electricity, aviation, shipbuilding and heavy machinery industries such as tele-communications, strong electric cables and instruments plants are now open to private sector participation. In addition, the government-held shares in selected public sectors, such as ONGC etc. are offered for investment funds, financial institutions, the public and workers by means of a policy of disinvestment which resulted in the very first private SEZ that began operations in Surat in 1998. This was under the jurisdiction of Mumbai SEEPZ Development Commissioner, a candidate of the central government. By the beginning of the 21st century, most developing countries in the world have recognized the significance of facilitating international trade to sustain economic growth and increased contribution to GDP of their nation. As part of its continuing commitment to liberalization, the Government of India has also adopted a multi-pronged approach to promote foreign investment in India. The Government of India has gone ahead with the second generation reforms and has made a number of policy changes to achieve this objective, the annual growth rate ranging between 6% and 9%. The Bharatiya Janata Party (BJP) government decided to launch the totally Free Trade Area policy in 2000, changed the name of EPZ as the SEZ.

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5 K. N. Ghorude, India’s SEZs: Role and Critical Success factors (Himalaya Publishing House, Delhi, 2008)
6 K. Rajiv, India’s Export Processing Zones (Oxford University Press, Delhi, 1989)
7 Ibid
8 Ibid
2.1 Historical Context of SEZs Development

The SEZs of the People's Republic of China are SEZs located in mainland China. The government of the People's Republic of China (PRC) gives SEZs special economic policies and flexible governmental measures. This allows SEZs to utilize an economic management system that is especially conducive to doing business that does not exist in the rest of mainland China. Since the late 1970s, and especially since the 3rd Plenary Session of the 11th Communist Party of China (CPC) Central Committee in 1978, the PRC government has decided to reform the national economic setup. The basic state policy has focused on the formulation and implementation of overall reform and opening to the outside world.11

During the 1980s, the PRC passed several stages, ranging from the establishment of SEZs and opening coastal cities and areas, designating open inland and coastal economic and technology development zones in Shenzhen, Zhuhai and Shantou in Guangdong Province and Xiamen in Fujian Province and designating the entire province of Hainan as SEZ.12

In 1984, the PRC further opened 14 coastal cities to overseas investment in Dalian, Qinhuangdao, Tianjin, Yantai, Qingdao, Lianyungang, Nantong, Shanghai, Ningbo, Wenzhou, Fuzhou, Guangzhou, Zhanjiang and Beihai.13 Since 1988, mainland China's opening to the outside world has been extended to its border areas, areas along the Yangtze River and inland areas. At first, the state decided to turn Hainan Island into mainland China's biggest SEZ and to enlarge the other four SEZs.14

In other words, the State Council expanded the open coastal areas, extending into an open coastal belt as the open economic zones of the Yangtze River Delta, Pearl River Delta, Xiamen-Zhengzhou-Quanzhou Triangle in south Fujian, Shandong Peninsula, Liaodong Peninsula (Liaoning Province), Hebei and Guangxi. In June 1990 the PRC government opened the Pudong new area in Shanghai to overseas investment, and

14 Ibid
additional cities along the Yangtze River valley, with Shanghai's Pudong new area as its “dragon head.” Since 1992, the State Council has opened a number of border cities, and in addition, opened all the capital cities of inland provinces and autonomous regions.\textsuperscript{15} In addition, 15 FTZ, 32 state-level economic and technological development zones, and 53 new and high-tech industrial development zones have been established in large and medium-sized cities.\textsuperscript{16} As these open areas adopt different preferential policies, they play the dual roles of windows in developing the foreign-oriented economy, generating foreign exchanges through exporting products and importing advanced technologies and of radiators in accelerating inland economic development.

Primarily geared to exporting processed goods, the 5 SEZs are foreign-oriented well-developed areas which integrate science and industry with trade, and benefit from preferential law and policies and special managerial systems.\textsuperscript{17} In 1999, Shenzhen's new-and high-tech industry became one with best prospects, and the output value of new-and high-tech products reached top level, making up 40.5% of the city's total industrial output value. Since its founding in 1992, the Shanghai Pudong New Zone has made great progress in both absorbing foreign capital and accelerating the economic development of the Yangtze River valley. The state has extended special preferential policies to the Pudong New Zone that is not yet enjoyed by the SEZs.\textsuperscript{18} For instance, in addition to the preferential policies of reducing or eliminating Customs duties and income tax common to the economic and technological development zones, the state also permits the zone to allow foreign business people to open financial institutions and run tertiary industries. In addition, the state has given Shanghai permission to set up a stock exchange, expand its examination and approval authority over investments and allow foreign-funded banks to engage in RMB business. In 1999, the GDP of the Pudong New Zone came to 80 Billion Yuan, and the total industrial output value, 145 Billion Yuan. EPZs are an international


\textsuperscript{16} Ibid


\textsuperscript{18} Ibid
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phenomena influencing increasing share of trade flows and employing a growing number of workers and increase the socio-economic status of the peoples.\textsuperscript{19} From 176 zones across 47 countries in 1986 the number had increased to over 3,000 across 116 countries by 2003.\textsuperscript{20}

India also favours this so in the year 2000, the government replaced the old EPZ regime by a new scheme of SEZ with several lucrative incentives/benefits that were not available in the earlier scheme, and in 2005, it enacted the SEZ Act and SEZs Rules were notified in February 2006. The policy was expected to give a big push to exports, employment and investment in SEZs. The Ministry of Commerce and Industry claims that these zones will attract investment of about Rs 1, 000 billion including FDI of Rs 250 billion and create additional 5, 00,000 direct jobs, by December 2007.\textsuperscript{21} The promotion of SEZ is an attempt to deal with infrastructural deficiencies, procedural complexities, bureaucratic hassles and barriers raised by monetary, trade, fiscal, taxation, tariff and labour policies. These structural bottlenecks affect the investment climate adversely by increasing production and transaction costs. Since country-wide development of infrastructure is expensive and implementation of structural reforms would require time, due to given socio-economic, socio-legal and a socio-political institution, the establishment of SEZs is seen as an important strategic tool for expediting the process of industrialization.\textsuperscript{22}

The zones offer numerous benefits such as:

(i) Tax incentives

(ii) Provision of standard factories/plots at low rents with extended lease period

(iii) Provision of infrastructure and utilities

(iv) Single window clearance

(v) Simplified procedures, and

(vi) Exemptions from various restrictions that characterize the investment climate in the domestic economy


\textsuperscript{21} Ministry of Commerce(2007)

\textsuperscript{22} G. Naresh Reddy, “Special Economic Zones Engines for Growth” the Management Accountant 348-354 (2009).
These benefits definitely help in creating the conducive environment for businesses that potentially attracts local and foreign investment agencies as well individuals. The competitive advantages of zones may also be explained within the framework of the “cluster approach”. The industrial clusters that contains external economies of scale and other advantages, helps the operating firms in reducing costs, developing competitive production systems and attracting investment.

The foundation of the modern jewellery industry in India, for instance, was laid in SEEPZ in Mumbai in 1987-88. It was there that the “wax setting technique” was introduced in jewellery production, which made mass scale production possible. It dramatically transformed the labour-intensive jewellery industry from its cottage industry status into a highly mechanized modern industry. SEZs accounted for over 55% of total Indian jewellery exports in 2002-03. Zones have also been instrumental in creating the base for the growth of the electronics industry through technology transfers, spillovers and demonstration effects. During 2000-02, the share of SEZs in total hardware exports was as much as 26%. The Indian software saga also really began in SEEPZ, Mumbai. The first major breakthrough in India’s software exports came in 1977 when the Tata established a unit in SEEPZ in partnership with Burroughs, an American company, to export software and peripherals. A further breakthrough in the progress of the industry occurred when, in 1985, Citibank established a 100% foreign-owned, export-oriented, offshore software company in SEEPZ. This company drew attention to the possibilities available for offshore software development in India. Soon after, Texas Instruments and Hewlett-Packard established subsidiaries in Bangalore in 1986 and 1989 respectively and the rest is history. The 1991 reforms did not resulted in a sustainable growth in manufacturing as there was a significant slow-down in the second-half of the 1990s. The bureaucratic red-tapeism, administrative procedures, rigid labour laws and poor infrastructure are believed to have affected the India’s SEZs Business Zones Development. The government reverted to EPZs with the expectation that if they could effectively be

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separated from the rest of the economy, then they could provide the engine of growth to propel the manufacturing sector. It was argued that the existing zones could not succeed in attracting investment because of the lack of government commitment to the programme, piecemeal reforms, policy reversals, poor site selection, and failure to provide world class infrastructure, weak incentives and poor regulation of the zones. In a major initiative to boost export-led growth and motivated by the success of Chinese SEZs, the government replaced the EPZ scheme with the SEZs scheme in 2000. The main difference between a SEZ and an EPZ is that the former is an integrated township with fully developed infrastructure whereas an EPZ is just an industrial enclave.26 Under the new scheme, all existing zones were converted into SEZs and three Greenfield SEZs became operational by 2004. However, the impact of SEZs remained far removed from expectations. In order to provide a significant thrust to the policy, the government enacted the SEZ Act 2005. The Act became operative in February 2006 after the SEZs Rules were framed and notified. In addition, state governments also enacted their own SEZ laws, primarily to cover state subjects.

2.2 Meaning and Definition of EPZ and SEZ

An EPZ is an industrial area that constitutes enclaves with regards to customs tariffs and the commercial code in vigor in the host country.27

According to International Labour Organization (1988): The concept of EPZ initially defined as zones where a more favorable fiscal regimes is applied to exporting enterprises, has progressively broadened to designate a range of concessions to the regulatory environment, which are generated to exporting enterprises which may be located anywhere within a country. It is delaminated industrial estate which constitutes a free trade enclave in the customs and trade regime of a country, and where foreign manufacturing firms producing many for export benefits from a certain number of fiscal and financial incentives.28

According to the World Bank (1992): An EPZ is an industrial estate, usually a fenced-area of 10 to 300 hectares that specializes in manufacturing for export. It offers firms conditions and a liberal regulatory environment.

According to Ministry of Commerce and Industry: SEZ is a specifically duty free enclave and shall be deemed to be foreign territory for the purpose of trade operations and duties and tariffs.

In research paper titled, “Origins and Performance of China’s SEZs,” Prof. James Kai-sing Kung says that in China, people's perception is that SEZs are like “rented territory.” To some they are a selling of the nation. And, second, they increase economic crime and augment inequality.

According to Curtis, Hill, Lin, 2006: The SEZs are geographical regions that have economic laws different from a country's typical economic laws. SEZs are used to stimulate private investment and economic development through preferential government policies. The benefits a SEZ offers to companies may include corporate tax reduction or elimination, tariff free trade, or deregulated labour markets.

According to EPZ Authority Ordinance 1980: The “Definitions” section of the SEZ Act mention classifications of zones such as Export Processing Zones, Free Trade Zones, Reconstruction Opportunity Zones, and Regional Development Zones and give them loose definitions. The only classification that has any existing legal framework is the EPZ.

According to SEZs in the Russian Federation, Article 2: Special Economic Zone means a part of the territory of the Russian Federation determined by the Government of the Russian Federation where a special regime for carrying on entrepreneurial business operates. Thus, a SEZ is a geographic region within a nation-state in which a distinct legal framework provides for more liberal economic policies and governance arrangements that prevail in the country at large, the intent being to stimulate investment, trade, and employment. In the Indian context, the new SEZ Policy can be thought of as ushering in a third generation of economic reforms, while the first two phases were dominated, respectively, by efforts to liberalize the macro-policy environment, and by the creation of institutions for regulating a market.

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economy. The phase three has a special emphasis on facilitating a global presence for India’s largest private-sector firms and rapidly enhancing the physical infrastructure within which such firms operate.

2.3 Rationale behind Establishment of SEZs

The main purpose of SEZs in India is to serve the promotion of exports. The Commerce Ministry of India has shown great confidence regarding its growth. The Commerce and Industries Minister, Mr. Kamal Nath claims that exports will ultimately grow by five times, GDP will rise 2%, and will generate around 3 million jobs across India. The government also claims that these SEZs will attract FDI, enable transfer of modern technology and will create incentives for infrastructure. India has also received a good response from these SEZs:

(a) Special tax incentives for foreign investments in the SEZs.
(b) Greater independence on international trade activities.
(c) Economic characteristics are represented as “4 principles”:
   (i) Construction primarily relies on attracting and utilizing foreign capital (ii) Primary economic forms are Sino-foreign joint ventures and partnerships as well as wholly foreign-owned enterprises
   (iii) Products are primarily export-oriented (iv) Economic activities are primarily driven by market forces. SEZs are listed separately in the national planning (including financial planning) and have Province-level authority on economic administration. SEZs local congress and government have legislation authority.

2.4 Tracing the Development of SEZs Worldwide

After the Great Depression at the end of 1920’s and especially in the second half of the 1960’s there was a massive orientation to the foundation of EPZs in the world. Since 1950’s most of the countries in the world have adopted export zones, for example, United State, Puerto Rico and currently coastal China for faster economic

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The concept has evolved and transformed from the original concept of industrial estates. The first example of this is the Shannon EPZ in Ireland set up in 1958. SEEPZ in India and Kaohsiung EPZ in Taiwan both set up in 1960’s. Currently, SEZ models have been implemented in more than 100 countries around the globe. India’s first EPZ was established at Kandla in 1965 and seven other Zones were established in Mumbai, Chennai, Surat, Falta, Kochi, Noida, and Vizag. India’s experience with EPZ was not a huge success.

Table-2.1: EOUs Vs SEZs

<table>
<thead>
<tr>
<th>S.No.</th>
<th>Export Oriented Units (EOUs)</th>
<th>Special Economic Zone (SEZs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>01</td>
<td>Establishment EOU unit can be set up at any place declared as “warehousing station” under Customs Act</td>
<td>SEZs unit has to be located within the specified Zones developed</td>
</tr>
<tr>
<td>02</td>
<td>Minimum investment Minimum investment in plant and machinery and building is Rs 10 Million for EOU. This should be before commencement of commercial production</td>
<td>There is no limit for SEZs</td>
</tr>
<tr>
<td>03</td>
<td>Custom Clearance Fast Track Clearance Scheme for clearances of imported consignments for EOU</td>
<td>In case of SEZs units, customs clearance for export is obtained within the Zone itself</td>
</tr>
<tr>
<td>04</td>
<td>Central sales Tax Central sales Tax paid on purchases is refundable (but not local tax)</td>
<td>In case of SEZs unit, supplier does not have to pay Central sales Tax</td>
</tr>
</tbody>
</table>

Source: Highlights by International Trade Policy Division

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A SEZ is a geographical region that has economic laws that are more liberal than a country's typical socio-legal laws and policy. The category of SEZ covers a broad range of more specific zone types, including FTZ, EPZ, Free Zones (FZ), and Industrial Estates (IE), Free Ports, Urban Enterprise Zones and others. Usually, the goal of a SEZ structure is to increase foreign investment.\textsuperscript{34} One of the earliest and the most famous SEZs were founded by the government of the People's Republic of China under Deng Xiaoping in the early 1980s. The most successful SEZ in China, Shenzhen, has developed from a small village into a city with a population over 10 Million within 20 years.\textsuperscript{35} Following the Chinese examples, SEZs have been established in several countries, including Brazil, India, Iran, Jordan, Kazakhstan, Pakistan, the Philippines, Poland, Russia, and Ukraine. Currently, Puno, Peru has been slated to become a “Zona Economica”. A single SEZ can contain multiple “specific” zones within its boundaries. The two most prominent examples of this layered approach are Subic Bay in the Philippines and the Aqaba SEZ in Jordan.

In a recent comprehensive econometric study on the SEZ policies in China and India, Leong investigates the impact of opening up the Chinese and Indian economy on economic growth in these countries using new panel data sets for both the national economies and the regional economies of China.\textsuperscript{36} The policy change to a more liberalized economy is explicitly identified using instrumental variables. The results provide support that export growth does have a positive and statistically significant effect on economic growth in these countries. In the case of the Chinese regions, the presence of EPZ may exert positive effect on the regional growth rate but the increase in regional growth is even more export in elastic than at the national level. The results dispel the popular view that adopting a policy of more openness in the economy has a dynamic effect on economic growth.\textsuperscript{37} In the two phases of liberalization in both the countries, the second stage is found statistically significant. One possible reason is that the scale of liberalization is greater in the second phase. Additionally, increasing

\textsuperscript{34} K. Rajiv, \textit{Indian Export Processing Zones: An Evaluation} (Oxford University press, New Delhi, 1989).
\textsuperscript{35} A. Kundra, \textit{The Performance of India’s Export Zones : A Comparison with the Chinese Approach} (Sage Publication, New Delhi, 2000).
the number of SEZ has very negligible effect on economic growth.\textsuperscript{38} Taken together, these results suggest that what contributes to greater growth is a greater scale of liberalization, rather than increasing the number of SEZ.

SEZs have been implemented using a variety of institutional structures across the world ranging from fully public (government operator, government developer, government regulator) to fully private (private operator, private developer, public regulator). In many cases, public sector operators and developers act as quasi-government agencies in which they have a pseudo-corporate institutional structure and have budgetary autonomy. SEZs are often developed under a public-private partnership (PPP) arrangement, in which the public sector provides some level of support (provision of off-site infrastructure, equity investment, soft loans, bond issues, etc) to enable a private sector developer to obtain a reasonable rate of return on the Zone.

2.5 Evaluation of SEZs Performance

The Industrial Policy Resolution of 1948 marked the beginning of the development of Indian industrial policy. The resolution not only defined the rough outlines of the policy but also the role of authority of the state in industrial development both as an entrepreneur and as authority. The Industrial Policy Resolution of 1956 gave the public sector a strategic role in the economy.\textsuperscript{39} It categorizes industries that would come under the exclusive jurisdiction of the State or would progressively come under State control and others. India has a planned economy with a focus on state-sponsored industrialization. The argument was that capital is scarce in India, thus it was necessary to regulate the flow of available capital in order to regulate socially desirable channels. This was achieved through a sophisticated system of industrial licensing and monopoly and control over key industries. More than 80% of Indian population still lives in the rural economy.\textsuperscript{40} Agri-centric development model prevailed during the 1950s and the 1960s. Agriculture contributes about a fifth of the total Gross Domestic Product (GDP). It provides the means for a livelihood to about

\textsuperscript{39} Walk the Talk: Interview with Minister of Commerce, \textit{Indian Express}, September 25, 2006.
\textsuperscript{40} J. Bharti, “SEZ land size to decide rehabilitation” \textit{Times of India}. New Delhi: Bennett & Coleman, February 6, 2007.
two thirds of the population of the country. The sector employs 59% of the workforce in Asian countries and is the largest single shareholder of the private sector job. Agriculture accounts for about 10% of total export earnings and provides raw materials to a variety of industries.

During the period of Jawaharlal Nehru, international cooperation was promoted in specific sectors and foreign investment was encouraged. First EPZ was set up in 1965 in Kandla, Gujarat. It was the forerunner of SEZS in India. After the death of Jawaharlal Nehru, Indira Gandhi became the Prime Minister of India in 1966. She also did a lot to the economic development of the country. The Foreign Investment Board was set up in 1968. In 1973, Foreign Exchange Regulation Act (FERA) was adopted. India established the SEEPZ between 1973-74. It was the first EPZ which was dedicated to the electronics industry. The doors of the Indian economy were opened in the 1980s. The government tried to increase the level of exports in order to balance this phenomenon. In 1984, the FZ policy was turned to a new beginning. After a change in policy regime in this period and the formation of the WTO with India to be a founding member, she opted for a deregulated capitalist strategy. It was the introduction of policy since July 1991, especially in industry. India initiated the process of industrial growth in 1948 when it announced its first industrial Policy Resolutions, 1948. With an ISI Policy framework, export promotion has also been a concern of the government that attempts to promote the EPZ as an export platform on the basis of economic incentives, such as the provision of better infrastructure and tax holidays that become a feature of Indian development. The country has had four phases in the evolution of EPZs policy since then.

2.5.1 Initial Phase 1965-1985

India was one of the first in Asia to recognize the effectiveness of EPZ model in promoting export with Asia’s first EPZ set up in Kandla in 1965. It was followed by Santa Cruz EPZ in Mumbai which come into operation in 1973 with different sets of objectives. The Policies were rigid and the package of incentives and facilities were not attractive. Entrepreneurs had to acquire individual clearance from various state government and Central government departments. FDI Policy was also highly restrictive.42

42 Supra note,34
Various committees were appointed by the government of India during this period to review the working of the Zones. These committees pointed out that the growth of EPZs in this phase was hampered by several handicaps including, the absence of a policy and made several concrete recommendations to improve the functioning of these Zones.43

In 1980, the government introduced the EOU. This scheme facilitates the setting up of EOUs beyond the boundaries of EPZs. The responsibility of administrating these units was also entrusted with the zone administration.44

2.5.2 Expansionary Phase 1985-1991

The government of India decided to establish four more zones in 1984. These were at Noida (Uttar Pradesh), Falta (West Bengal), and Chennai (Tamil Nadu). Thereafter, Visakhapatnam EPZ in Andhra Pradesh was established in 1984, though it could not become operational before 1994. All these zones with the exception of Chennai were set up in industrially backward regions.

2.5.3 Consolidating Phase 1991-2000

In 1991, the reformed trade and individual Policy led to liberalization of the Indian economy and various measures were taken by the government for revamping and restructuring EPZs.

The focus had been on delegating powers to zone authorities, providing additional fiscal incentives, simplifying policy provisions and providing greater facilities. The scope and coverage of the EPZ schemes was enlarged in 1992 by permitting the agriculture, horticulture and aqua-culture sector units. In 1994, trading, reengineering and reconditioning units were also permitted to be set up.

2.5.4 Emergence Phase 2000 Onwards

The EXIM Policy (1997-2000) has introduced a new scheme from April 1, 2000 for establishment of SEZs in different part of the country. SEZs are permitted to be set up in the minimum size of not less than 1000 hectares. The number of incentives both

fiscal and non-fiscal has also been extended to the units operating in SEZs. Several measures have been extended to the units operating in SEZs. Several measures have been adopted to improve the quality of governance of zones. These include relaxation in the conditions for approval process and simplifying customs rules.

SEZs Policy is thus the most significant thrust towards ensuring the success of export processing zones. The conversion of EPZ into SEZ started from November 1, 2000; the EPZ at Kandla, Santa Cruz (Mumbai), Cochin, and Surat have been converted into SEZs. In 1998, the first private SEZ began its activities in Surat. This was under the jurisdiction of SEEPZ Commissioner for Development, a candidate from the central government.

**Figure-2.1: SEZS in Different Parts of India**

![Map of SEZs in India](Image)

(Source: Ministry of Commerce and Industry)

From the beginning of the 21st Century, most developing countries in the world realized the importance of facilitating international trade for the sustainable growth of their economy and increased contribution to GDP of the nation. As part of its ongoing efforts to liberalize, the Indian government also has a multi-pronged approach that was adopted to encourage foreign investment in India. The Indian government has
moved in front with second-generation reforms and made several policy changes to achieve that goal. The annual growth rate was between 6% and 9%. The BJP government decided to re-launch the free trade zone policy in 2000. It changed the name of the EPZ to SEZ. The policy is to make SEZ an engine for economic growth through quality of infrastructure with attractive economic package to both the center and the state with the minimum possible regulations.

In 2003, other exiting EPZs namely Noida and Falta began converting into SEZs. In addition, approvals have been given for the setting up of 26 SEZs in various parts of the country in Private/joint sectors. The introduction of the SEZ Policy has marked the period of emergence of EPZ Policy in India. It is expected to go a long way in determining the success of EPZ now called SEZ in India. In 2008 there were 870 units operating as the functional SEZs. The Zones’ concept covers a variety of arrangements. Some of the more common terms applied to these areas are the following:

<table>
<thead>
<tr>
<th>S.No</th>
<th>Name of Zone</th>
<th>Identification</th>
</tr>
</thead>
<tbody>
<tr>
<td>01</td>
<td>Free Trade Zones (FTZs)</td>
<td>These types of the zones are fenced in duty-free areas, offering warehousing, storage and re-export operations</td>
</tr>
<tr>
<td>02</td>
<td>Export Processing Zone (EPZs)</td>
<td>EPZs are industrial estates aimed primarily at foreign market</td>
</tr>
</tbody>
</table>


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<thead>
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<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>03</td>
<td>Hybrid EPZs</td>
<td>They are typically sub-divided into a general zone open to all industries and separate EPZs are resend for export-oriented, EPZ-registered enteritis.</td>
</tr>
<tr>
<td>04</td>
<td>Enterprise Zones</td>
<td>EZs are introduced to revitalize distressed urban or rural areas through the provision of tax incentives and financial grants.</td>
</tr>
<tr>
<td>05</td>
<td>Free Ports</td>
<td>Free Ports encompass much layer area. They accommodate all types of activities, including tourism and retail sales permit on site residence and provide a broader set of incentives and benefits.</td>
</tr>
<tr>
<td>06</td>
<td>Single Factory Zones</td>
<td>These are schemes providing incentives to individual enterprise regardless of location; factories do not have to locate within a designated zone to receive incentives and privileges.</td>
</tr>
<tr>
<td>07</td>
<td>Specialized Zones</td>
<td>Specialized zones include science, technology parks, petrochemical zones, logistics parks, air port based zones and so on.</td>
</tr>
</tbody>
</table>

The word “Special” mainly means flexible laws and policies. The first special zone which bears any resemblance to the present day ones was set up in Spain in 1929 with the intention of increasing exports by value addition to the raw materials available in the country. Deng Xiaoping, the inspiring force behind China’s economic miracle
during the last 30 years, gave a big boost to the concept of SEZs in 1979.\(^{49}\) In opening up its vast domestic market to western capital and technology, he used the SEZs as role models to assess the success of his economic liberalization policies. The Chinese government gives preferential treatment to investors in the SEZs.

### 2.6 Essential Points of SEZs Scheme

A new export promotion scheme of SEZs was introduced with a simple and transparent policy and procedure for promotion of exports with minimum paper work. The most important feature of the Scheme is that the SEZ area is considered essentially as a foreign territory for the purposes of trade operations, duties & tariffs. Therefore, goods supplied to SEZ from the Domestic Tariff Area (DTA) are treated as deemed exports and goods brought from SEZ to DTA are treated as imported goods.\(^{50}\) The SEZ Scheme places full trust on the units and, therefore, import and export operations of the units in the Zone are on the basis of self-certification.

(a) No import license required.

(b) Manufacturing or services allowed.

(c) Inland Revenue is subject to full customs duty and import policy in force.

(d) Full freedom for sub-contracting.

(e) No routine examination by customs authorities of export/import cargo.

The UPA government currently in power conceived SEZ Act 2005, which was adopted in June 2005 and entered into force on February 10, 2006. The law provides for drastic simplification of rules and single window clearance on matters relating to the union and state governments. The state governments have adopted their own laws covering SEZs to state issues.

The law provides for single window clearance mechanism for developers and operators to ensure orderly development of SEZs where the responsibilities are assigned to the Board approval, formed by the Union Government. The Union

\(^{49}\) Goswami (ed). *Competitiveness of Indian Manufacturing: Results from a Firm Level Survey* (World Bank-CII study, 2002).

Government can set up a SEZ on its own or on the basis of proposals from the state government or private clients. At the regional level, the Development Commissioner and his/her office exercise administrative control of SEZ. An approval committee can reject change proposals for the establishment of companies in SEZ. All suits of civil nature and the crime in designated SEZs will be tried and charged by specially designated courts, and parties can appeal to the high Courts against the decisions of the designated courts. The corporate units in SEZ enjoy special privileges and protection afforded by the law. The law provides a special economic package to set up units in SEZ. This package includes the exemption from customs duties, excise duties, central, service tax, central sales tax and securities transaction tax to both the developers and the unit’s set up.

There is a three-tier administrative structure. At the summit, a Board of Approval at the level of the Union government was established for the functioning of SEZ. Next authority created by state governments for the creation and promotion of infrastructure within each state. Finally, it is provided in SEZ mechanism/authority for single window approval.

2.7 Salient Features of India’s EPZs & SEZs: Facilities/ Entitlement

The SEZ Policy aims at creating competitive, convenient and integrated Zones offering World class infrastructure, utilities and services for globally oriented businesses. The SEZ Act envisages key role for the State Governments in Export Promotion and creation of related infrastructure. SEZs are being set up to enable hassle-free manufacturing and trading for export purposes. Sales from DTA to SEZs are being treated as physical export. This entitles domestic suppliers to Drawback/DEPB benefits, CST exemption and Service Tax exemption. There is 100% Income Tax exemption on export profits available to SEZ units for 5 years, 50% for next 5 years and 50% of ploughed back profits for 5 years.

Table-2.3: Prominent Features of the Indian EPZs and SEZs.

<table>
<thead>
<tr>
<th>S.No</th>
<th>EPZs</th>
<th>SEZs</th>
</tr>
</thead>
<tbody>
<tr>
<td>01</td>
<td>Domestic sale up to 50% permissible</td>
<td>All items even those reserved for SSI will be permitted to be manufactured by SEZ units as the entire production is to be exported in normal course</td>
</tr>
<tr>
<td>02</td>
<td>Duty free import/procurement of capital goods, component &amp; consumable</td>
<td>Units to retain and transactions in Dollars through payment by way of salaries and domestic</td>
</tr>
<tr>
<td>03</td>
<td>Facility to retain 70% of earning EEFC account</td>
<td>There will be no restrictions on scrapping. There will be no questions of value addition and valuation etc</td>
</tr>
<tr>
<td>04</td>
<td>Non-fulfillment of condition of approval attract penal action under FTDR Act</td>
<td>No checking of accounts or goods by any other agencies, only domestic sale will subject to central excise duty &amp; sale tax</td>
</tr>
<tr>
<td>05</td>
<td>Ready Infrastructure</td>
<td>All units have to furnish information only through electronic mode so that everything is on record of the total value of imports, inter unit transfer, sales in domestic market</td>
</tr>
</tbody>
</table>

(Source: Current Status of SEZs in India and around, Arunachlam, P. SEZs in India: Principles, problems and prospects; Serial Publications, New Delhi.)
2.8 Visibility and Establishment SEZs

The SEZs are broadly divided on the basis of location, product, size and land area. They are as:

(a) Product: On the basis of products, the following classifications have been done-

   (i) Multi product SEZs occupying minimum 1000 hectares of land may produce garments to automobiles

   (ii) Sector specific SEZs occupying minimum 1000 hectares of land e.g., either to electronics SEZs

   (iii) Gems and Jewellery

   (iv) IT-ITES-BPO

   (v) Bio-Tech-SEZs occupying minimum 100 hectares of land

   (vi) Services and Warehousing SEZs

(b) Multi-Products SEZs: SEZ for multi-product means a SEZ where units may be set up for manufacture of two or more goods in a sector or goods falling in two or more sectors or for trading and warehousing or rendering of two or more services in a sector or rendering services falling in two or more sectors.

(c) SEZs for Specific Sector: It means a SEZ exclusively for one or more products in a sector or one or more services in a sector.

(d) On the basis of areas, we classify the SEZs into two:

   (1) Processing area: Processing area is that area where SRZ units can be located for manufacturing of goods or rendering of services,

   (2) Non-processing area: The non processing area is that area which is intended to provide support facilities to the SEZs processing area activities.
2.9 Kinds & Operation SEZs on the Basis of Activity

We can classify SEZs on the basis of activity into two categories:

(a) Manufacturing: Apparel, Garment and leather, Automobile and Auto components, Engineering-light, heavy and application. Pharmaceuticals, Food Processing, Telecom Equipment, Computer hardware and Microelectronics, Consumer Electronics and Appliances, Gems and Jewellery and Diamonds.

(b) Service: It enables Services, Biotechnology, Health Care, Financial services, Knowledge services, Entertainment, Leisure and recreation, Sports and related activities, Organized retail Business services both convention and exhibitions, Warehousing and Trade related Services.

The policy provides for setting up of SEZs in the public, private, joint sector or by State Governments. It was also envisaged that some of the existing EPZs would be converted into SEZs. Accordingly, the Government has converted EPZs located at Kandla, Baroda, Ahmadabad and Surat (Gujarat), Cochin (Kerala) Santa Cruz (Mumbai-Maharashtra), Falta (West Bengal), Greater Noida (Uttar Pradesh), Ilandaikulam, Madurai (Tamil Nadu), Nanguneri and Tirunelveli (Tamil Nadu), Nagpur (Maharashtra), Pithampur (Madhya Pradesh). In India, SEZs are divided into three categories, multi-product SEZs, industry-specific SEZs, free trade and commodity housing zone (FTWZ). The first category refers to SEZ units out to the manufacture/provision of services of two or more goods in a sector or good/services that may be established in two or more sectors. For multi-product SEZ Service, a contiguous area of 100 hectares or more is required.

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54 Section 3 of SEZ Act, read as: (1) A Special Economic Zone may be established under this Act, either jointly or severally by the Central Government, State Government, or any person for manufacture of goods or rendering services or for both or as a Free Trade and Warehousing Zone. (2) Any person, who intends to set up a Special Economic Zone, may, after identifying the area, make a proposal to the State Government concerned for the purpose of setting up the Special Economic Zone. Provided that where such a proposal has been received directly from a person under sub-section, the Board may grant approval and after receipt of such approval, the person concerned shall obtain the concurrence of the State Government within the period, as may be prescribed.

The second category is defined as a zone meant exclusively for one or more products/services. The minimum space required is 100 Hectares of contiguous and undeveloped land. Within sector specific SEZs, bio-technology, gems and jewelry, non conventional energy, electronics, hardware and software, including SEZ-IT can be put in space on 50 acres of Assam, Meghalaya, Nagaland and Arunachal Pradesh, Uttaranchal, with a minimum relaxed, Sikkim, Jammu and Kashmir (J & K), Goa and Union Territories. FTWZ is the third category; the minimum area requirement is 40 acres of land contiguous and free. Built up area should not be less than 10 hectares.

2.10 Socio-Legal Issues of SEZ in India

The socio-legal issues such as displacement, compensation, rehabilitation and residential real estate development and land speculation has been the threat of feasible relocation of units from other parts of the status of SEZs consequent loss of income reported. The farmers are protesting against the forced acquisition of their land. The development of SEZs would lead to job losses for farmers whose land will be acquired and really little job creation for the use of high technology or high network have individuals and the total generated and can be negative. The delivery of thousands of acres of inexpensive land to developers in the business and the relaxation of the laws of the land, including those relating to the welfare of workers in business, environmental protection, taxation, etc, will automatically promote industrialization and solve the country’s persistent unemployment difficulty overnight. Farmers and peasants in various states such as Uttar Pradesh, Uttarakhand, West Bengal, Orissa, and Punjab opposed to the acquisition of land and use of water for the SEZ is a major growing difficulty across the country. Mundra Zone, it expects to get at least 6 Million liters per day by the Sardar Sarovar project, as promised by Gujarat Water Infrastructure Ltd. The other main problem is the increase in various parts of the country; labour laws applicable to the rest of the country have relaxed SEZs. Existing laws are well intentioned and promote the welfare of workers. Relaxing laws only for zones shows the government’s lack of conviction in his own commitment to social justice.

59 According to official site of the Mudra SEZ, www.mundasez.com
Figure-2.2: SEZ’s Hybrid Industrialization

SEZ: A Hybrid Industry

As depicted in the chart above, SEZ is a hybrid industry which incorporates of three industries,

(a) Infrastructure (Complex Projects, Long gestation Period, Capital Intensive & Huge Sunk Costs)

(b) Real estate (High returns, geographical idiosyncrancies & Lack Liquidity)

(c) Services (Intangibility, Inseparability & Heterogeneity)

Many confusions and controversies are attributable to ignorance about its true nature

2.10.1 Land Acquisition and Rehabilitation

Land is the largest primary source of livelihood in an agrarian society. Land acquisition becomes the most obvious case of forcible transfer of resources from ordinary people to private corporations, destroying livelihoods, and displacing
people.\textsuperscript{60} In this process, invariably the gainers are the corporations and losers are the ordinary people connected to land in many ways, the peasants and tenants, agricultural workers and artisans, tribal’s and fishermen. The SEZ became the most grotesque reminder of this pro-corporate, anti-people bias built in this model of industrialization. Only rising popular resistance could force the government to moderate its stand, but the difference between acquiring SEZ land, and land for mining or industrialization is very little insofar as the destruction of social auditing, people’s livelihoods and displacement are concerned.

**Figure-2.3: SEZ’s Impact on Society**

![Diagram showing impact of SEZ on society](image)

The figure shows the five different types of impact of SEZ’s emergence on the society.

**Women and Working Hours**

Health problems of women are also related to working in one position continuously like bending, crouching, sitting or standing for several hours every day, over a period of time. These postures result in backaches, injury of the spinal cord, aches and pains in joints and shoulders.

\textsuperscript{60} B. Pranab, “Political Economy of Land Grab” *Economic & Political Weekly* (42)14 (2007).
Employment

There is very low level of awareness among women workers and unions about occupational health hazards at work. Very few workers saw any links between the nature of their work, posture at work and ailments they experience.

SEZ Act, 2005

The Section 3 of the SEZ Act stipulates identification of the area for setting up SEZs, keeping the issue of modalities for acquisition of land as well as rehabilitation and compensation package for land losers which in its nature, is totally open. Rules are also silent about such a vital social aspect involving thousands of possible land losers as well as agricultural workers.

Section 5(1) (a) of the Act says that notification of any SEZ shall be guided by the generation of additional economic activity and creation of employment opportunities. The same cannot be achieved if there is a serious social unrest, likely to erupt without specific guidelines on land compensation and rehabilitation package. Therefore, in order to avoid social unrest, there must be specific provisions in the Rules with regards to (a) Modalities of acquisition of the land (b) Grant of compensation and rehabilitation package for the land losers and agricultural workers.

The Indian Urban Land (Ceiling and Regulation) Act, 1976 was already repealed in 1999, releasing huge chunks of land into the market. Total amount of land expected to be acquired for SEZs across India would be 150,000 hectares. This land is predominantly agricultural and typically multi-cropped. This conversion would lead

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61 Section 3 of SEZs Act, read as: (1) A Special Economic Zone may be established under this Act, either jointly or severally by the Central Government, State Government, or any person for manufacture of goods or rendering services or for both or as a Free Trade and Warehousing Zone. (2) Any person, who intends to set up a Special Economic Zone, may, after identifying the area, make a proposal to the State Government concerned for the purpose of setting up the Special Economic Zone..., provided that where such a proposal has been received directly from a person under sub-section, the Board may grant approval and after receipt of such approval, the person concerned shall obtain the concurrence of the State Government within the period, as may be prescribed.

62 Section 3 of SEZs Act, read as: (1) The Central Government, while notifying any area as a Special Economic Zone or an additional area to be included in the Special Economic Zone and discharging its functions under this Act, shall be guided by the following, namely: (a) generation of additional economic activity (b) promotion of exports of goods and services; (c) promotion of investment from domestic and foreign sources; (d) creation of employment opportunities; (e) development of infrastructure facilities; (f) maintenance of sovereignty and integrity of India, the security of the State and friendly relations with foreign States.
to a loss of 1 million tons of food grains produced, thereby threatening the food security of the entire country. The SEZ Act states that as much as 75% of the area under a SEZ can be used for non-industrial purposes. This option will give rise to real estate business in SEZ which, by no means, would strengthen the local economy. On the contrary, this is likely to introduce scopes for a large scale real estate speculation. The land acquisition processes for SEZ, thus, have been causing widespread discontent among the farmers and common people in the state.

The foremost goal of any country is development. Development is development of people their increased living standards and improved quality of life. Industry provides goods, services and material comforts to increase living standards. Social values such as human dignity, self-reliance and gainful employment for every person set the quality of life. Such development can only come by generating, mobilizing and optimally utilizing natural and human resources.

The SEZ Act lays down that it is to be set up on a minimum 1,000 hectares of land. Traditionally these lands would have been under multiple uses. They could be agro-biodiversity farmlands, mangrove belts, wetland and even forest patches. Each of these has a critical ecological role in maintaining healthy environment besides being having an inherent link with people’s livelihoods. Thus, when these lands metamorphose in to SEZs, the ecological functions and human survival are bound to be adversely affected. The Supreme Court has elaborated on the right to adequate housing, shelter and livelihood as part of the all-encompassing Right to Life under Article 21 in the landmark case of Olga Tellis v. Bombay Municipal Corporation. Local people are resisting projects in other parts of country like West Bengal and Maharashtra on the grounds of the loss of productive lands in hinterland and costal area and on ecological degradation. Not only this much, but there are also some other

66 AIR, 1985
vital issues that needs to be mentioned the least which clearly goes against the rapid growing favors to the SEZ movement. These are as follows:

(a) Revenue loss
(b) Large-scale land acquisition by the developers which lead to displacement of farmers with meager compensation
(c) Acquisition of prime agricultural land having serious implications for food security
(d) Misuse of land by the developers for real estate purpose, and
(e) Uneven and aggravated growth creating regional inequalities.

The large scale acquisitions of land entailed by SEZ development have had serious consequences on the livelihoods and food security of weaker and vulnerable section in India. SEZs, due to their high demand for land, have emerged as the single largest threat to the livelihoods of peasant’s and violation of human rights in the nation.67 It is unfair and unjust that the SEZ promoters are required to be given more than 1,000 hectares of land. This is an outright violation of laws & constitution of the country. It violates a number of Land Reform Acts and the Parliament of India’s Decisions and Supreme Court Judgments confirming the Acts.68 Since environmental public hearing may not be mandatory for these projects and single window clearance procedure would be applicable to industries under SEZ, the affected people have no voice or opinion about the land acquisition processes and the projects. In other words, the eminent domain and public purpose clauses in the land acquisition will not be invoked to facilitate land acquisition by the state from rural populations for industrial development in SEZs.69

2.10.2 Loss of Land & Displacement

Displacement has been invariably without rehabilitation. The land acquisition Act, 1894, a law made during the British rule, is still being used in a shameless manner for acquiring not only properties, but also the livelihood of peoples in exchange for meager amount of cash. (Acres for heartache) Medha Patkar

In some SEZ, state governments are joint venture partners. In the case of some special incentives by means of concessional electricity and water tariffs have been offered. In M.G. Badappanavar v. state of Karnataka the court held that basic concept equality “equality is a basic feature of the constitution of India or any treatment of equal unequally or unequals as equals will be violation of the basic structure of India.

The SEZ Act, which violates the letter and spirit of the Constitution of India, it violates the fundamental rights of citizens guaranteed in Part three of the Constitution. Relaxation / inapplicability of the labour laws of numerous (which includes law disputes, Contract Labour (Regulation And Abolition) Act, 1970, Factories Act, 1948, Minimum Wage Act, 1948, Law on Trade Unions Act, 1926), environment (protection) Act, 1986 is not applicable to SEZ not required environmental clearance. Violate Panchayati Raj Act, 1996 for local self-government, in violation of laws granting rights and control to Adivasi communities over their lands, violating a lot of international human rights conventions. In summary, the special economic zones and other emerging development issues can be seen in broad and theoretical foundations of neoliberalism. As India is considered the policy implications emerging from SEZ could cause growing socio-political crisis, because society is much a lot more complex than assumed and that will lead to an organized or unorganized resistance and can even cause anti-neo liberal political forces. Thus, in order to steer clear of polarization of society, civil society should participate to build consensus on development problems.

71 AIR 2001 SC 260
Table 2.4: Land Required for the Zone in India

<table>
<thead>
<tr>
<th></th>
<th>Land Required for the Zone in India</th>
</tr>
</thead>
<tbody>
<tr>
<td>01</td>
<td>SEZ for multi product</td>
</tr>
<tr>
<td>02</td>
<td>SEZ for Services</td>
</tr>
<tr>
<td>03</td>
<td>Free Trade and Wearhousing</td>
</tr>
<tr>
<td>04</td>
<td>Biotechnology, Jewellery etc</td>
</tr>
<tr>
<td>05</td>
<td>SEZ for Electronics</td>
</tr>
</tbody>
</table>

In this context, a cursory look at the literature explaining factors shaping the export performance of a country brings out various demand and supply side factors. Until recently the policy focus in India was on the demand side while neglecting the supply side like, well-maintained institutional set-up, infrastructural facilities, macroeconomic environment, incentives, attitude toward foreign investment and issues related to labour market.\(^\text{72}\) Further, at the firm level, factors like size of the firm, location, availability of raw materials, technology and ownership pattern influence the phenomena.

SEZ Act, 2005 which was partially notified on February 10, 2006, is a self-contained legislation encompassing the framework of SEZs.\(^\text{73}\) Post notification of the Act a host of legislations and underlying rules and regulations have ceased to govern the SEZs and units therein, namely:

(a) Foreign Trade Policy 2004-09 notified under Foreign Trade (Development & Regulation) Act, 1992;
(b) Chapter XA of the Customs Act, 1962; and
(c) SEZ Rules and Regulations notified under Chapter XA of the Customs Act, 1962.

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The Act also makes modifications in a number of other legislations including Income-tax Act, 1961, Insurance Act, 1938, banking regulation Act, 1949, Indian Stamp Act, 1899.

2.10.3 Environmental Degradation

Right to Life includes Right to live in a pollution free environment. However the SEZ units are exempted from environmental impact analysis under the provision of the environment (protection) Act 1986. Further, the development commissioner will be empowered to issue consent and no objection letters in consultation with the officers of the state pollution control board. The units, which are classified as non-polluting industries, do not require a consent letter. In *MC Mehta v. Kamal Nath* court held that causing disturbance to ecological balance which would be hazardous to life. The development commissioner can give clearance without consulting the pollution control board. The units are permitted to submit a compliance report for maintaining prescribed pollution standards. Although the development commissioner has powers for a random check, the units within the SEZ are free to follow their own methods to maintain environmental standards.

There is a general consensus that Environmental laws should be complied with in SEZs like in the rest of the country. However, there is a concern about the time taken in granting various approvals. It needs to be mentioned that in the zones of Dubai, China and Panama, are Coastal Zones, and all approvals are accorded by the authority located in the Zone. State Government resolves that:

(a) The State Government would notify a list of non-polluting industries where no pollution clearance would be required in SEZ and NOC for such units, irrespective of their size, be given being an officer of PCB posted in the Zone.

(b) State Government will consider having a green-belt around each SEZ in order to avoid unplanned development.

(c) In the overall area proposed for any zone there may be small patches of forest land. It may not be possible to exclude the same from the layout. However, State Government shall provide land in lieu of it but cost of afforestation on it shall be borne by SEZ developer.

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74 Subash Kumar v. State of Bihar AIR 1991 SC 420
75 AIR 200 SC 1997
(d) Success of SEZ depends upon the effective single window mechanism. While there is no intention to relax application of environmental laws to SEZ, the essence is issuance of approval in a time bound manner in the zone itself. It is, therefore, proposed that, a Committee shall be constituted in each SEZ under the concerned DC which would consist of officers of Ministry of Environment & Forest, Government of India, State Pollution Control Board and experts on the subject and it should be empowered to accord all clearances which are required from the State Governments relating to development of SEZ or setting up of the units in SEZ. Convention on Biodiversity gives provisions for sustainable use of the resources that “development must be in harmony with nature”. Thus the “Right to development must be fulfilled so as to equitably meet the development and environment needs of present and future generations”, thereby maintaining its potential to meet the need and aspirations of present and future generations.

The SEZ Act 2005 does not require Environmental Impact Assessment as part of the application for new units. This is because SEZs are only permitted to contain “nonpolluting” industries and facilities. The companies do not require any public hearing where affected communities can interact with the companies and share their concern. Enormous power has been given to DCs for granting environmental clearance for SEZs. They are able to bypass the State Pollution Control Boards as they work directly under the government control. There is no space for filing any petition if the people are affected. Moreover, the state governments have also created complementary conditions for SEZs in coastal Zones by developing new Coastal

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76 Preamble of Rio declaration ; also see People United for better living in Calcutta v. State of W.B. AIR 1993 Cal 215.(There shall have to be both development and proper environment and as such , a balance has to be found out and administrative actions ought to proceed in accordance with therewith and not d’hors the same)
77 Principle 3 of Rio declaration
79 FIAS, “SEZs: Performance, Lessons Learned, and Implications for Zone Development” (World Bank, Washington, DC, 2008).
Regulation Zone Act. One particular area of concern in relation to SEZs is the extra water demands that will and are being placed on already strained and contested water resources. To mention two examples, on the POSCO SEZ in Odisha, the water requirement is 286 Million litres per day. This will be procured from Jobra barrage on Mahanadi River in Cuttack district and ultimately from the upstream Hirakud dam. There is already agitation against reservation of water from Hirakud dam for industrial use. Another case is that of Mangalore SEZ in Karnataka. In a letter addressed to the Prime Minister of India, Dr. Manmohan Singh in June 2006, the convener of the SEZs Impact Assessment Committee, an affiliate of the NGO Forum of Mangalore, it quoted the Mangalore SEZ Limited as having estimated the water need at 136 Million litres of water a day. This is despite the fact that Mangalore city is facing water crisis even without the SEZ. Therefore, SEZs do not only take scarce fertile farmland out of production, but may also take scarce water resources away from the competing utility.

2.10.4 Use of Water

The use of water for SEZ is one of the main problems rising from different parts of the country. According to official website of the Ministry of Commerce, SEZ is expected to get at least 6 Million liters of water per day from the Sardar Sarovar project. Increase of labour laws for the rest of the country have been relaxed for the SEZs. The existing laws are well intentioned and they promote workers’ welfare. Relaxing such laws only for SEZs, the government showed a lack of conviction in its own commitment in bringing and maintaining the social justice.

2.10.5 Posing Threats to Water & Air Security

The SEZ, which is posing big threat to the farming class, is an anti-people and anti-environment scheme. This is also a threat to the water security for the areas where SEZs are proposed and would certainly have an impact on the national agricultural sector where the conversion of land to SEZ would mean destruction of groundwater recharge systems. Industrial production and natural resource use and conversion often

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results in the creation of large amounts of water-borne pollutants. Moreover, in India, right to extract groundwater continues to be connected with the ownership of land. Hence SEZs, even in relatively small area, may suck huge quantity of water, drying up the wells and other water bodies of the surrounding area. Simultaneously, they will discharge their bi-products and wastes that will pollute the same water bodies in turn. Thus it will create a two-fold crisis in the area leading to conflicts between the zones and the local residents. The impact of all these could be quite serious in many areas.

**Figure-2.4 & 2.5: Waste Discharge by Zone & Polluted Water Collected by Local People**

(Figure 2.5: Pollution of water by SEZs and collecting the polluted water by the local people for domestic purpose)

Apart from the water pollution, SEZs are also the sources of pollution in the form of gas and particulate matters emissions that affects air quality causing serious damage to human health as well as the local biodiversity. Toxic air pollutants are associated with cancer, cardiovascular, respiratory and neurological diseases. Carbon monoxide when inhaled, affects bloodstream, reduces the availability of oxygen and can be extremely harmful to public health at large.

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82 Supra note, 51.
An emission of nitrogen-dioxide from transportation sources reduces the proper functioning of lungs, affects the respiratory immune defense system and increases the risk of respiratory problems. The physical and chemical properties of particulates are associated with health risks such as respiratory problems, skin irritations, eyes inflammations, blood clotting and various types of allergies.

2.10.6 Toxic Pollutants

Toxic pollutants released from industry including heavy metals, cyanides and pesticides and can be emitted into air, water or in solid wastes. Little is known about the qualities or precise resources of chemical and toxic residuals, since almost no government or industries do any sampling of toxic pollutants in the local region.

2.10.7 Effluents of Factory

The claim about industrial prosperity from setting up of SEZs to offset such problems remains unsatisfactory. As of the fiscal year 2004-05, share of SEZs in exports was a mere 5%, and they accounted for only 1% of factory sector employment in the same year. Moreover, the sectoral break-up of SEZs approvals shows that the largest number of approvals, nearly 61% has been in the IT sector. The manufacturing sector accounts for only one-third of total approvals. Industries in general consume 37% of the world’s energy and emit 50% of world’s CO2, 90% of world’s SO2 and almost all of its toxic chemicals are harmful to the human health and environment.

86 ibid
87 ibid
2.10.8 Dangerous Waste

Inorganic acids and acid mixtures account for the main portion of dangerous waste. This waste is exclusively generated by laboratory operations. As it is generated in the course of improving the industries products and chemical process, it has an impact on consumption and optimization of the systems operated at the customer’s locations, air and forests, and degradation of basic natural resources at whole.88

Figure-2.7: Effect of Pollution on Human Body

Table-2.5: Industrial Impact on the Society

<table>
<thead>
<tr>
<th>Industrial Impact</th>
<th>Societal Change (Gender, Livelihood, Poverty)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Food and Agriculture</strong></td>
<td></td>
</tr>
<tr>
<td>Less yield from crops - Reduced</td>
<td>Less milk/nutrition for children</td>
</tr>
<tr>
<td>calories intake for women</td>
<td>Higher food insecurity for women</td>
</tr>
<tr>
<td>Increased food prices</td>
<td></td>
</tr>
<tr>
<td><strong>Water</strong></td>
<td></td>
</tr>
<tr>
<td>Reduction in water availability</td>
<td>Impacts on mother and child nutrition</td>
</tr>
<tr>
<td>More dependence on unsafe water</td>
<td></td>
</tr>
<tr>
<td><strong>Health</strong></td>
<td></td>
</tr>
<tr>
<td>Water borne diseases - Increase</td>
<td>Infant mortality</td>
</tr>
<tr>
<td>of diseases like dengue, vulnerable, Malaria, etc</td>
<td></td>
</tr>
<tr>
<td>Respiratory diseases due to</td>
<td></td>
</tr>
<tr>
<td>Indoor-disease sensitivity</td>
<td></td>
</tr>
<tr>
<td>Air pollution and other emissions</td>
<td></td>
</tr>
</tbody>
</table>

(Source- P. Arunachalam, *Special Economic Zone in India Principles, Problems and Prospects* (Serials publications, New Delhi, 2008)

2.11 Constitution and SEZ

The Constitution of India guarantees Fundamental Rights to every citizen including the right to live and as the Supreme Court has pointed out the right to livelihood is inherent in the right to life. The ultimate aim of social security is to ensure that every one has the means of livelihood. In the light of the Act of 2005, the establishment of SEZs clearly violates the letter and spirit of the Indian Constitution. It violates the fundamental rights of citizens as guaranteed by the Part 3 of the Constitution. Realizing this fact, the Act was subjected to amendments in the State Assemblies of Uttar Pradesh and Haryana with the approval of the President of India. Later on, the Act got incorporated into the Ninth Schedule of the Constitution. It may be argued that by being incorporated into the Ninth Schedule, this law is exempted from judicial
review. However, if an amendment to the Act reverses the original objectives and violates the rights of the intended beneficiaries, this may breach the Ninth Schedule and require the approval of the national Parliament. This is a question that is remained unresolved till date. Relaxation / inapplicability of many labour laws (including Contract Labour Act,1970; Factories Act,1947; Minimum Wages Act,1948; Trade Union Act,1926; Environment (Protection) Act,1986 are not applicable to SEZs). It also does not need environmental clearance. The Act, in furtherance, seems to violate the Panchayati Raj Act, 1996 meant for the local self-government, violating laws on granting and monitoring, affecting the vulnerable community of indigenous people or the Adivasis to the level of threat to their existence and violating many international conventions on human rights. Even though India pursued restrictive import substation Policies, the government announced in Lok Sabha in April 1960 to establish the first FTZ at Kandla in Gujarat. The zone became operational in the year 1966-67. India thus acquired the distinction of establishing the first FTZ in Asia and second amongst the developing countries next to Puerto Rico where EPZ was established in 1962. A decade later, the second zone was set up at Bombay and four more EPZ in 1980’s at Calcutta, Noida, Cochin and Madras followed by yet another at Visakhapatnam. The EPZs in India were developed, owned and managed by central government. The zone units were permitted to Processing or manufacturing with the Project specific value addition for strict compliance. In the absence of a conducive macro-economic Policy frame work, inadequate infrastructure and the lack of promotional strategy, the performance was not significant in terms of contribution to export foreign exchange earnings, FDI and GDP. The prevailing scenario was appropriately described as if the EPZs are grafted in isolation on an inward looking economy, their performance will not be optional as is borne out by the India experience.

89 A. Nishant, Special Economic Zone Act 2005 as Unconstitutional (New Law College Bharati Vidyapeeth University pune, 2010).
Now, India has embarked up on an ambitious plan to emulate the Chinese model of SEZs to boost exports, attract FDIs and thereby accelerating the economic progress. The new EXIM effective from April, 2000 was introduced for setting up of SEZs in the country with a view to provide an internationally competitive and hassle free environment for exports. The units in SEZs were allowed to manufacture, trading, re-conditioning and service activities. The SEZ Act aims at providing competitive fiscal package both at Central and State level with minimum regulatory regime and quality infrastructure with a stable long term policy to promote investment in these areas. Existing incentives and facilities like exemption from customs and excise duty for development of SEZ and setting up its Units, Income tax, Sale tax and Service tax exemption were also incorporated in the SEZs legislation. Under the new SEZs legislation, i.e. the SEZ Act 2005, SEZs would be treated as deemed foreign territory for trade operations, duties tariff, and supplies from domestic industries would be treated as exports. Goods and services going into the SEZ area from DTA shall be treated as imports and goods coming from the SEZ area into DTA shall be treated as if these are being imported.

2.12 SEZs and Socio-Economic Experiment

The initial development of the SEZs is reflected by Asia’s first EPZ set up in Kandla in 1965. Seven or more EPZs were set up thereafter. The SEZ Policy provides for setting up of SEZ in public, private, joint sector or by Govt. There is also provision in this policy that EPZ would be converted into SEZ. One of the main problems with SEZ is locating land for SEZ. Many state governments are in the process of establishing SEZ. The environmental degradation and regional disparities and displacement, or that the compensation price of land, rehabilitation, residential

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93 Ibid.
94 SEZ Rule47 read as: Sales in Domestic Tariff Area.- (1) A Unit may sell goods and services including rejects or wastes or scraps or remnants or broken diamonds or byproducts arising during the manufacturing process or in connection therewith, in the Domestic Tariff Area on payment of Customs duties under section 30, subject to the following conditions, namely.- (a) Domestic Tariff Area sale under sub-rule (1), of goods manufactured by a Unit shall be on submission of import licence, as applicable to the import of similar goods into India, under the provisions of the Foreign Trade Policy: Provided that goods imported or procured from the Domestic Tariff Area and sold as such without being subjected to any manufacturing process shall be subject to the provisions of the Foreign Trade Policy as applicable to import of similar goods into India.
95 S.Dharminder, "Impact of SEZs on the Agriculture Sector" Mainstream (40)7 (2009).
96 "SEZs developers to be responsible for rehabilitation" Times of India, 22nd March 2007b.
property development and land speculation, threats have been flagged by possible relocation of units from other parts of the country and the resulting loss of revenue.

The farmers are protesting against the forced acquisition of their lands. The development of SEZs may destroy the employment of farmers whose land will be acquired and will create very little employment for high-tech or highly skilled and net employment to be good, produced a negative result.\(^\text{97}\) Handing over thousands of hectares of land cheaply to promoters of the industry and the relaxation of the laws of the country, including those relating to the welfare of industrial workers, the protection of the environment, taxes, etc would automatically promote industrialization and would solve the nagging unemployment problem of the country overnight.\(^\text{98}\)

The highest level of opposition in West Bengal was observed when land was purchased by the state government for the Tata group at Singur and Salim Group of Indonesia in Nandigram. Thus, land constitutes a key source of identity belonging to socio-economic bonding. It represents a social and productive asset as well as a source of security, and shapes prospects of substantive citizenship in much of rural India.

**Table-2.6: Employment, Investment and Exports in Four Important SEZs**

<table>
<thead>
<tr>
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<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Kandla SEZs</td>
<td>14310</td>
<td>74.55</td>
<td>227.74</td>
<td>1101.18</td>
<td>1482.66</td>
</tr>
<tr>
<td>2</td>
<td>Noida SEZs</td>
<td>23682</td>
<td>78.07</td>
<td>434.33</td>
<td>560.70</td>
<td>6893</td>
</tr>
<tr>
<td>3</td>
<td>Cochin</td>
<td>7147</td>
<td>98.36</td>
<td>393</td>
<td>696</td>
<td>1037.52</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>45139</td>
<td>250.98</td>
<td>1600.74</td>
<td>2357.88</td>
<td>10413.18</td>
</tr>
</tbody>
</table>


Chapter-II: Special Economic Zone (SEZ) in Historical and Present Scenario

Figure- 2.8: Employment in Indian SEZSs

(Source: Government of Commerce and Industry)

Table-2.7: Number of SEZs Approved by Government Till January, 2010

<table>
<thead>
<tr>
<th>Functioning SEZs (including former EPZs)</th>
<th>105</th>
</tr>
</thead>
<tbody>
<tr>
<td>Notified SEZs</td>
<td>348</td>
</tr>
<tr>
<td>SEZs with Formal Approval</td>
<td>573</td>
</tr>
<tr>
<td>SEZs with In-Principle Approval</td>
<td>147</td>
</tr>
</tbody>
</table>

*Source: Ministry of Commerce and Industry, January 2010*
The proponent of SEZ feels that many of the above apprehensions, however, could be addressed through appropriate policies and safeguards. However on the ground reality, the implementation of the SEZ scheme has been adopted in a ruthless manner for acquiring land.\(^9\) The biggest bone of contention in the SEZ skeleton is the building of SEZ units on prime agricultural land and the displacement and inadequate compensation provided to farmers,\(^10\) and other deprivation suffered by them and other rural workers.\(^10\)


2.13 SEZs Issues and Challenges

SEZs have emerged as one of the most relevant debates in the recent times with the socio-legal dimensions. Since Indian model of SEZ is quite different as compared to the rest of the world in terms of engagement and participation of private capital on such a big scale although in the world, the most of successful SEZs are established and run by government capital and state investment in infrastructure.\(^{102}\) The main issues and challenges relating to SEZ law in India are that it does not emphasize on the size of the SEZs.\(^{103}\) Most important and common issues related to the SEZ are relating to the environmental, land acquisition, economic, political and socio-legal issues. These problematic issues are pertinent to the entire nation in general and to the states of Uttar Pradesh, Uttarakhand, Haryana and Punjab in particular. The Indian model of SEZ envisages more on the role of private sector in the development of such Zones, in which the risk of financing, marketing and promotion has been vested with the private sector. But the international experience reveals that there is limited or no experience of private sector in this regard, especially in marketing of such projects.\(^{104}\)

It therefore makes us to think as to what extent the private developers will be in a position to market such projects. The setting up of SEZs requires huge amount of land, for example, Reliance SEZ’s size is 14,000 hectares. Now the question is from where will this land come from? In fact maximum portion of it will be from the cultivable land. Therefore, providing of land for the development of SEZs will take away the large part of cultivable land. The SEZ Act states that units not fulfilling the required criteria as specified in the letter of approval may be required to exit. The future of fixed assets created by the unit in such a situation is undefined. This is likely to discourage the establishment of capital-intensive operations within the SEZ.\(^{105}\)


The Industry and Commerce Ministry has rightfully taken credit for the creation of the SEZ Act of 2005 but the policy lacks transparency and seems ad-hoc in implementation. The ostensible goal of the SEZ Policy is to generate additional economic activity, development of infrastructure facilities, generate employment, promote investment from domestic and foreign sources, and facilitate easier exports of goods and services. So far, it has approved 237 SEZs out of which, 51 have commenced their operations. The industry ministry has showcased Nokia’s SEZs in Tamil Nadu, Apache (Adidas Group) in Andhra Pradesh, Flextronics in Tamil Nadu, Quart City in Chandigarh and Motorola and Foxcon in Tamil Nadu. Thousands of people were employed and hundreds of millions of rupees were invested. While SEZs are imperative in scaling the standard level of economy, the Indian form has not been well throughout where there is an arbitrary allotment of land for industrial purposes. Thus fertile farm land has been siphoned for industrial activity while the government continues to anguish for the loss of agricultural productivity. Moreover, the compensation handed out to farmers affected by this policy has been paltry and well below the market value. Even so, payments are delayed and political middlemen and corrupt bureaucrats get a cut of such payments.106

The government claims that the SEZs scheme is a tremendous success among investors, both in India and abroad. This should not really be surprising as industry does like tax cuts and exclusivity. The point is whether the industry loves this concept or not but that the nation has a comprehensive policy on SEZ, an optimal use of land and resources, and loopholes benefiting a few have been plugged. A. Lehman study of Hongkong said that some of the SEZs projects approved by the government are in multi-story buildings and benefits accrued from such schemes borne out political expediency and obvious nepotism hurt the nation financially than providing benefits. This is the reason for the spat between the industry and finance ministry over the SEZ Policy.

The finance ministry contends that the SEZs policy must be exclusive and have tangible benefits and not one that encourages claims of benefits. After a public political showdown between the two ministers, it looks like they have achieved an

understanding not to touch prime agricultural land and that there would be adequate compensation paid to farmers. The question is how the government defines prime agricultural land in a nation where agricultural activities are not taxed and there are no clear records of the agricultural activity. Additionally, how would the government value land when most financial transactions in real estate are in cash and below the radar with official records showing only the white portion of the sale amount? This problem is more acute in rural or semi-urban agricultural land than in urban lands that have some notional value attached to a location. This is a classic example where the lack of transparency in policy formulation can wreck even a great economic building concept. It builds fear in the minds of farmers and raises suspicion. Recently, a band of farmers chased away a group of surveyors from Karnataka Industrial Areas Development Board (KIADB) and the police was called to stop them from surveying their land situated near the new Bangalore airport. Their fear is that a KIADB acquisition notice will stop them from selling their land and equivalent compensation from the government will be less than a 10th of what they may get in the open market. Thus, while exports have fared well, the industry ministry has to revamp its SEZs policy to create a level of transparency and openness in identifying land that could be commandeered for this purpose. At the same time, the government has to ensure that only large-scale operations are allowed in SEZs and potentially away from the cities in dry-lands so that rural areas may benefit from the industrial investment.

The structure of SEZ Policy has been set up to succor to the large sized industries. The structure in no way will assist the small and medium scale industries, which has substantial chak in the development of industrial sector of India. SEZ Policy reveals that up to 75% of the portion of any SEZs can be provided to the residence, schools, banks, hospitals and green belts. These tenants of SEZ Policy show fostering real estate promotion rather than export promotion measures.

2.14 SEZs and Regional Disparities

In India, SEZs were initially located in comparatively well-off states with better infrastructure. Andhra Pradesh, Maharashtra, Tamil Nadu and Gujarat all wealthy states have managed to receive the majority of SEZs. In 106 out of 200 formally approved SEZs, 6 were located in these states. This concentration of SEZs in richer pocket intensifies income gaps and disparities between states in India. Thus, the country’s experience clearly indicates that SEZs intensifies an uneven economic growth within a country and the state has very little power in controlling these investments. Also the state efforts to redirect investments in backward regions have remained largely unsuccessful.

2.14.1 Economic Issues

The incentive structure of SEZ Policy attracts real estate players in the business of setting up and running SEZs due to earmark of non-processing area to 35% of the total area. The presence of large scale incentives and subsidy for doing exports from SEZs may induce other players to relocate their operations from non-SEZs to SEZs. The Ministry of Finance estimated that revenue loss arising from existing units is in the range of 7000 Billion. Incentive being provided by GOI to developers and unit holders do not match with the provision of WTO and comes under direct subsidy from state to firms and thus it is not compatible to the WTO standard.

2.14.2 Social Issues

Industrialization requires land acquisition in different parts of the country by converting agricultural land into industrial plot especially multi-crops land and thus creating a stir among the peasants. It deprives the farmers of their basic and traditional source of income which leads to social discontent and brings about lots of socio-legal problems. Rush of setting up SEZs in different parts of the country seems to be disincentive to peasants for agriculture which is already losing sheen.

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110 http://www.tandfonline.com/doi/abs/10.1080/10641734.2007.10505207#.Ug4Nh9JHJZ8
112 The Economic Times, 28 March (2007)
113 IDFC,2001
2.14.3 Legal Issues

The absence of democratic process in large zones will even deny Gram Panchayat elections and will form private monopolies responsible for providing wide range of service like water, power, sanitation etc. These services will not fall under any regulator of either sector or tariff type and provides enormous powers to private monopolies. The reaction of private administration will lead to stray sovereignties as per SEZ Act and it, thus, clearly violates the spirit of the Constitution of India as well as the functioning of the Panchayati Raj Act, 1996. There is no clearly defined exit route of the Units operating inside SEZs and pose uncertainty of fixed asset. Thus, less capital intensive industry is coming to set up shops in SEZs rather than high capital intensive industry. State SEZs policy does not talk about decentralization of authorities to DC of SEZs which leads to administrative complexity and act as hindrance to the success of SEZs.

While talking on the formulation of policies for the SEZ framework from the state end, a glance of the international experience is imperative. As has been discussed earlier in detail about China being the forerunner and America being the exponent in SEZ, the Courts and the legal set up in both these countries gives a lot much idea about the role of legal and administrative bodies from the grass-root level to the state at high. The experience of precedent is yet another avenue to be dealt with, especially if these two countries viz. China and USA are seen upon. China did not regard as relevant or persuasive the American precedent established by *Kelo v. City of New London*,114 (condemnation of private properties for a commercial developer in order to revitalize an ailing economy held to serve “public use” within context of the Takings Clause of the Fifth Amendment to the United States Constitution). The substantive and procedural “due process” that ensures fairness of compensation, and the democratically elected decision-making body to which a court could defer its decision on how much the public interest is actually served by a project, are lacking in China. Therefore, the logic underlying *Kelo*, even if accepted in an American setting, cannot be meaningfully applied to the Chinese context.

114 545 U.S. 469 (2005)
2.15 Challenges for SEZs

There are numerous challenges such as socio-legal impacts of SEZs in the society, some of which are as follows:

(a) Issue of availability of land for SEZs and difficulties involved in procuring/acquiring land.
(b) Issue of maintaining attractiveness of the SEZs scheme fiscal regime.
(c) Issues related to effectiveness of the Single Window Mechanism and coordination departments at the Central and State Government level.
(d) The issue of a large number of States not having SEZs Policy/Act to enable provision of the benefits envisaged under the SEZ Act and Rules.
(e) Issue of constraints leading to slow pace of development of infrastructure within the SEZs and their operationalization, as also inadequacies in the timely and adequate provision of external support infrastructure related to connectivity, provision of public utility services etc.
(f) Increasing unattractiveness of the SEZs incentive package vis-à-vis DTA units receiving benefits under schemes such as Focus Product Scheme, Focus Market Scheme, etc., which are unavailable to SEZs units.

2.16 Categories and SEZs Requirements

There are three types of SEZs:

(a) Multi-product SEZs to have an area of 1000 hectares or more.
(b) Services-sector SEZs to have an area of 100 hectares or more.
(c) To support sectors where India has a competitive advantage, such as gems and jewellery, information technology, bio-technology, Sector-specific SEZs. These sectors can be set up over an area of 10 hectares or more.

2.17 Resolving Problems of Infrastructure

The goal of SEZs is usually an increase in FDI in the country. There is a clear understanding that a well-implemented and designed SEZs can bring about many desired benefits for a host-country that increases the opportunities of employment, FDI attraction, general economic growth, foreign exchange earnings, international exposure, and the transfer of new technologies and skills. Hence, many developing
countries are also endorsing the concept of SEZs with the expectation that they will provide the engines of growth for their economies to achieve industrialization. But for this to be successful, their governments must enact legislation and create a focused administrative infrastructure. To the governments, the SEZs, in turn, offers highly attractive incentives and create zones of industrial development in the best possible locations.

One of the earliest and the most famous SEZ were founded by the government of the People's Republic of China under Deng Xiaoping in the early 1980s. In the face of fierce regional competition, South Korea is also showing strong economic performance and can boast a highly skilled labour force. It has started working strategically towards attracting investment, including the establishment of its first SEZs. The Incheon SEZ is all set to transform the country into a regional hub from which the foreign companies can expand their activities into the other parts of Asia.

The Zones includes a technology complex to house research centers and venture start-ups alongside the Korean Institute of Technology. These projects, which have high-level political backing, are supported by a package of generous financial incentives. Other incentives include simplified administrative procedures, heavily subsidized land leases on government owned land, tax breaks and linguistic support. Situated directly between Japan and China, South Korea is at the centre of a vast Asian market that targets for a total population of two Billion, including 500 Million in the Association of Southeast Asian Nations (ASEAN) countries, with which, along with China and Japan, Korea enjoys a special commitment to the economic cooperation.

The North-east Asia alone accounts for about 24% of the world’s population and 19% of global production among which, the Korean peninsula is an important land piece due to its geographical advantage and so the South Korea has claims in leading the industrial development process in the region.

South Korea's gateway strategy is designed to leverage its geographic and geo-cultural advantages while offering a new, friendly business face to potential investors.

in the form of SEZs in the southern part of the peninsula. Foreigners, foreign companies, and international economic organizations can be involved in free corporate activities in these economic zones offering a range of special advantages, including tax, labour, regulatory and other incentives.\footnote{Sang. H. Jang, “Land Reform and Capitalist Development in Korea” Paper presented at the spring conference of the Institute for Social Sciences, Gyeongsang National University, Jinju, Korea, May (2005).}

South Korea is a more economical, or to say a cheaper location than Japan and more straightforward from a regulatory point of view than China, that opened its markets decades ago.\footnote{A.G. Schweinberger, “Foreign Capital Flows, Tariffs and Welfare: a Global Analysis,” \textit{Canadian Journal of Economics} 2 (2001).} Generally, it is argued that the SEZs concept is attractive because it is much easier to resolve the problems of infrastructure and governance on a limited geographical area than it is to resolve them countrywide. Such economic zones cannot be insulated from the broader institutional and economic context of the country and be treated as an economy within the economy. Zones are a part of the economy and require overall improvement in the investment climate to ensure success in the long run. They should not, therefore, be viewed as an alternative to the overall development model. This is perhaps the reason why SEZs failed to fulfill the role of engines of industrialization in most countries on a sustainable basis.

\section*{2.18 SEZ as Generators of Economic Development}

A SEZ is a trade capacity development tool, with the goal to promote rapid economic growth by using tax and business incentives to attract foreign investment and technology.\footnote{Federation of Indian Chambers of Commerce & Industry (KPMG) ‘Driving Growth through SEZs’, \textit{International Convention on SEZs} (2002). http://www.google.co.in/search?output=search &scrlnt=psy=KPMG+%E2%80%98Driving+Growth+through+SEZs%E2%80%99+2C+International+Convention+on+SEZs%282002%29.&btnK=120 J.H. Dunning, ‘\textit{Multinational Enterprises and the Global Economy}’, Addison-Wesley, Great Britain (1992).} Today, there are approximately 3,000 SEZs operating in 120 countries, which account for over US$ 600 Billion in exports and about 50 Million jobs.\footnote{J.H. Dunning, “\textit{Multinational Enterprises and the Global Economy}”, Addison-Wesley, Great Britain (1992).} By offering privileged terms, SEZs attract investment and foreign exchange, spur employment and boost the development of improved technologies and infrastructure. There are 13 functional SEZs and about 61 SEZs which have been approved and are under the process of establishment in India. Most developing countries in the world have recognized the importance of facilitating international trade for the sustained
growth of the economy and increased contribution to the GDP of the nation. As part of its continuing commitment to liberalization, the Government of India has also, since the last decade, adopted a multi-pronged approach to promote foreign investment in India. The Government of India has pushed ahead with second-generation reforms and has made several policy changes to achieve this objective. The SEZs policy was first introduced in India in April 2000, as a part of the EXIM policy. Considering the need to enhance foreign investment and promote exports from the country and realizing the need of different levels of fields for industrial players to be made available to the domestic enterprises and manufacturers so to made them globally competitive, the Government of India in April 2000 announced the introduction of SEZs policy in the country that deems the SEZs to be foreign territory for the purposes of trade operations, duties and tariffs. To provide an internationally competitive and hassle free environment for exports, units were allowed be set up in SEZs for manufacturing of goods and rendering of services. All the import/export operations of the SEZs units are on self-certification basis. The units in the Zone are required to be a net foreign exchange earner but they would not be subjected to any pre-determined value addition or minimum export performance requirements. Sales in the DTA by SEZs units are subject to payment of full Custom Duty and as per import policy in force. Further Offshore banking units are being allowed to be set up in the SEZs.121

According to the Economic Survey, 2010–11, out of the total employment of 6,44,073 persons in SEZs, an incremental employment of 5,09,369 persons was generated after February 2006 when the SEZ Act came into force. The survey further states that

(i) At least double this number obtains indirect employment outside the SEZs as a result of the operations of SEZs units, and

(ii) This is in addition to the employment created by the developer for infrastructure activities. However, the employment generated by SEZs is not uniform across sectors and regions. Besides, the jobs so created by SEZs may have come at the expense of jobs in the agricultural sector.

The Government has converted EPZs of Kandla and Surat, Cochin, Santa Cruz, Falta, Madras, Visakhapatnam and Noida into SEZs. To provide a stable economic environment for the promotion of Export-Import of goods in a quick, efficient and hassle-free manner, the Government of India enacted the SEZ Act and the new law is aimed at encouraging PPP to develop world-class infrastructure and attract private investment for economic growth.  

The Ministry of Commerce and Industry lays down the regulations that govern the setting up and administering of the SEZs. The Central Government is involved in notifying SEZs and in overseeing their functioning, while the State Governments play a significant lead role in the development of SEZs in their respective States by stipulating the conditions to be adhered to by a SEZ and granting the necessary approvals. The SEZs Rules provide the simplification of procedures for development, operation, and maintenance of the SEZs and for setting up and conducting business in SEZs. This includes simplified compliance procedures, setting up a unit in SEZs and clearance on matters relating to Central as well as State Governments, no requirement for providing bank guarantees, contract manufacturing for foreign principals with option to obtain subcontracting permission at the initial approval stage and Import-Export of all items through personal baggage. With a view to augment infrastructure facilities for export production, it has been decided to permit the setting up of SEZs in the public, private, joint sector or by the State Governments. The minimum size of the SEZs shall not be less than 1000 hectares. Minimum area requirement shall, however, not be applicable to product specific and port/airport based SEZs. This measure is expected to promote self-contained areas supported by world-class infrastructure oriented towards export production. Any private/public/joint sector or State Government or its agencies can set up SEZs.

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122 Palit. Amitendu, Special Economic Zone in India Myths and Realities (Publisher, Anthem Press, 2012).


125 Ibid
Chapter-II: Special Economic Zone (SEZ) in Historical and Present Scenario

**Table-2.8: China and India’s Position**

<table>
<thead>
<tr>
<th></th>
<th>China</th>
<th>India</th>
</tr>
</thead>
<tbody>
<tr>
<td>When started</td>
<td>1980</td>
<td>Mostly after 1991</td>
</tr>
<tr>
<td>Democratic decision-making</td>
<td>Lot of discussion and debate preceded setting up of SEZs</td>
<td>Very little public discussion. Parliament passed law without debate</td>
</tr>
<tr>
<td>Size</td>
<td>Very large (Shenzhen: 32,700 hectares)</td>
<td>Small; the GoI first capped the size at 5000 hectares in April 2007 (after Nandigram). Recently there has been talk of relaxing this once again, after the new R&amp;R policy has been drafted</td>
</tr>
<tr>
<td>Ownership</td>
<td>State</td>
<td>Private corporations</td>
</tr>
<tr>
<td>On what kind of land</td>
<td>Mostly coastal wasteland</td>
<td>Mostly fertile cultivated land</td>
</tr>
<tr>
<td>Exports</td>
<td>Very good (Shenzhen: net exports 2006: $35 billion)</td>
<td>Poor so far (In 1998, a waiver of $1.67 Billion on customs duties was given to earn $1.04 Billion in foreign exchange). Exports have doubled during last year from Rs 34,000 Crore in 2005-06 to Rs 67,000 Crore in 2006-07</td>
</tr>
<tr>
<td>Employment</td>
<td>Several million low-paid jobs</td>
<td>Very limited so far: less than 200,000 jobs created.</td>
</tr>
<tr>
<td>Tax revenue collections</td>
<td>Only selective tax incentives provided</td>
<td>Across-the-board tax holiday given to companies</td>
</tr>
<tr>
<td>-------------------------</td>
<td>---------------------------------------</td>
<td>-----------------------------------------------</td>
</tr>
<tr>
<td>Overall economic success</td>
<td>Only Shenzhen has been a notable success, though at very high social and environmental cost</td>
<td>Only modest success in Export Processing Zones (EPZs) and too early to tell for the new zones</td>
</tr>
<tr>
<td>Overall economic success</td>
<td>Only Shenzhen has been a notable success, though at very high social and environmental cost</td>
<td>Only modest success in Export Processing Zones (EPZs) and too early to tell for the new zones</td>
</tr>
<tr>
<td>Ease of land acquisition</td>
<td>Land battles continue in some areas</td>
<td>Bloody, bitter resistance</td>
</tr>
</tbody>
</table>

Source: SEZs in India, Dept. of Commerce, Ministry of Commerce & Industry, Govt. of India.

### 2.19 Delegation of Powers for SEZ Administration

Effective zone administration is another area of lasting competitive differentiation. For this mechanism to work it is necessary for the government to delegate the powers under various central and state government functions at the zone level so that it becomes an autonomous administrative unit for all commercial activities. Various Government functions such as customs, excise, environment, labour, town & country planning, local body powers and approvals & clearances for setting up units have to be effectively delegated at the zone level and vested with the zone administrative body. SEZ is governed by a three tier administrative set up:

(a) The Board of Approval is the apex body in the Department

(b) The Unit Approval Committee (UAC) at the Zonal level dealing with approval of units in the SEZs and other related issues, and each Zone is headed by a DC, who also heads the Unit Approval Committee.
Figure-2.10: Level of Administrative Setup in SEZ

Board of Approval is the apex body in the Department
Unit Approval Committee at the Zonal level dealing with approval of units in the SEZs and other related issues
Each Zone is headed by a Development Commissioner, who also heads the Unit Approval Committee

Essential steps for the proposal of SEZ in any area or in another words division of power

2.19.1 Approval Mechanism of SEZs and Benefits to Developers

Any proposal for setting up of SEZs in the Private/Joint/State Sector is routed through the concerned State government who in turn forwards the same to the Department of Commerce with its recommendations for consideration of the Board of Approval. On the other hand, any proposals for setting up of units in the SEZs are approved at the Zonal level by the Approval Committee consisting of DC, Customs Authorities and representatives of State Government.

Figure-2.11: Position of the Development Commissioner in SEZs dealing

Board of Approval is the apex body in the Department
Unit Approval Committee at the Zonal level dealing with approval of units in the SEZs and other related issues
Each Zone is headed by a Development Commissioner, who also heads the Unit Approval Committee

Approval given for setting up new SEZs in Private/Joint/State Sector have so far been given for setting up of 117 new SEZs (including 3 Free Trade Warehousing Zones)
spread over 15 States and 2 Union Territories in the Private/Joint Sector or by the State Governments and its agencies. Of the 117 SEZs approved for establishment, 7 SEZs have already become operational, 6 SEZs are now getting ready for operation and the other are at various stages of implementation.

2.19.2 Benefits To SEZs Developers

There are various enactments under which SEZs units are provided with some benefits as well as incentives for the purpose of attracting large amount of investments, promoting exports and generating employments. Some selective benefits of these are mentioned below:

(a) 100% of the profits of developer arising from the business of developing SEZs, notified after April 1, 2005 under the SEZ Act, shall be deducted from taxable income. This deduction can be claimed at the option of the assessee for any 10 consecutive years out of 15 years, beginning from the year in which the SEZs have been notified by the Central Government. If a developer who sets up a SEZ after April 1, 2005, transfers the operation and maintenance of the SEZs to another developer, the transferee is entitled to the above deduction of profit for the remaining period.

(b) With regard to a developer who is entitled to claim an exemption under Section 80-IA of the ITA, the developer can claim an exemption for the remained unexpired exemption period under Section 80-IA, and thereafter it can claim the 10 years tax exemption available to such developer under Section 80-IAB.

(c) The developers of SEZs are not required to pay Minimum Alternate Tax.

(d) No dividend distribution tax shall be paid by a developer engaged in developing, operating and maintaining a SEZ.

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127 Ibid.
2.19.3 Benefits To SEZs Units

The first schedule of the SEZ Act exhibits various fiscal benefits to be given to SEZs units under certain terms and conditions. The Section 7 of the Act lays down the following:

(a) 100% exemption of profits and gains from business for the first 5 years.
(b) 50% exemption on profits and gains from business for the next 5 years.
(c) 50% exemption to the extent that such amount is re-invested in the SEZs Special Reserve Account. If the SEZs Unit has already availed the benefits for 10 years under Section 10A of the IT Act 1961, the above exemptions shall not be available then. Further, when a FTZ or an EPZ is converted into SEZs, the Units, which have already availed of the 10-year tax exemption in an FTZ or EPZ, cannot avail of the Section 10AA exemptions.
(d) Losses falling under the heads “Profits and Gains from Business or Profession” and “Income from Capital Gains” can be carried forward/set off as long as such loss is related to the business of the SEZs Unit (i) Machinery/plant was purchased for the business of the industrial undertaking in the SEZs, (ii) Building or land was acquired or building was constructed in the SEZs, (iii) The original asset was shifted and the establishment was transferred to the SEZs, and (iv) The assesses incurred such other expenses as are notified by the Central Government.
(e) Interest income received by a non-resident or a person who is not ordinarily resident in India, on a deposit made in an OBU situated in SEZs, shall be exempted from the total income.
(f) No tax deduction shall be made by the OBU from interest paid on deposits made on or after April 1, 2005 by a non-resident or a person not ordinarily resident in India; or on borrowings on or after April 1, 2005 from a non-resident or a person not ordinarily resident in India.
(g) The gross total income of an assessee having an OBU or an assessee being a Unit of an IFSC shall be deductible to the extent of 100% for 5 consecutive years from the year of grant of permission under the Banking Regulation Act/SEBI/other relevant law and 50% for the next 5 years. It further defines the exempted “income,” where (i) Income from an OBU in an SEZs, (ii) Income from business

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128 Supra note, 11
129 Supra note, 120
referred to in the Banking Regulation Act 1949, or any other Unit which
develops, and operates, or develops, operates and maintains a SEZ, (iii) Income
from an approved unit of an IFSC.

(h) Exemption from Securities Transaction Tax available to taxable securities
transaction entered into by a non-resident through the IFSC.

2.19.4 Other Benefits

(a) Exemption from Customs Duty- SEZ Units may import to procure from the
domestic sources fully duty free and all their requirements of capital goods, raw
materials, consumable spares, packing materials, office equipment etc. for
implementation of their projects in the SEZs shall be without requiring any
license or specific approval,

(b) Goods imported/procured locally which are duty-free could or should be utilized
within the approval period of 5 years.

(c) Domestic sales by SEZs Units shall be exempted from Special Additional Duty.

(d) Domestic sale of finished products and by-products is permitted on payment of
applicable Customs duty.

(e) Domestic sale of rejected, waste and scrap is permitted on payment of applicable
customs duty on the transaction value.

(f) Exemption from applicable excise duty on goods brought in from the DTA to
SEZs.

2.20 Foreign Direct Investment (FDI)

(a) 100% FDI under the automatic route is allowed in the manufacturing sector in
SEZ Units, except for arms and ammunition, explosives, atomic substances,
narcotics and hazardous chemicals, distillation and brewing of alcoholic drinks
and cigarettes, cigars and manufactured tobacco substitutes.

(b) Exemption from the applicability of the stringent law popularly known as the
Press Note 2 of 2005 that prescribes certain conditions which a foreign investor
proposing to make foreign direct investment in real estate sector in India has to
satisfy.
(c) Setting up OBUs has been allowed in SEZs. External Commercial Borrowings by SEZ Units up to US$ 500 Million a year is allowed without any maturity restrictions.

(d) Freedom to bring in export proceeds without any time limit.

(e) Flexibility to keep 100% of export proceeds in an EEFC account and freedom to make overseas investments with it.

(f) SEZs units allowed to “write-off” unrealized export bills.

2.21 Conclusion

Since India and China are experiencing socio-economic boom and the whole world is waiting in anticipation for them to emerge as super powers, a comparison between these two countries is inevitable. The Chinese SEZ model is different from India. A SEZ in China is not a small affair. There, entire cities are part of these zones, which is why there are only four SEZs. Apart from these, there are enterprise zones at a subsidiary level, whereas in India, numerous SEZs are mushrooming at a fast pace with yet several of them being pending in the government departments.

The failure of EPZ policies in some countries has been attributed to the lack of a comprehensive package of world-class infrastructure, quality governance, good location and attractive physical incentives. India was the first in Asia to set up an EPZ and has keenly pursued the policy of establishing EPZ/SEZ to further its economic policy objectives. The present study shows that the policy has yielded only modest results in terms of exports, employment and investments. The socio-economic costs of human displacement and the socio-legal costs of land acquisition have been observed to far outweigh the benefits that have accrued from the policy. Indeed, an expert group report released by planning commission appears to question the benefits of SEZs.

Land acquisition for SEZ has given rise to widespread protest in various parts of the nation. Large tracts of land are being acquired across the country for this purpose.

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131 Development Challenges in Extremist Affected Areas, Available online at http://planningcommission.nic.in
Already, many questions have been raised on two counts. One is the loss of revenue in the form of taxes and the other is the effect on agricultural production.

In addition, the SEZ Policy may have contributed to aggravating regional imbalances in the country. Considering the significant land displacement issues, there is need for the government to fine-tune the SEZs policy to facilitate the development of large employment generating SEZs and also to address the issues of regional disparities that are highly visible in the current development pattern of Indian SEZs. The SEZs story cannot be grasped in the fullness of its implications unless and until it is placed in the wider context of policies for rapid urbanization and up-gradation of Indian cities. More than half of the SEZs approved so far are in the IT/ITES (IT enabled services) sector. The jobs that will be generated will be for trained computer professionals and not for people who have recently been farmers and agricultural labourers.