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India's SEZ Policy - A Retrospective Analysis

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INDIA'S SEZ POLICY – A RETROSPECTIVE ANALYSIS

Malini L Tantri*

Abstract

This paper provides a critical review of India's SEZ policy over the last five decades (1960 to 2010). The analysis reveals that some of the major factors that contribute to the poor performance of EPZs were the loopholes in the policy structure of the country of the pre-reform period. Specifically, the supply side factors were not strongly developed to meet the standards of the growing international market. At the outset, the imitation of the Chinese model of trade policy in the country appears to be an improvement compared to conventional EPZs. Thereby, it fulfills the promise of promoting qualitative transformation of EPZs. Despite the numerous advantages in its favour, the SEZ policy in India needs a pragmatic re-visit. The most important argument in its favour stems from the various flaws in the policy formulation and execution, which is in conflict with other development objectives of the economy and calls for policy revision.

Introduction

Special Economic Zones (SEZs), in the present context, are described as engines of growth of the Indian economy. SEZs have been the prime subject of discussions ever since it received statutory approval in 2005. The argument in favour of SEZs is guided by the their capacity to create spillover effects on the domestic economy specifically by creating employment opportunities, attracting FDI, promoting a strong industrial base (Aggarwal 2005 and 2006), improving the social and physical infrastructure of the region (Shah, 2009), and as economic units enabling the economy to reach higher levels of production through optimum utilisation of resources and reduction of inefficiency (Tantri, 2011b). The issue of revisiting the SEZ policy gains further importance considering the argument of Menon and Mitra (2009, p-30) that "there is, anyhow, no immediate alternative to SEZs for India". If this argument holds any ground, then it is necessary to revisit the SEZs in the country from a historical perspective rather than assume that it will bring overall development of the country[i]. However, it is worth noting that SEZs have a long history in the origin and evolution of Export Processing Zones (EPZs) – SEZs are the metamorphosis of EPZs that have existed in the Indian economy since the 1960s. However, there is a very little in the literature that provides a historical understanding of this evolution and the metamorphosis. We can probably speculate that such metamorphosis from EPZs to SEZs could be due to the following: One, there might have been flaws in the idea behind promotion of EPZs and subsequently in articulating the EPZs policy; Two, there might have been failure in the execution of the EPZ policy. These two possible reasons are worth investigating. Further, how far the current SEZ policy meets the expectation of policy makers in these two criterions is worth exploring. With this background, this paper attempts a historical survey of the EPZ/SEZ policy followed in India in the last five decades (1960 to 2010). It will focus especially on the possible reasons that led to the realization on the part of policy makers and the government at large that the existing EPZs require a radical overhauling in terms

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of their objectives and the means with which to achieve them. This, in turn, led to the transformation of EPZs into SEZs. With this background in this paper we investigate how so far transformation from EPZs to SEZs is effective at the construction and implementation levels? What are the problems and prospects of the current SEZ policy? Further, some of the issues relating to current Indian SEZ policy discussed in this paper are presented through a comparative analysis of the Chinese SEZs experience. The exercise is based on an analysis of the various laws, policy documents, trade reports, government ordinances, regulations and literature on this issue. The rest of the paper is planned as follows. The next section outlines the evolution of the SEZ policy in India in the last five decades. The third section critically evaluates the major loopholes in the current SEZ policy. The last section summerises the paper and offers a few policy guidelines.

The Evolution of SEZ Policy in India

There is a close association between the approach followed to define the economic priorities of the country and the policy evolved to shape the EPZs/SEZs structure. In this paper, the evolution of the SEZ policy in India is explained in two phases, stretching over a period of almost five decades. The guidelines of the first phase emerged while framing the EPZs regime from the 1960s to 2000[ii]. This could be regarded as the pre-SEZs regime because the earlier EPZs metamorphosised into SEZs. The SEZs policy provided by the Ministry of Commerce, Government of India, in the current context, specifically 2000 onwards, could be regarded as the second phase. The rest of the SEZ policy analysis is structured as follows.

i. First Phase - Expansion of EPZs Structure in India[iii]
    1. First Sub Phase of EPZs Expansion (1960s to 1990)
    2. Second Sub Phase of EPZs Expansion (1990s to 2000)
ii. Second Phase - Emergence of SEZs Regime in India (2000 onwards)

First Phase - Expansion of the EPZs Structure in India

First Sub Period of EPZs Expansion (1960-1990)

Soon after independence, the economy opted for an inward looking attitude that was reflected in the industrial as well as the trade policy. The reason for such a development strategy was largely influenced by the colonial experience in India (Goldar, 2002) and the pessimism that prevailed all over the world at that time regarding the possible role of trade in the process of economic development. However, in the 1960s a few changes were noticed in the industrial and trade policies across the world. Developing countries, specifically, favoured export promotion measures. This also had an influence on the Indian economy. Consequently, for the first time in independent India, the Mudaliar Committee (1964) was appointed to review the national trade policy. Based on its recommendations and considering the needs of the time a few export promotion measures were introduced on an experimental basis. One such policy measure led to the evolution of the EPZs era through the setting country's first FTZ at Kandla (1965). The exercise to introduce the same, however, was first initiated in the late 1950s to promote the Kandla Port as a substitute to the Karachi port, which India lost to Pakistan at the time of partition[iv] (IIFT, 1990). As a part of this strategy, the townships of Adipur and Gandhidham were developed to

rehabilitate the refugee population from Sind. Initially, the Kandla FTZ was assigned multiple objectives: (a) developing Kandla port as a substitute to Karachi port (b) promoting 100 per cent export-oriented industries and (c) promoting industrial development in the region (IIFT, 1990). Thus, trade promotion was not the sole purpose behind promotion of FTZ at Kandla. Nevertheless, the creation of the first FTZ at Kandla gave India the distinction of being one of the pioneers to experiment with FTZs/EPZs in the Asian continent. Location wise, Kandla was placed in one of the backward regions of Gujarat at that time and a number of fiscal and non-fiscal incentives were offered to attract investors (Table 1). Availability of industrial units, assurance of continuous supply of electricity and water at very reasonable prices[v] and assurance to undertake all infrastructure requirements were some of the important facilities offered.

Table 1: Incentives Offered Initially (in 1960s) to KFTZ

Sl. No.	Incentives
1	Exemption from Central excise duty on finished products or on a few raw materials as specified
2	Exemption from import duties on goods for the purpose of export
3	No need to obtain licence as all imports for the zone purpose was listed under Open General Licence (OGL)
4	No excise duties on raw materials imported from the DTA
5	Facilities to access finance at concessional rates from Gujarat State Financial Corporation
6	Exemption from municipal tax
7	Exemption from octroi tax
8	Release of cement, steel, telephone and telegraph facilities on priority basis
9	20 per cent profit exempted from income tax for a period of 10 years
10	Reimbursement of Central sales tax

Source: IIFT (1990)

Within a decade, policy makers decided to set up similar zones in other parts of the country and a more prudent approach was followed. Accordingly, a study team constituted by the Trade Development Authority (TDA) in co-operation with the Department of Electronics visited several EPZs abroad and analysed the export prospects and feasibility of promoting similar zones in India. Consequently, the Government of India established the Santacruz EPZ (SEEPZ/SSEZ) in 1972, and it became operational in 1973-74 (GoI, 1979). Initially it was promoted as a single sector zone, with emphasis on electronic industries. However, in 1986, gems and jewelery were added to the Santacruz EPZ considering the growing international markets for them.

Table 2: Incentives Offered Initially (in 1970s) to SEPZ

Sl. No.	Incentives
1	Import of capital goods, raw materials, components, tooling etc under OGL
2	Duty free import of capital goods and equipments
3	Exemption from customs and countervailing duties on all raw material, components, tooling etc.
4	Exemption from Central Excise duties on products manufactured in the zone
5	Capital goods, raw materials, components etc., supplied to the zone from the domestic tariff area were treated as exports and eligible for all concessions as applicable to exports from the country
6	A single point clearance of application for industrial licensing capital goods imports, MRTP, FERA etc., by a specifically constituted SEEPZ Board

Source: GoI, 1979

It should be noted that, if we stick to nomenclature, Santacruz was the first EPZ of the country, and Kandla was the first and only FTZ in the country. Other than nomenclature, the major differences between the two lie in the history and prime objectives of their promotion. As stated above, the initial idea of creating a FTZ came soon after independence to make the Kandla Port a substitute for the Karachi port, the Santacruz EPZ, on the other hand, was proposed by the TDA for the promotion of the electronic industry after taking consideration the growing international demand for electronic goods and services. A deeper insight into the objectives behind the promotion of the Kandla and Santacruz zones reveals the divergent opinions of the decision makers with regard to role and responsibilities to be assigned to these zones. Perhaps, among others this could be considered as a factor responsible for the poor performance of EPZs. Later this was emphasised by the Tandon Committee (1980) as well. This was obviously in conflict with kind of policy initiatives needed to promote these two different types of zones.

Until the mid-Eighties Kandla and Santacruz were the only two operational economic zones in the country. However, there were demands later from the other States for analogous zones (Kundra 2000). The Central Government appointed a Cabinet Committee on Economic Policy and Co-ordination to consider these demands. The dismal performance of the Kandla and Santacruz zones prompted the committee to reject these demands (Kundra 2000). In the subsequent years, the government appointed a few committees to review the trade policy of the country in general and evaluate the performance of these zones in particular. The Alexander Committee on Import and Export Policies (1978), the Review Committee on Electronics (1979), the Dagli Committee on Controls and Subsidies (1979), and the Committee on FTZs and 100 per cent EOUs (1982) were set up. All these committees felt the need to restructure the trade policy of the country in favour of export promotion measures. The Review Committee on Electronics (1979) commented particularly on the poor performance of the SEEPZ. It identified the following factors as being responsible for the poor performance: (i) facilities available to the SEEPZ are not on par with those offered by similar zones in neighboring countries, (ii) long procedural formalities and prevalence of red-tapism and (iii) lack of power to the respective development commissioners. The committee also made a few recommendations to reshape the working of SEEPZ. The major ones are:

i) SEEPZ Board should be abolished and its duties and powers handed over to the Development Commissioner
ii) Exemption from corporate tax and tax on dividends for SEEPZ units, existing and new ones, for a five-year period with an in-built provisions to review extension of 'tax holiday' on merit at the end of five years
iii) A higher rate of depreciation for zonal units - at least 30 per cent a year
iv) Abolition of service tax
v) Exemption from levies other than central customs/excise duties
vi) Export credit/finance, market development grants for export promotion travels sales and publicity etc., and the zonal units should be treated on par with exporting units in the hinterland

Besides advocating a few incentives for exporting units, the committee emphasised on measures that might help reduce the cost of production and improve the administrative structure of the country. Subsequently, the Tandon Committee (1980) felt that even after two decades of operation there was no clarity in defining the objectives behind the promotion of such zones. At the same time, the committee also stressed the importance of such zones for economic growth, specifically in boosting exports of the country and recommended the creation of similar zones in other parts of the country. This recommendation was contrary to that made by the Cabinet Committee on Economic Policy and Co-ordination constituted in the late 1970s, which rejected the idea of setting up similar zones in other parts of the country. The Tandon Committee (1980) also emphasised the need to provide high quality infrastructure, institutions and incentives to promote such zones. In line with the recommendations of the Tandon Committee (1980), an inter-ministerial group was set up which proposed EPZs at Salt Lake in West Bengal, Chennai in Tamil Nadu, Cochin in Kerala, Nava Sheva in Maharashtra, Vishakapatanam in Andhra Pradesh, Mudgaon Vasco in Goa and Noida in Uttar Pradesh (Kundra, 2000). EPZs were approved only at Cochin, Chennai, Falta, Noida[vi] and Vishakapatanam[vii]. Subsequently, the Abid Hussain Committee (1984) reiterated the policy failure to provide an environment conducive for meeting the expectations of these enclaves. This committee recommended the following: a) adoption of a single window clearance, b) careful approach in selecting industries and c) concessions to be continued to sell 25 per cent of their output in the domestic market against valid import licence[viii].

On the whole, this phase witnessed a very prudent approach to the promotion of EPZs and, accordingly, a few EPZs came into existence. Meanwhile, various committees were constituted periodically to suggest means of improving the performance of the trade sector in general and these zones in particular. However, the government lacked a consistent approach in rectifying the supply side factors hindering the progress of EPZs. For instance, the government took the effort to identify a few more zones in the country as per the recommendation of the Tandon Committee (1980) but overlooked the recommendations to improve the institutional and infrastructure facilities in the zones. Moreover, the issue of ownership, administration, time-consuming administrative procedures and other structural problems received very little attention on the policy front. Accordingly, all six EPZs were owned and managed by the Central Government and it becomes one more form of a public sector unit, which

hardly faced any competition from other actors. The failure to provide better institutional arrangements to EPZs could be explained in terms of the loopholes in the economic policy of the country in the pre-reform period.

Second Sub-Period of EPZs Expansion (1990 to 2000)

The Indian economy has experienced significant policy changes since the 1990s because of the caution exercised by policy makers to reverse the failure of initial policies. This was carried out in acknowledgement of the macroeconomic failures of restrictive trade practices and under the pressure from international organisations committed to promote liberalisation. The focus of the new economic policy was not only to tackle the problems associated with the external sector but also to address the structural rigidities of the economy. These structural rigidities were cited as being responsible for the inefficiency of several sectors of the economy. This conscious effort had an impact and the Indian economy started to show signs of revival. The most important among them includes gradual improvement in country's trade balance and improvement in private participation in various economic spheres that eventually boosted capital formation in the country and increased inflow of FDI. The process of reshuffling the economic structure initiated in the 1990s (which also known as the Structural Adjustment Programme) also had an impact on the operation and working of EPZs and a good number of initiatives were taken on the policy front. Arrora (2003, quoted in Aggarwal 2004; p-6) identified nearly 164 circulars on EPZs/EOUs issued by the government during this phase.

The major policy developments noticed in this period[ix] include extension of the working of these zones from traditional activities to agriculture (1992) and allowing the private sector participation (1994). As a part of the government's commitment to promote private actors in such zones, the first private EPZ was set up in 1994 for the promotion of the gems and jewelry sector. This also symbolised the serious effort taken to rejuvenate the EPZs by providing a larger area for operation. Thus, major steps towards creating a competitive environment for EPZs and enabling them to compete in the world market took place in the post reform period. This also signifies the lack of major policy directions in the first phase of the EPZs regime.

Despite these, the fundamental problems remained unattended in these EPZs. Specifically, there was no law governing EPZ activities in the country and it depended completely on the government's EXIM policy. As a result, issues like protracted bureaucratic procedures and institutional and infrastructure problems in these enclaves remained unsolved. In fact, policy makers lacked the vision to identify deficiencies in the Indian economy and use the EPZs as a learning station before establishing them across the nation.

Second Phase: Emergence of SEZs Regime in India (2000 Onwards)

By the end of the 1990s, the Indian economy had overcome the external crisis of the early 1990s and had managed to withstand the East Asian economic crisis. Meanwhile, the parametres of economic performance were highly appreciated by the international organisations. This period also saw India, along with China, emerging as one of the economic giants in Asia. To improve its performance, Indian policy makers resorted to consistent policy interventions to address loopholes in the economy. One such

policy intervention led to the beginning of the second phase of the evolution of the SEZ policy in India with the EXIM policy statement of 1997-2002. Accordingly, the SEZ policy was put in place in the country on April 1, 2000. It was put forwarded as a 'qualitative transformation' of the earlier EPZs structure of the country (Government of India, 2000). This qualitative transformation was envisaged through 100 per cent FDI inflows from automatic channels, exemption from daily custom examination of export and import cargo, allowing import on self-certification basis and other measures. Thus, it was the very first attempt to admit and rectify the long cumbersome procedures hurting the EPZs structure in the country. It was given a legal framework in 2005 when the SEZ Act, 2005, was enacted followed by the SEZ Rules, 2006[x]. Besides this, every State Government enacted specific SEZ Acts and policies to push forward specific requirements through SEZs.

One of the striking departures of the current SEZ policy from the conventional EPZs policy relates to the clarity in defining the objective of its promotion. The EPZs policy was ambiguous in defining its boundaries. This was clearly reflected in the lack of specific policy measures to address different issues related to EPZs. It was also repeated by the different committees appointed by the government at different points of time. For instance, with respect to the Kandla FTZ, multiple objectives were reflected in its promotion campaign with special focus on the development of backward regions by facilitating the process of industrialisation. Completely different objectives were set for its successors, which in turn resulted in lack of clarity in shaping the EPZs. The SEZs, on the other hand, were established as enclaves that provide a free trade atmosphere for produce for exports and treated as foreign enclaves. Besides this, in the subsequent government circulars, the additional objectives of the SEZs are set to promote technology transfer, create employment and provide excellent infrastructure. The States assigned additional responsibilities to SEZs in line with their development agenda. Moreover, unlike EPZs where only the public sector played an active role, the SEZs allowed entry to the private, public and/or joint sectors. Further, along with manufacturing activities, the service sector was also allowed to operate for trade purposes. Free trade and warehousing activities too acquired a larger space for their operations.

Administration of SEZs

A few recommendations of the Review Committee on Electronics (1979) was finally put in place in the current SEZ policy specifically by making a significant change in the management of SEZs. This change resulted in greater powers devolving from the apex level to the zonal level. Specifically, the Development Commissioners of respective zones are made responsible not for the day-to-day operation but also to decide on the nature of enterprises to be allowed and labour related issues. Besides this, the striking feature of this SEZs system related to the recognition of the role of academicians in matters of SEZs approval. The role of these academicians, though, remains only on record and not in the form of effective intervention.

Further, labour related powers are transferred from the State Labour Commissioners to the Development Commissioners (DCs) of the respective zones to provide a hassle-free business environment and prevent all types of labour unrest. Further, despite the provision in the SEZs Act, the real practice with regard to labour power varied significantly in the seven conventional zones. Four

different types of arrangements were noticed in managing labour issues. The Development Commissioners, by law, exercise the powers of Labour Commissioner in Kandla, Santacruz, Noida and Vizag SEZs, while in Falta SEZ, the State Labour Commissioner is vested with control over labour issues. The Development Commissioner of the Chennai SEZ has voluntarily handed over power to the State Labour Commissioner to deal with labour issues and occasionally oversees the work of the latter. In the Cochin SEZ, the Development Commissioner has been provided with inspection officers to handle labour issues in the zone. Therefore, he assigns the State Labour Commissioner to deal with labor issues. The above arrangement is not in conformity with the provisions of the SEZs Act and thereby reveals inconsistency between practice and actual provision in the SEZ policy.

Moreover, the SEZs Act also fails to establish the source of the labour force. It is assumed that the existing labour market will supply the required work force. However, in practice, across the seven zones it was observed that the labour market fails to meet the specific requirements and gave scope for the entry of the intermediaries and subsequently exploitation of workers. Thus, there is a need for government intervention to ensure the supply of manpower to these zones to prevent any form of exploitation. An understanding the practice in Chinese SEZs will be quiet helpful in this regard. For instance, the Chinese government has set up 'A Labour Service Company' in each zone under Article 19 of the Rule on SEZs, which meets the demand for professional employees by the foreign companies. This was done in three different ways and channels (Chen, 1988). Initially, it was done via 'Transfer through Consultation and Selection'. A team of officials from the respective municipal organisation travelled to different parts of the country to recruit appropriate candidates for the SEZs. In 1982, it was followed by the 'Recruitment through Examination and Invitation'. The municipal government advertised the posts to be filled and selections were carried out accordingly. In this system, assurance was given to candidates for housing in the respective zones as well as employment for the spouse. Other incentives to attract skilled labour from mainland China included medical insurance, permanent residence to workers and their families irrespective of their background in Hukou, i.e., whether they were permanent or temporary residents, from rural or urban areas[xi] (Chu, 1985). The third system is known as 'Borrowing and Offering Joint Appointment'. The workers recruited through the first two channels enjoyed permanent residence in their respective regions while those recruited under the third channel were treated as temporary residents. The government attempted to arrest the persistent problem of unemployment in China by intervening in the supply of labour. In fact, in 1982 alone, 20,000 to 30,000 temporary workers were transferred to the Shenzhen SEZ (Oborne, 1986). In addition, the government also made efforts to train manpower in the region. The Municipal Government of Shenzhen founded a university in Shenzhen (Oborne, 1986).

Role of State Governments

Along with facilitating decentralisation in the administrative structure, the role of the respective State governments in improving the overall performance of the zones is duly recognised in the SEZs structure. This provision, however, was missing in the EPZs scheme. The role and responsibilities assigned to State governments under the current SEZ policy are: (1) forwarding the proposal for the creation of SEZs to the Board of Approval. While doing so, the respective State Governments shall ensure that the

proposal for the establishment of SEZs is in accordance with provisions specified in the SEZs rules of 2006, with respect to minimum area of land and other related terms and conditions. Meanwhile, it also needs to indicate whether the proposed area falls under reserved or ecologically fragile area as may be specified by the concerned authority. (2) before recommending any proposal for setting up SEZs, the state government shall ensure that required infrastructure facilities are provided and steps taken to adhere to various terms enlisted in the SEZs Act (Government of India, 2005 and 2006)

Thus, consent of the respective State governments regarding feasibility of SEZs and whether they are in a position to supply the required infrastructure is crucial to the whole process. The concerned State governments have also been given the power to enact State specific laws, rules and regulations pertaining to SEZs, basically to boost investors' confidence in the scheme and highlight the State government's role in various aspects relating to State levies, generation and distribution of power, environmental clearance etc. In line with the provisions, the respective State governments have taken policy decisions to meet state-specific development priorities. As a result, there are variations across the States with respect to State specific objectives (Table 3) and incentives offered to SEZs[xii]. Further, very little is known whether the objectives of the States are crafted in line with the comparative advantage of each State or whether they are designed arbitrarily and this provided the scope for further research.

Table 3: Objectives of SEZs across Major Indian States

Sl. No.	State	Objectives
1.	Karnataka	Attracting foreign investment and augmenting export from the State
2.	Orissa	To expand industrial and economic base through optimum utilization of natural and mineral resources
3.	Tamil Nadu	To bring large dividend to the State in terms of industrial and economic development and generation of additional employment
4	Andhra Pradesh	Industrial development and enhanced job opportunities.
5.	Rajasthan	To explore the inherent potential of the State in the field of gems and jewelry, handicrafts, woolen carpets etc., and increase export with high value addition.
6.	Kerala	Wealth creation and employment generation
7.	Maharashtra	Enhancing productivity and ease of doing business in the State by providing simple and transparent administration procedures
8.	West Bengal	Effectively utilize the local abundance in skill and craftsmanship and to provide employment opportunities
9.	Uttar Pradesh	Promoting industrial and economic growth in the State

Source: Various State specific SEZs Act and Policy

An Evaluation of India's Current SEZ Policy

In the quest to promote qualitative transformation through SEZs, the government has taken a set of measures to revamp the EPZs in India. Despite various factors in its favour and the changes initiated in the economic reforms and new trade policies (since 1990s), the SEZ policy has been received with some apprehension. This is reflected in loopholes existed in the SEZ policy itself. The challenges being posed by the current SEZ policy, which needs policy revision, can be categorsied thus: 1) Fiscal Dimension of SEZs; 2) Size and Location of SEZs, and 3) Land and Resettlement Issues.

Fiscal Dimensions of SEZs

Although India takes the credit for being the first country in Asia to experiment with the EPZs policy, it however failed to give crucial attention to matters on the policy front. It was reflected in the absence of the essential incentives' structure as highlighted by several trade committees of the late 1980s. Thus, to overcome this limitation and to boost the investors' confidence the Central and State governments offered a set of fiscal and non-fiscal incentives. The major actors who benefitted from the new SEZ policy include developers of the SEZs, unit-holders, domestic suppliers and financial institutions engaged in these special enclaves known as 'Offshore Banking Units' (OBUs)[xiii]. As against this, incentives were offered in the EPZs only to exporting units due to the restrictive practices followed regarding ownership and types of economic activities. The various exemptions and facilities provided by the Central government to the developer and unit-holders under the current SEZ policy are given in Table 4.

Besides offering incentives to SEZs developers and exporters, the SEZs Act also offered incentives to domestic suppliers[xiv]. This is an attempt to encourage the domestic producer to supply the inputs required by the units in the SEZs. Facilitating the forward and backward linkages between SEZs and DTAs is a means of enhancing the positive impact of SEZs on the economy. This is possible either by allowing the sale in the domestic area or through sub-contracts. However, the former has been criticised by development economists by arguing that it could result in exploitation of the domestic market rather than promote exports. Keeping this in mind, the Government has exercised caution and accordingly, trade between SEZs and DTA is brought under the coverage of exports and imports. Meanwhile, in order to promote backward linkages, permission has been granted for sub-contracting and outsourcing between zones and between DTA and SEZs. The major incentives offered to domestic suppliers included: (i) Income tax benefit as applicable to physical export under section 80 HHC of the Income Tax Act; (ii) Exemption from State levies and (iii) CST exemption. In addition to this, the SEZs Act also encompasses incentives to Off-Shore Banking Units in, an attempt to extend financial assistance on priority basis to these enclaves. It includes: (i) tax exemption under section 80LA of the Income Tax Act, 1961 (ii) no separate assigned capital requirement and (iii) exemption from CRR requirements.

Table 4: Major Incentives Offered by the Central Government to the SEZs Developers and Unit holders

Incentives	Developers	SEZs Unit
Income Tax Holiday	100 per cent deduction from profit derived from developing SEZs for 10 consecutive assessment years out of the first 15 years in which the SEZs is notified by the Central Government	Income tax holiday from the eligible profits and gains for 15 years as below a) 100 per cent for the first five years b) 50 per cent for the subsequent five years c) 50 per cent upon the creation of a specified reserve in the last five years
Other Direct tax benefits like DDT, Minimum Alternative Tax, Securities	Exemption of DDT declared or paid after April 1, 2005 by the developer	Exemption from the payment of Minimum Alternative Tax

transaction tax	Exemption from the payment of Minimum Alternative Tax	
Central Sales tax	CST exemption on all sales and purchase of goods other than newspaper	The benefit is same as applicable to the developer
Service Tax	Complete exemption from payment of service tax on all taxable services procured locally or from abroad.	The benefit is same as applicable to the developer
R and D Cess	Exemption from payment of R and D cess on import of technology	The benefit is same as applicable to the developer
Custom Duty	Import and export of all the goods, inputs including capital goods are exempt from the payment of custom duty – general rate being 12.5% and from the applicable countervailing and/or additional custom duties.	The benefit is same as applicable to the developer
Excise Duty	Exemption from the payment of excise duty on procurement of manufactured capital goods and all other inputs	The benefit is same as applicable to the developer
Other tax	In addition to this, the respective State governments have provided exemption from the payment of majority of State level taxes	The benefit is same as applicable to the developer
FDI	100 per cent FDI allowed for Township with residential, educational and recreational facilities on a case to case basis Franchise for basic telephone service in SEZs	100 per cent FDI allowed under automatic route in manufacturing sector with the exception of reserved industries No cap on foreign investment for SSI reserved items
Environment	-----	Exemption from public hearing under Environment Impact Assessment Notification
Drugs and Cosmetics	-----	Exemption from port restriction under Drugs and Cosmetics Rules
Sub-Contracting/Contract Farming	-----	SEZs units may sub-contract part of production or production process through units in the Domestic Tariff Area or through other EOU/SEZs Units SEZs Units may also sub-contract part of their production process abroad Agriculture/Horticulture processing SEZs units allowed to provide inputs and equipments to contract farmers in DTA to promote production of goods as per the requirement of importing countries

Source: Government of India 2005 and 2006

Incentives Structure across Indian States

Along with a central policy on SEZs in terms of the SEZs Act and SEZs Rules, every State has its own specific policy to resolve various issues related to SEZs. In this State specific policy, every State extend further tax concessions to various actors involved in the promotion, development and facilitation of SEZs. Uniformly across the States, tax exemptions are allowed in local taxes and levies including sales tax, purchase tax, octroi cess etc. Due to tax constraints, if it is not advisable to grant direct exemption, the taxes paid would be reimbursed. Besides this, a few benefits enjoyed by SEZs vary across the States (Table 5). For instance, in the case of electricity, a few States (Madhya Pradesh, West-Bengal, Andhra Pradesh, Karnataka and Jharkhand) extended subsidy without specifying the maximum number of years. However, in Maharashtra, Orissa, Gujarat exemption on electricity duty/tax has been extended for 10 to 20 years. Further, there are variations across the States in giving exemption for stamp and registration duty. Rajasthan defined exemption for stamp duty and registration fees very ambiguously whereas Tamil Nadu provided such exemption to land. It would be quite interesting to locate, whether or not the States that provide liberal incentives and subsidies have managed to improve the performance of their SEZsvompared to other states or have recorded any noticeable reverse trend. This calls for further research.

Table 5: SEZs Incentive Structure across Major Indian States

Sl. No.	State	Incentives
1.	Uttar Pradesh	Exemptions is given for Mandi Shulka
2.	Maharashtra	Exemption from payment of stamp duty and Registration fees till the 31st March, 2006 SEZs set up in C, D and D+ areas and No Industry Districts of the State have been exempted form payment of electricity duty for 15 years. However, units set up in other parts of the State have been exempted from payment of electricity duty for 10 years.
3.	Karnataka	Exemption from entry tax for SEZs units and developers. Reduction in tax on supply of petroleum products to SEZs Any sale of electricity to the zones should be exempted from payment of electricity tax
4.	Andhra Pradesh	Exemption from levy of tax on entertainment held within SEZs Exemption from the levy of the tax on luxuries provided within SEZs. 50 per cent exemption for payment of stamp duty and registration fee on transfer of land meant for industrial use in the SEZs. Complete exemption of stamp duty and registration fee for loan agreements, credit deeds, mortgages and hypothecation deeds executed by the SEZs units for assets in the SEZs in favor of banks or financial institutions will also be allowed The State exempts power in SEZs from Electricity Duty and Tax
5.	Tamil Nadu	All industrial units and their expansions to be located in the SEZs will be exempt from payment of Stamp Duty and Registration Charges toward land transactions

6.	Rajasthan	All industrial units and their expansions to be located in the SEZs will be exempt from payment of Stamp Duty and Registration Charges Exemption from work contract tax, entry tax, land building tax Exemption from payment of electricity duty to SEZs developers and units that generate, transmit, distribute power for a period of 10 years from the date of commencement of such services provided that the power so produce is consumed within the SEZs.
7.	Orissa	Exemption from work contract tax, entry tax, VAT, entertainment tax, luxury tax All transfer of SEZs land in favor of strategic Developer, Anchors Tenants Service Providers, SEZs Units would be exempt from payment of stamp duty and registration charges Power consumed (both purchased and self-generated) in development, operation and management of the SEZs by the SEZs developers would be exempted from payment of electricity duty/tax for a period of 20 years Power consumed (both purchased and self-generated) by the Units/ establishment within the SEZs would be exempted from payment of electricity duty/tax for a period of 20 years. However, there will be no exemption from payment of electricity duty/tax on sale of power outside the SEZs
8.	Kerala	Power generated within SEZs shall be exempted from payment of electricity duty for a period of 10 years from the date of commencement
9.	West Bengal	100 per cent electricity duty will be waived without any restriction in respect of all industries to be set up in Manikanchan SEZ and other SEZs
10.	Gujarat	Exemption from all State taxes including Sales Tax, VAT, Motor Spirit tax, luxury tax and entertainment tax , purchase tax and other State taxes. SEZs units shall be exempted from electricity duty for 10 years from the date of production or rendering of services Complete exemption on payment of Stamp Duty and Registration fees on transfer of land meant for industrial use in the SEZs area (this facility available to both developer and unit holder) Complete exemption on payment of Stamp Duty and Registration fees for loan agreement, credit deeds, mortgages etc., pertaining to SEZs units or which will be executed within the SEZs area
11.	Madhya Pradesh	Exemption from all State tax including commercial tax, turnover tax, VAT, Octroi, Mandi tax, Purchase tax, electricity cess, stamp duty and any other such type tax of the State Government SEZs shall be exempted from electricity duty, cess and any other tax or levy on sale of electricity for self-generated and purchased power
12.	Jharkhand	Exemption from sales tax, VAT, luxury tax and entertainment tax and State duties on transaction within the SEZs. Sales tax and other taxes on inputs made to SEZ units from suppliers within the State 50 per cent exemption will be allowed on Stamp Duty and Registration fee on transfer of lands meant for industrial use in the SEZs Complete exemption of stamp duty and registration fee for loan agreements, credit deeds, mortgages and hypothecation deeds executed by the SEZs units for assets in the SEZs in favor of banks or financial institutions

Source: Author's Compilation based on various State-specific SEZs Act and Policy

A critical evaluation of the various incentives offered in the SEZs, however, reveals that in the bid to push the SEZs as engines of growth the government (both Central and State) has placed too much emphasis on incentives. This is specifically so, because the objective behind the promotion of SEZs in the country is based on the SEZ policy rather than the comparative advantage of each State. Thus, with similar objectives and targeting of same international clients it becomes necessary for different State governments to engage in the war of incentives. Of course, lack of incentives to boost the confidence of exporters was a lacuna in the EPZs and different committees reiterated it in the 1970s and 1980s. This seems to be wrongly interpreted in the present context. A glance at the incentives offered across the States under the SEZs framework gives a clear indication of the tax incentive being used as the sole strategy in attracting investor's interests.

In the literature, the demand and supply side factors are considered as the two driving forces in shaping the export performance of a country. However, until recently the policy focus in India was on the demand side while neglecting the supply side. The supply side factors include well-maintained institutional set-up, infrastructural facilities, macroeconomic environment, incentives, attitude toward foreign investment and extent and type of foreign investment allowed in the host economy and labour market. Further, at the firm level, factors like size, location, availability of raw materials, technology and ownership pattern influence the phenomena.

In the context of other countries, the literature on the subject lists certain factors responsible for the success or failure of such enclaves. Factors identified in the literature include location of the zone (Madani, 1999; Cling and Letilly, 2001; Ota, 2003 and others), clustering and linkages with the domestic economy (Jenkins et al, 1998; Jayanthakumaran, 2003), infrastructure and supportive policy framework (Madani, 1999; Ge, 1999). Besides these, though incentives and subsidies are also considered essential for attracting investors' attention and hence crucial to the success of zones, empirical evidence on this issue is inconclusive. Thus, there is a need to concentrate on other factors on the supply side as the handicap to these factors may adversely affect the efficient working of other factors and the economy as a whole. For example, lack of high quality infrastructure may cause under-utilisation of foreign investment and further increase transport cost. In fact, a good number of industrial sectors outside the zones are contributing significantly in generating trade surplus without any additional incentives. For instance, without any equivalent tax concessions on par with SEZs, the EOUs are contributing almost 21 per cent to national trade (2008-09). Thereby it challenges those arguments that tax concessions offered outside the SEZs are incapable of promoting competitiveness. The experience of Chinese SEZs makes it further clear that an incentive is a necessary but not a sufficient condition for the promotion of SEZ policy. The Chinese government had realised this and had taken precautionary steps while extending incentives to these enclaves. Accordingly, it prescribed different slabs of incentives across zones, types of investors and projects. Meanwhile, due recognition was given to other factors, particularly infrastructure and institutional, because any lacunae in these factors can adversely affect the efficient working of other contributory factors and the entire economy.

Moreover, such incentives and subsidies could affect the government exchequer in two ways – i) on account of the expenditure for creating separate institutional arrangements to reduce the long chain of bureaucratic procedures and the creation and building world of class infrastructure exclusively

for these zones, and ii) due to the revenue loss in offering fiscal incentives in terms of tax concessions and subsidies by exercising its role as fiscal manager. This adds to the revenue and capital expenditure of the government, on the one hand, and result in massive revenue loss to the exchequer, on the other. Further, depending upon the magnitude and extent of the fiscal burden, the SEZs could also influence the distribution aspects of the government's budget due to depletion of revenue. As identified in the literature, government revenue is an important channel through which trade policy tends to have an impact on social welfare (Bussolo and Nicita, 2005). A further limitation of the current SEZ policy relates to its uniform tax sops to all sectors. As against the current trend of uniform incentive across sectors, the government could think of restructuring the incentives on the priority of a sector's development, i.e., different incentives for different sectors with emphasis on the comparative advantage of each region and priority of development. As already explained elsewhere in the paper, towards this understanding the practice followed in the Shenzhen SEZ is of great help.

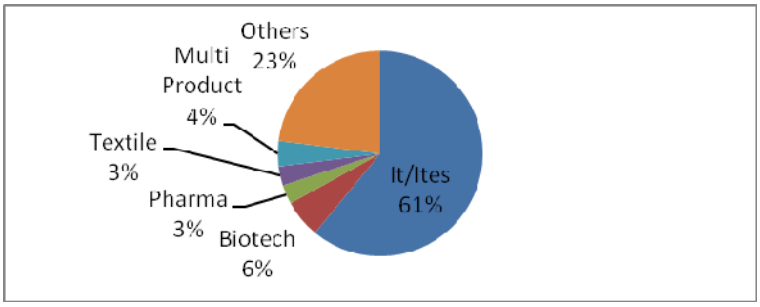
Size and Location of SEZs

Within ten years of the implementation of the SEZ policy in India, the economy has seen a surge in the number of exporting units as well as fresh proposals for setting up of different types of SEZs. By January 20, 2011, on a very large scale, 581 SEZs were given formal approval and 374 SEZs were notified. The total number of operating SEZs in the country now stands at 122 (www.sezindia.nic.in)[xv]. It should also be noted that there are large discrepancies between the numbers of SEZs projects approved and actually operational in the country. This indicates the long gestation period involved in the establishment of SEZs project in the country. As against India, China had only five SEZs in the last three decades and they came into existence through a piecemeal approach based on the experience of the initial SEZs. India, on the other hand, has given indiscriminate permission to most of the SEZs projects put before the Board of Approval (BoA) without considering the probability of their success, location advantage and availability of manpower in the region. Moreover, as of now, no study has been undertaken by the government to analyse the problems and prospects of the upcoming SEZs. In this context, there is a need to evaluate the experience of a few zones in the country before promoting them on a large scale. Such an evaluation will be helpful in revisiting the SEZ policy in the backdrop of problems and prospects of up-coming SEZs.

The government's approach with regard SEZs is also in conflict with its general practice, where many development policies are first tested on experimental basis and later, based on experience, promoted or modified accordingly[xvi]. The need to stop the process of approving more SEZs gains importance given the amount of revenue foregone in each zone[xvii]. The current practice of SEZs approval is in variance with the practice followed in the country during the EPZs regime, where the government was more prudent in taking decisions. All the seven conventional EPZs of the country were based on the recommendations of committees appointed for the purpose. These committees not only studied the feasibility of setting up of new zones but also carefully analysed the location advantage and the products that these zones sought to promote. In fact, a couple of EPZs as proposed by the committee did not see the light of day in the late 1980s due to flaws in the project proposal.

An analysis of sector wise and state wise distribution of the formal approval of SEZs brings to a light a few more malpractices. The electronics and IT/ITES sectors received maximum approvals in the country (Figure 1). In fact, there is an apprehension that the larger part of the increase in SEZs project in the country could be attributed to reallocation of investments from DTA to SEZs. This move was specifically noticed in the case of IT and IT-enabled industries. The prime reason for this was the introduction of the sunset clause on tax holiday for IT industries based upon the recommendations of the Kelkar Committee report on 'Direct and Indirect Tax Policy'. Before the Kelkar Committee, a committee headed by Dr Parthasarathi Shome also recommended the same (Palit and Subhomoy, 2008). In the 2002-03 budget, a sunset clause was included to be implemented from March 31, 2009 for STPI and EHTP. The government attempted to nullify the argument of gradually shifting IT industry from DTA to SEZs, however, a quick view of the profile of the new SEZs approved by the Government substantiates the counter argument that SEZs perhaps are leading the realignment of investment from DTA to SEZs. IT and ITES (including hardware) account for 61 per cent of the total approvals (www.sezindia.nic.in)[xviii].

Figure 1: Sector wise Distribution of SEZs Approval (Formal) in India



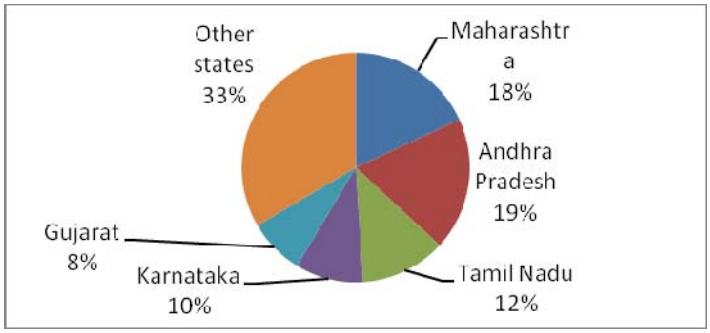
Source: www.sezindia.nic.in

This can be seen in the failure to promote SEZs in those industries – for instance handicraft products – in which India had a comparative advantage and capability to promote employment generation as well. Instead, maximum approval has been given to IT industries, which do not assure employment in the larger context and generate employment only for well-qualified and technical workers. Thus, there is a need to divert attention to other sectors identified under the 'target approach' of the various EXIM policy statements. In this context, it is to be noted that the need for caution in promoting industries was identified in the early 1980s by the Abid Hussain Committee (1984). Unfortunately, no thought is given to this issue. Decisions are taken rather arbitrarily regarding approval of SEZs. At least, now the Government can think of promoting SEZs for products that not only improve export performances but also have distribution effects. Moreover, the government can also promote SEZs for Indian products that are listed in bilateral trade agreements between India and other countries and have an assured international market. Such attempts will also minimise the risks associated with fluctuations of international markets and its corresponding impact on these enclaves[xix]. This can be implemented by promoting industries based on the comparative advantage of each State/region.

Towards this, understanding the stages of industrial development followed in China within the banner of SEZs will be quite helpful. Instead having a very ambitious SEZ policy, the process of industrialisation in Shenzhen was achieved in three stages (Wong and Chu 1985), each of which was introduced gradually. Initially, considering the inherent advantages and difficulties involved in the region, emphasis was placed on labour intensive but modern small-scale industries. In the second stage, a selective approach was followed with special emphasis on high technology industries. In the third stage, the industrialisation process was guided towards diversifying the industrial base of the region with advanced technology and modern scientific methods of production. The approach was helpful in developing the infrastructure base in the region in a systematic way and also to meet the targets set in its promotion plans (Tantri, 2011). Moreover, the need for caution in diversifying SEZs exports also gained importance considering their decisive role in deciding the import intensity of exports and their real contribution henceforth in net foreign exchange earnings of these enclaves[xx].

The promotion of SEZs based on the comparative advantage of each region may also help tackle problems related to regional disparities in development and thereby arrest problems related to migration. The SEZs, on the contrary, are presently concentrated in the developed States rather than underdeveloped ones in the country. For instance, developed states like Maharashtra, Andhra Pradesh, Tamil Nadu and Karnataka have received more approvals while others State have only 33 per cent of the total approved SEZs in the country (Figure 2). Further, little attention seems to given to the regional composition of SEZs in line with its trade potential, i.e., whether the zones promoted in every State and across regions are in line with its comparative advantage and resource base or allotment of SEZs was made in an arbitrary manner.

Figure 2: State wise Distribution of SEZs Approval (Formal) in India



Source: www.sezindia.nic.in

Within the developed states, SEZs are located in districts with development parametres that are above the national average (Mukhopadhyay, 2009). This in turn is assumed to have an adverse impact on the urban infrastructure due to congestion and diseconomies of scale (Mitra, 2007); specifically, it is feared that these zones may ruin the existing infrastructure without actually adding to the new infrastructure base in the country (Mukhopadhyay and Pradhan, 2009). Thus, SEZs may pose two types of threat in the promotion of balanced development (Tantri, 2011b). One, the developed States have received the lion's share of the SEZs approval in the country compared to the less

developed States. This further widens the already existing gap between developed States and the States lagging behind. It is quite possible that regions with SEZs receive more attention, which depletes the resource base of the surrounding regions and promotes a backwash effect rather than corresponding spread effects of development. . Second high concentration of SEZs in a region exhausts the resource base of the region and results into diseconomies of scale and congestion, which in turn poses a completely different set of challenges. Attempts should be made to integrate employment objectives with the help of SEZs. This cannot be assured merely by assigning one more objective to it. It demands more government intervention to make information available in the employment exchequer of each zone and the units operating in the zones to ensure speedy overall development. The government can erase the role of the intermediaries and reduce exploitation of labour as well. Thus, it would be quiet useful if the Government revisits the SEZs policy in this regard.

Land and Resettlement Issue

In the current SEZ policy land related issues are ignored, i.e., it is silent on issues related to acquisition of land, the compensation formula, etc. Since the government does not have sufficient land in its possession to allot it for the development of all SEZs, acquiring land from private owners, under lease or through purchase, is the only viable option. In this circumstance a few questions emerge – how will the private land be acquired? Who is authorised to acquire? What type of private land should be acquired? Most importantly, how much will these private owners get as compensation and what should be the criteria for determining compensation?

In the absence of any explanation in the SEZs Act, initially, the respective State governments were acquiring land from private owners within the banner of public purpose as defined in the Land Acquisition Act 1894. This was due to the ambiguity in defining what constitutes public utility service (Kasturi, 2008). There are divergent views, also, on who should acquire land for the development of SEZs. Bhaduri (2007) strongly advocates negotiation between a private actor and the landowner to rule out the possibility of government intervention. A few (Banerjee et al 2007, Bose 2007), however, strongly support government involvement considering the pitfalls in direct negotiations. The government took a cautious approach and declared April 5, 2007 as the cut-off point for land acquisition and accordingly the BoA set a few guidelines for the approval of SEZs[xxi]. Moreover, the real nature of government intervention in land acquisition differs across the major States. For instance, in Tamil Nadu, the government had a huge land bank in its possession before enactment of SEZs Act and it did not face any set back in dealing with land related issues in the promotion of SEZs[xxii]. Further, in the absence of a well-defined Rehabilitation and Resettlement Policy, the initial years also saw debates over the criteria for defining compensation. Generally, compensation is defined by the government based on the current market price, which is again questionable considering the practice of under-reporting in the land deed and sales to save on stamp duties (Gill 2007; Kasturi 2008). Even if it is above the market price, inflation further brings down the compensation value (Gill 2007). Thus, for the purpose, alternative models are suggested in the literature. A few argue in favour of monthly pension along with savings bonds (Gill 2007) and employment assurance for one person from each family. Mukhopodhyay (2009), on the other hand, proposes transfer of part of the profits from successful SEZs projects into a

community fund, which should be used for the development of physical and social infrastructure in the region. A related to this brings to the fore the issue of who should be compensated in land acquisition. As per the provision in the Land Acquisition Act 1894, compensation should be paid only to landowners and non-landowners like tillers, tenants, agriculture labourers and women are not eligible. The government has taken initiatives to address this issue by placing the National Rehabilitation and Resettlement Policy for approval in Parliament. Despite such a timely intervention, the issue of handling displacement caused by a development project is yet to be resolved. The experiences in the Nandigram SEZ in West Bengal, the Mangalore SEZ in Karnataka and the Jamnagar SEZ in Gujarat highlight the dimensions of this contentious issue. Moreover, other issues like how to distribute the expected benefits from such projects to the different stakeholders involved in the process are yet to be resolved.

Furthermore, the increase in the number of SEZs in the country has also been questioned considering the possible impact on agriculture and future food security[xxiii]. If one goes by Chinese experience, then it presents a gloomy picture. In the post-SEZs period, there was a drastic decline in area under cultivation in Shenzhen from 53,000 mu in 1980 to 3,000 Mu in 2005 (Tantri, 2011). This also had an impact on the food security of the region. This policy non-lesson seems to be missed in the haste to adopt the Chinese model of SEZs in India and the emphasis on policy attention needs to be taken seriously in India. Unlike the scenario in China, India's SEZs agenda has spread all over the country instead of being confined to one region. It points to the intensity of the problem that could crop up in near future if preventive action is not taken.

Conclusion

Based on the above analysis we argue that the failure of EPZs structure to make a mark on the Indian economy is specifically due to policy failure i.e., lack of a well-articulated policy to accommodate and execute factors necessary for their success. The major factors for this in turn could be seen in the loopholes in the policy of the pre-reform period. As noted by Grasset and Landy (2007), the strong presence of the license raj system and difficulties in accessing imports and exports made EPZs less attractive. Nevertheless, at the implementation level, a prudent approach was followed not only in choosing the number of zones in the country but also in choosing their location. The early 1990s witnessed changes in the operation and working of EPZs in line with the government's effort to reshuffle the economic structure as a part of economic reforms but a few structural issues were overlooked. For instance, the roles of State-specific agendas and the importance of decentralisation were not recognized.

It was in the first decade of economic reforms that a radical move was made by imitating the Chinese model of SEZs. At the outset, the imitation of the Chinese model of trade policy in the country appears as an improvement over the conventional EPZs. It fulfilled its promise of promoting qualitative transformation of EPZs. The current SEZ policy is also known for clarity in objectives, broader economic area to operate and recognising the role of different actors in the promotion of SEZs. Despite the numerous credits in its favour, the SEZ policy in India needs a pragmatic re-visit. Specifically, the current SEZ policy seems to be suffering from flaws in the ideas behind policy formulation and execution. The most important argument in its favour stems from the various flaws in the policy that

are in conflict with other development objectives of the economy. The major ones are the government's stand on incentives offered to different actors involved in the process, land acquisition and the compensation formulae and the sectoral and geographical expansion of SEZs. Thus, as a way ahead we argue that there is a need to restructure the SEZs scheme in the country by identifying the problems and prospects in expansion rather than just extending liberal incentive schemes. Based on the above policy analysis, we offer the following suggestions;

- Put a sunset clause on the number of SEZs in the country. Within ten years of promulgation of the SEZs policy in the country, there has been a surge in number of SEZs approved. As opposed to this, China promoted only five SEZs in the last three decades in stages based on the experience of the initial few. Further, very little is known about the problems and prospects of the newly notified SEZs. Building dossiers on every zone will help in correction and modification of the existing SEZ policy. The need to introduce sunset clause also becomes important in view of the magnitude of the revenue that the government may forego in each zone, which will obviously have severe fiscal repercussions on the Indian economy as explored in the current study.
- Diversify India's exports basket through SEZs to boost the performance of these zones and protect them against all external economic shocks. The corrective policy measures hinge on the type of land that should be allocated for the expansion of SEZs. If every State promotes SEZs in areas with a comparative advantage with regard to natural resource base, labour, capital, land and, most importantly, in conformity with development priorities, the problems of land grabbing, regional disparities and the possible consequences would recede. Further, the government, if possible can intervene in the supply of labour required in the upcoming SEZs. In this regard, the Chinese model will be of great use.
- As against the current trend of uniform incentive across sectors, the government could restructure the incentives based on the priority of the sector in the development process, i.e., different incentives slabs for different sectors with emphasis on the comparative advantage of each region and priority of development.
- In the current SEZ policy, it is assumed that the labour market in each zone can supply the required number of workers and therefore there is limited scope for government intervention. This, however, in the long run might give room for middleman and exploitations of workers. Thus, there is a pressing need for government intervention in this area. Government supervision will not only assure supply of the required manpower to these zones and prevent exploitation of labour but also act as a safeguard against interference by middleman/agents in labour supply. As a first step in this direction, the government can promote educational institutions in the regions according to the requirements of each zone.

Notes

[i] Earlier studies on this, however, suffer from a few limitations. For instances, Kundra (2000) has sketched the evolution of SEZs policy for the period 1980-1998, without critically evaluating evolution of SEZs policy since the beginning (1960s). Moreover, policy sketch was restricted only to EPZs structure. Aggarwal (2004, 2005), on the other hand, has provided the history of policy under four different time-period since the beginning, which in turn guided by the number of zones operating in each period followed by macro-economic scenario of the economy. Since author work came much before the enactment of SEZs act in the country, thus study fails to make any demarcation between the EPZs structure v/s SEZs policy. Besides these, recent studies (Aggarwal, 2006; Menon and Soumya 2009; Mitra, 2007: Sharma, 2007: Shivaramaksrishnana, 2009 and others) have explained the SEZs policy in a static dimension in particular concentrating on a few provision of current SEZs policy rather than sketching the difference between two policy regime and then elaborating problems and prospectus of current SEZs policy.

[ii] It is to be noted that in the present exercise we are following a completely different type of policy classification compared to previous studies (Kundra, 2000; Aggarwal, 2004 and 2005) of the same.

[iii] This classification of EPZs expansion is guided by the general macro economic structure of the country rather than number of zones in operation.

[iv] Because, Bombay port had to face severe work load, which was not in consistent with available infrastructure facilities.

[v] Water was provided at Rs 0.40 to Rs 0.65 per 1000 litres depending on water consumption (IIFT, 1990)

[vi] They become functional in 1985-86

[vii] was approved in 1989 and become functional in 1994.

[viii] For further details, please see Annexure Table 3.1 for detailed chronological development in policy initiatives that took place in this first sub-period

[ix] Please refer Annexure Table 3.1 for major chronological policy developments in the different phase of SEZs expansion in India

[x] Following this, a few amendments have done in the SEZs Act and Rules in the last few years

[xi] It is to be noted that in the traditional Chinese economic system migration between provinces was not allowed due to the rigid 'Hukou System' which categorizes the population into temporary and permanent residents. Permanent residents are not only entitled to jobs but also get the benefit of the various social security schemes provided by the local Government. On the other hand, temporary residents are entitled to jobs on a temporary basis without any assurance of social security.

[xii] The issue of incentives across major states is elaborated in the subsequent section

[xiii] The financial institutions engaged in these delineated duty-free enclaves are known as Off Shore Banking Units (Government of India, 2005).

[xiv] In the SEZs context, domestic suppliers are defined as those industrial units which are set up outside the SEZs and supply raw materials and/or assist in production related jobs (Government of India, 2005 and 2006).

[xv] Excerpted on 20th January, 2011

[xvi] For instance, NREGA, The Pradhan Mantri Adhrsha Gram Yojana

[xvii] As elaborated in the previous section

[xviii] Excerpted on 20th January, 2011

[xix] For discussion on empirical evidence on the cause and effect between fluctuations in world economy and Indian SEZs See Tantri (2011 and 2012).

[xx] See for detail Tantri (2010c)

[xxi] For discussion, please see Menon and Mitra (2009).

[xxii] See for Discussion on this Vijayabhaskar (2010)

[xxiii] See Shah (2010)

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Annexure Table 1: Chronology Order of Major Policy Developments in the EPZs/SEZs Evolution in India

(1960-2010)

Year	*Policy Initiatives*
	Policy Intervention in the First Phase of EPZs Regime (1960s to 1990)
1958	The early thought of creating FTZ in the western coastal of India
1961	Lok Sabha approved decision of promoting FTZ in Kandla, of India
1965	The establishment of FTZ in Kandla
1966-67	The Kandla FTZ become operational
1967-72	Number of concessions were offered to attract investment in the zone
1972	The establishment of Santacruz EPZ for electronics products exports
1973-74	Santacruz EPZ become operational
1978-84	Government constituted several committees for trade promotion and these committees offered numerous recommendations to improve the structure and performance of these enclaves • Committee to look into the problem hindering the growth of KAFTZ (1978). • Alexander Committee on Import & Export Policies (1978), • Review Committee on Electronics (1979), • Dagli Committee on Controls and Subsidies (1979), • Tondon Committee on Export Strategy (1980), • Committee on FTZs and 100% EOUs (1982), • Abid Huasin Committee on Trade policy (1984)
1980	DTA sale is permitted up to 25 per cent of production against import license on payment of applicable custom duties
	Sale of rejects up to 5 per cent allowed on payment of applicable duties
	Disposal of Waste and Scrap allowed on payment of applicable custom/excise duties
	Sub contracting of production process/part of production permitted for EPZs units with the approval of Commissioner of Customs
1981	Five-year tax holiday granted to EPZs units
1986	Reimbursement of Central Sales Tax to EPZs units Gems and jewelry sector given permission to operate in SEEPZ
1984	The decision to establish EPZs of Cochin, Chennai, Falta and Noida approved
1985-86	EPZs of Cochin, Chennai, Falta and Noida started functioning
1987	DTA sale permitted up to 25 per cent of production on payment of full customs duties
	EOUs granted five-year tax holiday and reimbursement of CST
1988	Sub contracting of production process/part of production Permitted for EOUs with the approval of commissioner of Customs
1989	The decision to establish Vizag EPZ was approved
	Policy Intervention in the Second Phase of EPZs Regime (1990s to 2000)
1991	DTA sale permitted up to 25 per cent of production on payment of 50 per cent of Custom duties
1992	The agriculture, horticulture and aquaculture sectors allowed to operate under the umbrella of EPZs/EOUs
1994	DTA sale permitted up to 50 per cent in the case of agro products on payment of 50 per cent of Custom duties
	Sub-contracting of production process/part of production Permitted for EPZs units with the approval of Assistant Commissioner of Customs

	Trading, re-engineering and reconditioning units also permitted to be set up in EPZs
	Vizag EPZ became operational
1995	Disposal of Waste and Scrap allowed on payment of 50 per cent of applicable customs/excise duty
	Sale of Rejects up to 5 per cent allowed on 50 per cent of applicable duties
1997	Disposal of Waste and Scrap allowed on payment of applicable excise duty in cease waste and scarp have been generated wholly from indigenous raw materials; otherwise duty to be leviable at 50 per cent of customs or excise duty, whichever id high
	Sub-Contracting of Production Process/part of production a) approval to be given by Development Commissioner for final processing by customs b) units using predominantly indigenous raw materials allowed to sub-contract part of production in the DTA
	DTA Sale a) permitted up to 25 per cent of production on payment of 50 percent of customs duties or excise duty, whichever is high b) permitted on payment of excise duty in case of goods produced wholly from indigenous raw materials c) additional DTA sale over and above 25 per cent of production of freely importable goods on payment of full duties subject to achievement of VA and meeting export obligations d) electronics hardware units allowed to sell up to 50 per cent of production on payment of production on payment of full duty without linkage with VA achieved e) permitted software units outline DTA sale
1998-99	Promotional measures/procedural changes announced like; • extension of tax holiday for EOUs/EPZs to 10 year • sub contracting facility for DTA • permission to set up private software technology parks
1999-2000	FTZ to replace EPZ and to be treated as outside the country's exports.
	Entitlement of DTA sales for EOUs and EPZs increased to 50 per cent of f.o.b. value of previous year.
	NFE as a percent of exports made uniform at 20 per cent for both EOUs and EPZs.
	Policy Initiatives During SEZs Regime (2000 Onwards)
2000-01	All existing EPZs converted into SEZs, as per the focus of EXIM Policy Statement of 1997-2002. Announced on April 1, 2000.
	The sale of tea by Export Oriented Units (EOUs) and units in Export Processing Zones (EPZs) in Domestic Tariff Area (DTA) was banned.
	With a view to simplify operating regime, Special Economic Zones (SEZs), EPZs and EOUs were exempted from industrial licensing requirement for establishment of projects for manufacture of items reserved for small scale sector.
	The units in SEZs were permitted to credit 100 per cent of their foreign exchange receipts to EEFC accounts except foreign exchange acquired by way of purchase against rupees from any person resident in India other than another unit in a SEZ
	The Union Budget for 2001-02 announced the following major policies for safeguarding the interest of domestic producers in the context of proposed complete removal of QRs and to boost the export; • A ten-year tax holiday to the developers of SEZs on the same lines as developers of industrial parks • A provision to exempt anti-dumping duty or safeguard duty on goods imported by 100 per cent EOUs, units in the Free Trade Zones (FTZs) or in the SEZs;
	With respect to SEZs, Foreign Direct Investment (FDI) was permitted under automatic route for all manufacturing sectors, except a small negative list.
	The SEZs developers have been allowed duty free import/procurement from DTA for development of SEZs to give a boost for development of integrated infrastructure for exports.
	The units in SEZs were allowed to bring back their proceeds in 365 days and retain 100 per cent of proceeds in Exchange Earners Foreign Currency (EEFC) account.
	The SEZs developers would be made eligible for various entitlements as provided for in the Income Tax Act.

	In order to speed up the approval process, the Government constituted a single Board of Approval for EPZs/SEZs/EOUs as a matter of procedural simplification. With respect to SEZs, Foreign Direct Investment (FDI) was permitted under automatic route for all manufacturing sectors, except a small negative list. The SEZs developers have been allowed duty free import/procurement from DTA for development of SEZs to give a boost for development of integrated infrastructure for exports. The units in SEZs were allowed to bring back their proceeds in 365 days and retain 100 per cent of proceeds in Exchange Earners Foreign Currency (EEFC) account. The SEZs developers would be made eligible for various entitlements as provided for in the Income Tax Act. In order to speed up the approval process, the Government constituted a single Board of Approval for EPZs/SEZs/EOUs as a matter of procedural simplification
2001-02	To speed up the approval process, the Government constituted a single Board of Approval for Export Processing Zones (EPZs)/Special Economic Zones (SEZs)/EOUs towards procedural simplification The EXIM Policy Statement of 2002-07 provided certain exemption with respect unite operating under SEZS. It includes; • Overseas Banking Units (OBUs) permitted to be set up in SEZs which, *inter alia*, would be exempt from CRR, SLR and give SEZ units and SEZ developers access to international finance at international rates • Income tax concessions would be given to units in SEZ • Exemption from CST (Central Sales Tax) to supplies from DTA (Domestic Tariff Area) to SEZ • Drawback/Duty Entitlement Pass Book (DEPB) to DTA suppliers • Transactions from DTA to SEZ would be treated as exports under Income Tax Act and Customs Act • Exemption to SEZ units from External Commercial Borrowings (ECB) restrictions, freedom to make overseas investment and carry out commodity hedging The Union Budget of 2002-03 further provided certain incentives to units working in SEZs. It includes; • 100 percent deduction of export profits under Section 10A to all SEZ units commencing production on or after April 1, 2002, for a period of five years, and thereafter at 50 per cent for the next two years. • Supplies to SEZs from DTA to be treated as physical exports instead of deemed exports for the purposes of duties, tariffs and central sales tax. At present, a person resident in India has been prohibited from taking any general or life insurance policy issued by an insurer outside India. It was decided, in consultation with Government of India, to exempt units located in SEZs from the purview of the above stipulations for taking out general insurance policies. Accordingly, Ads are free to allow remittances towards premium for general insurance policies taken by units located in SEZs from insurers outside India provided the premium is paid by the units out of their foreign exchange balances. Extension of the concessions available for infrastructure by way of 10-year tax holiday to the developers of Special Economic Zones (SEZs) on the same lines as developers of industrial parks. Setting up of Agri Economic Zones to promote agricultural exports on the basis of specific products and specific geographical areas. SEZs have been liberalised further by granting permission to developers for duty free import/procurement from DTA, to sell goods in the DTA in accordance with the import duty in force, for subcontracting a part of production abroad, to bring back their export proceeds in 365 days (as against normal period of 180 days) and to retain 100 per ent of the proceeds in the EEFC account. Introducing measures such as no requirement of license for setting up units in these zones for items reserved for SSI and granting of infrastructure status, under the Income Tax Act, to SEZ developers. Additional benefits to EOU/EPZ/EHTP/ STP Units include rationalisation of NFEP/ EP norms, supplies made by the trading units to the bonded warehouses to be treated as exports for the purpose of domestic sales entitlement, subcontracting of production abroad permitted, simplification of procedures regarding utilization of goods and greater delegation to Development Commissioners to approve EOU/EPZ projects.

2002-03	Units located in Special Economic Zone have been allowed to open, hold and maintain Foreign Currency Account with an authorized dealer in India subject to certain conditions, in lieu of the special provision for EEFC Accounts for units in the Special Economic Zones given earlier. The Reserve Bank formulated a scheme for the setting up of Off-shore Banking Units (OBUs) in Special Economic Zones (SEZs) by banks. Entities in the SEZs were granted general permission to undertake hedging transactions in the international commodity exchanges/markets to hedge their commodity price risk on import/export, provided such transactions are undertaken on "stand-alone" basis. A separate export promotion council for Export Oriented Units (EOUs) and Units of Special Economic Zones (SEZs) has been set up to enhance exports by these entities. It would function as an approved trade body like other export promotion councils and would facilitate the functioning of the concerned units. A number of incentives/facilities for Special Economic Zones (SEZs) were announced: • The stipulation of twelve months or extended period thereof for realization of export proceeds was removed in respect of SEZs, • Units in SEZs were permitted to undertake job work abroad and export goods from that country itself, subject to certain conditions, • Gem and jewelry units in SEZs and EOUs were allowed to receive payment for exports in the form of precious metals *i.e.,* Gold/Silver/Platinum equivalent to the value of jewelery exported, subject to certain conditions, and • Netting off export receivables against import payments as well as capitalisation of import payables was permitted, subject to stipulated conditions for SEZ units. Entities in the SEZs were granted general permission to undertake hedging transactions in the international commodity exchanges/markets to hedge their commodity price risk on import/export, provided such transactions are undertaken on "stand-alone" basis. Units for the generation and distribution of powers have been permitted within SEZs, to ease power related issues in and around SEZs.
2003-04	Units in SEZs were allowed to raise ECBs in compliance with the guidelines issued by Government of India, subject to the conditions that they (i) raise ECBs for their own requirement, and (ii) not transfer or on-lend any borrowed funds to their sister concerns or any other units in DTA.
2004-05	All supplies made to Special Economic Zones (SEZs) to be treated as physical exports with effect from September1, 2004 and entitled for benefits of Duty-Free Replenishment Certificate (DFRC) under the foreign trade policy. As per the existing guidelines, nominated agencies/approved banks can import gold on loan basis for on-lending to exporters of jewellery and by EOUs and units in SEZs for manufacturing and export of jewellery on their own account only. After a review of these guidelines, the maximum tenor of gold loan was enhanced to 240 days *i.e.*, 60 days for manufacture and exports, and 180 days for fixing the price and repayment. ADs were permitted to open standby LCs for tenor equivalent to the loan period and on behalf of entities permitted to import gold. The standby LC should be in favour of the internationally renowned bullion banks only. SEZ units obtaining gold/silver/platinum from the nominated agencies on loan basis required to export that jewellery within 90 days from the date of release, except outright purchase.
2005-06	SEZs Act 2005 has been passed in the parliament Supplies from domestic tariff area (DTA) to SEZs made eligible for benefits under Duty Free Entitlement Certificate (DFEC) and Target Plus Scheme subject to the specified conditions, provided the payments are realised in free Foreign exchange In exercise of the powers conferred by section 55 of the Special Economic Zone Act, 2005 (28 of 2005), the Central Government announced Special Economic Zones Rules (SEZs), 2006 containing definitions, procedures etc. regarding setting up and operation of SEZs
2006-07	SEZs Rule, 2006 came in force First SEZs Amendment Rules, 2006 was introduced
2007-08	Second SEZs Amendment Rules, 2006 was introduced. The major components of it includes • Minimum land requirements for development of different types of SEZs is revised • Minimum processing area requirements rationalized and revised (25-35-50%) • Directions for provision of specified type of infrastructure (eg 24/7 – power, AC) • Bar on use of previously used plant and machine

	• Empowering the Board of Approvals ("BoA") to relax contiguity criteria, allow change in categorization of SEZs • Reduction of validity period of in-principle approval (1 yr, extendable by 1yr at a time) • Procedural changes – introduction of new forms, approval letters etc
2008-09	Authorised Dealers allowed to SEZ developers to open, hold and maintain EEFC Account and to credit up to 100 per cent of their foreign exchange earnings
2009-10	Hazardous Wastes Management, Handling and Transboundary Movement Third Amendment Rules, 2010 came into exist
	Exemption to SEZ Developers from obtaining distribution licence
	Respective Development Commissioner of the jurisdictional Special Economic Zone to be the enforcement officer in respect of the notified offences committed in a Special Economic Zone.
	Sections 20, 21 and 22 of the SEZs Act 2005 come into force.

Source: Review Committee on Electronics (1979), IIFT (1990), Kundra (2000), Reserve Bank of India Annual Report for various issues, EXIM Policy statement of various year, Various issue of Economic Survey of India.

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