AUTHORS
Shely Gupta
Research Scholar, Meerut College, Meerut
Dr. Prateek Gupta
Lecturer, Dept. of Commerce,FASCL Mody Institute of Tech. and Science, Lakshmangarh, Rajasthan

Realities & Specialities of Special Economic Zones

ABSTRACT

India has shown an increasing trend in foreign trade since the last five decades as per the plan framed by the Government of India. India achieved a major milestone in her journey towards globalization when the Government decided to establish specially delineated duty free enclaves, appropriately named as Special Economic Zones (SEZs). SEZs are effectively contributing in generation of employment, export promotion, inflow of foreign capital and many more areas. Moreover, the Government is providing a number of incentives and various schemes have been launched to promote SEZs. The Government has decided to setup SEZs in almost every part of the country and to reinforce this decision, it has intended to establish more than 111 SEZs in the near future. A stable and hassle-free environment is essential to carry out exports and this, in turn, would require raising the level of production, reduction in duties and taxes and other forms of financial support. Keeping all these points in view, the Government of India designed a framework to setup SEZs. These Zones are involved specially in production of quality export-oriented goods and services at low costs. In this paper, an attempt has been made to analyse the basis which makes these Zones different and special.

1. INTRODUCTION

In the current era of globalisation, export promotion is playing a vital role in economic growth in developing countries. Various policies and techniques are being adopted to promote export competitiveness by governments in these countries. As a policy means of achieving this goal, the concept of Export Processing Zones (EPZs) has gained noticeable significance in recent years.

Export Processing Zone (EPZ) is an industrial area that constitutes an enclave with regard to customs' tariffs and the commercial code in force in the host country. Traditionally, the concept of EPZs evolved to compensate for anti-export-bias created by the import substitution industrial (ISI) policy regime. The EPZ offers quality infrastructure and hassle-free business environment permitting an economy to promote and diversify exports and develop a competitive industrial base. The vision of EPZs in an export-oriented regime is to establish a viable internationally competitive platform that is capable of attracting export oriented FDI to promote exports. The main characteristics of these Zones are Size, Concentration of economic activities and Capital intensity of the zone.

The growth and development of SEZs in China has set a role model for the globe, therefore there is a need of re-look over history of China's SEZs. In 1978, China set up SEZs to provide tax concessions. China started with four SEZs and the fifth one was set up in 1988. In the late 1980s, almost every city in China had its own science and technology development zone, where conditions were more or less similar to the SEZs. The size of the SEZs has been an important factor in the success of China's reform process. China has now declared the entire region or province as an SEZ. Every SEZ in China is spread over thousands of square kilometers. 'Shenzen', the largest SEZ in China has an area of 33,000 hectares. The Labour and 'Hire and Fire' policies have attracted foreign investors to invest in China's SEZs. Decentralization of power to the local authorities is another major reason for the success of SEZs in China. Local authorities have the necessary powers to frame their own policies to improve the SEZs and attract foreign and domestic investors. They can approve FDI proposals up to $ 30 million. A strong domestic market has played an important role in the success of China's SEZs. This promoted local purchases and technology transfers. Marketing is another factor in attracting foreign investment to the SEZs. The thrust of the SEZs in China was to attract FDI and technology. SEZ contributed more than 50% of China's foreign export earnings in the beginning and the result is quite visible as China enjoys 20 years experience in SEZ attracting billions of dollars of investment. There were 176 zones across 47 countries in 1986 in total. By 2003, the number of zones swelled to over 3000 across 116 countries. A large number of them are operating in developing countries. We can see the growth of such zones in following table-

Tahle - 1

Growth of SEZs

Year	1975	1986	1995	1997	2003
Countries	25	47	73	93	116
Zones	79	176	500	845	>3000

There was a need of economic reform in India too, in context of export promotion and economic development. As the concept of SEZ is quite wide and development oriented, therefore the Government of India decided to establish specially delineated duty free enclaves, appropriately named as Export Processing Zones (EPZs). The first zone was set up in Kandla in the highly backward region of Kutchh in Gujarat in as early as 1965. It was followed by the Santacruz Export Processing Zone in Mumbai which started its operations in 1973.

Prior to 1981, income tax concessions were not given to the zone units. Tax holiday of 5 years was extended to the units only in 1981. Besides, there were no standardised procedures for exemption from excise duties. There was no state sales tax exemption for Kandla until 1974. Central sales tax was not exempted until 1978 in both Maharashtra and Gujarat. Domestic tariff area sale was permitted only against import licenses and the rates of duty were exorbitant. Subcontracting of production was not allowed.

To provide fillip to exports, the government decided to establish four more zones in 1984. These were located at Noida (Uttar Pradesh), Falta (West Bengal), Cochin (Kerala) and Chennai (Tamil Nadu). Thereafter, Visakhapatnam EPZ in Andhra Pradesh was established in 1989, though it could not become operational before 1994. During the 1990s, when the government undertook to simplify and rationalise the tax structure and major tax cuts were being introduced in the rest of the economy, incentive package was made more attractive for the zone units also. Though there was no change in the tax holiday, duty on DTA sales was reduced to 50% of custom duty in 1991 and the rate of duty on sale of rejects was reduced to 50% of the applicable duty. Besides, DTA sales entitlement for agro based EPZ units was raised in 1992 to 50% of production. EPZ units were given option in 1995 to switch over to export promotion capital goods (EPCG) scheme. In the EXIM policy for 1997-2002, additional DTA sale was allowed to units based on indigenous raw materials, provided they fulfilled the export obligation.

The EXIM Policy (1997-2002) has introduced a new scheme from April 1, 2000 for establishment of the Special Economic Zones (SEZs) in different parts of the country. SEZ is an almost self contained area with high class infrastructure for commercial as well as residential inhabitation. SEZs are permitted to be set up in the public, private, joint sectors or by the State Governments with a 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 adopted to improve the quality of governance of the zones. These include relaxation in the conditions for approval process and simplifying custom rules. More recently, Development Commissioners are given the labour commissioner's powers. SEZ policy is thus the most significant thrust towards ensuring the success of export processing zones.

From November 1, 2000, the Export Processing Zones at Kandla, Santa Cruz (Mumbai), Cochin and Surat have been converted into SEZs. In 2003, other existing EPZs namely, Noida, Falta, Chennai and Vizag were also converted into SEZs. In addition, approval has been given for setting up of 26 SEZs in various parts of the country in the private/JV sectors or by the state. These include SEZs at Nanguneri (Tamil Nadu), Positra (Gujarat), Kulpi (West Bengal), Paradip (Orissa), Bhadohi and Kanpur (Uttar Pradesh), Kakinada (Andhra Pradesh), Dronagiri (Maharashtra) and Indore (Madhya Pradesh). Besides, Santacruz EPZ was also extended in terms of size by adding 11 acres. Introduction of the SEZ policy has marked the period of emergence of the EPZ policy in India. It is expected to go a long way in determining the success of the EPZs (now called SEZs) in India. An attractive package of incentives was offered to SEZ units in 2000. Non-fiscal incentives included exemption from industrial licensing for manufacture of items reserved for small scale industries (SSI), 100 per cent FDI through automatic route to manufacturing SEZ units with certain exceptions. Among the developers of the approved zones are such prominent corporate names as Reliance, Bajaj Auto, Mahindra & Mahindra, TCS, Wipro and Ranbaxy, as well as others known for their strategic orientation and long term commitments. Their participation provides a great deal of credibility of the process and reinforces the expectations of proponents of the whole programme.

2. BENEFITS TO SEZ DEVELOPER

The main characteristics of SEZs which make them different and special are the benefits provided by the Government to the units in SEZs and their developers in form of number of fiscal and non-fiscal incentives which are as follows:

- Developer of a SEZ may import/procure goods from DTA without payment of duty for the development, operation and maintenance of any Infrastructure, Utility, Facility or Service.
- Income tax exemption for a block of 10 years in 15 years from the date of operations at the option of developer.
- Income Tax exemption to Investors in SEZs.
- Investment made by individuals, etc., in the SEZ is also eligible for exemption u/s 88 of IT Act.
- Exemption from Service Tax.
- Exemption from Central Sales Tax on Sales made from Domestic Area to SEZ Developer.
- Full authority to provide services like water, electricity, security, restaurants, recreation centers, etc., on commercial lines.
- Generation, Transmission and Distribution of Power in SEZs allowed.
- Foreign investment permitted to develop township within the SEZ with residential areas, markets, play grounds, clubs, recreation centers, etc.
- Freedom in allocation of developed plots to approved SEZ units on purely commercial basis.

3. BENEFITS TO SEZ UNIT

Customs and Excise

o SEZ units may import or procure from the domestic sources, all their requirements of capital goods, raw materials, consumables, spares, packing materials, office equipment, DG sets, etc., in the Zone without any license or specific approval.

- Exemption from Customs duty on import of capital goods, raw materials, consumables, spares, etc.
- Exemption from Central Excise duty on procurement of capital goods, raw materials, consumables, spares, etc., from the Domestic Market.
- Goods imported/procured locally duty free could be utilized over a period of 5 years.
- Domestic Sales on payment of applicable duty.

Taxes

- 100% Income Tax exemption (Sec. 10A) for first 5 years and 50% for 5 years thereafter. Reinvestment allowance to the extent of 50% of ploughed back profits for the next 5 years.
- Exemption from Service Tax.
- Physical export benefit to DTA units for goods supplied to SEZ units.

Foreign Direct Investment

- 100% foreign direct investment under the automatic route is allowed in manufacturing sector in SEZ units.
- No cap on foreign investments for SSI reserved items.

Banking & Finance

- Setting up Off-shore Banking Units (OBUs) allowed in SEZs. Thus SEZ units can avail of financing at International rates.
- OBU's allowed 100% Income Tax exemption on profit for 5 years and 50% for next 5 years.
- External commercial borrowings by units up to $ 500 million a year allowed without any maturity restrictions.
- Flexibility to keep 100% of export proceeds in EEFC account with freedom to make overseas investment from it.
- Commodity hedging permitted.
- Exemption from interest rate surcharge on import finance.
- Facility to realize and repatriate export proceeds within 12 months.
- SEZ units allowed to 'write-off' unrealized export bills up to 5%.

EPZ exports increased in India from less than Rs.1 million in 1966 to over Rs.97,727 million in 2002. Over the same period, total employment increased from 70 to around 89,000, net foreign exchange earnings increased from Rs. 0.16 million to Rs. 43,195 million and value addition increased from 21% to 44%. Average annual growth rate of value addition was as low as 2.9%.

Foreign exchange earnings are one of the most important benefits expected from EPZs in India. The argument is that EPZs provide foreign exchange earnings that allow the economy to slacken the foreign exchange constraints regarding their import needs for the rest of the economy. The value of net foreign exchange earnings (NFE) increased from Rs. 3439 million in 1990 to Rs. 49020.

One of the objectives of EPZs has been to promote non traditional exports in general, in developing countries. EPZs make up for infrastructural deficiencies and procedural complexities, offer a more conducive investment climate and are therefore expected to offset the disadvantages of higher costs of producing in these countries. They are also expected to attract technology transfers which overcome some of the technological limitations of the firms in high tech sectors. Indian zones do not seem to have succeeded in this direction. Evidence suggests that the share of two high-tech sectors namely, pharmaceuticals and engineering products, declined continuously. Though the export basket of India is still dominated by relatively low-technology products which comprise about 80 percent of India's manufactured exports, the share of low technology industries in total manufactured exports is continually declining and that of high technology industries is slowly increasing.

Any proposal for setting up of SEZ 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 SEZ are approved at the Zonal level by the Approval Committee consisting of Development Commissioner, Customs Authorities and representatives of State Government. Approval is given for setting up new SEZs in Private/Joint/State Sector. Approvals have so far been given for setting up of 117 new Special Economic Zones (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. Another specialty of these Zones is employment. In the year 1966, total employment was only 70 but by 2000, 88,977 were employed in these Zones which is increasing at a high rate. Besides it, the units in these Zones manufacture a number of items for export. We can find items exported by the few Zones individually from the table given below:

Table - 2
Exports from SEZs

Zone	Items Exported
SEEPZ SEZ	Gem & Jewellery (57.3%), electronics hardware (16.7%), electronics software(15.4%) and trading (10.6%)
NOIDA SEZ	Gem & Jewellery (51.3%), electronics software (11.7%), engineering goods (10.9%), electronic hardware (6.3%), textiles and garments (3.9%) and plastics & rubber goods (2.1%)
MEPZ SEZ	Textile and garments (29.8%), electronic software (23.1%), engineering goods (21.7%), pharmaceuticals & chemicals (8.7%), leather / sports goods (7.4%) and electronics hardware (5%)
KANDLA SEZ	Pharmaceuticals & Chemicals (53.9%), plastics and rubber goods (14.6%), textiles & garments (11.1%), engineering goods (4.6%) and food & agro products (1.4%)
SURAT SEZ	Gem & Jewellery (92.7%), textiles and garments (2.8%) and engineering goods (1.1%)
FALTA SEZ	Textile and garments (66.9%), Leather / sports goods (17.6%), Food and agro products (3.3%), Plastics & Rubber goods (2.2%) and Pharmaceuticals & Chemicals (1.2%)
VISAKHAPATNAM SEZ	Gem & Jewellery (94.9%), Textiles & Garments (2.6%) and electronics software (2.3%)
KOCHI SEZ	Electronics hardware (28.3%), Food & agro products (22.3%), Plastic and rubber goods (10.3%), engineering goods (8.3%), gem & jewellery (6.2%), textile & garments (5.9%) and electronics software (3.4%)

In contrast, EPZs in India continue to be dominated by domestic investment. This was despite its edge in terms of labour costs, availability of trained manpower and a stable macroeconomic environment. The share of FDI in total investment increased slowly from 12% in 1989 to slightly over 18% in 2000. During 2000-2003, however, FDI inflows increased faster. By 2003, its share in total investment had increased to 25%, therefore, FDI is expected to assume a much larger role.

4. CONCLUSION

We can say that the concept of SEZs is not only good but has become essential in economic development for each and every nation. These SEZs have a wide scope but also face limitations as they need a huge infrastructure which creates crisis of land. We can learn a lesson from the crisis in Nandigram (West Bengal), where the proposed SEZ was met with wide-spread protests. Another problem is regarding competition, as nowadays, every developing country is busy in promoting export. Each one is trying to set up more and more number of SEZs, which are creating a wide competition in the international market. The entry of Multinational Corporations (MNCs) in a country blocks the path leading to the establishment of SEZs although they (i. e. MNCs) provide a bundle of facilities. These corporations keep changing their location whenever they see a slight cost advantage and their exit can result in sudden closure of factories and results in unemployment.

As India is one of the largest consumers of crude oil, upstream investment is a crucial facet in India's energy security. Tax arbitrage possibilities in special economic zones and excessive protection for refining are combining to harm India's energy security. Too many SEZs in a state have left the state government worrying about the implications it might have on the state revenue collections, especially sales tax. Apart from these, we always try to follow China's example, but copying the Chinese model entirely may not be beneficial to India as Chinese SEZs are much larger in magnitude, and in addition to export processing, they promote activities such as commerce, tourism, housing, agriculture and industrial production. Therefore, in this context, the scope of Indian SEZs is limited.

REFERENCES

1. *The Economic Times, 1st Feb.,2008*
2. *Business Today, 6th May, 2007*
3. *Business Today, 17th Dec., 2006*
4. *Chartered Financial Analyst, Feb.,2008*
5. *Indian Economics- The SEZs Rush, 21st June, 2006*
6. *Financial Management- Twilight zones, April, 2007*
7. *Asian Economic Review, April,2007*
8. *The Economic Challenger, April-June,2007*
9. *Agarwal A, performance of EPZs, Nov.,04*
10. *Agarwal A, EPZs in India, March,05*
11. *Siddiqui, J.A. (2002)- Economic Zoning: Strategy for Development*