



ISSUES OF SEZ - GS III MAINS

Q. SEZs can function as growth engines for development of the Indian economy and address the challenges faced by the Indian economy especially in the COVID years. Critically analyse (15 marks, 250 words)

News: *Govt. working on SEZ reforms: Commerce Secretary Barthwal*

What's in the news?

- The Centre is working on reforms in the Special Economic Zone (SEZ) domain so that movement of goods between domestic tariff area (DTA) and SEZ space is carried out smoothly without affecting the competitiveness of goods in the export markets.

Special Economic Zones:

- Special Economic Zones (SEZ) are enclaves within the territory of a country, in which business, trade and tax laws are different from the rest of the country.

Objectives:

In India the SEZs are governed as per the provisions of the SEZ act of 2005, which aimed to achieve the following objectives.

- To boost exports of goods and services.
- To create additional economic capacity.
- To generate employment.
- To attract domestic and foreign investments.
- To create a conducive administrative and business environment.
- To develop infrastructure facilities.

Incentives:

- Simplified procedures for development, operation and maintenance of the SEZ.
- Duty free import and domestic procurement of goods for the development, operation and maintenance of your company/SEZ unit
- 100% income tax exemption on export income for first five years, 50% for five years thereafter and 50% of the export profit reinvested in the business for the next five years.
- Exemption from GST and levies imposed by state government (supplies to SEZs are zero rated under the IGST Act, 2017, meaning they are not taxed)
- Exemption from Minimum Alternate Tax (MAT)
- Single window clearances for all state and federal government approvals
- Exemption in electricity duty and tax on sale of electricity by certain states in India
- Presence of customs officer in the SEZs to facilitate and expedite the trade processes
- Offering land to SEZ developers at concessional rates by some states.



However, the SEZ act is now more than 16 years old and several issues have emerged in the functioning SEZs in India. In India the SEZs have not been as successful as the SEZs in countries like Singapore and China.

Significance of SEZ in India:

1. Industrial Development:

- SEZs act as growth engines for industrial development by providing a conducive environment for businesses to set up manufacturing units.
- They offer various infrastructure facilities such as reliable power supply, transportation, and communication networks, which attract investments from both domestic and foreign companies.
- Example: The Kandla Special Economic Zone, established in 1965, was the first SEZ in India. It played a pivotal role in transforming the barren land of Kandla into a bustling industrial hub, generating employment opportunities and driving economic development.

2. Manufacturing Hub:

- SEZs focus on promoting manufacturing activities and export-oriented production.
- They provide a range of incentives, including tax benefits, duty-free import of raw materials and capital goods, and simplified regulatory procedures, which encourage manufacturing units to operate in these zones.
- Example: The Nokia SEZ in Sriperumbudur, Tamil Nadu, became a major manufacturing hub for mobile phones, attracting significant investments and contributing to the growth of India's mobile manufacturing industry.

3. Export Promotion:

- SEZs are primarily designed to boost exports and enhance India's global competitiveness.
- Companies operating in SEZs enjoy various export-related benefits, such as exemption from import and export duties, simplified customs procedures and access to global markets.
- Example: In the financial year 2021-22, SEZs accounted for exports worth USD 65.28 billion, contributing to about 16% of India's total exports. (Source: Ministry of Commerce and Industry, India)

4. Employment Generation:

- SEZs create significant employment opportunities, both direct and indirect, as they attract a large number of industries and businesses.
- This, in turn, leads to the development of ancillary industries and supporting services, generating employment for the local population.
- Example: As of March 2022, SEZs provided direct employment to approximately 24 lakh (2.4 million) people in India. (Source: Ministry of Commerce and Industry, India)

5. Attracting Foreign Direct Investment (FDI):

- SEZs serve as magnets for foreign direct investment (FDI) due to the attractive Incentives and a favourable business environment they offer to foreign companies.
- FDI inflows into SEZs contribute to technology transfer, Infrastructure development, and increased economic activity.



- Example: During the financial year 2021-22, FDI inflows into SEZs stood at USD 6.58 billion, showcasing the significant role SEZs play in attracting foreign investments. (Source: Department for Promotion of Industry and Internal Trade, India)

Challenges Faced by SEZs:

1. Land Acquisition and Infrastructure Development:

- As of March 2021, a total of 379 SEZs have been approved in India, covering an area of over 55,000 hectares.
- However, land acquisition for SEZs has faced delays and legal challenges due to issues related to compensation and land use.

2. Regulatory and Policy Changes:

- According to a report by the World Bank, India has made significant efforts to improve the ease of doing business, but regulatory changes continue to pose challenges for businesses, including those operating in SEZs.

3. Lack of Skilled Workforce:

- A study by the National Sample Survey Office (NSSO) found that the availability of skilled labour remains a challenge for SEZs, especially in remote or less-developed areas where some SEZs are located.

4. Export Dependence:

- In the financial year 2021-22, SEZs accounted for about 16% of India's total exports, which highlights their significant reliance on export-oriented industries.

5. Competition from Non-SEZ Areas:

- According to a report by the Reserve Bank of India (RBI), the presence of SEZs has led to concerns about potential spatial diversion, where businesses may prefer to set up operations in non-SEZ areas to take advantage of similar incentives.

6. Compliance and Approval Processes:

- A study by the World Bank found that India's businesses spend an average of 71 days per year to comply with labour-related regulations, which includes SEZs.
- This compliance burden can create delays and challenges for businesses.

7. Infrastructure Bottlenecks:

- Despite ongoing efforts to improve infrastructure in SEZs, a report by the Comptroller and Auditor General (CAG) of India noted that several SEZs continue to face challenges related to inadequate transportation and power supply.

8. Sustainability and Environmental Concerns:

- The development of SEZs can lead to environmental concerns.
- A study by the Centre for Science and Environment (CSE) highlighted instances of environmental degradation and violations of environmental norms in some SEZs.

9. Operational Costs:

- A report by the Associated Chambers of Commerce and Industry of India (ASSOCHAM) highlighted those operational costs, including compliance and infrastructure maintenance, can offset the incentives offered by SEZs for businesses.



Recommendations of the Baba Kalyani Committee:

The government constituted a committee headed by Mr Baba Kalyani, in 2018 to study the existing SEZs of India and prepare a policy framework to adopt strategic policy measures.

- Rename SEZs in India as 3Es - Employment and Economic Enclave.
- Framework shift from export growth to broad-based employment and economic growth.
- Separate rules and procedures for manufacturing and service SEZs.
- Ease of Doing Business (EoDB) in 3Es such as one integrated online portal for new investments.
- Extension of Sunset Clause and retaining tax or duty benefits.
- Unified regulator for IFSC.
- Dispute resolution through arbitration and commercial courts.

WAY FORWARD:

To address the underlying issues in the functioning of SEZs, the Union government has announced that it will bring a new legislation to govern the SEZs to create ease of doing business and enhance competitiveness. The new legislation will ensure

- States become partners in development of SEZs.
- Custom administration is hassle free and fully IT driven.
- The new proposed law needs to be in line with the recommendation of Baba Kalyani Committee, to effectively address the present challenges of SEZs, which include
- Shift in approach from export growth to broad-based Employment and Economic Growth. (Employment and Economic Enclaves- 3Es).
- Separate rules and procedures for manufacturing and service SEZs.
- Shift from supply driven to demand driven approach for 3Es development.
- Creation of enabling ecosystem development by funding high speed multi modal connectivity, business services and utility infrastructure.

If governed effectively SEZs can function as growth engines for development of the Indian economy and address the challenges faced by the Indian economy especially in the COVID years. The new SEZ legislation will be a good step in the right direction.