

SEZ A Report

Bharatiya Janata Party

Foreword

SEZ (Special Economic Zone) were the instrument which led the Chinese economy to new heights. In India the SEZ have become a thing of controversy thanks to reckless decisions taken by some of the State Governments that ignored the needs of farmers and other weaker sections. Prime Agricultural land was allotted to select industrial houses without paying attention to key issue of rehabilitation and adequate compensation. What happened in Singur, Haryana, Punjab and Maharashtra is a sad tale of Government's insensitivity and ineptness to address the issues of farmers and common man. BJP constituted a committee headed by senior BJP leader Shri M Venkaiah Naidu to study the impact of SEZ. It submitted its report to the BJP President Shri Rajnath Singh. We are publishing the report for the report to help readers in appreciating the impact of SEZ in the country.

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UPA distorts a sound policy

INTRODUCTION

The UPA government, which is now 30 months old, stands exposed on many counts: betrayal of the promises to protect the interests of the aam adami and kisans; weak and compromising approach to dealing with the threats to India's internal security; criminalization of politics and governance at the central level; scandals galore in ministry after ministry; including the country's defense establishment; and misuse of institutions for the purposes of partisan and vindictive politics.

One of the major scandals of the UPA government is the manner in which it has permitted a mushroom of over 400 proposed Special Economic Zones (SEZs) all over the country. By distorting a sound SEZ policy formulated by the previous NDA government, it has allowed many promoters to turn SEZs into the biggest land-grab racket in the history of independent India.

This is evident from the fact that, under the UPA government's framework of SEZs, the promoters are allowed to retain as much as 65%-75% of the acquired land for non-processing purposes – namely, for purposes other than the industries and services for which the SEZ is sought to be established. All the attractive incentives available to the processing zone will also be available to the land under the much larger non-processing zone. The current legal framework of SEZs also creates a huge disadvantage to industries and businesses in the Domestic Trading Area (DTA), with the distinct possibility of many of them turning sick.

Not surprisingly, many real estate companies, which have no track record in manufacturing or export businesses, have become SEZ promoters. It is one of the worst-kept secrets of the UPA government that granting permission to establish SEZs has become a huge source of corruption for the ruling party. This is a repeat of what happened in one of the biggest corruption scandals that rocked the Congress government in the early 1990s, when telecom licenses were issued to all and sundry on other considerations. Experts have already warned that many of the proposed SEZs will never come up, or become successful.

Nevertheless, they will have dispossessed kisans, khetmazdoors and other allied rural workers of their traditional sources of livelihood.

The Bharatiya Janata Party recognizes the need and usefulness of SEZs.

They are a necessary instrument to make India a strong and globally competitive exporter in manufacturing and services. If properly implemented, they will not only generate large-scale employment but also raise the standard of Indian industry and service businesses. They will enable India to attract FDI, procure latest technologies and learn best management practices from across the world.

Hence, we are proud of the fact that India's first SEZ policy was unveiled by the NDA government.

The BJP President has established a committee under the Chairmanship of Shri M. Venkaiah Naidu, to study and make suitable recommendations. The committee has had interaction with various sections of opinion including representatives of the agrarian sector, various chambers of commerce and industry, tax specialists and the state governments in which BJP is the ruling party or is a part of the ruling alliance. The committee has endeavored to (a) point out the distortions in the SEZ scheme promulgated by the UPA Government that need correction, and (b) present a proper perspective on before the nation.

Background

In April 2000, the NDA Government had incorporated in the EXIM policy, a Special Economic Zones Scheme with a view to providing an internationally competitive environment

for exports. Its objectives included making available to units in SEZs goods and services free of taxes and duties, integrated infrastructure for export production, quick approval mechanisms and a package of incentives to attract foreign and domestic investments for promoting exports. The present UPA Government has brought a central law for SEZs with a view to placing the policy on a firmer footing. Accordingly, the Special Economic Zones Act 2005 was enacted in May 2005 and subsequently Rules under it have been promulgated in February 2006.

That has set off a flurry of activity and even greater confusion and controversy. The differing viewpoints of the Ministry of Finance and the Reserve Bank of India on the one side and those of the Ministry of Commerce and Industry on the other are not a hidden secret. The differences between the Congress party and its Left allies show no signs of being reconciled. The Congress-Left conflicts on the labour matters are still to be played out.

Inconsistent statements have come from Union ministers on the objectives of SEZs, their desirable sizes and numbers, the proportion of the processing area, etc.

The issues concerning land have been highlighted by Congress leaders themselves in some states and these have imported a new intensity to the debate on SEZs.

The grant of approvals to SEZ projects across the country at breakneck speed has given rise to suspicions of extraneous factors playing a role and of business houses amassing large numbers of projects simply to preempt the ground.

As of now, the Board of Approvals has given "formal approvals" to 237 SEZ projects and "in principle approvals" to another 168. Thus as many as 400 SEZ proposals are in the pipeline. However, it appears that apart from the pre-existing 16 export processing zones which had been functioning before the passing of the 2005 Act, only 25 of the formally approved projects have been notified. The other projects are still in run-up stages and it is difficult to say how many of them will be seriously pursued.

On the other hand, it is surprising to see that in many cases the action for acquisition of land has been progressing rapidly even though the project has not yet been approved.

The eagerness of developers to amass land, particularly in projects adjoining major urban centres, has raised eye brows of people across the country and have, in fact, made a Union minister to term the promotion of SEZs as a "land scam". According to him, the SEZs serve as a ploy to hand over huge tracts of agricultural land to corporate big wigs. The tearing hurry with which SEZ projects have been approved, obviously without adequate scrutiny and some even without endorsement by the state governments concerned or at variance with their recommendations, lends credence to charges of corruption in the process.

It should have been expected that by providing the SEZ policy on a statutory basis the Government would impart a sharper purpose to it. It is unfortunate that what seems to have really happened is that a scramble has been generated among developers to make quick profits by exploiting cheaply acquired land for real estate development and little attention has been paid to achieving the real objective of generating industrial investments for the purpose of export. The controversies and scams that seem to be snow balling can only result in defeating the real objectives of the SEZs policy that had been put in place by the NDA Government in the year 2000.

Broadly speaking, the controversies raised by the SEZ policy of the UPA Government relate to the following :-

- Number and size.
- Real estate exploitation overwhelming the avowed purpose of generating investments for export oriented manufacturing and service businesses in the processing area.
- Loss of land to agriculture and inadequacy of compensation and other deprivation suffered by farmers and allied rural workers.
- Neglect of village abodes within SEZs.
- Impact on central and state revenues.
- Dilution of the export objective.
- Impact on regional balance in development.
- Ambiguities in the trade interface between SEZs and the Domestic Trade Area (DTA) and the likelihood of tax evasion through "transfer pricing" and other malpractices.

- Administrative weaknesses.
- Ouster of state government, municipal and local authorities from the regulatory administration of SEZs.

These matters will be discussed below seriatim.

Number, size and location

As the SEZ scheme now stands and the manner in which it is implemented there is a deluge of SEZ proposals. As of now, over 400 have been approved formally or in principle. The abnormality of this can be gauged from the fact that, as of now, there are only 393 SEZs all over the world. There is no cap on the number and it seems that more projects will continue to be added. More than half the number approved are very small in size related to IT, BPO and pharma industries. Many EOUs have also sought conversion as SEZ.

Experts believe that although SEZs appear to represent the correct approach to providing good quality infrastructure in pockets, providing a liberal and supportive business environment and thus giving the much needed push for manufacture and services for export, the government's current approach is not the appropriate way to achieve the intended result.

The smaller SEZ projects are primarily aimed at winning continuance of the tax benefits that are available, under the current dispensation, to software technology parks (STPs) and other EOUs until 2009. The question arises as to why the government cannot simply extend the term of those benefits so as to make them co-terminus with the benefits in SEZs.

Take the case of IT software and services (including BPO). These constitute India's leading export sector (with exports last year amounting to US\$ 23 billions and with a target of \$ 60 billions in 2010). They have benefited from the STPI scheme and are still comfortable with it. That scheme leaves decision making in the hands of the entrepreneur and also encourages decentralization and dispersal of industry. SEZ scheme will reduce their location options. The stipulation of land and constructed area means that small and medium scale enterprises cannot afford to set up their own SEZs. If they do not move to an SEZ, they will have to forego the tax advantages after 2009. If they do move to an SEZ, they will lose much of the tax advantages in the form of exorbitant

rents to be paid to the builder / developer. The SEZ scheme puts small and medium scale enterprises at a comparative disadvantage.

We strongly feel that the appropriate course is to extend for at least 10 years beyond 2009 the term of the tax benefits under the STPI and EOU schemes. That will obviate disruption of the on-going arrangement and undue proliferation of SEZs.

Approving a very large number of SEZs, instead of fewer well-chosen ones, is not a desirable practice. We share the apprehension expressed by various experts that only a few of the SEZs approved are likely to be implemented.

Many developers are just amassing approvals (as they do for mining concessions and as they used to do for letters of intent in the days of license raj) and will wait and watch until they see unmistakable commercial profit in taking up implementation.

We also believe that unless an SEZ has the critical mass it will not have world-class infrastructure needed for the production of exportable goods and services and will be remiss in its external linkages of transport, sewage disposal, electricity transmission, etc.

Real estate exploitation

The broad pattern of incentives to units in the processing area continues to be the same as it was under the April 2000 policy. This is also similar to the incentives given to export oriented units (EOUs) located outside the SEZs as also the IT and ITES (IT enabled services) units. These units, for their imports from abroad or from the domestic trade area are exempt from customs and excise duties, but their exports to the domestic trade area attract the imposition of customs duties. There is also exemption given from income tax and some other central and local taxes. How much this will succeed in attracting investments in units in SEZs remains to be seen.

However, the most striking feature of the present scheme is the incentives available to the developers to develop and exploit the vast areas outside the processing area. For multi-product SEZs such non-processing areas could be as much as 65 percent (even 75 percent with the approval of the Central Government) and for single-product SEZs as much as 50 percent. This is sought to be justified by the argument that

establishing social infrastructure, which would constitute things like housing facilities and entertainment, is critical for attracting and sustaining processing investments in the SEZs. For developing the non-processing area, the developers will be entitled to duty free imports as also exemption from income tax and other taxes. The disposal of real estate assets in the non processing area is not encumbered by any requirement that they be utilized only for the entrepreneurs and workers deployed in the processing area.

It is this component of development which holds the maximum attraction for the SEZ developers. They have, therefore, designed huge SEZ proposals entailing the use of thousands of hectares of land, mostly in the vicinity of large urban areas such as Delhi, Gurgaon and Mumbai. Aided by duty exemptions on their inputs and other tax exemptions as well as cheap acquisition of land from farmers and state governments, they are poised to make huge profits through real estate business. We can clearly see the specter of processing areas not taking off and yet the non-processing areas getting built and exploited to the fulfillment of the commercial objective of the SEZ developers.

The extremely large number of SEZs being approved lends further strength to our apprehension that the SEZ scheme will degenerate into a grand real estate venture, based on short changing the farmers and on tax exemptions. Even going by the most optimistic estimates, demand for land for export-oriented manufacturing and services will not be of such order as to fill the SEZs being approved. The SEZ developers are more certain of finding buyers for the residential, commercial and entertainment components.

This is the distortion that must be eliminated. The SEZs should be solely devoted to processing area and that too primarily for the purpose of export and if any social infrastructure has to be built, it should be only to subserve the processing area, for the provision of housing for workers and other stakeholders, their health care, education etc. As will be elaborated subsequently, if any further infrastructure has to be built in the surrounding areas, in the form of housing, health-care, education, etc., it should be treated as a township scheme which the Government should evolve a separate policy

with suitable obligations and incentives – legal and fiscal.

The committee feels that the minimum area of the processing zone in an SEZ should be raised from the present 35% of the total area of the SEZ to 60%. We just do not see any justification in permitting in any category of SEZs, more than 40 percent of the total area for "non-processing" utilisation.

Under the weight of strong protests from various quarters, the government decided to raise the minimum area of the processing zone in an SEZ from 25% to 35%. This, however, was done only to hoodwink the critics. For in the amendments to the SEZ rules 2006, which came into effect from August 10, the government has retained the powers to relax the limit from 35% to 25% on a case to case basis. Anyone who knows the Congress culture of governance knows that "case to case" relaxation or exemption is a provision for political kickbacks.

Protecting productive land and interests of land owning farmers and other rural workers

The SEZ proposals in the pipeline entail a huge requirement of land. Rightly, therefore, there has been an outcry across the country that adequate safeguards need to be provided in the SEZ policy to ensure that irrigated and agriculturally fertile land is not swallowed up by the SEZs. Some advice on these lines has recently been sent by the Union Ministry of Commerce and Industry to the state governments. However, the advice lacks specificity. There has to be a clear stipulation in the Rules that no fertile land can be included in an SEZ unless it is needed for its continuity and, in any case, its proportion must not exceed 10 percent. It should be prescribed that the SEZ proposals be supported by certification of the agricultural quality of land by the local revenue authority.

A lot of problems emanate from the lack of impact assessment of the project proposals, before they are taken up by the Board of Approvals. Such impact assessment must be made mandatory and the content and the format of the assessment should be clearly laid down. We feel that the impact assessment should focus on conservation of agriculturally productive land, effect on environment (this is particularly important so as to dispel the widely held

apprehension that making use of the overriding provisions of the SEZ Act the environmental requisites will be given a short shrift), balanced urban development as well as the objectives laid down in section 5 of the Special Economic Zones Act 2005, namely, generation of additional economic activity, promotion of exports of goods and services, promotion of investment from domestic and foreign sources, creation of employment opportunities and development of infrastructure facilities. The impact assessment exercises must have the involvement of experts from the relevant fields. Those undertaking the studies should be given the freedom to alter the proposed areas or to suggest alternative locations.

Compensation to farmers and farm workers

We now come to the important issue of remuneration to the farmers who are deprived of their land, which is their only livelihood and incomeearning asset. The BJP firmly believes that considerations of equity for farmers, farm workers and allied rural workers cannot be sacrificed for the benefit of promoters of SEZs and the business operating in them. This issue has to be considered in three parts, the first is of providing to them a fair opportunity price. Secondly, it has to be kept in view that when agricultural land gets transformed into industrial or urban land, it secures a huge value addition. The farmers must partake also in that added value. Thirdly, much land is also being transferred to SEZs from state government and gaon sabhas. The fairness of the price to be charged for such lands has also to be ensured.

For acquisition of land from farmers, two modes are followed. The first is of compulsory acquisition under the Land Acquisition Act, whereby the so called "fair" market price is determined by taking an average of recorded sales and adding 30 percent solatium to it. The other way is to let the SEZ developers purchase land directly from farmers. In either of the modes, the farmer stands at a disadvantage. In the compulsory acquisition mode, he is at a serious disadvantage because the recorded sales rarely disclose the real opportunity price. In the other mode also the farmer is a weaker bargaining party and the SEZ developer is immensely more powerful, given his financial prowess and the easy availability of real estate intermediaries.

We are of the view (and this is of general significance, transcending the subject of SEZs) that the State Governments must prescribe minimum prices for land in various areas, which will be valid both for registration of sales deeds as well as payment of compensation. The prices should be high enough to reflect the opportunity prices of land. Prescription of such minimum prices will not only secure the interest of the farmers to a substantial extent, but will also result in reducing the element of black money in land deals, higher realization of stamp duty and more economical use of land for urban and industrial purposes. The fixation of such minimum prices is within the purview of the state governments and they should be directed to discharge this important duty.

We feel that instead of the state governments using their coercive power of compulsory acquisition the SEZ developers should be required to obtain land from the farmers through direct purchases, but at prices higher than the minimum as suggested above. The farmers should also be assisted in collective bargaining.

The value addition that occurs when agricultural land is transformed into industrial-urban land is also huge, often a substantial multiple of the agricultural price. So that the farmer partakes in the added value, he should be made a stake holder in the transformed land. Some states have prescribed that the farmers are allotted equity shares in the developer companies. The benefit of that, in our view, can be illusory unless some form of annuity can be assured in a pre-specified amount. A more meaningful way will be to prescribe that in the developed land (in the processing area or in the residential / commercial area or in built industrial, residential or commercial accommodation) the farmer will be given a portion (which can be quantified with reference to the quantum of land taken from him). Such provisions are already being operated by many urban development authorities and can be adapted in relation to the SEZs. We feel that a minimum of 15 percent of the area in the processing and the residential/ commercial parts in the non-processing zone should go back to the farmers whose land has been taken.

A lot of land within the SEZ limits belongs to state governments (either originally vested in them as forest or

other land or previously acquired under the Land Acquisition Act for some public purpose, but not utilized for it) or to gaon sabhas or village communities. The transfer of such land must be against a fair opportunity price, which is best determined through a transparent bidding process. To deliver it to SEZ developers either as equity participation by the state industrial development corporation or at the price of compulsory acquisition would be a mere fig leaf for a commercial favour to the developer.

It has also to be ensured that the price obtained for village common lands is duly credited to the gaon sabha accounts and is utilized for the betterment of the village or village clusters.

Acquisition of agricultural land by SEZ developers will, in addition to the owner farmers, also displace the employment of actual tillers, farm workers and allied rural workers. Justice should be done to them through suitable compensation. In some states, a part of the acquisition amount goes to the share croppers. This is possible because land records are so maintained in these states that the share croppers are duly recorded. That, however, is not the case in most other states.

It is important, therefore, that, in addition to suitable financial compensation, the displaced farm labour and allied workers are given preference in employment either by the SEZ developer or in the business units in the SEZ. Every SEZ developer must be required to set up a training institution on a BOT basis, where appropriate training facilities for farm workers and other allied workers displaced from their traditional employment may be established. There should be a provision for their subsequent absorption in employment in the SEZ establishment and in the processing units. They should get a preferential treatment.

Each SEZ proposal must include a plan for rehabilitation of the workers who would be displaced from their traditional employment. A proper implementation of that plan should be a specific condition attached to the approval of the SEZ and the Development Commissioner of the SEZ should be enjoined to oversee the implementation of the rehabilitation plan.

Village abadis within SEZs

Unless special measures are taken to absorb the village abadis in the urban industrial environment of the SEZ the danger is that they will stay as segregated ghettos and will fester as locations of social distinction and conflicts. Every SEZ developer must be required to prepare a redevelopment plan for the village abadis falling within the SEZ limits and to execute that plan at his cost. The maintenance of the redeveloped abadis should be a part and parcel of the civic arrangements for the SEZ area in general.

Tax incentives and impact on revenues

It is unfortunate that the Central Government has not given out a credible assessment of the impact of tax concessions and exemptions on government revenues. The Ministry of Finance has estimated the loss of revenue to be of the order of Rs.97,000 crores until 2010, about Rs.50,000 crores of which will be due to loss of direct taxes and the rest as loss of custom and excise duties and other central taxes. There is no mention of the revenue loss that the state governments will suffer. On the other hand, the Ministry of Commerce and Industry has contended that due to increased economic activity the accrual of revenue will in fact go up by about Rs.50,000 crores. Due to lack of an agreed assessment the public is precluded from making an objective evaluation of the costs and benefits of the SEZ scheme.

All supplies of goods and services received by the developer or a unit in an SEZ, either from abroad or from the DTA, are exempt from customs and excise duties and from such taxes as the central sales tax, service tax and stamp duty (as is leviable by the Central Government). For the sales made from SEZ units to the DTA, custom duty has to be paid. In addition, SEZ developers and units in SEZs enjoy exemption from income tax and dividend distribution tax. The Central Government also requires the state governments that for sales to and from SEZ exemption of VAT / sales tax has to be granted. The state governments have granted partial or full exemption of the stamp duty leviable by them.

As has been stated above, insofar as the processing units are concerned the tax exemptions are similar to those available under the 2000 scheme or to the EOUs. It is a moot question

whether the package of tax exemptions will attract sizeable additional investments in processing units in SEZ over and above the investments that would have occurred in the normal course. Of course, availability of infrastructure and serviced land will be an attraction for the investors. That would be the case also in any industrial estate or an appropriately developed area, which is not a SEZ. The package of tax concessions, we feel, each entrepreneur will examine in his specific context and he will decide to make investments in a processing unit in a SEZ only if he sees a definite benefit in doing so.

We must, however, point out that while the incentives now given to processing units in SEZs are similar to those available in the erstwhile export processing zones or to EOUs, the tax incentives given to SEZ developers are unprecedented. This imbalance reinforces the apprehension that we have earlier expressed that whether the processing areas succeed or not, the real estate business in the non-processing areas, boosted by the unprecedented incentive package and particularly if it is near an urban conglomerate is more likely to be commercially successful.

We do not see any legitimacy for tax incentives for the non-processing area except in so far as it is used directly to support the units in the processing area in the form housing for entrepreneurs and employees and to serve their health care, educational and community needs. Giving tax incentives for creation and operation of hotels, restaurants, shopping malls and places of entertainment, all of which will be open to use by people not directly deployed in the processing area, will constitute an unjustifiable use of the exchequer, designed primarily to enhance the commercial profits of the SEZ developer. The discrimination so created vis-à-vis the businesses and the entities located outside the SEZ will be unjust and will be difficult to sustain even in courts of law.

A related issue concerns the facilities whose products will spill out for use by people and businesses located outside SEZs, for instance a power plant or an airstrip. The incentives held out for them include tax exemptions for capital inputs as well as consumables -- even the tax on the power generated. There is no justification in not recovering from the owners of

such facilities the tax exemptions that relate to the supplies provided by them outside of the SEZ.

The other observation that we have to make is that the incentive package offered for processing units in SEZs is likely to become the bench mark for policies of industrial promotion in the country. Sooner than later, there will be clamour from units located outside SEZs to be given the same dispensation as is being provided to the units in SEZs. This demand will be difficult to resist because, given the diluted export obligation by the SEZ units (in SEZs a unit has only to be foreign exchange positive in the sense that its exports have to exceed imports while an EOU is required to export most of its output), they are hardly distinguishable from the other industrial units operating across the country. We see the danger of emergence of a pattern of industrial development supported and sustained by subventions from the taxpayer.

Non-level playing field for business in DTA

The only export related requirement prescribed for units in an SEZ is that they have to be foreign exchange positive in the sense that their sales in foreign currency have to exceed their purchases in foreign currency and that too in an aggregate of 5 years. Given that weak requirement the units will make substantial sales in DTA and in so doing will be assisted by the support of, hopefully, a superior infrastructure and cheaper and both assured supply of power. That is why it is apprehended that units in DTA will lose the level playing field and will be at a comparative disadvantage. We realise the difficulties in segregating the production meant for export and that available for home consumption. But we cannot understand why the export requirement of units in SEZs cannot be maintained at the level of that of the units in the erstwhile EPZs or of EOUs. That can help restore the export objective of SEZs and go some way in allaying the apprehension of entrepreneurs in DTA.

Interface between SEZs and DTA

The trade interface between SEZs and the DTA is going to be large and complex because, firstly, trade permitted between the two is virtually limitless and secondly, because the interchange of goods and services will be at several stages starting from raw materials, through various intermediate

product stages and extending right up to the finished products. Their proper accounting will be essential for determination of tax benefits and liabilities. We do not see in the Rules a foolproof framework for such accounting. We see a vast scope for "transfer pricing" and other malpractices for the purpose of tax evasion and reaping of undeserved tax benefits.

SEZs and development of new townships

A major lacuna in the UPA Government's SEZ policy is that the development of housing and other social infrastructure requirements in the non-processing area is sought to be given the same fiscal incentives as the business units in the processing area. The BJP is firmly in favour of development of well planned and aesthetically appealing habitats, with modern amenities, for various sections of employees and stake-holders in SEZs. The current pattern of unplanned and chaotic and often illegal construction of housing and non-housing structures within and around modern business clusters has become a bane of urban development in India. Our country must eschew this pattern, and SEZs provide an opportunity to do so. Nevertheless, the Committee feels that the Union Government, in collaboration with State Governments, should evolve a New Township Development Policy with suitable rules and incentives (fiscal and non-fiscal) that attract investments and right kind of developers as has been argued elsewhere in this report, the incentives should be stronger at the proposed township is farther from existing Metros and big cities. In order to prevent the growth of slums, there should be adequate provision of housing, affordable means of mass transport, and access to basic social infrastructure amenities for people in the low income category.

The need for a policy on New Township Development is supported by another important factor. In the Indian conditions, unlike in China (which has only 6 mega size SEZs), the variable size of SEZs makes it almost impossible to design the SEZs as self-contained entities in terms of the use of residential units, commercial space and attendant social infrastructure amenities, such as hospitals and educational institutions. Besides, problems associated with the commercial viability and administrative ease of doing so, any such attempt would render SEZs vulnerable to the criticism that the

Government is allowing establishment of "foreign zones" within the country. In other words, there should be flexibility in the use of new townships for the benefit of the people and businesses working both within the processing zones of SEZs and without.

Reasonable balance

The apprehensions that the SEZ policy may induce further imbalances in the regional distribution of industrial activity emanates from several reasons. The number of SEZ proposals and the number of those approved vary greatly across states. It is observed that the numbers are far greater in the states that are already industrially more advanced. That is natural because those states have a greater capability to put together SEZ proposals and are managerially more competent to implement them. Such a differential trend can only be arrested, if some definite measures are taken to help the industrially backward states to generate and implement SEZ projects. So far such an effort on the part of the Central Government has been totally lacking.

Secondly, the SEZ projects tend to be located in the vicinity of large urban areas, obviously with an eye on the availability of qualified work force nearby and with a view to exploiting the real estate potential of the non-processing area within the SEZ. This approach of expediency needs to be firmly discouraged. There is no legitimate justification for it because for housing the work force needed for the SEZ more than adequate provision has been made by way of the non-processing area.

The state governments, while recommending SEZ proposals and the Board of Approvals while approving them must ensure that the SEZs are located not in the vicinity of larger urban areas and thereby further expanding their sprawl. The SEZs should be close to the smaller towns which have the potential for expansion and have the nucleus of trained manpower which can be gradually expanded by educational and training effort. In fact, the package of incentives for SEZs can be graded stronger if the SEZ is located close to a small town and weaker if it is close to a large urban area. In the scheme now being pursued we find total lack of such a perspective.

Thirdly, it is apprehended that new manufacturing units will tend to be located in the SEZs, because of the tax benefits and the better infrastructure they would provide, and the areas outside SEZ, will get to host fewer units. In fact, the fear is that even the existing units outside SEZs may consider relocating into SEZs, provided the costs of relocation are outweighed by the benefits available in the SEZs.

The provisions in the SEZ scheme to combat such a trend are somewhat contradictory.

On the one hand, checks are being provided against such relocations. On the other hand, even some incentives are being provided for relocation, such as exemption of capital gain tax on the disposal of industrial assets outside the SEZs, when such disposal is a precursor to relocation into an SEZ. This is a matter in which clarity of purpose has to be ensured.

SEZs and the IT Sector

As has been stated above, emergence of a large number of single product SEZs, particularly those for IT and ITES, is due to the fact that many of the EOUs and IT and ITES units are considering relocation simply to get a fresh lease of life for their tax concessions which, outside the SEZs, are due to conclude by 2009-10. Those concessions, as we have suggested above, should be extended for a further period of 10 years. The decision should be taken forthwith.

The prevalence of the uncertainty on this issue, as it obtains now is tragic and may become the reason for unnecessary and avoidable relocation decisions.

The Government should take a clear view right at this stage so that the future scenario is known to everybody.

Administrative weakness

Provisions have been made for single window approvals, composite application forms and unified returns and the Development Commissioner and the Approval Committee have been vested with powers under numerous laws with the objectives of minimizing the hassles of the SEZ developers as well as entrepreneurs. However, the fact remains that all activities concerning development of SEZs and setting up and operating units in them are tightly controlled at each stage. If in response to the market dynamics, any modifications are required, those also would require approvals. The procedures

prescribed in the Act and Rules remind us of the bad old days of licence raj.

We see overlap in the roles of the Development Commissioner and the private sector SEZ developer and can visualise turf disputes arising between them. The authority of the Development Commissioner to secure compliance of the Rules and his directions appears weak. In a face-off, the private sector developer is likely to be stronger. Even the supreme step of take over of management will be difficult to implement because ownership of the entire SEZ land vests in the developer. Disposal of failed projects will be extremely difficult and there will be the risk of the developer running away with the land that he has already amassed.

There should be an independent regulatory authority to deal with issues related to SEZs.

Conclusion

The committee feels disappointed that the device of SEZ introduced by the NDA Government with the objective of promoting manufacture for export and FDI has been so much distorted and degraded by the UPA Government that, instead of achieving its avowed objectives, it is raising tensions and apprehensions among various segments of our system. It has degenerated into a scramble for amassing real estate and for profiteering from it by shortchanging the farmer and using subventions from the taxpayer. A large section of our entrepreneurship, particularly that in the medium and small scale sector and in our leading export sector of IT and BPO feels left out and aggrieved farmers and village workers, who will be displaced by SEZs, are victims of apathy and insensitivity.

The Bharatiya Janata Party would like to take up these issues for debate in the Parliament and outside and bring pressure on the Government to reverse the distortions.

SUMMARY OF RECOMMENDATIONS

1. The committee feels that the minimum area of the processing zone in an SEZ should be raised from the present 35% of the total area of the SEZ to 60%.
We just do not see any justification in permitting in any category of SEZs, more than 40 percent of the total area for "non-processing" utilisation.
2. No fertile and irrigated agricultural land should be acquired by the Governments for SEZs.
3. Considerations of equity for farmers, farm workers and allied rural workers cannot be sacrificed for the benefit of promoters of SEZs and the businesses operating in them.
4. State Governments must prescribe minimum prices for land in various areas, which should be high enough to reflect the opportunity prices of land. Instead of the state governments using their coercive power of compulsory acquisition, SEZ developers should be required to obtain land from the farmers through direct purchases, but at prices higher than the minimum as suggested above.
5. In order that farmers get to benefit from substantial value-appreciation of their land after it has been developed, a minimum of 15 percent of the area in the processing and the residential / commercial parts in the nonprocessing zone should go back to the farmers on a pro-rata basis.
6. Where feasible, farmers should be allotted equity shares in the developer companies.
7. In addition to suitable financial compensation, the displaced farm labour and allied eligible workers should be given preference in employment either by the SEZ developer or in the business units in the SEZ. For this, every SEZ developer must be required to set up a training institution.
8. Each SEZ proposal must include a plan for rehabilitation of the people who would be displaced from their traditional employment and livelihoods. The Development Commissioner of the SEZ should be enjoined to oversee the implementation of the rehabilitation plan.

9. Every SEZ developer must be required to prepare a redevelopment plan for the village abadis falling within the SEZ limits and to execute that plan at his cost.
10. Tax incentives for business units in the processing zone of an SEZ should not be made available in the non-processing zone.
11. There should be level playing field for the Domestic Trade Areas (DTAs).
Business in the DTAs should not be put to a disadvantage because of the incentives available to those in SEZs. There should be no scope for abuse of benefits available in SEZs for sale of goods and services in DTA.
12. There should be special incentives for SEZs that are established closer to small towns.
13. The tax exemptions currently available to IT and ITES units upto 2009 should be extended for a further period of 10 years. This decision must be announced immediately, so that uncertainty on this issue, which has led many IT companies to consider relocation to SEZs, is put to an end.
14. The Union government, in collaboration with state governments, should evolve a New Township Development Policy with suitable rules. Stronger incentives (fiscal and non-fiscal) should be provided for new townships located away from existing metros and big cities. There should be adequate provision of housing, affordable means of mass transport, and access to basic social infrastructure amenities for people in the low-income category.
15. There should be independent regulatory authority to deal with the issues related to the SEZs.
16. There should be clear guidelines to protect workers' rights and promote their welfare and also guidelines for environmental protection.
