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Special Economic Zones and Industrial Parks in South Asia: An Assessment of Their Regulatory Structures

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Abstract

This paper reviews the policies and regulations for special economic zones and other spatial development modalities in the countries within proximity of the Eastern Corridor in South Asia, and it assesses whether those policies and regulations are effectively designed. The assessment finds mixed results. On the positive side, governments in these countries exhibit a strong political commitment to the zones' success, providing them with dedicated policies of both fiscal incentives and regulatory concessions, combined with administrative simplification to help zone developers and tenant enterprises. However, these arrangements include some notable shortfalls. For example, some incentives are inconsistent with the zone objectives, violate some international regulations, or miss necessary business facilitation measures. Moreover, there is no mechanism to evaluate the effectiveness and cost-efficiency of different incentives. Zone tenancy requirements are not always well specified, feasible, or consistent with zone objectives. As for the regulatory and institutional structures of zone programs, there are some common shortfalls, especially in terms of (a) clarity of zone objectives, (b) the roles of different agents, (c) the autonomy and inclusivity of those agents, and (d) the agents' authority to carry out their responsibilities, and there are some shortfalls in the resources that agents need to manage operations effectively. To maximize the benefits from these zones, governments of the region could adopt reforms to ensure that incentives and tenancy requirements are aligned with zone objectives and that regulatory frameworks are clear, fair, and effective.

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Introduction

This paper reviews the policies and regulations for special economic zones (SEZs) and other spatial development modalities in the countries within proximity of the Eastern Corridor in South Asia, and it assesses whether those policies and regulations are effectively designed.[1] It is part of an ongoing program at the World Bank that looks at the determinants of performance of SEZs in four countries in the South Asia region (SAR). The scope of analysis in this paper spans federal policies and regulations governing zones across Bangladesh, Bhutan, India, and Nepal (BBIN), as well as a number of Indian states. The paper is operationally focused and strives to support policy makers in the region in their efforts to enhance their effective implementation of spatial development policies in the BBIN region. There is no consensus on a definition for special economic zones, and no attempt is made here to resolve this debate. Instead, SEZs are taken as those special arrangements that display any of the structural features identified by Farole (2011): a *regulatory regime* distinct from that of the rest of the country; *a dedicated governance structure* charged with management of the zone regime; and a physical infrastructure composed of industrial or mixed-use activity parks that supports the activities of economic agents in them.

Zones have proliferated in the BBIN region, and this trend is poised to continue. Starting with a single export processing zone (EPZ) in Gujarat in 1965, India has developed more than 3,350 zones, according to the Ministry of Commerce and Industry. The government of Bangladesh has announced plans to establish 100 SEZs by 2025, and the government of Bhutan has said that it will establish several industrial parks. Nepal currently has 10 operational industrial districts, but the passage of new SEZ legislation in 2016 signals more to come.

The expansion of SEZs reflects the belief that they can play an important developmental role. This connection is evident in the objectives stated in the SEZ acts themselves, which identify such goals as (a) attracting foreign direct investment (FDI), (b) increasing exports, (c) enhancing productivity, (d) spurring industrialization, (e) expanding employment, and (f) supporting spatial development, among others. The economic rationale for economic zones rests mainly on two arguments. The first argument is that they can enhance productivity by providing returns to scale from the availability of shared infrastructure and through agglomeration effects such as knowledge spillovers. The second argument—a “second-best” argument—reflects situations in which the growth of industries is hindered by institutional limitations and other market failures that cannot be readily corrected at the national level because of fiscal or political constraints but can be overcome within specific geographical areas (Duranton and Venables 2018).

1 Throughout this paper, the terms special economic zone and zone are used as generic umbrella terms to cover all zone types. When referring to a specific zone type, such as an industrial district or EPZ, we refer to them by that particular term.

Success of zone programs requires that the programs meet multiple conditions covering geography, the business environment, and policy design. This requirement results in a weakest-link problem, in which programs can fail if they are missing key elements of the package. Although there is no single blueprint to guarantee the success of zones, international experience points to a set of good practices. Broadly speaking, the determinants of zone performance have to do with *zone characteristics*, which relate to factors such as the size, industrial focus, and location of the zone; *contextual characteristics*, which are factors that are exogenous to the zone itself, such as the institutional setup in the country; and *program characteristics*, which refer to the rules governing the development, operation, and regulation of zones. The focus of this paper is on program characteristics.

The assessment of the policy and regulatory frameworks in Bangladesh, Bhutan, India, and Nepal points to mixed results. On the positive side, governments in these countries exhibit a strong political commitment to the success of these zones, providing them with dedicated policies of both fiscal incentives and regulatory concessions, combined with administrative simplification to help zone developers and tenant enterprises. However, these arrangements include some notable shortfalls. For example, some incentives are inconsistent with the zone objectives, violate some international regulations, or miss necessary business facilitation measures. Moreover, there is no mechanism to evaluate the effectiveness and cost-efficiency of different incentives. Zone tenancy requirements are not always well specified, feasible, or consistent with zone objectives. As for the regulatory and institutional structures of zone programs, there are some common shortfalls, especially in terms of (a) clarity of zone objectives, (b) the roles of different agents, (c) the autonomy and inclusivity of those agents, and (d) their authority to carry out their responsibilities, and there are some shortfalls in the resources that agents need to manage their operations effectively.

To maximize the benefits from these zones, governments of the region could adopt reforms to ensure that incentives and tenancy requirements are aligned with zone objectives and that regulatory frameworks are clear, fair, and effective. To this end, the most significant steps include the introduction of a rigorous monitoring and evaluation system to keep incentives and requirements that are most effective and to rework or eliminate those that are not. Ensuring clarity of zone rules and responsibilities and coordination among relevant actors is also essential, especially when multiple agencies at both state and federal levels are involved. Increasing the role of the private sector in the development and operation of zones is necessary to encourage further investment and raise productivity. Ensuring that the regulators are independent and have the capacity to fulfill their responsibilities is another area that deserves consideration. In addition to bringing zones closer to achieving their objectives, the combined effect of these reforms would reduce mission creep and help avoid white elephants and politically motivated zones.

The rest of the paper is organized as follows. First, it provides an overview of the evolution of zone programs across the BBIN region. Next, it presents a framework for evaluating zone program design. After that, it discusses the incentives, requirements, and regulatory structures of zone programs in the BBIN region. Last, it offers policy recommendations.

The Proliferation and Diversity of Economic Zones in South Asia

Economic zones are everywhere in South Asia, but some countries have a longer history with them than others (see figure 1). This section provides an overview of the evolution of economic zones across India, Bangladesh, Bhutan, and Nepal (see summary highlights in figure 2).

In 1965, India became the first country in the region to set up an EPZ to promote exports from spatially confined areas that had a liberalized policy environment in the midst of a more closed economy. Firms operating in EPZs received fiscal incentives such as tax exemptions and subsidized credit from federal and state financial agencies. Initially, there was no formal EPZ policy, and the main driving force was earning foreign currency. EPZs were managed primarily by the Foreign Trade Policy of the Ministry of Commerce and Industry, which set overall policies in five-year cycles, complemented by evolving instructions by other ministries and government agencies. The authority over economic zones fell foremost under the commerce secretary, but the establishment of units was decided by a board of approval, an interministerial body, while the actual management of zones was carried out by a development commissioner (DC).

Over time, the landscape of economic zones became more diverse. In 1981, the government of India initiated the Export Oriented Units (EOU) scheme, which provided tax exemptions to enterprises that exported a minimum threshold of output. Amendments to the Foreign Trade Policy in 1994 allowed EPZs to be set up by state governments, autonomous agencies, and the private sector. These arrangements were further amended in 2000, expanding the economic and social mandates of EPZs and allowing the provision of infrastructure and services to the zones beyond regulatory incentives. The SEZ Act of 2005 expanded the objectives of the zones to include industrialization and development more broadly. Individual states have followed suit and adopted SEZ acts and policies.

Bangladesh too has a long history with various types of economic zones. The Bangladesh Small and Cottage Industries Corporation (BSCIC) was established in 1957 as a statutory body operating under the Ministry of Industries. As part of its establishment act, BSCIC was to “maintain common facility centres to afford common facilities to small industries” and “prepare schemes to set up . . . industrial units in fields of high priority.”[2] This program remains in operation today, overseeing as many as 74 operational industrial estates in 2018. Firms within the estates benefit from plot allocations at subsidized rates, initial tax exemptions, infrastructure facilities, and other forms of support.

2 Bangladesh Small and Cottage Industries Corporate Act, chapter 24, §2e–f (1957).

In Bangladesh, attention also shifted toward export promotion, and the government—which was under military rule at the time—passed the Bangladesh Export Processing Zones Authority Act of 1980. The act led to the establishment of the semiautonomous Bangladesh Export Processing Zones Authority (BEPZA). Under the successive chairmanship of military officers as a legacy to its roots, BEPZA owns and operates EPZs and leases serviced land to industrial tenants in eight export-processing zones. Investors receive a range of fiscal incentives such as tax exemptions, customs-free imports, and exemptions on dividends. The act also provided nonfiscal incentives, such as allowing full foreign ownership and full repatriation of capital and dividends, and a host of services aimed at helping investors navigate the sluggish business environment (World Bank 2018).

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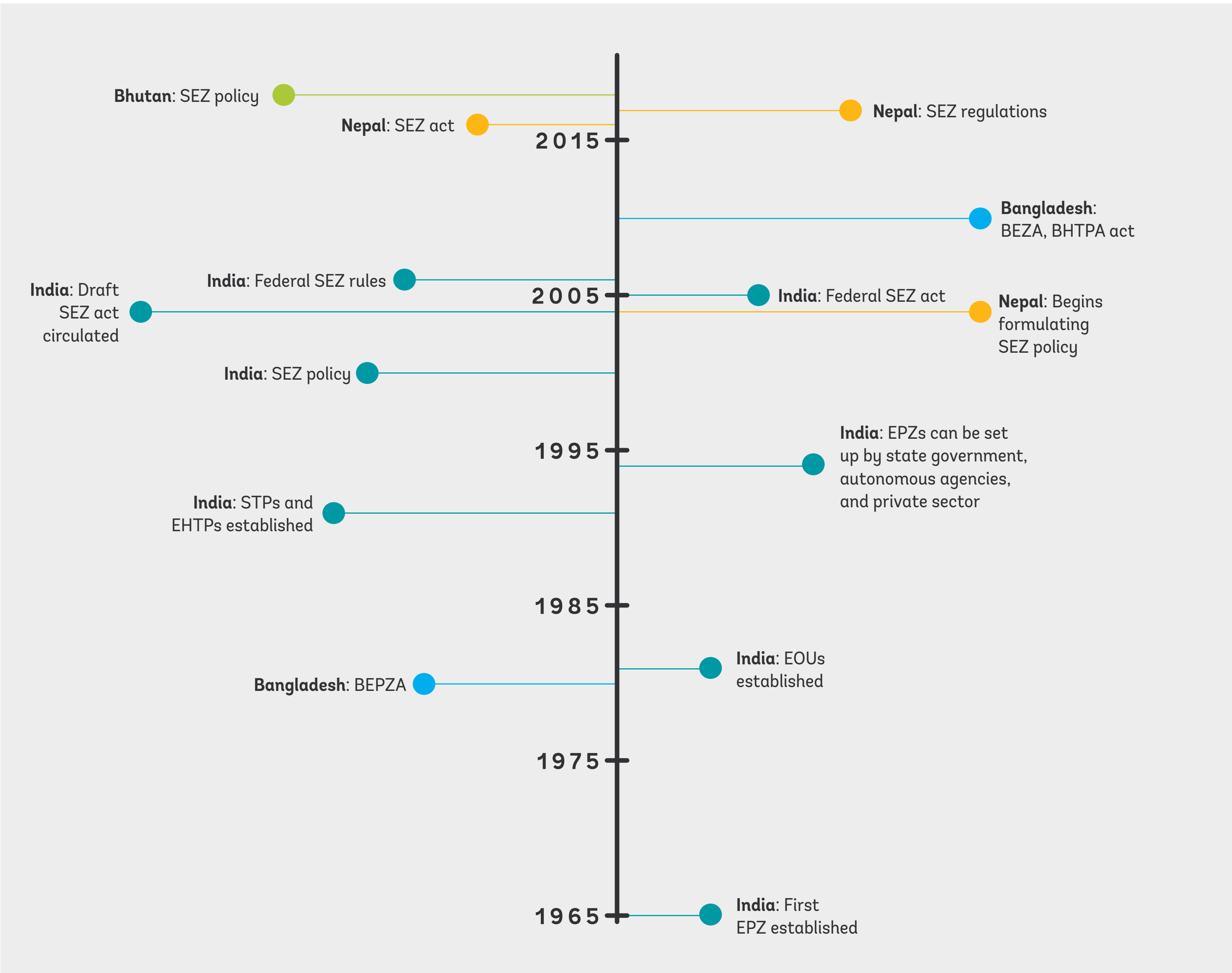
FIGURE 1. - Timeline of select federal economic zone policy milestones



Source: World Bank Staff.

Note: BEPZA = Bangladesh Export Processing Zones Authority; BEZA = Bangladesh Economic Zones Authority; BHTPA = Bangladesh Hi-Tech Park Authority; EPZ = export processing zone; EHTP = Electronics hardware technology park; EOU = Export Oriented Unit; EPZ = export processing zone; SEZ = special economic zone; STP = Software technology park.

The most recent shift in Bangladesh came with the passage of the Bangladesh Economic Zones Authority (BEZA) Act and the Bangladesh Hi-Tech Park Authority (BHTPA) Act in 2010. Under these new acts, the addition of new zones under BEPZA was disallowed as the objective of zone policy moved beyond export promotion to play a greater role in the national industrialization agenda producing goods for both domestic and foreign markets. Unlike EPZs that are publicly owned and operated by BEPZA, BEZA and BHTPA were intended to rely primarily on private capital and expertise to build and operate new zones. The government of Bangladesh announced plans to establish 100 economic zones (EZs) by 2025, to increase export earnings by US$40 billion, and to create 10 million jobs by 2025. As of October 2018, the government had approved 89 EZs—56 public and 23 private—of which 10 were inaugurated (WTO 2019; World Bank 2018). Although BEZA may prove to be short of inaugurating all planned EZs by the target date, it has amassed the largest public land bank in the country, allocated land to domestic and foreign investors, and received investment proposals worth nearly US$20 billion by 2020. It has established partnerships with foreign governments as well as international conglomerates such as the one with Sumitomo Corporation and the China Harbor Engineering Company. The other EPZ, BHTPA, was established to support the strategy of the government of Bangladesh to reach US$5 billion in ICT exports by 2021. It issues licenses to high-tech parks that support both manufacturing and services companies. The BHTPA offers training programs and incentives for technical quality certification and is aimed at supporting an entrepreneurial tech ecosystem.

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FIGURE 2. - Summary highlights of zone programs across the BBIN region

India:
- Initiated spatial development programs with EPZs in 1965
- Currently maintains federal and multiple state-level SEZ Acts and other zone programs
- Different zones types

Bangladesh:
- Established BSCIC in 1957
- Passed the BEZA and BHTPA acts in 2010
- Ambitious zone expansion plans

Nepal:
- Maintains 10 industrial districts, some started in the 1960s
- SEZ Act finalized in 2016
- Plans for expansion

Bhutan:
- Nascent zones program, with two currently in operation

Source: World Bank staff.

Note: BBIN = Bangladesh, Bhutan, India, and Nepal; BEZA = Bangladesh Economic Zones Authority; BHTPA = Bangladesh Hi-Tech Park Authority; BSCIC = Bangladesh Small and Cottage Industries Corporation; EPZ = export processing zone; SEZ = special economic zone.

The government of Nepal also has a long history with industrial districts. As of January 2020, Nepal had 10 industrial districts in operation across the country. Some of these, like the Balaju, Hetauda, and Patan industrial districts, have been in operation since the 1960s. These districts are tasked with providing the industrial sector with access to land and infrastructure to support development in lagging regions. Industrial Districts Management Limited (IDM), which began operation in 1988, manages industrial districts.

Nepal also more recently adopted a formal SEZ policy framework and has one operational SEZ. Having begun the process of formulating a SEZ policy in 2004 under the Ministry of Industry, Commerce and Supplies, the government institutionalized SEZs by establishing the SEZ Formation Order (2012) and forming an SEZ Development Committee to conduct feasibility studies for SEZs across the country. Parliament passed the Special Economic Zones Act of 2016 (Act No. 9 of the Year 2073), followed by the Special Economic Zones Regulations of 2017 to make the act fully operational and later the Special Economic Zone Act (First Amendment) 2075 Bill in 2019. Although the government has plans to establish several SEZs across the country, only the Bhairahawa SEZ is operational, and it remains largely vacant.

In contrast, Bhutan's engagement with economic zones is at a nascent stage. To boost industry and export competitiveness, the government of Bhutan is constructing four industrial parks set to be completed in 2021: Jigmeling Industrial Park in Sarpang, Dhamdum Industrial Park in Samtse, Motanga Industrial Park in Samdrupjongkhar, and Bondeyma Industrial Park in Mongar. The parks are intended to support a range of development objectives, such as spurring industrialization, increasing exports, expanding employment, and attracting FDI. These new parks will complement two existing industrial estates: Pasakha Industrial Estate near Phuentsholing in the south and Bjemina on the outskirts of Thimphu.

A common trend across these countries is that economic zones have evolved from a focus on enhancing exports and attracting FDI to broader developmental mandates. The objectives of federal and state SEZ acts and policies across South Asia are presented in tables 1 and 2, respectively.

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TABLE 1. - Objectives of economic zone acts and policies across South Asia

Country	Act or Policy	Objective
Bangladesh	The Economic Zones Act, 2010; Act No. 42 of 2010, preamble	"An act to make provisions for the establishment of economic zones in all potential areas including backward and underdeveloped regions and development, operation, management and control thereof including the matters ancillary thereto with a view to encouraging rapid economic development through increase and diversification of industry, employment, production and export."
	The Bangladesh Hi-Tech Park Authority Act, 2010; Act No. 8 of 2010, preamble	"An act to make provisions for the establishment of hi-tech parks in different places within the country for setting up and development of hi-tech industries in Bangladesh and for the establishment of the Bangladesh Hi-Tech Park Authority for proper management, creation and development thereof."
	The Bangladesh Export Processing Zones Authority Act, 1980; Act No. XXXVI of 1980, §3, 4A	"The objects of the Authority shall be: (a) To foster and generate economic development of Bangladesh by encouraging and promoting foreign investments in a Zone; (b) to diversify the sources of foreign exchange earnings by increasing export of Bangladesh through a Zone; (c) to encourage and foster the establishment and development of industries and commercial enterprises in a zone in order to widen and strengthen the economic base of Bangladesh; (d) to generate productive employment opportunity and to upgrade labour and management skills through acquisition of advanced technology."
Bhutan	The Industrial Infrastructure Development Division under the Department of Industry, Ministry of Economic Affairs, 2018; 20/ MoEA/DoI/IIDD/2017-18/1147, Annexure I	". . . to promote balanced regional development and enhance growth of country's economy. The industrial parks are developed to have clustering industries to promote private sector development and enhance socio-economic activity."
India	The Special Economic Zones Act, 2005; No. 28 of 2005, § 5(1).	"(a) generation of additional economic activity; (b) promotion of exports of goods and services; (c) promotion of investment from domestic and foreign sources; (d) creation of employment opportunities; (e) development of infrastructure facilities; and (f) maintenance of sovereignty and integrity of India, the security of the State and friendly relations with foreign States."
Nepal	Special Economic Zone Act, 2073, 2016; Act No. 9 of the Year 2073, preamble	"Whereas it is expedient to proceed with the industrialization process in the country through export promotion and to provide impetus to economic development through the provision of establishment, operation and management of Special Economic Zone"

Source: World Bank staff.

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TABLE 2. - State-level SEZ Act and policy objectives in India

Country	Act or Policy	Objective
Maharashtra	State government's policy regarding setting up of SEZs, 2001	"The SEZ scheme seeks to create a simple and transparent system and procedures for enhancing productivity and the ease of doing business in Maharashtra. . . . Exploiting the full potential of the concept of SEZs would bring large dividends to Maharashtra in terms of economic and industrial development and the generation of new employment opportunities."
Jharkhand	Department of Industries, Notification no. 2460, Ranchi, 02.08.2003 (Policy)	"Jharkhand Government intends to exploit the SEZ concept for impacting the State's socioeconomic fabric through enhanced job opportunities and industrial development."
Madhya Pradesh	The Indore Special Economic Zone (Special Provisions) Act, 2003; Statement of object and reasons	"The proposed legislation will attract investors by facilitating the development of world class infrastructure for making the products competitive in the international market and will also facilitate investments and creation of opportunities for employment for the people of the State"
Kerala	Policy regarding setting up of Special Economic Zones in the State, 2003, preamble	"The effort has been to create delineated duty-free enclaves with world-class infrastructure and fast track clearances to attract investments, including FDI, for servicing the global market."
West Bengal	The West Bengal Special Economic Zone Act, 2003, preamble	". . . to accelerate economic reforms and to promote the rapid and orderly growth, development and operation of industries in such Special Economic Zone"
Gujarat	Gujarat Act No.11 of 2004; Statement	"In order to achieve rapid economic growth to attract investment and to ensure systematic and integrated development of the industry in the State, it is considered necessary to enact a law for the establishment of the Special Economic Zone in the State."
Tamil Nadu	Act No. 18 of 2005, §3	"(a) generation of additional economic activity; (b) promotion of exports of goods and services; (c) promotion of investment from domestic and foreign services; (d) creation of employment opportunities; (e) development of infrastructure facilities; and (f) maintenance of sovereignty and integrity of India, the security of State and friendly relations with foreign State."
Chandigarh	Chandigarh Administration; No. 27/IT/2005/2122	"Whereas it is considered necessary and expedient to promote the Industry in general, including the Knowledge Industry comprising IT, IT Enabled Service and Business Process Outsourcing (BPO) Companies in Chandigarh to generate employment, increase exports and boost the economy."
Haryana	The Haryana Special Economic Zones Act, 2005 (Haryana) Act No. 9 of 2006), preamble	". . . to accelerate and facilitate both public and private sector participation in an internationally competitive and hassle free environment for export promotion thereby securing large dividends in terms of economic and industrial development and to act as strong catalytic of regional development in the State."
Uttar Pradesh	Uttar Pradesh SEZ Policy, 2007, preamble	". . . in order to foster the industrial and economic development"
Punjab	The Punjab Special Economic Zones Act, 2009 (Punjab Act No.17 of 2009), preamble	". . . to accelerate and facilitate both public and private sector participation in an internationally competitive and hassle free environment for export promotion thereby securing large dividends in terms of economic and industrial development and to act as strong catalytic of regional development and for the matters connected therewith or incidental thereto."
Karnataka	State Policy for Special Economic Zones – 2009, preamble	"They [SEZs] are expected to promote establishment of large, self contained areas supported by world–class infrastructure oriented towards export production. Exploiting the full potential of the concept of SEZs would bring large dividends to the State in terms of economic and industrial development and the generation of new employment opportunities. The SEZs are expected to be engines of new economic growth."

Source: World Bank staff.
Note: IT = information technology; SEZ = special economic zone.

Because of the SEZs' long history and expansion to accommodate new objectives, their diversity has increased over time, both in their sectoral focus and their formal classification. In India, approximately half of economic zones span multiple industrial activities (figure 3). The largest of those with sectoral focuses are in engineering, textiles, and food processing. Economic zones are also classified under many different categories, according to the Ministry of Commerce and Industry. These include SEZs and industrial regions, parks, estates, clusters, areas, and more, although these different labels do not imply that each is governed by a different regulatory regime (figure 4). Different names and types of zones may indeed reflect actual differences in their form or function, but differences also owe to varying terminology across countries, different translations from other languages, attempts by zone promoters to differentiate their product from those of competitors, or a desire on the part of successive governments to distinguish their industrial policies from previous ones.

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FIGURE 3. - Economic zones by industry, India

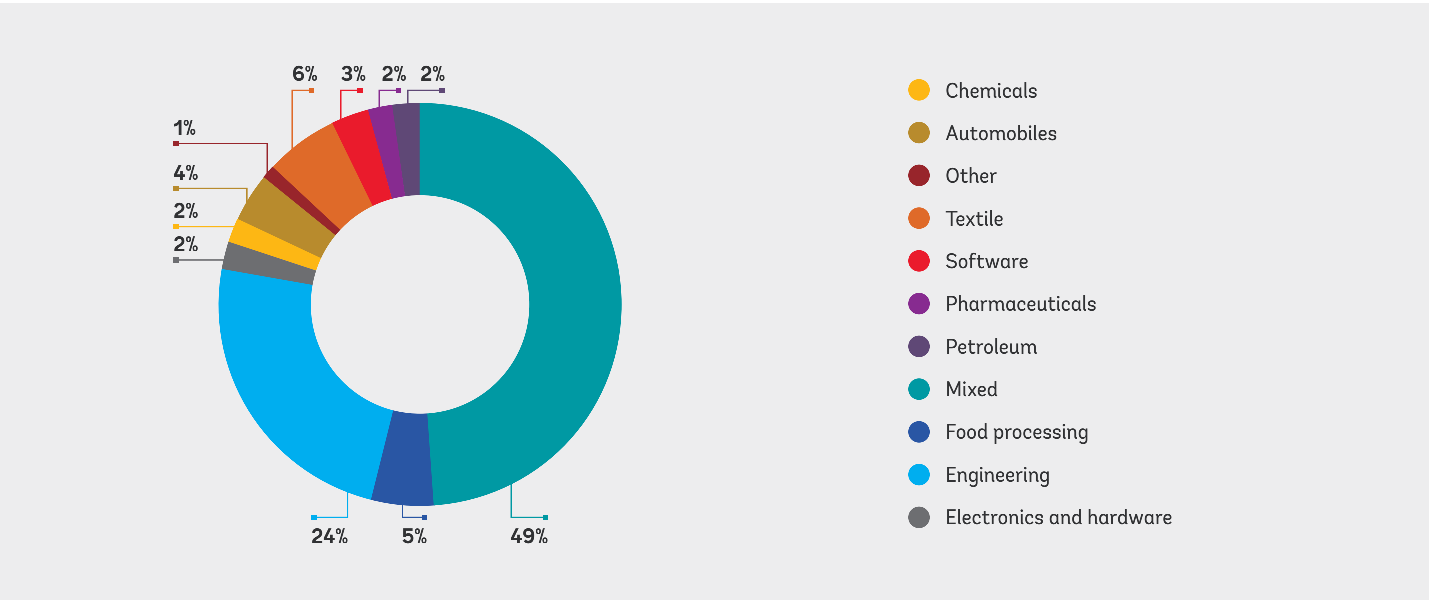

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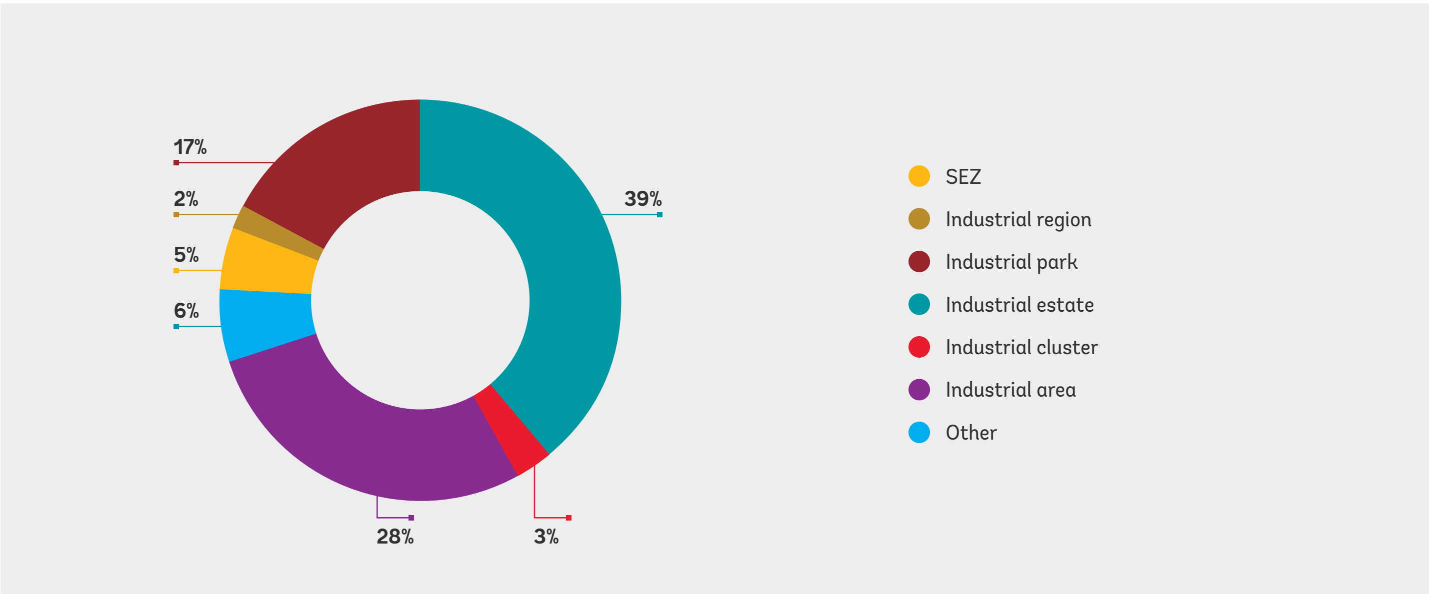
FIGURE 4. - Economic zones by classification, India



Source: Ministry of Commerce and Industry, government of India.
Note: SEZ = special economic zone.

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Good Practices for Zone Programs

This section sets the stage for assessing the policy and regulatory environment facing SEZs in the BBIN region by reviewing good practices. Broadly speaking, the determinants of successful SEZs include zone characteristics, contextual characteristics, and program characteristics (World Bank 2017). For zones to be successful, each of these elements needs to be sound. The term *zone characteristics* refers solely to the structure and layout of the zone. These include factors such as the maturity, size, operator, location, and industrial focus. For instance, the choice of location (whether the economic zone is situated near ports, consumer markets, and workers) plays an important role in its success. *Contextual factors* are exogenous to the setup of the zone itself, and they include factors such as the institutional quality in the country, rule of law, access to markets, the level of income, human capital, and population density. For instance, proximity to large markets can mean lower transport costs for goods. Human capital endowments, in terms of both abundance and skill level, can be an important factor for an investor depending on their production. Finally, *program characteristics* refer to the rules governing the development, operation, and regulation of the zone. These characteristics play an important role in a program's success. Successful zone programs will need to perform well across all of these determinants; however, as noted in Farole and Kweka (2011, 1), "although multiple factors contribute to the failure of an SEZ program, in most cases, they can be traced back to the initial planning stages, and derive from an ineffective regulatory and institutional framework." Program characteristics are the focus of this paper.

The paper evaluates SEZ program design along three dimensions (see figure 4). The first has to do with the fiscal and nonfiscal incentives provided to investors in the SEZs. The second concerns the requirements that zone developers and tenants must meet to qualify for these incentives. The third is related to the institutional and regulatory frameworks that govern the development, operation, and regulation of economic zones. Although there is overlap across these dimensions, the distinctions are useful to make the analysis tractable.

With respect to the incentives provided to zone developers and tenants, there is no single formula that is optimal, but incentives should be cost-effective and consistent with other legal obligations. On the fiscal side, these incentives may include relaxations from import duties on inputs; reductions on different types of taxes such as income, value added tax (VAT), or corporate taxes; and subsidized utilities. Because these fiscal relaxations constitute a cost through forgone revenue, it is important to assess their effectiveness in achieving their intended objectives. Another consideration is that fiscal incentives should be consistent with international laws such as antidumping regulations. Nonfiscal incentives frequently include relaxations from labor protection laws, or

regulations related to land-use or construction. Evidence suggests that tax incentives alone do not guarantee success of the zone. Although it is difficult to assess the isolated effect of individual exemptions, Farole (2011) found that infrastructure and trade facilitation had a significant positive effect on zone performance, compared with tax and other financial incentives that were less important. Furthermore, the provision of physical infrastructure, utilities, and other incentives does not guarantee their quality, affordability, or accessibility. It is also important that nonfiscal incentives such as relaxations of labor protections do not undermine worker safety within zones.

The requirements for tenant firms of SEZ programs vary from one case to another, but they should be consistent with zone policy objectives. Because many economic zone programs are geared toward attracting FDI, these requirements may stipulate a minimum foreign ownership for clients. In such cases, it is important to ensure that local and international firms compete on equal footing. Alternatively, if the zone is set up to increase exports, firms are often required to export a minimum percentage of their output. There may also be minimum requirements for investment or employment in order to qualify for incentives. One consideration regarding zone tenancy requirements is that zones should not simply enable existing firms to relocate to evade taxes but rather should stimulate economic activity that would not otherwise have taken off. The latter would support additional job creation rather than just displacement. Another consideration is that maintaining stringent domestic content requirements for products made in SEZs may discourage investors. Instead, working to build up domestic capacity and encourage knowledge spillovers between zone tenants and local firms outside the zone can be a way to facilitate the ultimate objective of convergence between well-performing zones and the rest of the country. (It should also be noted that maintaining export requirements alongside input subsidies can infringe upon international trade regulations.)

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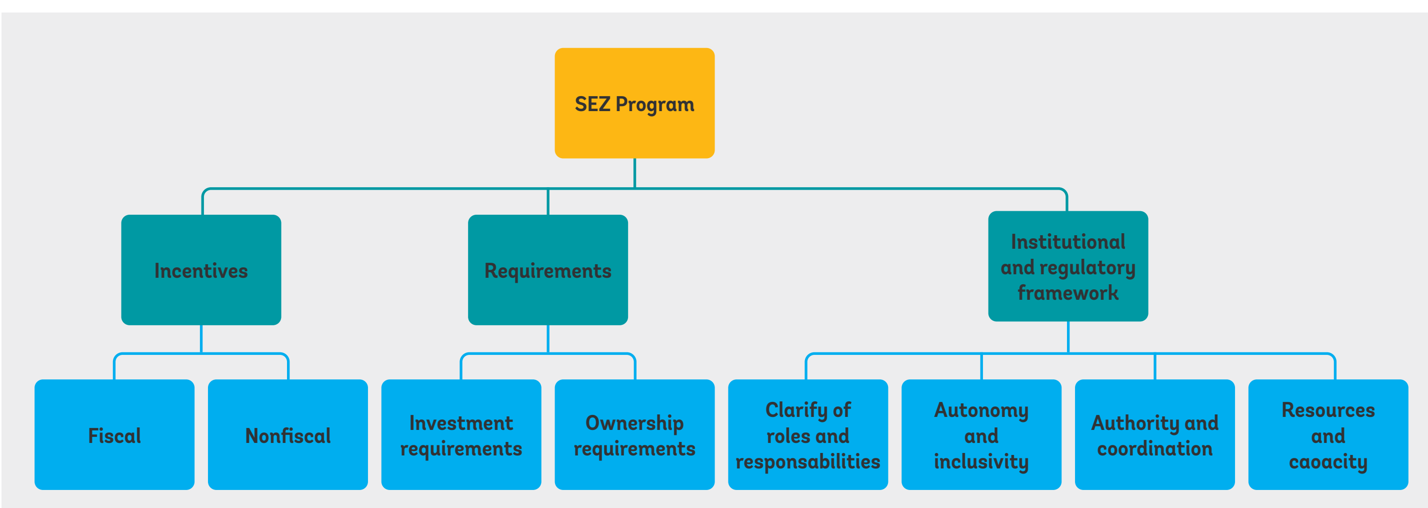
FIGURE 5. - Drivers of SEZ performance



Source: Adapted from World Bank 2017 and Farole and Kweka 2011.
Note: SEZ = special economic zone.

In terms of the institutional and administrative structure governing the operation of economic zones, there is no one-size-fits-all approach. Rather there are a number of good practices that are associated with successful economic zones. The four key principles identified by Farole and Kweka (2011) for an effective institutional framework are (a) clarity in roles and responsibilities, (b) autonomy and inclusivity, (c) authority and coordination, and (d) resources and capacity.

The operation of an economic zone involves the zone owner, developer, operator, and regulator. In many instances—especially among older economic zones—these roles were all played (at least in part) by the government, but this formula is not without risks. For instance, when the same government agency acts as the developer and regulator, private sector developers may perceive that they are at a disadvantage and consequently may be discouraged from investing. Moreover, an opaque structure in the management of economic zones can deter the engagement of the private sector. Therefore, clarity of roles and responsibilities is a key factor for successful economic zones. However, although several best practices guides have emphasized the advantages of private zone operators (Watson 2001; OECD 2009), the results of other studies have found that this factor alone has not led to improved performance (Farole and Kweka, 2011; Frick, Rodríguez-Pose, and Wong 2019).

Similarly, there is no one formula for demarcating SEZ responsibilities between federal and subnational authorities. However, coordination is important to ensure well-functioning SEZ programs. Often, local authorities have greater knowledge of local conditions with regard to infrastructure, land and capital endowments, and region-specific investment obstacles and investment needs. They may also have greater authority to provide incentives, enforce requirements, support firms, and ensure that the benefits of zone programs extend beyond their walls. Central governments can play an important role in coordinating zone programs, especially to mitigate the risk of splintering institutional and regulatory regimes under devolution. Different countries have gone about the division of labor differently. In the case of Indonesia, zone councils bring together central and regional authorities to support the national council in administering and overseeing SEZs. In Mexico, the federal SEZ law stipulates that once a zone is established, federal, state, and municipal governments must enter into a coordination agreement to clarify responsibilities of different actors, harmonize financial arrangements, ensure smooth provision of incentives, and facilitate administrative procedures (UNCTAD 2019, 172).

Successful economic zones also tend to have autonomous regulators with inclusive representation on their executive board. Good practices tend to favor establishing the regulator as an autonomous agency with representation from both key public sector entities and the private sector and ensuring that it is not involved in the ownership, development, or operation of zones (Farole and Kweka 2011; OECD 2009; Cheng 2019). If the regulator is embedded within a single ministry, involving other ministries and the private sector becomes more difficult. Experience has also shown that conflicts of interest arise when the regulator is engaged in the zone development process (Akinci and Crittle 2008). For instance, in Tanzania, where the Export Processing Zones Authority both regulates all zones and is the developer of the Benjamin William Mkapa SEZ, it has been suggested that lease rates for industrial facilities in the publicly run zone are below market rates (Farole and Kweka 2011).

Another way to promote autonomy of the regulator is to have its board report directly to the highest authorities in the government. For example, it might report directly to the president, prime minister, or minister of finance. Such an arrangement would serve to bolster the authority of the regulator, but it may also carry risks. For instance, the central authority may cause delays in decision-making if it is tending to other priorities of national interest, or it may engage in micromanaging the regulator, thus opening the door for political capture.

Including the private sector in the zone development process is also critical for success. Owing to limited public resources, many countries have relied on the private sector to provide the needed financing and expertise. Engaging the private sector at this stage is also important to ensure that investors' voices are heard. Private sector members on zone development boards should not be hand-selected by a government chairperson; boards should also include representatives from zone operators.

For the SEZ regulator to deliver effectively on its mandate, it must have the legal authority and coordinative capacity to monitor and enforce laws and standards and to act as a "one-stop shop" facilitator of investment. It must have domain over customs; land use and zoning; taxation; business registration and licensing; immigration; and environmental, labor, and social compliance. One of the principal reasons behind the establishment of economic zones is an otherwise cumbersome business environment. Providing the regulator with the power to make and enforce rules is thus key for its success. In contexts with devolution to local authorities, the regulator should be empowered over not only federal laws but also state laws. Given the large array of responsibilities that would fall under the regulator, it may be necessary to build up the capacity of the regulator gradually and focus on coordination among existing ministries in the meantime.

The regulator must be empowered in terms of both resources and capacity to carry out its functions. One way to ensure it is more financially independent is to link its budget to revenues earned through the zones. This would incentivize zone authorities not to compete on tax holidays. However, authorities should not be expected to be fully financially self-sufficient because that might encourage excessive charging of fees, which could discourage investors. To monitor and evaluate zone performance, zone authorities also require a high degree of capacity to compile statistics on outcomes. Moreover, capacity to develop zone master plans and assess those developed by the private sector requires technical expertise.

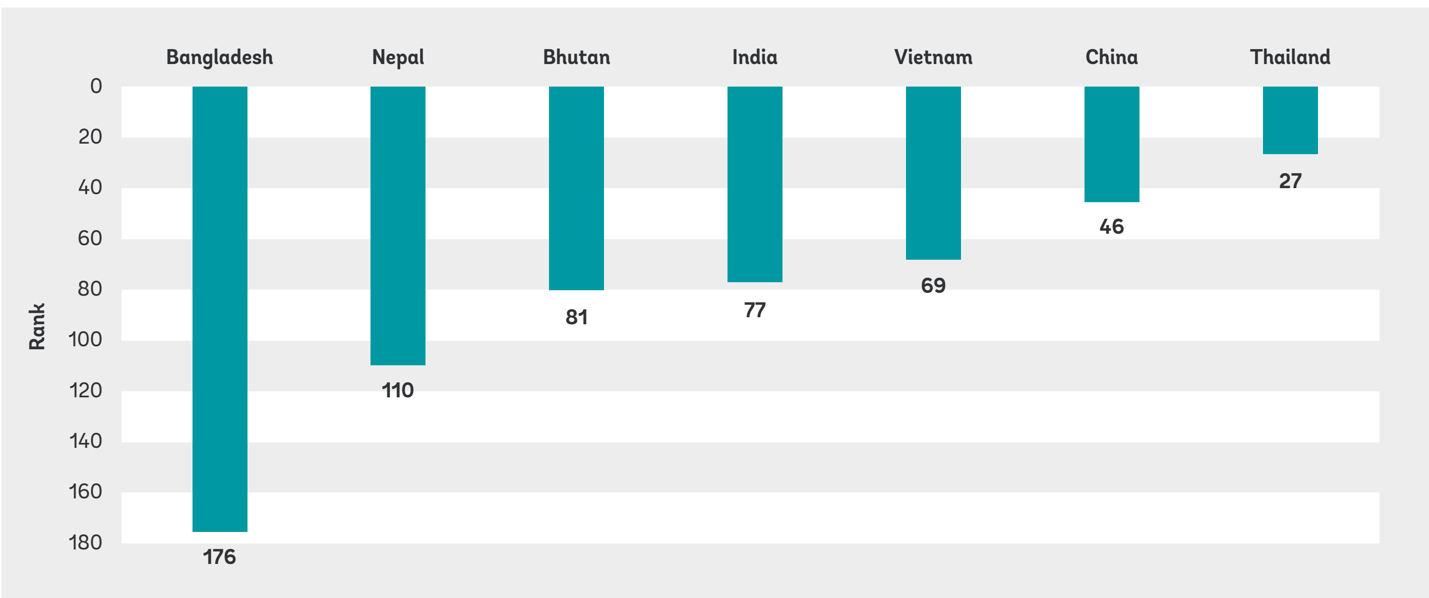
Finally, there is no question that investors' confidence hinges on a credible long-term commitment to economic zones by the government. Support from high-ranking authorities and a capable and empowered zone regulator serve as strong signals to the private sector of such a commitment. This, along with responsiveness to tenant firms' concerns, gives confidence to investors.

Incentives, Requirements, and Regulatory Structures of Zone Programs in South Asia

This section assesses the policy frameworks and regulatory frameworks of the SEZ programs in Bangladesh, Bhutan, India, and Nepal against good practices outlined in the previous section. More concretely, it reviews the incentives provided to firms in SEZs, the requirements for firms to enjoy those incentives, and the regulatory framework governing zone administration. Regarding the regulatory framework, the section looks at the clarity of objectives of the zones along with the roles assigned to different actors, the extent of the autonomy enjoyed by the operators, the authority operators have, and the adequacy of resources and capacity to enable operators to carry out their responsibilities. The bottom line is that although many features of good practices have been adopted in the design and operation of SEZ programs in South Asia, significant shortfalls remain. Addressing those shortfalls is necessary if these economic zone programs are to more effectively fulfill their objectives.

Before delving into the assessment of the policy and regulatory framework governing SEZs in South Asia, it is worth recalling that SEZs were adopted there, as elsewhere, to escape the regulatory and bureaucratic obstacles that the private sector faces nationwide. Such constraints in the business environment are indeed prevalent in our group of countries, as shown in figure 5, which is based on the World Bank's Doing Business surveys. The results indicate that Bangladesh is the lowest performer of the group, ranking at 176 out of 190 countries. Nepal and Bhutan perform relatively better, while India is the best performer, having improved its ranking significantly in recent years. It remains true, though, that our sample of countries continues to lag aspirational comparators that also have active SEZ programs, such as China, Thailand, and Vietnam.

> > >
FIGURE 6. - Doing Business rankings, 2019



Source: World Bank Doing Business surveys.
Note: Rank out of 190.

The incentives embodied in SEZ acts in the region are abundant, in the form of both fiscal incentives and regulatory concessions. A summary of the incentives offered across SEZ acts in India, Bangladesh, and Nepal is provided in table 3. Taking India as an example, the SEZ Act provides fiscal incentives to zone developers and entrepreneurs operating in zones. Those individuals are exempted from customs tariffs on goods imported and exported to the SEZ by the Customs Act, 1962 and the Customs Tariff Act, 1975 (chapter VI, §26.1a–g). The trading activities of SEZ units are done on the basis of "self-certification," where units inside the SEZ submit bills of entry for imports and exporters file shipping bills (Aggarwal 2012, chapter 4). These bills are processed without physical examination by customs. The SEZ also provides a host of tax concessions to units, including full income tax exemption for the first five years of operation, 50 percent exemption for the next five years, and 50 percent of the ploughed-back export profits for the following five years. SEZ developers also receive full income tax exemption for 10 years, with additional exemptions for offshore banking units within SEZs. Units and developers are also exempt from most indirect taxes, central sales tax, service tax, and VAT, and from all state sales taxes.

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TABLE 3. - Summary of incentives in India, Bangladesh, and Nepal based on federal SEZ acts

Bangladesh
Incentives for developers: • Income tax exemption for 12 years: first 10 years 100%, 11th year 70%, 12th year 30% • Exemption from customs duty on imports for zone development; stamp duty and registration fees for land registration for the first time; registration fees of loan or credit document; tax on dividend income for 10 years **Incentives for units:** • One-stop services • Tax incentives: tax holiday for 10 years; duty-free import of raw materials; exemption from dividend tax, stamp duty and registration fees, and VAT on all utility services; duty exemption on export; exemption of customs duty for import of vehicles; exemption of double taxation subject to double taxation agreement; exemption of salary income from income tax for expatriates; tax exemption on capital gains from transfer of shares • Other: full repatriation of capital and dividend; no cap on FDI; 100% backward linkage of raw materials and accessories to sell for export oriented industries in DTA; 20% sale of finished product to DTA by an Export Processing Area; subcontracting with DTA allowed; foreign loan allowed in compliance with existing laws; foreign currency account for nonresidents; foreign currency account for both local and joint venture industry; foreign investors free to enter into joint venture; provision of transfer of shares by foreign shareholders to local shareholders and investors; issuance of work permits to foreigners allowed up to 5% of total officers and employees of an industrial unit • Reinvestment of remittable dividend to be treated as new foreign investment; resident visa for investment of US$75,000 or more; citizenship for investment of US$500,000 or more
India
Incentives for developers: • Exemption from customs/excise duties for development of SEZs • Income tax exemption on income derived from the business of development of the SEZ in a block of 10 years in 15 years under section 80-IAB of the Income Tax Act (sunset clause for developers took effect April 4, 2017) • Other tax exemptions: central sales tax; service tax (section 7, 26, and second schedule of the SEZ Act); supplies to SEZ are zero-rated under IGST Act, 2017 **Incentives for units:** • Single-window clearance for central and state-level approvals • Duty-free import and domestic procurement of goods for development, operation, and maintenance of SEZ units • 100% income tax exemption on export income for SEZ units under section 10AA of the Income Tax Act for first five years, 50% for next five years, and 50% of the ploughed-back export profit for the next five years • Exemption from central sales tax, service tax, and state sales tax (these have now been subsumed into GST, and supplies to SEZs are zero-rated under IGST Act, 2017) and other levies as imposed by the respective state governments • Supplies to SEZs are zero-rated under IGST Act, 2017. • No routine examination by customs authorities of export/import cargo and full freedom for subcontracting
Nepal
• One-window service • Income tax concessions (industries situated in designated mountain districts receive 100 percent tax exemption for the first 10 years of operation, followed by 50 percent thereafter; industries in other areas receive the 100 percent income tax exemption for 5 years, followed by 50 percent thereafter; 100 percent dividend tax exemption for 5 years, followed by 50 percent exemption for 3 years; foreign investors entitled to 50 percent tax concession on income generated from service fees or royalties via transfer and or management of foreign technology to firms in SEZs) • VAT exemptions (100 percent exemption on exported goods and services; 100 percent exemption on raw materials sold to firms within SEZs) • Industries having rented land or building inside SEZ are entitled to concessions in the rent or lease amount (first year, 50%; second year, 40%; third year, 25%) • Customs duties concessions (firms exporting or selling domestically in convertible foreign currencies can import raw materials against the bank guarantee equivalent to import-related customs duties and other fees on such raw materials; firms can import capital inputs against a bank guarantee equivalent to import-related customs duties and other fees on such materials, which will be released after confirmation of input installation; firms can import one passenger vehicle and two cargo vehicles for 1% customs duties) • Income repatriation (foreign investors can repatriate foreign currency earnings from partial or total shares held in firms; foreigners can repatriate dividends generated from investments)

Source: World Bank staff.

Note: DTA = Domestic tariff area; FDI = Foreign direct investment; GST = goods and services tax; IGST = Integrated goods and services tax; SEZ = special economic zone; VAT = value added tax.

The incentives accorded in the SEZ legislation across Bangladesh, India, and Nepal tend to be similar and generous by international standards. Table 4 provides a summary of the main features of the incentives offered, along with a comparison to the share of SEZ laws globally that provide each incentive type.[3] As in almost 80 percent of SEZ laws globally, those in Bangladesh, India, and Nepal include fiscal incentives such as tax breaks and provide a special customs regime with either tariff reductions or expedited or simplified customs processing. Each country's legislation also provides investment facilitation to help streamline business registration and other bureaucratic procedures compared with a global average of one-third. Unlike about a quarter of SEZ laws globally, there are no additional investment protections that go beyond those of the rest of the country to accord further guarantees against expropriation or nationalization. The SEZ laws in Bangladesh and Nepal stipulate additional support in the process of land acquisition compared with a quarter of SEZ laws globally. The three countries also provide some means of trade facilitation through simplification of import/export operations compared with less than a fifth of SEZ laws globally. The operators of SEZs in the three countries are also required to supply zones with infrastructure such as electricity, fuel, water, and telecommunications services. In rare cases, SEZ laws also call for the provision of social amenities such as hospitals or schools. Among the SEZ laws covered in this analysis, only India's SEZ Act makes a reference to the provision of social infrastructure.

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TABLE 4. - Types of incentive instruments employed in SEZ legislation

	Bangladesh	India	Nepal	Share of SEZ laws globally that include investment attraction instrument (%)
Fiscal incentives	✔	✔	✔	77
Special customs regime	✔	✔	✔	74
Investment facilitation	✔	✔	✔	32
Investment protection	✖	✖	✖	26
Preferential land use	✔	✖	✔	25
Trade facilitation	✔	✔	✔	17
Infrastructure provision	✔	✔	✔	17
Social amenities	✖	✔	✖	3

Source: UNCTAD 2019 and SEZ legislation of Bangladesh, India, and Nepal.
Note: The global sample of SEZ legislation covers 127 acts. SEZ = special economic zone.

3 See World Investment Report 2019: Special Economic Zones (UNCTAD 2019) for a full comparison of SEZ incentives globally.

Notwithstanding the generous web of incentives provided in the SEZ acts in Bangladesh, India, and Nepal, these incentives suffer from at least four shortcomings. First, although it is difficult to discuss all these incentives in detail here, the most glaring shortcoming is that there is no monitoring and evaluation mechanism to assess the incentives' impact systematically to ensure their effectiveness and efficiency in achieving their objectives. This is a critical shortcoming because it means that (a) forgone revenues may be squandered, and (b) governments are deprived of an instrument correct for shortcomings within zones, learn from experience, and potentially implement successful policies beyond the zone's borders.

Second, some of the incentives may be inconsistent with governments' international commitments. A case in point is the fiscal incentives provided to firms through the SEZ Act in India, which prompted accusations of relying on prohibited export subsidies. Although the World Trade Organization's (WTO) Agreement on Subsidies and Countervailing Measures (SCM) does not directly refer to SEZs, the agreement prohibits the use of export subsidies contingent on the use of domestic goods over imported goods (Article 3, Annex 1 SCM) (UNCTAD 2019). The rules allow for some exceptions in the context of SEZs (Coppens 2013)—for instance, general infrastructure provided to all firms is not deemed a subsidy, and relief on duties and taxes of exported goods is also permitted. The United States accused India of employing prohibited export subsidies inconsistent with the SCM Agreement, and the WTO's Dispute Settlement Body ruled in favor of the United States (dispute number DS541) in 2019. The government of India has challenged the ruling in the WTO's appellate body but has also reportedly begun to prepare reforms to make SEZ provisions WTO compliant.

Third, reducing the regulatory requirements as an incentive for investors may also backfire, as happened in the case of insufficient protections for laborers in Bangladesh's EPZs. In 1989, the government of Bangladesh exempted EPZs from the Factories Act, the Industrial Dispute Act, and the Employment of Labor Act, which represented major nonfiscal incentives for investors (Aggarwal 2005). A 2006 Labor Act did not fall in line with international standards according to the International Labour Organization (ILO) and did not cover workers in EPZs. The EPZ Workers' Association and Industrial Relations Act of 2009 did not provide workers the right to unionize. Citing the adverse conditions faced by factory workers, the US suspended the Generalized System of Preferences (GSP) trade benefits with Bangladesh. Since then, a new Labor Act of 2013 and the Bangladesh EPZ Labor Act of 2013 have improved conditions, and in 2020 the government requested the restoration of GSP. The World Bank Group has also supported BEPZA's efforts to improve social and environmental conditions through the hiring of social and environmental counselors. The program has resulted in significantly improving the working environment, dispute resolution, and environmental compliance in EPZs.

Fourth, the generous incentives provided in some types of economic zones may not produce their full effect because they are not accompanied by necessary institutional support. For instance, tenants of the industrial districts under the BSCIC in Bangladesh benefit from various incentives, including plot allocations at subsidized rates, initial tax exemptions, infrastructure facilities, and various other supports, but they lack a one-stop shop for administrative procedures. In Bhutan, the government reportedly provides long-term leases on land for parks, basic infrastructure, and a range of fiscal incentives, but no business facilitation services.

In terms of requirements set out for firms to qualify for these incentives, South Asian countries taken different approaches, but in some cases requirements are inconsistent or vague. The case of Nepal is a positive one. The SEZ Act objectives are centered on export promotion, and firms in SEZs can sell their products domestically in the first year of operation, though they do not receive tax exemptions. Beginning with the second year of operation, firms must export at least 60 percent of goods or services produced within SEZs. On the other hand, in India, units are required to achieve positive net foreign exchange, calculated cumulatively for a period of five years from the commencement of production (Special Economic Zones [Amendment] Rules, 2018), but they are also required to meet a value-addition requirement (Special Economic Zones [Second Amendment] Rules, March 2019). Targeting both value addition and exports can be contradictory. Outside of the formal SEZ framework in Bangladesh, requirements for tenancy in industrial districts are not fully specified, leaving room for discretion and inviting the perception of bias, which in turn can deter firms and investors.

Multiplicity of zone policy objectives makes consistency with tenancy requirements problematic. Governments in the BBIN region tend to define zone policy objectives in broad and multiple terms. For example, India's 2005 SEZ Act expanded the mandate of economic zones to cover the generation of economic activity, investment, infrastructure, employment, and supporting Indian interests and external relations. In Bangladesh, BEZA has a mandate to support relatively underdeveloped regions and to support overall development through diversification of industry, greater employment, production, and export. Although broad objectives can allow flexibility in zone focus over time, they do not easily translate into concrete and measurable outcomes. In addition to causing ambiguity about the core objective(s) of the zone, this broad definition of objectives makes the assessment of their effectiveness difficult, and the failure in achieving one objective can be attributed to attempting to pursue others.

Turning to the institutional and regulatory framework governing zones, there are a number of shortcomings. These relate to the roles, authority, and responsibilities of different actors; the inclusivity of the private sector; the autonomy of the regulators; and the adequacy of resources and the capacity for regulators to fulfill their mandate.

The roles of the owner, developer, and operator are not always kept separate. This separation is particularly important when the government is responsible for regulating and promoting all zones in a country and some zones are owned and developed by the private sector and others by the government. This situation creates an actual or at least perceived conflict of interest. In Bangladesh, the government's role across these responsibilities is not yet settled. At the outset, BEZA and BHTPA were to rely on the private sector for the financing and management of zones, with the government acting as the regulator and facilitator. However, the majority of zones established have been publicly funded. The industrial districts under the BSCIC suffer from a range of challenges, according to a study by the Bangladesh Institute of Development Studies (Hossain et al. 2018). According to the study, (a) approximately a quarter of plots are unused, (b) the choice of location of the district was frequently politically motivated rather informed by feasibility studies, (c) poor maintenance of infrastructure within estates resulted from limited fiscal resources of the BSCIC, and (d) limited coordination among key agencies resulted in the absence of gas and electricity provision to districts.

In Nepal, as in Bangladesh with the BSCIC, industrial districts fall under the management of one public entity, possibly resulting in similar shortcomings. The IDM is responsible for essentially all activities in the development, operation, and regulation of industrial districts. It provides land, infrastructure, utilities, and other services to industrial districts; carries out feasibility studies on establishing new industrial districts and projects within them; engages in the promotion of industrial districts; evaluates policy impacts on industrial districts; provides consulting services to enterprises; and encourages private sector participation through either cooperative arrangement or full majority private sector ownership.

The clarity of roles and responsibilities is also undercut when the rules governing economic zones are subject to frequent changes. The example from India is most telling. India's SEZ Act of 2005 provided a new set of rules for the establishment, development, and management of economic zones. The act was complemented by a set of SEZ Rules from 2006, and by 2014, more than 80 additional instructions had been issued (Mukherjee et al. 2016, 56). The 2005 Federal SEZ Act encouraged states to pass their own SEZ legislation, and some have done so. Gujarat, Haryana, Madhya Pradesh, Tamil Nadu, and Punjab have state-level SEZ acts, whereas other states have put in place SEZ policies (table 5), though the objectives remain largely similar. West Bengal was among the first states to introduce an SEZ act; however, the state cabinet repealed it in 2012 for political reasons and instead introduced the Information and Communication Technology Incentive Scheme, 2012, providing a series of fiscal incentives and subsidies to investors. These amendments may have led to confusion among state and federal authorities over respective responsibilities and may have made it difficult for investors to make investment decisions and to plan ahead.

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TABLE 5. - Indian state-level SEZ policies and acts

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Madhya Pradesh	Policy	Act										
West Bengal		Act										Repealed
Gujarat			Act									
Tamil Nadu				Act								
Haryana				Act								
Punjab				Policy				Act				
Maharashtra	Policy											
Kerala		Policy										
Jharkhand		Policy										
Chandigarh				Policy								
Uttar Pradesh						Policy						
Karnataka								Policy				

Source: World Bank staff.
Note: SEZ = special economic zone.

The regulatory regimes do not always provide a voice for the private sector. In India, the structure is dominated by representation from public sector entities. This structure has three tiers. It is headed by the board of approval, which is a committee composed of 19 members representing the federal government, a nominee from the state government, the director of foreign trade, a development commissioner (DC), and a professor from the Indian Institute of Management (SEZ Act of 2005, Chapter III, §8.1). The board of approval is tasked with approving proposals for the establishment of SEZs, the provision of infrastructure in zones, and the involvement of foreign collaborators, as well as evaluating appeals brought to the zone developer by rejected tenants (Chapter III, §9.2a-i.) The second step in the hierarchy is the approval committee, which similarly has limited engagement with the private sector. Its members include the DC as the chairperson, representatives from the federal and state governments, and one representative of the developer designated as a special invitee (Chapter V, §13.2a-f). The approval committee is responsible for approving the import or procurement of inputs from the Domestic Tariff Area; approving the provision of services within the SEZ; monitoring the use of goods, services, warehousing, or trading within the SEZ; approving proposals for units; and monitoring and supervising compliance of conditions under which the developer has been granted approval (Chapter V, §14.1a-g). To set up a unit within the zone, prospective tenants must submit a proposal to the concerned DC, who in turn submits it to the AC. The third step in the hierarchy is the SEZ Authority, which includes representatives who are from the private sector but who are nominated by the government. The DC of each respective zone serves as the chief executive of the concerned SEZ Authority. The board of the authority is chaired by the DC and includes federal government representatives; it also includes two entrepreneurs who are nominated by the central government (Chapter VII, §31.5a-d). The SEZ Authority is charged with the development, operation, and management of the respective SEZ. Its duties include the development of infrastructure, the promotion of exports, the review of the functioning and performance of the SEZ, and the levying of user or service charges, fees, or rent for the use of properties belonging to the authority (Chapter VII, §34.2a-e). As a whole, there is an acute absence of a direct voice for private investors and companies involved in the zone program. A better example in this respect is the IDM in Nepal. It is governed by a board of directors that consists of appointees and representatives of the government representing the Ministries of Industry, Finance, and Energy, as well as a representative of the Nepal Industrial District's Chambers of Commerce.

The autonomy of the regulators and their ability to coordinate are often compromised, especially when they report to line ministries. In this regard, the experience of the BBIN region is mixed. In Bangladesh, BEZA reports directly to the prime minister's office, whereas BHTPA reports to the Ministry of Information and Communication Technology. In Nepal, both the SEZ Authority and the IDM fall under the Ministry of Industry. Reporting directly to a high authority such as the prime minister can increase the chances of greater autonomy of the regulator and make it easier to coordinate across line ministries.

Similarly, the multiplicity of spatial development modalities at the state level complicates coordination with the federal government. In India, even within the formal SEZ framework, the federal Department of Commerce does not have a formal mechanism for cooperation with state governments on land allocation, infrastructure provision outside the zones, or single-window clearance (Mukherjee et al. 2016, 222). In addition, there are many other zone programs that are initiated by state governments, sometimes through state-owned industrial development corporations with similar mandates as other SEZs, including attracting investment, generating revenue, and creating employment. For instance, the Haryana State Industrial and Infrastructure Development Corporation Ltd. (HSIIDC) develops industrial townships, industrial estates, industrial clusters, and theme parks. Such zones are governed by estate management procedures determined by the HSIIDC. Tenancy requirements vary and some zones have a sectoral focus, but zones frequently have minimum requirements for FDI, capital investment, or employment generation. Incentives provided to tenants vary by zone, but they range from basic infrastructure such as utilities and security to services such as banking, logistics, and, in large zones, even housing and schooling. While not all HSIIDC zones provide fiscal incentives like exemptions from VAT or utility subsidies, some do. The information technology (IT) policy for the state of Gujarat (2016–21) provides incentives for developers of IT/information technology-enabled services technology parks, including matching capital investments and tax exemptions. Although the state's previous IT policy (2014–19) supports some coordination with SEZs by noting it will facilitate IT parks obtaining SEZ status, more recent versions do not. There are many more such initiatives across different states, among them Sri City in Andhra Pradesh, an integrated business city that includes an SEZ and a domestic tariff zone, and the Dholera Special Investment Region in Gujarat, essentially an SEZ but constituted under Gujarat's Special Investment Region Act of 2009. The variety of incentives makes it challenging for investors to know how to make the most of available schemes. It also signals an area in which greater coordination between state and federal policy makers can lead to more aligned incentives.

In terms of resources, SEZ Authorities in India and the IDM in Nepal are somewhat financially independent, but that independence may lead to an excessive burden for investors. In India, each SEZ Authority maintains its own fund. It receives grants and loans from the central government and collects all sums due from user or service charges, fees, or rent for the use of properties belonging to the authority (Chapter VII, §35-36e). The fund is used for remuneration of authority employees, repayment of loans, and other operating and administrative expenses of the authority. In Nepal, the IDM is reliant on generating its own income. It does so through the rental of district land and buildings, revenue from the price differential between concessionally received electricity from the Nepal Electricity Authority, revenues from other utility provision such as water in some districts, entry fees from new tenants, and agreement fees from renewing tenants. The entry fees are fixed per industrial district by the IDM, and renewal fees are set at 60 percent of the initial fee. The IDM also receives government financing through public expenditure in repairs and reconstruction of industrial infrastructure. The key is to strike a balance between maintaining financial independence and keeping user charges affordable for tenants.

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Conclusion and Recommendations

In principle, the benefits from successful economic zones in South Asia can be wide ranging. Zones can support economic growth by attracting FDI, facilitate a transition to higher value-added production, and promote job creation. They can also foster greater economic inclusion. In developing countries, businesses tend to face a series of constraints, and typically, because of their size, small and medium enterprises (SMEs) are less well equipped to overcome them. Providing a friendlier business environment in zones to alleviate these constraints can make a big difference. Moreover, SMEs tend to have strong potential to provide jobs and are more likely to employ relatively vulnerable groups in society. Also, if zones are established in underserved regions, they may help mitigate inequality and balance regional development. Finally, experimenting in the SEZs by adopting regulatory innovations and soft policies can enable governments to find out what works best in a relatively low-cost way and to generalize the results for the entire country.

To realize these potential benefits, policy frameworks and regulatory frameworks governing the zones ought to be well designed and executed. Drawing on good international practices, this section offers some specific recommendations regarding incentive packages, tenancy requirements, and institutional setup.

Incentive packages should strike a balance between attracting investors and furthering the development objectives of zone programs. Maintaining this balance requires ongoing evaluation of the trade-offs between the costs and benefits of incentive packages, ensuring the packages' compliance with international laws, and monitoring the well-being of laborers. Such a mechanism is largely missing in South Asia. As a result, an opportunity is lost to have an avenue for testing new policies and possibly adopting them outside the zones.

SEZ authorities should be empowered to provide one-stop-shop services for tenant firms. Such services are often a key determinant of the success of economic zones, as they help overcome an otherwise adverse business environment. In some cases, even though SEZ policy or legislation stipulates that such services should be provided within zones, in practice they are absent. This disconnect should be resolved.

The requirements for eligibility to operate within zones should be clear, transparent, and consistent with the objectives of the zone program. When the authorities have a large degree of discretion in accepting tenant applications, it can create uncertainty and discourage investors. It may also leave room for rent-seeking and inefficient allocation of plots.

In order to clarify the roles of different agents in the zone governance framework, steps could be taken to avoid housing all aspects of zone development, operation, and regulation under the same entity. Responsibilities can be distributed among a variety of shareholders representing the government, zone owners, and an independent regulator. Although increasing the capacity of an independent regulator may take time, ensuring coordination among existing institutions is important in the interim period. In the longer term, agencies working on facilitation may most effectively collaborate and coordinate under a single umbrella to enhance bureaucratic expediency. However, these functions should remain separate from those of the regulatory body.

It is also critical that the rules governing zone development and operation at the state and federal levels be clarified to ensure their effectiveness. In India, frequent amendments to SEZ policy cause confusion for both administrators and investors, as does the web of different zone programs at the federal and state levels. The diverse and broad zone objectives also make the role of evaluation more difficult. Clarifying roles and establishing more concrete zone policy objectives would enhance zone effectiveness. Moreover, the wide range of spatial development policies at the state and federal levels requires greater coordination at different levels of government. Better coordination would help investors know how to make the best of different available schemes and would improve delivery of services to zone tenants. There should also be a uniform and meaningful classification of zones.

The institutional and regulatory structures can be made more inclusive by increasing the role of the private sector in the development and operation of zones. The private sector is often absent from the development, ownership, and operation of economic zones in South Asian countries. In cases where private sector representatives serve on boards of zone authorities, those individuals are typically handpicked by the government. This practice discourages new investment and may also result in unrealized potential where input from the private sector would support the efficiency and productivity of zones.

Given the extensive and diverse experiences that countries in the BBIN region have with economic zones, there is potential for regional collaboration. At a minimum, countries in the region can learn from each other's experiences. There may also be room for regional development zones or cross-border zones spanning two or more countries that foster greater regional economic cooperation.

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