

## Chapter 7

# Special Economic Zones in Pakistan: Isles of Excellence or Labs for Policy Reforms?

*Special Economic Zones (SEZs) have emerged as an important investment policy tool to address the problems of low investments, exports, and industrialization. The SEZs address these issues by ensuring business-friendly environment within a designated boundary, with facilitative institutional, legal, and infrastructural architecture. Since developing economies find it difficult to reform business environment all across the country at once, they use SEZs both as an island of excellence, and as a laboratory for policy and regulatory reforms, before gradually rolling out these changes outside the zone. To promote industrialization and exports, Pakistan began setting up Industrial Estates (IEs) in the 1960s, and Export Processing Zones since the 1980s. However, these endeavors were unable to achieve the intended objectives due to the absence of business-friendly environment and weak infrastructure. In 2012, following the success of SEZs in other countries, Pakistan passed the SEZ Act, which paved way for the setting up of SEZs. However, the SEZs' potential in the country is constrained by the fact that they are not insulated from the overall business and investment climate of the country, vis-à-vis complex processes and procedures for approvals, registrations, and licenses; legal challenges; and sufficient availability of skilled labour. In addition, challenges to one-stop shops, a weak framework for long-term operational sustainability of the zones, technical hurdles in the financing of zone enterprises, and weak monitoring mechanisms, also pose challenges to the potential success of SEZs. Going forward, for the zones to prosper, it is imperative to ensure swifter provision of utilities and infrastructure. Also, a well-designed institutional, legal and infrastructural architecture is required to provide a favourable business environment.*



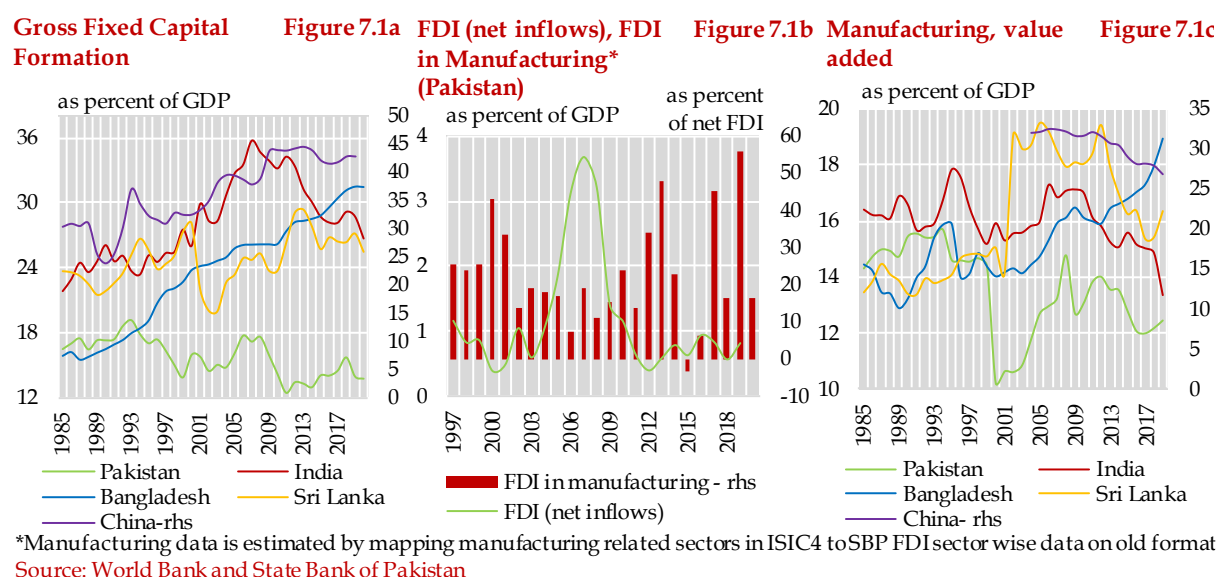
## 7 Special Economic Zones in Pakistan: Isles of Excellence or Labs for Policy Reforms?<sup>1</sup>

### 7.1 Introduction

Investment, especially in manufacturing and industrial sector, is one of the key drivers of economic growth and development. However, in Pakistan, investments have been falling over the past few decades and remain low relative to other emerging and developing economies (Figure 7.1a, b, and c). A host of macroeconomic reasons are responsible for low investment in the country, including persistently low savings rate amid high informality and low level of financial

intermediation, high inflation, and low tax revenues.<sup>2</sup>

In addition to macroeconomic constraints, there are several other factors limiting investment growth, as evident from Pakistan's rank in multiple indicators covering infrastructural, legal, institutional and operational parameters (Figure 7.2).<sup>3</sup> These include weak contract enforcement and dispute resolution mechanisms; lengthy documentation procedures; unfavorable tax administration; and regulatory uncertainty.



<sup>1</sup> This chapter has benefited from conversations with stakeholders from the Board of Investment (BOI); Export Processing Zone Authority; Sindh Economic Zones Management Company; Balochistan Industries and Commerce Department; Punjab Industrial Estate Development & Management Company; Faisalabad Industrial Estate Development & Management Company; Punjab Board of Investment and Trade; Khyber Pakhtunkhwa Board of Investment and Trade; Khyber Pakhtunkhwa Economic Zone Development & Management Company; Punjab Planning and Development Department; International Finance Corporation; Pakistan Business Council; Overseas Investors Chamber of Commerce and Industry; Pakistan China Joint Chamber of Commerce and Industry; former chairman BOI Mr Haroon Sharif, and former CEO National Industrial Parks Mr Syed Mohsin.

<sup>2</sup> A. Ali (2016). *Saving and Investment in Pakistan*. SBP Staff Notes 01/16. Karachi: SBP; J. Lopez-Calix and I. Touqeer (2013). *Revisiting the Constraints to Pakistan's Growth*. World Bank Policy Paper Series on Pakistan, no. PK 20/12. Washington DC: World Bank; A.H. Khan and K. Yun-Hwan (1999). *Foreign Direct Investment in Pakistan: Policy Issues and Operational Implications*. Manila: ADB; N. Akram (2011). "Impact of Public Debt on the Economic Growth of Pakistan," *The Pakistan Development Review*, 50(4): 599-615.

<sup>3</sup> E. Sanchez-Triana, D. Biller, I. Nabi, L. Ortolano, G. Dezfuli, J. Afzal, and S. Enriquez (2014). *Revitalizing Industrial Growth in Pakistan: Trade, Infrastructure, and Environmental Performance*. Directions in Development Series-Private Sector Development. Washington, DC: WB; J. Weiss and S. Lall (2003). *Industrial Competitions: The Challenge for Pakistan*. Manila: ADB; N. Nazeer and R. Rasiah (2016). "Explaining Pakistan's Premature Deindustrialization," *Lahore Journal of Economics*, 21: 351-368.

**Pakistan's Rank in Select Indicators**

**Figure 7.2**



Source: World Bank, WEF, Transparency International, World Justice Project, Property Rights Alliance

High cost and poor accessibility of utilities, constraints to availability of skilled labour, and several other operational factors are also impediments to a business-friendly environment.<sup>4</sup>

An increasingly accepted solution to these infrastructural, legal, institutional and operational problems faced by several EMDEs is the creation of Special Economic Zones (SEZ), which address several of these problems by insulating investors from structural flaws in the host economy. This is achieved by creating an ideal business environment in a designated area. This makes it easier for developing economies to implement the required infrastructure and policy reforms, which would otherwise be challenging to implement all across the country at once. The setting up of SEZs also helps governments to test policy reform experiments before rolling them out in the rest of the country.<sup>5</sup>

As Pakistan enters the second phase of the China Pakistan Economic Corridor (CPEC), focusing on business-to-business cooperation, the SEZs can play a pivotal role in attracting investment, and promoting industrialization, increased market accessibility and regional connectivity.<sup>6,7</sup> However, as literature on global best practices suggests, the success of SEZs depends partly on establishing a robust regulatory and institutional framework, with a focus on exploiting the country's competitive advantage.

In light of the literature on international best practices, this chapter evaluates the SEZ environment in Pakistan by surveying the SEZ framework, institutional setup, and various fiscal and non-fiscal incentives offered to investors. It explores Pakistan's experience with the Industrial Estates (IEs) and Export Processing Zones (EPZs), highlighting that on the whole, these initiatives did not achieve their potential because the promised utilities and infrastructure were not delivered, and real estate activities caused land prices to rise within these zones, crowding out industrial investments.

The chapter also discusses the challenges to the potential of SEZs in the country, where the absence of an effective One-Stop Shop (OSS) for ensuring a business-friendly climate in the zones, financing constraints for zone enterprises, and inadequate monitoring and evaluation mechanisms are found to be major stumbling blocks. In addition, the fact that the current regulatory regime does not insulate the SEZs from the overall legal environment of the country, and concerns over the availability of skilled labour, have also been identified as constraints to the potential success of SEZs.

<sup>4</sup> For a detailed discussion on constraints for investment in Pakistan, see, SBP Annual Report on State of Pakistan's Economy for FY19. "Chapter 7: Factors Constraining Investments in Pakistan: Beyond the Macroeconomics".

<sup>5</sup> World Investment Report (2019). *Special Economic Zones*. Geneva: UNCTAD; M. Alexianu, M. Saab, M. Teachout and A.K. Khandelwal (2019). *Doing Special Economic Zones Right: A Policy Framework*. London: IGC.

<sup>6</sup> The first phase of CPEC focused on removing the infrastructural and energy constraints. The second phase aims to increase industrialization and modernization in agriculture Sources: CPEC Secretariat at Ministry of Planning, Development and Special Initiatives ([www.cpec.gov.pk/news/167](http://www.cpec.gov.pk/news/167)), and Ministry of Planning Development and Special Initiatives press release, dated September 19, 2019 ([www.pc.gov.pk/web/press/get\\_press/348](http://www.pc.gov.pk/web/press/get_press/348)).

<sup>7</sup> K. Khan and S. Anwar (2016). "Special Economic Zones (SEZs) and CPEC: Background, Challenges and Strategies." *The Pakistan Development Review*, 203-216.

In view of these challenges, the setting up of an effective OSS is recommended, with a single facilitator, and demarcated roles and responsibilities to avoid overlapping of mandates, along with a recommendation for swifter dispensation of cases for SEZs with special commercial courts at its center. Further, to fill the skill gap, incentives to train local labour may be offered; and to facilitate financing for investors, creative solutions, like tripartite agreements, may be explored.

Accordingly, the chapter is organized as follows: the ensuing section describes the taxonomy, evolution, and factors responsible for the success of SEZs around the world. Section 7.3 then sheds light on Pakistan’s experience with industrial clusters and EPZs, as well as the current structure of SEZs in the country. Section 7.4 highlights some of the key challenges to SEZ growth in Pakistan, followed by policy options as a way forward for the SEZs (Section 7.5). Final remarks in Section 7.6 conclude the chapter.

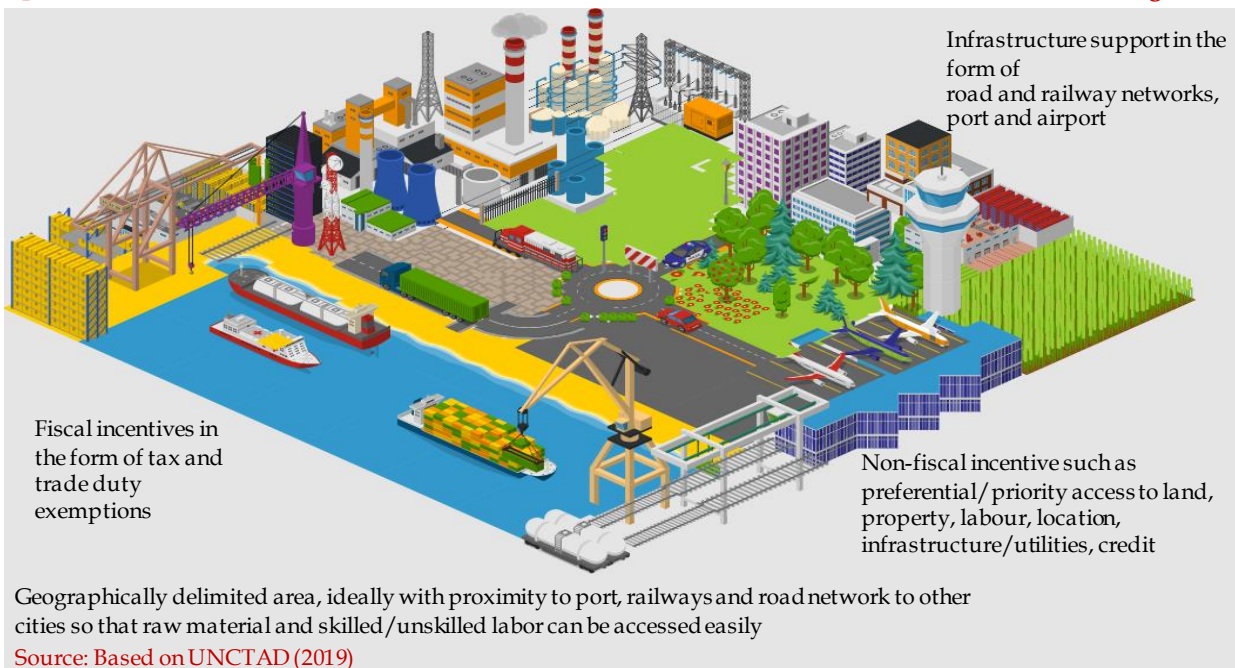
## 7.2 Taxonomy, Evolution, & Factors of Success

As an umbrella term, SEZ encompass several types of industrial and non-industrial business clusters, which countries have been experimenting with over many decades while eyeing distinct objectives (Figure 7.3). Some countries offer duty-free areas with warehousing, storage, and distribution facilities to traders; these are termed as Free Trade Zones (FTZs). Others have established Export Processing Zones, which allow enterprises to operate in free-trade conditions, and offer incentives like duty-free imports of plant, machinery, and raw materials for manufacturing export items.

Similarly, some countries set up Industrial Parks/Industrial Zones and Industrial Estates as sites that provide a broad set of facilities, like roads, transportation, public utilities and some common amenities that can be shared by a group of manufacturers and investors, albeit without fiscal or other incentives (Figure 7.4).<sup>8</sup> Increasingly, the term also includes technology development zones for high-tech

### Special Economic Zones: Some Basic Features

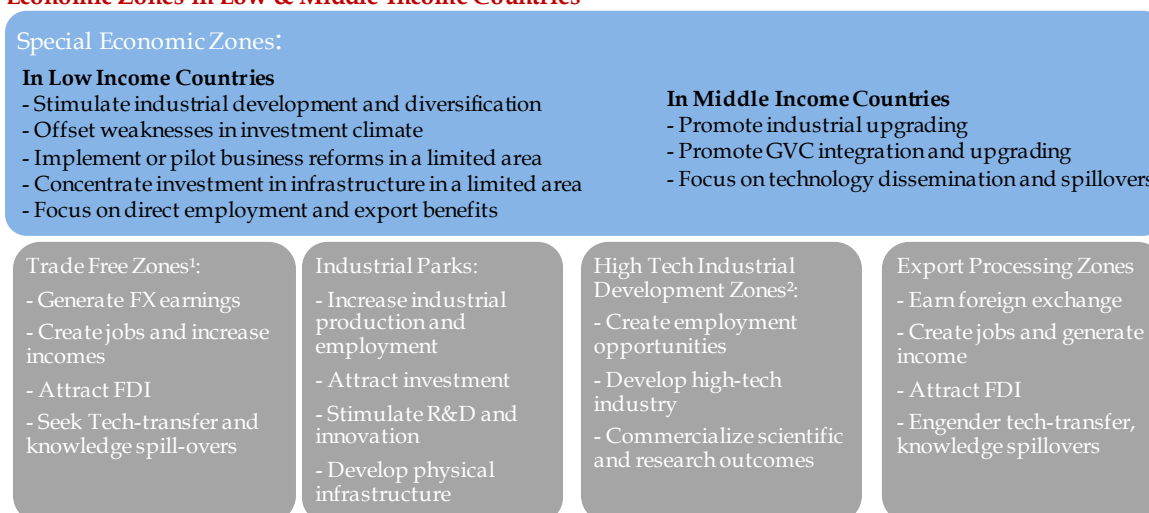
Figure 7.3



<sup>8</sup> Source: UNIDO (1997). *Guidelines for the Establishment of Industrial Estates in Developing Countries*. Vienna: UNIDO.

**The Objectives Governments Seek to Achieve by Establishing Different Types of Economic Zones in Low & Middle Income Countries**

**Figure 7.4**



Source: <sup>1</sup>UNESCAP (2005). *Free Trade Zone and Port Hinterland Development*. Bangkok: UNESCAP  
<sup>2</sup>S. Liang (2011). *Physical Planning Strategies of National High-Technology Industrial Development Zones in China*. Publicly Accessible Penn Dissertations 989. Pennsylvania: University of Pennsylvania.  
 UNCTAD (2019). *World Investment Report 2019*. Geneva: UNCTAD

industries, with a focus on industrial upgradation and creation of new industries, as well as health, tourism and education clusters.<sup>9</sup>

According to a 2019 survey, there were no less than 82 different terms to designate zones that were being used by countries to describe often similar types of zones in their legislation and publicity materials.<sup>10</sup> However, most of these were clubbed under the generic label of SEZs. In Pakistan too, there have been instances in the past (before the passage of the SEZ Act 2012) when industrial estates, such as Gadoon Amazai, were loosely termed as SEZs by researchers and investment promotional agencies alike.<sup>11</sup>

The term SEZ has only been recently defined, even though as an umbrella term the concept has existed for decades. The first notable

definition was used in a World Bank paper in 2015, where an SEZ was defined as an area with geographically delimited boundaries, administered by a single management/authority, offering fiscal incentives, such as reduced taxes and duties, and non-fiscal benefits like access to land, labour, utilities, infrastructure and administrative support.<sup>12</sup>

In 2019, the UNCTAD defined SEZs as “geographically delimited areas within which governments facilitate industrial activity through fiscal and regulatory incentives and infrastructure support”.<sup>13</sup> It was only after this definition that it became less common in academic work and publications to conflate SEZs with Free Trade Zones and Export Processing Zones.<sup>14</sup>

<sup>9</sup> World Investment Report, (2019). *Special Economic Zones*. Geneva: UNCTAD.

<sup>10</sup> F. Bost (2019). “Special Economic Zones: Methodological Issues and Definition”, *Transnational Corporations Journal*, Vol. 26, No. 2.

<sup>11</sup> One such example is A.A. Burki, K.A. Munir, M.A. Khan, M.U. Khan, A. Faheem, A. Khalid, and S. T. Husaain (2011). *Industrial Policy, Its Spatial Aspects and Cluster Development in Pakistan*. Consultant Report for WB. Lahore: LUMS.

<sup>12</sup> Z. Douglas (2015). *Global Experiences with Special Economic Zones Focus on China and Africa*. Policy Research Working Paper 7240, Washington DC: WB.

<sup>13</sup> World Investment Report (2019). *Special Economic Zones*. Geneva: UNCTAD

<sup>14</sup> F. Bost (2019). “Special Economic Zones: Methodological Issues and Definition”, *Transnational Corporations Journal*, Vol. 26, No. 2.

In other words, an SEZ, especially in developing economies, is envisaged to be an island of excellence in a sea of weak governance and insufficient infrastructure. Industrial Estates, on the other hand, may be geographically delimited and may even offer basic infrastructure, but they do not offer special regulatory regimes for fiscal, land, labour and utilities. Likewise, EPZs are also geographically demarcated areas, often with exemptions from custom duties and local labour laws, but with strict conditions preventing zone enterprises from domestic sales.

### *Evolution of SEZs*

Free economic zones have existed for over a millennium. The most ancient economic zones existed in the form of free ports that used to facilitate free trading activities.<sup>15</sup> In the modern era, initially, countries built FTZs to facilitate trade; however, the goal of industrialization and exports led to the formation of manufacturing enterprises within FTZs. This, in turn, led to the novel idea of Export Processing Zones. Over time, countries started experimenting with various forms of zones, the most promising of which were tailored in China.

### *Chinese SEZs; promising example of transition:*

China established four zones in two provinces - Guangdong and Fujian - in 1980. After four years, the country declared 14 coastal cities as 'Economic and Technical Development Zones (ETDZs)' with incentives similar to those for modern-day SEZs. The provinces with these zones attracted around 70 percent of total FDI in China during 1979-1991.<sup>16</sup>

The country also progressively transitioned to High-tech Industrial Development Zones (HIDZs), which promoted technology and

innovation. According to UNCTAD (2019), China alone has an estimated 47 percent share in total SEZs around the world. However, the Chinese model is unique, given its decentralized management structure, where a committee formed by the local government has enough powers to approve FDI projects (within certain limits) as well as regulate land and approve infrastructure improvements.<sup>17</sup>

### *SEZ growth, especially in developing countries:*

Following the success of China, SEZs became a popular tool for investment policy. From 176 SEZs in 47 countries in 1986, the total number of SEZs increased to 3,500 across 130 countries in 2006. By 2018, this number had reached 5,400 SEZs in 147 countries, with another 500 new projects expected to be in the pipeline. Around 89 percent of all the economic zones are located in developing countries. For developing countries, SEZs offer an opportunity to experiment and introduce reforms, and provide supporting infrastructure on piecemeal basis, since it is often difficult for them to roll these out all at once across the country. In these countries, the governments initially adopted free trade and multi-activity zones, with the primary focus on labour-intensive and export-oriented industries. Eventually, however, they moved towards specialized, innovation-oriented and service sector-focused SEZs (Figure 7.5).<sup>18</sup>

### *Measuring Success*

A universal criterion to judge the performance of SEZs is a challenging task. This is because of three main reasons. First, the primary goal of a zone can vary, and a verdict on its success or failure will mainly depend on achieving that goal. For some countries, the goal may be to attract FDI; for others it may be to

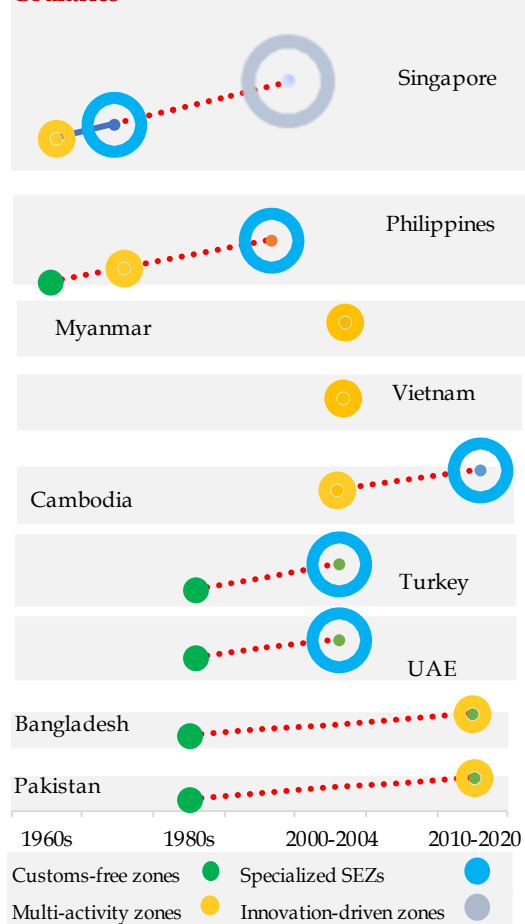
<sup>15</sup> H. Grubel (1982). "Towards a Theory of Free Economic Zones." *Weltwirtschaftliches Archiv*, 118(1): 39-61.

<sup>16</sup> Z. Zeng (2015). *Global experiences with special economic zones: focus on China and Africa*. Policy Research Working Paper Series 7240, Washington DC: WB; E. Graham (2004). "Do Export Processing Zones Attract FDI and its Benefits?" *International Economics and Economic Policy*, 1: 87-103.

<sup>17</sup> UNESCAP (2017). *Handbook on Policies, Promotion and Facilitation of Foreign Direct Investment for Sustainable Development in Asia and the Pacific*. Bangkok: UNESCAP.

<sup>18</sup> World Investment Report (2019). *Special Economic Zones*. Geneva: UNCTAD.

**Evolution of SEZs in Different Countries** **Figure 7.5**



Source: UNCTAD (2019)

experiment with different policy reforms.<sup>19</sup> The desired outcomes from SEZs are also evolving (Table 7.1).

Second, there are multiple types of SEZs with different focus areas, which makes it challenging for a single metric to judge their performance. For example, the same parameters cannot assess the performance of a high-tech zone and a free trade zone. Lastly, differences in management styles and compilation of statistics also make it difficult to measure the impact of SEZs in standardized

cross-country comparisons;<sup>20</sup> empirical studies on various facets of SEZs, such as their spillover onto the local economy, is scarce.<sup>21</sup>

Despite different characteristics and objectives, there are some broad parameters to help assess the effectiveness of SEZs. These parameters include linkages with domestic economy, technology transfer, and environmental impact. The common measures of success are the SEZs' contribution to exports, employment and FDI.

**Evolution of Special Economic Zones** **Table 7.1**

	Goals
<b>Zone 1.0</b>	FDI, exports, foreign exchange
<b>Zone 2.0</b>	Zone 1.0 + domestic linkage, bigger size, less reliant on fiscal incentives
<b>Zone 3.0</b>	Zone 2.0 + environmental and social development

Source: Zeng (2016)<sup>22</sup>

As documented in the World Investment Report 2019, current zone programs in China show that SEZs account for over 80 percent of cumulative FDI. In Vietnam that number is estimated to range between 60 and 70 percent, whereas in Malaysia, almost 90 per cent of total investment in SEZs is from foreign investors. In terms of exports, SEZs are estimated to contribute 31 percent to Mexico's total exports, 60 percent of the Philippines', 25 percent of Egypt's, and about 10 percent of India's. However, the economic impact and contribution of these zones, especially to FDI inflows, is hard to measure because of data scarcity. Countries and multilateral organizations do not track and consistently report key macroeconomic statistics separately for SEZs, whereas the fact that the consensus

<sup>19</sup> T. Farole (2011). *Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience*. Directions in Development Series - Trade. Washington, DC: WB.

<sup>20</sup> UNESCAP (2017). *Handbook on Policies, Promotion and Facilitation of Foreign Direct Investment for Sustainable Development in Asia and the Pacific*. Bangkok: UNESCAP.

<sup>21</sup> S. Frick and A. Rodrigues-Pose (2021). "Special Economic Zones and Sourcing Linkages with the Local Economy: Reality or Pipedream?", *European Journal of Development Research*. Journal no. 41287.

<sup>22</sup> D. Zeng (2016). *Special Economic Zones: Lessons from the Global Experience*. Private Enterprise Development in Low Income Countries, Synthesis Paper Series.

on the definition of SEZs is very recent adds to the problem of measurement.<sup>23</sup>

### **Factors of Success**

To create a successful special economic zone, a comprehensive strategy, based on multiple factors is required. Some of these observations, drawn from literature and experiences of other countries, are discussed below.

#### **Stated objectives and goals:**

A starting point for a successful SEZ is an explicitly stated clear set of objectives, which depends on the characteristics, comparative advantage, and location of that SEZ. The SEZs in China, which are amongst the world's most successful, have clear benchmarks and goals.<sup>24</sup> The identification of goals is crucial because they drive the overarching SEZ policy framework. For example, if the primary goal of an SEZ is to increase employment, then it would operate with a set of policies geared to attract labour-intensive industries. However, if the goal is to increase exports or transfer of technology, then the policy framework would reflect those objectives. Moreover, SEZs are more likely to be successful if the goals are aligned with the broader national industrial policy, followed by a practical actionable plan.<sup>25</sup>

#### **Establishing a robust regulatory framework:**

For SEZs to be successful, it is imperative to have separate laws and institutional setups governing SEZs within the national legal framework. For instance, China regulates SEZs with a decentralized structure comprising three layers: national laws

providing policy directives; provincial laws factoring varying conditions within provinces; and individual SEZ laws to account for the uniqueness of every SEZ.<sup>26</sup> Laws are also used as a tool to attract foreign investors by safeguarding their interests and streamlining ambiguities in zone operations. For instance, the law for SEZs in Turkmenistan guarantees protection to foreign investors from adverse effects caused by future changes in the regulations.<sup>27</sup> A law of this kind creates certainty for investors and allows them to plan for long-term investment.

South Korea's Special Act on Designation and Management of Free Economic Zones, 2017, is a good example of a regulation that clarifies the roles of relevant parties in an SEZ. It explicitly delineates the responsibilities for different governmental departments and management of the zone.<sup>28</sup> The law also contains legislation on the ways to improve the living standards for foreign investors; for example, Article 20 and 22 provide for foreign language services and education system for foreigners.

Another example of a law increasing SEZs' efficiency is the Bangladesh Economic Zones Act, 2010. Article 13(d) of the law empowers the government to exempt a zone from the Electricity Act, 1910, which helped reduce the average time for a firm to obtain electricity connection within the SEZ to 31 days, from 100 days for firms outside the zone.<sup>29</sup> Article 13(h) allows exemptions from the Building Construction Act 1952, and the number of days to get a construction permit is two days, whereas it is 68 days for a firm outside the SEZ.

<sup>23</sup> World Investment Report (2019), Special Economic Zones. Geneva: UNCTAD.

<sup>24</sup> D.Z. Zeng (2015). *Global Experiences with Special Economic Zones: Focus on China and Africa*. Policy Research Working Paper No. 7240. Washington, DC: WB.

<sup>25</sup> A. Aggarwal (2019). "SEZs and Economic Transformation: Towards a Developmental Approach", *Transnational Corporations*, 26(2), 27-47.

<sup>26</sup> H.R. Zheng (1987). "Law and Policy of China's Special Economic Zones and Coastal Cities", *NYLS Journal of International and Comparative Law*. Vol. 8: No. 2.

<sup>27</sup> World Investment Report. (2019). *Special Economic Zones*. Geneva: UNCTAD

<sup>28</sup> Source: Korean Legislation Research Institute:

([www.elaw.klri.re.kr/eng\\_service/lawView.do?hseq=46782&lang=ENG](http://www.elaw.klri.re.kr/eng_service/lawView.do?hseq=46782&lang=ENG))

<sup>29</sup> A.K. Khandelwal and M. Teachout (2016). *Special Economic Zones for Myanmar*. IGC Policy Note. London: IGC

### *Business friendly environment:*

Another key factor of success is an enabling business environment with One-Stop Shop (OSS) or single-window operation. Here, the key driver of success is not merely the assembly of representatives of all regulatory institutions under one roof to fast-track registration, licensing, and other regulatory requirements, but more importantly, it is the explicitly notified preferential timelines and simplified procedures for SEZs that contribute to an SEZ's success.<sup>30</sup>

### *Infrastructure:*

The infrastructure – encompassing roads, railways, water, electricity, health, education, and training facilities for zone residents – is a critical success factor. Khadaroo and Seetanah (2008), found positive correlation between transport infrastructure and FDI inflows, modeling their analysis on Mauritius and applying it to 20 other African countries.<sup>31</sup> All the successful zones in Dubai, Singapore, China and Malaysia have quality infrastructure, whereas zones in South Korea also provide recreation facilities for foreign investors, along with state-of-the-art educational and medical services.<sup>32</sup>

### *Fiscal incentives:*

Fiscal incentives like tax holidays, exemptions on dividends and income tax, and duty-free imports, positively correlate with the zone's performance and help it attract initial investment.<sup>33</sup> However, it is important to note

that fiscal incentives are usually effective for a limited period. In the long run, it is the locational advantage and provision of infrastructure and other services to the SEZ that makes it successful and keeps industries from moving out of the SEZ once fiscal incentives come to an end.<sup>34</sup>

### *Mechanism for dispute resolutions:*

This is an important feature behind the success of several SEZ, because it helps avoid escalation of disagreements and lengthy litigation.<sup>35</sup> Special courts or arbitration tribunals set up especially for swifter resolution of disputes related to zone enterprises can be attractive for foreign investors. The resolution of cases in a short amount of time becomes crucial for countries where the judicial system is overburdened. Dubai's Dispute Resolution Authority, the Dubai International Financial Centre (DIFC), is one such example of a special mechanism formed for resolving cases within SEZs.<sup>36</sup>

### *Location, competitive advantage, and zone size:*

Strategic location is also very crucial for zone success. Frick et al. (2018), who use data for 255 zones from 22 countries, show a negative correlation between SEZ growth and distance from major ports, cities, and markets.<sup>37</sup> Moreover, while calculating the zone growth for the first five years of zones operations, it also shows that larger zones have more potential to succeed. Also, the location

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<sup>30</sup> T. Farole, C. Baissac and J. Gauthier (2013). *Special Economic Zones: A Guidance Framework for Policymaking*. Draft. Washington DC: World Bank

<sup>31</sup> A. J. Khadaroo and B. Seetanah (2010). "Transport Infrastructure and Foreign Direct Investment". *Journal of International Development*, 22, 103-123.

<sup>32</sup> Source: Korean Free Economic Zone ([www.fezone.go.kr/global/en/why/environment.do](http://www.fezone.go.kr/global/en/why/environment.do)).

<sup>33</sup> A. Aggarwal (2005). *Performance of export processing zones: a comparative analysis of India, Sri Lanka and Bangladesh*. Working Paper No. 155. New Delhi: Indian Council for Research on International Economic Relations.

<sup>34</sup> T. Farole (2011). *Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience*. Directions in Development Series- Trade. Washington, DC: World Bank.

<sup>35</sup> T. Cheng (2019). "From Special Economic Zones to Greater Special Economic Region-Hong Kong Special Administrative Region as a Model for Legal Infrastructure Design", *Transnational Corporations Journal*, Vol. 26 (3).

<sup>36</sup> D.Z. Sharar, and M.A. Khulaifi (2016). "The Courts in Qatar Financial Centre and Dubai International Financial Centre: A Comparative Analysis", *Hong Kong Law Journal*, Volume 46, Part 2.

<sup>37</sup> S. A. Frick, R. Andrés and W. Michael (2018). *Towards economically dynamic Special Economic Zones in emerging countries*. Papers in Evolutionary Economic Geography (PEEG) 1816, Utrecht: Utrecht University.

decision should be taken in consideration of the availability of skilled labour and raw materials.<sup>38</sup>

### 7.3 Economic Zones: Review of Pakistan's Experience

The concept of delimited industrial estates in Pakistan goes back to its earliest economic policies. In the first five-year national development plan (1955-60), the government had adopted the idea of enabling industrialization through designated locations featuring reasonably priced land, which was furnished with roads, water, power, sewerage, telephone lines and rail sidings.<sup>39</sup> This was in accordance with other developing economies, such as Thailand, the Philippines and Singapore, which set up Industrial Estates in the same era as a steppingstone for industrialization, and subsequently rapid economic growth.<sup>40</sup>

#### Setting up Industrial Estates at Provincial Level:

By the start of the 1970s, all the provinces began to set up Industrial Estates (IEs), mostly under the umbrella of their respective small-scale industries corporations. Based on locally available factors of production, these IEs were initially established to promote the formation of clusters in small and cottage industries by facilitating them with required infrastructure and utilities. Some of these IEs also offered fiscal incentives in the form of income tax holidays and exemption from customs duties on machinery imports; these incentives varied

across IEs, subject to the level of development in the region.<sup>41</sup>

Some of the earlier estates became hubs for different industries. For example, the manufacturing of surgical instruments, leather garments, and sports items successfully nurtured in Sialkot; whereas household appliances, machinery, foundry, and agriculture tools industries found their footings within Gujranwala IEs (IE-I, IE-II and IE-III).<sup>42</sup> Meanwhile, few IEs befitted the large-scale manufacturing sector; for instance, Hub Industrial Trading Estate (HITE) attracted large automobile assembling units, auto vendors, as well as cement, textile spinning, food processing and light engineering clusters.<sup>43</sup>

Notwithstanding these success stories, several IEs were unable to attain maximum colonization, despite fiscal incentives. This is because some of the IEs could not deliver on the promise of utilities<sup>44</sup> and other required infrastructure; whereas others faced location disadvantages since the time they were set up.<sup>45</sup> Even when provincial governments established new IEs, private enterprises resisted moving in because of poor planning, inadequate industrial zoning, deficient infrastructure and exorbitant land prices.<sup>46</sup>

Another reason why several IEs did not succeed in subsequent years was real estate activities, which increased land prices and created disincentives for investments in industrial establishments in those IEs. Allottees of industrial lands in IEs kept holding on to the plots in anticipation of an

<sup>38</sup> A. Aggarwal (2005). *Performance of export processing zones: a comparative analysis of India, Sri Lanka and Bangladesh*. Working Paper No. 155 New Delhi: Indian Council for Research on International Economic Relations.

<sup>39</sup> First, Five Year Plan 1955-60, Planning Commission of Pakistan.

<sup>40</sup> ERIA Study Team (2016). 'The Development of Industrial Estates', in Nishimura, H., F. Kimura, M. Ambashi, and S. Keola (eds.), *Lao PDR at the Crossroads: Industrial Development Strategies 2016-2030*. ERIA Research Project Report 2015-2, Jakarta: ERIA, pp.61-98.

<sup>41</sup> H. Pasha and Z. Ismail (1988). "Determinants of Success of Industrial Estates in Pakistan", *Pakistan Economic and Social Review*, 26(1), 1-19.

<sup>42</sup> Punjab Small Scale Industries Corporation

<sup>43</sup> SMEDA, 'District Economic Profile Lasbela'

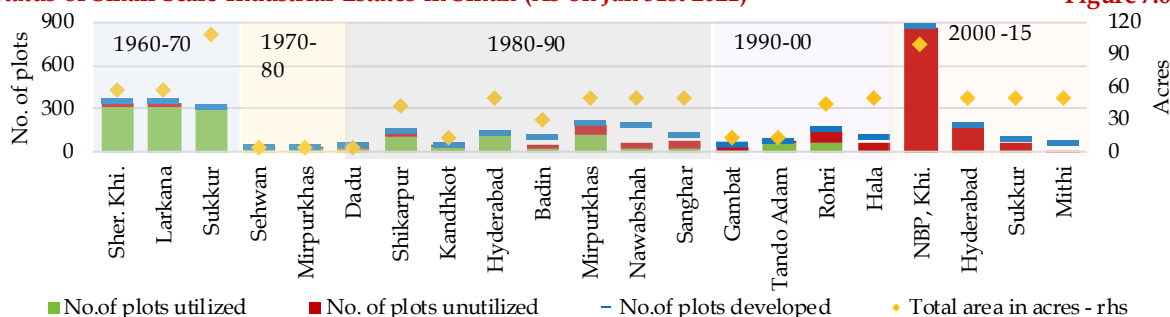
<sup>44</sup> According to the data compiled by Punjab Small Scale Industries Corporation, as of May 2021, 35 percent of IEs (7 out of 20) have been facing issues in supplying gas to industrial units

<sup>45</sup> H. Pasha and Z. Ismail (1988). "Determinants of Success of Industrial Estates in Pakistan", *Pakistan Economic and Social Review*, 26(1), 1-19.

<sup>46</sup> *Ibid* footnote 11

Status of Small Scale Industrial Estates in Sindh (As on Jan 31st 2021)

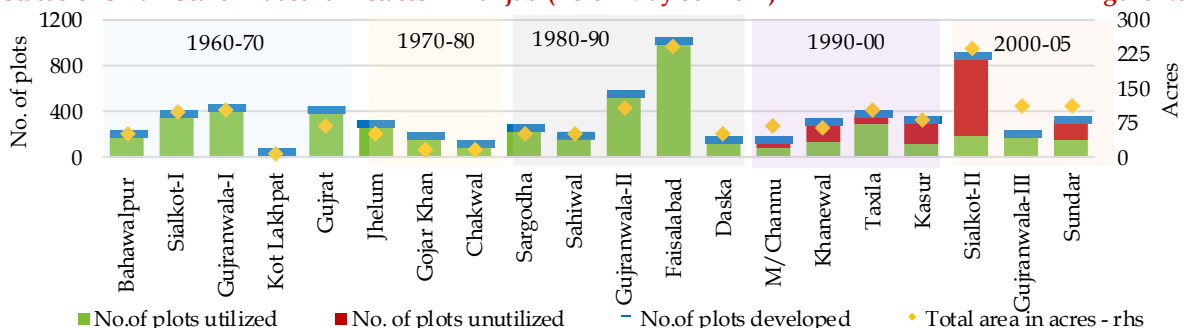
Figure 7.6a



Source: Sindh Small Scale Industries Corporation

Status of Small Scale Industrial Estates in Punjab (As on May 5th 2021)

Figure 7.6b



Source: Punjab Small Scale Industries Corporation

increase in land prices, instead of setting up industrial units. As a result, industrial plots were left unutilized. This trend was more prominent in the IEs established after the 1990s, including the estates located in Karachi, Hyderabad, Sialkot, Sukkur and Kasur (Figure 7.6a and 7.6b). Other IEs, such as the Gadoon Economic Zone, faced mass closure of industrial units, once tax holiday period came

to an end, sales tax exemptions were withdrawn and utility subsidies were removed (Figure 7.7).

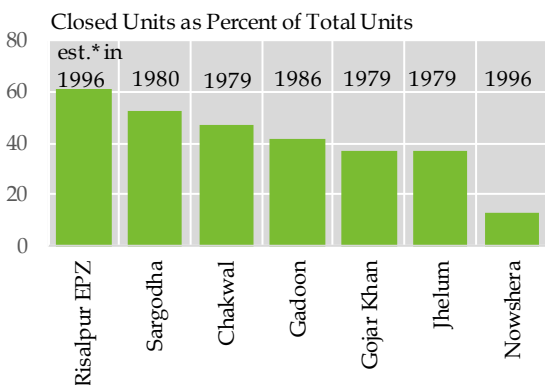
### The Era of EPZs:

By 1980, the government started to consider export processing zones (EPZ) as a policy tool to focus on export-led growth. Accordingly, the autonomous EPZ Authority (EPZA) was constituted via an ordinance in February 1980, with the mandate to plan, establish and run the EPZs.

The EPZs offer many incentives to businesses, including: duty-free import of machinery, equipment and materials; freedom from national import and foreign-exchange regulations; ease of repatriation of capital and profits; and exemption from sales tax on inputs, including electricity and gas.<sup>47</sup>

By FY20, the authority had developed seven EPZs across Pakistan. Of these, the Karachi EPZ is owned, developed and operated by the EPZA, whereas those in Gujranwala, Sialkot and Risalpur are owned, developed and operated by the respective provincial

Status of Closed Industrial Units in Different Industrial Estates Figure 7.7



\* established

Source: Punjab Small Industrial Estates, KPK Industrial Directory 2020 by KPK Economic Zones Development and Management Company

<sup>47</sup> Export Processing Zones Authority ([www.epza.gov.pk/incentives/](http://www.epza.gov.pk/incentives/)).

**The Status of Export Processing Zones**

**Table 7.2**

	Year of operation	Area Acre	Sectors/Products	Operating units	No. of workers as on Jun 2021	Exports Imports	
						Cumulative flows* (in million US\$)	
Karachi EPZ	1981	305	Multiple	266	30,000	7,088	4,442.6
Risalpur EPZ	2002	92	Multiple	28	1,000	24.3	24.3
Gujranwala EPZ	2004	113	Multiple	13	100	5.8	4.6
Sialkot EPZ	2005	238	Multiple	37	1,000	72.7	53.3
Tuwairqi Steel Mill	2006	220	Steel billets/DRI	1		29.3	182.8
Saindak EPZ	2007	1284	Blister copper	1	1,500	2,445.8	994
Duddar EPZ	2009	1500	Zinc and lead	1	500	296.8	189.5
<b>Total</b>		<b>3752</b>		<b>310</b>	<b>34,100</b>	<b>9,962.6</b>	<b>5,891.1</b>

\* Since respective year of operation.

Source: Export Processing Zone Authority, as on June 30th 2021

authorities. The latter are under joint venture (JV) agreements,<sup>48</sup> where the EPZA’s role is limited to few activities, such as issuing NOCs for import/exports, and income tax collection. In addition to these multi-party EPZs, three single-enterprise EPZs have also been established: Saindak EPZ, Duddar EPZ, and Tuwairqi Steel Mill.

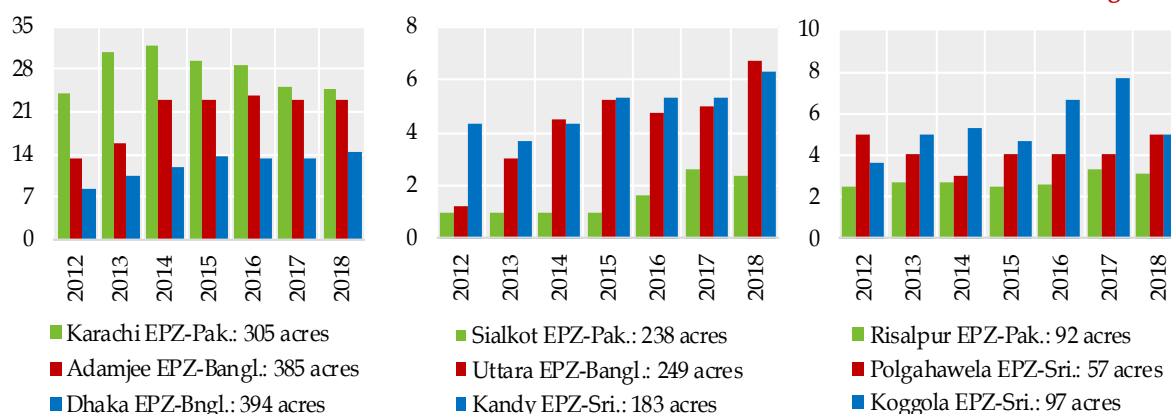
The performance of EPZs in Pakistan has not been significant in comparison to those in the region. EPZs in Bangladesh, for instance, set up under Bangladesh Export Processing Act of 1980, have been able to attract a total investment of US\$ 5.2 billion since the first EPZ commenced operations in 1983. Between 2009 and 2019, US\$ 60.1 billion worth of exports were contributed by Bangladesh’s EPZs, which equals 18.5 percent of total merchandise exports from the country during

this period. These EPZs produce goods for multiple international brands, including Nike, Reebok, Mother Care, Nikon, Sony, and Mitsubishi. As of 2019, these zones provided direct employment to almost half a million workers.<sup>49</sup>

In contrast, exports by EPZs in Pakistan since their inception to-date totaled around \$10 billion, or 1.9 percent of the country’s overall merchandise exports during this period (Table 7.2). About 70 percent of these exports came from a single EPZ – Karachi EPZ, where 49 percent of exports in FY21 (FY20: 44 percent) came from reprocessing worn (used) clothing. Exports by other EPZs, such as Risalpur, Gujranwala and Sialkot, have been much less. Insufficient activity in Pakistan’s EPZs is also reflected from the Night Time Activity dataset

**The Comparison of Night Time Activity Around Global EPZs**

**Figure 7.8**



Source: Devseed project by World Bank, for complete reference see foot note 50

<sup>48</sup> Gujranwala and Silkot EPZ were developed under joint venture (JV) with Punjab Small Industries Corporation whereas Risalpur was developed under JV with Sarhad Development Authority.

<sup>49</sup> Bangladesh Export Processing Zones Authority, Annual Report (2018-19).

in comparison to similar EPZs in other developing countries (**Figure 7.8**).<sup>50</sup>

Anecdotal evidence suggests that poor availability of infrastructure, utilities and absence of an OSS prevented EPZs set up under JVs in the country from taking off. Real estate activities were another reason why other multiparty EPZs were not successful. Unlike the Karachi EPZ where industrial land has been given on annual ground rent, the land in other multiparty EPZs were sold to prospective investors without putting in place effective safeguards to discourage real estate activities.

### **The Emergence of SEZs:**

In the wake of the underlying issues that hindered the success of IEs and EPZs, Pakistan adopted the SEZ model of industrialization in 2012 with the passage of the Special Economic Zone Act 2012. The Act allows federal and provincial governments to set up SEZs either in the public or private sector, or in public-private partnership (PPP) mode. The first SEZs under the Act were notified around 2015-16, coinciding with a major amendment in the law. However, it was not until 2019 that regulatory activities and notification of SEZs picked up (**Figure 7.9**).

The SEZ Act 2012 originally treated the SEZs as extra-territorial zones outside the customs area of Pakistan,<sup>51</sup> which meant that purchase of goods produced inside the SEZ by domestic buyers outside the SEZ would be subject to import duties and taxes. This limited the zones' attractiveness to local and foreign investors, who wanted to cater to the growing

domestic demand. Accordingly, the Act was amended in 2015, whereby the SEZs were brought into the country's customs territory. In addition to this amendment, a host of rules and regulations have been passed over the years to streamline the regulatory framework for the SEZs.

Currently, 22 SEZs have been approved, of which 21 have been notified.<sup>52</sup> Thirteen of these 22 approved SEZs had previously existed as Industrial Estates and Industrial Parks, whereas nine SEZs have been approved under CPEC, of which four have been given priority status.<sup>53</sup>

From the developers' perspective, a majority of the SEZs are by the public sector development companies, two are in public-private partnership mode,<sup>54</sup> and three are private sector SEZs, of which two are sole enterprise SEZs. However, two more private sector SEZs are in the pipeline.<sup>55</sup> The province-wise breakdown shows that Punjab hosts 10 SEZs, six are located in Sindh, three in Balochistan, two in Khyber Pakhtunkhwa, and one in Islamabad. As of June 2021, the notified SEZs were at different stages of development, and none of them were completely colonized with fully operational zone enterprises.

The latest available data suggests that the 22 approved SEZs cover more than 15,000 acres; plot demarcation has been completed for 11 SEZs, and more than 3,000 plots have been demarcated so far.<sup>56</sup> Per acre price of industrial plots varies from Rs 3.0 million (in Khairpur) to Rs 65 million (in Korangi Creek IP), depending on the costs of land acquisition

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<sup>50</sup> Night Time Activity data captures nightlight images using satellites. The brightness or radiance in these images for the observed SEZ site boundaries have been used as a proxy to determine the consumption of electricity in these SEZs (WB).

<sup>51</sup> Customs area refers to an area in which imported goods or goods for export are ordinarily kept before clearance by the customs authorities.

<sup>52</sup> Dhabeji SEZ has been given in-principle approval; it has not been notified.

<sup>53</sup> These four are Rashakai SEZ, Allama Iqbal Industrial City, Dhabheji SEZ and Bostan SEZ (Source: Economic Survey of Pakistan 2020-21).

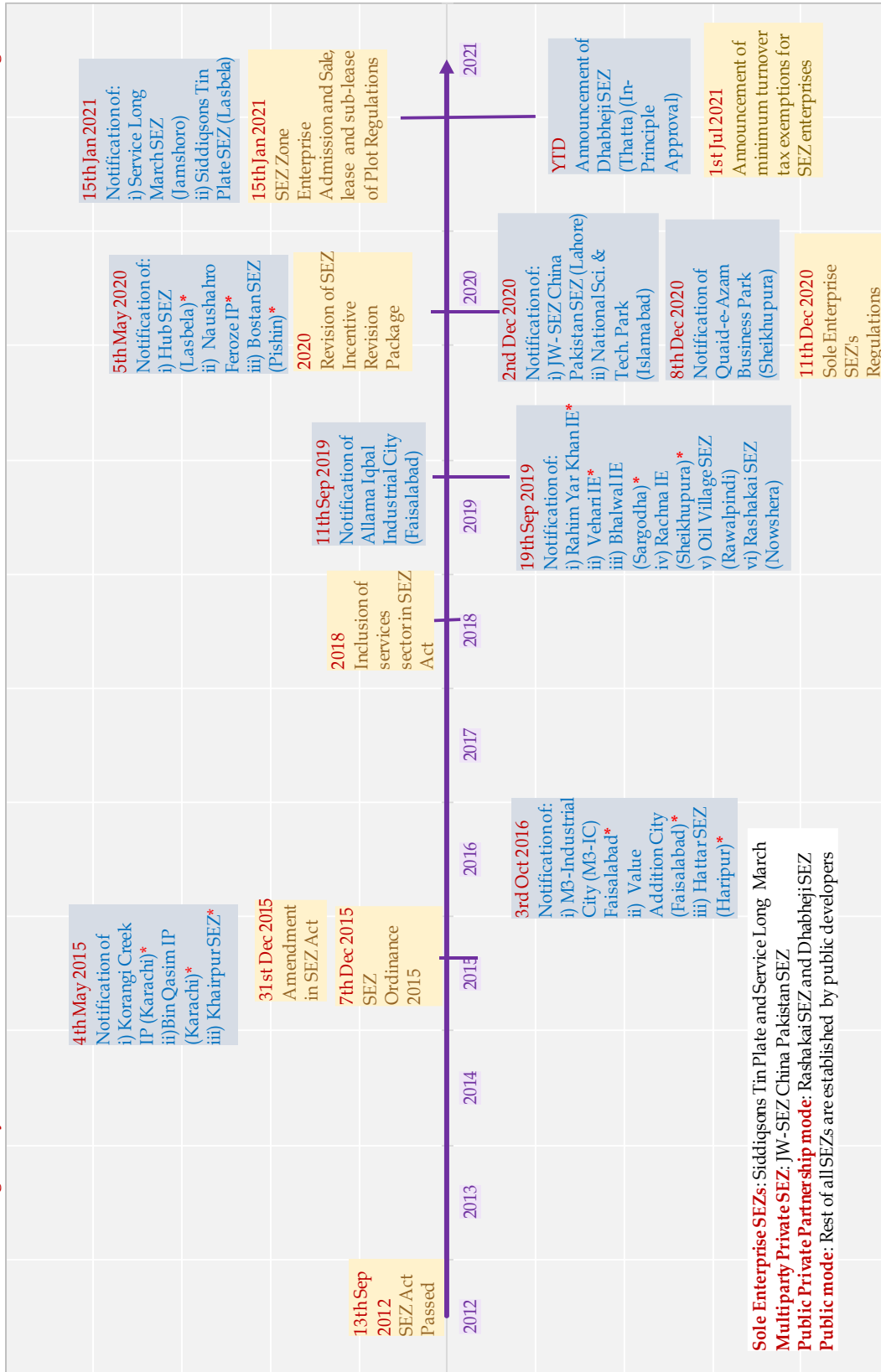
<sup>54</sup> These are Rashakai and Dhabeji SEZs.

<sup>55</sup> These are: Zameen SEZ and Roshan SEZ. Source: BOI Annual Report (2019).

<sup>56</sup> Source: BoI. ([www.invest.gov.pk/sez](http://www.invest.gov.pk/sez))

Figure 7.9

Timeline of SEZs Regulatory Framework and Notification of SEZs



**Sole Enterprise SEZs:** Siddiqsons Tin Plate and Service Long March  
**Multiparty Private SEZ:** JW-SEZ China Pakistan SEZ  
**Public Private Partnership mode:** Rashakai SEZ and Dhabheji SEZ  
**Public mode:** Rest of all SEZs are established by public developers

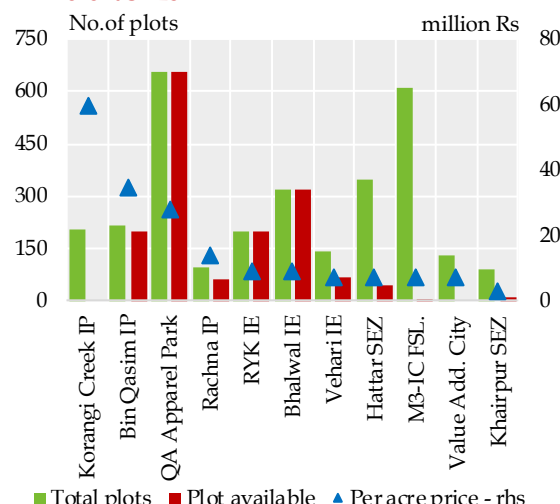
\* shows the SEZ previously existed as an Industrial Estate  
 Source: Board of Investment, Pakistan Economic Survey 2019-20

and development. Around 100 percent of the plots have been sold in three SEZs (Korangi Creek IP, M3-IC, and Value Addition City); and nearly 90 percent of the plots in Hattar and Khairpur SEZs have also been sold (Figure 7.10), whereas others are at different stages of sale.

From geographical perspective, these SEZs are mostly located near the coastal areas of Sindh, - i.e., in proximity of less than 100 kilometers - or in northern Punjab (Figure 7.11). Most of the approved SEZs are located in districts with relatively better multidimensional poverty index (MPI) scores, which in the absence of other detailed district-wise information may be construed as a proxy for the state of human development in those districts, since the MPI is based on education, health and standard of living indicators.

However, some SEZs are located in districts with poor MPI scores. This presents both an opportunity and a challenge. The opportunity exists because the SEZs have found to have had positive impact on the incomes of individuals and businesses located in the surrounding areas of the SEZ<sup>57</sup>, with measurable impact up to a distance of 50 kilometers.<sup>58</sup> A signature example of this is Shenzhen, China, which became a major manufacturing base from a fishing village after an SEZ was set up in the region.<sup>59</sup> The challenge, however, stems from the availability of skilled labour, given poor literacy rates in some districts. This is because

**Status of Plots and Price in Different SEZs** **Figure 7.10**



Source: Board of Investment website, accessed on August 8th, 2021

the availability of skilled labour is often more critical to the success of SEZs than fiscal incentives.<sup>60</sup>

In comparison to SEZs in the region, where some SEZs in China are province-sized,<sup>61</sup> the size of Pakistan's approved SEZs so far is small, with M3-Industrial City, Faisalabad being the largest SEZ with a size of 4,356 acres, and Naushehro Feroze being the smallest manufacturing SEZ with a size of 80 acres (Figure 7.12)<sup>62</sup>. However, the Punjab Industrial Estates Development & Management Company plans to set up a 10,000-acre SEZ at Pind Dadan Khan, which, if approved would be two-thirds of total acreage currently under approved SEZs in Pakistan.<sup>63</sup>

<sup>57</sup> J. Wang (2013). "The Economic Impact of Special Economic Zones: Evidence from Chinese Municipalities", *Journal of Development Economics*, p. 133-147, and P. Ciżkowicz, M. Ciżkowicz-Pękała, P. Pękała and A. Rzońca (2015). *The effects of special economic zones on employment and investment: spatial panel modelling perspective*. NBP Working Paper No. 208. Warsaw: Narodowy Bank Polski, Economic Research Department.

<sup>58</sup> World Bank (2017). *Special Economic Zones: An Operational Review of Their Impacts*. Economic and Sector Work (ESW) Studies. Washington, D.C.: WB

<sup>59</sup> T. Cheng (2019). "From Special Economic Zones to Greater Special Economic Region - Hong Kong Special Administrative Region as a Model for Legal Infrastructure Design.", *Transnational Corporations Journal*, Vol. 26 (3).

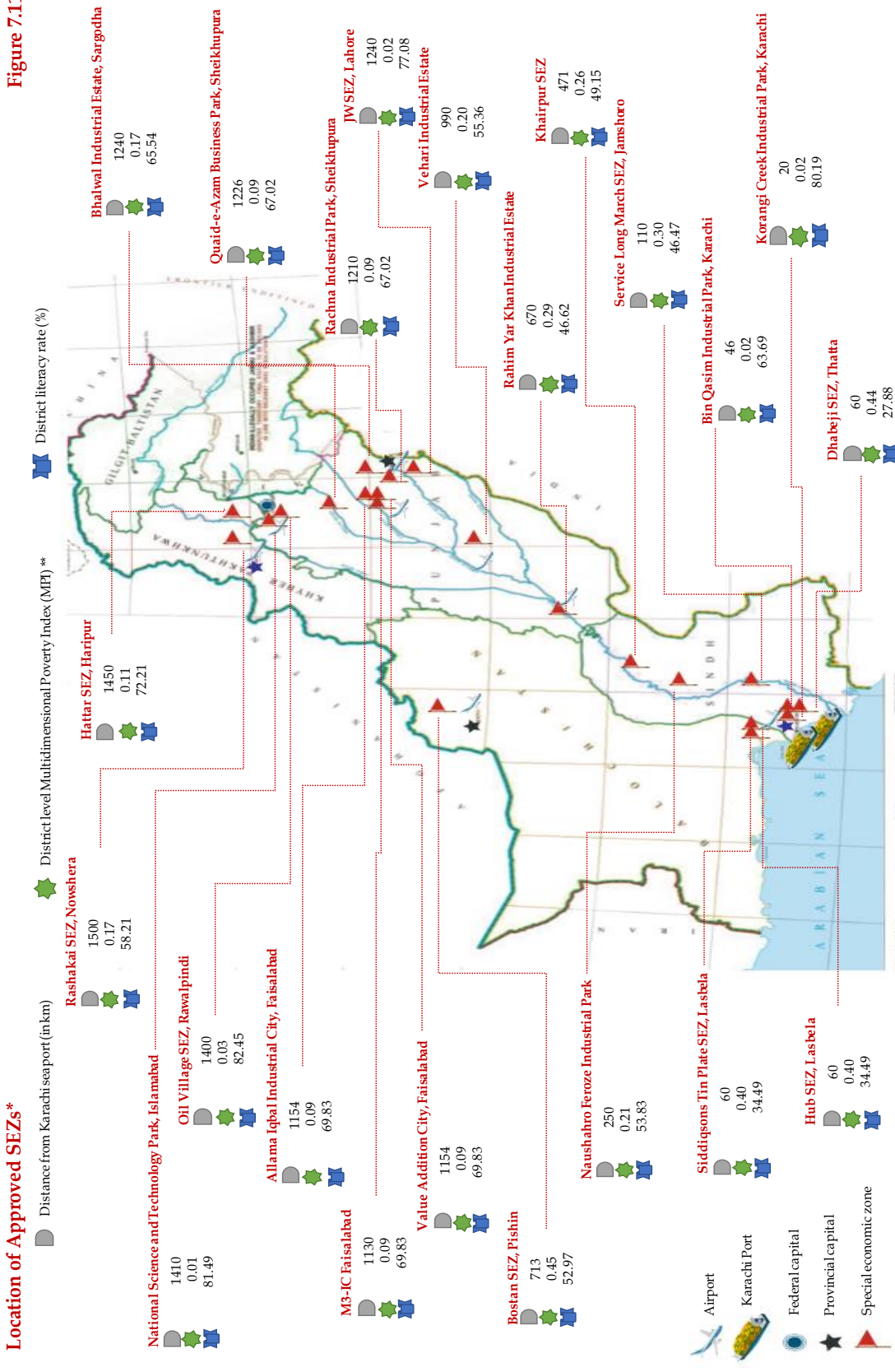
<sup>60</sup> UNESCAP (2017). *Handbook on Policies, Promotion and Facilitation of Foreign Direct Investment for Sustainable Development in Asia and the Pacific*. Bangkok: UNESCAP

<sup>61</sup> World Investment Report. (2019). *Special Economic Zones*. Geneva: UNCTAD

<sup>62</sup> The average size of Pakistan's SEZs in Figure 7.12 is the average of all approved SEZs, as of June 2021. However, the average size of SEZs of other countries are indicative in nature. These averages are calculated from the data of a subset of regional SEZs published by the World Bank in April 2021 under its project (P172858). This is the latest publicly available cross-country comparison of a sub-set of SEZs, whose total number is estimated to be more than 5,000 across the world.

<sup>63</sup> Punjab Industries Sector Plan 2018, Promoting Industrial Development and Investment, Government of Punjab 162

Figure 7.11

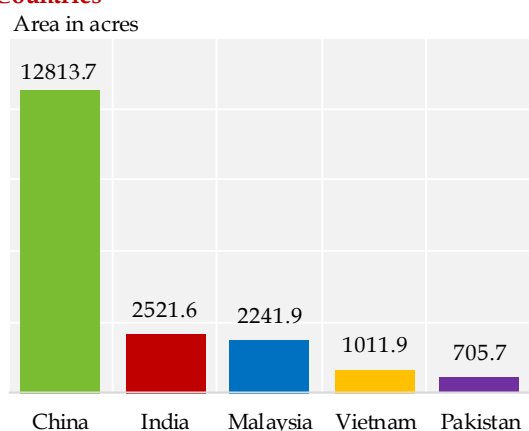


\* Approved as of June 30, 2021  
 \*\* MPI is a multi-dimensional measure of poverty, calculated on that basis of education, health and standard of living. It is measured on a scorecard of 0 to 1 where 0 is the best possible score, and 1 is the worst possible score.  
 Source: Map of Pakistan - Survey General of Pakistan; List of approved SEZs - Board of Investment; Distance between Karachi port and SEZs - Google Maps; Pakistan - Bureau of Statistics; and Multidimensional Poverty in Pakistan - Planning Commission (2017)

**Comparison of Fiscal Incentive Structures Across SEZs in Different Countries****Table 7.3**

	Vietnam	India	Indonesia	Bangladesh	Pakistan
Developer incentive	No established framework	Yes	Yes	Yes	Yes
Type of corporate tax exemption	Abs. exemp.	Abs. exemp.	Depends on firm qualifications	Abs. exemp.	Abs. exemp.
Corporate tax exemption	100%	100%	20-100%	100%	100%
Duration of corporate tax exemption	4 years	5 years	5 - 15 years	2 years	10 years
Exemption on					
Withholding tax	0%	0%	0%	50%	0%
Property/ land tax	Land use tax postponed; depreciation of fixed asset at double rate	0%	Partial reduction in property tax	50%	0%
VAT/Sales tax	0%	100% exempt from sales tax (central and state)	100% exempt from VAT, luxury sales tax, and excise tax on raw materials	80% exempt from utility consumption tax	0%
Import duty on capex	100%	100%	0%	100%	100%
Import duty on input	0%	100%	0%	100%	0%
Capex duration	One-time	Perpetual	N/a	Perpetual	One-time
<i>Memorandum items</i>					
Legal framework year	2006	2005	2009	2010	2012
Minimum investment required	None	None	\$37mln	None	None
Standard corporate tax	20%	30%	25%	25%	29%

Source: World Bank 2017

**Average Size of SEZs in Different Countries** **Figure 7.12**

Source: Board of Investment and World Bank.

**Incentive Structure:**

The SEZ Act 2012 spells out different incentives for developers and zone enterprises. For zone developers, co-developers and zone enterprises, income tax is exempted for 10 years from the date of signing of the development agreement. Developers

and zone enterprises also have one-time exemption from all customs duties and taxes on the import of capital goods. In comparison to regional countries, the fiscal incentives for SEZs in Pakistan appear better on some parameters, such as the duration of corporate tax exemption. However, on other parameters, other countries offer better incentives, such as the duration of exemption on capital expenditures (capex). (Table 7.3).

**Performance Criteria:**

The SEZ Act 2012 and the ensuing rules and regulations do not stipulate specific economic or social policy parameters that zone enterprises must undertake at the time of filing an application on the SEZ MIS for the approval of SEZ Committee.

However, zone enterprises applying for Sole Enterprise SEZ must provide a host of undertakings. These include: investing at least

US\$50 million in the project,<sup>64</sup> of which at least 30 percent should be equity-financed; exporting at least US\$75 million in the first five years of operations;<sup>65</sup> ensuring net foreign exchange earnings after third year of commencement; giving 50 percent jobs to those residing in the district in which the SEZ is located; registering at least 200 employees with the EOBI; and providing entrepreneurship development training to locals under its vendor development plan. These conditions are relaxed for sole SEZ enterprises that invest in underdeveloped areas of the country or invest in top five importing sectors, the lists of which are identified in the regulations.<sup>66</sup>

### **Regulatory Structure:**

The SEZ regulatory framework is evolving, and the government continues to issue new regulations to deal with the emerging concerns and opportunities. For example, in December 2020, 'Sole Enterprise Special Economic Zone' regulations were formulated to allow large enterprises to develop SEZs solely for themselves, whereas in January 2021, 'Zone Enterprise Admission and Sale, Lease and Sub-Lease of Plot Regulations' were announced. The latter has helped increase SEZ activities and eliminate risks of real estate speculation by providing digital solution for approval of zones by the government, and allocating plots and zone enterprise status to enterprises within the zone (**Annexure-I**).

The regulatory structure for SEZs involves several organizational layers and actors. Brief description of each of these, and their roles and responsibilities, are discussed in **Table 7.4**, whereas the list of members of various regulatory bodies and committees are in **Annexure-II**.

## **7.4 Challenges to SEZ Growth in Pakistan**

Pakistan had a slow start to SEZs. As described in section 3, most regulatory developments and notifications of SEZs happened six years after the passage of the SEZ Act 2012. Even to date, there is no fully operational, completely-colonized SEZ in the country, albeit the number of SEZs has started to grow since the amendment in the law and the rolling out of new regulations.

It takes about two years from the conceptualization of an SEZ by a developer – public or private – to the preparation of its application documents (which includes market feasibility studies, master plans, development plans and other documents etc.) to its approval and official notification as an SEZ by the government. It then takes about another two years for the developer to develop the zone as per the development agreement, before it can admit zone enterprises. This entails both civil works (such as land leveling and provision of sewerage, roads) as well as supply of utilities infrastructure. Once a zone enterprise is admitted, it may take another two and a half years for setting up of the industrial unit, before the enterprise can commence operations. In total, it can take about six and a half years from the time an SEZ is conceptualized till it becomes fully colonized with operational zone enterprises.

Considering these indicative timelines, and the fact that most SEZs have been notified 2019 onward, things are appearing to be shaping up. Global experience suggests that the success or failure of SEZs can only be assessed after at least a decade of the SEZs becoming fully operational and sufficiently colonized.<sup>67</sup> Since the SEZs in Pakistan are still in development phase, it is early to evaluate their success or failure at present.

<sup>64</sup> In addition to cost of land acquisition and development

<sup>65</sup> Albeit, no less than \$7.5 million of exports each year

<sup>66</sup> Regulation 4 and 5, Sole Enterprise Special Economic Zone, Regulation 2020

<sup>67</sup> World Bank (2020). *Assessment of Special Economic Zones in Pakistan: Suggesting Steps towards Improved Performance*. Washington, D.C.: WB.

## Main Features of Regulatory Structure of SEZs

Table 7.4

Name of Organization/Committee	Description
<b>Board of Approval (BOA)</b>	Chaired by the Prime Minister, the BOA comprises top political, technical and business leadership of the country. Its main functions are: approval of regulations for implementation of the SEZ Act; approve or reject zone applications and development agreement; take decisions on policy issues; notify additional benefits for developers or zone enterprises as per law; and review annual reports by the SEZ Authorities.
<b>Approvals Committee</b>	This committee exercises the powers and responsibilities as delegated by the BOA, including the screening of zone applications.
<b>Board of Investment (BOI)</b>	Originally established as the federal Investment Promotion Agency (IPA), the BOI works as the Secretariat of the BOA and the Approvals Committee to implement the SEZs framework. It is a coordinating agency for all activities pertaining to SEZs, developers and zone enterprises; it processes applications for development of zones and submits them to BOA for its approval; and it also approves all development agreements proposed by SEZAs. The BOI is also the SEZ Authority for SEZs in the Islamabad Capital Territory.
<b>Provincial investment promotion agencies (IPAs)</b>	The responsibilities of provincial IPAs include assisting the concerned SEZ Authority in its overall operations, as well as facilitating developers and zone enterprises in various matters relating to the SEZ.
<b>SEZ Authority (SEZA)</b>	The Act requires SEZAs to be set up as the highest SEZ authority for a province. Its main responsibilities are: preparation of zone application; selection of developers; formulation of zone regulations; and liaison with federal and provincial government departments and organizations.
<b>SEZ Committee</b>	Chartered by the BOA for each SEZ, the SEZ Committee comprises representatives from the developer, the BOI, provincial IPAs, respective SEZA, and the relevant district government. The developer appoints the chairperson of the SEZ Committee, which in most cases is a representative from the developer itself. The SEZ Committee is responsible for examining and approving SEZ entry applications; providing certification of zone enterprises; oversight of enterprises; and coordinating with various government departments.
<b>Zone Enterprises</b>	A zone enterprise is an enterprise admitted to an SEZ by a developer through a detailed selection process involving the developer and the relevant SEZA, with the BOI as the monitoring authority. In the case of Sole Enterprise SEZ, the developer and the Zone Enterprise may be the same entities.
<b>Developer</b>	Developer means an enterprise which has entered into an agreement with the relevant SEZA to develop an SEZ. The development agreement is reviewed by the BOA.

Source: Special Economic Zones Act, 2012

However, certain challenges to the prospects of growth and success of SEZs in Pakistan require the attention of policymakers. This section sheds light on some of those challenges, where broader policy-oriented concerns will be in focus.<sup>68</sup>

### SEZ Policy & Objectives

Being the capstone of the Investment Policy 2013, the objective behind SEZs in Pakistan is stated to be a step towards ease of doing business and to stimulate industrial growth with quality infrastructure.<sup>69</sup> However, these are not clearly spelled out in the manner of a separate SEZ policy document.

Countries have a variety of objectives, from improving industrial growth, attracting FDI and job creation to supporting technology access and upgradation, skills transfer, and foreign exchange earnings (Table 7.5). Although global literature suggests that wide-ranging objectives are not always desirable because of the often-competing priorities, scarce resources, and a lack of dedicated organization to prepare detailed policy and regulatory framework, clearly spelled out objectives are nevertheless needed to guide policymaking, including design of regulations and incentives, site selection for SEZs, industry clusters, and the selection of zone enterprises.

At present, Pakistan has provisions for Special Economic Zones under the SEZ Act

<sup>68</sup> In the absence of publicly available market feasibility studies for each SEZ, it would be difficult to comment on the feasibility aspects vis-à-vis factors of production and marketability of goods produced inside the SEZs.

<sup>69</sup> Paras 1.4(b) & 4.1, Investment Policy 2013, Board of Investment of Pakistan

Summary of Stated SEZs Objectives

Table 7.5

	Jobs	Exports	FDI	Technology	Diversification	Upgrading	Foreign Exchange	Others
Bangladesh	✓	✓	✓	✓	✓	✓		✓
India		✓	✓					✓
Vietnam	✓		✓	✓				
Ghana	✓		✓	✓	✓		✓	✓
Kenya	✓		✓	✓	✓	✓	✓	✓
Nigeria	✓	✓	✓	✓		✓	✓	
Senegal	✓	✓	✓				✓	
Tanzania	✓	✓	✓	✓	✓	✓	✓	✓
South Africa			✓	✓	✓	✓		✓
Pakistan			✓					✓

Source: Based on review of individual country SEZ laws of Pakistan and South Africa; Farole T (2011), *Special economic zones in Africa: Comparing performance and learning from global experiences*

2012; Industrial Estates under provincial industries departments; and Special Technology Zones under the Special Technology Zones Authority Act (STZA) 2021.

Meanwhile, the Export Processing Zones have a separate authority, with plans to establish new zones under Export Processing Zones Authority Ordinance 1980. In addition, Gwadar Free Trade Zone is being set up under a separate concession agreement and does not come under the SEZ or the EPZ law, whereas under Digital Pakistan Policy,<sup>70</sup> the Ministry of IT & Telecom plans to recommend incentives for technology SEZs under the SEZ Act.

These investment policy instruments often overlap with each other. For instance, technology SEZs can be set up under the SEZ Act (like the recently set up SEZ called the National Science and Technology Park), as well as under the STZA. Likewise, separate from the Gwadar Free Zone, the EPZA is setting up a 1,000-acre Gwadar EPZ.<sup>71</sup> Similarly, at a time when SEZs are being promoted, the policy emphasis on EPZs adds complexity, considering that with the reduction in customs duties, EPZs (where imports are free) are not as attractive as

before.<sup>72</sup> In addition, there have also been instances when different budgetary measures have given special incentives to industries outside the SEZs, which erodes the special fiscal incentives provided to companies inside the SEZs.<sup>73</sup> While these overlapping instruments offer choices to prospective investors, they also compete for same investors, add complexity to governance, and may prevent SEZs from realizing their potential.

### One Stop Shop

Among the key policies and interventions that make a Special Economic Zone 'special' from the rest of the industrial areas is a business-friendly environment insulated from weak governance and overall difficulties of doing business that often mark developing countries. To that end, one stop shop (OSS), also known as one window operation, is a key intervention for zone enterprises. The OSS reduces delays and uncertainty around securing registrations, permits, licenses, and approvals as well as provision of public goods from multiple governmental agencies.

<sup>70</sup> Digital Pakistan Policy (2018), Ministry of Information Technology and Telecommunication ([www.moitt.gov.pk/SiteImage/Misc/files/DIGITAL%20PAKISTAN%20POLICY.pdf](http://www.moitt.gov.pk/SiteImage/Misc/files/DIGITAL%20PAKISTAN%20POLICY.pdf))

<sup>71</sup> According to EPZA, PC-1 has been submitted for 500 acres build through PSDP/CPEC funding, and financial and technical proposals have been invited for expression of interest for another 500 acres on build operate and transfer basis.

<sup>72</sup> *Ibid* footnote 11.

<sup>73</sup> For instance, government has exempted industrial units located in erstwhile FATA and PATA of federal excise levy. Source: Federal Board of Revenue (Circular no. 02 of 2021, titled "Finance Act, 2021 – Explanation of Important Amendments in Sales Taxes Act, 1990 and Federal Excise Act, 2005.")

As per the SEZ Act 2012, there are two layers of the OSS. The Board of Investment is stipulated to act as an OSS for liaison and facilitation between all federal ministries, authorities and agencies at one end and provincial SEZ Authorities, developers and zone enterprises at the other. As for coordination of developers and zone enterprises with relevant departments, authorities and agencies at provincial and local government level, the provincial SEZ Authorities are to act as a liaison and facilitating agency.<sup>74</sup> However, in both cases,

the OSS does not exist in true sense in any of the SEZs in Pakistan.

As far as plots inside the zone are concerned, it is the developer's responsibility to ensure the supply of gas, electricity, and other utilities to zone enterprises at the zero point of the plot, whereas the relevant provincial SEZ Authority is to ensure availability of public utilities to zero point of SEZ and serve as liaisons and facilitating agency.<sup>75</sup> At the same time, the SEZ Committee is to serve as the point of contact between the zone enterprise and utility

**Responsibility Matrix: Infrastructure, Utilities and Security**

**Figure 7.13a**

	Infrastructure and utilities			Co-ordinate with Federal Govt. (FG)/ Provincial Govt. (PG)			Facilitate interaction of Developer. & Enterprises.		
	Ensure services within vicinity	Build and/or operate/distribute within the zone	To SEZ zero point	To facilitate Developer	To facilitate Zone Enterprise		With all FG/PG	With PG/LG	
<b>Firefighting facilities</b>	SEZA	Developer					BOI	SEZA	
<b>Medical facilities</b>	SEZA	Developer					BOI	SEZA	
<b>Acad. &amp; voc. training fac.**</b>	SEZA	Developer					BOI	SEZA	
<b>Roads</b>		Developer	FG & PG	SEZA			BOI	SEZA	
<b>Electricity</b>		Developer	FG & PG	SEZA	SEZ Committee	SEZA	SEZ Committee	BOI	SEZA
<b>Natural gas</b>	SEZA*	Developer	FG & PG	SEZA	SEZ Committee	SEZA	SEZ Committee	BOI	SEZA
<b>Water</b>		Developer	FG or PG	SEZA	SEZ Committee	SEZA	SEZ Committee	BOI	SEZA
<b>Sewerage/ drainage</b>		Developer	FG or PG	SEZA	SEZ Committee	SEZA	SEZ Committee	BOI	SEZA
<b>Waste water treatment</b>		Developer			SEZ Committee	SEZA	SEZ Committee		SEZA
<b>Security</b>	SEZA/PG	Developer					BOI		

**Responsibility Matrix: Liaison among Different Agents**

**Figure 7.13b**

	Between FG and SEZA/Developer/Enterprise		Between PG/LG and Developer/Enterprise	
	BOI	SEZ Committee	SEZA	SEZ Committee
<b>Liaison for approvals/registration with regulators/tax authorities</b>				

\*SEZA obtains commitment from concerned gas pipeline company; \*\* Academic and vocational training facilities

FG: Federal government; PG: Provincial government, LG: Local government; BOI: Board of Investment; SEZA: Special Economic Zone .

Source: Special Economic Zone Act 2012 and Special Economic Zones Rules, 2013

<sup>74</sup> Section 29, SEZ Act 2012

<sup>75</sup> The zero point of an SEZ refers to the nodal point (in public goods delivery) which is the closest to the entry point of the SEZ. The zero point of a plot refers to the nodal point closest to the plot within the SEZ.

providers; facilitate between enterprises and government regulators and tax authorities; and assist zone enterprises in obtaining approvals and registrations (Figure 7.13).<sup>76</sup> This overlapping mandate and institutional fragmentation over responsibilities has caused delays in the provision of public goods needed by the SEZs.<sup>77</sup>

In practice, different developers are experimenting with different models. For instance, in the case of Khyber Pakhtunkhwa Economic Zones Development & Management Company, and Faisalabad Industrial Estate

Development & Management Company, the OSS is based on new hires by these development companies. However, unlike the recommended new hires model (Box 7.1), new hires in these development companies are not officially operating on behalf of any government department or regulator, and instead get things done through personal relations. The Punjab Industrial Estates Development & Management Company, on the other hand, had adopted the secondment model, albeit one where the deputed staff did not have authority to approve or reject

**Box 7.1: Three Models of OSS**

According to Mangal M. (2019), SEZs can be institutionalized under three operating models differentiated on the basis of responsibilities of the front and back offices and hiring needs. These models have been categorized as Secondment, New Hire and Front Desk only.

The **Secondment model** comprises a front office and a back office, which are located inside the zone; the back office comprises government representatives from different departments. In this model, the front office acts as an intermediary between the investor and the government ministries. The office receives the investor’s application for different permits and directs these applications to the back office. In the back office, different ministries depute their representatives to the SEZs, which are authorized to approve or reject the application. The decision is communicated to the front office, which then informs the investor. This model is cost-effective and does not need new hiring, but at the same time it may encompass bureaucratic hurdles, such as delays in approvals, lack of appropriate skills, and an unwillingness to implement the rules and regulations in SEZs.

In the **New Hire** model, instead of deploying the ministries’ representatives, the regulator hires its own staff and trains it according to the SEZs’ specific needs, and deposes them in the back office. These employees are authorized to perform respective duties under the different ministries. Similar to the Secondment model, the front office acts as the intermediary between the investor and the back office. Though this model circumvents the traditional bureaucratic hurdles, it may pose significant financial cost in terms of hiring and training new human resource.

The third model of **Front Desk Only**, operates without the back office at the SEZ, whereas the front office is responsible for taking investor applications to different government ministries individually or to an OSS. This model requires minimum human and financial resources. However, it may work only under certain conditions; for example when an SEZ is located near government offices; facing similar standard operating procedures as non-SEZs and; businesses may use digital means to apply and get permits.

Source: Mangal M. (2019). “Institutional Structure of Special Economic Zones.” Reference No. MYA-1903. London: International Growth Centre.

applications, and only acted as post-offices for the respective departments.

Two major challenges with OSS are its the lack of authority, and weak integration of policies across the board. For instance, to improve the ease of doing business, the investment

promotion agencies (IPAs) of Punjab, Sindh and Khyber Pakhtunkhwa have launched online portals that contain relevant information for registrations, licenses and approvals, and direct businesses to the

<sup>76</sup> Sections 23, 17 & 27 Special Economic Zones Act 2012

<sup>77</sup> World Bank (2020). *Assessment of Special Economic Zones in Pakistan: Suggesting Steps towards Improved Performance*. Washington, D.C.: WB

respective federal and provincial government websites.<sup>78</sup>

However, these portals are one stop windows that lead to other windows i.e., the portals lead to websites or portals of other government departments, because every department has its own systems and requirements. Real fast-tracking of permits, licenses, approvals etc. has not taken place yet, as there is no stated policy or regulation that fast-tracks government procedures for SEZ developers and enterprises. Nor do SEZ Authorities have authority to hold federal or provincial bodies accountable to ensure the provision of public goods at the zero points of SEZs or SEZ plots, or to fast-track various registrations and approvals.<sup>79</sup>

Similarly, as far as infrastructure outside the zone is concerned, it is the responsibility of the federal and provincial governments to ensure provision of gas, electricity, other utilities, and road access to the zero point of the SEZs. At the same time, the law tasks the SEZ Authority to obtain commitment from the relevant gas pipeline company.<sup>80</sup>

This structure of responsibility is based on the fact that gas companies are owned and controlled by federal government whereas in the case of electricity, generation and

transmission are a federal domain and distribution is a provincial domain. Similarly, providing access road to an SEZ is the responsibility of provincial government; however, connecting that road to national highway via interchanges is a federal subject.

In practice, when a developer faces delays in provision of public goods at the SEZ zero point, it approaches the relevant SEZ Authority, which then writes to the BOI, and the BOI coordinates with the relevant federal authority. However, in the absence of clearly spelled out preferential turnaround time for SEZ projects, and a dedicated delivery unit that can coordinate among various federal and provincial agencies, administrative delays and the absence of an effective OSS pose a challenge to the success of SEZs in Pakistan.<sup>81</sup>

### Other Investment Environment Constraints

In addition to inadequate infrastructure and coordination failures that the SEZs help address by insulating businesses from a relatively weak governance environment in the rest of country, successful SEZs are effectively also islands of excellence in terms of ensuring a business-friendly environment.

**Pakistan's Ranking and Scores in Relevant factors of WJP Rule of Law Index**

**Table 7.6**

	Pakistan	India	Sri Lanka	China	Singapore	Republic of Korea
<b>Regulatory Enforcement Rank (out of 139 countries)</b>	<b>123</b>	<b>78</b>	<b>72</b>	<b>76</b>	<b>4</b>	<b>21</b>
Administrative proceedings are conducted without unreasonable delay *	0.33	0.43	0.41	0.61	0.90	0.78
Due process is respected in administrative proceedings *	0.20	0.53	0.42	0.33	0.88	0.66
<b>Civil Justice Rank (out of 139 countries)</b>	<b>124</b>	<b>110</b>	<b>103</b>	<b>74</b>	<b>8</b>	<b>13</b>
People can access and afford civil justice *	0.40	0.39	0.48	0.60	0.63	0.69
Civil justice is not subject to unreasonable delay *	0.33	0.20	0.21	0.72	0.91	0.81
Civil justice is effectively enforced *	0.36	0.41	0.38	0.60	0.92	0.80
Alternative dispute resolution mechanisms are accessible, impartial, and effective *	0.51	0.60	0.57	0.67	0.75	0.85

\* Indicates score where 1 is best

Source: The World Justice Project Rule of Law Index 2021

<sup>78</sup> Punjab Board of Investment and Trade, Government of Punjab ([www.pbit.gov.pk/Investors%20Facilitation/](http://www.pbit.gov.pk/Investors%20Facilitation/)); Sindh Investment Department ([sindhinvestment.gos.pk/#/](http://sindhinvestment.gos.pk/#/));

Khyber Pakhtunkhwa Board of Investment and Trade ([www.kpboit.gov.pk/investment-facilitation/](http://www.kpboit.gov.pk/investment-facilitation/))

<sup>79</sup> Source: JICA (2020). *Special Economic Zone Survey Report 2020*. Tokyo: JICA.

<sup>80</sup> Section 27 SEZ Act 2012 and Rule 14 SEZ Rules 2013.

<sup>81</sup>Source: JICA (2020). *Special Economic Zone Survey Report 2020*. Tokyo: JICA

To this end, the challenges pertaining to legal environment and availability of skilled labour force at competitive wages are worth considering.

**Legal environment:**

Pakistan does not fare well in the legal environment with respect to business. Both local and foreign investors often face weak contract enforcement, and delays in case filing, serving, trial, judgement and the enforcement of court decision. Dispute involving the Pakistani government and well known foreign investors have also raised concerns regarding contract enforcement issues in the country<sup>82</sup> (Table 7.6). The SEZs in Pakistan are not currently insulated from the country’s legal environment.

In Pakistan, the current SEZ law assigns exclusive original civil jurisdiction<sup>83</sup> to the High Court of the province in which the SEZ is located with respect to all disputes between the developer and any governmental authority or agency. Similarly, exclusive original civil jurisdiction rests with the district court of the district in which the SEZ is located, for disputes between the developer and the zone enterprises and between zone enterprises of the concerned SEZ.<sup>84</sup> The law is silent on disputes between zone enterprises and businesses outside the SEZs, i.e. suppliers and vendors to the enterprises inside the zone or the domestic buyers of the goods produced by zone enterprises.

Experience from SEZs around the world has shown that in addition to geographical location and physical infrastructure, a well-designed legal infrastructure is crucial to success.<sup>85</sup> The absence of a business-friendly

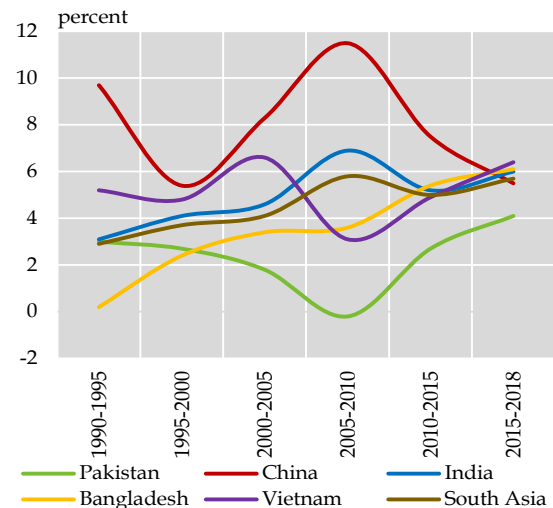
legal framework, therefore, can prove to be a challenge for SEZs in Pakistan.

**Skilled labour:**

The availability of skilled labour is one of the problems faced by investors in developing economies. To this end, the SEZs do not only provide an opportunity to experiment with different labour policies, they also help create a pool of well-trained workers for businesses.

For instance, the SEZ framework in the early period of China’s Shenzhen SEZ allowed to experiment with more flexible labour markets and incentive-based compensation; at that time, it was the only place in China where employee wages comprised both flat wages as well as performance-linked wages.<sup>86</sup> Similarly, South Korea’s Foreign Investment Zone offers differentiated labour regimes for its various sectoral clusters.<sup>87</sup> On the other hand, low-skilled workforce and limited

**Per-Hour Labour Productivity Growth Figure 7.14**



Source: APO Productivity Databook 2020

<sup>82</sup> For details see Chapter 7, “Factors Constraining Investments in Pakistan: Beyond the Macroeconomics” in the SBP’s Annual Report on the State of Pakistan’s Economy for FY19.

<sup>83</sup> Exclusive jurisdiction refers to power of a court to adjudicate a case to the exclusion of all other courts. Original jurisdiction of a case refers to the court that first hears a case through to its conclusion.

<sup>84</sup> Section 38, SEZ Act 2012

<sup>85</sup> C. Teresa (2019). “From Special Economic Zones to Greater Special Economic Region – Hong Kong Special Administrative Region as a Model for Legal Infrastructure Design”, *Transnational Corporations Journal*. Vol. 26 (3).

<sup>86</sup> A. Khandelwal and M. Teachout (2016). “Special Economic Zones for Myanmar.” London: IGC

<sup>87</sup> World Bank (2020). “Assessment of Special Economic Zones in Pakistan: Suggesting Steps Towards Improved Performance”. Washington, D.C.: WB

opportunities to conduct vocational trainings proved to be a drag in some SEZs in Africa.<sup>88</sup>

In Pakistan, labour productivity is weak, as is the supply of well-trained skilled labourers (**Figure 7.14**). According to the World Bank's Enterprise Surveys, 24.2 percent of firms in Pakistan identified inadequately educated workforce as a major constraint, compared to 9.4 percent in India, 15.7 percent in Bangladesh, and 16 percent in Sri Lanka.<sup>89</sup> In Punjab, for example, the total supply for the top 30 most demanded manufacturing sector occupations is only 10.6 percent of the total demand; in Sindh, the supply meets only 20.7 percent of total demand.<sup>90</sup> Even though the M3-IC and the Value Addition City have not yet been fully colonized and completely operational, firms in these SEZs have been facing scarcity of quality labour.<sup>91</sup>

Under the current SEZ law, the SEZs are not insulated from the labour and employment laws applicable in the rest of the country.<sup>92</sup> On the other hand, labour training institutes have not yet been set up within SEZs, because the developers are waiting for the SEZs to be sufficiently colonized by operational industries.

### **Zone Operation & Maintenance**

Global literature on SEZs suggests three major types of stakeholders, apart from the regulator: owner, developer, and operator.<sup>93</sup> In some cases, development and running of operations are done by the owner. In other cases, the owner may give the contract for development to a separate entity, and for operations to another. In Pakistan's SEZ law, the concept of separate operator or manager does not exist. Instead, developers have been tasked with the maintenance of infrastructure

and utility services.<sup>94</sup> Accordingly, developers can charge for maintenance and other services, such as fees for the issuance of No-Objection Certificates (NOCs), sales deed, and for change in directorships. However, proceeds from the sale of land contributes the most to the developers' total earnings.

Discussions with stakeholders suggest that some developers are considering purchasing electricity from power distribution companies at bulk rates and sell it to zone enterprises at the government-notified industrial tariff, and thereby earn the spread between the two rates. As per the SEZ law, developers have the right to set up captive electric power plants or install hydel power generators to sell electricity within a particular SEZ, and outside the SEZ in case of excess supply. However, the developers have not yet set up their own captive power plants. On the other hand, developers can only charge for maintenance on a no-profit-no-loss basis for medical facilities and vocational training facilities.<sup>95</sup>

Aside from these, no explicit framework for incentives exists for operators as a separate entity or for developers running the SEZ as operators. The current SEZ law and regulations in Pakistan focus on first-time colonization, with little focus on operations and maintenance of the SEZs in the long run. For investors, this is a concern over long-term sustainability of the SEZ projects given Pakistan's experience with Industrial Estates and EPZs in the past.

### **Financing for Zone Enterprises**

The current SEZ framework in Pakistan bounds zone enterprises to commence construction of facilities within six months of the acceptance of its zone entry application. It

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<sup>88</sup> T. Farole (2011). *Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience*. Direction in Development Series- Trade. Washington D.C.: WB.

<sup>89</sup> World Bank. *Enterprise Survey 2011-14*. Washington DC: WB.

<sup>90</sup> For details, see Special Section 1 in SBP's Third Quarterly Report on The State of Pakistan's Economy for FY-20.

<sup>91</sup> Source: JICA (2020). *Special Economic Zone Survey Report 2020*. Tokyo: JICA.

<sup>92</sup> Section 30, SEZ Act 2012

<sup>93</sup> M. Mangal (2019). "Institutional Structure of Special Economic Zones." ICG Policy Note, Reference No. MYA-1903. London: IGC

<sup>94</sup> Section 21, clause (iv), SEZ Act 2012 & annexure (7) of SEZ Rules 2013.

<sup>95</sup> Section 27, SEZ Act 2012, & Rules 9(14) and 9(15) of SEZ Rules 2013

also bounds them to start commercial activities within 24 months of being admitted into the SEZ and the acquiring of the required licenses and permits. In addition, title to land purchased by zone enterprises can only be registered in their name only after they have been in operations in the concerned SEZ for at least six months.<sup>96</sup>

If a zone enterprise does not want to construct facilities after being allotted the plots inside the SEZ, it cannot sell the plot to any other investor; the plot can only be surrendered back to the developer at the original purchase price, net off any administrative charges deducted by the developer.<sup>97</sup> Even if a zone enterprise sells its business (including land, plant & machinery and other facilities) to another company, the new owner of the enterprise cannot later sell the plot to anyone else;<sup>98</sup> it can only surrender it to the developer at the original purchase price of the plot net off any administrative charges. These requirements are aimed at preventing real estate speculation of plots inside the SEZs and to fast-track the colonization with operational zone enterprises. However, there are corollaries to this.

At one end, since the land title is not transferred until at least six months after a zone enterprise commences operations, the enterprises are unable to mortgage the land to obtain bank financing for the construction of manufacturing and other facilities. This is so even if zone enterprises have paid for the land in full. At the other end, in the scenario where a zone enterprise commences operations, gets the land title, and then wants to obtain bank financing for expansion or any other purpose, the amount of bank financing is constrained by the surrender value of the plot as described above.

In normal course of business, different banks offer different loan-to-value ratios for mortgaged properties, where the collateral value of mortgaged properties is pegged to the market value. However, in case of SEZs, there is no market to sell off the plots purchased by the zone enterprises. Therefore, the surrender value of the SEZ plot becomes the collateral value. The collateral value of the SEZ plots is limited to the respective surrender value even if the selling price of new plots in the same SEZ is higher.

### **Monitoring & Evaluation**

Effective Monitoring and Evaluation (M&E) are crucial for a successful SEZ programme.<sup>99</sup> It is a critical part of SEZ policy framework, especially if developing economies want to expand the policy, legal and institutional experiments outside the zones, or want to scale up the number of zones across the country. Adequate M&E also ensures whether or not the financial and non-financial economic objectives achieved in a desired period outweigh the fiscal cost of the incentives provided to the SEZs.

To this end, M&E is aimed at cost-benefit analysis; qualitative evaluation of policy experimentation for infrastructure and regulation; spillovers (such as developing local vendors, technology transfer, worker training); attracting foreign investors and integrating with global value chains; and to make constant improvements towards a business-friendly environment.<sup>100</sup>

In Pakistan, both the developers and the SEZ Authorities are stipulated to monitor and ensure compliance with all applicable zone regulations by zone enterprises. The SEZ Committee is also required to conduct

<sup>96</sup> Rule 44, SEZ Rules 2013 & Section 16, clause (g), SEZ Act 2012

<sup>97</sup> These charges range between 6-10 percent of the purchase price, and vary from one developer to another as per zone regulations.

<sup>98</sup> Section 16, clause (h), SEZ Act 2012, & Rule 6 of SEZ Zone Enterprise Admission and Sale, Lease and Sub-Lease of Plot Regulations, 2021.

<sup>99</sup> M. Alexianu, M. Saab, M. Teachout and A.K. Khandelwal (2019). "Doing Special Economic Zones Right: A Policy Framework", IGC Policy Note. London: IGC

<sup>100</sup> P. Manwaring, M. Teachout (2020). "Special Economic Zones Policy Considerations for Uganda." IGC Policy Note. London: IGC.

oversight of zone enterprises, whereas provincial SEZ Authorities are required to report bi-annually to the BOA about the SEZs in their respective province. They also have to submit an annual report whose key components comprise: (a) summaries of the status of each SEZ, including the number of zone enterprises in operation, new zone enterprises starting operations in the year, the amount of remaining unsold or un-leased land; and (b) details of any problems or issues within SEZ that require remediation.<sup>101</sup>

Similarly, the secretary BOA/BOI are required to submit an annual report to the BOA that contains information related to: (a) SEZs activities, progress and future outlook; (b) estimated addition made to exports, GDP, employment and generally acceptable performance indicators; (c) seminars, conferences, training programs organized; and (d) recommendations by Chairman BOI.<sup>102</sup> In practice, however, these reports are not publicly available.

## 7.5 The Way Forward: Policy Options

A 'one size fits all' approach to the analysis of SEZs' problems and their solutions is not recommended. This is because SEZs serve different purposes for different countries – not only in terms of the desired outcomes but also the country's specific broader economic and governance challenges. However, based on the most common factors of success discussed in Section 7.2, the unique challenges to investment and industrial growth in Pakistan in general and the challenges for SEZs discussed in the preceding section, the following recommendations can help the country realize the potential that SEZs characteristically offer.

### *SEZ Policy & Objectives*

An SEZ policy framework with clearly stated objectives is one of the key factors of success of SEZs around the world, as highlighted in section 7.2. Given the absence of such a framework in Pakistan, it is pertinent to draft a detailed SEZ policy to guide the evolving legal

framework and to address various facets of provincial industrial policies. Equally important is the reconciliation of the SEZ policy with other instruments of investment policy, such as the STZA and EPZA, and with various federal and provincial industrial policies, economic growth frameworks and budgetary measures.

While the concerned authorities are to carry out specialized evaluation exercises on their own end and accordingly implement the required regulatory changes, as part of general direction, the following themes could be considered. For instance, a clear policy framework is needed to inform whether or not different objectives may be assigned to different SEZs. If so, then the design, facilities, infrastructure and incentive structures for the SEZs may need to be tailored accordingly.

Similarly, the policy needs to shed light on whether or not SEZs are to be used to transform undeveloped regions. And if so then what measures shall be taken to ensure availability of enabling environment such as road, health and education facilities in the vicinity of the SEZ, and what facilitative policy instruments may be available for such SEZs without simultaneously creating disincentives for enterprises in other SEZs. Likewise, if hi-tech zones are a part of policy priority, then whether or not regulatory frameworks exist to enable and incentivize pro-active creation of a network of researchers; start-ups; venture capitalists and other financiers; academia and well established relevant businesses. Lastly, the SEZ policy may also address the issue of overlapping mandates to reduce complexity.

### *One Stop Shop*

A successful SEZ requires a policy regime that speeds up coordination among all relevant ministries, departments, and agencies at various levels of government. As identified in the previous section, presently there are several bodies with overlapping responsibilities, which leads to project delays. In recognition of these risks, the SEZ

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<sup>101</sup> Sections 17, 20, 23 of SEZ Act 2012 & Rule 56 of SEZ Rules 2013.

<sup>102</sup> Rule 58, SEZ Rules 2013.

framework stipulates the BOA, BOI and SEZAs to promote simplified administrative procedures for SEZs with regards to relevant federal and provincial authorities and agencies, which in turn are to fully cooperate to facilitate developers and zone enterprises.<sup>103</sup>

Accordingly, the government has already approved one window operation by SEZAs whereby the provincial government will either delegate authority for implementing labour, environment and other laws and the collection of local and provincial taxes from SEZs, or it will depute representatives of various departments in the SEZA office. In addition, federal government departments (FBR, SECP etc.) will depute representatives to perform similar functions in the zone.<sup>104</sup>

With increasing number of zone enterprises, there is a need to fast-track the implementation of the approved SEZ legal framework, where four key measures may be considered.

First, the proposed legal framework needs to clearly define the final responsibility and

accountability in terms of coordination with various ministries and departments. For instance, in South Africa, the country's SEZ Policy assigns the responsibility of "oversight and accountability" of the development and operations to the relevant minister or the mayor, as the case may be.<sup>105</sup>

Second, the simplification of procedures needs to include measures such as; not asking businesses the same information many times, which can be made possible by creating a centralized database with unique identification of businesses. The SEZ Act in India simplifies this process by empowering the government to issue a single form for permission under multiple acts for developers and enterprises.<sup>106</sup>

Third, the system should also ensure limited human interaction achieved by means of automation and creation of platforms that allow businesses to submit all documents and payments along with applications in one go.<sup>107</sup>

### Box 7.2: Establishment of Commercial Courts in Punjab: A Recent Development

Commercial courts specialize in lawsuits arising from commercial disputes, such as contract violation, breach of intellectual property rights, and fraud cases. These specialized courts improve the business environment and investor confidence by reducing the time and cost of commercial litigations.

In line with international best practices<sup>1</sup>, the Punjab government has recently established a mechanism for setting up commercial courts in the province through the Punjab Commercial Court Ordinance notified on April 13, 2021. The ordinance grants the government power to constitute the commercial courts at the district level. The court is empowered to preside over all commercial disputes within its jurisdiction, with claim values of Rs 500,000 or more. The ordinance clearly spells out the parties to the dispute, including domestic or foreign companies, partnership firms as well as private individuals.

A Commercial Court Secretariat will also be established under the ordinance. Along with maintaining case records, the secretariat will be responsible for training and education of commercial court judges on matters related to business and finance.

<sup>103</sup> Sections 28 & 29, SEZ Act, 2012.

<sup>104</sup> BoI, Annual Report (2018-19).

<sup>105</sup> Policy on the Development of Special Economic Zones in South Africa (2012) ([www.thedtic.gov.za/wp-content/uploads/NIPF-1.pdf](http://www.thedtic.gov.za/wp-content/uploads/NIPF-1.pdf))

<sup>106</sup> Chapter V (Single Window Clearance), Section 19, The SEZ Act, 2005, India

<sup>107</sup> A. Stone (2006). *Establishing a Successful One Stop Shop: The case of Egypt*. Presented at IMF/AMF High-Level Seminar on Institutions and Economic Growth in the Arab Countries. Washington, D.C.: IMF

The ordinance also provides for an e-filing system for cases, and binds the court to dispense verdict within 180 days after the case is filed, with no more than two adjournments. This is significantly swifter dispensation as compared to the 1,071 days it currently takes to resolve a commercial case in Pakistan. In fact, it is close to the best performing country, Singapore, where it takes 164 days to dispense a case.<sup>2</sup>

The ordinance also directs the creation of the Commercial Appellate Tribunal. An aggrieved party can appeal to the tribunal within 30 days of the court's judgment, and the tribunal is bound to resolve the appeal within 120 days (Figure 7.5.1).

*References:*

<sup>1</sup> The Punjab Planning & Development Board, "Enforcing contracts under ease of doing business 2021"

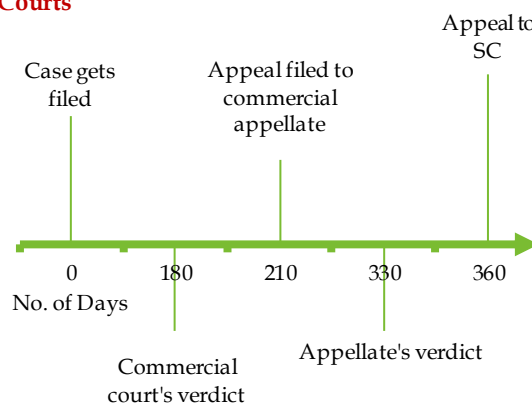
<sup>2</sup> *Ibid* reference 1

Such a system should have time-stamped process flow, from receipt of application to completion of request. For example, "Digital Beijing" initiative in the Zhongguancun e-Park in China simplifies documentation procedures using technology.<sup>108</sup> Using an online system, companies in this park can submit applications and documents, register with government bodies, and interact with government officers online.

Fourth, equally important is to ensure shorter timelines for applications concerned with SEZs. These will not be possible only by moral suasion but by clearly codifying preferential turnaround times for SEZs. In the case of a physical OSS model, the representatives of various ministries, departments and organizations need to be empowered to act on behalf of their ministries.<sup>109</sup> Otherwise, coordination failures will continue to exist, and the one stop will remain ineffective. A physical OSS may also consider longer work hours, as was successfully experimented in Egypt, to help fast-track applications.<sup>110</sup>

**Case Timeline under Commercial Courts**

**Figure 7.2.1**



Source: Punjab Commercial Court Ordinance, 2021

**Other Investment Environment Constraints**

In order to insulate the SEZs from the country's overall weak investment environment, the following measures can help create business-friendly legal environment and increase the availability of skilled labour force.

*Legal environment:*

Until April 2021, when the Punjab government promulgated the Punjab Commercial Courts Ordinance 2021, Pakistan did not have a dedicated commercial court. The establishment of commercial courts in Punjab is an encouraging development, considering that commercial courts can improve the state of contract enforcement in the country and to provide speedy justice to domestic and foreign investors.

In light of this development, it is recommended that these courts are set up in the districts in which the SEZs have been established. Alternatively, the jurisdiction of the nearby commercial courts may be

<sup>108</sup> V.D. Ndou (2004). "E-government for Developing Countries: Opportunities and Challenges", *The Electronic Journal of Information Systems in Developing Countries*, 18(1), 1-24.

<sup>109</sup> P. Manwaring and M. Teachout (2020). *Special Economic Zones: Policy considerations for Uganda*. IGC Policy Note. London: IGC.

<sup>110</sup> A. Stone (2006). *Establishing a Successful One Stop Shop: The case of Egypt*. Presented at IMF/AMF High-Level Seminar on Institutions and Economic Growth in the Arab Countries. Washington, D.C.: IMF.

expanded to include the SEZs as well. In Punjab's case, the government can set up a commercial court by notification under the current ordinance. Other provinces will have to pass their own laws to set up commercial courts with defined timelines for the dispensation of original verdicts as well as appeals at all levels.

Accordingly, since the SEZ Act 2012 grants exclusive original civil jurisdiction to the district and high courts for disputes between various parties, the SEZ legal framework will need to provide jurisdiction to these commercial courts for SEZ-related disputes, involving zone enterprises, developers, all tiers of governments/governmental bodies, and non-SEZ enterprises doing business with anyone involved with SEZs.

After having set up commercial courts, in the medium to long term, another solution could be to introduce international judges by setting up international commercial court with strong arbitration rules for SEZs to increase the trust of foreign investors. Since the proceedings and judgements of these courts are in English language under British common law, the model for international commercial court has been a success.<sup>111</sup>

In just the last ten years, a host of international commercial courts have sprung up in developing, emerging and developed economies. These include the Dubai International Financial Centre (DIFC) Courts in 2004, Qatar International Court in 2009, Abu Dhabi Global Market Courts in 2015, Singapore International Commercial Court in 2015, Astana International Financial Centre Court in 2015, China International Commercial Court in 2018, and the Netherlands Commercial Court in 2019. Although some of these are housed in financial SEZs, such as the DIFC Courts, others have countrywide jurisdictions. In the spirit of SEZs being fenced-in test beds for

broader economic reforms, an SEZ specific international commercial court can inspire confidence of foreign investors that Pakistan seeks to attract.

### *Skilled labour:*

Addressing the challenge of labour availability at internationally competitive prices at SEZs in Pakistan requires assessments and deliberations on four broad areas before the right steps could be taken.

The first revolves around incentives. The current SEZ framework in Pakistan does not offer any incentive to zone enterprises for labour training. In contrast, in Philippines, SEZ enterprises get additional tax deductions for labour training expenses.<sup>112</sup> Similarly, the Slovak Republic and Serbia offer grants and aid for training and re-skilling labour, while Albania allows tax deductions equivalent to 200 percent of the training costs.<sup>113</sup>

The current SEZ framework in Pakistan stipulates SEZ developers to operate vocational training centres on a no-profit-no-loss basis.<sup>114</sup> In order to incentivize developers, especially those in the private sector, and to ensure that the institutes grow and evolve with the industry's changing needs, one solution is to allow developers to set up for-profit institutes, whilst simultaneously addressing monopolistic concerns vis-à-vis training centres inside the SEZ.

In consideration of vocational training as a public good, another option for the government, SEZA in particular, is to partner with developers and zone enterprises to set up vocational training centres in public-private partnership (PPP) mode. This can help identify skills development needs, create programs to address those needs, and find sustainable funding sources. The PPP model was followed by Malaysia's Penang Skills Development Centre, which is credited for

<sup>111</sup> G. Dimitropoulos (2021). "International Commercial Courts in the 'Modern Law of Nature': Adjudicatory Unilateralism in Special Economic Zones", *Journal of International Economic Law*, Volume 24, Issue 2.

<sup>112</sup> Section 42, The SEZ Act of 1995 (Philippines SEZ act)

<sup>113</sup> M. Petrovic (2017). *Tracking Special Economic Zones in the Western Balkans: Objectives, Features and Key Challenges*. Regional Study under Economic Reform Programmes. Paris: OECD

<sup>114</sup> Rule No.15, SEZ Rules 2013.

being a key factor for Malaysia's economic transformation over the past two decades.<sup>115</sup>

The second area of assessment relates to the availability of skilled labour itself. The National Vocational & Technical Training Commission (NAVTTTC) recently published a study on future employment opportunities in fast-track prioritized CPEC SEZs in light of potential industries and indigenous endowments.<sup>116</sup> In addition to such demand side assessments, the supply side also needs to be evaluated vis-à-vis availability of skilled labour in various vocations demanded and indicative wages through various skill gap surveys.

These supply-side surveys need to be conducted in the districts in which SEZs are located or planned, and in the districts from where labour may be expected to travel from or migrate, given current and historical trends. To this end, annual district-level labour force surveys will go a long way, since the Labour Force Survey currently conducted by the Pakistan Bureau of Statistics is only representative at the provincial level.

The third area relates to assessing the needs of the business community vis-à-vis existing labour laws. For instance, one related concern flagged by the business community is that the increase in minimum wages is higher than the increase in labour productivity, which is leading to a decrease in competitiveness compared to other countries.<sup>117</sup> To this end, periodic construction of labour productivity data,<sup>118</sup> and indices like CPI for Industrial Workers,<sup>119</sup> to gauge workers' cost of living,

can help set minimum wages that are suitable for businesses and workers alike.

Lastly, there is a need to integrate national and provincial labour policies and skills strategy with the SEZs. For instance, the existing National Skills for All Strategy and the Technical and Vocational Education and Training (TVET) Policy for Pakistan does not spell out explicit measures for SEZs.<sup>120</sup> In light of increasing emphasis on the SEZs in Pakistan, there is a need to revisit SEZ-related federal and provincial policies and surveys, including the need for English and Chinese language training for workers in case of foreign investor concentration, and traveling and housing facilities for workers if the SEZs are located far from the pool of skilled labour sources.

### **Zone Operation & Maintenance**

The current SEZ framework allows developers to set up captive power plants or install hydel power generators. In addition, the cabinet has also approved the policy of allowing developers to purchase gas, electricity and other utilities in bulk and supply the same to the enterprises at rates notified by SEZA in consultation with the stakeholders.<sup>121</sup>

These are encouraging developments that require a policy framework to give clear direction to stakeholders, and address risks, such as monopolistic concerns. In addition, it requires creating awareness among the business community, and encouraging it to bring their enterprise mindset to SEZs as developers and operators, which public sector

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<sup>115</sup> Farole, T. (2011). *Special Economic Zones in Africa: Comparing Performance and Learning from Global Experience*. Directions in Development Series- Trade. Washington D.C.: WB.

<sup>116</sup> The study, "Job Market Forecast and Skilled Labour Profiling Fast Track Special Economic Zones - China Pakistan Economic Corridor", is published by the NAVTTTC, and was conducted jointly with the Centre of Excellence for CPEC and the PIDE.

<sup>117</sup> Charter of Economy (2020), The Pakistan Business Council ([www.pbc.org.pk/wp-content/uploads/PBCs-charter-of-economy.pdf](http://www.pbc.org.pk/wp-content/uploads/PBCs-charter-of-economy.pdf)).

<sup>118</sup> For example, the U.S Bureau of Labor Statistics publishes the Labor Productivity and Costs (LPC).

<sup>119</sup> Labor Bureau India, for instance, publishes a monthly Consumer Price Index for Industrial Workers.

<sup>120</sup> National Vocational and Technical Training Commission, National Skills for All Strategy, ([www.navttc.gov.pk/wp-content/uploads/2020/10/National-Skills-for-All-Strategy-2018.pdf](http://www.navttc.gov.pk/wp-content/uploads/2020/10/National-Skills-for-All-Strategy-2018.pdf)); Technical and Vocational Educational Training Policy ([www.navttc.gov.pk/wp-content/uploads/2020/10/NTP2018.pdf](http://www.navttc.gov.pk/wp-content/uploads/2020/10/NTP2018.pdf))

<sup>121</sup> BoI, Annual Report (2018-19)

developers may not necessarily have given the incentive structure in the public sector.<sup>122</sup>

Successful SEZs earn from services rather than sale of plots. This is because plot sales generate one-time revenue, which is often used for setting up another SEZ or is paid off as dividends to the developer. For SEZs to be sustainable, developers need a source of continuous inflows, such as income from various services.

Captive power is one such example of income from service: the sooner a developer colonizes the SEZs with operational zone enterprises, the earlier it would start earning revenues from selling power. Similar opportunities exist for selling RLNG; offering warehousing services; providing effluent treatment plants, desalinization plants and labs for testing; arranging conferences, seminars and meeting halls alongside co-working places; and setting up for-profit vocational training institutes. A policy framework that covers these aspects can help provide the necessary direction for long run sustainability of SEZ projects.

### **Financing for Zone Enterprises**

In the absence of collateralizable land at the SEZs, the borrowing needs of zone enterprises may be facilitated by provincial and federal governments, since under the current SEZ framework the first charge remains with the developer i.e., the SEZ plot can only be surrendered back to the developer, which makes banks hesitant to lend to zone enterprises. These considerations necessitate a clear bank financing policy framework for the SEZs, where lessons may be drawn from the Chinese experience. Literature on Chinese SEZs shows that preferred credit policies, such as bank guarantees by the government and subsidized loans, were offered to zone enterprises in various SEZs and clusters.<sup>123</sup>

In light of this, government guarantees could be provided to secure bank loans taken by zone enterprises for which the SEZ framework may be accordingly revised, facilitating banks to meet the borrowing needs of zone enterprises. Subsidized financing facilities may also be introduced for exporting and non-exporting zone enterprises with collateral requirements in sync with the realities of land title and valuations inside the SEZ.

Another option on the policy menu is to strengthen the cancellation policy of the SEZ plots sold to zone enterprises in case they do not commence operations in time or fail to meet other criteria, and to accordingly transfer the land title sooner rather than later. Currently, the title of the SEZ plot is not transferred to zone enterprises until six months have passed since the commencement of operations, even if purchase price of the plot has been paid in full. The government is hesitant to transfer the title before this period because it is concerned that zone enterprises may not set up production units at all or may not set them up in time, which will negatively affect SEZs performance. However, a stronger plot cancellation policy with clearly defined milestones may be considered in light of the proposed commercial courts solution and their potential jurisdiction over SEZs.

Lastly, instead of selling SEZ plots to zone enterprises, an altogether new regime may be considered, where the government provides land to developers on rent and the developers in turn provide the plots to zone enterprises on ground rent. This can substantially reduce the upfront cost of land paid by the developers and the zone enterprises, leading to a lowering of the amount of capital expenditure required for the setting up the project. In addition, this measure may also nudge developers away from the real estate model of developing and operating SEZs and may instead encourage innovative service-focused business models.

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<sup>122</sup> S. Burgess and M. Ratto (2003). "The Role of Incentives in the Public Sector: Issues and Evidence", *Oxford Review of Economic Policy*, 19(2): 285-300.

<sup>123</sup> Zeng D, 2010, Building Engines for Growth and Competitiveness in China Experience with Special Economic Zones and Industrial Clusters, World Bank

## Monitoring & Evaluation

Given the importance of Monitoring and Evaluation (M&E) to the success of the SEZs, the information basis required for M&E needs to be expanded to include various indicators of inputs, outputs, outcomes and impact. This means that in addition to conventional datasets related to annual investment, number of companies, production, sales, exports, and taxation, indicators measuring spillovers also need to be tracked. These may include education and skill level of employees; ratio of foreign employees and consultants in total employees; spending on research & development; share of imports against sourcing through local vendors as well as surveys on types of goods and services sourced locally or imported along with the reasons for not sourcing locally.

A host of government agencies may be relied on for the purpose of monitoring and evaluation. For instance, Nepra can undertake monthly performance assessments in SEZs to assess average frequency and duration of power interruption. Similarly, sales tax and customs data can shed light on the degree of value-addition as well as linkages to vendors located outside the zones. A combined manufacturing index for SEZs may be constructed by Pakistan Bureau of Statistics to evaluate the trends in production inside the SEZs.

In addition, a periodic regulatory impact assessment would help towards improving the regulatory and legal environment for the SEZs. Another dynamic dimension of M&E is motivational studies of existing and prospective investors, which are important tools to assess the changing needs and interests of investors in various sectors of economy.

In terms of investor feedback, lessons may be learnt from South Korea, where a centralized investor feedback portal allows SEZ-related enterprises to provide feedback directly to the

highest government offices, including the PM office and key line ministries.<sup>124</sup> The usage of online reporting platforms for feedback and surveys, as against brick and mortar complain centres, can improve the feedback process, and hence improve the aftercare services at the SEZs. For the purpose of independent evaluation, a periodic specialized survey may be commissioned to assess different aspects of business environment in SEZs across the country.

Lastly the M&E framework of SEZs in Pakistan may also be revised to adopt international best practices as per which SEZ performance reports are to be submitted to the parliament, or otherwise made public via a government website.<sup>125</sup>

## 7.6 Final Remarks

The two main rationales and conceptions of SEZs around the world are islands of excellence and laboratories for policy reforms. In both these conceptions, the SEZs in Pakistan have room for improvement.

The current SEZ framework and the ensuing government decisions have envisioned SEZs as designated areas that offer a business-friendly environment, as per international best practices. There have been some positive developments recently, such as the passing of the SEZ MIS regulations, which prevent real estate speculation. However, that vision is yet to be fully implemented; the one stop shop has not been set up, whereas overlapping coordination functions have led to delays in provision of infrastructure and utilities. In addition, policy frameworks to ensure business friendly climate in SEZs with respect to skilled labour and facilitative legal environment have not been announced.

As far as policy reforms is concerned, the current SEZ framework does not envision SEZs in Pakistan as areas that offer special policy and regulatory environment to businesses. Under current SEZ framework, all

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<sup>124</sup> Source: JICA (2020). *Special Economic Zone Survey Report 2020*. Tokyo: JICA

<sup>125</sup> M. Alexianu, M. Saab, M. Teachout and A.K. Khandelwal (2019). *Doing Special Economic Zones Right: A Policy Framework*. IGC Policy Note. London: IGC

the SEZ authorities, organizations and persons engaged in the creation, development, operations and management of a SEZ are required to follow respective applicable laws and standards of Pakistan including vis-à-vis environment, employment, procurement, and building code, unless specifically exempted, relaxed or otherwise provided in the SEZ Act.<sup>126</sup>

However, the current SEZ framework does not offer exemptions, with the exception of building codes. Here, Bangladesh's SEZ Act offers some useful insights. Not only does it exempt the SEZs in Bangladesh from various national and local government laws, it also allows the government to modify any other Act or do any other thing necessary to remove difficulties for growth and development of SEZs.<sup>127</sup>

A concerted effort is required to address the challenges to the growth of SEZs in Pakistan, by graduating the SEZ framework from one that focuses on first-time colonization to one that also provides direction on operation and maintenance, financing, sustainability, monitoring and operation, and so forth. This necessitates deliberations over the creation of a separate centralized autonomous SEZ authority that would perform several functions. In addition to approving zones and developers, these functions include providing and updating regulatory guidelines; coordinating with relevant government departments across different levels on SEZ-

related matters; continuously monitoring zone performance aimed at providing best infrastructure and facilities within the SEZs; and assessing the impact of various policy reforms on the business climate within the SEZs.<sup>128</sup>

In some countries, the role of the SEZ authority is performed by existing ministries; for example, in Kosovo, the Ministry for Trade and Industry acts as the regulator for all its free economic zones.<sup>129</sup> In others, such as Uganda and Sri Lanka, the Investment Promotion Agencies control the SEZs.<sup>130</sup> However, UNCTAD's World Investment Prospects Survey 2019, which includes 120 IPAs from 110 countries, notes that only 7.5 percent of the IPAs were performing the role of the SEZ authority in their country.

The findings of UNCTAD's survey resonate with international best practices, which suggest not to delegate regulatory powers to an IPA. Generally, the mandate of IPAs is to facilitate investment, and regulatory responsibility may lead to a conflict of interest and affect the performance of its core functions.<sup>131</sup> Instead, autonomous or separate bodies are established as an institutional structure, with the mandate to regulate and manage SEZs and act as principal interface with developers and zone enterprises,<sup>132</sup> as is the case in Bangladesh, Jamaica, Kenya, and Philippines.<sup>133</sup>

<sup>126</sup> Rule 35, SEZ Rule, 2013.

<sup>127</sup> L. Cotula (2017). "The State of Exception and the Law of the Global Economy: A Conceptual and Empirico-legal Inquiry", *Transnational Legal Theory*, 8(4), 424-454.

<sup>128</sup> World Investment Report. (2019). *Special Economic Zones*. Geneva: UNCTAD

<sup>129</sup> M. Petrovic (2017). *Tracking Special Economic Zones in the Western Balkans: Objectives, Features and Key Challenges*, Paris: OECD

<sup>130</sup> Page, J. and F. Tarp (2017). *The Practice of Industrial Policy: Government-Business Coordination in Africa and East Asia. WIDER Studies in Development Economics*. Oxford University Press.

<sup>131</sup> OECD (2021). *Middle East and North Africa Investment Policy Perspectives*. Regional Study under Economic Reform Programmes. Paris: OECD

<sup>132</sup> A. Altbeker, K. McKeown and A. Bernstein (2012). *Special Economic Zones: Lessons for South Africa from International Evidence and Local Experience*. Proceeding of Round Table convened by CDE. Johannesburg: Centre for Development and Enterprise

<sup>133</sup> SEZs in Bangladesh, Jamaica, Kenya and the Philippines are regulated and supervised by Bangladesh SEZA (BEZA), the Jamaica SEZA (JSEZA), Kenya SEZA, Philippines Economic Zone Authority (PEZA), respectively. The institutions are constituted under their countries SEZ acts.

### Annexure-I: Selection of Zone Enterprises

As per the latest regulations, potential zone enterprises have to submit an application to purchase land from the developer and apply for zone enterprise status through an online Special Economic Zone Management Information System (SEZMIS) maintained by the BOI. The regulatory framework has a set of defined documents and other criteria for zone enterprise applications, which potential zone enterprises have to file through the SEZMIS. Once the SEZ committee approves the zone enterprise application, the developer admits the zone enterprise into the SEZ.<sup>134</sup> The module is aimed at increasing transparency and shortening the time taken to complete the application process.

Approved by the Board of Approvals (BOA), the SEZMIS came into force in January 2021. It is a digital solution for registering zones for BOA's approval, and allocating plots and zone enterprise status to enterprises within the zone through an application made to the SEZ Committee.<sup>135</sup> Once the SEZ Committee awards zone enterprise status to an investor, it must commence construction within six months and business operations within 24 months;<sup>136</sup> the zone enterprise status on the other hand is needed by enterprises to become eligible for fiscal incentives.

Prior to the SEZMIS, land allocation and awarding of zone enterprise status took place separately. Neither were there regulations binding allottees to apply for zone enterprise status within a prescribed time, nor did a mechanism exist for simultaneous application for land allotment and zone enterprise status. Developers allotted the land, and then application for zone enterprise status was presented to the SEZ Committee via a separate process. The allottees looking to benefit from real estate activity did not apply for the enterprise status with the intention of avoiding construction deadlines, and instead sought capital gains on the allotted SEZ land.

This lacuna was corrected in SEZ Zone Enterprise Admission and Sale, Lease, and Sub-Lease of Plot Regulations, 2021. Article 3(20) of the regulation directs simultaneous admission and transfer of land possession to the investor with the status of zone enterprise. In addition, Article 3 (3-4) mandates potential investors to register on SEZ MIS, keeping all the stakeholders informed of the status of plots and applications. Accordingly, through the SEZMIS, the SEZ committee provides simultaneous time-bound approval for: (a) sale of plot, (b) possession of plot, (c) provision of utilities, and (d) enterprise status, leaving no room for real estate speculation. The developers too can only sell those to which infrastructure has been provided at their respective zero points, or has given an undertaking and timeframe for the same.

The portal's design complies with all the necessary regulations, and its interface acts as a checklist for all essential documents. It can only be used by an SECP-registered company, and have two types of users: zone developers and zone enterprises. After signing into the portal, the developer and the enterprise follow the application flow, with a different set of documents required at each step. Apart from this, complaints can also be registered via the portal.

The SEZ MIS increases the efficiency of the filing system and contributes towards creating an enabling business environment in the country. Within five months of its establishment, there were 70 active zone enterprises, compared to 200 for the eight years before the SEZ MIS (**Table A1**).

	Approvals under SEZ MIS	
	Before SEZ MIS 2012-20	After SEZ MIS Jan-May 2021
Approved Zone Enterprises	200	70
Investment (billion Rupees)	334.2	304
FDI (million US\$)	1,081.7	646.6

Note: FDI is not actual flows but commitment at the time of zone enterprise admission.

Source: Board of Investment

<sup>134</sup> SEZ Zone Enterprise Admission and Sale, Lease, and Sub-Lease of Plot Regulations, 2021.

<sup>135</sup> According to the SEZ Act, 2012, BOA will charter a committee for zones.

<sup>136</sup> Section 16, clause (1) (e), SEZ Act 2012

## Annexure-II: List of Members for Different Regulating Bodies of SEZs

Board of Approval	Approvals Committee	Provincial SEZ Authority	SEZ Committee
Chairperson: Prime Minister; Vice Chairperson: Minister of Finance	Executives: heads of Provincial investment boards	Chairperson: Chief Minister of concerned province	The developer shall appoint the chairperson of the committee
Ministers for Industries, Production, Commerce, State & Frontier Regions Division	Representatives from Ministers for Industries, Production, Commerce, State & Frontier Regions Division	Vice Chairperson: Minister of Investment Department	Representatives from the developer
Two members from Majlis-e-Shoora	Private sector representatives	Chief Executive Officer appointed by Chief Minister of the province	Representatives from BOI, provincial investment promotion agency,
Chairman and Secretary BOI; Chairman FBR; Deputy Chairman Planning Commission; Governor SBP	Co-opted members from concerned federal and provincial government	Secretary of Provincial BOIs	Representative from SEZ Authority and relevant district government
Chief Minister of each province		Secretaries of provincial industries, finance, commerce, investment, work and services, livestock, agriculture and planning and development departments	
Executives: heads of Provincial investment boards		Two members to be appointed by CM of relevant province	
Presidents of: Federation of Pakistan Chambers of Commerce and Industry; Pakistan Business Council; and Overseas Investors Chamber of Commerce		A member to be appointed by the relevant chamber of commerce and industry	
A professional nominated by Prime Minister			

Source: Modified & Amended Special Economic Zones Act, 2012, as amended up to December 31, 2015