

## Policy pointers

**Business clustering can** make economic sense, but many special economic zones (SEZs) have been associated with compressions of land, labour and human rights.

**Legal regimes are partly** to blame — for example, where they undermine rights or exempt SEZs from national laws — though activists have in a few instances mobilised law to challenge SEZs.

**While public debates** focus on the economic performance of SEZs, we must also consider the social and environmental dimensions, exploring the place of law as part of the problem and the solution.

**Policymakers should** carefully think through SEZ laws and recognise the role of social actors — including people impacted by SEZs — in shaping law reform.

## Special economic zones: engines of development or sites of exploitation?

Special economic zones (SEZs) have spread rapidly over the past 20 years, including in many low- and middle-income countries keen to attract private investment for industrial development. But while much debate has focused on their economic performance and success factors, there are concerns over land expropriations, poor labour conditions and lost public revenues. These concerns are often partly rooted in the legal regimes that underpin SEZs — their failure to protect affected people, their exempting SEZs from national laws or their weak arrangements to ensure compliance. At the same time, activists have in a few cases mobilised the law to contest SEZs and their impacts. This briefing discusses these trends and points to possible ways forward for research, policy and practice.

SEZs are geographic areas where the rules of business differ from the rest of the country (see Box 1). They aim to promote industrial development in strategic locations to catalyse wider economic transformation. With historical roots in antiquity, modern antecedents in 1950s Ireland and a contemporary testing ground in 1980s China, they have proliferated in low-, middle- and even high-income countries.

In poorer countries, SEZs often form part of policy efforts to enter or climb up the 'value chain ladder' by encouraging businesses to carry out processing activities locally. Many SEZ schemes promote foreign direct investment (FDI) in labour-intensive manufacturing for export, covering sectors such as garment, agro-processing and light machinery industries. SEZs present some similarities with other spatial development initiatives such as growth corridors, and their creation can be associated with large-scale infrastructure developments — including roads, railways and

deep-sea ports to connect industrial complexes to market.

### Spaces of exception

Many factors can drive the concentration of industrial activities in strategic geographic areas. Available infrastructure or natural resources can dictate location, while businesses of the same economic sector or linked by complementarities or value chain relations can gain competitive advantages by clustering in the same territory. Clustering has enabled small- and medium-scale enterprises to pool services, infrastructure and expertise, establish associations to address common problems and ultimately develop competitive industries.<sup>1</sup> Many states have adopted industrial policies to promote business clusters, building infrastructure or supporting training or research and development.

But SEZs go beyond these parameters in that they provide special legal and/or institutional

## *SEZs raise questions about rights, citizenship and political organisation*

arrangements to encourage businesses to set up shop in specific geographic areas. While they present strong links to international economic law, SEZs are primarily governed by country-specific

national or local legislation.

As such, SEZ regimes are extremely diverse. But many SEZ laws create spaces of exception where aspects of ordinarily applicable law do not fully

apply.<sup>2</sup> So, although SEZs are typically located within the territory of one state, their integration into global value chains is often mediated by rules and institutions that depart from national regulation. Many investor-state contracts extend SEZ benefits to individual companies outside formal SEZs.

Governments often justify this set-up as a policy imperative to promote growth through increased investment and trade. And while some orthodox economic perspectives view SEZs as an undesirable distraction from economy-wide trade and investment liberalisation, others emphasise their potential as an industrial policy tool. There is evidence that SEZs have fostered industrialisation in some East Asian economies, but results elsewhere have been mixed.<sup>3</sup>

### **When normal rules do not apply**

By modifying the application of national laws, SEZs raise questions about rights, citizenship and political organisation. In institutional terms, they can involve shifts in the regulatory powers of the legislature and the executive, with some SEZ laws leaving significant room for executive discretion.<sup>4</sup> In the absence of effective accountability, this can result in abuses. Many SEZ laws also affect the substantive rules applicable to business conduct. They often waive or reduce taxes to attract globally mobile capital. This may involve exemptions from profit and value added taxes and duty-free imports.

### **Box 1. Different types of special economic zone**

The form and function of an SEZ can vary, depending on the government's objectives, the sectoral focus, target market and the economic activities involved. They can be run by government, the private sector or under public-private partnerships. Examples include:

- Export processing zones (EPZs)
- Free trade zones
- Industrial zones, and
- Agricultural growth poles (agropoles).

Border lines between these types are blurred and their relative importance can vary over time. In some countries, the rise of middle classes has fostered shifts away from EPZs in favour of activities servicing domestic markets; while budget constraints and policy reforms have increased the role of the private sector in creating and operating SEZs.

There is mixed evidence as to whether tax incentives drive significant FDI flows and positive outcomes, and their overall costs and benefits. But tax exemptions can undermine the ability of authorities — particularly in poorer countries — to finance public services.<sup>5</sup> In several countries, SEZ legislation also affects the application of laws other than tax. Rules on land and labour rights can have particularly direct impacts on human rights and the fabric of society.

### **Land rights and acquisition**

When an SEZ is created, there are often disputes over land acquisition, particularly where it involves converting land from agricultural to industrial use or the expropriation of homes, farms and other economic, social or cultural assets. Land disputes may originate from deep-rooted issues such as growing population densities and the perceived social legitimacy of government action, but are often exacerbated by legislation. For example, some laws automatically consider the creation of an SEZ as a 'public purpose' that justifies compulsory land acquisition.<sup>6</sup> Landholders often have limited opportunities to meaningfully inform decisions on overarching development pathways and resulting land acquisitions.

This widespread use of expropriations to transfer land for commercial activities raises questions about the meaning and bounds of public purpose. Although many national laws entitle landholders to compensation, this can be inadequate for restoring livelihoods — because some resource claims are not legally recognised or compensable or compensation standards are low. Laws often place the burden of compensation costs on the developer, so if a company collapses, people can be left without compensation or redress.

Where SEZs are backed by powerful alliances between authorities, national business elites and foreign capital, such legal regimes can enable 'legalised land grabbing'.<sup>7</sup> In Myanmar and Cambodia, SEZs have been associated with land speculation in surrounding areas and reports of human rights abuses linked to displacement, while livelihood disruptions caused by land dispossession have led to protests in India, Madagascar, Vietnam and the Philippines.<sup>8</sup>

### **Labour rights**

Many governments promote SEZs to create new jobs. But there are widespread concerns about labour rights in SEZs. At their worst, SEZs are enclaves where workers experience overtime work in unsafe conditions, wage discrimination and harassment, while being denied fundamental rights to freedom of association and collective bargaining. Many factors can facilitate these bad practices, but the law is often partly to blame. Some exceptional

SEZ legal regimes restrict unionisation and deploy worker welfare associations to compete with and undermine trade unions; elsewhere, rights exist on paper but are not backed by effective compliance arrangements (see Box 2).

In practice, enjoyment of labour rights partly depends on factors beyond legislation, such as the corporate practices of businesses operating in SEZs or of their buyers, while the enclave nature of SEZs can make it difficult for workers to unionise regardless of legislation. Labour rights abuses take place in and outside SEZs, and in some cases working conditions may be better inside SEZs than outside.<sup>9</sup>

But legislation does matter, particularly where it translates into separate institutional configurations. While the ministry responsible for labour would in principle handle industrial relations in most countries, some SEZ laws vest this responsibility with SEZ authorities. Yet, the primary mission of these authorities is not to protect labour rights, but to promote SEZ development. Also, labour disputes may be subject to special SEZ tribunals rather than national labour courts. These administrative and judicial set-ups can create conflicts of interest if trade-offs arise between labour rights and productivity concerns, further undermining labour rights. Conflict of interest issues are particularly pressing where an SEZ is run, in full or in part, by a private company rather than a government agency.

## Women's rights and economic empowerment

SEZs may attract young, migrant women whose economic empowerment can be enhanced by their inclusion in the labour market and global value chains. But women are often excluded from decision making over land acquisition, and the loss of income and increased food insecurity outside the SEZs after land expropriations often exacerbate gender inequalities. The loss of tax revenues can also have gendered impacts, if it adversely affects expenditure on public services such as education and health.

Further, outright discrimination exists in many workplaces, particularly where women have insecure and low-status jobs that involve repetitive tasks, excessive overtime, occupational health and safety risks, and limited career development opportunities. These gender dimensions receive too little attention in public debates on SEZs.<sup>10</sup>

## The role of investment protection

While SEZs are primarily regulated by national law, international treaties can also have a bearing on SEZ governance. Several trade agreements govern the customs treatment of goods

### Box 2. SEZ legislation: Pakistan v Cambodia

In Pakistan, national labour laws do not fully apply in EPZs, where:

- Minimum wages are established through arrangements separate from those applicable nationally
- Strikes are banned, and
- Labour disputes are referred to the EPZ dispute resolution mechanism rather than national courts.<sup>11</sup>

In Cambodia, labour rules on minimum wages, employment contracts and dispute resolution theoretically apply inside and outside all SEZs. But compliance is often a problem and investigations have documented labour abuses both inside and outside the SEZs.<sup>12</sup>

originating from SEZs.<sup>13</sup> And although most investment treaties — legally binding agreements between states to promote cross-border investment — say little or nothing about SEZs, they respond to a similar policy thrust, establishing legal arrangements to deepen economic integration as an avenue to growth.

Under investment treaties, states typically agree to provide each other's investors with protection against adverse conduct by public authorities. Depending on the circumstances and how these legal protections are interpreted and applied, foreign investors may be entitled to compensation for adverse changes in SEZ terms. Further, many investor-state contracts protect investments against adverse regulatory change — for example, through provisions that 'freeze' applicable national law at a specified point in time or require the government to offset or compensate losses incurred by the investor (stabilisation clauses).

Many investment treaties and contracts allow investors to bring disputes to investor-state arbitration if they consider that the state has breached its obligations. To date, investors have brought at least 20 arbitrations to challenge diverse aspects of SEZ regimes.<sup>14</sup> Several stemmed from the withdrawal or modification of tax incentives, but strengthening labour rights or tightening land compensation requirements could also adversely affect investors' rights or returns and trigger claims.

The often large compensation payouts that tribunals have awarded investors, coupled with the significant legal costs and uncertainty associated with arbitration, could make it more difficult for cash-strapped states to adopt reforms to problematic aspects of their SEZ regimes. This 'regulatory chill' risk calls for properly considering decisions on treaties and contracts, and compounds the case for rigorously thinking through national policy on SEZs.

Some recent investment treaties require states not to promote investments by derogating from national labour legislation or waiving its

application, but these have not yet been tested in investor-state arbitration.

## Law as an arena to contest SEZs

While the law plays a key role in constituting and sustaining SEZs, it has also provided arenas for labour, agrarian and other social movements to contest the creation and operation of SEZs. In Cambodia and India, activists have brought complaints to the International Finance Corporation's compliance advisor ombudsman and the national courts respectively, as part of wider strategies to demand adequate compensation for expropriated land and compel the authorities to revoke land allocations to SEZ promoters.<sup>15</sup> And in Madagascar, the constitutional court struck down several provisions of a proposed SEZ law in the face of civil society opposition before finally approving a revised bill.<sup>16</sup>

Activists have also employed transnational strategies, seeking redress in the home country of parent companies that drive SEZ implementation or influencing key export market governments. This includes asking Thailand's National Human Rights Commission to examine alleged human rights violations associated with Thai companies' involvement in developing SEZs in Mekong countries.<sup>17</sup> In Bangladesh, wage strikes in late 2016 forced a week-long shutdown of nearly 60 factories in one industrial zone, leading the European Union — a key export market — to threaten to suspend trade benefits under legislation governing its Generalised System of Preferences.<sup>18</sup>

## Conclusion

SEZs have gained significant traction as a policy tool to promote industrial development in low-

medium- and high-income countries, and a growing number of states have adopted SEZ laws. But while business clustering can make economic sense, many SEZs have been associated with compressions of land, labour and human rights. Dispossessing the land rights of marginalised people and suspending their labour rights are unacceptable ways to promote FDI. If not properly thought through, SEZ laws can violate human rights and undermine the foundations of political organisation.

Legal regimes are part of the problem, for example where they fail to protect affected people or where they exempt SEZs from national laws. Legal instruments can also make it more difficult for states to reform SEZ regimes, though activists have in a few instances mobilised law to challenge SEZs. So, while much public debate focuses on whether SEZs can successfully drive economic growth, and under what conditions, we must also interrogate the role the law plays in sustaining and contesting them.

Policymakers should properly consider the legal regimes governing SEZs and recognise the role of social actors, including people impacted by SEZs, in shaping law reform. Legal scholars can support this by considering law both in the statute books and in practice, as well as the social, political and economic contexts in which the law operates.

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Thanks to Jean-Paul Gauthier, Emily Polack, Mustafizur Rahman and Brendan Schwartz for their helpful comments.



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ISBN 978-1-78431-632-7

This briefing has been produced with the generous support of Danida (Denmark), Irish Aid and Sida (Sweden).

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## Notes

<sup>1</sup> For example, Dei Ottati, G (2018) Marshallian industrial districts in Italy: the end of a model or adaptation to the global economy? *Cambridge Journal of Economics* 42(2) 259–284. / <sup>2</sup> Cotula, L (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. On spaces of exception in economic governance, see also Bracking, S (2012) Secrecy jurisdictions and economic development in Africa: the role of sovereign spaces of exception in producing private wealth and public poverty. *Economy and Society* 615–637. / <sup>3</sup> Zeng, Z (2015) Global experiences with special economic zones: focus on China and Africa. World Bank; Farole, T (2010) Special economic zones: performance, policy and practice — with a focus on sub-Saharan Africa. World Bank. / <sup>4</sup> For example, Sections 11A and 24 of Bangladesh Export Processing Zones Authority Act 1980. / <sup>5</sup> For example, Tavares-Lehmann, A *et al.* (eds) (2016) Rethinking investment incentives: trends and policy options. Columbia University Press; Abramovsky, L *et al.* (2018) Are corporate tax incentives for investment fit for purpose? Revisiting economic principles and evidence from low- and middle-income countries. Institute for Fiscal Studies. / <sup>6</sup> For example, Section 11 of the Bangladesh Export Processing Zones Authority Act 1980. / <sup>7</sup> Woods, K (2014) A political anatomy of land grabs. Transnational Institute. / <sup>8</sup> See, for example, International Commission of Jurists (2017) Special economic zones in Myanmar and the state duty to protect human rights; Thame, C (2017) SEZs and value extraction from the Mekong: a case study on the control and exploitation of land and labour in Cambodia and Myanmar's special economic zones. Focus in the Global South; Reuters (10 June 2018) Vietnam police halt protests against new economic zones. / <sup>9</sup> Richardson, B *et al.* (2016) Labour rights in export processing zones with a focus on GSP+ beneficiary countries. European Parliament. / <sup>10</sup> On SEZs and women's economic empowerment, see International Finance Corporation (2011) Fostering women's economic empowerment through special economic zones: comparative analysis of eight countries and implications for governments, zone authorities and businesses. On the more negative gender aspects, see Tejani, S (2011) The gender dimension of special economic zones. In: Farole, T and Akinci, G (eds) Special economic zones: progress, emerging challenges, and future directions. World Bank; and Tavoyan Women's Union (2015) Our lives not for sale: Tavoyan women speak out against the Dawei special economic zone project. / <sup>11</sup> Articles 3(5), 4 and 7 of the Export Processing Zones (Control of Employment) Rules 1982; under Article 30 of Pakistan's SEZ Act 2012, national labour laws apply to SEZs other than EPZs. / <sup>12</sup> Article 11 of Cambodia's 2005 Sub-Decree on the Establishment and Management of the Special Economic Zone and Kennard, M and Provost, C (25 July 2016) Inside the corporate utopias where capitalism rules and labor laws don't apply. *These Times*. / <sup>13</sup> For example, Articles 25 and 29 of the 2004 Protocol on the Establishment of the East African Customs Union and the related Customs Union (Export Processing Zones) Regulations. / <sup>14</sup> Marisi, F (4 April 2018) Five key takeaways from the Asia FDI Forum IV. [www.linkedin.com/pulse/five-key-takeaways-from-asia-fdi-forum-iv-flavia-marisi/](http://www.linkedin.com/pulse/five-key-takeaways-from-asia-fdi-forum-iv-flavia-marisi/) / <sup>15</sup> Sampat, P (2010) Special economic zones in India: reconfiguring displacement in a neoliberal order? *City & Society* 22(2) 166–182; and Bedi, H (2013) Judicial justice for special economic zone land resistance. *Journal of Contemporary Asia* 45(4) 596–617. / <sup>16</sup> Constitutional Court of Madagascar, Decision 22-HCC/D3 (11 August 2018). / <sup>17</sup> Suk, W (17 July 2018) Reckoning with human rights violations in Thailand's extraterritorial investments. *The Diplomat*. / <sup>18</sup> Hossain Ovi, I (24 March 2017) EU warns Bangladesh of GSP suspension over labour rights. *Dhaka Tribune*.