Nokia SEZ: Public Price of Success

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The government claims that the special economic zones will bring in investment, increase exports and economic activity, and create employment. The Nokia Telecom SEZ near Chennai is often held up as a stellar success of such claims. A closer look at the figures indicates that Nokia's investment is almost entirely paid for by public subsidy, much of the production is sold domestically, employment generation is below projections and workers are short-changed.

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Since 2006, when the Special Economic Zone (SEZ) Act came into force, the number of operating zones has increased from only a handful to 315 with an additional 253 receiving preliminary approval. According to a recent press release by the Ministry of Commerce and Industry, 2.53 lakh employment opportunities have been generated in them. Further "physical export" has increased from Rs 66,638 crore in 2007-08 to Rs 90,416 crore in 2008-09. With Rs 10,385 crore of "physical export" between 2006 and 2009, investments of Rs 2,225.47 crore (of which foreign direct investment (FDI) is Rs 834 crore) and 14,859 workers provided direct employment, the Nokia Telecom SEZ in Chennai, Tamil Nadu is usually placed on top of the list of SEZ "success stories" mentioned. According to the ministry "these figures establish beyond doubt that the response to the SEZ policy has been overwhelming and the scheme has been able to achieve the envisaged objectives".[1]

The above numbers used to justify the success of the SEZ policy are presented as self-evident. But given the wide-ranging exemptions from most taxes in the national SEZ Act it is not obvious to see business gains as being equal to public benefits. Moreover, little is known about the actual employment conditions. With the help of the Right to Information Act it is now possible to shed the secrecy surrounding investment deals and take account of what the Nokia deal actually means for the economy of Tamil Nadu, and as one of the important claimed success stories of SEZs.[2]

A memorandum of understanding (MOU) was signed between the Tamil Nadu government and Nokia for the establishment of a SEZ on 6 April 2005.[3] It was at the time known from newspaper reports that other states had also been interested in attracting Nokia. One Tamil Nadu official was quoted as saying

> it was a tough contest involving Maharashtra, Haryana and Tamil Nadu. Because of the swift responses from Chennai and the special package that was offered, Nokia opted to settle for Tamil Nadu.[4]

The MOU in addition to all the benefits of the national SEZ policy offers extra tax incentives, control over the labour force, and land at a concessional rate.[5]

VAT Reimbursement

Since SEZs are ostensibly meant for export promotion, it is fairly surprising that the main tax incentive offered by the Tamil Nadu government was to reimburse Nokia for valued added tax (VAT). VAT is only a cost to the company when it sells within India since export products are not going to attract this tax. This clearly indicates that, right from the start, the company planned to sell a significant share of its phones in the Indian market.

The MOU states:

> Sales from the SEZ to the DTA will be liable for VAT and CST. Such VAT and CST will be refunded to Nokia by the State Government in terms of the mutually agreed mechanism for the residual period (10 years minus period for which waiver availed in the pre-VAT scenario).

There are two cases to be considered for VAT/CST. The first is when Nokia sells mobile phones within Tamil Nadu. The Tamil Nadu government will, in this case, receive the VAT money from the vendor of the phone and reimburse it to Nokia. This results in a loss of income for the state. The second case of reimbursement concerns sales by Nokia in a state other than Tamil Nadu. Here the phones will attract central sales tax (CST) which will be collected by the respective state government from the vendors, but it is the Tamil Nadu government which reimburses Nokia for the payment of this tax. This reimbursement becomes a cost for the government to be paid in competition with other expenditures like education and health.

If 4% VAT/3% CST (CST was 3% for the fiscal years 2007-08, which is used in the example here) is to be reimbursed, the sum would quickly become very large given Nokia's position as market dominant in India. Sales in 2007-08 were Rs 3,578 crore, meaning Rs 107 crore would have been paid by the Tamil Nadu government to Nokia (excluding the share of sales in