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Developing an Indonesian Regulatory Framework in the Face of SEZs 5.0

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ABSTRACT

Today's "SEZ 5.0," is based on novel digital inventions that offer a gateway to economic progression. The interest of this research dives towards a number of attributions according to studies that render SEZs difficult to implement as an autonomous economic growth instrument (particularly in the Indonesian context), which merits further research as the aim of this study. This research is novel in the way that it illuminates the numerous key lessons from effective SEZ practices, as well as, making sure that SEZs are "special" in contexts of a business-friendly atmosphere supported by a sound statutory



and regulatory model, along with the articulation of sustainable practices and adaptability towards the volatility of the market. The findings of this research suggest that it is possible to gauge the success of SEZs, the nexus between SEZs and international economic law merits further examination, Indonesia can capitalize on the prevalence of financial services in SEZs, and SEZs in Indonesia can be enhanced via policy and regulatory reforms. This research recommends key policy lessons for the Indonesian SEZ governance.

Keywords: SEZ, Economic Zone, Indonesia

INTRODUCTION

Plenty of emerging economies have utilized Special Economic Zones (SEZs) as instrument for encouraging industrial development and economic growth. SEZs are defined as geographically demarcated regions inside the state's territorial limits in which the laws governing the conduct for doing business (particularly investments, both for foreign and domestic investors) operate differently from the ones that dominate in that state's jurisdiction.¹ The final outcomes of the implementation of SEZs in emerging economies as a "high-cost" investments are extremely varied, with specific areas or nations (specifically those situated in eastern Asia) enjoying more success while others (particularly those in Africa) barely seeing such SEZs' benefits.² SEZs are designed to support market dynamics by assisting

¹ Julien Chaisse and Xueliang Ji, "The Pervasive Problem of Special Economic Zones for International Economic Law: Tax, Investment, and Trade Issues," *World Trade Review* 19, no. 4 (2020): 567-588.

² Douglas Z. Zeng, "The Past, Present, and Future of Special Economic Zones and Their Impact," *Journal of International Economic Law* 24, no. 2 (2021): 259-275.

in the elimination of market failures³ as an instrument for a country's strategic industrialization planning. By means of incorporation "common" legal and regulatory standards, most SEZ regulations are primarily devised to be "investor-friendly," as well as more "comprehensible" to international investors.⁴ Governments which employ this innovative style of autonomous economic regulation do not always rigorously adhere to the existing rules of global commerce and investments, instead they utilize customized national legislation and regulation to encourage overseas business and capital to come into their SEZs and invest. By undertaking this style to entice investors, such governments are literally creating enclaves within their border where global economic "standards" are in use while still being governed by the sovereignty of the said nation.⁵

Whereas market sentiment is assumed by the traditional rules of economics to be the primary driver in international commerce, SEZs necessitate deliberate governmental participation. Thus, the SEZ symbolizes a brand-new one-sided concession of the state for the sake of economic and industrial growth, by portraying itself as an answer or supplementary means to favorably promote the local market into

³ The aspirations in this work regarding market efficiency and failures are strongly influenced by the views of Joseph E. Stiglitz (Columbia University) and Jay K. Rosengard (Harvard University) in their work with a social-democratic twist, which succeeded in identifying six market failures that had a negative impact on the government's role in redistributing income and resources. Such market failures are: 1) failure of competition; 2) public goods; 3) externalities; 4) incomplete markets; 5) information failures; and 6) macroeconomic disequilibrium (crisis). See Peter Abelson, "Teaching Public Economics with Special Reference to Australian and US Cultures," *Australian Economic Review* 52, no. 3 (2019): 279-293.

⁴ Georgios Dimitropoulos, "International Commercial Courts in the 'Modern Law of Nature': Adjudicatory Unilateralism in Special Economic Zones," *Journal of International Economic Law* 24, no. 2 (2021): 361-379.

⁵ Georgios Dimitropoulos, "National Sovereignty and International Investment Law: Sovereignty Reassertion and Prospects of Reform," *Journal of World Investment and Trade* 21, no. 1 (2020): 71-103.

the regional or international investors.⁶ There are plenty of variables which promote SEZs, including but not limited to socioeconomic security, governmental stability, minimal regulatory risk, and an all-around supportive business climate, which may additionally attract investors from overseas and help them reach sound investment resolve.⁷

By means of statutory and legislative customizations as well as the creation of a more favorable commercial climate for investors, SEZs can support and enhance those “attractive variables” even more. Once they have proved lucrative enough, such SEZs may be expanded all over the country for widespread implementation. However, finding the right regulatory and statutory tweaks necessary is easier said than done. SEZs can nevertheless be viewed as a crucial addition to the overall appeal in a country’s marketing bundle as well as an indication of the government’s determination in creating a favorable business environment even when such effort falls short of delivering certain productivity results or anticipated overseas investment.⁸

Findings from various literatures suggest that SEZs are difficult to implement correctly as an autonomous economic growth strategy, whereas effective SEZs normally require up to 10 years before they begin producing tangible outcomes beneficial to the overall economy.⁹ SEZs should be approached by lawmakers with a particular outcome in mind, a determination for the long run, and a powerful team of experts with profound understanding of the

⁶ Julien Chaisse and Georgios Dimitropoulos, “Special Economic Zones in International Economic Law: Towards Unilateral Economic Law,” *Journal of International Economic Law* 24, no. 2 (2021): 229-257.

⁷ Zeng, “The Past, Present, and Future of Special Economic Zones and Their Impact.”

⁸ United Nations Conference on Trade and Development, *World Investment Report 2020: International Production Beyond the Pandemic* (New York: United Nations Publications, 2020).

⁹ World Bank, “Drivers of Participation,” in *World Development Report 2020: Trading for Development in the Age of Global Value Chains* (Washington, D.C.: World Bank, 2019), pp. 36-63.

particular context of the country. The highlighted traits gained from “winning” SEZ initiatives, involve crucial components such as strategically planned site for SEZs; integrating SEZ with the greater economic growth planning of the country; recognizing the marketplace and harnessing comparative advantage; as well as most crucially, making sure that SEZs are “unique” in the context of investor-friendly atmosphere, while also taking into account environmental sustainability and resistance towards exogenous volatilities.¹⁰

At the end of the day, SEZs are actually not a “panacea,” and definitely not a single strategy that works for all situations context-wise, all broadly applicable experiences ought to be looked at appropriately—by taking a cautious stance and taking into account the unique circumstances of a nation or industry.¹¹ With this in mind, plenty of international organizations frequently push a uniformed domestic regulatory change in accordance with the international standards.¹² However, this article contends that international organizations ought to acknowledge the constraints of numerous emerging economies (including Indonesia) in accomplishing so; thus, acknowledging the need for customized support for SEZs assuming that such SEZs possess immediate and tangible demand.

In light of this, the current paper’s objective is to describe and evaluate the overall structure of regulations and related mechanisms that exist in SEZs in order to draw foreign capital generally in investment activities and financial industry in particular. It provides a *tour d’ horizon* of the current SEZ frameworks, which affects capital exchange and investment choices. On the surface, this endeavor may seem moderate, but it fills a significant lacuna in the scholarship that has, for the vast majority, concentrated on the financial impacts of SEZs by not explicitly considering the implications of possible key takeaways for creating a localized regulatory framework.

¹⁰ World Bank.

¹¹ Zeng, “The Past, Present, and Future of Special Economic Zones and Their Impact.”

¹² World Bank, “Drivers of Participation.”

Literature studies have been carried out by the authors within the framework of this research to test the novelty of this research, along with the intention of mapping the scholarly works surrounding SEZs, especially those literatures with an Indonesian context. The method used by the authors to search for the literature is done by using the Google Scholar search engine with the keywords: "Special Economic Zone, SEZ, *Kawasan Ekonomi Khusus*, KEK, Indonesia." From the various literatures, most of the works is in the nature of studies of non-law disciplines, while from the various literatures found, writings with a focus on legal and policy studies that have been found include but not limited to: 1) *Reformasi Hukum dan Realisasi Investasi Asing pada Era Presiden Joko Widodo* by Sutrisno and Poerana in 2020, Sutrisno and Poerana in their research tried to examine whether the policy package in President Jokowi's initial period had succeeded in increasing foreign investment in Indonesia and to project foreign investment policy in the second period of Jokowi's presidency. The findings of this study are that Jokowi's policy package succeeded in significantly increasing the value of cumulative foreign investment, but failed to increase the annual growth percentage. Secondly, the Omnibus Law and its regulations that will be relied upon to increase foreign investment have gained resistance from various parties. The study by Sutrisno and Poerana is more aimed at assessing President Jokowi's policy package legacy in relation to SEZs, but does not provide an elaborative and thorough explanation of the components of a successful SEZ program. In fact, this research actually developed from what was left by Sutrisno and Poerana, with the aims to measure the effectiveness of the SEZ which will later be used for policy-making by the authorities;¹³ 2) *Kawasan Ekonomi Khusus (KEK) Mandalika dalam Implementasi Konsep Pariwisata Berbasis Ecotourism: Peluang dan Tantangan* by Estriani in 2019, this study by Estriani analyzes the concept of ecotourism as an alternative to the eco-friendly-based tourism sector in the Mandalika SEZ. Even

¹³ Nandang Sutrisno and Sigar Aji Poerana, "Reformasi Hukum Dan Realisasi Investasi Asing Pada Era Presiden Joko Widodo," *Undang: Jurnal Hukum* 3, no. 2 (2020): 237-266.

though this study is more towards eco-tourism, what is interesting from Estriani's findings is that SEZ Mandalika faces a number of challenges due to the lack of grassroots community participation. This work was written by answering several questions that were actually premised from the findings of Estriani's research, in which a number of important factors for the success of an SEZ are the participation of the surrounding community. This article also provides a more extensive explanation regarding the factor of community participation along with other factors obtained from various experiences of SEZs abroad, in order to facilitate better policy and regulatory making;¹⁴ 3) *Kawasan Ekonomi Khusus dan Pembangunan Ekonomi Regional: Sebuah Studi Literatur* by Suryani and Febriani in 2019, this work by Suryani and Febriani is a review of legal literature from various SEZs in Indonesia. Even though the research object is only based on two SEZs in Indonesia, namely: SEZ Mangke and SEZ Tanjung Lesung, this research draws generalizations which according to the authors are not really representative enough. Therefore, this paper is written with the attention that there is no panacea for the development of SEZ, both in Indonesia and overseas. The significance of this work compared to that of Suryani and Febriani is that the aim of this work is to provide a view that seems to be generally accepted but is based on experience and lessons learned from various SEZs abroad which in common sense can be generalized with a contextual tweaks;¹⁵ 4) *Legal Aspect of the Implementation of Land Acquisition for Development on Tourism Special Economic Zone* by Sibuea in 2019, this research by Sibuea has a very narrow scope, which actually focuses on normative juridical aspect of land acquisition processes in the Mandalika SEZ and Tanjung Kelayang SEZ. The findings of Sibuea's research found that the process and mechanism for

¹⁴ Heavy Nala Estriani, "Kawasan Ekonomi Khusus (KEK) Mandalika dalam Implementasi Konsep Pariwisata Berbasis Ecotourism: Peluang dan Tantangan" *Mandala: Jurnal Hubungan Industrial* 2, no. 1 (2019): 64-79.

¹⁵ Nurafni Irma Suryani and Ratu Eva Febriani, "Kawasan Ekonomi Khusus Dan Pembangunan Ekonomi Regional: Sebuah Studi Literatur," *Convergence: The Journal of Economic Development* 1, no. 2 (2019): 40-54.

implementing land acquisition in the SEZs resulted in land conflicts. What is unique about the research by the authors that is distinct from Sibuea's is that although it does not focus specifically on the land acquisition process of the SEZ, this work discusses the complexity of expropriation which actually still has relevance to the land acquisition process. Furthermore, this paper develops more deeply the issue of expropriation with various overseas experiences in relation to the practice of international economic law where SEZ has very high foreign exposure. Furthermore, after reading the research findings from Sibuea, it actually strengthens the recommendations of the authors regarding the importance of clear and transparent legal construction for the success of the SEZ;¹⁶ and 5) *Tumpang Tindih Kewenangan Pengembangan Kawasan Ekonomi Khusus Batam* by Dalla and Hutabarat in 2018, this research by Dalla and Hutabarat emphasizes dualism in authority and SEZ management in Batam due to local autonomy. The problem of dualism of authority has resulted in disharmony between the two institutions in administering effective governance. Various governmental efforts have also not been able to resolve this problem. The research by Dalla and Hutabarat is different from the focus of the study by the authors, but in fact this research by Dalla and Hutabarat again reinforces the findings of the authors regarding the importance of collaboration between various levels of government to ensure the smooth running of the SEZ. In fact, the authors' study also extends to the possibility of collaboration between the private and public sectors to ensure the seamless implementation of a pro-business and government SEZ based on documented best practices.¹⁷ A brief description of each of the previous studies and their distinction from the topic of this study (hence, novelty) can be seen in each footnote for reason of readability.

¹⁶ Harris Y. P. Sibuea, "Legal Aspect of the Implementation of Land Acquisition for Development on Tourism Special Economic Zone," *Negara Hukum* 10, no. 2 (2019): 191-210.

¹⁷ Alexander Yanuard Dalla and Friska Natalia Hutabarat, "Tumpang Tindih Kewenangan Pengembangan Kawasan Ekonomi Khusus Batam," *Jurnal Inovasi Kebijakan* 2, no. 2 (2018): 139-148.

The formulation of the problem which is the focus of this research also has novelty in its practical sense by looking at potential sectors that SEZ policy makers in Indonesia can focus on. These findings can be achieved by examining various literatures and deducing potential sectors for SEZ in Indonesia accompanied by extensive elaboration of these sectors. Practically in its application, this approach is novel because it has never been done by previous studies. In addition to further signify the uniqueness of this paper, is that from various literature on SEZ (especially relating to Indonesia), there is almost no research that examines the historical aspects of the development of the SEZ itself which will later be useful in terms of providing insight regarding future SEZ developments so as to be able to position Indonesia in a strategic and favorable position, first and foremost to deal with this changing global demand which will be beneficial for policy making.

The objectives of this research are to discern the development of SEZs in order to comprehend its historical upbringings as well as the measures of SEZs success based on the indications from various overseas literatures. This first objective will also scrutinize the critical issues regarding the SEZs' governance against international economic law's compliance, which will be beneficial in the further elaboration and analysis of this paper. The second objective of this research would be to find the best and potential emerging sector for the Indonesian SEZ. In this part, the authors will dig deeper into the prevalence and dynamic nature of the financial services sector in SEZs, along with bringing the case for financial service in support of SEZ, which would be beneficial in positioning Indonesia's SEZ into meeting future global demands. The last objective of this paper would be to provide suggestions and recommendations in terms of policy-making and regulatory reform ideas, which will be built upon earlier findings. A conclusion will be provided at the very end of this paper to sum up the overall findings of this paper.

This entire research is constructed using normative juridical legal research. The data that will be the main source of reference for this research analysis is secondary data which consists of legal

materials which are authoritative texts known in legal research.¹⁸ The secondary data used will be obtained from a literature study. The secondary data used mainly come from foreign literature because this study does not only focus on the scope in the Indonesian context, but also from various foreign sources to build a commonly accepted generalizations, one way or another considering that whenever discussions about SEZs arise, it is impossible to only limit the outlook at the context of a particular jurisdiction. The data obtained will then be deduced and analyzed qualitatively. The practical benefits of this research are not only limited for the formulation and development of SEZs policies and regulations in Indonesia, but are academically beneficial for the development of a body of knowledge in relation to the studies of SEZ in Indonesia.

AN INTRODUCTORY REMARK ON SEZs

The Development of SEZs: SEZ 1.0 to SEZ 5.0

The developing trend of SEZs as sovereign economic growth mechanisms is covered in this part of the paper. Since the very first intentional zone was established in Shannon, Republic of Ireland—SEZs have changed significantly, evolving from initially “enclaves” to the current SEZ 5.0. The perfect illustration of SEZ 1.0 can be seen in 1959, particularly in Shannon, Republic of Ireland, where the very first region in the form of an enclave specifically for industrial activities was created.¹⁹ SEZs was originally focusing their configuration for exports (called “export processing zones” or “EPZs”)—have existed

¹⁸ David Tan, “Metode Penelitian Hukum: Mengupas dan Mengulas Metodologi dalam Menyelenggarakan Penelitian Hukum,” *NUSANTARA: Jurnal Ilmu Pengetahuan Sosial* 8, no. 8 (2021): 2463-2478.

¹⁹ Robert Mogielnicki, “Mapping Free Zones in the Gulf: Trends and Dislocations” in *A Political Economy of Free Zones in Gulf Arab States*, ed. Timothy M. Shaw (Cham: Palgrave Macmillan, 2021), pp. 1-22.

from the 1970s, predominantly in the eastern Asia and South America.²⁰ The majority of the goods created in EPZs—typically more than 80% of total production—must be shipped abroad. EPZs are typically gated and restricted-access areas with stringent border checks.²¹

It symbolizes an autonomous commercial growth policy by a country that encourages business and draws in foreign capital through the utilization of national legislation, rather than international economic law mechanisms (like those of GATT or WTO).²² EPZs (along with SEZs) enable governments to experiment and create novel approaches at a more localized levels beneath an “exclusive” commercial governance, unlike agreements with other states that occasionally call for challenging application at the level of the whole state’s domain.²³ At some point, EPZs might potentially be seen as an even more flexible “pilot” form of the international economic law initiatives in unifying worldwide trade, whilst still operating under a state’s total autonomy. The aforementioned approach was effective in a number of states or markets soon after more than a decade of EPZs, like in Korea, Taiwan, China, Vietnam, and Bangladesh.²⁴

The beginning stages of SEZs—namely EPZs, also known as “SEZ 1.0,” were effective in that they largely achieved their primary

²⁰ SEZs were created initially to draw capital from overseas to invest in industrial activities at labor-intensive countries, whilst also promoting exports and participation in global commercial activities. See Ekaterina Turkina and Ari Van Assche, “Global Connectedness and Local Innovation in Industrial Clusters,” *Journal of International Business Studies* 49, no. 6 (2018): 706-728.

²¹ Seth Schindler and J. Miguel Kanai, “Getting the Territory Right: Infrastructure-Led Development and the Re-Emergence of Spatial Planning Strategies,” *Regional Studies* 55, no. 1 (2021): 40-51.

²² Zeng, “The Past, Present, and Future of Special Economic Zones and Their Impact.”

²³ Chaisse and Dimitropoulos, “Special Economic Zones in International Economic Law: Towards Unilateral Economic Law.”

²⁴ Zeng, “The Past, Present, and Future of Special Economic Zones and Their Impact.”

goals of luring foreign investment, boosting exports, and benefitting from foreign exchange. Nonetheless, SEZs possess drawbacks as well; that they frequently turn into isolated areas that depend largely on continuous financial concessions from the government while contributing little to the wider economic growth of a country.²⁵

Due to the aforementioned drawbacks and the evolving socioeconomic and governmental landscape globally, multiple nations started to adopt an increasingly contemporary definition of SEZs, characterized by being multipurpose, larger in scope, and far less dependent on governmental incentives. These SEZs are sometimes referred to as “SEZ 2.0,” with some nations, like China, designating town or an entire region as a SEZ in order to try out a larger scale and market-focused economic policies.²⁶ Such a strategy acted as a catalyst for China’s swift socioeconomic development. Since then, the number of such extensive SEZs has grown substantially. The SEZ demand is a result of the increased state rivalry for attracting foreign investment as well as an upsurge of domestic policies related to industry.²⁷

The next stage of SEZ development was pushed by a recent craze in the industry and manufacturing sectors, namely the momentum and movement toward an increasingly all-encompassing and holistic strategy as global warming and sustainable development grow in importance. In order to create holistic approaches addressing worldwide shifts into environmentally friendly and sustainable

²⁵ Zeng.

²⁶ In the South China Sea, Hainan has an extensive tradition of being a major hub for trade. Therefore, since 1985, the entire island Province of Hainan has been designated as SEZ by the Chinese Government, making it among the very first provinces to be launched as entirely a SEZ. Some analysts also asserted that Hainan was strategically chosen since being a single-island province which was cut off from Beijing’s political influence and would be subject to a lesser political intervention. See Bret Crane et al., “China’s Special Economic Zones: An Analysis of Policy to Reduce Regional Disparities,” *Regional Studies, Regional Science* 5, no. 1 (2018): 98–107.

²⁷ Zeng, “The Past, Present, and Future of Special Economic Zones and Their Impact.”

development alongside trade and investment laws, with greater domestic and communities' inclusion, the "SEZ 3.0" shift integrates the lessons learned from SEZ 1.0 and 2.0.²⁸ These zones are typically referred to as "eco-industrial parks" or "EIPs." An EIP is usually characterized as a specific space for industrial purposes at an appropriate location that guarantees sustainable development by means of incorporating socioeconomic and environmental considerations.²⁹ It is becoming more widely acknowledged as an efficient instrument for resolving issues pertaining to equitable and environmentally conscious industrialization within the context of the Sustainable Development Goals (SDGs). On the other side, it is also employed to meet local and worldwide sustainability obligations whilst addressing global requirements for an environmentally-friendly supply chain.³⁰

As part of the "SEZ 4.0" transformation, SEZs are additionally shifting into greater value-added service-based sectors (like financial and commercial service) alongside "favorable to businesses" rules and regulations. For instance, China has planned to employ free trade zones (FTZs) as a means for trying new initiatives to enable wider trade in addition to opening up its service industries (like financing), by relaxing regulations on foreign and Chinese firms—kicked off by the launch of the Shanghai Pilot FTZ in 2013.³¹

Given the advent of technological advances and the fourth industrial revolution, nations started to use these recently developed instruments to create "SEZ 5.0." Companies engaged in commerce

²⁸ Etienne Kechichian and Mi Hoon Jeong, *Mainstreaming Eco-Industrial Parks* (Washington, D.C.: World Bank, 2016).

²⁹ Brian Baldassarre et al., "Industrial Symbiosis: Towards a Design Process for Eco-Industrial Clusters by Integrating Circular Economy and Industrial Ecology Perspectives," *Journal of Cleaner Production* 216 (2019): 446–460.

³⁰ Junjun Liu et al., "Green Supply Chain Management and the Circular Economy: Reviewing Theory for Advancement of Both Fields," *International Journal of Physical Distribution and Logistics Management* 48, no. 8 (2018): 794–817.

³¹ Guangwen Meng and Douglas Zhihua Zeng, "Structural Transformation through Free Trade Zones: The Case of Shanghai," *Transnational Corporations* 26, no. 2 (2019): 95–115.

and shipping in such SEZs can submit codified data, primarily digital, using an entirely computerized customs program, resulting in significantly quicker and far more precise customs clearances.³² The SEZs previously discussed and their most significant traits are summarized in Table 1 below.

TABLE 1 The Development of SEZs and Their Main Features

Generation	SEZ Designation	Key Features
SEZ 1.0	Export Processing Zones	Emphasizing foreign investment and exports, with a lack of connections to the overall economy.
SEZ 2.0	Multi-function SEZ	Broader in size, multi-functioning, and better connected to the local and overall economy.
SEZ 3.0	Eco-industrial parks	Balancing between the country's competitiveness and sustainability, with efforts in consolidation of both aspects.
SEZ 4.0	Free Trade Zone	Zone's focus is on providing value-added service sectors and shifts towards "favorable to businesses" initiatives.
SEZ 5.0	Intelligent Zones or Digital Zones	Manufacturing and services use technological innovations, and commercial and industrial processes are entirely incorporated with digitized and computerized information.

Source: Compiled and summarized by the authors

³² Zeng, "The Past, Present, and Future of Special Economic Zones and Their Impact."

Gauging the Success of SEZs

It is challenging to assess the success and immediate impact of SEZs because there is a shortage of data regarding this and it is challenging to identify suitable “benchmark” for contrasting the results to. The positive influence of SEZs in promoting socioeconomic and business growth appears to vary substantially throughout nations and regions, according to dispersed surveys.³³ Successful SEZs have the power to bring in a significant amount of foreign as well as domestic capitals, and they also significantly increase capital investment, job creation, and economic development. The main goal of SEZs in emerging markets is typically to establish, expand, and enhance industries by luring foreign direct investment, and countries that have historically encountered difficulty luring foreign investment exhibit a greater willingness to embrace SEZ.

It is challenging to evaluate the “net benefit” of a SEZ initiative given the challenges in obtaining information and benchmark. A much recent research project analyzes 346 SEZs in 22 emerging economies, including South Korea, employing information gathered from satellite imagery of illuminated areas as a novel method to gauge SEZ activity.³⁴ The research’s main discovery reveals that SEZs have trouble substantially outperforming the real economy of the country. Only a few of the research’s observed SEZs saw development that was significantly greater than the overall standard, and a lot saw growth that was slower than anticipated—with one notable consensus, SEZs generally fare more effectively in countries which are transparent, dynamic, and innovative.³⁵

Another survey by Lu et al. showed that SEZs in China have boosted the number of businesses in the targeted regions which has had a beneficial impact on investments in capital, job creation,

³³ Zeng.

³⁴ Susanne A. Frick, Andrés Rodríguez-Pose, and Michael D. Wong, “Toward Economically Dynamic Special Economic Zones in Emerging Countries,” *Economic Geography* 95, no. 1 (2019): 30–64.

³⁵ Frick, Rodríguez-Pose, and Wong.

manufacturing efficiency, and remuneration.³⁶ The projected financial benefits of the SEZ throughout a three-year period are £12.8 billion (US\$15.62 billion).³⁷ A further examination of 2,660 SEZs established in China between 1998 and 2018 reveals that the creation of SEZs along with associated bureaucratic enhancements to quality greatly increase foreign capital entering China, boosting the overall economic development of the country.³⁸

SEZs have proven crucial in the Middle East in promoting export-oriented development for nations like the United Arab Emirates. The SEZs in the United Arab Emirates, in which the very first free-trade area was founded at the Jebel Ali Port in 1985, are among the most prominent models. In total, it created 135,000 employment opportunities, earned over £65.6 billion (US\$80 billion) in exports, and has contributed to more than 20% of Dubai's GDP.³⁹ One thing is for sure, the evaluation of numerous results demonstrates that the success of SEZs cannot be measured by homogeneous benchmark or generalized across countries.

However, in this paper, the authors would like to map several "agreed" and "acknowledged" measures of SEZs success based on several scholarly studies, namely:

1) Export Enhancement and Market Diversification

SEZs have not always had a beneficial impact on exports in a number of states. Davis et al. contend that nation-states which do not remove trade barriers and do not implement export-oriented policies are more inclined to see a adverse effect on exports despite having

³⁶ Yi Lu, Jin Wang, and Lianming Zhu, "Place-Based Policies, Creation, and Agglomeration Economies: Evidence from China's Economic Zone Program," *American Economic Journal: Economic Policy* 11, no. 3 (2019): 325–360.

³⁷ Lu, Wang, and Zhu.

³⁸ Yijia Song et al., "Effects of Special Economic Zones on FDI in Emerging Economies: Does Institutional Quality Matter?," *Sustainability (Switzerland)* 12, no. 20 (2020): 1–21.

³⁹ Jung Taik Hyung, "Promoting Dynamic & Innovative Growth in Asia: The Cases of Special Economic Zones and Business Hubs," ed. Hyung-Gon Jeong and Douglas Zhihua Zeng, *KIEP Research Paper Policy Analysis* (Sejong City, 2018).

SEZ.⁴⁰ Nations that kept a number of trade impediments and remained stubborn in implementing imports substituting regulations, will limit the positive effects of SEZs on exports.⁴¹ On the other hand, a research in Poland discover a favorable correlation between SEZs and firm-induced export—primarily through increased firm output and overseas investments.⁴² The deep-observational research also supports SEZs' beneficial effects on a country's export tendency, export frequency, and export magnitude.⁴³

For the case or market diversification, studies have also evaluated the influence of SEZs on product diversification in South Asia and discover the inconsistent effects that SEZs poses. When these results were pulled, India was expanding its SEZ policy significantly. Research by Alkon in 2018 examined the diversification performance of SEZs in India and discovered notable variations among the various SEZs in terms of their export statistics. In many instances, SEZs also failed to achieve the desired diversification standards.⁴⁴ Based on the findings regarding SEZs' impact towards export diversification, it is safe to say that SEZs' contributions to export diversification have differed according to nation, industry, and the particular nature of the commodity. As a result, the anticipated impact of bringing a SEZ can

⁴⁰ Christina L. Davis, Andreas Fuchs, and Kristina Johnson, "State Control and the Effects of Foreign Relations on Bilateral Trade," *Journal of Conflict Resolution* 63, no. 2 (2019): 405–438.

⁴¹ Allison Murray, "Given Today's New Wave of Protectionism, Is Antitrust Law the Last Hope for Preserving Free Global Economy or Another Nail in Free Trade's Coffin?," *Loyola of Los Angeles International and Comparative Law Review* 42, no. 1 (2019): 117–146.

⁴² Jarosław Michał Nazarczuk and Stanisław Umiński, "The Impact of Special Economic Zones on Export Behaviour. Evidence from Polish Firm-Level Data," *Ekonomie a Management* 21, no. 3 (2018): 4–22.

⁴³ Nazarczuk and Umiński.

⁴⁴ Meir Alkon, "Do Special Economic Zones Induce Developmental Spillovers? Evidence from India's States," *World Development* 107 (2018): 396–409.

be significantly beneficial, although this is highly dependent on the state's socioeconomic climate (again context-wise).⁴⁵

2) Industrial Advancement and Knowledge Transfer

Knowledge transfer is an essential industrial practice that results in the adoption and distribution of experiences, expertise, technologies, tools, assets, and commodities to the recipient.⁴⁶ Initial examinations regarding the contribution of SEZs to a country's industrial modernization and knowledge transfer also produce varying findings. According to a few studies, the knowledge capacities of SEZ employees are affected considerably by the existence of SEZs. There is strong indication that SEZs have facilitated industrialization and knowledge transfer in the recently developed East Asian countries, like South Korea, China, and the Philippines,⁴⁷ — where major technological advancement in the semiconductor industry has taken place, mostly in manufacturing areas (particularly, SEZs).⁴⁸ In the Philippine eco-zones, at which manufacturing has largely given way to engineering, research, and development, the Philippine SEZ Administration has observed a significant increase in zone workers' talent and skill levels.⁴⁹

Another research revealed further illumination on this subject matter. According to a working paper by Hausmann et al., their

⁴⁵ Ronald B. Davies and Arman Mazhikeyev, "The Impact of Special Economic Zones on Exporting Behavior," *Review of Economic Analysis* 11, no. 1 (2019): 145–174.

⁴⁶ Vander Luiz da Silva, João Luiz Kovaleski, and Regina Negri Pagani, "Technology Transfer in the Supply Chain Oriented to Industry 4.0: A Literature Review," *Technology Analysis and Strategic Management* 31, no. 5 (2019): 546–562.

⁴⁷ Zeng, "The Past, Present, and Future of Special Economic Zones and Their Impact."

⁴⁸ Rachael M. Joo and Jose S. Medriano, "Imperial Run-off: Korean Golf in the Clark Special Economic Zone in the Philippines," *Inter-Asia Cultural Studies* 23, no. 1 (2022): 1–27; Rajah Rasiah and Siu Hong Wong, "Industrial Upgrading in the Semiconductor Industry in East Asia," *Innovation and Development* 11, no. 2–3 (2021): 413–440.

⁴⁹ Jana M. Kleibert, "Exclusive Development(s): Special Economic Zones and Enclave Urbanism in the Philippines," *Critical Sociology* 44, no. 3 (2018): 471–485.

analysis of SEZs in Panama are showing that SEZs are in fact providing Panamanians with secure and well-paying employment opportunities that demand a greater degree of skill, training and expertise—hence, demanding the workforce to upgrade through knowledge and technology transfers.⁵⁰ The Hausmann et al. research lends credibility to the idea that those who were immigrants, particularly those drawn by SEZs, are creating beneficial ripple effects in employment sectors that boost the productive capacity of Panamanian workforce. In fact, in much more sophisticated industry sectors as well as among employees with the highest levels of education, these effects are typically more pronounced.⁵¹ A further research utilizes nighttime illumination data from 346 SEZs in 22 developing nations as a measure for both the success of the SEZ and the local economy. The findings demonstrate that SEZs have a beneficial effect on the financial well-being of the regions bordering those SEZs. The geographical extent of development spillovers is constrained, and they exhibit a significant impact of radial decline. Additionally, SEZs in places with greater isolation appear to exert lesser of an effect on nearby regions.⁵²

3) Employment Opportunities

Numerous studies have examined the connection between SEZs alongside numerous labor sector consequences, including the impact of SEZs on creating employment, labor conditions, and the formation of unions.⁵³ To investigate the link between SEZs and creation of jobs, Zheng drew from Chinese SEZs data. Empirical findings show that

⁵⁰ Ricardo Hausmann, Juan Obach, and Miguel Angel Santos, “Special Economic Zones in Panama: Technology Spillovers from a Labor Market Perspective,” *Special Economic Zones in Panama: A Critical Assessment* (Cambridge, MA, 2017).

⁵¹ Hausmann, Obach, and Santos.

⁵² Susanne Frick and Andrés Rodríguez-Pose, “Are Special Economic Zones in Emerging Countries a Catalyst for the Growth of Surrounding Areas?,” *Transnational Corporations* 26, no. 2 (2019): 75–94.

⁵³ Zeng, “The Past, Present, and Future of Special Economic Zones and Their Impact.”

SEZs generally had a substantial effect on new startups and incumbent company growth; as a consequence, SEZs boost local employment opportunities through the establishment of new employers and the development of currently operating companies.⁵⁴ The legislation regulating labor rights in SEZs is discussed by Cotula and Mouan, who use the case research conducted in Bangladesh, Ethiopia, and Kenya as samples. Collectively, the SEZ legal structures in the three nations show how policies intended to advance the rights to assembly, health and safety, as well as fair working hours.⁵⁵

Bancarzewski and Hardy discover that Polish SEZs have higher labor unionization rates compared to those in the private sector beyond the SEZs. The stark differences in the rates of unionization among corporations within and outside of SEZs indicate in the course of SEZs which are actively encouraging staff forming unions.⁵⁶

It is challenging to make generalizations about the aggregate effect of SEZs due to the contradictory findings of various researches. A pro-business legal and regulatory environment, an unwavering dedication from government officials, and efficiently run governmental services represent a few of the predominant variables that serve crucial parts of SEZs' success. According to numerous research projects and current scholarship, there are indeed plenty of variables that contribute to the inconsistent success of SEZs.⁵⁷

⁵⁴ Liang Zheng, "Job Creation or Job Relocation? Identifying the Impact of China's Special Economic Zones on Local Employment and Industrial Agglomeration," *China Economic Review* 69, no. December 2020 (2021): 101651.

⁵⁵ Lorenzo Cotula and Liliane Mouan, "Labour Rights in Special Economic Zones: Between Unilateralism and Transnational Law Diffusion," *Journal of International Economic Law* 24, no. 2 (2021): 341–360.

⁵⁶ Maciej Bancarzewski and Jane Hardy, "Workers' Resistance in Special Economic Zones in Poland," *Employee Relations* 43, no. 1 (2021): 193–207.

⁵⁷ Douglas Zhihua Zeng, "Special Economic Zones in Sub-Saharan Africa: What Drives Their Mixed Performance?," in *The Oxford Handbook of Industrial Hubs and Economic Development*, ed. Arkebe Oqubay and Justin Yifu Lin (New York: Oxford University Press, 2020), 1008–1023.

Consider This Critical Issue: SEZ Obedience Towards International Economic Law

SEZs are a crucial tool in the government's arsenal for fostering commerce and investments, as was previously stated. One is able to easily notice an exceptionally significant fundamental shift by the government towards the concessions, organization, and broader scheme that SEZs give, as more countries compete in developing the best regulatory environment possible.⁵⁸ In these cutthroat conditions, tensions in the implementation of the policies may occur, causing investors to file objections on their own account or on behalf of their governments to safeguard their investment interests.⁵⁹

Investors are still able to bring claims of (indirect) encroachment or a violation of equal treatment and fairness principles in court according to a foreign investment commitment.⁶⁰ For example, in *Goetz v Burundi*,⁶¹ the complainants contested the revocation of a free zone license in the immediate wake of a regime shift in Burundi. Another ICSID dispute, namely the *Manufacturers Hanover Trust Company v. Arab Republic of Egypt and General Authority for Investment and Free Zones*⁶²—this case was the very first

⁵⁸ Zeng, "The Past, Present, and Future of Special Economic Zones and Their Impact."

⁵⁹ Julien Chaisse, "Dangerous Liaisons: The Story of Special Economic Zones, International Investment Agreements, and Investor-State Dispute Settlement," *Journal of International Economic Law* 24, no. 2 (2021): 443–471.

⁶⁰ Chaisse and Ji, "The Pervasive Problem of Special Economic Zones for International Economic Law: Tax, Investment, and Trade Issues."

⁶¹ ICSID, "Antoine Goetz and Others v. Republic of Burundi (ICSID Case No. ARB/95/3)" (World Bank, 1999).

⁶² ICSID, "Manufacturers Hanover Trust Company v. Arab Republic of Egypt and General Authority for Investment and Free Zones (ICSID Case No. ARB/89/1)" (World Bank, 1993).

documented commercial dispute involving investments at SEZs that result in a binding decision.⁶³

Both cases aforementioned above demonstrate the significance of SEZ administration for foreign investment regulations, with regards to the international economic law. The *Goetz v. Burundi* decision served as a foreshadowing example in which political shifts can reveal the dispute-in-waiting due to the status quo of a SEZ regulation structure can result in violations of widely accepted norms for treatment and safeguarding investors' interest.⁶⁴ SEZs are common governmental phenomena notwithstanding almost always being developed by the national authority using a "top-down" approach.⁶⁵ SEZs range in scale from just one factory to a whole gigantic region or province in this regard.

SEZs are created by nations for an assortment of reasons and purposes. The most prevalent of these purposes is to improve the economic situation of a particular region.⁶⁶ Since country of emerging economies can use its specific regions to gauge the effectiveness of a certain economic policy pilots,⁶⁷ to put it simply, SEZs are oftentimes

⁶³ The contention was made by a New York Bank, which had been granted permission to run a branch office in the Egyptian Special Economic Zone in 1975. This instance was the very first investor-State dispute involving SEZs to be put forward before ICSID for trial.

⁶⁴ Olaoye Kehinde, "Goetz v. the Republic of Burundi I&II: How Foreign Investors Challenge 'Free-Zone Regimes,'" in *International Economic Law and the Challenges of the Free Zones*, ed. Julien Chaisse and Jiaxiang Hu, 1st ed. (Alphen aan den Rijn: Wolters Kluwer, 2019), pp. 310–330,

⁶⁵ Douglas Zhihua Zeng, "How Do Special Economic Zones and Industrial Clusters Drive China's Rapid Development?," World Bank Policy Research Working Paper (Washington, D.C., 2016).

⁶⁶ Julien Chaisse and Jiaxiang Hu, "International Economic Law and the Challenges of Economic Zones: An Introduction," in *International Economic Law and the Challenges of the Free Zones*, ed. Julien Chaisse and Jiaxiang Hu, 1st ed. (Alphen aan den Rijn: Wolters Kluwer, 2019), pp. 1–18.

⁶⁷ Michael R. Castle Miller, "The Ciudades Modelo Project: Testing the Legality of Paul Romer's Charter Cities Concept by Analyzing the Constitutionality of the

employed as a kind of “regulatory sandboxes.”⁶⁸ For instance, similar to FTZs, China has experimented with various economic and business policies via SEZs prior to trying to implement them to a wider audience nationally.⁶⁹ Following China’s lead, several South East Asian countries have also made widespread utilization of SEZs to implement novel economic strategies and draw investors from abroad.⁷⁰ In the United Kingdom, to help small and medium-sized businesses (SMEs) and alleviate the impacts of Brexit, municipal authorities have experimented and created entrepreneurship areas and provided a few rebates on local taxes on real estate.⁷¹ It is important to note that such experimentation through SEZs is indeed feasible, however any government trying to do so must be wary of its greater repercussions.

Another issue worth noting for SEZs is tax incentives. In order to draw in greater amounts of foreign capital, SEZs in Asian countries rely substantially on tax benefits.⁷² Businesses can benefit from incentives like tax concessions in SEZs with the firm backing of the national government.⁷³ For international investors in particular, the benefits may be significant. Although a low-tax environment within

Honduran Zones for Employment and Economic Development,” *Willamette Journal of International Law and Dispute Resolution* 22, no. 2 (2017): 271–312.

⁶⁸ Lotta Moberg, *The Political Economy of Special Economic Zones: Concentrating Economic Development*, 1st ed. (New York: Routledge, 2017).

⁶⁹ Jie Huang, “Challenges and Solutions for the China–US BIT Negotiations: Insights from the Recent Development of FTZs in China,” *Journal of International Economic Law* 18, no. 2 (2017): 307–339.

⁷⁰ Arisara Romyen et al., “Assessing Regional Economic Performance in the Southern Thailand Special Economic Zone Using a Vine-COPAR Model,” *Economies* 7, no. 2 (2019): 1–10.

⁷¹ Ross Brown, Jose Liñares-Zegarra, and John O.S. Wilson, “The (Potential) Impact of Brexit on UK SMEs: Regional Evidence and Public Policy Implications,” *Regional Studies* 53, no. 5 (2019): 761–770.

⁷² Frick, Rodríguez-Pose, and Wong, “Toward Economically Dynamic Special Economic Zones in Emerging Countries.”

⁷³ James Alan Brown, “Territorial (In) Coherence: Labour and Special Economic Zones in Laos’s Border Manufacturing,” *Antipode* 51, no. 2 (2019): 438–457.

SEZs is advantageous for company operations, such tax measures could have unfavorable impacts, as they might result in tax evasion and uncompetitive state practices.⁷⁴ Furthermore, companies who receive tax incentives inside SEZs are able to compete better compared to those who receive nothing at all. The intensity of rivalry among nations in providing benefits is impacted by fiscal incentives and tax cuts. Therefore, benefits from taxes must be meticulously monitored to protect the international norms of competition, especially the ones laid by GATT (i.e., national treatment rule).⁷⁵ Far worse, competition in taxes may have a detrimental impact on the global fiscal frameworks.⁷⁶ As expected, nations may reduce their marginal tax rates to a minimum as part of a “race towards the bottom” scenario brought on by rivalry over taxes. Such governments desire to increase their appeal to overseas capitalists in this manner, but they may come under increasing pressure because it is difficult to get lawmakers to make alterations to their fiscal laws.⁷⁷ Succinctly, SEZs may probably undermine international competition norms in this instance involving taxation. An SEZ may expand the privileged basis as opposed to securely providing concessions to investors, which could make SEZs unlawful according to international taxation laws.

⁷⁴ Sebastian Beer, Ruud de Mooij, and Li Liu, “International Corporate Tax Avoidance: A Review of the Channels, Magnitudes, and Blind Spots,” *Journal of Economic Surveys* 34, no. 3 (2020): 660–88.

⁷⁵ Adam A. Ambroziak and Christopher A. Hartwell, “The Impact of Investments in Special Economic Zones on Regional Development: The Case of Poland,” *Regional Studies* 52, no. 10 (2018): 1322–1331.

⁷⁶ Rosanne Altshuler and Timothy J. Goodspeed, “Follow the Leader? Evidence on European and US Tax Competition,” *Public Finance Review* 43, no. 4 (2015): 485–504.

⁷⁷ Ifeoma Betty Ezike, Angela Ifeanyi Ukemenam, and Ikenna Franklin Chijioke, “Free Trade Zones: A Strategic Evaluation of Nigeria Success (Failure) Story,” *Journal of Management and Economic Studies* 1, no. 5 (2019): 66–78.

Issues of expropriation⁷⁸ within SEZs also caught the limelight of international economic law observers. Despite this, there is no precise distinction made among actions taken by governments that are not entitled to compensation and those that constitute inverse, compensated expropriation.⁷⁹ The interaction that exists between an international investor along with the nation that hosts it is complicated because it relies on conflicting objectives and priorities. On one side, an investor from another country possesses the right to assume specific safeguards from the country that welcomed them because, by investing in a host nation, they are submitting their financial assets to the host country's sovereignty. On the flip side of this narrative, the government has the authority to enact laws within its borders due to its dominance and territorial authority.⁸⁰ In addition to that, the principle that is well-known in international law states that a country are not held responsible for monetary recompense whereas in the ordinary practice of their policing authority that they implement non-discriminatory and genuine legislation that promote the greater welfare of their people (again, public good).⁸¹ Although the state's ability to exercise authority had never been completely unrestricted, but as the legal framework on expropriation continues to evolve, more limitations are being placed

⁷⁸ The idea of expropriation has become commonplace nowadays—that is, the acknowledgment or understanding to the fact that there exist means which, according to the laws and written works of academics, comprise of an act of disposing of someone of its property by the state or a governmental entity for public good. See Abdul Hamid Kwarteng and Thomas Prehi Botchway, "State Responsibility and the Question of Expropriation: A Preliminary to the 'Land Expropriation without Compensation' Policy in South Africa," *Journal of Politics and Law* 12, no. 1 (2019): 98–107.

⁷⁹ Chaisse and Ji, "The Pervasive Problem of Special Economic Zones for International Economic Law: Tax, Investment, and Trade Issues."

⁸⁰ Chaisse and Hu, "International Economic Law and the Challenges of Economic Zones: An Introduction."

⁸¹ Martins Paparinskis, "A Case Against Crippling Compensation in International Law of State Responsibility," *Modern Law Review* 83, no. 6 (2020): 1246–1286.

on that ability. Thus, it is even more crucial to come to an arrangement on expropriation standards within SEZs.⁸²

Compliance with WTO rules for SEZs is also another issue to ponder. However, unless stated to the contrary, SEZs that lie within the territorial limits of member nations of the WTO will be subject to WTO rules and regulations.⁸³ The WTO seeks to strike a compromise among facilitating exporters' and importers' commercial activities and enabling states to uphold their ecological and social priorities.⁸⁴ The manner in which to keep the national treatment norm and SEZ benefits in equilibrium depends upon how the WTO agreement interacts with SEZ incentives. The fact that SEZs go against the GATT's concept of national treatment must be acknowledged.⁸⁵ One could consider SEZs' specialized incentivization style to be discriminatory.⁸⁶

SEZs create an issue that requires more scrutiny as it makes a drive that is influenced by international competitors for bringing in investments; technological developments that downplay the significance of time and region; as well as the service providence tendency which distorts the line between fully spoiling investors or making promises that cannot be kept. The proliferation of SEZ serves as a sign of ambitious economic policy, that frequently results from extensive preparation by municipal, national, and central

⁸² Chaisse and Ji, "The Pervasive Problem of Special Economic Zones for International Economic Law: Tax, Investment, and Trade Issues."

⁸³ Sherzod Shadikhodjaev, "SEZs under the WTO's Scrutiny: Defining the Scope of Trade Issues," in *International Economic Law and the Challenges of the Free Zones*, ed. Julien Chaisse and Jiexiang Hu (Alphen aan den Rijn: Wolters Kluwer, 2019), 216–242.

⁸⁴ Chaisse and Ji, "The Pervasive Problem of Special Economic Zones for International Economic Law: Tax, Investment, and Trade Issues."

⁸⁵ Regis Y. Simo, "Trade in Services in the African Continental Free Trade Area: Prospects, Challenges and WTO Compatibility," *Journal of International Economic Law* 23, no. 1 (2020): 65–95.

⁸⁶ Jennifer L. Tobin and Marc L. Busch, "The Disadvantage of Membership: How Joining the GATT/WTO Undermines GSP," *World Trade Review* 18, no. 1 (2019): 109–132.

governments.⁸⁷ SEZs are a fresh form of cooperation among market forces and the government that illustrates how traditional unilateral action is evolving quickly to serve political as well as economic purposes.⁸⁸ What the government must pay attention to when implementing the SEZ is not to easily lean towards convenience or ambiguity which, if not fulfilled, will not only result in the emergence of international disputes based on the principles of international economic law, but also damage the reputation and the namesake of the country in the international stage. International economic law should be closely considered by governments and lawmakers when creating SEZs. Failure to do so might swiftly lead to lawsuits and rulings by tribunals that many states might consider to be undesirable.

EMERGING SECTOR FOR INDONESIAN SEZ 5.0

The Prevalence & Dynamic Nature of the Financial Services Sector in SEZs

Services-related undertakings have been present in SEZs for quite some time. As a rule of thumb, no SEZ would typically compete successfully in the global market for luring industrial (or service-related) investments without first having top-notch facilities and an atmosphere that encourages business,⁸⁹ this includes intervention

⁸⁷ Panagiotis Delimatsis, "Financial Services Trade in Special Economic Zones," *Journal of International Economic Law* 24, no. 2 (2021): 277–297.

⁸⁸ Chaisse and Dimitropoulos, "Special Economic Zones in International Economic Law: Towards Unilateral Economic Law."

⁸⁹ Cui Liu and Yuzhuo Cai, "Triple Helix Model and Institutional Logics in Shenzhen Special Economic Zone," *Science and Public Policy* 45, no. 2 (2018): 221–231.

from financial intermediaries. On a gradual basis, intermediary activities for supporting industrial operations are the variables influencing the SEZ and those who benefit from it. In this case, electronically facilitated activities like telecommuting, internet, data services, corporate solutions, banking, and financial services grew more and more relatable, primarily due to advancements in technology.⁹⁰

These services proliferated more quickly than more conventionally transacted services like transportation or leisure, in which geographical proximity and the idea of “territory” are still important. The sudden surge in demand for services that are enabled by technology prompts concerns about cost-efficiency in the industrialized world.⁹¹ In this way, SEZs can potentially serve as engines for local economic expansion and growth by drawing in companies offering financial services to set up base of operations within SEZ.⁹² Cross-border provision of such business-related services opens up fresh prospects for international transaction by SEZs at an expense threshold that is becoming more advantageous and allows for diversified exports.⁹³

We cannot deny that any contemporary economy’s foundation and key facilitator is its financial industry. According to a large corpus of socioeconomic research, the development of financial services and long-term economic development are strongly positively correlated.⁹⁴ Especially in the Indonesian context in order to achieve

⁹⁰ Delimatsis, “Financial Services Trade in Special Economic Zones.”

⁹¹ Maria Demertzis, Silvia Merler, and Guntram B. Wolff, “Capital Markets Union and the Fintech Opportunity. “Capital Markets Union and the Fintech Opportunity. *Journal of Financial Regulation*”, *Journal of Financial Regulation* 4, no. 1 (2018): 157–165.

⁹² Delimatsis, “Financial Services Trade in Special Economic Zones.”

⁹³ Richard Kyalo Mutuku, “Africa Rising: A Pathway of Three Frontiers – Internet of Things, Population Growth and Free Trade Area,” *The African Review* 47, no. 1 (2020): 141–160.

⁹⁴ Dinabandhu Sethi and Debashis Acharya, “Financial Inclusion and Economic Growth Linkage: Some Cross Country Evidence,” *Journal of Financial Economic Policy* 10, no. 3 (2018): 369–385.

socioeconomic development, financial services is a “make-or-break” endeavor, particularly in light of the difficulties Indonesia have had in establishing stable financial institutions. Two basic features associated with financial services are that they promote the general welfare while creating an economic ripple effect. Governments thereby intervene in the financial sector to lower overall risk and improve the stability of the financial regime.⁹⁵ Practically speaking, having accessibility to funding along with other financial products and services is a prerequisite for every business-related endeavor. In addition, financial inclusion and accessibility are prerequisites for sustainable development.⁹⁶

The effects of the digital age have been significant but not as apparent in emerging economies. In reality, over fifty percent of the worldwide exports and imports associated with services in developing nations are made by the five Asian countries.⁹⁷ Global financial services hubs quickly expanded as a result of the expansion of the financial services industry, such as Singapore and Hong Kong. There is no denying that Indonesia as one of the largest markets in Asia has the potential to grow into a hub for the activities of the world’s financial services sector. In this case, SEZs will greatly help facilitate the entry and growth of financial service providers to do business in Indonesia. The growth potential of the Asian market

⁹⁵ Fernando Duarte and Thomas M. Eisenbach, “Fire-Sale Spillovers and Systemic Risk,” *Journal of Finance* 76, no. 3 (2021): 1251–1294.

⁹⁶ The three primary functions that the financial services sector and financial technology perform toward achieving the Sustainable Development Goals (SDGs) are as follows. The initial act is to improve how monetary assets are currently allocated to promote sustainable growth. The second entails increasing monetary resources in broad terms, that can help contribute to the SDGs. The third entails utilizing FinTech and the internet of things to immediately accomplish the SDGs itself. See Douglas W. Arner et al., “Sustainability, FinTech and Financial Inclusion,” *European Business Organization Law Review* 21, no. 1 (2020): 7–35.

⁹⁷ The five Asian countries (and territories) are China, Singapore, South Korea, Hong Kong, and India. See Delimatsis, “Financial Services Trade in Special Economic Zones.”

(especially the Southeast Asian market) also cannot be ignored. As the top emerging countries' prosperity is growing, and as a consequence, so are outbound capital movements.⁹⁸ Indonesia just needs to be ready and prepared for receiving such inflows of capitals into the country.

SEZs serving as the global financial services hubs may provide considerable tax benefits, reaching out to as low as zero percent tax on revenue and earnings for a number of decades, in addition to providing complete financial account interchangeability. Several global financial services hubs even went as far as to establish a distinct and autonomous court system to provide an alternate, quick, and efficient method of resolving private and business conflicts in order to outperform their rivals.⁹⁹

In general, wider reforms to regulations are required for a financial SEZ to thrive owing to the unique nature of the financial sector. Policymakers have the option to restrict the geographic reach of these alterations by using SEZs to confine them within the SEZ ecosystem.¹⁰⁰ Indonesia is a particularly fascinating nation to dig into this, despite neither being the first nor the only one to aggressively seek out financial service providers in its SEZs. Indonesia's enormous scale and its maintained industrialization are two factors in determining this premise. Indonesia will certainly need to refocus on the service sector in order to increase the proportion of service industries in its economy and expand its geopolitical power in the world stage.

⁹⁸ Delimatsis.

⁹⁹ As a prime example, Qatar has set up the Qatar International Court and Dispute Resolution Center in Doha, which is staffed by justices with experience abroad. Qatar, which is primarily a nation under civil law, added a common law-based judicial mechanism to make it even more appealing for overseas investors. See Teresa Cheng, "Special Economic Zones: A Catalyst for International Trade and Investment in Unsettling Times?," *Journal of World Investment and Trade* 20, no. 1 (2019): 32–67.

¹⁰⁰ Elizaveta A. Gromova, Natalia S. Koneva, and Elena V. Titova, "Legal Barriers to the Implementation of Digital Industry (Industry 4.0) Components and Ways to Overcome Them," *Journal of World Intellectual Property* 25, no. 1 (2022): 186–205.

The Case of Financial Services Companies in SEZs

The development and subsequent propagation of cutting-edge technological advances in finance, structures, and marketplaces are all made possible by the ongoing, dynamic growth of innovation in financial services. Through its greater emphasis on technological advances instead of the field of finance, financial technology, also known as or Fintech, is revolutionizing the way that financial services operate.¹⁰¹ For governments all over the globe, drawing and supporting the expansion of Fintech startups and companies has emerged as the ultimate goal.¹⁰² A fierce rivalry exists to entice these financial entrepreneurs into a particular jurisdiction. For someone working in a highly monitored industry like the finance industry, the prospect for a simple experimentation and swift debut of a specific financial service or platform in a practical setting by means of the regulatory sandbox may appear extremely appealing.¹⁰³

To further enhance the financial sector, a number governments and associated institutions started the Global Financial Innovation Network (GFIN)¹⁰⁴ in January 2019, in response to meet the demand

¹⁰¹ Douglas W. Arner, Janos Nathan Barberis, and Ross P. Buckley, "The Evolution of Fintech: A New Post-Crisis Paradigm?," *Georgetown Journal of International Law* 47, no. 4 (2016): 1271–1320.

¹⁰² Delimatsis, "Financial Services Trade in Special Economic Zones."

¹⁰³ Delimatsis.

¹⁰⁴ An alliance of more than 70 organizations, the Global Financial Innovation Network (GFIN) is dedicated to promoting innovations in finance in the best possible way for customers. It aims to give progressive businesses a more effective method to communicate with oversight bodies, assisting them as they move between nations and try to commercialize new concepts. For businesses looking to experiment with cutting-edge goods, services, or models of operation in multiple jurisdictions, this involves the option to submit to participate in a pilot program. The GFIN also seeks to establish a fresh structure for collaboration among financial sector authorities on innovation-related issues,

for worldwide coverage to maximize the advantages of streamlined connectivity and technological advancements and expand revolutionary concepts while also ensuring the least amount of regulatory supervision. GFIN enables, for instance, the development of goods, services, or business models across different nations in addition to providing an important platform for collaboration among policymakers in which they can benefit from one another's perspective.¹⁰⁵

The vast majority of the aforementioned fintech-related company operations are capable of taking place in a reasonably safeguarded environment, for instance an innovation center in a SEZ.¹⁰⁶ The regulatory bodies, nonetheless, are constantly on guard as they try to strike a balance between resilience, managing systemic risk, and bringing in financial innovators. Innovation in finance introduces ambiguity to such a degree that lawmakers lack the capacity to support technological advancement in finance while continuing to guarantee accountability and regulation simplification while keeping the integrity of the markets.¹⁰⁷ Fintech makes this trilemma, against which financial managers are frequently faced, with. As a whole, policymakers must take thoughtful measures to handle the possibility of arbitrage in regulations and fragmentation of markets due to the oversight of innovations on the one hand and advances in the financial industry on the other hand.¹⁰⁸

exchanging various perspectives and methods. See Nick Bernards, "Tracing Mutations of Neoliberal Development Governance: 'Fintech', Failure and the Politics of Marketization," *Environment and Planning A* 51, no. 7 (2019): 1442–1459.

¹⁰⁵ Delimatsis, "Financial Services Trade in Special Economic Zones."

¹⁰⁶ Andrea Ciffolilli and Alessandro Muscio, "Industry 4.0: National and Regional Comparative Advantages in Key Enabling Technologies," *European Planning Studies* 26, no. 12 (2018): 2323–2343.

¹⁰⁷ Delimatsis, "Financial Services Trade in Special Economic Zones."

¹⁰⁸ Chris Brummer and Yesha Yadav, "Fintech and the Innovation Trilemma," *Georgetown Law Journal* 107, no. 2 (2019): 235–307.

ENHANCING SEZ 5.0 IN INDONESIA: ESSENTIAL POLICY & REGULATORY REFORMS

SEZs are adapting continuously to correspond with the current business and economic conditions, as well as with international economic laws. The inconsistent outcomes across the entire spectrum demonstrate that SEZs are difficult to get right and often require quite some time to produce significant returns.¹⁰⁹ Despite the fact that the conception and execution of the particular SEZ programs are very context-specific,¹¹⁰ the different lessons learned remain valuable in order to deduce a number of broad, overarching tenets—and this is what this paper strives to achieve, in order to contribute academically to the policy and regulatory reforms in Indonesia, by pointing out several lessons learned by deducing generalized best practices. The significant policy lessons of SEZs are discussed in the paragraphs below taking into account different international experiences with SEZ design, construction, and operation.

The very first suggestion for policy reform is that SEZs should be an essential component of a long-term developmental plan, which is the bigger picture. SEZ initiatives ought to be completely incorporated into the overall economic advancement plans—both in national and regional levels. The SEZ initiatives ought to be created in a way that optimally supports or complements current comparative advantages, or even develops newer comparative advantages or a certain region or country (in this case, Indonesia). Such comparative advantages ought to be supported by thorough tactical planning, practicability, as well as master planning procedures which consider seriously the economic sustainability, market focus, enterprises,

¹⁰⁹ Zeng, “The Past, Present, and Future of Special Economic Zones and Their Impact.”

¹¹⁰ Frick, Rodríguez-Pose, and Wong, “Toward Economically Dynamic Special Economic Zones in Emerging Countries.”

development path, accessibility to facilities technological advancement capacity, and ecological responsibility. These components are all emphasized by lessons learned by China and South Korea.¹¹¹

Secondly, SEZs require strong political and legislative frameworks. As we comprehend so far, to encourage commerce and investment from abroad, SEZs make use of national laws that have been adjusted to suit global demands—Consequently, they may not always adhere to the rules of foreign commercial and investments practices (like those of GATT's and WTO's), given that they remain governed by the pertinent nation's sovereign authority.¹¹² SEZs are nevertheless increasingly under the watchful eye of international laws as a result of greater state pressure in the world stage, particularly by WTO in regards to incentives and benefits. Hence, in order to ensure seamless operations of SEZs, SEZ policies must attempt to embrace as many aspects of global economic and investment norms, ideals, and principles as much as they can. The obligations and duties of multiple stakeholders can also be made clearer with the aid of a foreseeable and straightforward policy and regulatory structure, which can also offer security and assurance to investors and the host country. A system like this also ensures that the appropriate entrepreneurial, social, and ecological criteria prevail in the SEZs whilst also ensuring

¹¹¹ For instance, throughout South Korea's modernization, exports were constantly given the utmost importance, and the authorities set up a large collection of policy tools to support export-oriented sectors, particularly by means of SEZs. On the other side, the primary purpose of SEZs in China is to execute nationwide and localized growth policies by establishing catalysts acting as hubs for industrialization and economic expansion. This is also achieved by utilizing SEZs. See Gift Mugano, "Special Economic Zones: Showcasing Success and Failures," in *Special Economic Zones: Economic Development in Africa*, ed. Gift Mugano (Cham: Palgrave Macmillan, 2021), pp. 181–204,

¹¹² Chaisse and Dimitropoulos, "Special Economic Zones in International Economic Law: Towards Unilateral Economic Law."

that SEZs bring in the appropriate investors.¹¹³ A sound legal framework will also boost SEZs' resilience whilst protecting SEZs from unanticipated threats like political shifts or international economic turmoil. Furthermore, a SEZ's success is further aided by robust, long-term governmental dedication, which guarantees program continuity and sufficient delivery of a range of complimentary products and services. In addition, for the successful execution of the various programs, strong collaboration among the national and local authorities as well as a clear understanding of each party's authority and duties are crucial.¹¹⁴

Of equal importance is the development of a welcoming business climate, such as effective government services to support these SEZs. Overcoming the barriers for conducting business operations in a country constitutes a few of the main goals of SEZ programs. Rather than concentrating primarily on financial benefits like tax relief, that somewhat the norms of the international economic laws are at present increasingly opposing as to deeming them as "unfair competitions," SEZs must make an effort to create a setting that is business-friendly. Furthermore, for the sake of economic growth, these SEZs can also be utilized and employed to be "pilot" for experimental policy and regulatory changes toward higher degrees of market-driven market liberalization in line with the objectives of the international economic laws. This is clearly demonstrated across numerous East Asian jurisdictions, particularly the Shenzhen SEZ.¹¹⁵

¹¹³ Douglas Zhihua Zeng, "What Determines the Heterogeneous Performance of Special Economic Zones? Evidence from Sub-Saharan Africa," *Global Policy* 13, no. 4 (2022): 495–506.

¹¹⁴ Zeng, "The Past, Present, and Future of Special Economic Zones and Their Impact."

¹¹⁵ For instance, Shenzhen's SEZ administration is granted a great deal of autonomy by local laws. Shenzhen SEZ could be managed by either the public or private sector, but the creation of SEZs requires central government-level approval. The argument for removing barriers to trade impeding China's economic growth as well as promoting the liberalization of trade which increases China's exports capacity is supported by the appropriate mix of the public and private sectors in the Shenzhen SEZ management. See Chaisse and Ji, "The Pervasive Problem of

Infrastructure, which includes both tangible and intangible infrastructures, is a further key consideration. For the former, a SEZ needs to possess top-notch interconnectivity in regards to highways, seaports, telecommunications, waste treatment facilities, and so forth, in addition to critical services like steady supplies of clean water, electricity, and fuel. For the latter, key intangible, facilities like labor supplies, instructional and educational programs, technology dissemination channels, and invention spaces must also be provided by SEZs. Policies could be put in place to draw in individuals with specific talents from abroad or other regions of the country when they are not readily accessible domestically. Additionally, it is crucial to encourage breakthroughs in technology and transmission as well as higher-valued industries that correlate to various phases of development in order to stimulate and smooth the process of industrial upgrading. SEZs should eventually be connected to the wider regional economy by means of regional vendor networks.¹¹⁶ Regardless of several “enclave” style SEZs’ previous triumphs, the survival of modern SEZs is becoming more dependent on the economy of their surroundings.

Meticulous preparation, layout, and oversight are frequently required for SEZs to be successful. A thorough evaluation of economic circumstances, interaction, manufacturing base, logistic network, business climate, labor, and land availability should be part of the assessment during the preparation phase, one and another to make sure the SEZ is in an appropriate position and is built around real commercial demands. By means of a public-private collaborative strategy, the private sector could be urged to participate in the seamless and effective running of SEZs. Additionally, a system for supervision and assessment must be in place. Successful SEZ programs can positively influence widespread development, but they are costly and extremely perilous projects. Therefore, laws should be

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¹¹⁶ Zeng, “The Past, Present, and Future of Special Economic Zones and Their Impact.”

established and efficiently carried out to specify the measures for the success of SEZ programs and the requirements for managing the transitions that must be handled when SEZs approach the conclusion of their operational lifespan. This necessitates the use of a strict reporting and appraisal mechanism to track and assess their accomplishments on a continuous and periodical basis.¹¹⁷

Last but not least, SEZs must reconcile industrial expansion with communal and urban development. SEZs' beneficial effects on hosting communities extend far deeper than their financial viability, which is a matter that deserves deep consideration. SEZ programs are impossible to be successful if they ignore ecological sustainability, fall short to provide chances for skilled employees to advance their careers, or gain an edge over their competitors by abusing low-income employees. On the other hand, SEZ programs which emphasize highly skilled employees and aim to create the social structures that promotes upwards mobility, preserving pleasant work atmosphere, and natural environment flourishing will find themselves in an advantageous position to support overall modernization.

CONCLUSION

SEZs are special areas that have different features and goals depending on the changes in the manufacturing and global markets due to technological advancements. They started as export-focused "enclaves" but have evolved into more complex and diverse zones that can offer various sectors and even "smart city" solutions that are environmentally-friendly and digital. To be successful, SEZs need to have regulations and legislation that are aligned with global standards and that can ensure their smooth operation as a separate solution between the government and the market forces. They also need to have solid strategic planning, and a supportive business climate, which includes a functional policy and regulatory system. Most of the current studies focus on the financial services sector for

¹¹⁷ Zeng.

SEZs in Indonesia, but more studies are needed to explore the legal framework and application of SEZs in other sectors and contexts. SEZs are very complicated structures, and they need to be adapted to the local situation and needs in order to be useful. This paper suggests some areas for future socio-legal studies that can combine theoretical and empirical knowledge to produce new insights on SEZs in Indonesia.

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