

AFRICA FREE ZONES ORGANIZATION

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Key legal fundamentals for free zones and special economic zones attractiveness

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INTRODUCTION

ATTEMPT TO DEFINE A FREE ZONE : REMINDER

- The core definition of a free zone is contained in the **Revised Kyoto Convention of the World Customs Organization (WCO)**
- A free zone is a **territorial zone** in which companies have the benefit from a **tax and customs regime which derogates from the general laws of the country**
- In order to benefit from such derogatory measures which are often also accompanied by other advantages, the said companies have to be **approved by an organ** which regulates such approval on the basis of a **number of criteria**
- We can enumerate a large variety of free zones with differing objectives, markets and activities: free trade zones, export processing zones, freeports, enterprise zones, single factory export processing zones, etc.



INTRODUCTION

FREE ZONES CONSTITUTE A VALUABLE TOOL IN ORDER TO OVERCOME SOME OF THE EXISTING CONSTRAINTS TO ATTRACTING INVESTMENT AND GROWING EXPORTS IN A GIVEN ECONOMY

- **Success** of free zones is linked to the **competitiveness** of the national economy and the **continuous management of the zones**
- The **success** of a zone is an **engine** for **economic growth**
- **Industrial transformation** is closely **linked** to a **favorable**, attractive and competitive **regulatory environment**

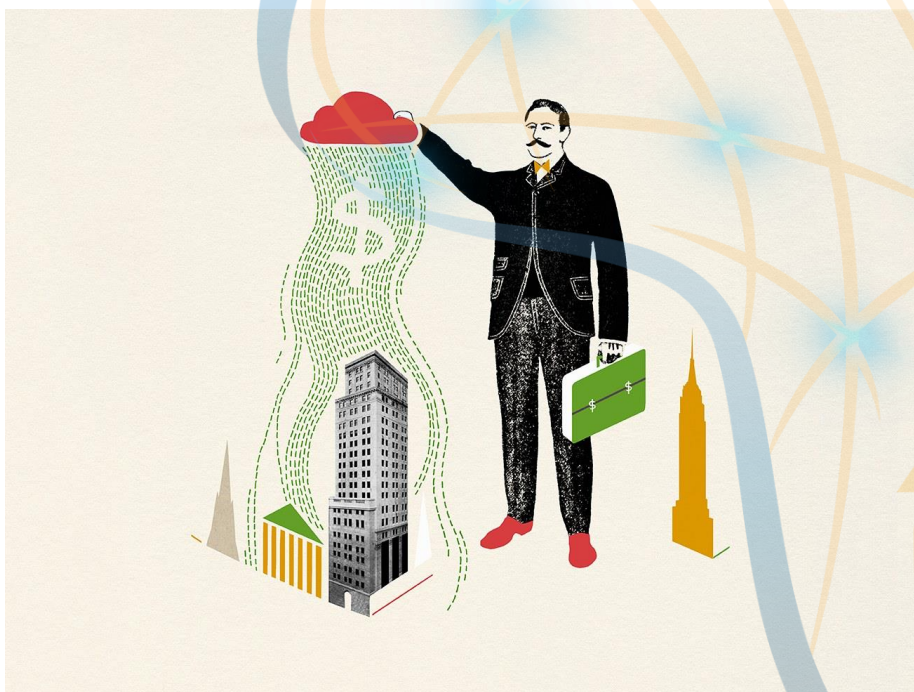
The purpose of this presentation is to:

- **identify investment incentives / legal tools for the purposes of creating a business-friendly environment in free zones (part 1)**
- **high-light the importance of a wider favorable national investment climate in the success of free zones (part 2)**

I. CREATING A BUSINESS-FRIENDLY ENVIRONMENT IN FREE ZONES BY THE IMPLEMENTATION OF INVESTMENT INCENTIVES

1. THE AIM AND DEFINITION OF INVESTMENT INCENTIVES IN FREE ZONES

PRESENTATION OF THE MAIN INVESTMENT INCENTIVES / LEGAL TOOLS



- **Regulatory incentives: attracting investment projects by offering derogations**
 - ✓ Easing of social and labor market requirements
 - ✓ Simplification of administrative procedures for companies within the zone in order to cut red tape
- **Fiscal incentives: easing of the tax burden on the investing companies or their employees**
 - ✓ reduced corporate tax rates / tax holidays
 - ✓ Lower or no import or export duties and taxes
- **Financial incentives: out of hand public spending to attract companies or induce them to invest**
 - ✓ justified by a need to compensate investors for the perceived disadvantage of a particular location

I. CREATING A BUSINESS FRIENDLY ENVIRONMENT IN FREE ZONES BY THE IMPLEMENTATION OF INVESTMENT INCENTIVES

2. THE SETTING UP OF INVESTMENT INCENTIVES IN FREE ZONES

EXAMPLES

▪ Regulatory incentives:

- **Gulf countries:** exemption from limits on foreign ownership
- **MENA countries:** waive restrictive practices towards foreign land ownership
- **Jordan and Kuwait:** labor market regulations eased through easier access to hiring expatriates
- **Tunisia:** wavering of national rules against limited duration employment contracts

▪ Fiscal incentives:

- **Algeria, Egypt, Kuwait and United Arab Emirates:** complete exemption from corporate and private income taxes
- **Lebanon, Morocco and Yemen:** corporate tax holidays that are more generous than what is available under their general investment incentives

HOW INCENTIVES SHOULD BE LEGALLY IMPLEMENTED

▪ Fiscal transparency and policymaking

- Investment incentives policies need to be coordinated
- Investment incentives must be transparent
- Expenditure reporting frameworks and procedures should be developed to publicly report the cost of incentives where the information is available

▪ Designing the incentives legal framework

- Investment Incentives should be made to maximize efficiency
- Free zones must be carefully designed

▪ Evaluation and monitoring incentives

- The ability of the administering body to effectively monitor incentives should be ensured
- The costs and benefits of current and proposed investments incentives should be assessed
- **The investment incentives should have «sunset clauses»**

THE NEED TO GO FURTHER THAN SIMPLE INCENTIVES

INCENTIVES DO NOT COMPENSATE FOR A POOR INVESTMENT CLIMATE

- Experience shows that the incentives do not compensate for a poor investment climate and allocation of financial resources, human capital and time in zones should be devoted to delivering quality services and assuring a **competitive business environment**

THE NEED FOR AN ENABLING ENVIRONMENT

- Attracting investment by the creation of a positive investment climate fostered by, amongst others:
 - Infrastructure
 - Human capital
 - Investor-friendly regulatory frameworks
 - good public governance
 - Rule of law



II. MAIN FINDINGS – THE IMPORTANCE OF A WIDER NATIONAL INVESTMENT CLIMATE

1. A BETTER INVESTMENT CLIMATE IS ASSOCIATED WITH HIGHER LEVELS OF PRODUCTIVITY

INVESTMENT CLIMATE IN FREE ZONES

- ✓ **High levels of corruption** result in **lower levels** of **foreign direct investment**
 - ✓ Destructive self-interest is when politicians use the privileges of free economic zones for their own enrichment
- ✓ **Importance** of trade and transport facilitation
- ✓ **Access** to a **large local** and **regional** market is correlated with higher levels of investment
- ✓ **High quality** infrastructure
- ✓ Long term success of a zone depends on going beyond the gates of the zone

FACTORS DETERMINING PERFORMANCE

- ✓ **Utilities**
- ✓ **Transport and trade facilitation**
 - ❖ Reliable transport and infrastructure
 - ❖ Zone transports and trade facilitation as part of a larger integrated regional development initiative
- ✓ Business **regulatory** environment
- ✓ Tariffs and preferences
- ✓ Level of taxes



II. LESSONS LEARNED: PITFALLS TO AVOID AND BEST PRACTICES

2. IMPORTANT FACTORS FOR THE EFFICIENCY OF THE ZONE

ADEQUATE ENVIRONMENT IN THE INDUSTRY POLICY FRAMEWORK

- **Political leadership** at the **highest level** critical for the success of special economic zones
 - ✓ In **Costa-Rica**, the **President** Jose Maria Figueres played an important **role** by **attracting Intel** in the free zone program
 - ✓ **Vietnam** gave its economic zone program a **high level of political attention**
- **Successful zone** programs are an **integrated** component of a long-term national growth
- The policy instruments must be flexible to adjust the evolving needs of the host country
- Political long term stability is important
 - ✓ This is one of the explanations of East Asian zones success



II. LESSONS LEARNED: PITFALLS TO AVOID AND BEST PRACTICES

2. IMPORTANT FACTORS FOR THE EFFICIENCY OF THE ZONE

THE IMPLEMENTATION OF STRATEGIC PLANNING

- **Strategic planning** is needed
 - ✓ **Lack of noticeable investment** focus in African zones partly due to **insufficient attention to strategic planning and positioning**
 - ✓ Considering **world context** it is **important** that **zone markets** are **tested** and meet investor's needs
- **Comparative advantage** and clear sources of **competitive differentiation**
 - ✓ Bangladesh has a clear comparative advantage in labor
 - ✓ Successful development of Jebel Ali Free Zone in Dubai designed as a regional logistic hub
- **Social infrastructure** such as schools, professional training, hospitals and recreational facilities are highly needed
 - ✓ Attract or train skilled workers
 - ✓ Release the pressure on public infrastructure in the communities around the zone



CONCLUSION

SUCCESS OF FREE ZONES

- Depends on the extent to which they create **links** with the **local economy**
 - ✓ **Generating employment**
 - ✓ **Increasing transfer of know-how**
- **Highlights the necessity that the legal framework for such zones include «sunset provisions»**

MORE THAN INCENTIVES THE IMPORTANCE OF THE INVESTMENT CLIMATE

- **Complexity** of each **national environment** means that **no best practice** that any country could adopt or imitate **can guarantee success**
- **Need for coordination between free economic zones by offering different specialized clusters seems to be another core for success**



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