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The work is concerned with free economic zones classification and basic principles of operation. Foreign experience of free economic zones creation is regarded. Considerable attention is paid to the history of free economic zones organization in Russia. The main causes of failures of their implementation are analyzed. At present the work on creation of special economic zones of main types – industrial and production, innovation and technological, tourist and recreation - has started in Russia. The main part of the work is devoted to Canadian experience of regional development.

JEL Classification: *R0, R1.*

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I. Regional Development in Canada

1. An Introduction to Regional Development in Canada

Russia, like Canada, has to a large extent, similar problems when it comes to their peripheral regions. "When the Baltic States became independent in 1991, the Kaliningrad Region (oblast in Russian), suddenly became an exclave separated from the rest of Russia" (*Joenniemi and Prawitz 1998, 1*). Since then its socio-economic future has been the topic of many discussions, particularly because it is the only Special Economic Zone (SEZ) in Russia at the moment[1]. Because of its large land mass, many regions of Russia have trouble interacting with each other. Special trade and production conditions for these regions may be the only way that they can attract inflow of capital and subsequently economic development.

For Canada the conditions are, in a sense similar. Its large distances between centres of economic activity cause similar problems. In response the Canadian federal government (in fact, some provinces have done as well) have set up special/privileged regional development programs for these challenged regions. These creations are clearly surrogates for SEZ. The one in Ontario, for instance, is called FedNor and covers all of northern Ontario. Others are found in the east as well as in the west.

2. Canadian Regional Development Programs, Surrogate SEZs

This first section of this paper will begin by providing the reader with a brief synopsis of Canada's past and present regional development programs, surrogate SEZs[2], and initiatives aimed at fostering economic development in 'disadvantaged areas.' This section is particularly important in illustrating the shift from a top-down to a bottom-up ap-

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[1] See for instance *Fyodorow, 1998*; *Oldberg, 1998* and *Lange, 1998*. For a look at development potential in the Oblast, see *Hecht, 2005*.

[2] *Guangwen, 2003* points out clearly that there are basically two types of zones in the world: a Territorial Type and a Regime Type. The later is associated with specific firms in a country and the former with the location of firms in space. Canada only has the latter.

proach philosophical approach to regional development, the latter being grounded in endogenous growth theory and entrepreneurial activity[3]. In light of the above paradigm shift this section proposes local based systemic competitiveness as a viable framework for economic development initiatives. This multi dimensional framework is rooted in Michael Porter's (1990, 1996, 1998) paradigm of *Competitive Advantage*.

When the department of Regional Economic Expansion (DREE) was first established in 1969, its purpose was to counteract the perceived widening gap among the more affluent metropolised areas of Canada and the remaining disadvantages 'black holes' of the rest of the country. In other words, a federal department was established to provide development programs for regions that can only be described as special economic zones (SEZs). In total, 23 projects were first created and placed under DREE (*Carvalho and Smith 1992, 6*). Two major economic tools were used to help these SEZs, funds for local infrastructure and tax incentives for private firms. Both acted as incentives, for the "relocation and expansion of dynamic firms in dominant industries in designated growth centres in the less developed regions" (*Carvalho, 2001*). This incentive approach was directed towards attracting industrial branch plants. Branch plants were believed to exhibit rapid rates of innovation and formulation of backward and forwards linkages with the local economy. Optimally, by fostering these economic linkages, the intent was to create local spin-offs and hence replicate the metropolitan model (growth poles) of economic growth. The effects, however, were different. The policy makers often failed to identify 'the propulsive firms in key industries'[4]. The results were meagre at best as indicated by the considerable literature critiquing the policies of the DREE and it was closed as an independent government department in 1982[5].

Another downfall of DREE's policies was the failure to create endogenous jobs and more importantly, create them incrementally. The failure can be attributed to three main reasons: (1) endogenous jobs were not created because "the [subsidised] plant was often in direct

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[3] For an extensive coverage of this new approach please see *Lewis and McNair, 1993*.

[4] Partially because they underestimated the assumptions of perfect information, perfect resource mobility and factor price flexibility (as prescribed by neo-classical theory).

[5] See, for instance, *Coffey and Polése, 1992.*

competition with an endogenous plant [which was not subsidised]..." resulting in a relative decline in the local labour force (*Bradfield 1988, 172*), (2) the skills sought by the newly subsidized plants were not available locally, forcing the plant to import a skilled/educated labour force consequently having little impact on the local job market, and (3) the global shift that took place at this time towards a more versatile economy. Understandably, the inherited nature of branch plants persuaded them to relocate subsequently again upon finding a more profitable region. Rarely did the branch plants rely on the social capital of their new community; they depended upon their interior network for information. Consequently, these firms never did form backward and forward linkages with endogenous business, often widening the disparity gap. In retrospective, past government policies have failed in promoting and rewarding the growth and success of competitive local Canadian companies. The wrong incentive mechanisms were used, the wrong programs were implemented; "hundreds of billion of dollars in government spending were wasted and resources were dissipated in a futile effort to ensure an equitable distribution of opportunities across Canada" (*Lazar 1996, 120*).

It was, therefore, not surprising that "with the growth pole concept losing acceptance, comparative advantage formed the (new[6]) top down approach" (*Carvalho and Smith 1992*). Essentially, the comparative advantage approach acknowledged the fact that different regions have unique attributes and that "the export sector experiences growth in response to [the unique] regional specialisation to markets outside of the region" (*Carvalho and Smith 1992, 6*).

But, by the early-1990s, it was evident that that the fundamental factor attributing to failure was not the theory used but rather the hierarchical top-down approach implemented by a centralized governing agency. Essentially, it was the detachment of the decision-making body from the endogenous economic reality (of the disadvantaged area), which inhibited the ability to identify firms that not only were key in growing industries but more importantly, firms that were innovative,

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[6] Examples of these new programs include the Atlantic Canada Opportunities Agency (ACOA), Canada Economic Development for Quebec Regions (CED-QR), Federal Economic Development Initiative in Northern Ontario (FedNor), and Western Economic Diversification (WD).

self-reliant and compatible to the region. Hence, the birth and adoption of the new, bottom-up approach, and the conceptual shift towards endogenous economic theory[7].

The result was, as alluded to earlier, that in came "community based economic development (which) involves non-directive, decentralised efforts that increasingly depend on (the local) private initiatives" (*Carvalho and Smith 1992, 6*). Hence, community economic development efforts and support are primarily geared towards helping grass-root level development exemplified by endogenous entrepreneurial activity. Clearly, it is important to note that a comprehensive approach to local economic development must focus on business retention, new business formation and business attraction from outside the community. Even more importantly it must evolve in that order.

Today, all Canadian level of governments appear to be moving toward a policy framework, for the SEZ needy regions of Canada, that encourages and reinforces cultivating entrepreneurial activity at the local level and the private sector's pursuit of competitiveness on a national and international level. The fundamental element of economic growth and welfare within this approach is that of innovation – a dynamic force of 'creative destruction', "embodied in new products, new production processes new markets, new sources of raw materials and new forms of organization" (*Malecki 1994, 121*).

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[7] For a good review, see *Beaumier,1998; updated 2002*. For an intensive analysis leading up to the formation of DREE and its demise, as well as the evolution of new programs replacing DREE, see *Brandon and Hecht, 1980*.

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II. Northern Ontario's Surrogate Special Economic Zone (SEZ), FedNor

1. Introduction

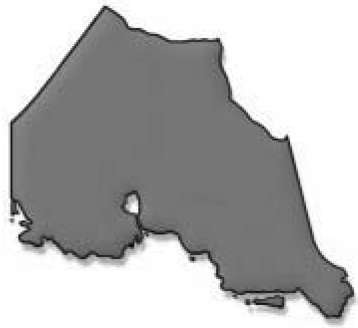
With the new development framework, as described above, receiving acceptance by the federal and provincial government policy branches, the federal government launched in 1987, the Federal Economic Development Initiative in Northern Ontario (FedNor). On its website it claims "FedNor is a federal regional development organization in Ontario that works with a variety of partners, as both a facilitator and catalyst, to help create an environment in which communities can thrive, businesses can grow and people can prosper" (*FedNor 2005a*). Clearly these objects are fundamental to local and regional development of a SEZ whether explicitly called this or not. The present minister responsible for FedNor, Tony Clement claims in his introductory website letter, September 9, 2006, that "Canada's new government believes that local challenges are best defined and met by local communities. With FedNor's help, your government is delivering on its commitment to Northern and rural Ontario" (*FedNor 2005c*).

In light of the above, the major purpose of this section of this paper is six fold:

(1) To provide for the reader the introduction and mandate of the Canadian surrogate SEZ, FedNor;
(2) To present an overview of the governance of FedNor;
(3) To describe its structure and regional programs;
(4) To focus on the nature of help that is provided to the region, its business and individuals to help them develop;
(5) Examine the financial structure of FedNor in term of inflow of funds as well as their dispersion;
(6) Look for indications of successful endeavours and trends in the FedNor region.

The FedNor region or special economic zone, as the name implies, encompasses, as can be seen in *Fig. II-1*, the northern part of Ontario. It encompasses approximately 70% of Ontario's land mass but only some 8% of its population. It consists of the Northeast and Northwest Economic Regions of Canada. In these are found respectively eight

(Nipissing, Parry Sound, Manitoulin, Sudbury, Greater Sudbury Division, Timiskaming, Cochrane and Algoma) and three (Thunder Bay, Rainy River, and Kenora) census divisions.



Source: FedNor 2005b.

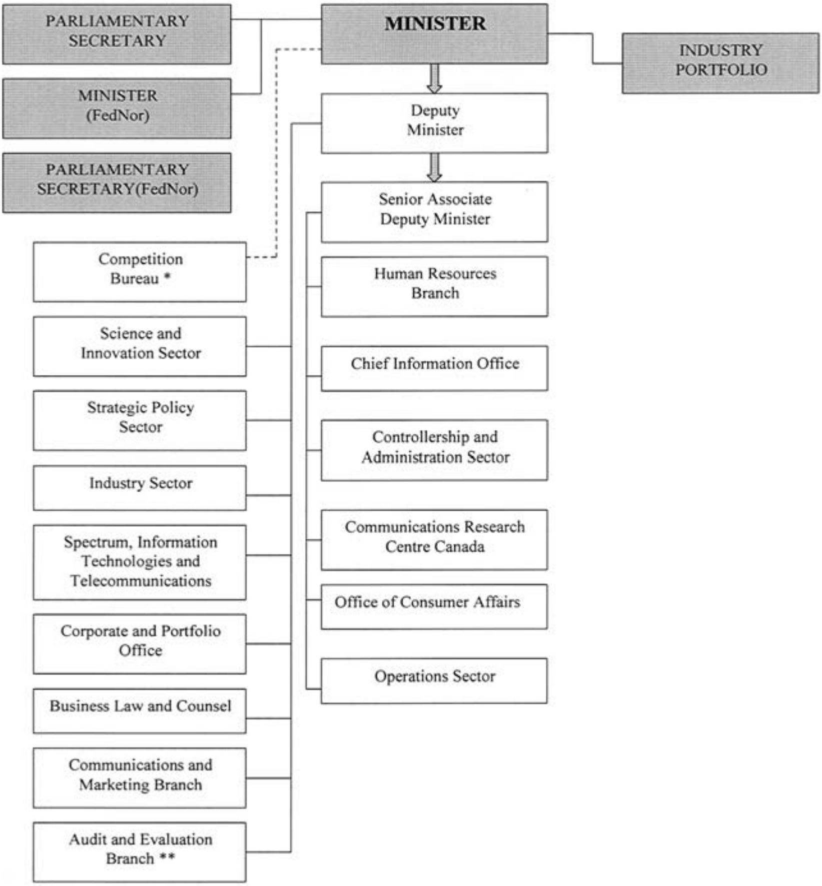
Fig. II-1. FedNor Geographic Coverage

A quick glance at the socio-economic conditions in comparison to the rest of Ontario shows them to be substantially lower. Let me give just a couple of examples: the population change, 1991–2001 was 4.2% for the southern Ontario census divisions and – 3.8% for the north; average income of all workers in the south was $31,449.4 and only $28,672.3 in the north; labour force participation rate was 66.1% for the south and 61.4% in the north and the average value of owned dwellings was $164,229.1 in the south and only $115,888.5 for the north. These figures represent conditions in 2001.

2. Governance

FedNor's mandate is derived from the *Government Organization Act* of 1987. FedNor is presently part of the federal government's Ministry of Industry. "The Minister of Industry has jurisdiction over policy issues regarding: industry; trade and commerce; science; consumer affairs; corporations and corporate securities; competition and restraint of trade, including mergers and monopolies; bankruptcy and insolvency; intellectual property; telecommunications; investment; small businesses; and regional economic development across Canada" (*FedNor 2006b*).

It is solidly imbedded in the Canadian economic governmental economic milieu (see *Fig. II-2*).



* The Commissioner of Competition reports to the Deputy Minister for administrative and financial purposes and reports to Parliament via the Minister in respect of independent law enforcement role

** The Director General, Audit and Evaluation Branch, reports to the Deputy Minister as chair of the Audit and Evaluation Committee

Source: FedNor 2006b.

Fig. II-2. FedNor's Organizational Structure

Its head office is located in Sudbury which also houses the Director General, corporate services (including finance and human resources), policy and planning, communications and claims processing for all of FedNor's programs. Two of the main offices are found in Sault Ste. Marie and Thunder Bay. Additional offices are dispersed over the north and are found in Kenora, North Bay, Ottawa, Parry Sound, and Timmins.

3. Regional Programs

1. Northern Ontario Development Program (NODP)[8]

"The (NODP) was created in 1987 with the mandate to promote economic growth, diversification, job creation and sustainable communities in northern Ontario, through a community-based approach. The NODP invests in projects focussed on one or more of the following six priorities: Community Economic Development; Information and Communications Technology (ICT); Innovation; Trade and Tourism; Human Capital; and Business Financing Support.

2. Community Futures (CF) Program (Ontario)

The Community Futures (CF) Program is an also an ongoing national program administered by FedNor in Ontario. The CF Program supports a network of 61 Community Futures Development Corporations, or CFDCs, throughout rural Ontario – 24 located in the Northern Ontario and 37 in rural Southern Ontario. CFDCs are incorporated, not-for-profit, community-based development organizations, governed by local boards composed of volunteers that serve all rural areas in the province. CFDCs offer a variety of services supporting community economic development and small business growth. They operate local investment funds that provide repayable financing for local small businesses and social enterprises. In addition, CFDCs provide strategic community planning and socio-economic development, including: support for community-based projects; business information; and advisory services. In Northern Ontario, CFDCs are an integral part of FedNor's program delivery network and play an important role in the delivery of FedNor/IC priorities such as youth, trade, and telecommuni-

[8] Much of the information in this section is taken from the FedNor Business Plan 2006–07 (*FedNor 2006a*).

telecommunications through separate agreements under the Northern Ontario Development Program.

3. Other Program Delivery

As Industry Canada's main point of presence in Northern and rural Ontario, FedNor has the organizational capacity and established networks necessary to effectively deliver national initiatives and expanded program delivery opportunities in Ontario. FedNor delivers funding for economic development of Official Language Minority Communities (OLMCs) in collaboration with IC's Ontario Regional Offices. FedNor delivers the Eastern Ontario Development Program (this is a relative new program having only started in 2004) which promotes socio-economic development in Eastern Ontario, leading to a competitive and diversified regional economy and contributing to the successful development of business and job opportunities, as well as sustainable self-reliant communities. The program targets five priority areas including: business and community development; access to capital; skills development; retention and attraction to youth; and technological enhancement."

In terms of actual initiatives taken and the activities involved *Table II-1* gives a good summary.

Table II-1

FedNor Major Initiatives and Activities

Type of Initiative	**Summary of Activities**
1	2
Trade	• Expansion of export and domestic markets • Networking through export clubs • Export and trade related skills development
Innovation	• Technological innovation • Applied research and development • Commercialization of research activities
Investment	• Repayable loans, loan guarantees or equity positions for local private businesses • Establishment of community based investment funds • Financing for business start-ups and/or expansion • Loan loss reserves • Business planning

1	2
Connectivity	• Telecommunication infrastructure • Telecommunication networks • Information and communication applications technology (e.g. E-commerce)
Community Partnerships	• Job creation, economic development and diversification and enhanced business competitiveness • Strategic community economic infrastructure • Work experience for Northern youth in the areas of business development • Broad-based regional co-operative tourism marketing initiatives

4. Focus of Help

According to its website, FedNor focuses on six major area of need in the north.

1. Community Economic Development

The aim of this program is to "create employment and stimulate growth in the North through partnerships with community groups and not-for-profit organizations".

2. Innovation

FedNor is committed to promote interaction between science and industry. To help Northern companies bring new products and services to market, it will especially provide support for the early stage research and development. Some of these have included in the past state-of-the-art mining technology, medical research and biotechnology.

3. Information and Communications Technology

To help with the communication in the sparsely populated north, "FedNor is committed to enhancing telecommunications infrastructure and networks throughout the North. This is an effort to increase opportunities for local business, build high speed data linkages to rural areas and to facilitate community economic development".

4. Trade and Tourism

In regards to trade, FedNor is trying to increase international and inter-provincial trade by assisting firms with trade skills development, trade expansion and export development, in part through electronic commerce especially for small and medium-sized enterprises. Furthermore they try to stimulate tourism by helping infrastructure development, marketing and promotions, product development, training and education.

5. Human Capital

The focus of FedNor in this area of help is rather specific. It wants to help especially women, youth, Aboriginal, and Francophone people in acquiring skills for a knowledge-based economy. For youth, the focus is on helping them get Internships for up to a year, which they will finance up to 90% of total costs if they work for an NGO and 50% if they work for a small local enterprise.

6. Business Financing Support

If a small or medium enterprise can not get normal financing, FedNor will help by working through a wide range of partners that could possible provide financial assistance. It may involve 'loan loss reserves' with financial institutions and by providing capital to community-based investment funds. Since the Community Future Development Corporations is also located in Northern Ontario it also can provide access to capital via loans, loan guarantees or equity investments in order to create or maintain employment.

5. Financial Sources and Distribution

FedNor's two main funding vehicles are the Northern Ontario Development Program (NODP) and the Community Futures Program (CFP). They frequently work together on projects in the north. In 2005–2006 alone, FedNor invested $97 mln directly in projects and leveraging more than $110 mln in additional funds from other sources.

To deliver its programs, FedNor employs a staff of 140 and uses 80% of its resources to run its operations. It ensures that national initiatives and priorities are delivered in a way that is tailored and adjusted to local needs, and that local strategies are able to take full advantage of national programs. Its "bottom-up meets top-down" approach gives communities access to FedNor officers who are able to establish a network of local contacts (FedNor 2006a). Its actual expenditures to the various programs are summarized in *Table II-2*.

Table II-2

FedNor Major Expenditure Outlays

Program Resources Summary ($ mln)	
Northern Ontario Development Program	
Community Economic Development	9.1
Information and Communications Technology	9.4
Innovation	7.2
Trade and Tourism	3.3
Human Capital	3.6
Business Financing Support	3.6
Total – Northern Ontario Development Program	36.2
Community Futures Program	20.3
Eastern Ontario Development Program	9.6
Total Program Resources	**66.1**

Source: FedNor 2006a.

6. Indications of Success and Trends Emphasis

According to updates on the FedNor website, the number of successes in the North is many (*FedNor 2006c*). But, as was mentioned earlier, if one looks at specific indicators of well being in Ontario, or Canada as a whole, the FedNor region does lag substantially behind the south[9]. Unfortunately one does not know what conditions would be like if the North did not have this surrogate SEZ program.

But it should still be pointed out that in 2001, as can be seen from *Table II-3*, the south had more then 10 times as many people as the north, all of its income measures (v20, v36, and v40) were higher as are the value of its owned dwellings (v43), its labour measures (v25 to v27) are better, its employment in better jobs are higher (v28 to v35) except in those sectors with high number of government jobs, its labour force is better educated (v15 to v18) even though the north has proportionally

[9] For an early critical review see *Douglas, 1989*.

more universities (v5), its population is more mobile (v9 to v12), it has received more immigrants and hence has a more diversified ethnic mosaic (v14, v22), and clearly its people rely less on government income for their existence (v37 to v39). It is interesting to note that the north percentage of one person household is higher (v41), and so are its median age (v6), its proportioned of workers that worked in the usual place in 2001 (v23) and its percentage with French as the mother tongue is four times as high (v8) as the rest of Ontario. On the other hand, its proportion of owned dwellings is lower (v42), as are its percentage of people that are protestants (v44) and that are those that have no religion (v45). Together, all these variables seem to point to a less dynamic population and one has to ask the question if the cause is being in the periphery of the province and the country and with its associated disadvantages, and/or is due to the inherent characteristics of the population itself. Clearly, the programs advocated for the north by FedNor tries to address both of these potential causes though its surrogate SEZ programs.

It would be prudent for the Russian government to examine its situation and see if the situation in Canada and the federal government surrogate SEZ programs in northern Ontario, FedNor, are relevant for them. Although the funds involved by the federal government are rather meagre, its psychological implication of being classified and labelled as living in a deprived region with may be rather large. The option of increasing the funds substantially is probably not there from a political perspective. Helping the population to leave the region, as they already do on their own, is again, from a political perspective, not acceptable and is hence not on the FedNor program list. No politician wants his/her region to become depopulated.

Table II-3

Comparison of Well Being between North and South Ontario (Based on 2001 Census Division Averages)

	v3	v4	v5	v6	v7	v8	v9	v10	v10a
North	919,150	–3.8	0.4	39.3	74	16.3	87.4	0.8	11.9
South	11,588,517	4.2	0.3	39	82.9	4.1	86.8	1.3	12

	v11	v12	v12a	v13	v14	v15	v16	v17	v18
North	64.9	2.4	32.6	0.6	1.2	24.8	13.8	11.9	13.6
South	60.1	4.2	35.7	3.3	6.9	26.9	17.3	16.2	16.5

	v19	v20	v21	v22	v23	v24	v25	v26	v27
North	48.7	28,672.3	40,918.6	96.9	83.4	76.3	61.4	55.5	9.6
South	54.9	31,449.4	42,630.5	98.4	81.2	80.2	66.1	62.3	5.7
	v28	**v29**	**v30**	**v31**	**v32**	**v33**	**v34**	**v35**	**v36**
North	16.7	3.6	19.6	14.3	9.7	14.8	4.1	8.1	20,453.5
South	24	4.8	15.9	15.1	10.3	15.2	5.2	7	24,051.2
	v37	**v38**	**v39**	**v40**	**v41**	**v42**	**v43**	**v44**	**v45**
North	71.3	15.7	13	56,869.7	25.9	70.7	115,888.5	36.6	14.7
South	74.6	12.1	13.3	62,967.4	22.9	74.3	164,229.1	48.1	16

Table II-4

Definition of Variables in *Table II-3*

v3	2001 population
v4	Population increase 1991–2001 in %
v5	University present; 1 – yes, 0 – no
v6	Median age in the community
v7	Language: English mother tongue as % of total population
v8	Language: French mother tongue as % of total population
v9	% of population, one year or older, that did not move in the previous year
v10	% of population, 1 year and older, that lived in a different province or country 1 year ago
v10a	% of pop., 1 year and older, that lived in a different dwelling but same province 1 year ago
v11	% of population 5 years or older that did not move in the last 5 years
v12	% of population, 5 years and older, that lived in a different province or country 5 years ago
v12a	% of pop., 5 year and older, that lived in a different dwelling but same province 5 year ago
v13	1991 to 2001 Census Division in migration as a % of total population
v14	% of visible minorities in the community
v15	Population 20–24 years of age studying full time (%)
v16	Population 20–34 years of age with a university certificate, diploma or degree
v17	Population 35–44 years of age with a university certificate, diploma or degree
v18	Population 45–64 years of age with a university certificate, diploma or degree
v19	% of population that have some earnings and are working full time
v20	Average income of all workers
v21	Average income of full time workers only

v22	Language used most often at work - English and/or French (as %)
v23	Worked at usual place (%)
v24	Car transportation to work in %
v25	Labour force participation rate – %
v26	Labour force employment rate – %
v27	Labour force unemployment rate – %
v28	Experienced labour force in manufacturing industries – %
v29	Experienced labour force in fire and real estate industries – %
v30	Experienced labour force in education and health industries – %
v31	Experienced labour force in business services industries – %
v32	Management occupations (%)
v33	Business, finance and administration occupations (%)
v34	Natural and applied sciences occupations (%)
v35	Social science, education, government service and religion Occupations (%)
v36	Median total income of persons 15 years of age and over
v37	Earned income as % of total
v38	Income from government transfers as % of total income
v39	Other money as % of total income
v40	Median income ($) of couple families
v41	% of one-person households
v42	% of owned dwellings
v43	Average value of owned dwelling ($)
v44	% of population that are protestants
v45	% of people with no religious affiliation

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III. Atlantic Canada's Surrogate SEZ Programs, ACOA

1. Introduction

Atlantic Canada, consisting of the provinces of New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland and Labrador, has been a laboratory (testing ground) for regional economic development initiatives, typically under the agency of Canada's federal government. Since the 1960s, the federal government has brought into existence various centralized organizations to reinvigorate the Atlantic economy. Included among these entities are the Atlantic Development Board (ADB, 1962–1969), the Department of Regional Economic Expansion (DREE, 1969–1982), the Department of Regional Industrial Expansion (DRIE, 1982–1987), and the Atlantic Canada Opportunities Agency (ACOA, 1987 – Present)[10]. Provincial governments also established agencies in the mid-1960s to promote regional economic development. In retrospect, these agencies were relegated to land-use planning activities[11].

Regional economic planning was beleaguered by the 'inconsistent visions' of successive federal agencies. Prior to ACOA, development initiatives were undertaken on region-wide basis and embraced several economic sectors (*Heseltine 1998*). For example, the ADB did not develop a comprehensive plan for the entire region, despite a mandate to do so. It was criticized for uncoordinated spending and a lack of "targeting of specific projects to specific regions" (*Hodge and Robinson 2001, 169*). Conversely, DREE followed a comprehensive approach in its effort to eliminate regional disparities by providing regions with municipal infrastructure, transportation, housing, and education. Provincial

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[10] The ADB's Atlantic Development Fund ($180 mln) was used to facilitate regional development by investing in physical infrastructure and creating employment, rather than aiding private industrial firms to locate in Atlantic Canada via location incentives and subsidies (*Hodge and Robinson 2001, 168*). The ADB, formed to eliminate regional disparities, was incorporated into DREE in 1969.

[11] The provincial agencies are Nova Scotia's Voluntary Planning Board (1966), Newfoundland's Department of Community and Social Development (1966), New Brunswick's Community Improvement Corporation (1966), and Prince Edward Island's PEI Development Plan (1967).

grant systems and assistance programs “encouraged scattered development throughout Atlantic Canada” (*Heseltine 1998, 18*).

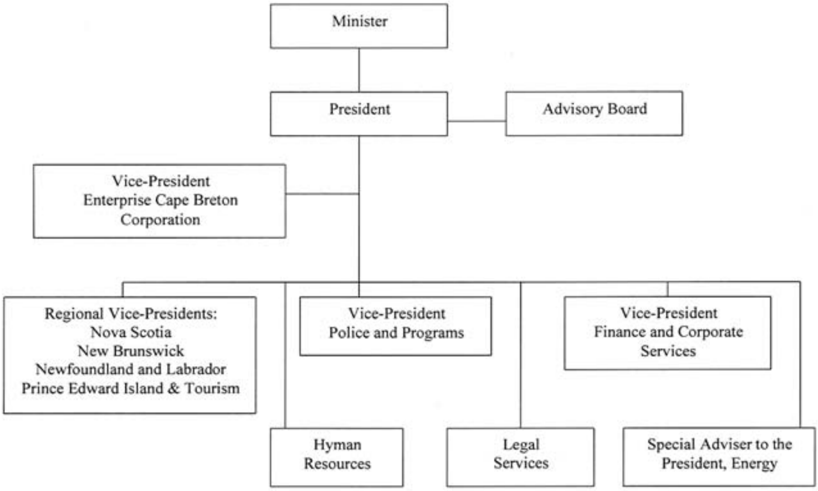
Since ACOA, regional economic development has become a provincial responsibility (*Polèse 1999*). Economic expansion and development programs have become more focused, with an emphasis on “strategic assistance to private-sector initiatives” (*Heseltine 1998, 16*). This represents a change from regional strategies to program strategies. In other words, emphasis has switched from eliminating regional disparities to promoting programs within regions (*Hodge and Robinson 2001*). Assistance is also aimed at economically declining and underdeveloped sub-regions (e.g. Nova Scotia’s Cape Breton Island).

Since the mid-1980s, the move towards Community Economic Development, based on provincial regions, has yielded the recent (since 1993) incorporation of Economic Development Commissions in New Brunswick, Regional Development Authorities in Nova Scotia, Enterprise PEI in Prince Edward Island, and Regional Economic Development Boards in Newfoundland and Labrador. These agencies focus on “coordinating economic development initiatives and capturing benefits from development opportunities” (*Heseltine 1998, 16*).

Considered to be the successor of the ADB, ACOA was established as a federal government economic development organization (i.e. a federal government department that forms the Industry Portfolio) to develop the regional economy of Atlantic Canada via business and employment opportunities. It encourages enterprise, supports business growth, and strengthens the productivity of all economic sectors that create and sustain employment, increase earned incomes, and develop regional economic capacity. Long-term business growth is facilitated by enhancing Atlantic Canada’s economic environment and investment climate. Atlantic Canada is undergoing structural adjustment as its economy shifts from resource-based activities to knowledge-based activities (*Wallace 2003*). Consequently, ACOA’s aggressive and broad-based (yet focused) strategic approach to regional economic development is intended to transform barriers into opportunities. Future opportunities can be realized by building on the region’s existing strengths such as human resources, research capacity, and competitive advantages (*Wallace 2003, 1*).

2. Governance

ACOA's mandate is derived from the *Government Organization Act, Atlantic Canada* 1987. ACOA is part of the federal government's Industry Canada portfolio. Its headquarters in located in Muncton, New Brunswick. A network of 36 regional and field offices are maintained in cities and towns throughout Atlantic Canada. The organizational structure of ACOA is depicted in *Fig. III-1*.



Source: ACOA 2005b.

Fig. III-1. ACOA's Organizational Structure

3. Structure of Regional Programs

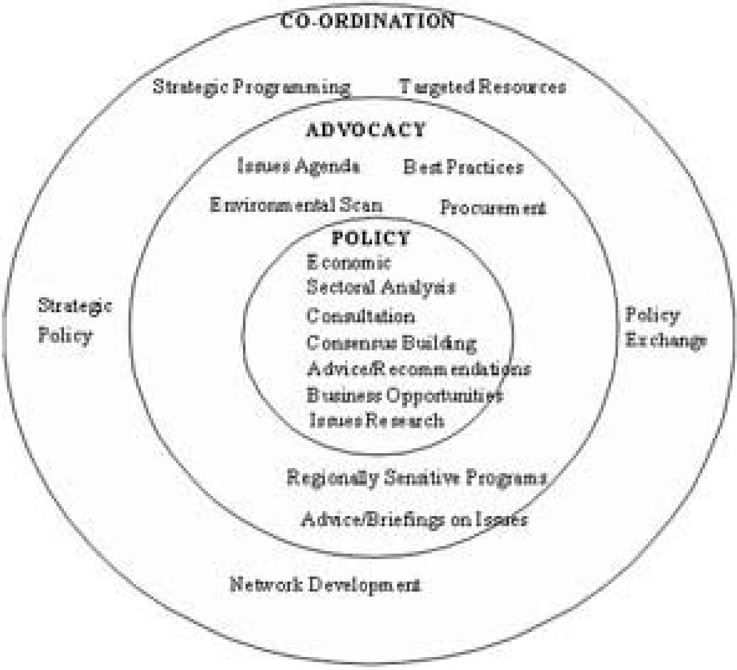
ACOA provides a wide variety of incentive programs to private-sector industries, especially entrepreneurs and small business owners and managers, along with funding for research and development, work-force training, and community economic development to non-commercial organizations, communities, along with academic and research institutions. As noted, emphasis is placed on developing regional economic capacity (i.e. promoting and supporting new opportu-

nities for economic development) by promoting the following strategic priority areas:
(1) policy, advocacy, and coordination;
(2) innovation and technology;
(3) entrepreneurship and business skills development;
(4) community economic development;
(5) access to capital and information; and
(6) trade, tourism, and investment.

These six strategic priorities collectively constitute ACOA's core mandate. They can be condensed into three major 'program activities' – enterprise development, community development, and policy, advocacy, and co-ordinatation. A detailed analysis of the program activities is found in Section II of the Report on Plans and Priorities, 2005–2006 Estimates (*ACOA 2005b*).

ACOA also advocates the interests and positions of Atlantic Canada through a national procurement assistance program "to win an equitable share of federal government contracts for goods and services" through the Supplier Development component of the BDP (*National Resources Canada 1999, 1*). Activities associated with the 'policy, advocacy, and coordination' strategic priority (i.e. program activity) are conveyed in *Fig. III-2*.

According to ACOA (2005b), "Policy is at the centre of this relationship because it provides the research, analysis and advice needed to back up advocacy claims and to guide coordination efforts. Policy, advocacy and co-ordination encompass mandated/legislative issues, strategy, program direction and approach, and horizontal policy issues. ACOA's economic focus is broadened by horizontal policy considerations to include social, environmental and cultural dimensions." Details about each aspect of this program activity are available in Section II of the Report on Plans and Priorities, 2005–2006 Estimates (*ACOA 2005b*).



Source: ACOA 2005b.

Fig. III-2. Interrelationship and Scope of Policy, Advocacy and Co-ordination Functions

ACOA connects its strategic priorities and clientele through various programs and services (i.e. targeted incentives and program initiatives). Key programs and services provided by ACOA include:

1. Atlantic Investment Partnership (AIP)

The AIP facilitates substantial investments in innovation, trade and investment, entrepreneurship and business skills development, and community economic development.

1.1. Atlantic Innovation Fund (AIF)

The AIF (2001–2006) was established to accelerate research and development activities. It "supports projects and activities that have a strategic importance for the development and commercialization of technology in Atlantic Canada" (*ACOA 2006, 6*). Investments are provided to public-sector agencies and private-sector firms in order to establish linkages between the two sectors. Total funding between 2001 and 2006 was $286.7 mln.

1.2. Atlantic Trade and Investment Partnership (ATIP)

The ATIP (2001–2006) assists firms in exporting their products and services through trade missions, export strategy development in key industries, trade education and skills development, and "export internship for graduate students" (*ACOA 2006, 6*). SMEs are given assistance in establishing and expanding export markets. Foreign direct investment is promoted through investment research, marketing campaigns, and 'investment development partnerships' (*ACOA 2006, 6*). Two province-specific programs are offered:

(1) Export Partnering Program – aimed at firms in New Brunswick that have never exported or want to export a new product; and

(2) E-business and Export Mentoring Program (eXPORT) – aimed at firms in Nova Scotia that want to export or establish themselves in e-commerce activities.

Total funding between 2001 and 2006 was $34.4 mln.

1.3. Entrepreneurship and Business Skills Development Partnership (EBSDP)

The EBSDP (2001–2006) assists entrepreneurs to establish new businesses and existing businesses to compete and expand by developing "skills in technology management, innovation, and business management" (*Wallace 2003, 4*). This program has three principal components, each targeting a specific population group:

(1) Innovation Skills Development Initiative – aimed at the recruiting and training of staff members;

(2) Women in Business Initiative-aimed at prospective and existing female entrepreneurs[12]; and

(3) Young Entrepreneurs Development Initiativ-aimed at developing business skills among 15–29 year olds.

Total funding for the EBSDP was 41.6 mln.

1.4. Strategic Community Investment Fund (SCIF)

The SCIF (2001–2006) was established to strengthen the economic base of small and rural communities by stimulating investment and cre-

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[12] The Women in Business Initiative includes the following services: business counselling and community outreach program, business management training allowance, consultant advisory services, and access to financing.

ating employment. It “support[ed] initiatives that help[ed] communities adopt new technologies, improve the competitiveness of their industrial base, and develop selective infrastructure identified as being critical to their economic development” (*ACOA 2006, 7*). This fund “assisted in creating an environment…that encourages and enhances the development of strategic sectors, the adjustment to a knowledge-based economy, the adoption of new technologies and innovative practices, and the capacity to compete in the global economy” (*ACOA 2006, 26*). Total funding between 2001 and 2006 was $174 mln.

2. Business Development Program (BDP)

The BDP (1995–2005) was established to facilitate the establishment, growth (expansion and/or modernization) and competitiveness of small- and medium-sized enterprises (SMEs) through “access to capital in the form of interest-free, unsecured, repayable contributions” (*ACOA 2006, 7*). The program assists non-profit organizations to provide specialized services and infrastructure for SMEs along with agencies involved in Community Economic Development efforts. In terms of growth and competitiveness, loans are provided for “new technology adaptation, software development, management training, [along with] marketing and export development” (*Wallace 2003, 4*). SMEs operating in rural areas and those not meeting the criteria of commercial lenders are targeted. Financial contributions are also provided to non-commercial organizations providing services to SMEs. Total funding between 1995 and 2005 was $1,501 mln.

3. International Business Development Agreement (IBDA)

The Canada/Atlantic Provinces Cooperation Agreement on International Business Development (*IBDA, 1994–2004*) was established to optimize trade and export opportunities for SMEs. Specifically, assistance is provided to SMEs in their study of, access to, and success in foreign markets. IBDA components include: export training and awareness; market information and intelligence; and planning and research. This agreement is based on a federal-provincial partnership involving the federal departments of ACOA, Industry Canada, and Foreign Affairs and International trade and the provincial governments of New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland and Labrador. Total funding between 1994 and 2004 was $9.2 mln. The agreement is expected to be extended for another five years, with a budget of $10 mln.

4. Seed Capital ConneXion Program for Young Entrepreneurs (SCCPYE)

This program was established to assist young entrepreneurs (under 30 years of age) to access funding and business counselling and training in order to begin, expand/improve a small business and to acquire business skills training.

5. Community Business Development Corporations (CBDCs)

CBDCs are non-governmental and non-profit organizations that collaborate with both public-sector agencies (from all government levels) and private-sector firms to provide advisory and financial services to SMEs. They each maintain a 'revolving investment fund' to facilitate the initial financing of SMEs. Currently, 41 CBDCs exist in Atlantic Canada.

6. Canada Business Service Centres (CBSCs)

These centres supply selected and relevant information government policies, programs, and services available to entrepreneurs and enterprises. ACOA is a 'federal managing partner' of CBSCs in Atlantic Canada. CBSCs are located in each provincial capital and 103 regional sites.

7. Regional Economic Development Organizations (REDOs)

REDOs plan and implement local economic development in partnership with all levels of government (municipal, provincial, and federal) and community organizations. These community-based organizations identify, prioritize, and implement new development initiatives. ACOA collaborates with and finances 52 REDOs consisting of:

(1) 15 Community Economic Development Agencies in New Brunswick;
(2) 11 Regional Development Authorities in mainland Nova Scotia;
(3) 2 Regional Development Authorities on Cape Breton Island (Nova Scotia);
(4) 4 Community Economic Development Corporations in Prince Edward Island; and
(5) 20 Regional Economic Development Boards in Newfoundland and Labrador.

In Newfoundland and Labrador, Regional Economic Development Boards were incorporated on the basis of economic zones. Financial support comes from the Canada/Newfoundland Strategic Regional Diversification Agreement which is federally administered by ACOA and provincially administered by the Department of Development and Rural Renewal.

8. Atlantic Canada Tourism Partnership (ACTP)

Tourism Atlantic was established to coordinate the planning (i.e. research and promotion) and development of new tourism products within Atlantic Canada. Regionally, the Atlantic Canada Tourism Partnership (*ACTP, 2003–2006*) includes ACOA and the provincial tourism departments. Locally, planning and development are conducted under the auspices of BDPs. ACTP funding between 2003 and 2006 was nearly $10 mln.

4. Horizontal Initiatives

Federal programs (horizontal initiatives), aimed at building economically viable and self-sustaining communities, are managed/delivered by ACOA. They assist communities in meeting "specific economic needs" and overcoming "adjustment challenges" via strategic planning, infrastructure enhancement, and employment sustainability (*Wallace 2003, 1*). ACOA acts as the lead agency for the following programs:

1. Infrastructure Canada Program (ICP)

This program (2000–2006) provides funding for physical infrastructure; primarily municipal infrastructure and provincial highways. It is aimed at long-term economic growth and involves both municipal and provincial governments as well as the private sector. For instance, the Canada-Scotia Infrastructure Program. Priority is given to municipal infrastructure projects that improve environmental quality (primarily clean air and water). Other project involve transportation, communication, housing, tourism, and cultural/recreation facilities (*ACOA 2006, 26)*. Total funding between 2001 and 2006 was $183.8 mln.

2. Canada Strategic Infrastructure Fund (CSIF)

Focusing on public-private partnerships, the CSIF directs investments to infrastructure projects that are regionally and/or nationally significant in terms of supporting economic growth and improving living standards. Established in 2001, the fund compliments the ICP but it focuses upon public-private partnerships. Investments are made five key infrastructure categories "vital to advancing Canada's social and economic objectives" (*ACOA 2006, 27*):

(1) highway and railway infrastructure;
(2) local transportation infrastructure;
(3) tourism or urban development infrastructure;
(4) water or sewage infrastructure; and
(5) broadband telecommunications.

Eligible project funding is based upon population thresholds. At least $10 million will be allocated to communities in Prince Edward Island and Newfoundland and Labrador where populations are below 750,000. At least $12 mln will be allocated to communities in Nova Scotia and New Brunswick where populations are between 750,000 and 1.5 mln (*ACOA 2006, 27*).

3. Community Futures Program (CFP)

The CFP (2000–2005) assists local economic development efforts of CBDCs. It also enables communities to attain economic growth, employment stability, structural diversity, and community sustainability. The program also assists SMEs. Total funding between 2000 and 2005 was approximately $160 mln.

4. Adjustment Programs (APs)

Structural adjustment programs "address special economic circumstances" existing in Atlantic Canada (*ACOA 2006, 8*). Several programs are initiated and/or managed by ACOA on behalf of the Federal Government.

4.1. Atlantic Canada Cultural and Economic Partnership (ACCEP)

This three-year program (2002–2005) stimulated regional economic development by funding cultural activities associated with the 400th anniversary of the arrival of the French in North America. It is jointly managed and financed by ACOA and the Department of Canadian Heritage.

4.2. Cod Fishery Action Plan (CFAP)

This program assists individuals and communities affected by the cod fishery closure in the Gulf of St. Lawrence and along the northeast coast of Newfoundland. Established in 2003, the CFAP is designed to "create alternative employment opportunities and expand scientific research into the decline of the cod stocks" (*ACOA 2006, 28*).

4.3. Argentia Management Authority (AMA)

Formed in 1994 as a non-profit organization, the AMA manages a $5 mln federal fund designed "to mitigate the economic impact of the U.S, naval facility closure at Argentia, Newfoundland" (*ACOA 2006, 28*). The AMA has attracted firms and created employment.

Other Federal initiatives administered by ACOA include: Canadian Fisheries Adjustment and Restructuring, Military Base Closure Funds, Borden-Cape Tormentine Redevelopment, Atlantic Groundfish Strategy, Interdepartmental Partnerships with Official Language Communities. Other horizontal initiatives involving ACOA are: Canadian Rural Partnership, Team Canada Incorporated (TCI), Team Canada Atlantic (*TCA, 1999–2007*), Enhanced Representation Initiative (*ERI, 2003–2008*), Canadian Agriculture and Food International (CAFI), and Aboriginal Economic Development (AED)[13]. The Enterprise Cape Breton Corporation, whose profile is given in the proceeding section, delivers ACOA's programs in Cape Breton (Nova Scotia).

5. Focus of Help

ACOA's primary goals are twofold (*Natural Resources Canada 1999, 1*): (1) to ensure that a wide variety of business development tools and resources are available to help more small businesses start-up, survive, prosper, and create good, long-lasting jobs; and (2) to ensure that all economic development programs and activities in Atlantic Canada are coordinated and designed to improve the climate for business growth.

An important and related outcome of ACOA's efforts is the reduction of structural gaps in skills, innovation, and productivity vis-à-vis the rest of Canada[14]. These efforts should facilitate knowledge-based economic growth.

ACOA provides its clients with various practical tools that enable them to build new enterprises and viable communities. Business development tools and resources are available for all stages of the product lifecycle. These tools include advice, financial support as well as reference guides and informative publications. ACOA's programs and services are designed in response to federal government initiatives. The correlation between expected government outcomes and the agency's responses is summarized in *Table III-1*.

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[13] ACOA has implemented the Aboriginal Business Service Network in 41 communities.

[14] Specifically, these gaps include: "technology adaptation; export capacity; access to capital and foreign direct investment; and research and development capacity" (*Wallace 2003, 1*).

Table III-1

Government Outcomes and Agency Responses

Government of Canada's Outcomes	ACOA's Response(s)
An innovative and knowledge-based economy	Innovation
Income security and employment for Canadians	Enterprise Development Community Development
A Secure and fair marketplace	Entrepreneurship and Business Skills Development
A vibrant Canadian culture and heritage	Atlantic Canada Cultural and Economic Partnership Interdepartmental Partnership with Official Languages Communities Memorandum of Understanding with Industry Canada – Investment in Acadian and Francophone Youth
Strong regional economic growth	Enterprise Development Community Development Policy, Advocacy, and Co-ordination
Sustainable cities and communities	Community Development
Aboriginal peoples	Aboriginal Economic Development
Canada's environment protected/restored from pollution	Sustainable Development Strategy

Source: ACOA 2005b.

6. Financial Sources and Distribution

Programs linked to ACOA's core mandate (strategic priorities) are classified in *Table III-2*.

Table III-2

Strategic Priorities and Related Programs

Strategic Priority Area	Related Program(s)
1	2
Policy, Advocacy, and Coordination	Canadian Business Service Centres Infrastructure Canada Program Canada Strategic Infrastructure Fund Community Futures Program Adjustment Activities
Innovation and Technology	Atlantic Innovation Fund Innovation Skills Development Initiative

1	2
Entrepreneurship and Business Skills Development	Entrepreneurship and Business Skills Development Partnership Women in Business Initiative Young Entrepreneurs Development Initiative Seed Capital ConneXion Program for Young Entrepreneurs
Community Economic Development	Strategic Community Investment Fund Community Business Development Corporations Regional Economic Development Organizations
Access to Capital and Information (for SMEs)	Business Development Program
Trade, Tourism, and Investment	Atlantic Trade and Investment Partnership International Business Development Agreement Export Partnering Program E-business and Export Mentoring Program Atlantic Canada Tourism Partnership + Tourism Atlantic

Source: ACOA 2005b.

The distribution (destination) of ACOA's financial assistance is summarized in the *Fig. III-3* (*Wallace 2003*).

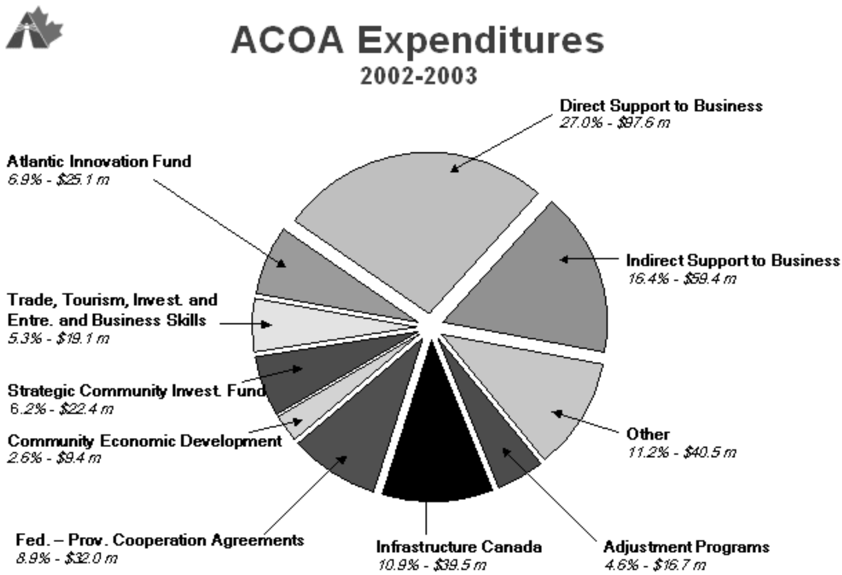

Fig. III-3. ACOA Expenditures, 2002–2003

Total planned spending and expected employment creation by strategic priority is summarized in *Table III-3*. Details, including provincial allocations, are available in sections II and III of the Report on Plans and Priorities, 2005–2006 Estimates.

Table III-3

Planned Spending by Strategic Priority Area
($ mln)

Strategic Priority Area (Program Activity) and Program Sub-Activity	2005–2006	2006–2007	2007–2008
1	2	3	4
ENTERPRISE DEVELOPMENT	*266.9*	*208.0*	*208.6*
* SME Development and Growth	264.1	208.0	208.6
* Innovation	128.2	85.7	87.8
* Entrepreneurship and Business Skills Development	34.6	26.0	26.0
* Trade	27.3	24.6	24.6
* Investment	7.8	6.6	6.6
* Tourism	31.2	29.6	28.1
* Other Support to SMEs	34.9	35.5	35.5
* Access to Information	2.8	-	-
COMMUNITY DEVELOPMENT	*154.3*	*58.4*	*58.1*
* Community Economic Development	75.9	42.7	42.4
* Special Response Measures	26.2	15.7	15.7
* Infrastructure Programming	52.2	-	-
POLICY, ADVOCACY, AND CO-ORDINATION	*16.7*	*16.3*	*16.2*
* Policy Research	11.0	10.7	10.7
* Advocacy	3.9	3,8	3.8
* Co-ordination	1.8	1.8	1.7
TOTAL FINANCIAL COMMITTMENTS	*437.9*	*282.7*	*282.9*

Source: ACOA 2005b.

Planned spending for the five transfer payment programs, each exceeding $5 mln, is summarized in *Table III-4*.

Table III-4

Planned Spending by Transfer Payment Program ($ mln)

Transfer Payment Program (Operating Period)	Total Funding	2004–2005	2005–2006	2006–2007	2007–2008
Business Development Program (1995–2005)	1,500.9	147.1	138.6	124.3	121.8
Community Futures Program (2000–2005)	159.8	9.6	8.8	8.8	8.8
Atlantic Investment Partnership Fund (2001–2006)	547.2	155.6	128.0	52.8	55.8
Saint John Shipyard Adjustment Initiative (2003–2008)	55.0	2.0	22.0	14.0	14.0
Infrastructure Canada Programs (2000–2006)	183.8	38.4	51.2	-	-

Note: The Atlantic Investment Partnership Fund includes AIF, SCIF, ATIP, Tourism, and EBSD funding.
Source: ACOA 2005b.

The funding of major horizontal initiatives is summarized in *Table III-5.*

Table III-5

Planned Spending on Horizontal Initiatives ($ mln)

Horizontal Initiative (Operating Period)	Total Funding	2004–2005	2005–2006	2006–2007	2007–2008
Atlantic Canada Tourism Partnership (2003–2006)	9.9	-	-	-	-
United States Marketing Initiative (2005–2006)	8.3	-	2.8	-	-
Overseas Marketing Initiative (2005–2006)	1.2	-	0.4	-	-
Canada/Atlantic Provinces Agreement on International Business Development (2004–2009)	10.0	-	-	-	-
International Business Development Agreement (1994)	9.2	-	0.1	-	-
Team Canada Atlantic (1999–2007)	6.1	-	1.2	-	-

Note: Between 1994 and 2004, $9.1 mln was spent on the Canada/Atlantic Provinces Agreement on International Business Development and $4.1 mln was spent on the Team Canada Atlantic missions.
Source: ACOA 2005b.

7. Indications of Success and Trends of Emphasis

Measurable results of regional economic development initiatives often take a long time to achieve or materialize. Despite persistent regional disparities, some progress has been made in reducing these disparities “in per capita income during the past forty years” (*Desjardins, Hobson, and Savoie 2002, 46*). Since failures receive more publicity than successes, it is paramount to present tangible examples of success. ACOA has “contributed to the development of transport networks, utilities, energy supplies, research agencies, and the infrastructure needed for economic expansion and social adjustment” (*Wynn 1998, 190*). Evidence of significant progress, in terms of performance results and impact measurement, includes the following examples (*Wallace 2003, 1; ACOA 2006, 6*):

(1) The five-year survival rate of ACOA-assisted business start-ups is 2.5 times better than that of all new businesses in the Atlantic region;
(2) ACOA program spending generates, on average, $1.25 in tax revenues for every dollar invested in business start-ups and expansions;
(3) Growth in employment in high-knowledge sectors in the past decade [1993–2003] was 5 times that of low-knowledge sectors;
(4) Since the 1980s, productivity gains in manufacturing have exceeded those for Canada;
(5) Regional/national gaps in employment and participation rates have narrowed; and
(6) A vibrant entrepreneurial business community has emerged.

Between 1998 and 2003, ACOA’s initiatives, programs, and services resulted in increases in terms of employment growth, incomes, productivity, export trade and foreign direct investment, research and development, and tourist spending. The quantity, quality, and survival of entrepreneurs (SMEs) also increased during the 1998–2003 interval[15].

[15] For specific examples of successful activities in Nova Scotia, consult ACOA’s Partnering for Success newsletter. For examples of the successful application of new technologies by innovative firms, see Innovative Skills Challenges – Profiles from Atlantic Canada. For examples of successful export development activities among SMEs, see The Canada/Atlantic Provinces Cooperation Agreement on International Business Development – Report on Activities and Results 2000.

During 2004, economic and employment growth along with foreign trade all remained positive. Since 2005, ACOA has pursued an integrated approach to accelerate economic activity involving economic development along with the social economy and social enterprise. The federal government has allocated $708 mln towards the economic development of Atlantic Canada. This amount will be spent between 2005 and 2010. The AIF ($300 mln) has been renewed. A new Innovative Communities Program (ICP), worth $290 mln, will be implemented to “diversify the economies of vulnerable communities and strengthen human capital, trade, investment and tourism in Atlantic Canada” (*ACOA 2005b*). Planned spending, according to strategic priority, is summarized in *Table III-3*. *Table III-6* relates the corresponding employment to be created from future spending.

Table III-6

Planned Employment (Full-time Equivalents) by Strategic Priority Area

Strategic Priority Area (Program Activity) and Program Sub-Activity	**2005–2006**	**2006–2007**	**2007–2008**
ENTERPRISE DEVELOPMENT	*456*	*411*	*411*
* SME Development and Growth	435	411	411
* Innovation	205	181	182
* Entrepreneurship and Business Skills Development	63	54	54
* Trade	44	48	48
* Investment	13	13	13
* Tourism	54	57	56
* Other Support to SMEs	58	58	58
* Access to Information	21	-	-
COMMUNITY DEVELOPMENT	*147*	*105*	*101*
* Community Economic Development	139	104	100
* Special Response Measures	1	1	1
* Infrastructure Programming	7	-	-
POLICY, ADVOCACY, AND CO-ORDINATION	*75*	*68*	*68*
* Policy Research	37	30	30
* Advocacy	26	26	26
* Co-ordination	12	12	12
TOTAL EMPLOYMENT CREATION	678	584	580

Source: ACOA 2005b.

"In the area of enterprise development, [ACOA] will continue to foster the growth and competitiveness of SMEs by supporting efforts to build the region's innovation capacity, entrepreneurship and business skills capabilities, and trade and investment opportunities" (*ACOA 2005b)*. "ACOA will also work to bolster the economic health of the region's communities by promoting better cooperation and coordination among partners, strengthening local strategic planning processes, increasing the availability of investment capital, and creating more and better sustainable jobs, particularly in rural areas" *(ACOA 2005b*). A criticism of ACOA is that it is not always capable of identifying and nurturing business opportunities that are ignored by entrepreneurs and investors (*McIver 2004*). In terms of capitalizing business opportunities, there is "little indication of greater risk-taking or a significant commitment to financing unproven but potentially rewarding industries" (*Wynn 1998, 191*). Another criticism is that ACOA uses successful businesses to subsidize those that are unsuccessful (*McIver 2004*).

Table III-7

Comparison of Well Being between Rural and Urban Atlantic Canada (Based on 2001 Census Division Averages)

	v3	v4	v5	v6	v7	v8	v9	v10	v10a
Rural (N=42)	836,076	–4.09	0.14	39.51	84.61	13.18	89.81	1.68	8.52
Urban (N=4)	1,449,653	–0.63	1	38.33	85.58	11.44	88.5	2.19	11.37

	v11	v12	v12a	v13	v14	v15	v16	v17	v18
Rural (N=42)	72.2	4.87	22.93	0.49	1.15	22.56	13.56	11.28	12.28
Urban (N=4)	64.45	6.29	29.3	0.9	2.36	29.98	23.23	19.08	18.55

	v19	v20	v21	v22	v23	v24	v25	v26	v27
Rural (N=42)	41.78	22,769.81	34,348.31	97.89	80.55	79.71	59.63	49.44	17.57
Urban (N=4)	49.88	26,380.75	37,507.75	97.85	85.9	75.73	61.4	53.85	13.05

	v28	v29	v30	v31	v32	v33	v34	v35	v36
Rural (N=42)	21.01	2.83	17.02	11.58	7.62	12.88	3.79	6.43	16,730.36
Urban (N=4)	13.55	4.87	20.04	17.83	9.26	18.21	5.44	8.04	19,224.75

	v37	v38	v39	v40	v41	v42	v43	v44	v45
Rural (N=42)	67.7	21.8	10.47	45,840.14	21.28	79.13	78,924.88	49.3	8.04
Urban (N=4)	70.79	17.43	11.4	52,833.25	23.46	69.5	97,839.50	38.83	6.93

Note: Variables are defined in *Table II-4*.
Source: Statistics Canada, 2001 Community Profiles
Available: http://www12.statcan.ca/english/profil01/CP01/Index.cfm?Lang=E

A comparison of urban and rural areas in Atlantic Canada, summarized in *Table III-7*, indicates that urban areas had nearly twice as many residents (v3), higher measures for income (v20, v36, and v40), education (v16 to v18), residential mobility (v9 to v12), people working at the same place (v23), and value of owned dwellings (v43). Although differences in labour force measures (v25 to v27) are marginal, service sector employment is more pronounced in urban areas (v29 to v35). Rural areas are more dependent upon income from government transfers (v19 and v38). Part of both the national and regional periphery, rural areas has a less dynamic demographic base.

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IV. Enterprise Cape Breton Corporation, a Surrogate SEZ Support Entity

1. Introduction

Enterprise Cape Breton Corporation (ECBC) was established in 1988 as a Crown corporation pursuant to Part II of the *Government Organization Act, Atlantic Canada* (1987). Considered to be the successor of the former Industrial Development Division of the Cape Breton Development Corporation (*DEVCO, 1967–2001*), its mandate is "to promote and assist the financing and development of industry" on Cape Breton Island and in the Mulgrave area of mainland of Nova Scotia (Natural Resources Canada 2002). ECBC is also committed to diversifying the regional (Cape Breton Island) and local (Mulgrave area) economic bases, which previously relied upon the coal and steel industries, increasing business development, and creating employment via the development of infrastructure and growth of small- and medium-sized enterprises (SMEs)[16].

ECBC's mission statement reads as follows: "ECBC is the principal federal government organization for economic development in Cape Breton. ECBC, in partnership with all levels of government, the private sector and other community stakeholders [e.g. educational institutions and economic development groups], will use its broad and flexible powers to assist, promote and co-ordinate efforts that foster an environment supportive of the generation of wealth to effect sustainable job creation throughout Cape Breton and Mulgrave" (*ECBC 2005b, 3*). This goal is consistent with that of the Atlantic Canada Opportunities Agency (ACOA).

ECBC's "geographic focus, local control and flexible mandate" constitute the characteristics of a special economic zone (SEZ) for regional development.

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[16] Cape Breton has traditionally relied upon the resource extraction sector, especially coal mining, steel making, and ground fishing, which has undergone economic restructuring and transition.

2. Governance

ECBC is part of the federal government's Industry Canada portfolio. It is controlled and managed by a Board of Directors whose president is also the president of ACOA. The head office is located in Sydney and a satellite office operates in Port Hawkesbury. ECBC works closely with two federal entities which provide economic development planning – ACOA and the Cape Breton Growth Fund Corporation (CBGFC). It also collaborates with the two Regional Development Authorities on Cape Breton Island.

ECBC maintains four operations: the Point Edward Resource Centre, the Port Hawkesbury Business Facility, the Silicon Island Art and Innovation Centre, and the MacDonald House. It also maintains four subsidiary companies:

(1) Cape Breton Growth Fund Corporation (CBGFC);
(2) DAAR (Cape Breton) Limited – a real estate holding and development company;
(3) Cape Breton Marine Farming Limited (inactive); and
(4) Gulf Bras d'Or Estates Limited (inactive).

3. Structure of Regional Programs

ECBC administers its own economic development programs based on six strategic priority areas which are concurrently related its mandate and mission statement and similar to ACOA's strategic priorities (*ECBC 2004, 5*):

(1) delivery/service agent for government services (i.e. provision of services to/for the federal government);
(2) support to business (goal is to "encourage private-sector investment in projects that enhance the competitiveness of commercial enterprises and increase trade opportunities to produce long-term, sustainable jobs"; programs include capital access, human resources initiative, e-commerce initiative);
(3) support to communities (goal is to assist communities to "plan and implement community development projects that have a direct link tom long-term, self-sustaining economic policy"; programs include community capacity building, festival and events initiative, convention and sporting events initiative, Cape Breton Business Partnership);

(4) investment (goal is to new business investment; plans include promotional activities and business class immigrants);
(5) advocacy (goal is to advocate local "interests, priorities and concerns in government decisions"); and
(6) policy and research (goal is to provide "a sound basis for ECBC's policies, priorities and programs").

Economic development assistance activities are focused upon the following priority sectors:
(1) tourism;
(2) knowledge-based industry;
(3) manufacturing and processing; and
(4) natural resources.

Programs administered by ECBC "provide direct assistance to businesses and entities that provide support to business" (*ECBC 2001c*). Investment assistance is targeted to capital projects and business improvement[17]. They are based upon three fundamental criteria: viability/sustainability, need/incrementally, and accessed net economic impact on the region (*ECBC 2001c*).

1. Cape Breton Growth Fund Corporation (CBGFC)

The CBGFC is a wholly owned subsidiary of ECBC and has the same mandate as ECBC. Programming assistance, aimed at consolidating and broadening the economic base of Cape Breton Island, is offered to commercial and non-commercial projects "in the form of a loan, repayable contribution, or equity investment" (*Natural Resources Canada 2002*). Established in 2001 after the closure of DEVCO, the CBGF provides financing from the federal and provincial governments (i.e. delivery of economic adjustment funding). It is targeted to SME development, technology development, and venture capital. Nearly $133 mln was spent since 1988. CBGFC has received $91 mln in funding (*ECBC 2004, 4*). Once these economic adjustment funds are committed, CBGFC will be integrated into the ECBC. It is expected that the CBGFC will conclude its operations in 2006.

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[17] Projects supported by ECBC: fixed roof accommodations; tourism attractions; oil and gas; boat building; new technology and knowledge-based industries; aquaculture; food processing; other manufacturing and processing; human resources; innovation assistance; marketing activity assistance; studies assistance; investment prospecting and trade missions; and infrastructure assistance. Details about these project initiatives are available online (http://www.ecbc.ca/e/guidelinesdetail.asp).

2. Community Adjustment Fund (CAF)

The CAF was established "to provide support through quality infrastructure that will facilitate the long-term sustained growth of affected communities" (*ECBC 2005a, 61*).

ECBC administers and delivers programs on behalf of ACOA (since 1995) and CBGFC. The following programs and services are delivered on behalf of ACOA:

(1) Business Development Program (BDP);
(2) Consultant Advisory Services (CAS);
(3) Infrastructure Canada Program (ICP);
(4) Community Futures Program (CFP); and
(5) Atlantic Investment Partnership (AIP).

About $249 million in programming assistance has been provided between 1987 and 2003. Anticipated funding for the 2004–2008 period is $39 mln.

4. Focus of Help

Programs and services are direct towards creating employment, identifying opportunities, investing in strategic infrastructure, and providing advice/counselling to businesses. The target ration of project assistance has significantly shifted from commercial projects towards non-commercial projects. The current ratio is 40% commercial and 60% non-commercial[18].

5. Financial Sources and Distribution

As of 31 March 2004, the ECBC has funded 9 commercial projects ($1.8 mln), 17 non-commercial projects ($1.2 mln), and 47 festivals/events ($200 thousand) (*ECBC 2004, 7*).

6. Indications of Success and Trends of Emphasis

ECBC monitors and reports 'performance targets' for all of its strategic priorities, excluding the service provider role (i.e. delivery/service agent for government services). *Table IV-1* summarizes performance measures by strategic priority.

[18] Previous ratios for non-commercial projects were 30% for 2002–2003 and 50% for 2003–2004.

Table IV-1

Performance Measures by Strategic Priority ($ mln)

Strategic Priority	2001	2002	2003	2004	2005	Total
(1) Support to Business						
• Jobs Created	413	68	124	404	65	1,074
• Leveraged Funds	43.1	2.9	5.7	3.3	14.9	$69.9
• New Export Sales	55.7	2.9	81.1	0.5	20.4	$160.6
(2) Support to Communities						
• Leveraged Investment	0.9	5.0	6.9	1.7	4.1	$18.6
(3) Investment						
• New Investment on Cape Breton Island	42.2	-	3.5	16.0	14.1	$75.8
(4) Policy and Research						
• Completed Research Projects	8	8	9	7	3	35
(5) Advocacy						
• Operational Cost-Efficiencies (2 Year Target)	-	-	-	0.15	0.10	$0.25

Source: ECBC 2005a, i.

Overall, "efforts to develop and diversify Cape Breton have yielded results. Pockets of development have emerged, which build a foundation for further development and growth" (*ECBC 2005b, 8*). Employment has increased since 1993 while employment income (per earner) has increased steadily since 1996. "Higher paying, specialized jobs" are emerging in the automotive and pharmaceutical sectors. *Tables IV-2* and *IV-3* summarize the impact of ECBC projects upon employment generation and labour income.

Table IV-2

Total Employment Created from ECBC Sponsored Projects

Fiscal Year	Number of Jobs
1999/2000	3,083
2000/2001	2,567
2001/2002	4,073
2002/2003	5,496
2003/2004	9,384

Source: ECBC 2005b, 10.

Table IV-3

Total Labour Income Created from ECBC Sponsored Projects

Fiscal Year	Labour Income ($)
1999/2000	94,812,000
2000/2001	74,615,000
2001/2002	100,294,000
2002/2003	146,826,000
2003/2004	250,601,000

Source: ECBC 2005b, 10.

The following economic impacts, based on $182 mln of assistance, were achieved between the 1999/2000 and 2003/2004 fiscal periods (*Foster 2004*):

(1) 9,384 jobs generated by ECBC development programs;
(2) $667 mln of labour income ($133 mln per year);
(3) increased federal ($91 mln), provincial ($84 mln) and municipal ($11 mln) revenues; and
(4) every dollar committed by ECBC generated an extra $5 of household income.

During the 2000–2001 period, the CBGFC assisted 165 projects ($15 mln) which created 674 jobs (*Natural Resources Canada 2002*).

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V. Quebec's Surrogate SEZ Regional Development Zones, CED-QR

1. Introduction

Economic development at the subprovincial or regional level in Canada has been a feature of federal and provincial policy for some time. The review of DREE in 1972 and the subsequent decentralizing of Canadian regional development efforts led to the creation of regional development agencies in the Atlantic Provinces, Quebec, and the western provinces. The programs of these regional agencies have objectives and programs that are national in scope as well as more particular programs suited to the conditions in each region. This section examines the regions and regional development programs of the Quebec agency in terms of their characteristics and functions as surrogate special economic zones.

Furthermore, these federal programs are typically designed to work closely with municipalities as well as with extensive networks of associations and not-for-profit organizations that are working on issues of local development. This section focuses primarily on federal programs although it must be recognized that these other programs can be an important component of these surrogate special economic zones. For example, there is an extensive network of associations and non-governmental organizations working on issues of local development. Included among these groups is the Association des Centres Locaux de Développement du Québec (ACLDQ). The CED-QR agency is also working closely with the Chantier de l'économie Sociale to set up a capital fund for Quebec's social economy enterprises. The aim of the fund is to improve access to long-term financing for such enterprises. The province has also experimented in the past with the creation of special economic zones. For example, over a decade ago, the Government of Quebec, under the Ministry of Finance (2000) created a Montréal Foreign Trade Zone at Mirabel airport. The zone had limited success, if at all, and its enabling legislation was repealed.

The purpose of this section of the paper is to provide a summary description of the Government of Canada's regional development agency and efforts in the Province of Quebec. The topic is developed under six headings:

(1) To identify the mandate of the agency and consider its characteristics as a surrogate Canadian special economic zone;
(2) To present an overview of the governance of the agency;
(3) To describe its structure and regional programs;
(4) To focus on the nature of help that is provided to the region, its business and individuals to help them develop;
(5) To examine the financial structure of the inflow of funds as well as their dispersion; and
(6) To look for indications of successful endeavours and trends in the region.

2. Mandate

The Federal Office of Regional Development-Quebec (FORD-Q) was created in 1991. This agency was given a five-year budget of $1.3 bn to: define federal objectives pertaining to regional development in Quebec; negotiate and administer economic development agreements with the provincial government; and administer support programs for appropriate initiatives in each region of Quebec. In 1998, FORD-Q became Canada Economic Development for Quebec Regions (CED-QR). Then, in 2005, the Agency, which previously had come under the authority of Industry Canada, became a fully autonomous entity known as the Economic Development Agency of Canada for the Regions of Quebec.

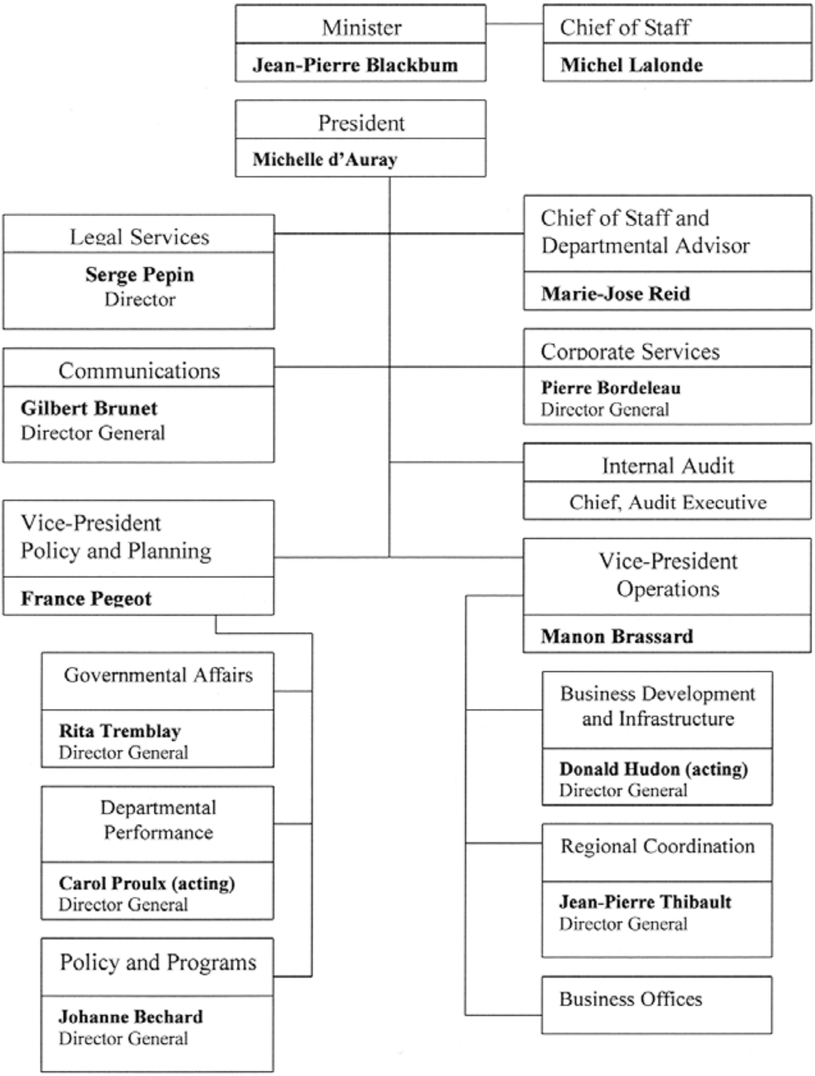
The Agency's mandate since its inception has been to respond to the specific economic characteristics and needs of the regions of Quebec. It gives special attention to regions experiencing slow economic growth and inadequate employment, with a view to the enhancement of prosperity and employment in the long term. The Agency supports development of the economic potential of the regions of Quebec and the creation of sustainable employment by fostering a business climate that enables small and medium-sized businesses to prosper and grow. In this sense policies in these regions resemble those of special economic zones elsewhere in the world that and so these regions can be treated as surrogates for special economic zones.

3. Governance

Canada Economic Development is an agency of the Canadian federal government with a specific focus economic development in Quebec. Formerly under the *Department of Industry Act,* recent legislation now gives the agency the same mandate and legal status as ACOA and WD (which have had their own legislation since 1988). It now has the status of a federal agency with its own budgets and requires the Minister to account to Parliament for the Agency's activities and results on an annual basis and to provide a five-year assessment of its activities and programs as a whole. The Honorable Jean-Pierre Blackburn is the current Minister of the Economic Development Agency of Canada for the Regions of Quebec and the Minister of Labour.

The Agency works collaboratively with a broad array of local and regional economic development organizations, other federal departments and agencies, and the Quebec government. Canada Economic Development has its head office in Montreal and a network of fourteen business offices across various regions of Quebec. The business offices are nerve centres for the delivery of the programs and services and have an active role in establishing the Agency's priorities and approaches and in adjusting programs and services to the local situation.

Responsibility for the management of the agency on a day-to-day basis is assumed by the President and an executive staff. The executive, as shown on *Fig. V-1*, is responsible for program development and the delivery, as well as for negotiating and managing partnership agreements with other federal departments and outside organizations, such as financial institutions.



Source: CED-QR 2006c.

Fig. V-1. CED-QR's Organizational Structure

4. Regions of Quebec

The geographic regions of Quebec form the basis for the priorities and implementation of development programs. This clear focus on subprovincial regions is a notable difference between the federal government's economic development program in Quebec and the programs operating in the Atlantic region (ACOA) and in western Canada (WD).

Quebec's regions are distinct with different development challenges and problems. Thus, each region has its own regional priorities and initiatives, related in part to the economic base and predominant resource sector of the region.

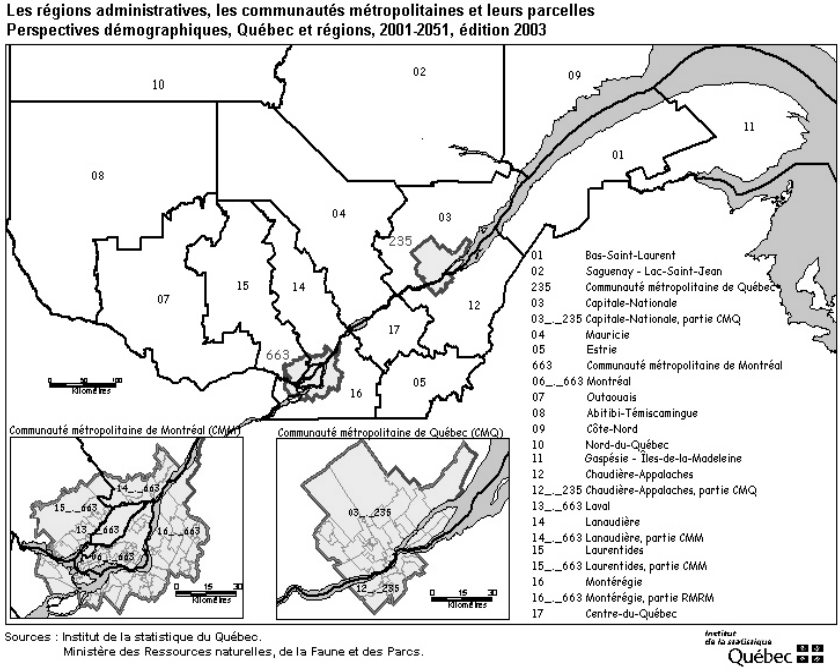
The Government of Quebec recognises seventeen regions as shown on *Table V-1* and *Fig. V-2*.

Table V-1

Administrative Regions of Quebec

Bas-Saint-Laurent	(01)	Nord-du-Québec	(10)
Saguenay–Lac-Saint-Jean	(02)	Gaspésie–Îles-de-la-Madeleine	(11)
Capitale-Nationale	(03)	Chaudière-Appalaches	(12)
Mauricie	(04)	Laval	(13)
Estrie	(05)	Lanaudière	(14)
Montréal	(06)	Laurentides	(15)
Outaouais	(07)	Montérégie	(16)
Abitibi-Témiscamingue	(08)	Centre-du-Québec	(17)
Côte-Nord	(09)		

On its website, the Economic Development Agency of Canada uses the same administrative regions as the Province of Quebec with two exceptions. It excludes the capital (Quebec City) and groups together Laval, Lanaudiиre, and the Laurentides into a single region, thus defining 14 regions, as shown on *Table V-2*. Each of these regions can be considered as a surrogate special economic zone.



Source: Institut de la Statistique du Québec 2005.

Fig. V-2. Administrative Regions of Quebec

Table V-2

Program Regions of Quebec, CED-QR

Bas-Saint-Laurent	(01)	Nord-du-Québec	(10)
Saguenay–Lac-Saint-Jean	(02)	Gaspésie–Îles-de-la-Madeleine	11)
Mauricie	(04)	Chaudière-Appalaches	(12)
Estrie	(05)	Laval (13), Lanaudière (14), Laurentides	(15)
Montréal	(06)	Montérégie	(16)
Outaouais	(07)	Centre-du-Québec	(17)
Abitibi-Témiscamingue	(08)		
Côte-Nord	(09)		

These regions are further categorized by the Economic Development Agency of Canada, on the basis of their urban and economic characteristics, into five groups (*Source*: Report on Plans and Priorities 2005–2006):

(1) metropolitan Montreal;

(2) major urban centres: Gatineau (part of the Ottawa-Hull region) and Québec City;

(3) central areas and university cities: the Estrie, Centre-du-Québec, Chaudière-Appalaches, Laurentides, Lanaudière and Mauricie regions – and the cities of Rimouski, Rouyn-Noranda, Saguenay, Trois-Rivières and Sherbrooke;

(4) outlying areas: Abitibi-Témiscamingue, Bas-Saint-Laurent, Côte-Nord, Gaspésie–Îles-de-la-Madeleine, Nord-du-Québec and Saguenay–Lac-Saint-Jean; and

(5) vulnerable communities: characterized by an aging industrial structure, these communities are undergoing adjustment difficulties; they may also be urban districts struggling with problems of social cohesion.

These categories reflect basic core-periphery distinctions of economic structure within an urban systems framework. Within this framework, Montreal is the core, a highly diversified gateway city, while in the periphery is comprised of resource communities, single industry towns, and aging urban-industrial districts. The programs of the Agency, to be described in the next section of this paper, are customized to respond to the particular needs of the different types of regions.

Table V-3 provides a summary table showing the seventeen regions of Quebec, their population size and growth rates, the size of their economies, and the CED-QR programs that apply to particular regions.

Table V-3

Quebec Administrative Regions and Selected Characteristics

Quebec Regions	Region Type*	Population	Population Change, %		Gross Provincial Product $M***	CED-QR Programs		
						FCEDI	CEDI-CR	CEDI-Vitality
1	2	3	4	5	6	7	8	9
Name		**2004**	**2001–2005**	**1996–2001**	**2004**			
Québec		7,651,500	2.7	1.4	246,213			
Montréal (06)	(1)	1,876,932	1.2	1.2	88,664			

1	2	3	4	5	6	7	8	9
Capitale-Nationale (03)	n.a.	638,917	2.6	0.9	22,996			
Outaouais (07)	(2)	338,491	5.9	4.9	8,455		X	
Montérégie (16)	(3)	1,352,349	4.6	1.6	36,558			
Estrie (05)	(3)	291,917	3.1	2.5	8,773			
Chaudière-Appalaches (12)	(3)	383,376	1.3	0.8	11,378		X	
Laval (13)	(3)	365,000	5.9		9,387			
Lanaudière (14)	(3)	413,600	7.1		8,118		X	
Laurentides (15)	(3)	500,000	7.9		12,769		X	
Centre-du-Québec (17)	(3)	224,991	1.8	2.3	6,827			
Mauricie (04)	(3)	259,424	0.0	-0.7	6,843		X	X
Bas-Saint-Laurent (01)	(4)	202,095	–1.3	–2.6	5,125		X	X
Saguenay–Lac-Saint-Jean (02)	(4)	278,519	–2.9	–3.0	8,519		X	X
Abitibi-Témiscamingue (08)	(4)	145,321	–2.6	-3.7	4,089		X	X
Côte-Nord (09)	(4)	98,861	–3.3	–4.3	4,165	X	X	X
Nord-du-Québec (10)	(4)	39,892	2.2	0.6	1,578		X	X
Gaspésie–Îles-de-la-Madeleine (11)	(4)	96,929**	–2.4	–7.8	1,969	X	X	X

Notes: n.a. – not applicable; not a designated region of CED-QR.
* The region types listed in parentheses correspond to those listed on the previous page.
** Based on the 2001 population.
*** Gross domestic product at base prince ($ mln, current value).
Sources: Institut de la Statistique du Québec 2006; CED-QR 2006a.

5. Structure of Regional Programs

Since the Agency's inception a number of different programs have been initiated and over time modified. With the most recent change in the federal government the new government has modified some programs and reprioritised some areas of focus. Below is a list of all programs, past and present, which are associated with the Agency.

Programs relative to the Agency's core mandate include:
(1) Innovation, development entrepreneurship and access program SMEs (IDEA-SME);
(2) Regional Strategic Initiatives (RSI) Program;
(3) Community Futures Program (CFP);

(4) Community Economic Diversification Initiative – Vitality (CEDI-VITALITY); and
(5) Dedicated programming: Canadian Support Program for the Gaspésie and the Iles-de-la-Madeleine Economy.

Program relative to the special mandate from the Government of Canada include:
(1) Infrastructure Canada Program (2000);
(2) Canada Infrastructure Works (1994); and
(3) Canadian Apparel and Textile Industries Program (CATIP).

Other programs associated with which the Agency include:
(1) *Canada Small Business Financing Act* (CSBFA);
(2) Softwood Industry and Community Economic Adjustment Initiative contribution program (SICEA); and
(3) Program for Export Market Development (PEMD).

Other government-wide management initiatives include:
(1) Modern Comptrollership;
(2) Human resources management;
(3) Government on-line;
(4) Sustainable Development Strategy; and
(5) Application of section 41 of Part VII of the *Official Languages Act*.

The following headings describe programs relative to the Agency's core mandate.

1. Innovation, Development, Entrepreneurship and Access Program for SMEs (IDEA-SME)

The IDEA-SME program promotes the development of small and medium-sized enterprises, and helps them to become more competitive on world markets. As the name of the program suggests its primary target clientele are small and medium-sized enterprises (SMEs). But notably, this category is very broad and in addition to traditional commercial enterprises, it includes SME support organizations, business associations, and economic development organizations. It also includes an important category known as social economy enterprises.

The program supports a number of activities including innovation, testing and experimentation to enhance natural resources, productivity, e-business, market development and export, social economy capacity building, entrepreneurship and business climate development.

2. Regional Strategic Initiative (RSI)

Each of the regions has developed a regional strategy to promote in a coordinated fashion the implementation of projects and initiatives that support the economic strengths of a region. The strategies are designed according to the specific needs of the regions and on the basis of the following priorities:

(1) increased use of technology by SMEs;
(2) development of tourist attractions;
(3) drawing power and international reach; and
(4) adjustment to the new global economic environment.

Brief documents are available on the Agency website for each region. In addition to a regional profile, there are reports summarizing the region's intervention strategies, and identifying its priority areas for future development.

3. Community Futures Program (CFP)

The Community Futures Program (CFP) supports local economic development and strengthens the ability of communities to realize the following main objectives:

(1) stability, economic growth and job creation;
(2) diversified, competitive local economies in rural areas; and
(3) sustainable communities.

The CFP in Quebec supports 57 Community Futures Development Corporations, located in designated rural regions, 9 Business Development Centres, located in the suburban areas, and 15 Community Economic Development Corporations, located in disadvantaged urban areas. These community businesses belong to a network which provides access to the Quebec CFDC Common Fund, an investment fund.

4. Community Economic Diversification Initiatives (CEDI)

This program aims to foster and support projects that address economic sectoral issues affecting communities in economic crisis. Two initiatives have been developed to respond to the specific needs of the targeted communities.

The first of these is the Fishing Community Economic Diversification Initiative (FCEDI). This program aims to foster and support projects related to economic issues shared by fishing communities, and targets the following regions: Côte-Nord (Basse-Côte-Nord and the Minganie), Gaspésie (the coastal communities between Saint-Godefroi and Cap-Chat) and Iles-de-la-Madeleine.

The second sectoral program is the Community Economic Diversification Initiative, which emerged from the recommendations of the Coulombe Report (CEDI-CR). This program aims to foster and support projects which address economic issues affecting communities hardest hit by the reduction in coniferous supply resulting from the implementation by the Government of Quebec of the Coulombe Report's recommendations. The CEDI-CR targets the following four regions: Abitibi-Témiscamingue, Bas-Saint-Laurent, Côte-Nord, Gaspésie – Iles-de-la-Madeleine, Mauricie, Nord-du-Québec, and Saguenay – Lac-Saint-Jean. It also applies to 21 single-industry municipalities outside these regions.

The purpose of this initiative is to enable these communities to strengthen their social structure and open up to new economic sectors with high value-added and attractive high-growth potential. As with the other regional programs of the Agency, the CEDI-CR provides a comprehensive approach to creating social, cultural and economic conditions conducive to entrepreneurship.

5. Community Economic Diversification Initiative – Vitality (CEDI – Vitality)

The new Conservative government in Ottawa introduced some modifications to the CEDI program in September 2006 and announced the Community Economic Diversification Initiative – Vitality (CEDI – Vitality). This four-year $85 mln program will be offered to entrepreneurs and not-for-profit organizations in seven regions: Abitibi-Témiscamingue, Bas-Saint-Laurent, Côte-Nord, Gaspésie – Iles-de-la-Madeleine, Mauricie, Nord-du-Québec, and Saguenay – Lac-Saint-Jean. It will also be available in 21 additional regional county municipalities (RCMs). *Table V-3* indicates the regions eligible for the funding.

The program focuses assistance on the worst-off regions, those experiencing a slowdown or elimination of certain traditional economic activities in the manufacturing and natural resources sectors; regions dependent on a single activity; and others facing significant demographic decline through population exodus. The regions supported by this program include 21% of the Quebec population.

6. Other Initiatives Eligible Under Regular Programming

Within the various programs offered by the Agency, other cultural festivals and sporting events are recognized as important within the economic, tourism, cultural and social sectors of Quebec. To this end support is available for the marketing and renewal of festivals and sporting events in Quebec and to increase attendance.

6. Horizontal Initiatives

CED-QR also delivers programs relative to the special mandate from the Government of Canada.

1. Infrastructure Programs

Canada Economic Development administers one of the federal government's joint infrastructure programs. In Quebec, these include the Canada-Quebec Infrastructure Works Program and the Municipal Rural Infrastructure Fund. The priorities of these programs are to improve the quality of life in cities and towns.

2. CANtex Canadian Textiles Program

The CANtex Canadian Textiles Program is a program being implemented by Canada Economic Development in Quebec, and by Industry Canada in the rest of the provinces. Through various repayable and non-repayable financial contributions the program intends to increase the competitiveness of textile manufacturing companies. The projects funded are intended to: enhance their productivity; reduce their costs; improve their efficiency; and diversify their production into higher value-added textile products for growing niche markets.

3. Other Programs Associated with the Agency

As a federal agency, Canada Economic Development also contributes to broader government-wide management initiatives. These include initiatives to modernize comptrollership and human resources management and to promote the government's on-line presence. Also notable is the overall strategy of sustainable development, as laid out in the "Sustainable Development Strategy, Action Plan 2000–2003" and updated in the document "For a Cost-effective Sustainable Development, Sustainable Development Strategy 2003–2006."

7. Focus of Help

The Agency is trying to achieve two overarching outcomes which are strategically aimed at improving competitiveness in the global economy and in sustaining regional vitality. With the various programs offered by the Agency program priorities are established that aim to reach these outcomes. Each of these strategic outcomes is outlined below, followed by a discussion of program priorities.

The first strategic outcome is to increase enterprise competitiveness. The Agency works primarily with SMEs and non-profit organizations that provide services to enterprises to help them in the adoption of:

(1) advanced business practices (e.g. e-business, strategic planning systems);
(2) innovation in processes, equipment and products; and
(3) commercialization of new products and development of new export markets.

The second strategic outcome is to increase the vitality of communities. The Agency therefore works closely with local and regional economic agents, entrepreneurs and community stakeholders to promote the vitality of communities. In so doing, the Agency fosters, among other things:

(1) enhanced local capability to take charge of local development;
(2) startup and expansion of small enterprises of local scope (entrepreneurship), including social economy enterprises; and
(3) improvement of collective infrastructure, namely, transportation infrastructure; drinking water (filtration plants and distribution networks) and wastewater (water supply and sewers) infrastructure; and infrastructure with an economic and cultural role.

These strategic outcomes are consistent with the Government of Canada's national interest in increasing global competitiveness and maintaining regional vitality. Within the Agency's programs for the regions of Quebec the priorities are to: i) promote innovation and the knowledge economy; and ii) assist regions experiencing difficulties adjusting to the new global economy.

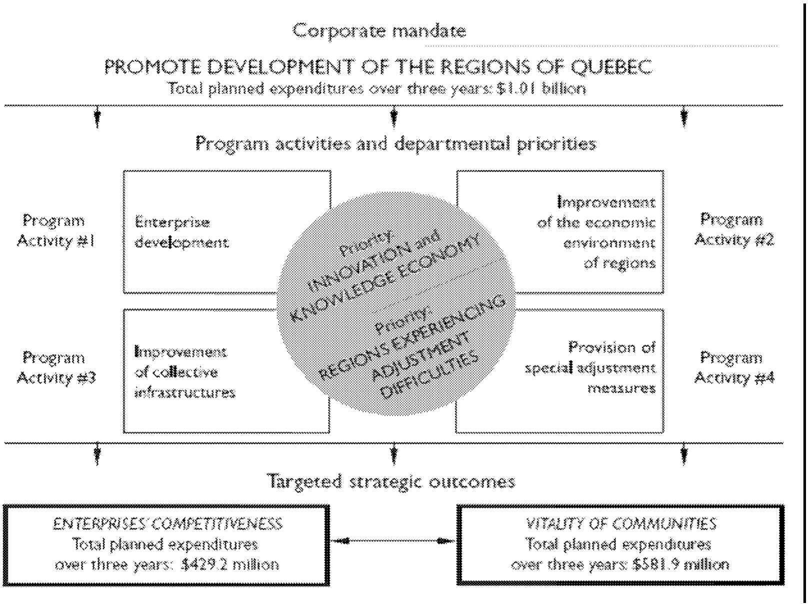
To help realise its first priority (promote innovation and the knowledge economy), the Agency will intervene to:

(1) "foster the development, perfection, testing and experimentation of new or improved products or processes;
(2) improve productivity;
(3) foster commercialization of innovation;
(4) elicit the startup and expansion of enterprises in innovative or new economy-related niches; and

(5) foster the dissemination and sharing of the products of research".

With respect to its second priority (assist regions experiencing adjustment difficulties) the Agency intends to:

(1) "reinforce local capability to take charge of local development;
(2) foster the development of small enterprises of local and regional scope, including social economy enterprises; and
(3) foster the establishment of strategic enterprises, that is, enterprises operating in areas of activity that are promising for a region, for instance in its efforts to diversify".



Source: CED-QR 2006d.

Fig. V-3. Corporate Mandate and Funding Priorities CED-QR

8. Financial Sources and Distributions

The financial sources for the Agency's programs are, in general, directly from the revenues of the Government of Canada. As previously indicated, the bulk of funds are distributed primarily through the core programs of the Agency, and secondarily through other federal programs with which the Agency is associated. These various programs are summarized below.

Programs relative to the Agency's core mandate:

(1) Program of assistance for development of SMEs in Quebec (IDEA-SME);
(2) Regional Strategic Initiatives (RSI) Program;
(3) Community Futures Program (CFP); and
(4) Canadian Support Program for the Gaspésie and the Iles-de-la-Madeleine Economy.

Program relative to the special mandate from the Government of Canada:

(1) Infrastructure Canada Program.

Other programs with which the Agency is associated:

(1) *Canada Small Business Financing Act* (CSBFA);
(2) Softwood Industry and Community Economic Adjustment Initiative contribution program (SICEA);
(3) Canadian Apparel and Textile Industries Program (CATIP); and
(4) Program for Export Market Development (PEMD).

In general, the Agency budgets for a total planned expenditure over three years of $1.01 bn. These funds are distributed to the two strategic outcomes as follows: enterprise competitiveness – $429.2 mln; and vitality of communities – $581.9 mln.

This total is further distributed across all the various programs of the Agency. Almost half of all the funds distributed by the Agency are dedicated to the support its core program activities and priorities. Thus, over the three year period, $317.7 mln are directed to the Innovation and knowledge priority and $156.4 mln are directed to the priority regions and communities experiencing adjustment difficulties.

9. Indications of Success and Trends of Emphasis

The Agency measures its own success in terms of the dollars invested, the contribution agreements or projects approved, and the number of jobs created, maintained or transformed.

The most recent data reported on the Agency's website is for the Fiscal Year 2004–2005 and reported as of 31 March 2005. *Fig. V-4* provides an overview by intervention priority of the Agency's main achievements documented with regard to overall projects in progress in 2004–2005.

In summary, the total value of the 2,099 development projects that were in progress in 2004–2005, stood at $3.8 bn. The Agency contribution is to paying $952.8 mln over the next few years for implementation of these projects. The projects contributed to the creation and maintenance (including the transformation) of more than 14,000 jobs in the different regions of Quebec. In addition to these measures the table indicates positive responses to an annual survey of Canada Economic Development projects. For example, 73.9% of beneficiaries indicated that they would not have been able to complete their projects without financial assistance from the Agency, and 50.1% mentioned the help contributed to increased sales.

Another indication of the success of these regional development initiatives is the evolution of local social networks and the development of local capacity. According to one study (*Landry, Amara, and Ouimet 2002*).

"A new vision of regional development is gradually tending to replace the traditional vision. According to this new vision, development is no longer considered an event, but rather a process in which regional players are proactive and not continually waiting for events to happen. This new vision of development finds expression with such terms as *innovating communities*, *learning regions*, *clusters* and *interactive learning*".

Evidence of this increased organizational capacity throughout Quebec is seen in the expanded clientele which includes social economy enterprises, non-profit organizations (NPOs) which provide services to enterprises as well as facilitation and mobilization services to the development milieu, and communities.

DEPARTMENTAL PERFORMANCE Main results observed as of March 31, 2005	
Number of projects in progress in 2004-2005	2,099
Indicator of promotion of regional development	
▪ total value of development projects in progress (total cost, irrespective of funding source)	*$3.8 billion*
Incentive effect of financial assistance	
▪ proportion of beneficiaries stating that they would not have completed their projects without Agency assistance (completion effect)	73.9%
Indicators of enterprises' competitiveness	
▪ proportion of respondent enterprises stating increased sales	51.0%
▪ average sales increase	$657,000
Indicators associated with vitality of communities	
▪ total value of development projects in progress (total cost, irrespective of funding source)	*$2.2 billion*
▪ initiatives stemming from local agents owing to services provided by Agency-funded development organizations	395
Agency's financial commitment to encourage completion of projects in progress in 2004-2005	
▪ total value of financial assistance approved by the Agency	*$952.8 million*
▪ actual expenditures in 2004-2005	*$286.3 million*
▪ total expenditures incurred (including spending from prior years)	*$505.3 million*

Intervention priority *Innovation—Knowledge economy*	
Number of projects in progress	916
Indicator of enterprises' competitiveness	
▪ proportion of respondent SMEs stating increased sales	50.1%
Indicator of effect of completion of innovation projects	
▪ proportion of respondent SMEs stating that the main result of their project was:	
- reduction in production costs	26.5%
- improvement in corporate business processes	26.5%
- commercialization of new products or services	24.8%
- enhancement of productivity	8.7%
- grant of patent	2.2%
- other results	11.3%
Expenditures made to generate the results shown above	
▪ actual expenditures in 2004-2005	*$101.3 million*
▪ total expenditures incurred	*$175.6 million*

Intervention priority *Regions experiencing adjustment difficulties*	
Number of projects in progress	690
Indicator of support to regions experiencing adjustment difficulties	
▪ total value of development projects in progress (total cost, irrespective of funding source)	*$486.7 million*
Indicator of entrepreneurship effect	
▪ enterprises in pre-startup, startup or expansion	1,287
Employment indicator	
▪ jobs created, transformed or maintained	3,592
Local empowerment indicator	
▪ initiatives originating locally as a result of services provided by development organizations funded by the Agency	168
Expenditures made to generate the results shown above	
▪ actual expenditures in 2004-2005	*$62.9 million*
▪ total expenditures incurred	*$124.5 million*

Note: Performance report for the period ending March 31, 2005 (Summary).
Source: CED-QR 2005c.

Fig. V-4. Indications of Program Success, CED-QR

“Regional development cannot succeed without the local economic milieu playing a very active role in it and taking it in hand; this is a lesson learnt from decades of efforts by North American and European governments in local and regional development. It is from this observation that the agency’s interest in Local capability to energize development of the local economy stems, its first activity with respect to improving the environment for economic development of the regions. Co-operation and convergence of the efforts of a region’s development agents are essential conditions for enhancing its economic prosperity and standard of living. To bring together local players and achieve consensus on strategies and priorities that are promising for economic development, the regions have to be able to count on the vitality of local and regional development agencies” (*CED-QR 2004*).

From another perspective, the evidence from peripheral regions might lead one to be less optimistic about development prospects of those regions experiencing progressive declines in population through out migration. In a recent study of five peripheral regions of Quebec (Gaspé, Bas-Saint-Laurent, Saguenay-Lac St-Jean, Abitibi-Témiscamingue, Côte-Nord), Polèse and Shearmur (2006) reflect on the implications of regional decline for the formulation of local economic development strategies. They argue that (*Polèse and Shearmur 2006, 43–44*):

“Regional decline will become an increasingly prevalent occurrence in nations at the end of the demographic transition whose economic geographies display centre-periphery relationships. In such nations, local economic development strategies cannot (and should not) be put forward as a means of arresting population and employment decline… The task becomes one of ensuring the transition to an economic base concomitant with future (lower) population levels, which means not only a change in public discourse (different from “we will grow again if we only pull together”), but also the setting of new goals… Devising positive decline strategies will not be an easy task and will doubtless entail an even greater reliance on community solidarity and cooperation than past economic growth strategies”.

Table V-4 summarizes a statistical comparison of urban and rural areas in Quebec. Urban areas had nearly twice as many residents (v3), higher measures for income (v20, v21, v36, and v40), education (v16 to v18), employment (v 25 and v26), residential mobility (v10 to v12), people working at the same place (v23), and value of owned dwellings (v43). Urban areas also registered more employment in the service sector employment (v29 to v35) along with more members of visible minorities (v14). Rural areas are more dependent upon income from government transfers (v37 and v38), have a higher rate of unemployment (v27) and have a higher share of residents whose mother tongue is French (v8). They experienced population decline (v4).

Table V-4

Comparison of Well Being between Rural and Urban Quebec (Based on 2001 Census Division Averages)

	v3	v4	v5	V6	v7	v8	v9	v10	v10a
Rural (N=83)	2,681,061	–1.02	0.02	40.16	4.98	92.32	89.39	0.3	10.31
Urban (N=16)	4,556,418	3.06	0.31	37.97	6.29	86.86	87.2	0.76	12.04

	v11	v12	v12a	v13	v14	v15	v16	v17	v18
Rural (N=83)	69.64	0.88	29.48	0.4	0.47	23.24	12.16	11.27	11.82
Urban (N=16)	61.07	2.09	36.84	1.96	4.03	18.12	20.94	22.04	19.48

	v19	v20	v21	v22	v23	v24	v25	v26	v27
Rural (N=83)	47.22	25,178.58	34,303.18	96.6	82.86	81.85	61.11	54.79	11.47
Urban (N=16)	55.16	31,551.81	41,226.06	94.55	87.43	78.58	67.52	63.22	6.52

	v28	v29	v30	v31	v32	v33	v34	v35	v36
Rural (N=83)	25.89	3.53	16.19	11.07	7.44	13.77	4.1	7.19	18,587.55
Urban (N=16)	21.63	5.46	17.06	16.26	10.23	19.57	6.8	8.21	23,771.44

	v37	v38	v39	v40	v41	v42	v43	v44	v45
Rural (N=83)	71.33	18.61	10.06	48.648.23	25.86	71.94	80,332.84	4.01	5.14
Urban (N=16)	78.32	11.48	10.22	61,260.69	23.39	65.41	114,403.00	3.71	5.15

Notes: Urban is defined as a census division with a population greater then 100,000; all others are rural. Variables are defined in *Table II-4*.

Source: Statistics Canada, 2001 Community Profiles.

Available: http://www12.statcan.ca/english/profil01/CP01/Index.cfm?Lang=E

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VI. Western Canada's Surrogate SEZ Regional Development Zones, WD

1. Introduction

Western Canada presents two different area-based economic development programs. One is the federal authority, Western Economic Diversification Canada, which serves a pan-regional development role that is broadly similar to that of ACOA. The other is a new inter-provincial initiative, The British Columbia-Alberta Trade, Investment, and Labour Mobility Agreement. Both programs have a territorial basis as well as other elements in common with special economic zones.

This section of the paper first provides a summary description of The British Columbia-Alberta Trade, Investment, and Labour Mobility Agreement. It then describes the Government of Canada's regional development agency, Western Economic Diversification Canada, and its efforts in western Canada.

For the purpose of this paper, Western Canada includes the four provinces Manitoba, Saskatchewan, Alberta, and British Columbia, as shown on *Fig. VI-1* below.

Fig. VI-1. Western Canada – British Columbia, Alberta, Saskatchewan, and Manitoba

2. The British Columbia-Alberta Trade, Investment, and Labour Mobility Agreement

The British Columbia-Alberta Trade, Investment, and Labour Mobility Agreement is a comprehensive inter-provincial trade agreement that was signed on 28 April 2006 and will come into force by 01 April 2007. The implementation of the agreement will be monitored over a two-year transitional period ending on 01 April 2009. By that time the agreement will be extended to coverage of municipalities; school boards; publicly-funded academic, health and social service entities, financial institutions and financial services and Crown corporations. Ongoing efforts will be made to reduce exceptions and ensure broad and comprehensive coverage. It is also interesting and significant to note that British Columbia and Alberta hope to encourage other provinces and the federal government to join the agreement.

The British Columbia-Alberta Trade, Investment, and Labour Mobility Agreement creates a market of 7.5 mln people and constitutes, in effect, Canada's second largest economy next to Ontario. Its purpose is to create a more open, competitive economy where goods, services and investments can move freely. By eliminating economic barriers between these two provinces, the Agreement hopes that billions of dollars can be saved, reinvested or passed on to consumers.

The agreement establishes a set of General Rules and Special Provisions that apply to all government measures across all sectors of the economies of British Columbia and Alberta. The Agreement clearly specifies for investors, businesses and workers whether a measure is subject to the rules of the agreement or if it is an exception.

The agreement also establishes a dispute resolution mechanism that is intended to be effective and enforceable. The dispute resolution process is accessible to both governments and individuals and involves a consultative and cooperative approach. When necessary, disputes will go to an arbitration panel which can issue a binding report, and apply fines in the case of non-compliance.

Government measures covered in the agreement include legislation, regulations, standards, policies, procedures and guidelines that affect trade, investment and labour mobility. Below are highlighted some key areas covered by the Agreement (*British Columbia, Ministry of Economic Development 2006b*):

(1) Business Establishment:

(a) Businesses will not face duplicate registration and reporting requirements;

(b) Businesses will not be required to maintain a local office or be resident in a province.

(2) Labour Mobility:

(a) Occupational standards will be reconciled so skilled workers can seek opportunities in either province;

(b) More employment opportunities and greater labour mobility will attract more skilled workers.

(3) Energy:

(a) Companies will benefit from Canada's only energy trade agreement, providing significant opportunities in both provinces;

(b) Standards in both provinces will remain compatible regionally and within North America;

(c) Management of land use, conservation and development will be conducted in a non-discriminatory manner.

(4) Transportation:

(a) Commercial vehicles may operate in either province without added registration requirements;

(b) Businesses and consumers will benefit from lower shipping costs;

(c) The region's status as North America's gateway to the Asia Pacific will be enhanced.

(5) Procurement:

(a) Government procurement will be even more open to suppliers in both provinces;

(b) An open tender process for contracts;

(c) A wider array of services will be covered.

(6) Business Subsidies:

(a) Harmful business subsidies will be curtailed.

Government measures that are exempt from the agreement include Provincial regulations and policies for water, taxation, royalties, labour standards, occupational health and safety, procurement of health and social services, social policy, and Aboriginal policies and programs, public safety and security, environmental and consumer protection, health and social services, and conservation of non-renewable, exhaustible or other essential resources.

3. Western Economic Diversification Canada (WD)

This section highlights the key features of the Government of Canada's regional development agency in western Canada**,** Western Economic Diversification Canada (WD). As with the previously described federal programs of eastern Canada, this discussion of WD has six objectives:

In light of the above, the major purpose of this section of this paper is six fold:

(1) To identify the mandate of the agency and consider its characteristics as a surrogate Canadian special economic zone;
(2) To present an overview of the governance of the agency;
(3) To describe its structure and regional programs;
(4) To focus on the nature of help that is provided to the region, its business and individuals to help them develop;
(5) Examine the financial structure of the inflow of funds as well as their dispersion; and
(6) Look for indications of successful endeavours and trends in the region.

4. Mandate

Western Economic Diversification Canada (WD) was established in 1987 to help lessen economic dependence on natural resources in the western provinces (British Columbia, Alberta, Saskatchewan and Manitoba). Under the *Western Economic Diversification Act*, 1988, the department is mandated to "promote the development and diversification of the economy of Western Canada and to advance the interests of Western Canada in national economic policy, program and project development and implementation".

This is a very broad mandate whose territorial basis encompasses the entire area of the four western provinces. WD does not differentiate among geographic sub-regions within the provinces. In this respect, the mandate and operations of WD are different from those of FEDNOR, CED-QR and ACOA with their sub-regional foci. Nonetheless, several of the programs offered by the WD support local initiatives in both urban areas and rural communities. Furthermore, as will be shown, the majority of WD grants and contributions are delivered in partnership with other levels of government, particularly the provincial governments, each of which has their own economic development ministries whose programs are delivered in many instances at the sub-regional and community levels. For more information on these provincial programs, see for example:

British Columbia Ministry of Economic Development

http://www.gov.bc.ca/bcgov/content/docs/@2O2CY_0YQtuW/mpi0603rev.pdf

Ministry of Alberta Economic Development

http://www.alberta-canada.com/regionalDev/regionalEconomicDevAlliances/

Saskatchewan Regional Economic and Co-operative Development

http://www.rd.gov.sk.ca/default.asp

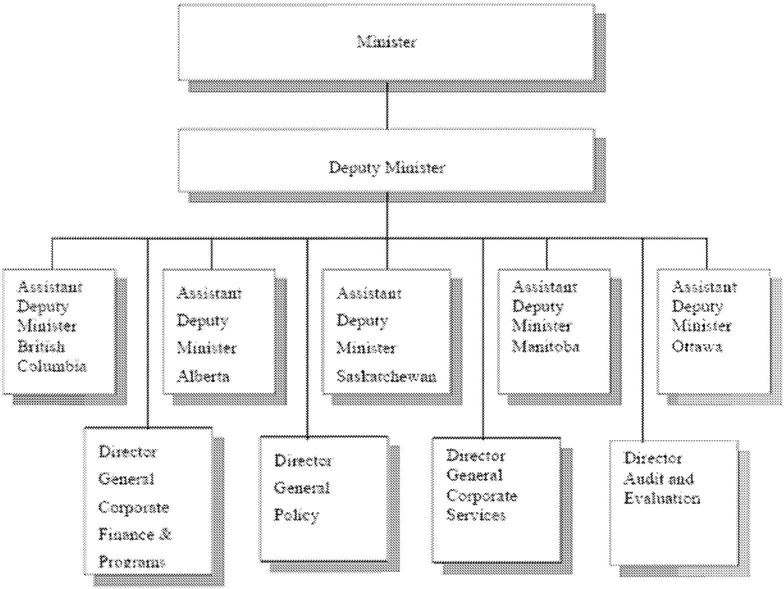
Manitoba Competitiveness Training and Trade

http://www.gov.mb.ca/iedm/index.html.

5. Governance

Western Economic Diversification Canada (WD) is a department of the Government of Canada. The Minister of Western Economic Diversification is a member of the Cabinet of Canada and also serves as the chief executive of Western Economic Diversification Canada. The post is traditionally held by an MP from Western Canada, although occasionally the responsibilities have been accorded to the Industry minister. The current Western Economic Diversification Minister is Carol Skelton and the Deputy Minister is Oryssia Lennie.

The department's head office is located in Edmonton, Alberta, co-located with the Regional Office for Alberta. Regional offices are located in each of the other western provinces - Winnipeg, Saskatoon and Vancouver – with a liaison office in Ottawa. Regional satellite offices also exist in Calgary and Victoria. The department's Deputy Minister is located in Edmonton, and Assistant Deputy Ministers are located in Vancouver, Edmonton, Saskatoon, Winnipeg and Ottawa. Each of the western Assistant Deputy Ministers is responsible for the delivery of programs and services in their region, as well as corporate responsibilities. The Ottawa based Assistant Deputy Minister plays the lead role in the department's advocacy activities. Overall, Western Economic Diversification has approximately 350 employees. *Fig. VI-2* shows the organizational structure of WD.



Source: Treasury Board of Canada 2006, 54.

Fig. VI-2. WD's Organizational Structure

6. Structure of Regional Programs

Western Economic Diversification Canada's programs are not delivered at the regional level within the western provinces. Rather, as previously indicated, the majority of WD grants and contributions are delivered in partnership with other levels of government, particularly the provincial governments, which have their own economic development programs delivered at the sub-regional and community levels. Overall, the programs of Western Economic Diversification Canada are of three kinds: partnerships, direct, and other national programs (i.e. horizontal initiatives), as described below.

1. Partnerships

The majority of WD grants and contributions are delivered in partnership with other levels of government. These partnerships include (Treasury Board of Canada 2006):

1.1. Western Economic Partnership Agreements (WEPAs)

WEPAs are multi-year funding commitments to strengthen economic activity and improve quality of life in western communities. They are cost-shared equally with each of the four western provinces, with a total of $200 mln allocated to initiatives identified as federal and provincial priorities.

1.2. Urban Development Agreements (UDAs)

UDAs are partnerships of federal, provincial and municipal governments working in collaboration on broad issues such as inner city revitalization, strengthened innovation or sustainable economic development.

1.3. Canada-Saskatchewan Northern Development Agreement (C-SNDA)

The C-SNDA is a five-year $20 mln agreement that will help northern Canadians improve regional economic infrastructure, employment prospects, educational and business expertise. It will also increase research and industry innovation, and improve the region's ability to attract business investment.

2. Direct Programs

WD's also directly support projects delivered, either alone or in partnership with other organizations. These other organizations include universities and other post-secondary academic institutions, research institutes, industry associations and other not-for-profit organizations.

2.1. Western Diversification Program (WDP)

The WDP invests in projects that support WD's strategic priorities of innovation, entrepreneurship and community economic development, including a number of partnership programs undertaken with other levels of government.

2.2. Loan and Investment Program (LIP)

The LIP allows financial institutions to supply loan capital to clients to whom it would not otherwise make loans. Under this program, WD contributes funds to a "loan loss reserve", which partly offsets higher risks associated with eligible loans to small businesses. Eligible clients apply directly to the financial institutions partnered with WD under this program.

2.3. Canada Foundation for Innovation Support Program (CFISP).

The CFISP reimburses qualified western research institutions up to 90 per cent of eligible direct costs incurred, to a maximum of $20,000, to assist with the cost of preparing a Canada Foundation for Innovation proposal.

2.4. Western Canada Business Service Network (WCBSN)

The WCBSN is a group of several independent organizations that receive funding from WD to provide a range of services to help create and build small businesses across the West. [This includes the ninety Community Futures Development Corporations (CFDCs), the four Women's Enterprise Initiative Centres (WEIs), and the four Francophone Economic Development Organizations (FEDOs)].

3. Horizontal Initiatives

Finally, like the other federal regional development agencies, WD delivers a number of national programs in the western provinces, including (*Treasury Board of Canada 2006*):

3.1. Urban Aboriginal Strategy (UAS)

The UAS, funded by Indian and Northern Affairs Canada, aims to reduce the level of disparity that urban Aboriginal people currently face by tailoring government programs to address the local needs and priorities of Aboriginal people living in cities. WD is responsible for implementation of Urban Aboriginal Strategy projects in British Columbia, Alberta and Manitoba. Service Canada delivers this initiative in Saskatchewan.

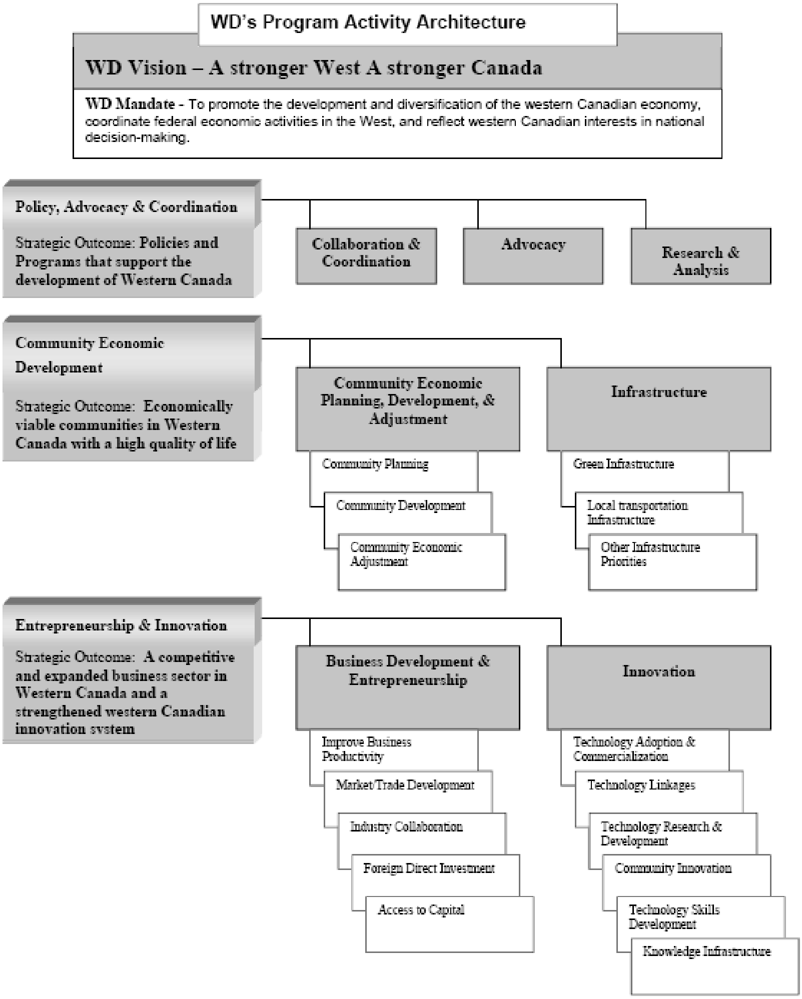
3.2. Municipal Rural Infrastructure Fund (MRIF)

The MRIF will invest $278 mln in the West to improve and increase the stock of core public infrastructure in areas such as water, wastewater, culture and recreation. Delivered by WD in the West, the source of funding for this program is Transport, Infrastructure and Communities.

3.3. Infrastructure Canada Program (ICP)

The ICP is a six-year program that has invested over $543 mln in more than 1,600 projects that are improving the environment, supporting long-term economic growth and enhancing community infrastructure across the West. Although no new applications are being accepted, program funds are still being disbursed.

7. Focus of Help



Source: Treasury Board of Canada 2006, 8.

Fig. VI-3. WD's Program Activity Architecture

Since the Agency was established in 1987, a number of different programs have been initiated and modified over time. With the most recent change in the federal government the new government has re-prioritised some programs. Western Economic Diversification Canada now focuses on achieving three strategic outcomes:

(1) Policy, Advocacy and Coordination: policies and programs that support the development of Western Canada;
(2) Community Economic Development: economically viable communities in Western Canada with a high quality of life; and
(3) Entrepreneurship and Innovation: a competitive and expanded business sector in Western Canada and a strengthened western Canadian innovation system.

Each of the strategic outcomes is summarized in *Fig. VI-3*, along with the particular program activities.

8. Financial Sources and Distributions

The financial sources for Western Economic Diversification's programs are, in general, from the revenues of the Government of Canada, and through contributions and other transfer payments from its partnerships with other levels of government. The allocation of resources among the various programs is summarized in *Table VI-1*.

Overall, in 2005–2006 the Agency budgeted for a total planned expenditure of almost \$307 mln. Of these funds, \$48 mln were direct operating grants and \$258 mln were contributions and other transfer payments leveraged from partners. The funds were distributed to the three strategic outcomes as follows:

Policy, Advocacy and Coordination:	\$11.1 mln
Community Economic Development:	\$54.7 mln
Entrepreneurship and Innovation:	\$97.4 mln

If the federal infrastructure program is included with Community Economic Development, then the total is \$143.5 mln.

Table VI-1

Actual Spending by WD Program Activity, 2005–2006

Program Activity	Operating ($ thousands)	Contributions and Other Transfer Payments ($ thousands)	Total ($ thousands)
(1) Policy, Advocacy and Coordination			
* Collaboration & Coordination	4,770	35	4,805
* Research and Analysis	2,385	527	2,912
* Advocacy	3,414	0	3,414
(2) Community Economic Development			
* Community Economic Planning, Development and Adjustment	9,630	45,026	54,655
* Infrastructure	5,921	137,532	143,453
(3) Entrepreneurship and Innovation			
* Business Development and Entrepreneurship	15,245	39,772	55,018
* Innovation	7,062	35,330	42,392
TOTAL	48,427	258,187	306,649

Source: Treasury Board of Canada 2006, 55–56. Adapted from Table 2.

9. Indications of Success and Trends of Emphasis

WD undertakes an annual review of its own performance and reports to the Parliament of Canada. It also periodically audits and reviews its various programs and priorities in terms of their alignment with, and progress towards, the Department's and federal government's strategic outcomes. The WD website provides a reasonably complete archive of these past reviews and reports.

The annual performance reports provide numerous detailed examples of the progress being made towards achieving the Department's three strategic outcomes. Probably the best indications of the success of the program can be found in excerpts directly quoted from the most recent performance report (*Treasury Board of Canada 2006, 25–55*).

In terms of policy, advocacy, and coordination, it has been noted that:

"During 2005–2006 the department drafted an Advocacy Strategy to better target its resources to maximize the department's influence on initiatives that have the greatest impact on the West.

WD's advocacy work on the Asia-Pacific Gateway and Corridor Initiative is strengthening Canada's position in international commerce through deeper and broader linkages with the Asia-Pacific region".

With respect to community economic development, it has been observed that:

"In 2005–2006, WD undertook a number of activities to support the realization of communities in Western Canada that are economically viable with a high quality of life. Efforts included the implementation of the new Municipal Rural Infrastructure Fund (MRIF) in Saskatchewan and Manitoba. As of March 31, 2006 approximately $26 mln (63 per cent of available funding) was approved for 37 projects in Manitoba and $15 mln (35 per cent of available funding) was approved for 95 projects in Saskatchewan. Although the results of these investments will not be known for some time, they are expected to improve and increase the stock of core public infrastructure in areas such as water, wastewater, culture and recreation, as well as improve the quality of life and economic opportunities for smaller communities.

In 2005–2006, five-year, cost-shared tripartite Urban Development Agreements (UDAs) were signed by the federal, provincial and municipal governments for both Saskatoon and Regina. These UDAs will see an investment of $10 mln in each city targeted to promoting a positive business climate, enhancing competitiveness, developing strategic infrastructure and improving the level of Aboriginal participation in the economy".

Finally, the following remarks have been made about entrepreneurship and innovation:

"In 2005–2006, WD supported numerous phases along the technology commercialization continuum. This included support for organizations such as technology transfer offices at post secondary institutions that identify, protect and license technologies, as well as support for technology adoption and adaptation. Approximately 31 per cent of WD's total innovation-related project approvals in 2005–2006 were for projects that supported the adoption or commercialization of new technologies in Western Canada.

WD's earlier investments in this area have led to numerous results including an increase in the number of technologies developed in research institutions having commercialization potential… To illustrate, as of March 31, 2006, BCCA's Technology Development Office activities have resulted in 93 new invention disclosures, 39 patent applications, 49 licensing deals, and the creation of two new spin-off companies.

WD's ongoing support of $20 mln since 1995 to Telecommunications Research Laboratory (TRLs), Canada's largest information and communications technology research and development consortium, has proven an effective mechanism for increasing the investment for commercialization of new technologies in the West.

During 2005–2006, WD approved $7.1 mln towards more than 150 projects that support international commerce activities including export readiness and advisory services, trade development, strategic support for trade missions and investment attraction activities, supplier development, conferences, and research.

In October 2004, WD led the Western Canada Technology Capabilities Study Tour that brought 18 representatives from Canadian trade offices in the US to Western Canada to showcase the innovation and science and technology capabilities of the region.

In addition, during 2005–2006 WD and Transport Canada collaboration led to the Federal Budget commitment of $591 mln in new funding for a national Asia-Pacific Gateway and Corridor Initiative to strengthen Canada's position in international commerce with that region.

In 2005–2006, multi-year contribution agreements were put in place with the ninety Community Futures Development Corporations (CFDCs), the four CF Associations, the four Women's Enterprise Initiative Centres (WEIs), and the four Francophone Economic Development Organizations (FEDOs). WD's total commitment under these agreements ($139.9 mln) will ensure that business services and access to capital by western small and medium-sized enterprises (SMEs) will continue to be offered.

In 2005–2006, the members of the WCBSN reported delivering over 760,000 business services and provided lending of $53.8 mln that levered an additional $81 mln and resulted in the creation of approximately 4,400 jobs".

Other than WD's own performance reports, there is very little scholarship published related to the assessment of WD programs. Ultimately, it is difficult to assess whether, and to what extent WD programs have contributed to the economic development and diversification of the west.

A general overview of the nature, extent and trend of regional disparity in the four western provinces is shown by a brief analysis of the 2001 Census data. In the four western provinces there are 91 Census Divisions of which 13 are metropolitan or large urban centres (including for example, Vancouver, Calgary, Regina, and Winnipeg) and 78 are rural. This urban-rural, and to some degree south-north, disparity remains one of the most distinctive dimensions of socioeconomic variation in western Canada. *Table VI-2* provides a snapshot of socioeconomic differences between urban and rural conditions. (Note that this table provides the same information and variables as was provided for eastern Canada in previous sections of this paper).

For western Canada, the table shows that rural areas experience, on average, declining growth rates, higher rates of unemployment, the absence of university-educated youth, lower average incomes, and lower average dwelling values. These indicators reflect the condition of uneven development in western Canada and the development challenge of its rural and remote regions.

They also affirm the general direction of Western Economic Diversification's strategic emphasis on community economic development, innovation and entrepreneurship.

Table VI-2

Comparison of Well Being between Rural and Urban Western Canada (Based on 2001 Census Division Averages)

	v3	**v4**	**v5**	**v6**	**v7**	**v8**	**v9**	**v10**	**v10a**
Rural (N=78)	5,225,255	–0.24	0.09	37.06	82.66	2.37	86.35	1.91	11.74
Urban (N=13)	6,306,075	6.05	0.85	37.44	82.16	1.67	82.83	2.5	14.67

	v11	**v12**	**v12a**	**v13**	**v14**	**v15**	**v16**	**v17**	**v18**

Rural (N=78)	62.61	6.03	31.35	1.38	4.35	17.94	11.9	11.69	13.71
Urban (N=13)	52.84	8.66	38.48	4.18	10.51	26.05	19.45	19.98	21.14
	v19	**v20**	**v21**	**v22**	**v23**	**v24**	**v25**	**v26**	**v27**
Rural (N=78)	48.61	26,060.50	36,280.79	97.55	70.41	77.06	67.34	62.06	8.03
Urban (N=13)	50.54	29,852.77	40,190.23	98.4	79.26	77.64	67.55	62.84	6.52
	v28	**v29**	**v30**	**v31**	**v32**	**v33**	**v34**	**v35**	**v36**
Rural (N=78)	14.35	3.42	17.05	11.7	8.29	12.6	3.58	6.96	19,425.37
Urban (N=13)	15.28	5.5	17.56	17.49	10.05	17.35	5.69	7.87	22,046.46
	v37	**v38**	**v39**	**v40**	**v41**	**v42**	**v43**	**v44**	**v45**
Rural (N=78)	74.37	15.46	10.17	53,512.59	24.86	72.57	111,252.82	45.34	23.78
Urban (N=13)	75.27	12.32	12.4	60,657.23	25.34	68.93	167,425.77	39.37	28

Note: Urban is defined as census division with a population greater then 100,000; all others are rural.
Variables are defined in Table II-4.
Source: Statistics Canada, 2001 Community Profiles.
Available*: http://www12.statcan.ca/english/profil01/CP01/Index.cfm?Lang=E.*

Further to this point, it is interesting to note that the need to address this regional disparity has been affirmed by the Organization for Economic Co-Operation and Development (OECD) in a recent review undertaken at the request of the Government of Canada. According to the OECD report, The Territorial Review on Canada, (2002, abstract):

"Canada is composed of three macroregions: a southern ribbon with all the important metropolitan areas, a zone of rural and non-metropolitan adjacent regions and a sub-continent of remote northern territories. Disparities between these macroregions persist and may even be growing. Opportunities for growth are lost because of these imbalances and also because specific regional advantages are not fully tapped. In many regions, weak local governance is hindering the emergence of local grass-roots projects, diffusion of R&D results to SMEs is slow and dialogue between higher education institutions and firms is poor. This report underlines the need for federal agencies and sectoral departments to continuously assess the consistency of their policies with regard to the three macroregions in order to enhance territorial cohesion and better tailor programmes to local conditions".

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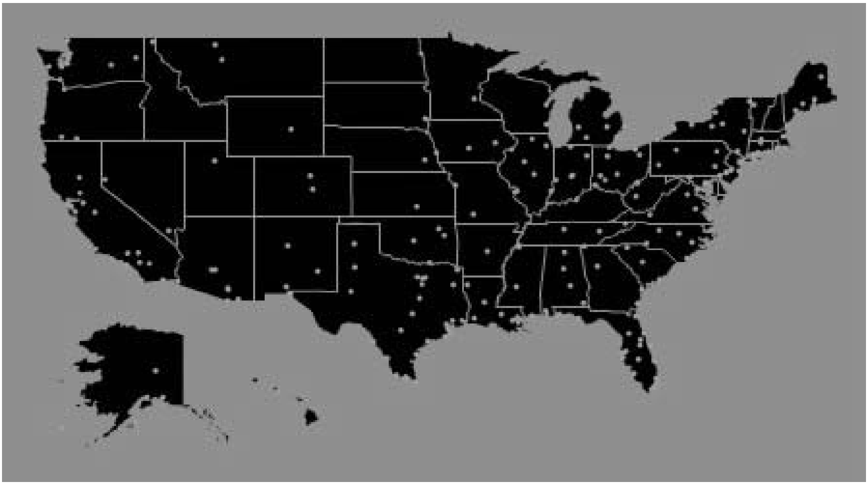
VII. U.S. Foreign-Trade Zones, Surrogate SEZs

1. Introduction

Normally we do not think of the U.S. as requiring free trade zones because of its general strong support philosophy of free trade worldwide. Yet, a U.S. Foreign-Trade Zone (F-TZ) Program, similar to SEZs, was already established in 1934 to help business import goods to the USA. "These special geographic areas – Foreign-Trade Zones – are usually established 'in or adjacent to' U.S. Ports of Entry and are under the supervision of the U.S. Customs Service" (Foreign-Trade Zone Center 2006a). The program focuses on the small and medium size enterprise (SME). One may think of them as being equivalent in operation and size to 'industrial parks' in cities. Merchandise can move into the zones from abroad or from the U.S. The zones are secure areas under U.S. Customs supervision but for import duties and tax considerations they are outside of the U.S. territory. Only once goods leave these zones to enter the US will import duties be considered. The firms operating in these zones can be American or foreign (*Coble International 2006*).

U.S. F-TZs are not mainly export oriented as many traditional SEZs in the world are. Nor are they directly related to improving the local economies, although the jobs they create certainly have a positive influence on the local region. They are found in more then 200 communities, see *Fig. VIII-1*, of which 157 were active in 2004 with more then 2,700 firms operating in them[19], and "conducted more than $317 bn in business, exported $22 billion in goods and provided jobs for 337,039 working Americans" (National Association of Free Trade Zones 2005). In fact these have been set up, and continue to be fostered, in order to improve the competitiveness of American industry in a global setting.

[19] It is amazing that these zones have been in operation so long. The 66th annual report was given in 2004.



Source: Foreign-Trade Zone Resource Center 2006a.

Fig. VII-1. Foreign-Trade Zones in the United States

Overall, American F-TZs have kept a relative low profile and have not been affected by WTO or NAFTA discussions. A helping organisation for these Foreign-Trade Zones is The National Association of Foreign-Trade Zones (NAFTZ), a non profit organisation which aims to “connect global businesses with local communities through the U.S. Foreign-Trade Zone (F-TZ) Program” (*Foreign-Trade Resource Center 2006b*).

2. Governance

As already indicated above, the legal status of the American Foreign-Trade Zone status was established under the authority of the *Foreign Trade Zones Act* of 1934. Presently, the Executive Secretariat of the Board is located within the ‘Import Administration’ of the U.S. Department of Commerce, Washington, D.C. They are, hence, embodied in one of the major departments of the U.S. government. At the micro scale, the local customs port director, in whose jurisdiction the F-TZ is located, is in charge of overseeing all the activities in the zone. The zones, however, also fall under the normal laws of each state and local government jurisdictions.

Interestingly, the actual physical FTZ entity can be sponsored by a "qualified public or private corporations, which may operate the facilities or contract for the operation by public or private firms" (*U.S. Customs and Border Protection 2006*). They have to operate in a public manner and advertise their services and fee rates. "A typical general-purpose FTZ provides lease storage/distribution space to users in general warehouse-type buildings with access to various modes of transportation. Many foreign trade zone projects include an industrial park site with lots on which zone users can construct their own facilities" (*Coble International 2006*). If a good does not fit under the standard zone handling categories, then a sub zone can be set up. However, certain goods, like liquor, firearms, and clocks, can not be processed or stored in any F-TZ.

3. Regional Distribution

As the map above shows, every state has at least one F-TZ. Of the 200-odd approved zones, 60 are not active (i.e. they have the legal status to commence operations but the demand is probably not there). This fact, however, does show that the U.S. is proactive in providing businesses with such opportunities across its lands.

4. Focus and Advantages

Clearly, the focus of the American Foreign-Trade Zones is to help American business to stay competitive. In these zones, firms can store, exhibit, break up, repackage, sell, assemble, distribute, sort, grade, clean, mix with foreign content, manipulate, destroy or manufacture goods. By putting the 'The Executive Secretariat of the Board' of the F-TZs under the Import Administration of the U.S. Department of Commerce, it shows the importance to the American government of this program. Not only are they helping American firms to stay competitive against foreign firms, they also want to give them the same advantage as firm have in SEZs in other countries.

The American F-TZ website, Foreign-Trade Zone, Resource Center (2006c), lists five major overall advantages to firms using the American F-TZs:

(1) relief from inverted tariffs (tax final product not components);

(2) duty exemption on re-exports;

(3) duty elimination on waste, scraps, and yield loss;
(4) weekly entry savings (submit information on weekly shipments vs. per shipment);
(5) duty deferral.

Relief from inverted tariffs means that, by not taxing the components brought in from abroad, but rather only the final product; it puts the American firm on an equal footing with the foreign firm exporting a similar final product to the U.S. The import duties and excess tax on components tend to be substantially higher then those of a finished product. Also, many 'raw' materials for final products have waste associated with them. Leaving this waste at the port of entry saves duties and further transport costs. Reporting all weekly shipments in one report saves import handling charges which are usually based on a per shipment fee. Not having to pay duties until the product is shipped to the consumer saves substantial up front costs.

That the Americans are very concerned about competitive advantage can be seen from a 2004 review of foreign SEZs by the American Foreign-Trade Zone office staff (McGilvray 2004). They looked at the operational parameters and advantages of SEZs in 63 countries, from Argentina to Zimbabwe. Information collected for each country looked at the type and number of zones, their locations, company facilities, whether the zones are outside of the customs territory, ownership, government operation, benefits (e.g. duty free admission, duty free export, manufacturing, need for manufacturing approval, use of foreign and domestic raw materials, entry for domestic consumption, whether duty is paid on entry, and whether duty is paid on components or products) tax exemptions, financial incentives (e.g. grants, loans, and leases/rents), regulatory exemptions, restrictions (e.g. export-only manufacturing, export certain percent of output, domestic content, and domestic investment), and other miscellaneous items.

The detailed foreign SEZ survey came up with a couple of very specific recommendations which are discussed below. Based on the findings, the following recommendations were proposed to increase the efficiency of the U.S. F-TZs in relation to their foreign counterparts (*McGilvray 2004, 10–11*):

(1) "expedite the processing of simple manufacturing requests for existing FTZ sites; and

(2) simplify application guidelines/formats for SMMs and (improve)…pre-application counselling procedures".

SMM refers to small- and medium-sized manufacturers. Clearly the present global economy framework required greater speed and simplicity to improve the competitiveness of U.S. FTZ firms[20].

5. Financial Sources and Industrial Sector Distribution

As already indicated above, the America Foreign-Trade Zone source of income comes from the firms operating in these zones. Most of the firms operating in them are related to oil, automotive, pharmaceutical, and electronic products. About 64% of the inward movement of merchandise comes from the U.S. and the rest from abroad. Of the outflow, only 18% went, in 2004, abroad and the rest was destined for the U.S. market (Foreign-Trade Zone Board 2004).

6. Indications of Success and Trends of Emphasis

How successful have been these Foreign-Trade Zones in the U.S.? One could look at the shipment of merchandise into these zones as a potential indicator. In 2004, the annual report reports the in shipments as $305.2 bn; in 2000 it was $238 bn and in 1995 only $143 bn[21]. In other words, the shipments more then doubled in value in nine years. Even the number of F-TZs increased from 134 to 157 over this time period. The number of firms in 1995 was just over 2,700 while the number of employees was 316,000. That the number of firms stayed constant over these nine years and the number of employees had only increased slightly attest to the increased productivity of the firms and workers over the time period involved (*Foreign-Trade Zone Board 2004*).

From the overall data, it seems that U.S. Foreign-Trade Zones are still relative healthy despite the emergence of NAFTA and the general expansion of free trade on the global scale under the jurisdiction of the

[20] That the 2004 Staff report was taken seriously is seen in the 2006 Staff Report entitled "Improving the Temporary/Interim Manufacturing Procedure for Small and Medium-Sized Manufacturers".

[21] See the annual reports of the Foreign-Trade Zones Board (http://ia.ita.doc.gov/ftzpage/annual-report.html)

WTO. It may be prudent that counties like Canada[22] and Russia examine closely their SEZ policies on such zones.

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[22] According to McGilvray (2004), Canada had only two such zones, called Customs Free Zones, which are supposedly found in Stephenville, Newfoundland and Sydney, Nova Scotia. They, along with the Export Distribution Centres, operate under the Canada Border Services Agency (2006a, 2006b).

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VIII. Export Processing Zones in Latin America and the Caribbean

1. Introduction

In 2002, twenty-two countries in Latin America (i.e. Central and South America) and the Caribbean accounted for 258 (24%) of the world's 1,072 Export Processing Zones (EPZs)[23].There were 83 EPZs in Central America (8%), 98 in the Caribbean (9%), and 77 in South America (7%). The introduction of EPZs within Central America and the Caribbean began during the late-1960s and early-1970s (Baraga 2002). The first established in Colombia (1964), the Dominican Republic (1965), and Mexico (1965). The number and economic importance of EPZs in the region rapidly increased during the 1990s. Mexico has the most extensive EPZ program with 850 zones while Brazil has only a single Free Trade Zone (FTZ)[24]. In terms of size, the majority of operational zones are small (i.e. less than 1,000 hectares) and typically enclosed. The contemporary spatial distribution and temporal introduction of EPZs and FTZs within the Americas is summarized in Table 1[25]. EPZs are prominent in counties with geographic proximity, transportation and communication connections, and trade access to targeted markets (*Madani 1999*).

Although this section focuses upon Latin America and the Caribbean, some brief observations about quasi-EPZs in North America (Canada, America, and Mexico) are warranted to differentiate their functions and operations.

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[23] The only comprehensive and comparative data available at the global scale remains unpublished (World Export Processing Zone Association). These recent figures are taken from *Granados 2005*.

[24] Only four of the 19 EPZs authorized by Brazil's federal government in 1996 are now being constructed. These zones are designed to facilitate economic development in less developed regions (*UNCTAD 2000; McGilvray 2004*). In Panama, EPZs are currently being established on the sites of former American military bases.

[25] Statistical data does not always explicitly distinguish between EPZs, FTZ, and other types of zones. EPZs are often subsumed within the FTZ category. Disaggregated figures by regime are used wherever possible. Zones established on the basis of meso-regions are excluded from this study. For examples and details see UNCTAD 2000.

Canada does not have EPZs. FTZs were proposed, but never implemented, in the maritime province of Nova Scotia (*Calkin, Diblee, and Haites 1979*). Since 2001, Canada has been using Export Distribution Centres (EDCs), a temporary import instrument which operates like an FTZ. Located in or near seaports and international airports, EDCs are storage or distribution spaces provided in general warehouse buildings which allow for storage, sorting, repacking, and refurbishing of domestic and foreign goods for re-export (without paying duties and taxes). Manufacturing and assembly are not permitted (*Canada Revenue Agency 2001*). Privately owned and publicly operated Customs Free Zones (CFZs) permit export-only manufacturing. Canada's only CFZ is located on the site of a former naval base in Sydney, Nova Scotia (Sydport Industrial Park).

The United States of America has general Foreign-Trade Zones (F-TZs) which are industrial parks located at ports of entry. Firms establish themselves in these zones to postpone import duty payments on semi-finished components. Specific sub-zones are offsite F-TZs corresponding to an individual firm's production facility. American F-TZs are platforms for processing and marketing goods to the domestic market.

Mexico established FTZs in 1946. Many of these multi-factory zones were incorporated into the Border Industrialization Program (1961) and the Maquiladora Program (1965) which enables export processing units (i.e. individual production facilities) to locate anywhere. In other words, the maquila regime permits temporary import (in-bond factories) but it does not involve an industrial enclave. In 2002, Mexico approved the development of two FTZs that permit the manufacturing, distribution, and sale of products. Firms operating in these zones will receive various incentives, including tax benefits, without being required to export their output. Numerous states have applied to covert their "bonded areas" (i.e. export processing units) into EPZs.

Under the provisions of the North American Free Trade Agreement (NAFTA), the Canadian and Mexican zones are obsolete because all of Canada and Mexico become an EPZ. Interestingly, there are no provisions for the elimination of the American F-TZs.

2. Establishment

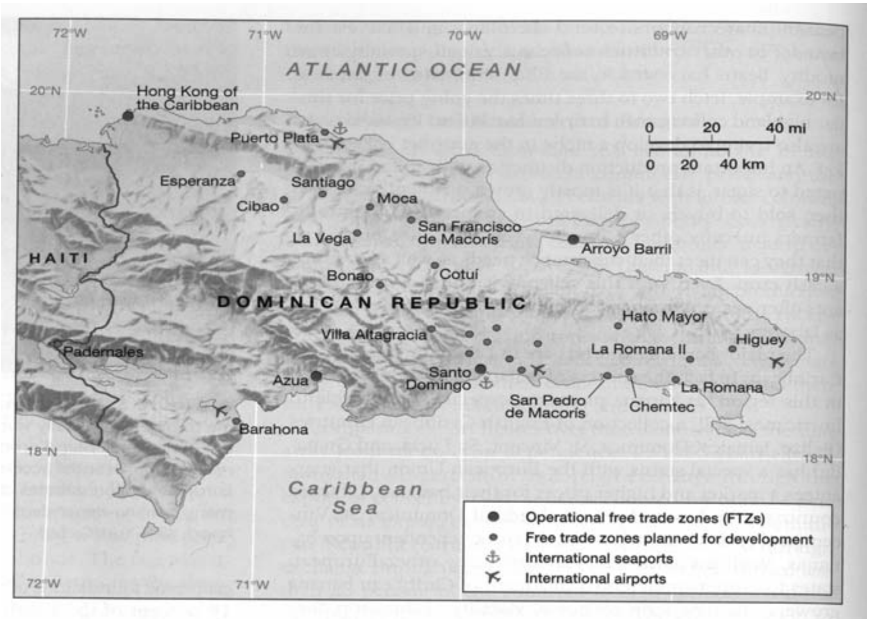
The existence of different types of zones is related to their role(s) as instruments of regional economic development by attracting foreign investment, creating employment and absorbing excess labour, advancing workforce and management skills, transferring technology and knowledge, generating foreign exchange and tax revenue, accessing foreign markets. EPZs are also used to induce domestic entrepreneurs to become involved in non-traditional export production (*Madani 1999; Braga 2002*). In other words, EPZs have catalytic and demonstration effects on local firms and industrial sectors. Within the context of Latin American and the Caribbean, EPZs were created to reduce unemployment and underemployment as well as to increase foreign earnings (*Jenkins, Esquivel, and Larraín 1998*). EPZs have increased trade, created employment, and attracted foreign investment in many parts the western hemisphere (Granados 2005)[26]. Within South America, EPZs "do not have the same importance for the national economy...as they do in Central America and the Caribbean" (*Granados 2005, 75*). South American FTZs are often used as growth poles (e.g. Chile and Colombia). It should be noted that not all zones are successful in all counties.

EPZs are an effective policy instrument for economic development. They have been implemented during the early phases of industrialization as well as during the later phases of industrialization to facilitate export-led growth strategies (*World Bank 1992; Jenkins, Esquivel, and Larra'n 1998; Madani 1999; Cling and Letilly 2001*). Hence, countries whose economies are developing and/or experiencing transition should not rely exclusively on EPZs to attain long-term economic growth and to reduce unemployment levels. Likewise, EPZ should not replace, defer, or impede economic reforms aimed at liberalizing domestic policies (e.g. macroeconomic, trade, and exchange reforms). They should compliment national reforms and facilitate liberalization efforts such that developing countries can improve the extent of their global competitive advantage (*Madani 1999*). In the long run, EPZs should be used as an instrument of transition towards becoming an export-processing country (*Kaplinsky 1995b; Granados 2005*).

[26] Examples include Bolivia, Costa Rica, Dominican Republic, El Salvador, and Honduras.

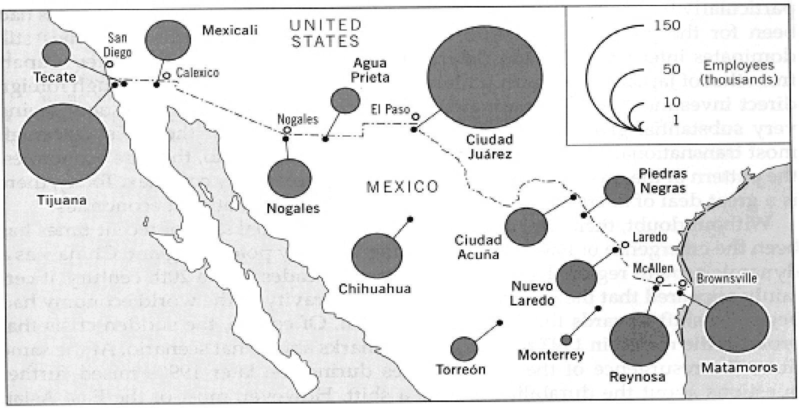
Latin American and Caribbean EPZs are primarily associated with the labour-intensive stages of manufacturing in the textile/garment industry. Also using low-cost labour and imported components, the Mexican and Brazilian EPZs are focused upon the microelectronics industry. South American FTZs tend to be industry-specific (e.g. Brazil and Chile). Data entry and data processing (e.g. Barbados, Jamaica, and Saint Lucia) and financial services (e.g. Aruba) also occur in Caribbean EPZs. The provision of services, such as call centres and tourism, is increasing in Central American EPZs (e.g. Costa Rica, Dominican Republic, and Panama) and South American FTZs (e.g. Colombia, Uruguay, and Venezuela).

Within Central America and the Caribbean, EPZs are located near major urban and industrial centres (especially in Costa Rica and Honduras) and ports with superior infrastructure and skilled workers. EPZs developed in isolated rural areas have been largely unsuccessful. Legislation in several Central American countries (Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, and Nicaragua) permits EPZs and EPZ firms to locate anywhere. In Jamaica and the Dominican Republic, EPZs have been established in several locations, thereby making their entire territories a large EPZ. *Fig. IX-1* shows the spatial configuration (or 'geographical diversity') of EPZs in the Dominican Republic that has enabled backward linkages, regional development, and the catalyst/demonstration effect (*Madani 1999*). Although Mexican maquiladoras are neither EPZs nor FTZs, their spatial concentration within border cities gives them a functional dynamic similar to that of EPZs. *Fig. IX-2* shows the unique arrangement of these quasi-EPZs.



Source: Rowntree, Lewis, Price, and Wyckoff 2000, 200.

Fig. VIII-1. EPZs in the Dominican Republic



Source: Dicken 2003, 79.

Fig. VIII-2. Major Maquiladora Centres in Mexico

3. Legislation

The majority of Central American countries have specific EPZ laws. Some countries also include the “EPZ regime” within legislation that embraces other regulations (*Jenkins, Esquivel, and Larraнn 1998*). For example, the Regime of Temporary Admission (RTA) in Costa Rica, Honduras, and Guatemala, the Free Zone (FZ) law in Honduras and the Fiscal Precincts (FP) law in El Salvador.

EPZ laws in Costa Rica, Nicaragua, the Dominican Republic, and Saint Lucia also confer EPZ status to firms located outside industrial parks (i.e. single factory EPZs)[27]. In Saint Lucia, fenced-in EPZs do not exist; there are only individual plants with EPZ status. RTA laws in Costa Rica and Guatemala as well as FP law in El Salvador allow export-oriented firms to locate anywhere. They can import raw materials, equipment, and machinery duty-free but domestic sales are prohibited. In Costa Rica and Guatemala, manufacturing firms locating in rural or under-developed areas receive additional incentives. Honduras’ FZ law allows clusters of export-oriented firms located within designed municipalities to qualify for incentives. Free Zones are not fenced-in industrial parks. In Trinidad and Tobago, any firm may apply for EPZ status provided that its plant is fenced. Major concerns with allowing “geographically diverse” EPZs along with EPZ firms to locate anywhere (i.e. an open production area) include the costs of providing (and periodically upgrading) infrastructure, utilities, and customs services at multiple sites.

4. Incentives

Tables VIII-2 through IX-6 summarizes the incentives that are provided to EPZ/FTZ firms and EPZ developers in Central America, the Caribbean, and South America. The typical ensemble of incentives provided to export-oriented firms operating in EPZs/FTZs includes:

(1) long-term income tax holidays and concessions;
(2) unlimited duty-free imports of raw materials, machinery and equipment necessary for the production of exports;
(3) tax exemptions and/or concessions;

[27] Individual factories with in-bond or special duty exemptions also exist in Monserrat and Saint Kitts and Nevis.

(4) free repatriation of capital and profits;
(5) free management of foreign exchange (e.g. repatriation of profits in hard currencies);
(6) streamlined customs procedures (e.g. on-site inspection or expedited authorization by zone operators); and
(7) local sales.

Special infrastructure, access to advanced telecommunications and transportation networks, along with subsidized utilities and rental rates are also important incentives. Central American and Caribbean countries offer similar provisions. Variation among countries exists in term of the length of income tax holidays (sometimes based upon export performance) and range of tax exemptions (e.g. exclusion of municipal, property, and sales taxes). Income tax holidays are either absent or being phased out (and replaced with reduced rates) in South America. In Costa Rica and Guatemala, additional incentives are given for firms locating in underdeveloped regions. Local market sales are permitted in Central America provided that there is no competition with domestic industry and provided that import duties are paid (*Willmore 2000*). Cuba, Argentina and Brazil are the only exceptions; unlimited domestic sales are possible subject government approval. Central American countries usually require that a certain percentage of manufacturing output be exported in order to receive incentives[28]. South American countries typically do not use this prerequisite.

EPZ/FTZ firms can be foreign, domestic, or joint ventures. To attract foreign firms, some zones have no restrictions on foreign ownership. Typical incentives to private sector developers of EPZs/FTZs include:
(1) income tax holidays;
(2) import duty exemptions for raw materials, machinery and equipment used to construct and develop the zone;
(3) exemption of certain taxes (e.g. municipal, sales, and real estate taxes).

[28] The minimum export conditions apply in Argentina (100%), Costa Rica (75%), Guatemala (80%), Honduras (95%), and Nicaragua (60–80%).

5. Public-Private Partnerships

EPZs were initially established and managed by the public sector but private sector developments are increasingly common (often by foreign firms). Some countries have EPZs that are owned, operated, and promoted by both public and private entities while others have state owned but privately operated EPZs[29]. The first privately developed EPZ in the Caribbean was constructed in the Dominican Republic in 1965 while the first private EPZs in Central America were established in Costa Rica in 1985. Infrastructure quality and management services in private EPZs often exceed that of their public sector counterparts (*Jenkins, Esquivel, and Larraín 1998; Madani 1999*). Likewise, EPZs that are developed, owned, and managed by private sector firms offer foreign investors a stable business environment with fewer administrative delays and bureaucratic costs, especially the time required for imports and exports to clear customs. Private EPZ can have "a large degree of autonomy" from political changes in national governments (*Madani 1999, 9*). Federal governments have assisted in the development of private EPZs by providing for their regulatory environment and, sometimes, for their overseas promotion. In terms of institutional jurisdiction, national port authorities typically enforce customs regulations in Latin American and Caribbean EPZs.

6. Relevant Policy Recommendations

Based on the preceding overview of the Latin American and Caribbean experience, the following three legislative amendments are recommended for the Russian Federation (*Jenkins, Esquivel, and Larraín 1998; Madani 1999; Granados 2005*):

(1) the diversification of EPZ activities;
(2) the development of backward linkages; and
(3) the coordination EPZ legislation.

The structural composition of export-oriented activities in EPZs should be broadened to include other economic activities. Particular industrial sectors (e.g. services) and sub-sectors (e.g. back office func-

[29] Mexican zones are publicly owned and operated. Privately owned and operated zones exist in Brazil, Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, and Uruguay.

tions and data processing) should be targeted through promotional campaigns. EPZs should not be exclusively composed of textile and garment firm because this sector is to foreign trade restrictions. Electronics and services would respectively enable the acquisition of new technologies and workforce skills.

Backward linkages with “intermediate-producing” local firms should be developed by creating sufficient demand for goods and services among foreign firms operating within EPZs. This would enable foreign direct investment within EPZs to produce a positive effect upon economic activity and growth (i.e. circular and cumulative causation).

EPZ legislation should be harmonized in by establishing a private-public agency (e.g. zone authority) with a mandate to manage the EPZ, implement EPZ and customs laws, and promote backward linkages. EPZ laws should distinguish between firms exporting outside of the Russian Federation and firms exporting outside and inside the Russian Federation. Uniform yet different incentives should be provided for these two types of firms (i.e. fewer incentives for firms exporting outside and inside the Russian Federation). Income tax holidays should not be permanent nor should all taxes be waived. Instead, income tax should not exceed 10 years while other taxes (e.g. sales, municipal, and property taxes) should be modest (*Madani 1999*).

Finally, EPZs and EPZ firms should not be encouraged to locate in underdeveloped, remote, and rural areas (in order to facilitate regional economic development) since these areas lack of infrastructure, well-trained workforce, and local suppliers. Entire regions and municipalities should not be designated as EPZs for the same reasons, especially if they cannot develop and manage industrial parks. It is also not recommended that ‘single factory’ EPZs (i.e. firms with EPZ status) be widely implemented.

Table VIII-1

Export Processing Zones and Free Trade Zones in the Americas, 2002

Country (Zone Type)	First Zone Established	Number of Operational Zones*	Size of Operational Zones**
1	2	3	4
North America			
Canada (CFZ)	1995	1	Small Area
United States (F-TZ)***	193 4	469 (249 MF + 220 SF)	Small Area; Industry Specific
Mexico (FTZ)****	1965	850 (6 MF + 844 SF)	Small Area; Performance Specific
Central America			
Belize (EPZ)	1999	30 (4 MF + 26 SF)	Small Area
Costa Rica (EPZ)	1977	139 (12 MF + 127 SF)	Small Area
El Salvador (EPZ, FTZ)	1973	14 (6 EPZ, 8 FTZ)	Small Area
Guatemala (FTZ)	1971	18 (14 MF + 4 SF)	Small Area
Honduras (EPZ)	1972	284 (32 MF + 252 SF)	Small Area
Nicaragua (EPZ)	1976	72 (10 MF + 62 SF)	Small Area
Panama (FTZ, EPZ)	1948	12 (1 FTZ+ 11 EPZ)	Small Area; Industry Specific
Caribbean			
Antigua and Barbuda (FTZ)	1997	1 MF	Small Area
Aruba (FTZ)	(1950s)	1 MF	Small Area
Bahamas (FTZ)	1955	3 MF	Small Area
Cuba (EPZ, FZ)	1997	3 MF	Small Area
Curacao (FTZ)	late-1950s	3 MF	Small Area
Dominican Rep. (EPZ)	1965	603 (54 MF + 549 SF)	Small Area; Industry Specific
Haiti	1960	4 MF	Small Area
Jamaica (EPZ)	1976	3 MF	Small Area
Puerto Rico (F-TZ)	1947	3 MF	Small Area
Saint Kitts and Nevis (FTZ)		4 MF	Small Area
Saint Lucia (FTZ)	1986	2 MF	Small Area
Trinidad and Tobago (FTZ)	1990	17 MF	Small Area; Industry Specific
South America			
Argentina (FTZ)	1997	10 MF	Small Area
Bolivia (FTZ)	1991	15 MF	Small Area
Brazil (FTZ)*****	1967	1 MF	Small Area
Chile (FTZ)	1975	2 MF	Small Area
Colombia (FTZ)	1964	12 MF	Small Area

1	2	3	4
Ecuador (FTZ)	1974	8 MF	Small Area
Paraguay	2001	1 MF	Small Area
Peru (FTZ)	(1990s)	4 MF	Small Area
Uruguay (FTZ)	(1987)	9 MF	Small Area
Venezuela (FTZ)	1986	4 MF	Small Area

Notes:
* MF= Multi-Factory Zones (Industrial Parks); SF = Single Factory/Enterprise Zones.
** Small Area = Firms must locate within the zone to receive incentives; Industry Specific = Zones admitting only specific industries but firms may locate anywhere to receive incentives; Performance Specific = Zones admitting only firms complying with performance standards (e.g. investment amount, technology sophistication, employment generation) but firms can locate anywhere to receive incentives.
*** General FT-Zs are 'import processing zones' in the form of industrial parks offering warehousing and logistics.
**** In Mexico, 'maquiladora zones' refers to export processing units (i.e. individual factories or plants). There are 107 industrial parks corresponding to EPZs. The six FTZs are delineated at the state/regional level.
***** Brazil's Manaus Free Trade Zone is actually an 'import processing zone'. Most of its output is sold in the domestic market.
Sources: World Bank 1992; Shatz 2001; Braga 2002; Singa Boyenge 2003; McGilvray 2004; Granados 2005; World Economic Processing Zone Association 2006.

Table VIII-2

Incentives for FTZ Firms in North America

Incentive	Canada (CFZ)	United States (F-TZ)	Mexico (FTZ)
Income Tax Holiday	reduced (based on export output)	none	reduced (25% income tax)
Import Duties on Raw Materials, Machinery, Equipment	100% exemption	100% exemption	100% exemption
Tax Exemptions	sales, property, VAT, excise, inventory	(range of taxes)	VAT, inventory, excise
Repatriation of Capital and Profits			
Foreign Exchange			
Customs Procedures	streamlined import/export procedures		streamlined import/export procedures
Local Sales	permitted		up to 40% of output

Sources: UNCTAD 2000; Warden 2000; McGilvray 2004.

Table VIII-3

Incentives for EPZ/FTZ Firms in Central America

Incentive	Belize (EPZ)	Costa Rica (EPZ)	El Salvador (EPZ, FTZ)	Guatemala (FTZ)	Honduras (EPZ)	Nicaragua (EPZ)	Panama (FTZ)
Income Tax Holiday	20 years	8 years for manufacturing firms; 6 years for commercial firms (both until 2007)	10 years (EPZ)	10 years for manufacturing firms; 5 years for commercial firms	20 years	10 years	15 years
Import Duties on Raw Materials, Machinery, Equipment	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption
Tax Exemptions	VAT, excise, capital gains, dividend, transfer, sales, property	excise, sales, consumption, real estate transfer, property, municipal	VAT, sales, corporate, property transfer, municipal	VAT, sales, property, municipal	excise, sales, corporate, property, municipal	excise, sales, corporate, property, municipal	sales, property
Repatriation of Capital and Profits	tax exempted	tax exempted	tax exempted	tax exempted	tax exempted	tax exempted	tax exempted
Foreign Exchange	free management	free management	free management	free management	free management	free management	free management
Customs Procedures	streamlined import/export procedures	streamlined import/export procedures	streamlined import/export procedures	streamlined import/export procedures	streamlined import/export procedures	streamlined import/export procedures	streamlined import/export procedures
Local Sales	prohibited	up to 25% of output	up to 15% of output	up to 20% of output	permitted (upon payment of customs duties)	permitted (based on jobs created and local inputs)	permitted (on payment of customs duties)

Note: Factories with in-bond or special duty exemptions also exist in Belize and Guatemala.
Sources: Jenkins, Esquivel, and Larraín 1998; UNCTAD 2000; McGilvray 2004; Jenkins 2005.

Table VIII-4

Incentives for Private EPZ/FTZ Developers in Central America

Incentive	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua
Income Tax Holiday	10 years (until 1992)	15 years	10 years	20 years (conditional)	15 years
Import Duties on Raw Materials, Machinery and Equipment	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption
Tax Exemptions	none	10 years	5 years (real estate taxes only)	none	100% exemption

Sources: Jenkins, Esquivel, and Larraín 1998; Jenkins 2005.

Table VIII-5

Incentives for EPZ/FTZ Firms in the Caribbean

Incentive	Bahamas (FTZ)	Cuba (EPZ)	Curacao* (FTZ)	Dominican Rep.** (EPZ)	Haiti	Jamaica (EPZ)	Puerto Rico (F-TZ)	Saint Lucia (FTZ)	Trinidad and Tobago (FTZ)
1	2	3	4	5	6	7	8	9	10
Income Tax Holiday	20 years	12 years	reduced (2% income tax)	15 years (25 years if border location)	8 years	10 years	10–25 years	15 years	10 years
Import Duties on Raw Materials, Machinery and Equipment	100% exemption	100% exemption	100% exemption	100% exempt	100% exempt	100% exempt	100% exemption	100% exempt	100% exempt
Tax Exemptions	all taxes	EPZ labour		inventory, construction, real estate transfer, municipal	all taxes	sales, property	excise, property, municipal	tax exempted	VAT
Repatriation of Capital and Profits	tax exempted	tax exempted		tax exempted	tax exempted	tax exempted	tax exempted		

1	2	3	4	5	6	7	8	9	10
Foreign Exchange	free management	regulated	free management	free management	free management	free management	free management	free management	
Customs Procedures				streamlined import/ export procedures		streamlined import/ export procedures	streamlined import/ export procedures		
Local Sales		up to 25% of output	up to 25% of output	up to 20% of output		prohibited		prohibited	

Notes:

* FTZs in Curacao and Aruba include free zones for warehousing and services.

** The 25-year tax holiday in the Dominican Republic only applies to the Dominican-Haitian border zone.

Sources: Kaplinsky 1993; Willmore 1995a; Willmore 1995b; Madani 1999; Willmore 2000; McGilvray 2004.

Table VIII-6

Incentives for FTZ Firms in South America

Incentive	Argentina (FTZ)	Brazil (FTZ)	Chile (FTZ)	Colombia (FTZ)	Ecuador (FTZ)	Paraguay (FTZ)	Peru (FTZ)	Uruguay (FTZ)	Venezuela (FTZ)
Income Tax Holiday	none	3–10 years (25% income tax)	none	reduced (15% income tax)	20 years	none	10 years (based on export output)	none	10 years
Import Duties on Raw Materials, Machinery and Equipment	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption	100% exemption
Tax Exemptions	VAT, property, sales, utilities, export, municipal	business, sales, real estate	VAT, corporate, sales, real estate	VAT, sales	VAT, sales, municipal	VAT, all taxes	VAT, excise, sales, municipal	VAT, excise, all taxes	all taxes
Repatriation of Capital and Profits		tax exempted		tax exempted (to be eliminated)	tax exempted			tax exempted	tax exempted
Foreign Exchange	free management	free management	free management	free management	free management			free management	
Customs Procedures	streamlined import/export procedures	streamlined import/export procedures		streamlined import/export procedures				streamlined import/export procedures	
Local Sales	unlimited (upon payment of duties)	unlimited	permitted (upon payment of taxes)	permitted (upon payment of taxes)	prohibited		permitted (upon payment of duties)	prohibited	

Sources: UNCTAD 2000; McGilvray 2004; World Bank 2005.

Note: The proposed Brazilian EPZs allow for up to 10% of output to enter the local market.

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IX. International Experiences of Creation and Functioning of SEZ

As of July 2006, there were between 1,200 and 2,000 free economic zones of various types (the respective expert estimates vary) in the world. They range from free zones and ports to free entrepreneurship and offshore zones, and technopolises.

1. Western Europe

The oldest free trade zones first had emerged in German cities of Hamburg and Bremen back in the 19th century, later followed by the city of Kiel and some other German towns. It was not accidental that it was these cities that gave a rise to free trade zones. Hamburg, for instance, is a *Lande* town, a huge maritime and river port situated by Elba river, within 100 km. from the Northern Sea. There are an international airport and various industrial facilities there. The local FTZ embraces two sites in the port and a part of the territory of another zone situated in the town of Kukshaven (which is administered by the government of the Lower Saxony). FTZ “Hamburg” includes numerous six- and eight-storey warehouse facilities and other storehouses (with a total storage area of over 600,000 sq.m.), storage facilities for fruits and vegetables, and oil and petroleum derivatives.

The administration structure of the zone appears considerably distinct from others. The administration of the free port exercises control over the free trade zone (and forms a part of the *Lande* Hamburg’s government) and has a power to exercise customs functions, except for duties collection. Corporations and private individuals exercise independent control over individual warehouse facilities, albeit construction of new storage facilities requires a mandatory approval by the administration of the zone. Local authorities control a special company that operates facilities and owns a considerable proportion of transit warehouses in the FTZ, as well as some other facilities.

In Denmark, a similar zone had emerged in the territory of the port of Copenhagen back in the late-19th century. The capital city also is a huge sea port and has an international airport and an automobile and railroad ferry connecting DK with the Swedish city of Malmö. The area boasts advanced export-oriented industries, and the largest trade companies and banks are headquartered there. Nowadays, the territory of FTZ occupies some 700,000 sq.m., with a diverse and huge net of storage facilities (including, a granary with the capacity of 30,000 t., a. 30 storages, a few dozens of transport depots, among others). The overall storage capacity of these facilities accounts for over 280,000 sq.m. The warehouse stock is expanding, as businesses that are co-participants in the zone construct new facilities on the sites they rent from the FTZ administration. The latter is formed by the administration of the Copenhagen port and administers the zone through a joint-stock company (fully owned by the port administration). Thus, the joint-stock company (and, logically, the port administration) is the owner of all the facilities situated in the zone.

It should be noted that operations of the zone are under the national government's control. Endorsed by a special act, the zone has the right to store, sort and repackage, mark, process and exhibit goods. To establish any industrial facility and organize retail trade in the zone, one needs a special permit from the Ministry for Public Works. Consumption of non-declared goods subject to duties is limited in the zone.

In Austria, there are several free economic zones located, accordingly, in Linz, Graz, Solbad-Halle and Vienna.

The oldest among them is the zone in Linz. Linz is a big city in the northern part of the country, in the Upper Austria *Lande*. It is a river port by Danube, which also has an airport and forms a major transportation hub. Additionally, the city has an advanced, export-oriented industrial complex. The local zone operates huge production facilities, with the total storage area accounting for a. 40,000 sq.m., outdoor storage pads – a. 100,000 sq.m., a refrigerator facility – 5,800 sq.m., an industrial facility of a. 13,000 sq.m., assembly shops – 5,000 sq.m., and there also are some administrative structures there.

The other FTZs are smaller in size. In compliance with the national law, free trade zones may deal not only with trading, storing, marking and exhibiting of goods, but production as well. Of the noted zones three are managed by LLCs, and the fourth one – by a joint-stock company, with local administrations, as well as banks, chambers of commerce and industrial associations being represented in those management structures.

In Greece, there are two free trade zones located in the city of Saloniki and the port of Pyreus, accordingly. They were established in 1925 and 1932, respectively. In Saloniki, the zone is administered by a special autonomous body that constitutes a division of the national Ministry for Merchant Fleet, while the Pyreus zone is managed by the local port administration.

Along with significant benefits granted to FTZs (for example, enterprises established therein upon consent of their administration, the Ministry for Merchant Fleet and the Finance Ministry enjoy the right of free importation of raw materials; there also are certain benefits with regard to transit cargo, etc.), there also exist serious restrictions. More specifically, it is prohibited to import in the zones commodities that fall under the national government's monopoly, such as salt, kerosene, matches, cigarette paper, etc.); importation into the zones of domestic produce requires a special permit; similarly, the processing of goods designated for domestic consumption is impossible without the customs authorities' approval.

In the 1960s, Finland began to vigorously create free trade zones, which consequently emerged in Hanko, Helsinki and Turku. They fall under jurisdiction of a joint-stock company, in which local municipalities are stakeholders. It should be noted that in addition to them, the national government also keeps its watchful eye on the zones, with its agencies controlling storage rates and handling operations therein.

Ireland is a shining example of introduction of FTZs. Back in 1947, the Irish government ruled to establish the first duty free zone in Shannon. The principal mission of the zone became generation of job opportunities and giving a boost to passenger and cargo flows via the local airport. The territory of the zone became subject to duty free import/export regime, with the 10% corporate profit tax rate applicable to any suchlike operations therein. That resulted in a considerable rise in the cargo and passenger flows there, gave a rise to new industrial enterprises and boosted advancement of the western part of the country as a whole. Nowadays, Shannon is a highly developed industrial center represented mostly by high-tech companies, with over 110 foreign firms operating there. They generated over 6,000 new jobs and secured over USD 1 bn-worth exports.

In the mid-1980s, there was established a technopark in the port town of Limerick, within 24 km. from Shannon. Presently it has become home to some 80 companies that deal with development of science-intensive production.

2. Japan

One of the most developed countries worldwide, Japan is keen to establish free economic zones in its territory in order to boost foreign trade and regional development. By contrast to the US and other developed nations, Japan practices the nationwide regional development planning. The public planning includes a general nation's development plan and a great number of region-specific development plans drafted by national ministries. The framework of the plans implies creation of free economic zones.

Japan has paid a particular attention to development of technoparks. This can be attributed to the following reasons: in the 1950s–1970s, the country was vigorously purchasing patents and licenses from overseas. A massive inflow of advanced foreign technologies has enabled the government to create a range of modern production companies and radically restructure numerous sectors of the national economy, save time and considerable funds.

A mass utilization of foreign patents and licenses, however, bore certain negative effects: first, the national economy found itself increasingly dependent on foreign, primarily the US, equipment and technology; second, there started the process of reduction of domestic fundamental research. That is why yet in the late-1960s, along with a mass import of foreign technologies, the government and national monopolies began pursuing the goal of a vigorous advancement of domestic research and development and solidification of the nation's research and engineering capacity.

The policy resulted in the rise of a number of technoparks. By contrast to the US, where such R&D zones were established mostly by private capital, in Japan it was the governmental initiative. The first technopark was built in 1970 in Ibaraki prefecture, in north-east to Tokyo. The town of science Tsukuba was situated on a 28,00 hectares, and its population shortly reached some 200,000. Interestingly, this pioneer project has become the largest one to date.

The Japanese experts tend to believe that underlying the success story of this technopark were:

- a considerable volume of public investment (Y 1,300 bn);
- creation by the government of all the necessary infrastructure;
- self-sacrificing labor (local staff worked 4–6 extra hours a day, without compensation);
- procurement by the national government of advanced equipment to create an adequate industrial base.

Another technopark was created in 1974 in Kyushu, in the south-western part of the country. Its area is 42,000 sq. km., populated by 1,300 mln resident. The zone focuses on electronics, robotics and other science-intensive production spheres. Its distinguishing feature has become a high rise in industrial output, which had been accounting for 30–40% annually between 1977 and the mid-1990s.

Behind this success story lie the following reasons:

- favorable natural and climatic conditions;
- a sufficient supply of qualified workforce;
- a highly developed transportation network, well adjusted to development of the electronic industry;
- presence of an adequate industrial base that formed the basis for the development of the technopark.

The noted science towns have contributed to the progress in the nation's research and engineering potential, which determined its industrial policy. However, the national economy evolved over time. The change was steered by changes in the domestic, as well as the world, economy. New economic priorities emerged, which demanded for changes in the nation's economic development and for new ways and means of their realization.

In the 1980s, the Japanese government launched a wide-scale program aimed at creation of technololises. Underlying such a policy twist was the fact that in the 1970s the country faced dramatic economic upheavals. Specifically, the two oil crises fueled inflation and caused a drastic deceleration of growth in the domestic economy. By the time the country had exhausted reserves for extensive growth by means of attraction of new workforce and renewal of assortment of industrial products. Plus, environmental problems pushed capital construction costs up, salaries and wages were on the rise, and the equipping of new work stations became more expensive. As a result, the economy became keen to save resources and find itself on the path of capital growth.

At the time, the Japanese industrial sector found itself increasingly oriented towards science-intensive sectors, with electronic machine building and manufacture of cutting-edge means of communication coming to the focus of attention. To boost them up, the government launched a series of public programs aimed at the financial and organizational support of R&D works conducted by the biggest firms in the high-tech area.

One of those programs was "Technopolis", which was developed in 1980 by the national Ministry of Foreign Trade and Industry. The program provides for creation in certain economically lagging prefectures of some 20 research and engineering zones, *aka* "technopolises", which meant a city and a contiguous territory, where high-tech enterprises, research institutions, universities that trained researchers and engineers and a housing complex, along with a modern production and social infrastructure could co-exist and operate in full harmony. The government conceived the program as a concept that would allow looking into the 21st century and one of the most efficient strategies of an accelerated advancement of the nation's research and engineering potential, which should form a critical factor of its success in the rivalry on the world market.

The program was supposed to pursue the following objectives: redistribution of the industrial sector from the center to the periphery of the country; its reorientation towards science-intensive and energy-saving technologies; intensification of research throughout the country by regalvanizing local universities' activities; acceleration of the innovation process, etc. The program rested upon the "soft infrastructure", that is, the rise of a network consisting of research centers, data exchange means and cadres training system. One of the principal objectives became encouragement of development of local economies in territories beyond the Pacific polis, that is, to "unload" the overpopulated Tokyo-Osaka megapolis and boost up economic development in new regions.

The technopolises development guidelines set the following criteria of granting a territory with the respective status: it should be situated within 30 min. ride from a “mother” city and one-day ride from Tokyo, Nagoya and Osaka, the local population should be no less than 200,000, with a total area of no more than 500 sq. miles (roughly as big as the Silicon Valley in the US). Plus, such a territory should comprise a harmonious combination of research and industrial complexes, universities, research centers and residential blocs, and developed information infrastructure. In addition, it should be comfortable to live in and display opportunities for cultural life and recreation; it should be situated in a picturesque area and in harmony with local traditions and natural conditions. Finally, all the parties concerned, including business, universities and local authorities, should take part in the process of planning SEZ activities.

The government provided for various credit and tax incentives in the territory of technopolises. More specifically, during the first operational year high-techs firms were allowed to write off 30% of equipment costs and 15% of those of buildings and facilities. In addition, the government funded one-third of research conducted by laboratories under prefectures and small companies.

Local authorities’ role in the process of planning and construction of technopolises was critical. The powers of the national Ministry for Foreign Trade and Industry were limited by setting main criteria of creation of technololises, provision of technical support, tax benefits, and loans disbursed by the Japan Development Bank. The future success of the creation and functioning of technopolises as the basis of the long-term strategy aimed at ensuring the country’s leading position in the 21st century should have rested on the nation’s natural immanent characteristic, that is patience and ability to withstand hardships.

Presently there are 19 technopolises in the country. Most of them focus on electronics, development of new materials and ceramics, and robotics, while some other deal with research and production in the area of medical electronics, biotechnology, and optical fiber.

Focused on science-intensive produce, technopolises have helped boost competitiveness of the nation’s exports and a more intense involvement of the country in the international labor division. In parallel with that, the government has also completed liberalization of foreign trade and lifted barriers to capital and labor movement. However, overseas, the traditional practice of long-standing relations in the business world and partnership between the government and the national business community were perceived as signs of protectionism and preservation of the closeness of the Japanese economy. In the 1980s, a huge positive balance of trade with the US and Europe fueled serious conflicts and formed one of the key intergovernmental economic challenges for Japan.

In a move to optimize the foreign trade balance and re-orient the industrial sector towards the domestic market, in the 1990s, the Japanese government initiated measures on encouragement of import, including, in particular, creation of special foreign trade zones. They were created in compliance with the 1991government concept for formation and development of free import zones. The legal base for this initiative became the *Act on forex transactions and foreign trade* and the *Act on emergency measures on assisting imports and attracting direct foreign investment in Japan.* The national Parliament passed these bills in July 1992 (with a consequent extension of their effect for another ten years, as approved in 1996). In compliance with the new acts, the national sea ports and airports became home to foreign trade zones, *aka* "Free import zones". These zones constitute a combination of free trade and import-substitution production zones. They deal with storing, processing, exhibiting and sales of goods and corporations that reside therein enjoy a special preferential economic and foreign trade regime.

The zones are funded both from the local budgets and by private companies. In addition, the national Central Bank disburses loans to finance development of their infrastructure. The primary focus of the zones is the domestic market.

By early 2004 there were 23 free import zones in the country (of which 5 were established in 1992, 10 – in 1993 and another 8 – in 1994). They are situated in cities or prefectures and fall under the respective jurisdictions. A model example of this type of zones is "Sakaiminato" located in Tottori prefecture. Its distinguishing feature is that the design of its development was worked out in cooperation with local experts, and local authorities control and manage the zone. The design provides for the following measures:

1) transformation of the Sakai port into the Western Japan's gateway for friendship and international cooperation;

2) development of the local industrial sector by boosting the efficiency of import and the information sphere;
3) intensification of international connections by means of trade and industry.

To facilitate operations by businesses that service import cargo, the noted government concept provided for a series of benefits, including:

- disbursement by the Japan Development Bank and the Foundation for Support of Small- and Medium-Sized Businesses of low-interest loans;
- differentiated taxation of incomes from real estate and profit of businesses operating in the locations where import cargo is stored;
- beneficial payment for shipment and supply of equipment for wholesale and retail trade and transportation companies;
- exemption of processing, wholesale trade and transportation companies from land tax;
- provision to entrepreneurs of debt warrants from the Foundation for Formation of Production Base;
- beneficial insurance of SMEs;
- free supply by the Japanese Foreign Trade Development Association of information and provision of consultations with respect to import-related issues and holding fairs and exhibitions.

Another success story is the free import zone “Hokkaido” established by New Chitose airport in the southern part of Hokkaido island. The zone is closely associated with “Chitose Rinku” industrial complex, which is located in 5 km. from it. The area of the complex is 214 hectare, and it became home to 82 corporations and a research park. The national government has contributed greatly to the establishment and development of the zone. Specifically, it secured aircraft to deliver import goods, construction of “turn-key” ready for lease office facilities, supply of Internet-connected PCs, provision of assistance to conduct of feasibility studies for construction of import cargo transportation and processing facilities. Thanks to its favorable location, a good organization and the governmental support, the zone has grown into the most vigorously developing regional trade and distribution center.

In Japan, there also exists such a peculiar kind of free trade zones as bonded zones (customs warehouses to store duty-free goods) of five categories:

1) the bonded zones that fall under the Finance Ministry's jurisdiction: within such zones located by ports of importation foreign cargo (including that designated for export, import or transit) may be unloaded, transported and stored for a month. These territories are used for a fixed fee by any economic agent participating in foreign trade for the period of completing a customs declaration and other paperwork;
2) bonded hangars controlled by the head of the local customs office and designated for the same purposes as above;
3) customs warehouses, where foreign cargo can be stored for up to 2 years (and even longer, providing a special permit). While in the warehouse, the cargo is exempt from customs duties;
4) in-bond enterprises that are allowed to manufacture goods from foreign materials without paying customs duties for those;
5) in-bond exhibition zones: these are territories specially designated for holding international exhibitions. They fall under the local customs agency head's competence. The system was designed to simplify coordination of conduct of international exhibitions and shows by foreign states. Foreign cargo can be used or displayed there upon filling out the customs declaration, according to simplified procedures.

Thus, free economic zones have spread throughout the country and formed an efficient vehicle of regional development. But their rise and development is country-specific, which in the case of Japan suggests a pro-active contribution of the government to their emergence and advancement, which particularly concerns R&D zones.

3. SEZ in China

Today, there are 4 special economic zones in China (such as Shenzhen, Zhuhai, Shanton), 14 open maritime cities in the coastal province Hebei, in Guangxi Zhuang autonomous region, the economic triangle in the south of the maritime province of Fujian, as well as in Yangtze delta and the Pearl River delta, and in Shandong peninsula and Liaodong peninsula. Plus, there are 14 duty-free trade zones, including

Tianjin, Dalian, Fujian, Gungzhou, Haikou, Qingdao, Fuzhou, Shanton and Zhuhai ports, among others; duty-free zones formed by 13 open border cities, such as Huichun (Jilin province), two cities in Heilongjiang province, as well as in Manchuria and the Inner Mongolia, Tacheng and Bole in Xinjiang Uyghur autonomous region, Xichou and two other cities in Yunnan, and two cities in Guanxi Zhuang autonomous region, to name a few; 53 high- and new-technology zones, over 70 R&D zones for the trained overseas Chinese; 38 export-oriented processing zones; and created in 1998 free economic zone Hainan, and the Pudong New Zone, which is located across the river from the old part of Shanghai.

The launch of economic reforms and transition towards the "open doors" policy have enabled the southern provinces of Guandong and Fujian to pursue an independent economic policy by creating in 1980 special economic zones that later formed an integral element of the Chinese economy.

An important step in this respect became creation of special economic regions (SER). Typically, within 30-sq.km. precincts there exists a specific economic policy and a special system of economic administration, similar to that of the European free ports. Specifically, oriented towards external markets and providing for tax and customs benefits, simplified registration and other administrative procedures and softer regulation of businesses, SERs mostly rely on export-oriented processing industries and consolidate R&D, production and trade into a single complex. The status of the Chinese SERs appears distinct from those of export-oriented processing zones elsewhere and from the status of the Hong Kong special administrative region. The SERs' mission is to attract foreign investment, ensure importation of advanced high- and new technologies, borrowing foreign partners' management practices, creating additional jobs for China's citizens, enhance the quality of their cadres and the general level of economic activity on the whole.

Chinese researchers single out three stages of emergence of local SERs. During the first one (5–7 years) there emerges production, engineering, transport, social and other infrastructure, and the zone attracts foreign capital, equipment and technologies, while its administration acquires management skills and establishes foreign trade connections. The second stage of equal length was associated with the transition from a significant specific weight of trade and the services sector in the economic structure towards prevalence of industrial and foreign trade activities; along with that there occurs the rise in application of advanced technologies in traditional industries and their modernization. While implementing this stage, the goal is to have 50–60% of investment made at the expense of foreign capital, while the proportion of exported goods should reach up to 70%. The third stage leads to maturity of the zone, with reconstruction of traditional production facilities and a considerable proportion of science-intensive and high-tech industries there. Thus, over 20 years of the Chinese economic reforms the country saw the rise of a relatively perfect SEZ regime, which appears favorable to foreign investment.

The specificity of emergence of SEZs in China is exemplified by special economic zone Shenzhen. It was inaugurated in August 1980, upon enactment of the Act "Regulation of special economic zone in Guandong province". After 20 years of economic growth the zone has found itself ahead of even such largest economic centers as Bejing, Tianjin, Shanghai, Fujian, and Guandong. Embracing 327.5 sq. km., encircling Hong Kong and separating it from the mainland China, this zone displays the fastest growth rates: thus, between 1980–2001 the average annual growth rate of its GRP exceeded 29.5%, that of industrial output – 45% and foreign trade – 39%, while the annual growth in real foreign investment was at the level of 28%. That is why the city was the national champion in terms of the volume of foreign trade, second – by its industrial output and third – by annual revenues to the local budget and attraction of foreign investment. The city is dominated by the so-called secondary and tertiary industrial production: more specifically, the primary to the secondary to the tertiary sectors ratio was 0.9:52.6:46.5, while the respective ratio of foreign investment in these sectors was 0.2:63.3:36.5.

Nowadays, the Chinese SEZs are characterized by the following distinguishing feature, that is, the zones of new and high technologies, or analogues to the US technoparks, whose proportion in the nation's GDP and the aggregate value of export and import accounts for 4% and 10%, respectively, appear strategically significant for the modern economic policy. Their transformation into the locomotive for the sector for new and high technologies against the backdrop of the ongoing optimization of China's economic structure is evidenced by the fact that, starting from 1991, their key economic indicators have been displaying an average annual growth of 40%. In 2003, they continued their rapid advancement and for the first time ever generated over YUAN 2 trn in incomes, or at 32% more than in 2002. It is worth mentioning that proceeds from sales of produce of the high-tech enterprises located in the Bejing R&D zone and in the Shanghai R&D zone for new and high technologies together exceeded YUAN 150 bn.

Thus, the Chinese model of territorial and economic openness on the basis of various kinds of SEZs appears fairly realistic and allows a relatively painless transition towards market and the country's gradual integration into the system of international labor division and foreign trade.

4. SEZ in Hungary

Hungary presently has several types of special economic zones: industrial parks, entrepreneurship zones, free customs territories of trading (storage) and industrial types. There also exists such a specific form of doing business in the country as offshore corporations for non-residents.

Industrial parks display a particularly successful performance. There were 112 of them in 2001, of which only 95 were actually functioning at the time. According to the national Ministry of Economy, the number of employees there is a. 110,00, the number of enterprises operating therein is a. 1,000. The enterprises' annual output is estimated at the level of 1,600 bn Forint (a. USD 6 bn), with exports accounting for a. 80% of their output. The overall volume of investment in development of the industrial parks exceeded USD 1.5 bn and they boast a productivity rate twice as high as throughout the country.

The industrial parks enjoy a number of tax and customs benefits, which are provided to the domestic and foreign investors alike:

- exemption from local taxes for the term of 10 years;
- exemption of imported production equipment (at 50–100%);
- exemption from corporate profit tax, providing profit is reinvested in production expansion and creation of job opportunities;
- reduced or postponed payments for public utility services .

Thanks to creation of industrial parks, Hungary has undergone the process of an accelerated advancement of its southern and eastern regions and their catching up with the average nationwide level. Presently these areas have become home to one-third of the currently existing industrial parks.

The industrial parks established on the basis of national research centers play a significant part in the rise of the national economy. This equally creates favorable prospects for the rise of university cities and towns (Budapest, Eger, Debrezen, etc.).

Securing as much as 18% of the nation's industrial output, industrial parks are turning into the locomotive of the national economy. As concerns their future, they can further emerge as one of important forms of development of the subcontractors network for western companies. Plus, with the completion of the privatization process in Hungary they may also turn into targeted objects for foreign capital and attract up to USD 4 bn in foreign investment.

To stimulate economically lagging areas with a high unemployment rate, the national government established entrepreneurship zones, pioneered by Zakhon. To extrapolate its experiences onto the other ten zones, the government made it a testing area and pays a particular attention to its development. To encourage capital investment in the zones, the national law provides for considerable investment and regional benefits. As well, investors can take part in various tenders to obtain support from public and social development foundations.

The country also uses such a form of SEZ as free customs trade (storage) territories. However, because of a number of reasons, particularly, external pressures, their number is on the decline: while there had been a. 90 of them in 1995, only 10 have survived by 2002. These territories, from where goods are exported overseas without any additional processing, are located mostly by river ports and airports.

Such a form of attraction of foreign capital as free customs industrial territories has proved to be a success in Hungary. This status, providing compliance with a number of simple customs regulations (fenced and guarded industrial territory of a fixed size, with a customs checkpoint), can be granted to practically any foreign enterprise or even its department. There were 136 such zones by late-2002, home to 103 enterprises, the bulk of which was formed by suppliers to transnational companies.

The volumes of output of these companies have recently posted roughly a 50% annual growth. The period of economic growth in the country, which has been in place since 1997, was mostly driven by a rapid production expansion at the very customs territories, wherein there operate such renown multinationals as Sony, Nokia, Phillips, TDK, GM, Ford, to name a few. The attractiveness of such zones in the eyes of foreign investors is explained by the fact that their importation of equipment is exempt from customs duties and VAT, while raw materials, units and details used in the production process are equally exempt from customs duties, VAT, consumer tax and environmental tax.

Today, the free customs territories ensure a 25% share of the nation's gross industrial output and nearly 70% of its industrial export. The enterprises located in such territories have recently played a critical part in shaping the nation's foreign trade: to cite a particular example, between 2000 and 2001 their share in the nation's aggregate volume of export exceeded 43% and in import – 30%, with their balance of foreign trade being constantly positive. As much as nearly 90% of their export and sof imports falls on the EU.

Industrial enterprises established in such territories (mostly brand-new, turn-key ones) have introduced a high technological culture to the country. In parallel with that, there also rose the use of the domestic contractual works and services, as well as raw materials and intermediate products. This success rests upon the possibility to export these goods from the noted territories to other domestic enterprises for the sake of their processing, and this can be done without any special permit. As a result, the proportion of the domestic labor and materials in the overall cost of a produce manufactured by enterprises within a free customs industrial zone now reaches 1/3.

Hungary also practices such a form of cooperation as offshore business, which sometimes is wrongly attributed to the category of free economic zones, Below we provide fundamental distinctions between these two forms of organization of business.

Since 1994 foreign investors have enjoyed the right to establish offshore companies in the territory of the Hungarian Republic. To be granted the status, one should simultaneously meet the following requirements:

- founders of such companies may become only foreign citizens – there may not be any domestic residents (citizens of Hungary or permanent residents) among direct or indirect owners of such companies; neither the company, nor its owners may have any interest in other economic companies within the country, nor the company may have any representative offices in Hungary;
- the company may be found only in two forms: limited liability company or joint stock company. The founders should apply to the national Finance Ministry for a license that grants benefits for which companies registered in a free customs territory are eligible;
- the company's operations should be focused on trade outside Hungary, exclusively between third countries, and provision of services to foreign customers (exclusive of the financial sector);
- to conduct official business inside the country the company should hire a lawyer, who must be a "domestic entity"; most of the company's management, Board and staff should also be "domestic private individuals"; only an auditor company registered in Hungary may conduct auditing of the company;
- the bank account necessary for the company's functioning can be run in Hungary.

The aforementioned conditions show that this case concerns an administrative center of the company, from where, bypassing Hungary' territory, it exercises control over trade between third countries. Among its services there may be consultancy to foreign clients, marketing research, etc. Thanks to the requirement to run its banking account in Hungary, the local banks service trade operations of offshore companies.

The latter have recently been on the rise: while there were 188 of them in 1997, their number grew up to 247 in 1998, 309 – in 1999, 418 – in 2000, 443 – in 2001, and 475 in 2002. Up to 1997 such companies had enjoyed the 85% benefit with respect to corporate profit tax and the additional tax (on dividends). Thus they ultimately *de-facto* paid corporate profit tax at a meager rate of only 2.7% and tax on dividends at a 3.45% rate.

5. The Portuguese SEZs

Since 1980 Portugal has had free economic zones in Madeira and the Azores.

From the perspective of legal status, one might as well reckon with them the territory of Macau (in the southern China, the area of 16 sq. km.), which was under the Portuguese jurisdiction until 1999.

Portugal has concluded agreements on avoidance of double taxation with Austria, Italy, Belgium, Mozambique, Brazil, Norway, Bulgaria, Spain, Finland, Switzerland, France, UK, Germany, the US, and Ireland.

Let us consider the Portuguese SEZs in greater detail:

SEZ “Santa Maria” is situated on the island with the same name. In its territory, it is allowed to conduct all kinds of industrial, commercial and financial operations. The territory of the SEZ occupies nearly 40 hectare and has a deep-sea port and an international-class airport.

The legal base of operations conducted by enterprises registered in the zone implies a number of benefits, including:

- simplification of all customs formalities; free export and import of goods;
- exemption of re-exported goods (processed an unprocessed alike) from customs duties;
- temporary discharge of the property right for imported from the EU consumer goods from the moment of their importation to and until the moment of their exportation from the SEZ;
- exemption of joint-stock companies’ incomes from duties;
- exemption of enterprises within the SEZ from duties;
- exemption from duties of incomes resulting from transfer of patents, logos, production processes, etc.;
- free movement of foreign corporations’ capital;
- subsidies for vocational training (up to 100% for citizens of the Azores);
- rental subsidies (up to 50% of the respective costs for the term of 5 years);
- construction subsidies (up to 50% of the respective costs in the event of construction of production facilities);
- subsidies for equipment purchases (up to 50% of costs for industrial enterprise).

In addition to regular kinds of entrepreneurial, commercial and financial activities, up to recently offshore companies had been allowed to conduct financial operations in the SEZ. Being daughter companies of national and foreign financial corporations, they could carry out transactions with non-residents of Portugal. At the time, they were eligible for substantial benefits in the SEZ, including untaxed profits and no control over exchange transactions.

Registered and operating in the SEZ, corporations can expand their operations throughout the Azores, providing they are profitable and meet the following conditions: they operate in a priority sector of the local economy; they focus on external markets; they are not rivals to any other local corporations that do not enjoy the same benefits. The informational provision of enterprises keen to realize projects and operating in the SEZ is conducted through ZOFRAM (the Santa Maria SEZ Development Company).

Free economic zone in Madeira. The legal regulation of operations of this particular zone likewise implies a series of benefits:

- exemption of joint-stock companies' incomes from duties;
- exemption from duties of an increase in their authorized capital;
- exemption from duties of transfer of a part of an authorized capital, quotas, licenses and other property owned by residing in the SEZ corporations;
- subsidies for vocational training (up to 50% of the respective costs);
- subsidies (up to 50% of the respective costs) for introduction of energy-saving production processes.

This SEZ, likewise, until recently had been home to offshore companies.

Any company keen to reside in Madeira is granted an access to the European markets, thus making the archipelago, for non-EU corporations, an ideal gateway to the EU. It is particularly thanks to Madeira's rise as an international business center that some international auditor companies increasingly frequently open their representative offices there.

The performance of the Portuguese SEZ can be depicted using the following data: the number of officially registered in the zones companies that operate therein in 2002 accounted for 834 vs. 544 ones in 2000. Of the said number, most companies (nearly 70%) are involved in banking, insurance and other kinds of financial operations (while industrial production usually proves to be loss-making in the Portuguese free economic zones). In 2002 alone, the companies in question earned a. USD 87 bn, or nearly a half of the nation's GDP, while the respective tax revenues to the national budget accounted for some USD 10 bn.

In late-2003, the national parliament passed new acts that kept a low or zero tax status for the companies that operate in the free trade zones. Presently, the corporate profit tax rates will vary from 0 to 3%, depending on the date of registration of a given company, while the tax on financial transactions will rest upon the same condition and vary between 7.5 and 12.5%. All the respective licenses are due to expire in 2011, subject to further revision beyond the deadline.

But the above impressive advancement has found itself under the sword of Damocles - at their meeting in Brussels on January 21, 2003, the Finance Ministers of the EU countries signed an agreement which imposed an effective ban on offshore companies' (the so-called "tax harbors") operations in the territory of EU and some other European countries.

The Portuguese economic community now holds heated debates regarding the effect the two novelties should have both on the number of companies currently operating in the zones and the tax revenues, however, the questions have remained unanswered as yet.

6. SEZs in Turkey

Free zones in Turkey were created and still function on the basis of Act on Free Zones No. 3218 promulgated yet in 1985 and effective as of 1987. At the time, there emerged two pioneer special economic zones in the country: in Mercina and Antalya. In 1999, they were joined by the Aegean free economic zone in Izmir and a free entrepreneurship zone in Istanbul, which located in the precincts of the Ataturk International Airport.

The number of the zones has been steadily on the rise from year to year, with a general purpose to fuel development in still lagging areas. As of today, there are 21 zones in the country.

The Turkish zones are encouraged to take a maximum advantage of the country's geographic position, its proximity both to the Middle-East and Eastern and Western European markets. Given that, a special attention is paid to intensification of export-oriented investment and production by attracting foreign capital and technology, securing the zones' regular and consistent contribution to development of the national economy, a more intense use of external financial sources and capitalization on international trade opportunities.

National acts No. 5084 and 25365 of Feb. 6, 2004, contained amendments to Act No. 3218 with regard to tax incentives. As they came in force, all those who had been granted licenses prior to the promulgation of Act No. 5084 were exempt from all kinds of taxes and duties up to 2009. As concerns those who obtained such licenses after the noted date, they still retain this right until the end of the year in which Turkey becomes the EU member.

In the national economic zones it is allowed to carry out business activities of any kind, including storing, production, packaging, banking. The zones boast necessary infrastructure, office, production and warehouse facilities, which can be rented at privileged rates. In addition, there exists a regime favorable to entrepreneurship:

- free economic zones form completely duty-free, including corporate profit tax and income tax, enclaves;
- entrepreneurs that operate therein are also exempt from various duties and levies;
- by contrast to most countries, it is allowed to sell on the domestic market goods produced in the SEZs or imported via them, and such operations are subject to ordinary foreign trade regulation;
- in the SEZs, it is allowed to use any hard currency;
- there are no restrictions, taxes, duties and prior conditions with regard to transfers by investors of their personal or corporate profits;
- foreign citizens with the Turkish residence permit can own companies with 100% foreign capital registered in the SEZs;
- it is allowed to employ foreign specialists and management;
- the Act on free economic zones and Act No. 2822 of May 5, 1983, put an arrest on strikes and lockouts for the term of 10 years from the moment the firm starts its operations in the SEZ;
- the quality of infrastructure created in the SEZs matches international requirements;
- land lease rates are quite moderate;

- the cost of workforce is very low vis-à-vis other countries of the same level of development (sometimes, it makes up as much as 10% of that in developed countries);
- red-tape formalities have been reduced to minimum both with regard to the stage of capital investment and that of production and sale of output;
- the law on pricing and quality of goods and services, and control over them, which is effective elsewhere in the country, has no legal effect in the SEZs.

In addition, investors can capitalize on other benefits provided by the government policy, which is oriented towards encouragement of private investment.

A critical advantage of the Turkish free zones appears their proximity to ports and other international hubs. These conditions, that normally boost entrepreneurship in free economic zones, generate a favorable investment climate and secure considerable advantages for investors in the SEZ by reducing production costs and giving a boost to competitiveness of domestic and foreign companies that operate in their precincts.

In a move to establish conditions for businesses in the free economic zones, complete infrastructural objects and other facilities in the territories allocated for the SEZs, the government has created a special SEZ Organization and Development Fund under the aegis of the national Central Bank. Its resources come from license fees for the right to conduct business operations in a zone; the 0.5% rate of a tax on the costs of all the goods that cross the SEZ borders, and special payments stipulated in contracts concluded by private individuals or corporations that operate in the SEZs.

Each zone to some extent maintains its genuine profile, depending on its location and area of focus. Thus, free economic zones in Mersina and Antalya, which are situated in fertile agricultural territories, focus primarily on creation of agricultural processing enterprises and servicing the local agrarian sector, as well as export of agrarian produce. In Izmir, the local SEZ centers on electronics and telecom equipment, while the Ataturk airport entrepreneurship zone in Istanbul is famous for production and sales of prêt-à-porter clothing and high-end electronics; Adany SEZ focuses on heavy industry.

The regulation of free economic zones' operations falls under the competence of a specially created Head Department for SEZs in the structure of the Secretariat for Foreign Trade under the Head of Staff of the Prime Minister. The same agency grants licenses on commercial operations in the SEZs.

The currently existing 21 zones have become home to 3,401 corporations, including 652 foreign ones. In 2003, the volume of export and import operations via the zones grew at 49.6% and reached USD 16,608.66 mln, or equivalent to 14% of the nation's foreign trade turnover. Practically all the zones reported growth in this regard, with the trade turnover in 6 of them being over USD 1 bn.

As concerns foreign trade partners, the most intense trading was with the EU, whose proportion in the overall volume of the nation's import/export operations conducted in the free zones in 2003 accounted for 30.3%; the EU was followed by OECD countries, except for those holding membership in the EU, – 5.2%, the CIS countries – 3%, other states – 16%, while the proportion of the rest of Turkey was 45.5%.

As for the assortment, the processing sector contributed with 94.4% of the overall turnover of the free zones, while agricultural output accounted for 5.4%, and the mining sector reported a meager 0.2% of that.

7. SEZs in the Philippines

The Philippines constitutes a shining example of a successful use of free zones for the sake of attraction of investment and promotion of socio-economic development. The national Congress passed numerous acts on establishment of various special zones, subject to jurisdiction of the national Economic Zone Administration.

Back in 1923, it was the national Chamber of Commerce that had put forward the concept of creation of a free trade zone in the country. In 1937, a special committee under the President of the country recommended to establish a free port or a free trade zone. However, another 30 years had passed before the respective bill was submitted to the Congress. Finally, in 1969 the latter passed an act on establishment a free port in Marivelez (Bataan Island). The act provided for a creation of a free trade zone there, as well as organization of its administration, whose mission would be planning, developing and managing the zone.

Because of budget constraints, the project was suspended for a while, and the zone started its full-scale operations only in Nov. 1972. Interestingly, the government participated in the zone with Peso 200 mln as a star-up capital. A special presidential decree granted to the Administration of the zone an exclusive jurisdiction and police power within its precincts.

In the late-1979, the government authorized the Administration to allocate sites for special export zones, to be developed by the private sector, with enterprises located therein enjoying the same benefits as those in public zones. However, the first three private export zones were established only in 1991. Later, the number of such zones grew notably.

These particular zones operate as separate enclaves with various industries there. The latter consume import raw materials and intermediate products to process, assembly and manufacture export goods. Special companies deliver public utility, canalization, trash and waste disposal, communication, transportation services, and supply water and electricity. There also are housing blocs, commercial facilities and roads in the zones. The zones are constantly developed and improved for the sake of attraction of as much investment as possible.

The national government formulates its obligations towards private export zones as follows; “We must vigorously encourage, stimulate and accelerate a reasonable and balanced industrial and socio-economic advancement of the country for the purpose of providing our people with jobs, especially in the rural areas, increase the productivity of their labor and their personal incomes, thus improving the population’s living standards, particularly by means of establishment of special economic zones in strategic territories of the country suitable for that”.

As an institution that implements the government policy, SEZ administrations are in direct contact both with the private sector and foreign investors. The holder of a general SEZ control and management mandate, they also exercise marketing functions on behalf of the government, thus promoting attractiveness of the zones to investors. The efficiency of the zones’ performance is measured using such criteria as employment, investments, and export.

In compliance with the effective law, special zones are “selected territories with a great capacity in terms of their transformation into agrarian, industrial, tourist, trading, banking, investment and financial centers".

There exist the following kinds of special zones:

Industrial zone: an area subdivided into and developed according to a comprehensive plan and under a single permanent control, with pre-established conditions for principal infrastructure and already erected standard factory and communal facilities;

Export-processing zone: a specialized industrial zone, which is physically and/or administratively located outside the customs territory and oriented mostly to export production;

Free trade zone: an isolated secured area contiguous to the port of importation, wherein imported goods can be handled for an upright re-shipment to other countries or placed for storing, sorting, etc., without paying customs duties;

Tourist center: an area with hotels, resorts, etc. that deliver various recreational services to local and foreign tourists, travelers, and investors;

Agro-industrial zone: a specialized industrial zone focused on a complete cycle of agricultural production, from the primary stage and up to the processing of final produce.

Special zones appear very compact, and, as a rule, their area totals a. 25 hectare (except for Kavite and Laguna zones, whose areas accounts for 50 hectare each). Zones can be established as a result of a private initiative or that of local administrations endorsed by the central government and by the initiative of the latter.

In 1999, there were 106 special zones in the country, of which 100 (4 public and 96 privately owned) ones were managed by the SEZ administration. Zones are at different stages of maturity, with 39 functioning ones, as of 1999. The number of enterprises operating in the zones grows steadily, and in 1997 it reached 784 vis-à-vis 77 registered in 1988. Interestingly, the number of enterprises registered in public zones is considerably greater than in the later created private ones.

Enterprises located within the zones are eligible for the following tax benefits: accelerated depreciation, exemption from export duties, license fees, duties on imported equipment and raw materials, as well as the national and local taxes, all substituted with the 5% tax on their gross income.

The zones in the Philippines have been in existence for over 20 years and still remain a strategic vehicle of economic development. Between 1988 and 1997 the aggregate volume of investment in the zones accounted for a. USD 7 bn. The average annual growth rate in investment was 160%.

The aggregate number of jobs created within the public zones between 1995 and 1997 accounted for 1.4 mln. It should be particularly noted that 5 new jobs in a zone give a rise to another 8 new ones outside it. Between 1995 and 1997 the average annual growth rate in employment accounted for 35%, while the aggregate volume of salaries and wages of the staff employed in the public zones made up a. USD .1 bn. As a result of the multiplicative effect the staff's incomes spent on food, clothing, housing, etc. in turn generate employment and incomes in the respective sectors which satisfy needs of those who work in the zones.

8. SEZ in Egypt

Main fundamentals of the functioning of the Egyptian SEZs were stipulated in Act No. 43 of 1974 "On the Arab and foreign investment and free zones", further specified in "Act on investment" No. 230 of 1989 and 'Act on encouragement of investments and investment guarantees" No. 8 of May 11, 1997.

The pioneer 90-hectar SEZ was established in early 1976 in the precincts of the city of Port Said, close to the port that forms the northern gateway between the Suez Channel and the Mediterranean sea. A special customs regime was introduced in the city and turned it into one of the biggest commercial centers in Egypt. Established in the SEZ enterprises and warehouse facilities were designated for storing various export and import products, as well as production of a range of consumer goods.

New SEZs consequently arose in 1976–77 in Alexandria, Naser City (Cairo), and Suez. The Alexandria zone occupies 630 hectare in the outskirts of the city, within 20 km. from the port. The zone comprises huge warehouse facilities and outdoor lots to store timber, cars and other products, with their consequent shipment to the domestic market or re-export to other countries. The zone provides temporary storage and pre-sale servicing, processing and packaging of domestic goods, mostly clothing, as well as footwear, deep-frozen vegetables, etc.

The SEZ in the city of Suez, which forms the southern gateway to the Read Sea, have a strategic location, thanks to proximity to the markets of a number of African and Asian countries. The area became home to enterprises of the basic industries, including oil-refining, mining, cement, and the sector for mineral fertilizers. The zone consists of two lots: Port Tauficka, home to maritime logistics companies, industrial and warehouse facilities, and Adabya were necessary infrastructure is under construction. The SEZ in Naser City is situated by the Cairo airport. It is characterized by a well developed system of transport communications and the presence of qualified workforce. Its enterprises export pharmaceutical, textile, food, chemical and other consumer goods. As well, SEZs were created in Ismailyia, in the middle of the Suez channel and in the city of Damietta, west to Alexandria, where a modern port was built. Damietta is a large center of the wood-working, furniture and leather production. Presently yet another zone is under construction in the city of Safaga.

Under the Egyptian law, certain companies are allowed to operate under the free zone regime, regardless of their location. To this effect they are bound to obtain a special permit (license), which is granted only for a certain project or kind of operations. They are called “private free zones”.

Along with the aforementioned kinds of zones, there also are special industrial development territories and residential areas, which are divided into the new settlements and the new industrial zones.

The new settlements are situated in previously untouched desert areas. The largest of them are satellite towns by Cairo: the ones named after 10th of Ramadan, 6th of October, Sadat City, and El-Arab. They fall under jurisdiction of the Ministry for the New Settlements. To encourage investment, investors are offered lots with infrastructure and tax exemption for 10 years.

The new industrial zones are located by settlements from where the local workforce can commute to them. The zones are managed by special committees for investment permits led by governors. As a rule, enterprises situated in the new settlements and the new industrial zones enjoy the SEZ regime. They are protected from nationalization and confiscation of property, and administrative agencies have no right to intervene in pricing or to cap their profits. Their licenses can be canceled only by the Prime Minister's decree upon a submission of the administrative bodies, however, in that case an investor can appeal to the administrative court within 30 days upon the date of issuance of a notification of such a decision.

A company has the right to import, on its own or via a third party, necessary for its operations materials, equipment, vehicles (except for passenger cars) without obtaining a special import license or registration in the import register, nor it has to pay any import customs duties. Companies that operate in the SEZs are exempt from the tax on profit from commercial and industrial operations or the profit tax on joint-stock companies for the term of 5 years, starting from the first fiscal year or since the start of production operations, accordingly. Companies that operate in the new industrial zones and the new settlements are exempt from taxes for the term of 10 years. In the event a company is situated and operate under the free zone regime beyond the territory of the Nile vale, the tax exemption period is extended up to 20 years, as per Act No. 8 on guarantees of investment of May 11, 1979.

As of mid-1998, in compliance with the said Act, the Egyptian zones became home to 2,170 enterprises with the overall volume of investment in them of 65.8 bn. Egyptian Pounds, including 472 enterprises with the investment volume of E.P. 22.9 bn operating in 6 SEZs located in Cairo, Alexandria, Port Said, Suez, Ismailiya and Damyette. Of 1,700 enterprises located outside the SEZs 809 ones were industrial enterprises, 309 – financial, 155 – construction, 141 tourist, 182 – provided other services and another 102 were agrarian. In the public SEZs, 60% of investment falls on domestic corporations, 19 % on investors from other Arab countries and 21% on foreign capital. In 2001, Egyptian export soared up to USD 600 mln vs. 550 mln reported in 2000.

9. SEZs in India

On tax regime for Soft Technology parks

The country-specific entities, STPs fall under jurisdiction of an autonomous division of the national Ministry of Communication and Information Technology, known as the Software Technology Parks in India. The agency was created in 1991 to give a boost to software export.

The principal mission of STPs is to render a complex of services to ensure access to data bases, telecom means, computerized networks and Internet, and consulting services.

The development pattern of STPs has proved to be a success, and currently corporations that use it secure 90% of domestically designed software exports, which in 2004/05 fiscal year stood for USD 15.5 bn.

STPs constitute 100% export-oriented structures, which deal with R&D and sales of software. Such entities have become popular worldwide and integrated concepts of 100% export-oriented units (EOU), export production zones (EPZ), and technology parks.

The national government introduced benefits for enterprises that operate in the STP framework. The benefits are enumerated in the national economic law – specifically, the Foreign Trade Policy 2004–09 (FTP); Income Tax Act (Sections 10A and 10B) and the Customs Act (Section 65). A corporation may become eligible for the benefits and privileges only if approved by a specially authorized staff member of the Department of Information Technology (DIT) under the national Ministry of Communication and Information Technology.

In compliance with FTP, companies located in the territory of a STP, can import duty free all kinds of goods, including raw materials, components and capital assets needed for software production, services delivery in this area, sales or other operations associated with this area, if they are not prohibited by the law. The enterprises enjoy the right for a duty-free importation of goods for all kinds of allowed operations, and such enterprises are not subject to the local trade regime of the state wherein they are located.

Products allowed for duty-free importation:

1. Capital assets (as defined by FTP) and spare parts to them:

- power supply units; auxiliary power plants; transformers;
- environmental control equipment;
- quality control equipment;
- auxiliary hoist equipment;
- sources of continuity of service; equipment posts, storages, module furniture, PC posts; antistatic carpets, teleconference equipment, server control systems, air-conditioners and electric panels;
- safety systems;
- facilities refurbishment tools and means.

2. Raw materials, intermediate products, spare parts and packing materials.

3. Prototypes and samples for produce design and modernization.

4. General designs, detailed designs, microfilms, and data bases.

5. Office equipment, including automated telephone systems, fax machines, video-projecting systems.

6. Spare parts and stationery for the aforementioned equipment.

The benefits apply to new and second-hand goods alike. The corporation first has to apply to DIT for a special permit for importation of capital assets. Should customs authorities have any doubts as to whether a given device is designated to principal or auxiliary operations, the decision is to be made by an authorized staff member of DIT.

With the exception of capital assets and spare parts, goods should be used within 2 years. The deadline can be extended, if approved by an authorized staff member of DIT.

Like SEZs, STPs can be public and private. Presently there are 44 public and 25 privately owned technology parks, and the latter partly fully belong to foreigners.

The city of Bangalor is the heart of the national IT-industry. It is home to some 1,500 IT-companies (there were just 15 of them back in 1991) and 130 biotechnological companies. In 2004 alone, 198 IT-companies and 18 biotechnological ones opened their representative offices there. The IT sector in Bangalor boasts an army of a. 750,000 specialists. In 2005–06 financial year export of IT products from the area reached USD 5.1 bn., while in 2005–06 it may further grow up to USD 6.1 bn. The geography of location of IT companies is spreading, thanks to their rapid rise in such cities as Mangalor, Maysur, Hubli, Belgium, Gurgaon, and Hoyda.

10. SEZs in Iran

Free economic zones in Iran are administered by the High Council on SEZs, which operates on the basis of the Act on Trade and Industrial Zones passed on August 29, 1993. Today, all the Iranian free zones are divided into free economic zones (FEZ) and special economic zones (SEZ). There presently are 8 operating zones in the country: 4 SEZs: Qeshm, Qish, Sirjan and Chabahar, while the other four free zones: Sarakhs, Arg Bam, Bandar-E-Anzali and Bandar Shahid Raja’ee have the status of open OTZ and SEZ. This division appears fairly relative, for over time all the zones should be transformed into SEZs. The current distinction between the two groups lies with (tax) benefits: while the former group is exempted from corporate profit tax for 15 years, the other one enjoys benefits with regard to export, import and the tax on commercial profit (the Iranian equivalent to VAT).

Located in the biggest Iranian island in the Persian Gulf, Qeshm SEZ displays the most rapid growth rates. The zone absorbed USD1.5 bn in investments , of which 30% belongs to private corporations. Of the said amount 50% of investment poured into the industrial sector, 30% in infrastructure and services, and 20% – in trade. Enterprises in the zone produce and export some 147 kinds of goods, such as popular overseas water pumps (120,000 units annually). There also is a Czech-Iranian joint venture there, which produces crystalware and multilayer pipes, a Chinese-Iranian enterprise on production of anodic and cathodic copper (3 mln t. a year). In the SEZ, there also are production facilities where the following goods are manufactured: PVC granules, projectors, VHKs, heating and kitchen appliances, watches, and many others.

The construction of a transport and warehouse zone is in progress in the island, with a number of large overseas customers, such as Toyota, having their handling warehouse facilities there, thus making it possible to ship their produce both to Iran and the Arab and European countries. In 1998 there appeared an airport, which facilitated handling operations.

Today, there are a. 500 national and foreign companies operating in the island, with most of them involved in trade and services. As well, industrial companies have recently begun their operations there, which contributed to some decline in the volume of import operations. These companies mostly produce presses for machine engineering, electric goods, textiles, electronics, food stuffs, beverages, fish products, medical equipment, pharmaceutical products, various kinds of packing goods, wooden items, sports goods and toys, and other consumer goods.

Recently Renault and the Iranian Bank of Industry and Mining have launched a huge project in the island with the purpose of manufacturing 5,000 “Sinad” passenger cars a year. Investment in the project reached

USD 52 mln. It is envisaged that 60% of assembly parts and units will be supplied from Iran, and 40% – from overseas.

That it is expedient to foreign investors to start industrial production in the island can be explained by a complete tax exemption, including corporate profit tax, for the term of 15 years.

With its SEZs, STZs and FEZs Iran works out new elements of development of the national economy and, in particular, elements of encouragement of foreign and domestic investors, duty-free customs and free exchange regimes, to name a few.

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Whilst free economic zones in different countries have played a notable part in socio-economic development of some isolated areas, or in advancement of a certain industry, or in attraction of foreign capital or renewal of a national SME sector, their rise, nonetheless, does not constitute a sufficient ground to regard them as a universal remedy for economy modernization. In the developing countries, the degree to which free economic zones affect the rest of their territory appears fairly limited. This is particularly true, so far as developed economies are concerned, however, their governments, as a rule, do not put forward the task of spreading such an influence throughout the country. Rather, organization of free economic zones plays a back-up and stimulating role in regalvanizing business activity in a given region or accentuating the need to develop a particular industry. Meanwhile, though the functioning of free economic zones in the developed countries does not appear a panacea to their various socio-economic challenges, the zones nonetheless play an important part in their socio-economic life. By contrast, for many developing countries they form poles of trade and economic, research and engineering, and social growth. In addition, they form test fields in terms of the opening of an economy and ways of its integration into the world one.

It is in the developing countries that establishment of free economic zones is associated with serious investment and subsequent efforts by the government to have them advance, for without a strictly organized centralized support, they are doomed to failure. According to a survey on 26 countries held by the Russian Academic Institute for Oriental

Studies, the budgetary costs of investment attraction accounted on average for 4 USD per 1 USD of foreign investment.

With numerous success stories, there have been failures to organize free zones, as exemplified by Sri Lanka, Guatemala and Senegal, to name a few countries. Free economic zones not only were a fiasco – they simply discontinued to exist there. Later, some governments tried to regalvanize them, and with some luck. The reasons behind the fiascos were mostly those of political, economic and organizational nature.

X. The Background of the Rise of SEZs in Russia

Back in the 1980s, still in the Soviet time, some experts vigorously advocated the idea of creation of SEZs in the country. In some publications they proved the need for establishment in the USSR of open sectors and territories, which would help attract foreign capital. To this effect special task forces were formed under the state-planning agency, *aka* Gosplan. Originally, Belarus and the Baltic Republics were picked as a test field for such experiments, however, these ideas passed away along with the collapse of the USSR.

The contemporary process of the rise of free economic zones can be split into several stages.

The first stage covers the late-1980s, when local administrations vigorously launched campaigns on organization of special economic zone, while experts designed plans and documents and put forward various recommendations. It was at the time when the federal center favored initiatives by the heads of Primorsky krai and Leningrad oblast on design of projects of establishment of SEZs "Nakhodka" and "Vyborg" (the respective legislative ruling was made later).

As free economic zones overseas were displaying high efficiency, a rapid rise in foreign investment, fast growth rates of production and infrastructure advancement, different Russian regions put forward ideas of creation local free economic zones. Some of them appeared rather bizarre, such as an idea to establish some 40 special economic zones along the Baikal-Amur railway, which were supposed to utilize the local natural resources.

It was suggested to have most zones focus on the mineral sector. However, at the time, there were no funds to establish zones, nor there was any strict legal base in existence, which has entailed numerous biases in the fundamentals of formation of free economic zones. Hopeless to mobilize their own resources or attract foreign investment, regional authorities relied heavily on the federal center. That happened not only in the case of start-up capital, which would seem quite natural, but so far as the funding of the production infrastructure and social sphere were concerned, for they appeared fairly loose in the would-be SEZs territories. Hence, the implementation of numerous (over 100) projects of creation of SEZs throughout Russia was going to lay a heavy burden on then deficit federal budget.

The second stage covers 1990–91. Its distinguishing feature became the rise of the legal base. The latter consisted of such acts, as the Decree of the USSR President "On foreign investment in the USSR (October 1990); Resolution by the Supreme Council of RSFSR of October 24, 1990 and Resolution of the Council of Ministers of RSFSR of November 23, 1990 – both on "Nakhodka" SEZ; Resolution by the Supreme Council of RSFSR of September 13,1990 and Resolution of the Council of Ministers of RSFSR of June 7, 1990 – both on "Eva" SEZ (in Jewish autonomous okrug; Resolution of the Council of Ministers of RSFSR of June 7, 1991 – on "Altay" SEZ; Resolution of the Council of Ministers of RSFSR of June 11, 1991, on Lenigrad free entrepreneurial zone; Order by the Chairman of the Supreme Council of RSFSR of June 9, 1991, on "Vyborg", Kuzbass" and "Sadko" SEZs; Resolution of the Council of Ministers of RSFSR of September 25, 1991, "On priority measures on development of free economic zones in Chita and Kaliningrad oblasts"; Resolution of the Council of Ministers of RSFSR of May 27, 1991, on "Sakhalin" SEZ; Resolution of the Council of Ministers of RSFSR of September 15, 1991, on "Amber" SEZ; Resolution of the Council of Ministers of RSFSR of June 3, 1991, on "Dauria" SEZ; Order by the Chairman of the Supreme Council of RSFSR of May 21, 1991, on "Technopolis Zelenograd" SEZ; Resolution of the Council of Ministers of RSFSR of November 8, 1991, on "Altay" free entrepreneurship zone; Resolution of the Council of Ministers of RSFSR of November 8, 1991, on "Gorny Altay" ecological and economic zone.

The Act "On foreign investment in RSFSR" promulgated in September 1991 contained a chapter on free economic zones and has notably regulated their creation. In compliance with the Act, free economic zones were to be established to attract foreign capital, advanced foreign equipment, technology and management experiences, and to develop local export capacity. Free economic zones implied a beneficial regime of economic operations for foreign investment and enterprises with foreign participation, such as simplified procedures of registration of enterprises with foreign participation. Specifically, enterprises in which foreigners had invested up to RUR 75 mln were to be registered directly in the SEZ ; beneficial tax rates: up to 50% of tax rates set for foreign investors in the territory of RF; lower fees for the use of land and other natural resources; provision of the right for a long-term lease (up to 70 years) with the right for sub-lease (beyond SEZs, the term was just 50 years); lower export and import customs duties; a simplified border-crossing procedure and entrance and departure procedures for foreign citizens, including non-visa procedures; the right for an unlicensed export and import granted to enterprises fully owned by foreign investors, as well as for joint ventures with the proportion of foreign investment over 30%. Such enterprises could also keep their forex-denominated gains from export of their output at their own disposal.

The third stage covers the period between 1992 and 1994. At the time it became clear that numerous decisions on creation of SEZs could not be realized - just a very few of them were operating, while the collapse of the economy, political instability, absence of investment, among other reasons, did not allow implementation of the designed projects. Quite naturally, the RF Government was now keen to liquidate the zones that embraced vast territories and replace them with the concept of formation of microzones, which were supposed to form a special kind of free customs zones and export-production zones. They were to be selected basing on the principle of combination of a favorable geographic location and minimum costs of their infrastructural development.

In 1992, the presidential Decree “On some measures on developing free economic zones” was promulgated, followed by the Tax Code of RF and the Act “On customs tariff” (1992); the presidential Decree “On improvement the work with foreign investment”. As well, the work started on drafting an Act on SEZs (the general concept had been put forward yet in the late 1980s, but the law has not been passed as yet). In 1994, the presidential Decree “On regulation of matters of creation and functioning of free economic zones of the Russian Federation” was promulgated. In parallel with that, the President and the Canbinte made decisions on specific zones, such as the presidential Decrees of 1992 on “Sheremetyevo” free trade zone, of 1993 – on “Moskovsky Francoport” free customs zone, on “Sherizone”; and the presidential Decree of 1993 and the Resolution of the RF Government of 1994 on “Ingoushetia” zone favorable economic zone.

As a result, there have emerged several categories of free economic zones in Russia:

1. the federal-level SEZs, that comprised:
   - free trade zones (“Sherizone” by Sheremetyevo airport);
   - free customs zones: “Moscow Franco-Port” (by Vnukovo airport); Franco-Port Terminal;
   - R&D zones (SEZ in Zelenograd, with the focus on microelectronics, informatics, and communication);
   - Tourist and resort zones (“Kavkazskiye Mineralnye Vody”).

   Common for all these zones, tax rates are lower and customs procedures are simplified in them.
2. SEZ established to implement certain economic programs:
   - “Ekologicheskaya mini-model obschestva buduschego” in Altay;
   - Production zone “ElAZ” in Tatarstan;
   - “Ulyuanovsk-Vostochny” airport.
3. Closed administrative-territorial entities (*aka* ZATO) or the so-called research towns, which are territorial entities where high-tech weapons (for instance, nuclear) and their components were designed and produced.
4. SEZs of offshore type represented by territories with special tax regimes (Kalmykia, Ingushetia, SEZ “Altay”, economic and ecological zone “Altay” and the city of Barnaul in Altai krai, Buryatia, towns of Uglich and Kursk. Later, “inland” offshores were also established in Moscow, Leningrad and some areas of Novgorod and Kaluga oblasts.

Thus, the process of emergence of free economic zones in RF in the early-1990s was characterized by the following features:

- the absence of a clear understanding of their actual objectives and mission;
- vast territories allocated for their establishment – the size of all the formally created “free zones” accounted for more than one-third of the country’s territory;
- innumerous benefits and privileges granted to SEZs and lobbying of their interests in the RF Government;
- the local authorities’ aspiration to sovereignty through creation of SEZs.

The fourth stage is characterized by creation of special economic zones on the basis of federal acts “On special economic zone in Kalinigrad oblast” and “On special economic zone in Magadan oblast”. Their creation can be attributed to their peculiar geographic location.

Back in the early-1990s, to compensate for the isolation of Kalinigrad oblast from the rest of Russia, the federal center ruled to create first a free economic zone and consequently a special economic zone. In the early-1990s, its functioning was governed by presidential decrees and governmental resolutions, which provided for a whole series of benefits to domestic and foreign entrepreneurs, including tax ones (which were abolished in 1995–96). Between 1996 and until April 1, 2006 the principal document behind regulation of economic activity in Kalinigrad oblast was the federal Act “On special economic zone in Kaliningrad oblast”. In compliance with the Act, the local special economic zone is created in the territory of the whole region, except for areas occupied by strategic and defense objects, as well as objects developed by the oil and gas sector, which are located on the continental shelf and in Russia’s exclusive economic zone.

Russian experts provide quite ambiguous assessments of the zone’s performance.

In the period prior to the 1998 crisis the country had appreciated a rapid saturation of the national consumer market with cheap imports, which helped remedy shortages of goods and curb the price rise, particularly thanks to the SEZ regime. However, some experts raised far greater concerns regarding SEZs, for they viewed such a regime as a factor that ensured an additional contribution to the industrial production slump. Specifically, failing to withstand competition with imports, many domestic producers went bankrupt, and Kaliningrad oblast was atop of the list in terms of industrial slump rates (with the respective data presented in Table 1, it is easy to calculate that while between 1991 and 1998 vis-à-vis 1990 the physical volume of industrial output across Russia as a whole fell by 54%, the respective index in Kalinigrad oblast made up 72%). In the long run, for the population a low level of prices could not compensate for the slump in the real sector, and that was mirrored in the deterioration of indicators that characterize the level of the population’s monetary incomes.

Post-crisis, the situation has become yet more equivocal. On the one hand, the oblast became one of the leading regions in terms of the dynamic of industrial output; the free customs zone makes the oblast favorable to placement of enterprises whose profile became supplies to the "mainland" Russia of goods whose production is based on import raw materials and assembly parts (as these items were exempt from customs duties). On the other hand, the above means that the structure of the local economy has become, in many senses, artificial and not able to coexist with other regions, should uniform economic rules be introduced.

The situation with attraction of investment in the oblast appears equally ambiguous. On the one hand, despite of the free customs regime, the actual investment attractiveness of the oblast appears far inferior to that of Russia on the whole, to say nothing of the neighboring Baltic States.

On the other hand, it would have been hard to hope for a greater investment inflow in the oblast, for it is absolutely evident that this particular region is not the most investment-attractive one. While making his decision, any investor, and especially a foreign one, would focus primarily on the most capacious markets (Moscow and St. Petersburg). Plus, naturally, he would be keen to place his enterprises either at least around these cities, if not in straight in them, or along transportation routes between them (Novgorod oblast). Had it even not been an exclave and without problems with transit supplies via Lithuania, Kaliningrad oblast in any case would have remained relatively unattractive to investors. Finally, distances indeed matter in Russia, and while St. Petersburg is just 650 km. from Moscow, Kaliningrad oblast is located within nearly 1,000 km from the former and 1290 km. from the latter.

In addition, a relatively poor investment attractiveness of the oblast can be attributed to a low efficiency of the federal policy towards the region, rather than the SEZ regime itself. The free customs regime has remained unstable, which the world conceives as one of the major of any free economic zone. As noted above, the mid-1990s saw the abolition of tax benefits, and the early 1998 – import quotas (which is in direct conflict with the common concept and practice of a free economic zone). In early 2001, the effect of the free customs zone regime was suspended, due to the promulgation of Section II of the Tax Code of RF (more specifically, the Chapter on VAT), which did not provide for the free customs zone regime in the oblast. To crown the list of uncertainties, the federal law recently has introduced more and more restrictions on the regional administrations' right to grant tax benefits[30], which *per se* means a complete abolition of the regional law in this respect.

The special economic zone in Magadan oblast was created by special Act of May 31, 1999 "On special economic zone in Magadan oblast", and its operations are regulated by local regional acts: the one promulgated on June 29, 1999 No. 75-OZ "On special economic zone in Magadan oblast" and that of July 5, 1999, No. 80-OZ "On changing the administrative and territorial structure of Magadan oblast".

During the years of the zone's existence the gross regional product of the oblast grew 2.5 times, new enterprises were built, revenues to toe regional consolidated budget were on the rise, and the poverty level dropped dramatically – from 35.9% in 2003 to 18.4% in 2005. The existence of the zone helped stabilize situation on the regional labor market – the unemployment level slid notably and the real average salaries and wages grew substantially.

According to the noted federal Act, while conducting their financial and economic operations in the Oblast's territory and carrying out a separate operational account, the SEZ participants are exempt from taxes in the part collectable to the federal budget (effective until December 31, 2005). Foreign goods they import into SEZ are placed and used within its territory without collecting customs duties, taxes and economic policy measures (effective until December 31, 2014). In the event goods produced by the SEZ participants are imported from its territory to beyond the RF territory are exempt from customs duties and other charges (effective until December 31, 2014). Between January 1, 2006 and through December 31, 2014 participants in the SEZ are exempted from corporate profit tax, should they invest their profit in production expansion and advancement of the social sphere in the territory of the Oblast.

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[30] Once Section I of the Tax Code of RF came into effect in 1999, it has prohibited to grant benefits with regard to federal taxes collectable to regional budgets; upon the promulgation of the Chapter of the Tax Code on corporate profit tax the regional administrations were deprived of the right for an unlimited lowering of the regional rate of the tax in question.

A thorough analysis of the socio-economic performance of the participants in the Magadan oblast SEZ between 2002 and 2005 reveals a collapse in 2003. Underlying that was the suspension, with FZ No. 176 "On the 2003 federal budget" of the effect of benefits with respect to excises and VAT on the goods imported into the SEZ territory from overseas. That had a negative impact on the advancement of the mining sector which was a core one in the economic structure of the region. Of the overall number of corporations and individual entrepreneurs registered in the Oblast as of January 1, 2005, only 3% became participants in the SEZ. But it was they who secured the biggest part of the Oblast's industrial output and provided the bulk of services in the region. In 2004, the number of their staff accounted for 19% of the overall number of employees in the region, thus suggesting that all the biggest local corporations are enumerated in the list of the SEZ participants.

The zone contributes to the regional Fund for socio-economic development, thus making it possible for the Fund to finance various local social programs. These funds have helped remedy the most acute challenges the region faced in such areas as health care, education, and the housing sector. This extrabugetary fund is the only source of co-funding of federal targeted programs, federal acts and Government resolutions.

As concerns actual data, as of October 1, 2005, the list of the SEZ participants comprised 333 residents (of which nearly a half were trading companies). According to the criteria set by the Federal Act "On SEZ in Magadan oblast", the status of participant in the SEZ can be granted only to those corporations and individual entrepreneurs who have been registered in the zone in compliance with the federal law, conduct economic operations and hold no less than 75% of their capital assets in the Oblast.

The overall number of the SEZ residents has lately been on the decline, which can be attributed primarily to changes in the national tax policy. More specifically, a part of corporations and individual entrepreneurs have completed transition to the simplified taxation system and the presumptive tax system, by which, since January 1, 2004, the tax-sharing arrangements between the levels of the budgetary system were changed (exclusive of the federal share). Accordingly, the SEZ participants are no longer entitled for benefits with regard to these taxes.

The data on foreign trade activities evidence that during the past four years the number of corporations involved in import/export operations has been declining. Because of the aforementioned reasons, the year 2003 was most unfortunate in terms of the overall volume of imported goods. As concerns the structure of imports, there arises another negative trend, namely, the proportion of food stuffs in them is growing against the share of machinery and equipment, which is on the decline.

Asked to identify a major challenge facing the zone, its management singles out the instability of the legal area, which complicates the possibility for a medium- and longer-term operational planning. During the period of its existence, the zone has faced numerous challenges associated with adoption by various federal agencies of departmental acts, which proved to be conflicting with the national law, hampered realization of the legal regime of SEZ, introduced some elements of destabilization and affected investment in the region.

Only in 2004 alone, the local tax agencies issued over 600 rulings against the SEZ participants, and they all concerned illegality of their eligibility for tax exemptions. All the rulings were appealed against in arbitration courts and consequently recognized invalid, as they conflicted with Art. 76 of the RF Constitution, Art.1 and 21 of the Tax Code of RF and Art. 5 of the federal Act “On SEZ in Magadan oblast”. However, despite both the RF Prosecutor General’s office and the Supreme Arbitration Court of RF recognize the legality of usage of the benefits stipulated in the Act on the SEZ, the tax agency maintains aggressive stance against the SEZ participants, and so far the latter have had to go to the court of law to prove legality of their actions.

The deadline of the effect of the special legal regime, as per the basic law, is December 31, 2005. Pres. Putin signed the federal Act “On amending Art. 5 of the federal Act “On special economic zone in Magadan oblast”. The State Duma passed the bill on Nov. 25, 2005, and the Federation Council approved it on Dec. 7, 2005. The Act extends the SEZ status for the Oblast for another year, with the said regime providing for exemption of corporations that conduct economic activities in the said territory from taxes in the part due to the federal budget (except for contributions to the Pension Fund and the Social Insurance Fund).

According to the amended Act on the SEZ, in the period between January 1, 2006 and December 31, 2014, corporations that participate in the SEZ should be exempt from corporate profit tax, providing they reinvest their profit in production expansion and development of the region's social sphere. The amendments provide for the postponement of the date of the start of effect of the said provision to January 1, 2007.

The extension of the effect of the special tax regime was necessitated by preparation of the final version of the bill "On special economic zone in Magadan oblast", which requires amendments to the Tax and Customs Codes of RF. Such an extension should entail a rise in revenues to the oblast and municipal budgets, because of an envisaged greater entrepreneurial activity.

The promulgation of federal Act No. 116-FZ of July 22, 2006, "On special economic zones in the Russian Federation" signified the start of a new stage of development of free economic zones in Russia. Once passed, the Act has put an end to all earlier established special economic zones, but those in Kaliningrad and Magadan oblasts.

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Thus, the world practice evidence that special economic zones appear an efficient vehicle, which gives a boost to export, entrepreneurial activity, generates new job opportunities and promotes regional socio-economic development. Zones vary greatly by their objectives, conditions of creation, forms of governance, composition of residents and other characteristics, and one cannot pick a universal model suitable for replication. Their common feature is a pro-active governmental and local municipalities' involvement at the initial stage and in creation of favorable conditions of doing business there, an adequate material basis, social and engineering infrastructure, and tax benefits.

If such projects ever fail, that occurs, as a rule, because of the following factors:

- absence of a well elaborated development strategy;
- loose connections with universities;
- an unfavorable geographic location;
- absence of a leader in the management team;
- demand for facilities and land;
- red-tape management practices.

XI. Export Processing Zones: Definitions, Concepts, and Typology

1. Introduction

Various terms exist to describe zones used to achieve regional economic development, many of which are used interchangeably: Export Processing Zones (EPZs), Free Trade Zones (FTZs), Export Processing Free Zones (EPFZs), Free Export Zones (FEZs), Industrial Free Zones (IFZs), and Special Economic Zone (SEZs). These, and other related, terms reflect temporal and spatial variation in their use (refer to *Table VII-1*). Some authors argue that the basic concept of the various terms is similar so that EPZs are synonymous with FTZs. Others argue that the terms are conceptually different. EPZs are considered an extension of FTZs that were established for commercial purposes, where manufacturing was prohibited. Many FTZs include EPZs but many EPZs are not FTZs. For instance, an EPZ can take the form of a small area (e.g. a single factory or an industrial park) while a FTZ can take the form of a larger area (e.g. an industrial township or entire city). Likewise, it is widely accepted that SEZs and Maquiladoras are, respectively, the Chinese and Mexican versions of an EPZ. The terminological diversity is attributed to “the evolving nature and distinct purpose of each zone” (*Sadni-Jallab and Blaco de Armas, 2004, 273*). Although a zone’s designated purpose is typically conveyed in official terminology, its actual function can be distinctively different. Some zones mutate “to match the economic environment and the policy agenda of each host country” (*Madani 1999, 12*). Countries can also simultaneously establish different types of zones. All of these different types of zones clustered near major developed market economies (i.e. North America, Europe, and Japan). They have been located in or near large cities, transportation terminals (i.e. airports and seaports), free trade zones, and underdeveloped regions. They are associated with the labour-intensive stages (often assembly and manufacturing) of the garment (textiles/clothing), automobile, and microelectronics industries. Recently higher value-added products include software, pharmaceuticals, and publishing.

Table XI-1

Terminological Variation and Evolution

Term	Initial State and Institutional Use	Current Users in the Americas
Free Trade Zone (FTZ)	Since 1800s; ILO (1982)	Antigua and Barbuda, Argentina, Aruba, Bahamas, Bolivia, Brazil, Canada, Chile, Colombia, Curacao, Ecuador, El Salvador, Guatemala, Panama, Peru, St. Kitts and Nevis, St. Lucia, Trinidad and Tobago, Uruguay, Venezuela
Foreign-Trade Zone (F-TZ)	United States (1934)	United States, Puerto Rico
Industrial Free Zone (IFZ)	Ireland (1959); UNIDO (1971)	Colombia
Maqiladoras	Mexico (1965)	Costa Rica, El Salvador, Guatemala, Haiti, Honduras, Mexico, Nicaragua, Panama
Free Zone (FZ)	UNCTAD (1973)	Antigua and Barbuda, Bolivia, Brazil, Costa Rica, Cuba, Honduras, Panama, Paraguay, Peru, Saint Lucia, Trinidad and Tobago, Uruguay, Venezuela
Export Free Zone (EFZ)	Ireland (1975); UNIDO (1976)	Jamaica
Export Processing Free Zone (EPFTZ)	UNIDO (1976); UNCTAD (1983)	
Export Processing Zone (EPZ)	Puerto Rico (1947); WEPZA (1978); UNIDO (1979); UNCTC (1982); ILO (1983)	Belize, Costa Rica, Cuba, Curacao, Dominican Republic, El Salvador, Honduras, Jamaica, Nicaragua, Panama, Puerto Rico,
Special Economic Zone (SEZ)	China (1979)	
Free Economic Zone (FEZ)	Grubel (1982)	[Russia]
Free Export Processing Zone (FEPZ)	OECD (1984)	Belize
Special Processing Zone (SPZ)		Peru

Abbreviations: ILO = International Labour Organization; OECD = Organization for Economic Co-operation and Development; UNCTAD = United Nations Conference on Trade and Development; UNCTC = United Nations Centre on Transnational Corporations; UNIDO = United Nations Industrial Development Organization; WEPZA = World Export Processing Zone Association.

Sources: International Labour Organization 1988; Kusago and Tzannatos 1998; Sadni-Jallab and Blaco de Armas 2004.

2. Export Processing Zones (EPZs)

EPZs are administratively unique areas with infrastructures and favourbale investment, production, and trading conditions to attract export-oriented industries. They are associated with export-oriented industrialization (as an economic development strategy) and foreign direct investment (as an inward investment strategy). Note that countries can operate EPZs while pursuing Import-Substitution Industrialization. EPZs can be instituted during the early or late stage of industrial development in developing market economies[31]. The intended functions of EPZs are to attract foreign investment and boost manufacturing capacity. EPZs can be differentiated in terms of spatial segregation (fenced-off industrial enclaves), domestic market access (in the host country), and operation ownership/management (public or private entity). EPZs are extensively used in Central America and the Caribbean for export-oriented manufacturing. The following institutional definitions are internationally used:

"EPZs are all government authorized areas such as free ports, free trade zones, custom free zones, industrial free zones or foreign trade zones or any other type of zone" (*World Export Processing Zone Association 1978*).

"An EPZ is a relatively small, geographically separated area within a country, the purpose of which is to attract export-oriented industries, by offering them especially favourable investment and trade conditions as compared with the remainder of the host country. In particular, the EPZs provide for the importation of goods to be used in the production of exports on a bonded duty free basis" (*United Nations Industrial Development Organization 1980, 6*). This definition is also cited and used by *Dicken 2003, 179*.

"EPZs are industrial estates which form enclaves within the national customs territory and are usually situated near an international port and/or airport. The entire production of such zones is normally exported. Imports of raw materials, intermediate products, equipment and machinery required for export produc-

[31] Older newly industrializing countries (NICs), such as the Dominican Republic, introduced EPZs during early stages while newer NICs, such as Honduras, implemented EPZs during the later stage. In several older NICs, there has been a shift from labour-intensive assembly to "capital-intensive high-technology goods" (*Knox, Marston, and Nash 2004, 326*).

tion are not subject to customs duty" (*United Nations Conference on Trade and Development 1985, 10*).

"An EPZ [is] a clearly delineated industrial estate which constitutes a free trade enclave in the customs and trade regime of a country, and where foreign manufacturing firms producing mainly for exports benefit from a certain number of fiscal and financial incentives" (*International Labour Organization/United Nations Centre on Transnational Corporations 1988, 4*).

"An export processing zone is an industrial estate, usually a fenced-in area of 10 to 300 hectares, that specializes in manufacturing for export. It offers firms free trade conditions and a liberal regulatory environment" (*World Bank 1992, 7*).

"EPZs [are] industrial zones with special incentives set up to attract foreign investors, in which imported materials undergo some degree of processing before being re-exported" (*International Labour Organization 2006*).

Definitions used by the International Labour Organization/United Nations Centre on Transnational Corporations and by the World Bank are considered to be narrow. They exclude EPZs that are not confined to industrial parks (e.g. single factory EPZs and SEZs) and EPZs that allow firms to sell their product(s) within the host country's domestic market (e.g. Dominican Republic, Mexico, and Brazil).

The remaining selected definitions of EPZs are taken from scholarly sources, primarily university textbooks and research reports:

"Small geographically separated areas within countries designed to attract export-oriented industries…EPZs are, therefore, export enclaves set up for the processing and assembly of export products from mainly imported materials and components" (*Healey and Ilbery 1990, 294*).

"A delineated, enclosed and policed area of a country which has an industrial estate specializing in the production of manufactured goods for export" (*Proctor and Markman 1995, 7*).

"EPZs are…geographic zones (not necessarily industrial parks) established outside the customs territory of a particular country, where products can be stored, processed and manufactured without payments of import duties, and with the intention of exporting most of the output" (*Jenkins, Esquivel, and Larraín 1998, 2*).

"An export processing zone is defined as a territorial or economic enclave in which goods may be imported, stored, repacked, manufactured, and reshipped with a reduction in duties and/or minimal intervention by customs officials" (*Madani 1999, 5*).

"Geographic areas set aside by government to use production-for-export sites in which incoming firms are to be given preferential treatment" (*Fik 2000, 245*).

"Small, closely definable areas within which especially favourable investment and trading conditions are created by governments in order to attract export-oriented industries, especially foreign-owned. These conditions include the absence of foreign exchange controls, the availability of factory space and warehousing at subsidized rents, low tax rates, and exemption from tariffs and export duties" (*Knox, Agnew, and McCarthy 2003, 47*).

"Small areas within which especially favorable investment and trading conditions are created by governments in order to attract export-oriented industries" (*Knox, Marston, and Nash 2004, 555*).

"Export Processing Zones (EPZs) are special industrial parks providing duty relief to export-oriented firms operating in the zones. They are enclaves within a county where foreign and domestic goods may enter duty free in order to be stored, distributed, combined with other foreign and/or domestic products, or used in manufacturing operations" (*Sadni-Jallab and Blaco de Armas, 2004, 272*).

"Specially created legal spaces or industrial parks within a county where, to attract foreign-owned factories, duties and taxes are not charged" (*Mihelic Pulsipher and Pulsipher 2006, GL-3*).

The major purposes (goals or policy objectives) of EPZs to host countries are (*Madani 1999; Granados 2005*):
(1) to provide foreign exchange earnings via non-traditional exports (i.e. export diversification);
(2) to provide jobs to alleviate unemployment or underemployment (i.e. occupation and income creation);
(3) to attract foreign direct investment; and
(4) to promote technology and knowledge/skill transfer.

The last item refers to the demonstration effect, that stimulates local entrepreneurs, and the catalyst effect, which creates forward and backward linkages with local firms via subcontracting. EPZ are also used to facilitate the development of marginal regions (i.e. slow growth areas).

The major roles of EPZs are (*Madani 1999; Granados 2005*):

(1) to advance the implementation of economic, trade, and/or exchange reforms;
(2) to acquire foreign currency which is used to pay for imports and create jobs;
(3) to test free-market concepts/practices; and
(4) to facilitate technology and/or skills transfer.

The major incentives of EPZs include:

(1) investment incentives -> tax allowances (e.g. tax holidays of varying lengths, tax exemptions and/or low tax rates), no foreign exchange controls, and freedom to repatriate profits;
(2) trade concessions (minimal trade restrictions) -> reduced or no duties on imports of raw materials, intermediate inputs, and capital equipment necessary for the production and/or exports of (semi-)finished products;
(3) lenient or no restrictions on foreign ownership of productive assets;
(4) adequate and inexpensive land and buildings -> provision of factory space and warehousing at low cost/rent (rental rates are often subsidized);
(5) adequate and inexpensive infrastructure and services -> provision of energy, water, roads, transportation and communication facilities (e.g. subsidized utility rates);
(6) minimal or no workplace standards regarding wages and work conditions (i.e. health and safety issues);
(7) minimal or no environmental/pollution standards;
(8) plentiful, cheap, and non-unionized labour (or constraints on labour organizations);
(9) market access (to the host country's domestic market and/or neighbouring foreign markets)[32].

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[32] For example, Caribbean countries have preferential access to European Union markets via the LomйConvention and to the United States markets via the Caribbean Basin Initia-

These incentives, along with EPZ administration and customs procedures, establish an advantageous regulatory framework and business environment for foreign direct investment by multinational corporations. *Granados 2005, 71* notes that "multilateral and regional trade obligations recently acquired by many countries in Latin American and the Caribbean remove the main incentives conferred by EPZ and accentuate their temporary nature".

3. Free Trade Zones (FTZs)

The term 'free trade zone' has been used since the 1800s. FTZs have occasionally been called 'free zones' or 'free port zones.' Initially, they were exclusively associated commerce and trade. Today, many FTZs include manufacturing activities; primarily the processing of imported goods for re-export. FTZs are "geographically circumscribed and deemed to be outside the national customs territory" (*Granados 2005, 72*). FTZs incentives are similar to those provided in EPZs. The major difference is that income tax holidays are typically not offered in FTZ. Instead, reduced tax rates are available. FTZ are common in South America. Two institutional definitions, both from the World Bank, exist:

"A free zone or free trade zone is a fenced or otherwise isolated physical area in or near a port or airport, where no customs duties are collected – the zone is considered the be outside the economy's tariff area" (*World Bank 1992, 24*). This definition assesses FTZs as 'fenced-in' EPZ (either an enclave or industrial park).

"EPZs with free trade and other equal footing export policies, which include: realistic exchange rates; free access to raw materials, inputs and capital goods at world prices, easy access to short term trade financing at market interest rates; and easy access to investment licensing and financing for the creation of export production capacities" (*Rhee, Katterbach, and White 1990, 4*).

4. Special Economic Zones (SEZs)

SEZs are unique phenomenon with particular circumstances. They are characterized by minimal state interference and focus on manufac-

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tive. Mexico has access to the United States and Canada via the North American Free Trade Agreement.

turing activities. They were established in 1979, as part of China's 'open policy' (industrial reform and regional development programs), to earn foreign currency and to test foreign management techniques and manufacturing technology[33]. Specifically, SEZs were designed to attract FDI "that could generate exports, the proceeds of which could supply China with the capital it needed to build its basic infrastructure and thus achieve sustained economic growth" (*Rowntree, Lewis, Price, and Wyckoff 2000, 486*). Free-market ideas are practiced in SEZs, which are open to global capitalism. Emphasis is on labour-intensive manufacturing activities. SEZs are larger than EPZs (ranging in size from industrial parks to entire cities) and located in the southern coastal regions. SEZ incentives (to attract FDI) are similar to those of EPZs except that duty free allowances are applied on a selective basis. For example, firms brining in new technology are rewarded with better concessions (e.g. a longer tax holiday). Since 1990, China has established Economic and Technology Development Zones (EDTZs), which function as FTZs, to encourage foreign investment, economic growth, and high-technology clusters. These zones have fewer restrictions and are located in both coastal and inland areas.

5. Maquiladoras

Mexico established an FTZ program in 1946 but only a few zones were operated (McGilvray 2004). The Border Industrialization Program (1961) extended the FTZ such that it paralleled the entire Mexican-American border. In 1965, the Maquiladora Program was implemented. This program involves capital mobility from the United States rather than labour mobility from Mexico. Foreign-owned factories located in northern Mexico assemble imported components that are exported to the United States as finished goods. Under this program, American firms establish production facilities (factories or plants) in Mexico which employ Mexican workers to produce goods using American parts. The final products are exported to the United States without any customs duties and tariffs. Incentives include low taxes, streamlines customs procedures, lenient workplace and environmental standards, and ac-

[33] SEZs "served to give Chinese businesspeople a little more latitude in experimentation with free market and joint-venture activities" (*Salter, Hobbs, Wheeler, and Kostbade 2000, G-8*).

cess to the American market. Unlike the FTZs, maquiladora plants can locate anywhere in Mexico but they are concentrated along the Mexican-American border. *Granados 2005, 74* notes that the "maquila regime…does not fall in with the typical EPZ scheme" because it does not involve geographic enclaves of production facilities. Instead, bonded factories and/or warehouses use temporary importation (regime of temporary admission) for the assembly of non-traditional exports. Many of these factories are located near the Mexican-American border. Under the provisions of the North American Free Trade Agreement (NAFTA), the need for EPZs is gone – all of Mexico becomes an EPZ. Also, the products of these factories will have unrestricted access to the Mexican market.

Maquiladora operations also exist in Central America (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua), the Caribbean (Dominican Republic and Haiti) and South America (Peru and Paraguay) (*Braga 2002; Singa Boyenge 2003*).

6. EPZ Typology

Based on the aforementioned terminology, the International Labour Organization (2006) has developed a typology of EPZs that classifies the different terms featured in *Table IX-1*. As indicated in *Table IX-2*, this classification system traces the evolution of EPZs in terms of economic sector; from commodity trading to product assembly to service provision. Differences reflect policy objectives (i.e. economic goals). Today's physical form reflects industrial diversity by including zones designated for a specific industry, commodity, factory, or firm.

Granados 2005, 72–73 suggests a functional classification scheme for EPZs according to the following dimensions:

(1) economic activity – processing (substantial product transformation) or marketing (minimal product transformation; limited warehousing, packaging, and labeling);
(2) economic sector – good or services;
(3) product destination – external or internal market; and
(4) activity scope – general (several firms in industrial parks) or subzone (individual firms outside of industrial parks).

The last dimension refers to geographic diversity in terms of contrasting a concentration of firms within a fenced-in site with individual firms with EPZ status that operate at dispersed sites. Another useful dimension is ownership and operation/management in terms of public, private, or a private-public partnership.

7. EPZ Distribution

The precise number of EPZs in the world is somewhat difficult to verify because of terminological variation and data aggregation, which does not differentiate among different types of zones. Moreover, some countries do not disclose information about their EPZs. Recent estimates of the global scale of EPZs vary from 933 in 2000 to 1,072 and 3,000 in 2002, to 5,174 in 2003. An appreciation of the rapid growth of EPZs, especially during the 1990s, is acquired from a review of figures presented in *Table VII-3*. The number EPZs increased 29-fold between 1984 (176 EPZs) and 2004 (5,174). *Fig. XI-1* provides a spatial summary of the contemporary spatial arrangement of EPZs.

Table XI-2

Typology of Zones

	Trade		Manufacturing	Services			
1	2	3	4	5	6	7	8
	Free Port	*Special Economic Zone (SEZ)*	*Export Processing Zone (EPZ)*	*Enterprise Zone*	*Information Processing Zone*	*Financial Service Zone*	*Commercial Free Zone*
Physical Form	entire city or jurisdiction	entire province, region, or municipality	enclave or industrial park	part of city or entire city	part of city or "zone within zone"	entire city or "zone within zone"	warehouse area, often next to port or airport
Economic Goals	development of a trading centre and diversified economic base	deregulation; private-sector investment in a restricted area	development of export industry	development of small- and medium-sized enterprises in depressed areas	development of an information processing centre	development of an off-shore banking, insurance, securities hub	facilitation of trade and imports
Duty Free Allowances	all goods for use in trade, industry, and consumption	selective basis	capital equipment and production inputs	none	capital equipment	varies	all goods for storage and re-export
Typical Activities	all	all	light industry and manufacturing	all	data processing, software development, computer graphics	financial services	warehousing, packaging, distribution, transshipment

1	2	3	4	5	6	7	8
Typical Incentives	business start-up; minimal tax and regulatory restraints; liberalized labour codes; free repatriation of profits; preferential interest rates	reduced business taxes; liberalised labour codes; reduced foreign exchange controls	tax exemptions (up to 15 years); regulatory relief; no foreign exchange controls; free repatriation of profits; trade union restriction	zoning relief; simplified business registration; local tax abatement; no trade unions	deregulation of telecommunications access to market-priced INTELSAT services; no trade unions	tax relief; confidentiality; deregulation of currency exchange and capital movement; free repatriation of profits	no import quotas; tax-free reinvestment of profits
Domestic Sales	unrestricted within freeport; outside freeport, upon payment of duty	highly restricted	limited to small portion of production			limited to small portion of production	unlimited, upon payment of duty
Other Features	additional incentives and streamlined procedures	developed by socialist countries	may be extended to single-factory sites				
Examples from the Americas	Bahamas	none (China)	Dominican Republic	None (Indonesia)	Caribbean	Caribbean, Cayman Islands	Panama, United States

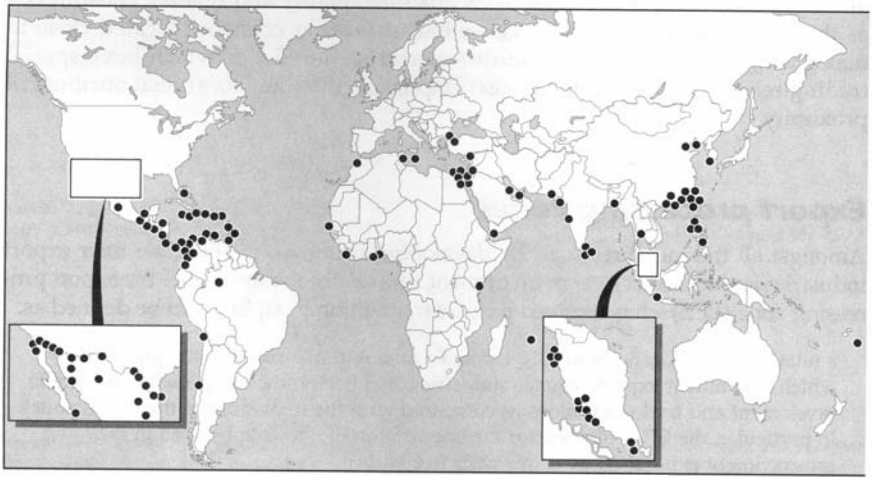
Source: Adapted from International Labour Office 2006.
Available: http://www.ilo.org/public/english/dialogue/sector/themes/epz/typology.htm

Table XI-3

Worldwide Number of EPZs

Year	Estimated Number	Source(s)
1	2	3
1966	2	Knox, Marston, and Nash 2004, 325
1975	79	ILO 2002
1981	60	Wong and Chu 1984, 1.
1984	68	Healey and Ilbery 1990, 294
1985	173	Knox, Marston, and Nash 2004, 325
1986	176	ILO 2002
1989	200	UNCTC 1990, 1
1990	86	World Bank 1992
1995	500	ILO 2002
1996	839	UNCTAD 1998
1997	845	ILO 2002

1	2	3
1998	850	OECD 2000; Knox, Marston, and Nash 2004, 325
2000	993	Granados 2003
2002	1,072	Granados 2005
2002	3,000	ILO 2002
2004	5,174	ILO 2004



Source: Dicken 2003, 180.

Fig. XI-1. Worldwide Distribution of EPZs

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Annex 1. Summary of ACOA's Program Activities

ACOA's three major strategic outcomes are: (1) enterprise development, (2) community development, and (3) policy, advocacy, and coordination.

Enterprise Development

Critical to developing an innovative economy is fostering the start up, growth and competitiveness of Atlantic SMEs. This is achieved through investment in areas such as venture capital, SME skills and training, research and development, expanding trade and promoting foreign direct investment. To achieve these results, ACOA will focus on:

(1) *Innovation* – strengthening innovation systems, supporting strategic sectors, building innovation capacity, addressing skills gaps, carrying out a stronger federal innovation advocacy role, and improving regional coordination.

(2) *Entrepreneurship and business skills development* – creating an environment in which entrepreneurship is widely perceived as a career option and life-long learning is part of Atlantic Canada's business cul-

ture. Emphasis is also placed on skills development; entrepreneurship education, particularly among young Atlantic Canadians; and the development and growth of women and Aboriginal entrepreneurs.

(3) *Trade and investment* – increasing the level of export activity and foreign direct investment in Atlantic Canada. This approach is focused on five main elements: awareness; skills development; capacity building; policy, advocacy and co-ordination; and investment attraction and development.

Community Development

Given that a larger portion of Atlantic Canada's population is based in rural areas than is the case for Canada as a whole, developing the strength of these communities is one of ACOA's priorities.

ACOA's vision with respect to community development is to create viable and sustainable Atlantic Canadian communities that have the resources and capacity to take full responsibility and accountability for their own economic development. Recognizing that the region is built on the strength of its many communities, the Agency works to empower and help them achieve their economic development goals, and to ultimately create increased economic opportunities for Atlantic Canada. ACOA works in partnership with other government departments, community groups and non government organizations to lever support and co-ordinate economic development efforts.

In the next year, the Agency will continue to be committed to:

(1) promoting coordination and cooperation between community economic development (CED) partners in Atlantic Canada;
(2) strengthening the community strategic planning process;
(3) increasing availability of business capital in rural communities;
(4) creating sustainable jobs in these communities; and
(5) encouraging community ownership of CED activity, and empowering communities to direct their own future.

Policy, Advocacy and Coordination

The Policy function centres on how ACOA makes decisions and how it relates to and influences the decisions of others. ACOA performs this role by means of discrete research, ongoing analysis of issues and trends, and through events such as roundtables and conferences that engage other parties and stakeholders. It also performs this role by active participation in the interdepartmental policy development process.

Research projects contributed significantly to determining the areas in which ACOA acts to most effectively carry out the Agency's mandate.

The Advocacy role has two main thrusts: to maximize regional industrial benefits from major federal procurement contracts; and, to help ensure that national policies and programs have due regard for Atlantic Canada's interests. The role of Co-ordination within ACOA is to provide leadership on major economic issues and in the management of special projects and key initiatives. Initiatives to be addressed in 2005–2006:

coordinating the Government's response to "The Rising Tide" strategy;

(1) Engaging economic partners in addressing:

(a) immigration;

(b) Government of Canada's New Deal for Cities and Communities;

(c) development if offshore oil and gas;

(d) innovation.

(2) Monitoring and engaging with lead departments on issues such as

(a) regional and sectoral strategies;

(b) aquaculture;

(c) Aboriginal development; and

(d) the social economy.

Source: ACOA 2005b (Section I – Overview).

http://www.acoa.ca/e/library/reports/rpp2005/index.shtml

A detailed analysis of the program activities is available in Section II (Analysis of Program Activities) of the Report on Plans and Priorities, 2005–2006 Estimates (*ACOA 2005b*).

XII. Contemporary State and Challenges Facing Development of Special Economic Zones in Russia

1. Fundamental Provisions of the Federal Act "On Special Economic Zones in the Russian Federation"

On July 22, 2005, Pres. Putin signed Federal Act No. 116-FZ "On special economic zones in the Russian Federation". As a follow-up the RF Ministry for Economic Development and Trade issued about 26 documents, including draft Government Resolutions and circa 10 decrees by the RF Minister for Economic Development and Trade. These documents have completed the by-law legislative base.

Special economic zone is understood as a part of the state and customs territory of the Russian Federation set by a Government Resolution, within which becomes effective a special regime of conduct of entrepreneurial activity in the part of taxation, customs regulation and activities by controlling bodies.

There will be created two kinds of SEZ: industrial (to accommodate production facilities within a total area of no more than 10 sq. km. for no more than 20 years); research and development (to create and commercialize R&D by introducing into production new technologies, that are based upon advanced research and scientific achievements (with a total area of no more than 2 sq. km. and for the term of no more than 20 years).

The *modus operandi* of such zones will be as follows: at the stage of creation of a SEZ, the RF Government sets kinds of activities allowed within its territory. While this list needs to be specified, meantime within the SEZ territory it will not be allowed:

– to produce and process minerals and metal scrap;
– to produce and process items of ferrous and non-ferrous metallurgy (except for production of especially refined metals and alloys, and materials for electronics);
– to produce and process excised goods (except for passenger cars and motorcycles).

The permit to operate within a SEZ territory can be granted both to the so-called SEZ residents, i.e. entities eligible for the peculiarities of entrepreneurial activities specific of such a zone, and non-residents that conduct their operations within the SEZ territory in compliance with the RF law, however, not being entitled for the respective benefits and privileges.

Procedures of creation of a special economic zone are stipulated in the Procedures on Conduct of the Tender on Selection of Applications for Creation of a Special Economic Zone approved by Resolution of the RF Government of September 13, 2005, No. 563. These procedures imply five basic stages:

1. Announcement of a tender on creation of the SEZ, while the RF Ministry for Economic Development and Trade acts as its organizer. The Ministry produces an Order on conduct of the tender and publishes it in media.
2. Pretenders submit their applications. It is supreme bodies of the executive power of the RF Subjects, together with executive and administrative bodies of municipalities in the territory of which it is planned to create the SEZ that take part in the tender. The form and contents of such applications and the list of concomitant documents are set by Resolution of the RF Government "On approving procedures of completion and submission of an application for creation of a special economic zone" of September 13, 2005, No. 564, with the RF Ministry for Economic Development and Trade being authorized to collect such applications.
3. Sizing up. Following preset procedures, the Federal Special Economic Zones (SEZ) Management Agency selects applications for creation of special economic zones of the same type. Commissions on selection of special economic zones created under the Agency open envelopes with applications inside, examine those and select winners in the tender. According to the tender results, Commissions nominate winners in it, namely, regional and municipal entities, wherein such zones will be established.
4. Approval of the tender results and legal fixing the tender: commissions' decisions on creation of a special zone in a particular territory are included in the respective Resolution of the RF Government.
5. Conclusion of agreement on creation of the special economic zone: the agreement is concluded between the RF Government, the Supreme executive body of the RF Subject and the executive body of

the municipal entity on the territory of which the special economic zone will be created, within 30 days upon the date of the adoption by the RF Government of the Resolution on creation of the special economic zone.

To ensure uniformity of the SEZ management practices across the Russian Federation, the following management structure is envisaged:

- the mission to develop and pursue a uniform government policy with regard to creation of SEZ and their functioning is assigned to a specially authorized federal agency of executive power (the authorized federal ministry);
- the task of coordination and control over CEZ is assigned to the federal agency of executive power authorized to exercise functions with regard to SEZ management (it is planned to create a new federal agency to cope with this task);
- a particular SEZ is to be managed by a territorial body of the federal agency (hereinafter referred to as the Territorial Body).

Peculiarities of the Tax, Customs and Administrative Regime Offered to SEZ Residents

The draft Federal Act introduces the category of taxpayers formed by SEZ residents. The SES resident is an individual entrepreneur or a commercial entity registered within the territory of a given municipal entity within the borders of which the SEZ is located; he has concluded with the Territorial Body an agreement on conduct of industrial and production or research and development operations.

In the industrial zones, a mandatory condition for granting the SEZ resident status to a given entity is its obligation to ensure capital investment worth at least no less than Euro 10 mn. (exclusive of non-material assets). Plus, within a year upon the date of conclusion of the said agreement the SEZ resident is bound to ensure capital investment worth a total of no less than Euro 1 mn.

To lift the administrative burden on economic agents, it is envisaged to create a vehicle, which should ensure implementation of the “single window” principle. This means that the investor (entrepreneur) will have to interact with the least possible number of authorities on all or most of matters. This principle will be realized by delegating a number of powers to the federal agency of executive power duly authorized to exercise administrative functions with regard to a given SEZ (the federal agency).

It is envisaged to introduce the following tax particularities with regard to CEZ residents (amendments to the Tax Code of RF):

1) as concerns residents of an industrial SEZ and with regard to the corporate profit tax it is proposed to set:
   - accelerated procedures of recognition of costs on R&D works;
   - a special procedures of accrual of depreciation with regard to fixed capital (*aka* the accelerated depreciation with coefficient 2);
   - lifting the 30% limitation associated with the extension of losses reported in one tax period towards next tax periods;
2) it is intended to provide for residents in R&D zones a lower uniform social tax rate (at the level of 14% , along with the retaining of the regression principle);
3) on the federal level, it is planned to fix exemption of SEZ residents from property tax and land tax for 5 years from the moment of registration of their new status. The bill comprises provisions of direct effect that set the customs regime of the free customs zone. In compliance with the regime in question, foreign goods are placed and used inside the SEZ territory exempt from customs duties and VAT, while domestic goods are placed and used there subject to the conditions applied to exportation in compliance with the export customs regime and are subject to excises, but exempted from export duties.

In the event the aforementioned goods are exported to beyond the borders of the customs territory of the Russian Federation, they are exempted from import duties and taxes, but remain subject to export customs duties payable in a normal way.

The creation of such zones and their functioning should result in:

- attraction of both foreign and domestic companies' investment in processing industries;
- stimulation of regional development;
- development of high-tech industries and the services sector;
- generation of highly qualified job opportunities.

Successful implementation of the fundamentals of the Federal Stature "On special economic zones in the Russian Federation" necessitates enactment of a series of bylaws. Since the moment the Federal Act came in force, there appeared 42 legal acts aimed at implementation of its provisions.

Table XII-1

Documents Needed for Realization of the Federal Act "On Special Economic Zones in the Russian Federation"

Subject of document	Art. Of the Act	Name of document	Legal form of document
General matters of CEZ administration		(Documents on the Federal CEZ Administration Agency and its territorial bodies)	
	7, p.4	Statute on the Supervisory Board of CEZ	Resolution of The RF Gov-t (Art. 7 p.7)
Creation of CEZ/termination of CEZ	6 6, p.2 6, p.2 6, p.3	Decisions of the RF Government on tender on creation of CEZ, including: – procedures of drafting and submitting the application; – list of documents concomitant with the application, including justification for appropriateness and effectiveness of creation of CEZ for solving objectives of the federal, regional and local importance; – Statute on conduct of the applications selection tender (methodology of the selection)	Resolution, Decrees by the Gov-t
	6, p.1 4, p.6 37, p.6 34, p.2	Resolution by the RF Government, including:: – the list of types of operations allowed in the SEZ territory; – (if needed) the list of prohibited operations involving goods placed under the customs regime of the free customs zone; – maximum land lease rate	Draft model Resolution
	6, p.4	Agreement on establishment of SEZ, including: – volume and timelines for financing the engineering, transport and social infrastructure from budgets of all levels;	Draft model agreement

Subject of document	Art. Of the Act	Name of document	Legal form of document
	17, p.5 = 27, p.5	– design of development and the respective material and technical equipping of CEZ and territories contiguous to it; – complex of measures on designing a perspective plan of SEZ development and procedures of their funding; – shares of participation of RF, a RF Subject, municipal entity in the property rights for infrastructure facilities; – use and maintenance procedures, including capital refurbishment of the jointly owned infrastructure facilities of the CEZ; – procedures of ownership, use and control of the jointly owned infrastructure facilities upon termination of the SEZ operations; – obligations assumed by the RF Subject in the part of tax benefits; – procedures of formation of the Supervisory Board of SEZ; – obligations assumed by the RF Subject with regard to delegation to the federal agency of the executive power authorized to exercise the SEZ administration functions of powers on management and control of land lots and other real estate objects within the territory of the SEZ for the term of its existence; – obligations of the executive agency of the municipal entity on the delegation to the federal agency of the executive power authorized to exercise the SEZ administration functions of powers on management and control of land lots and other real estate objects, which are owned by the municipality, within the SEZ territory for the term of its existence; – procedures of interaction between the SEZ administrative agencies and executive agencies acting on behalf of the public agencies of RF Subjects,	

Subject of document	Art. Of the Act	Name of document	Legal form of document
		executive and administrative agencies of municipal entities in the course of evaluation of design documentation	
	17, p.5 = 27, p.5	– procedures of interaction between the SEZ administrative agencies and federal agencies of the executive power authorized to conduct evaluation of design documentation	Joint inter-mini-sterial orders
	6, p.7	Resolution by the RF Government on an early termination of the SEZ existence	Draft model Resolution
	7, p.7	Act on Supervisory Board of CEZ	Gov-t Resolution
General matters of operations of the administrative agency	8	Procedures of conduct of the register of SEZ participants, including: – draft register of SEZ participants ; – procedures of producing an excerpt from the register of SEZ participants	
	8	Model performance report form of the SEZ administrative agency	
	8	List of printed and electronic media, which publish information of land lots and assets available in the SEZ territory	
	8	Model form of visa application by the SEZ resident for issuance of an invitation for foreign citizens to apply for the RF entry visas	
	8	Construction permit granting procedures	
	8, p.2	Management company attraction procedures	Order by MEDT
Receiving the status of the SEZ participant	13	Model form of application for conclusion of agreement on conduct of industrial and production operations, Model form of business plan; Model form of conclusion on the submitted business plan	Order by MEDT
	13, p.2 18, p.1	Procedures and criteria of inclusion banks and other credit institutions in the list for preparation of conclusions on business plans, particularly in the event of amending conditions of agreements on conduct of industrial and production operations (for indus-	Order by MEDT

Subject of document	Art. Of the Act	Name of document	Legal form of document
		trial zones)	
	n/a	Act on the expert council on R&D zones	
	23, p.1	Model form of application on conclusion of agreement on R&D operations, Model form of business plan	
		Act on the expert council on R &D zones	Order by MEDT
	23, p.7 28, p.3	Act on evaluation of business plan by the expert council on R&D zones, particularly while amending agreements on conduct of R&D operations	Order by MEDT
	9, p.1 12 21, p.4	Model agreement on conduct of industrial and production operations, including: – envisaged industrial and production operations; – investment volumes and timelines; – timelines for conclusion of land lease agreement; – (if needed) contract on lease of public/municipal assets; – timelines for submission of documents for conducting evaluation and endorsement of design and technical documentation; – system of penalties for an early termination of the agreement	Order by MEDT (Art.12, p.6)
	9 p.2 10, p.2 27, p.1 31, p.4	Model agreement on conduct of R &D operations, including: – envisaged R&D operations; – timelines for conclusion of land lease agreement; – (if needed) contract on lease of public/municipal assets; – timelines for submission of documents for conducting evaluation and endorsement of design and technical documentation; – system of penalties for an early termination of effect of the agreement	Order by MEDT (ст.22, п.5)
	9, p.5	Form of the SEZ participant certificate and procedures of its granting	Order by MEDT
Start of opera-	12, p.3	Model form of land lease contract,	Order by

Subject of document	Art. Of the Act	Name of document	Legal form of document
tions in the SEZ territory	33, p.2	Procedures of conclusion of the land lease contract, Land lease fee rate	MEDT
	12, p.3	Model form of agreement on the lease of public and/or municipal real estate	Order by MEDT
	8	Procedures of granting real estate permits for construction and reconstruction of real estate objects and their connection to engineering infrastructure objects, including :	
	17, p.4 27, p.4	– form of an aggregate expert conclusion on design and technical documentation	
Modification of conditions of operations/termination of operations	18	Model form of application for amending the agreement on conduct of industrial operations, Model form of business plan; Model form of conclusion on the submitted business plan	
	28	Model form of application for amending the agreement on conduct of R&D operations;, Model form of business plan;	
	11 11, p.8	Model judicial claim laid by the SEZ territorial administrative agency on disfranchisement of the status of the SEZ participant and the claim submission procedures (including procedures of interaction with customs and tax authorities)	
Control over operations of the SEZ participants	8	Procedures of exercise of control by the SEZ administrative bodies over the SEZ resident’s compliance with the agreement on conduct of industrial or R&D operations	
	11, p.3	Regulation of conduct of planned complex inspections and early inspections of the SEZ residents	
Customs regime	37		

Procedures of creation of a special economic zone are stipulated in the Procedures on conduct of the tender on selection of applications for creation of a special economic zone approved by Resolution of the

RF Government of September 13, 2005, No. 563. These procedures imply five basic stages:

1. Announcement of a tender on creation of the SEZ, while the RF Ministry for Economic Development and Trade acts as its organizer. The Ministry produces an Order on conduct of the tender and publishes it in media.
2. Pretenders submit their applications. It is supreme bodies of the executive power of the RF Subjects, together with executive and administrative bodies of municipalities in the territory of which it is planned to create the SEZ that take part in the tender. The form and contents of such applications and the list of concomitant documents are set by Resolution of the RF Government "On approving procedures of completion and submission of an application for creation of a special economic zone" of September 13, 2005, No. 564, with the RF Ministry for Economic Development and Trade being authorized to collect such applications.
3. Sizing up. Following preset procedures, the Federal Special Economic Zones (SEZ) Management Agency selects applications for creation of special economic zones of the same type. Commissions on selection of special economic zones created under the Agency open envelopes with applications inside examine those and select winners in the tender. According to the tender results, Commissions nominate winners in it, namely, regional and municipal entities, wherein such zones will be established.
4. Approval of the tender results and legal fixing the tender: commissions' decisions on creation of a special zone in a particular territory are included in the respective Resolution of the RF Government.
5. Conclusion of agreement on creation of the special economic zone: the agreement is concluded between the RF Government, the Supreme executive body of the RF Subject and the executive body of the municipal entity on the territory of which the special economic zone will be created, within 30 days upon the date of the adoption by the RF Government of the Resolution on creation of the special economic zone.

In the late 2005, the Federal Special Economic Zones Management Agency held a tender on selection of applications for establishment of special economic zones.

Later, on November 28, 2005, the tender Commission was convened under the chairmanship of Mr. G. Gref, the RF Minister for Economic Development and Trade, to nominate winners. As many as 47 Russian regions expressed the willingness to establish special economic zones. The Regions submitted 72 applications, of which 29 ones – for organization of R&D zones and 43 – for organization of industrial zones. Yet another two applications for creation of industrial zones submitted by Orenburg oblast and Khanty-Mansy autonomous okrug were declined on the grounds the documentation they had submitted failed to meet application completion procedures and requirements to submission.

The Commission selected 6 applications, of which four dealt with establishment of R&D zones, and another two - with creation of industrial zones.

The noted four R&D zones will be located in St. Petersburg (conduct of research in and production of information technology and analytical instrument-making); the town of Dubna (information and nuclear physics technology), Zelenograd, a Moscow city outskirt (micro-and nanoelectronics, optical electronics, information and communication systems, bioinformation and biosensor technologies, nanotechnologies and nanomaterials); and the city of Tomsk (information, communication, and electronic technologies, new materials, nano-and biotechnology).

The Commission found it far harder to pick winners in the other category. Finally its members made their choice by nominating a joint Russian-Italian project in Lipetsk oblast already in progress – manufacture of home appliances and electric appliances, and furniture (with *Merloni* as a principal partner), and the town of Elabuga in Tatarstan, wherein it is envisaged to produce assembly parts for the automobile industry and organize a highly sophisticated petrochemical production, with such renowned partners from overseas as *General Motors, Toyota, Caterpillar, KFZ, George Fisher, RBL, Mando, and Nicolson.*

Table XII-2

Main Characteristics of Russia's Special Economic Zones

SEZ location	SEZ area	SEZ profile	Public investment in SEZ infrastructure
St. Petersburg	Two sites with a total area of 200 hectares	Software, communication devices and home electronics, automated technological process control systems, medical equipment. Design and manufacture of analytical devices	a. RUR 1.5 bn, including a. 50% from the federal budget
Town of Dubna, Moscow oblast	Two sites with a total area of 187.7 hectares	Electronic instrument making, design of new types of aircraft, development of alternative energy sources	RUR 2. 5 bn, of which 65% from the federal budget
Town of Zelenograd	Two sites with a total area of over 155 hectares	Design and development of microchips, produce of integral optics, optical electronics and intellectual navigation systems, bioinformation and biosensor technologies. Organization of a complete cycle of very precise assembly of electronic produce	a. RUR 5 bn, including 50% – from the federal budget
Tomsk	Two sites with a total area of 197 hectares	Information and communication, electronic and medical technologies, and production of new materials	a. RUR 1.9 bn, of which 70% – from the federal budget
The city of Lipetsk	10.3 sq.km.	Home appliances and assembly parts	a. RUR 1.8 bn, of which 42% – from the federal budget
The city of Yelabuga, Tatarstan	20 sq.km.	Automobile assembly parts, buses, home appliances. High-tech petrochemical production	a. RUR 1.6 bn, of which 49% – from the federal budget

The RF Ministry for Economic Development and Trade believes that establishment of a single special economic zone should attract at least a RUR 9 bn-worth investment, along with a 5–7% decline in costs incurred by investors. It is envisaged that the annual output of every SEZ from the above list should worth a total of RUR 6 bn. The volume of federal funding of their operations in 2006 was RUR 8 bn.

Presently, the pace of and efficiency in creation of new economic zones is going to have a critical impact on prospects for implementation of and progress in the project both in the eyes of investors and for the national economy as a whole.

2. Special Economic Zones of R&D Type

(a) Special Economic Zone in Dubna

General Information on the Special Economic Zone in Dubna

The Dubna R&D special economic zone is established to attract investors and secure conditions for conduct of R&D operations, developing samples and manufacturing sample lots of high-tech produce, as per the priority guidelines of research and technical and innovation activities, experimental designs, testing and staff training, fixed with Dubna as a "research town" of the Russian Federation by presidential Decree of December 21, 2001, No. 1472. With this status, a particular attention will be paid to encouragement of activities in such areas as data and nuclear physics technologies.

The main objectives of creation of the R&D zone are:

- increasing Russia's share on the world markets for high-tech products and, primarily, on the one for information technology;
- creating a modern Russian model scientific-technical park, which will include a university, research and engineering centers, and innovation enterprises;
- creating in Dubna a center for development and dissemination of the culture of software design and manufacture.

In the course of the project implementation it is envisaged to respond to the following challenges:

- working out a modern model of development of research towns as key elements of the emerging national innovation system;

- developing mechanisms of concentration , in modern conditions, of intellectual and other resources within a certain territory to tackle priority challenges in the research and technical sphere;
- fine-tuning vehicles of interaction between the federal authorities, those in a given RF Subject and local self-governance, forging mechanisms of public-private partnership (P3) in implementation of territorial development projects;
- perfecting mechanisms of creation of CEZ and their functioning as a vehicle of the government support of activities in the high-tech sphere.

Additionally, the Dubna project will be solving some other particular tasks, such as development of a mortgage mechanism to provide housing to attracted specialists and urban development and engineering infrastructure development of Russian modern towns.

The Dubna SEZ Profile

Underlying the selection of the Dubna SEZ profile was the effective law and examination of the following factors:

- the existing research and technical profile of the local research and production organizations;
- the existing network of uch organizations and possibilities to identify clusters by certain types of research and technical activities;
- prospects for Russia's competitiveness on the world markets for high-tech produce;
- proposals by potential investors and organizations of the local research and production complex.

The main (profile) operational areas of Dubna SEZ have become data technologies and nuclear-physics technology. The former area embraces software production, manufacture of data collection, processing and transmission systems, production of distributed computing, provision of services associated with introduction and maintenance of such products and systems, development and production of samples and sample lots of electronic elements, devices and systems, as well as R&D operations in other research, engineering and technology areas, which appear critically dependent on information technology.

In addition to the noted operational avenues, it is also intended to develop some other research and technology areas, which will be determined by applications and business plans put forward by pretenders for residency in the zone.

The Concept of Establishment of the Dubna R&D SEZ

The creation of the zone is back-upped by the infrastructure and research and engineering capacity of the existing local research, engineering and educational institutions, such as the Joint Institute for Nuclear Research, the "Dubna" University under the Moscow Oblast Governor, JSC "MKB Raduga", federal public unitary enterprise "Atoll" to name a few, and with account of the existing local innovation infrastructure.

The concept in question suggests creating an R&D SEZ, which would rest upon the interaction between four basic modules:

- innovation belt circumscribing JINR and other local research and engineering organizations;
- the university as a local center for innovation and education;
- "The Russian Software Center" technopark;
- The local innovation infrastructure and mechanisms that secure innovation activities.

The Innovation Belt around JINR and other Local Research and Engineering Organizations

The future of JINR is associated with advancement of its three operational components, as follows:

1. Solidification of the Institute's position in the international labor division system with regard to fundamental research and, primarily, physics of elementary particles, nuclear physics, physics of condensed mediums, as well as development of fundamental research with the use of nuclear-physics methods in medicine, biology, science of materials, and ecology. Fundamental research now finds itself increasingly dependent on information technologies.
2. Advancement of the educational component at JINR. Presently, the Institute offers advanced training to talented youth: there is a local branch of the Research Center for Nuclear Physics under Moscow Lomonosov University in the town; JINR has founded a training and research center, which delivers advanced educational services and, in parallel runs a special training in JINR's research facilities for Bachelors from Moscow Lomonosov University, Moscow Engineering and Physics Institute, Moscow Physics and Technical University,

Moscow Institute for Radotechnics and Electronics, as well as from high schools from the countries that participate in the project on the following subjects: nuclear physics, physics of elementary particles, physics of condensed mediums, theoretical physics, technical physics, and radiobiology. JINR has postgraduate training on 10 subjects, and there are 9 thesis councils on various specialties. The cooperation between the Institute and the public university “Dubna” is especially important, as the project provides for establishment and development at JINR of the University’s training and research laboratories on physics, applied nuclear physics, biophysics, and information technologies. The Center’s Laboratory for Information Technologies should become home to a center for advanced training of local Bachelors in their profile specialties.

3. Conduct of applied research and innovation. The Institute’s output is critical for both the fundamental research and the national economy. Advancement of the in-depth fundamental research is combined there with application of nuclear-physics research methods to the medical sphere, biology, science of materials, ecology and other areas of research and engineering.

There is a number of spin-off companies that have excelled in advancement of the Institute’s research, such as “Kompaniya Kontakt” Ltd. (telecommunication), the federal public unitary enterprise “Dedal” (protection systems), JSC “Aspect” (radiological control devices), research and engineering company “Alpha, JSC “Holding company “Trekpor Teknology” (donor and medical plasmopheresis), “Intergrafika” Ltd. (systems of computerized visualization of educational processes), and others.

It is planned to further research and design across the following sections: new materials and chemicals (materials for micro- and nanotechnology, polymers, ceramic materials and nanoceramics, design of chemicals and materials with pre-set qualities), ecology and rational use of natural resources (technologies of monitoring of the natural and man-caused sphere), production of atom-smashers for solving applied problems, research and design in the area of control over moving of radioactive materials by means of neutron analysis, R&D in the area of manufacture of tracking membranes, cryogenic equipment, manufacture of sample reactors with subcritical mass, and R&D in the area of therapy of oncology.

To encourage innovation and create the innovation belt around JINR, the Concept envisages:

– promotion of cooperation with AFK “Systema”, which is the Institute’s principal partner;
– support to creation of spin-off companies that deal with development and manufacture of products on the basis of the Institute’s achievements in research and engineering;
– creation, in cooperation with AFK “Systema”, of “Dubna-Systema” managing company to encourage small enterprises in the research and engineering area;
– completion of innovation projects on creation of competitive high-tech products and technologies on the basis of formation at JINR of task forces, including those formed by highly qualified researchers and experts from Russia and overseas.

On the basis of other main local enterprises (the federal public unitary enterprise “Raduga”, the federal public unitary enterprise “Research Institute “Atoll”, JSC “Priborny zavod “Tenzor”, JSC “DMZ”) there have been created over 50 research and engineering companies. It is intended to select non-profile research areas of large enterprises of the local research and production complex and form spin-off companies.

Encouragement of advancement of the newly created research and engineering companies forms one of the priority objectives for the local innovation and engineering incubator.

“Dubna” University as an Innovation and Educational Center of the Research Town

Between 1994 and 2004 the University has given a rise to a highly efficient research and faculty team, including some 300 PhDs and Doctors in science, members of the national Academy of Sciences, the Academy of Medical Sciences, the Academy of Natural Sciences, the Russian Academy Society.

There have been created specialized chairs and laboratories (including commercialized ones) that focus on research and design in such spheres as environmental science, data technologies, biophysics, applied nuclear physics, energy, geophysics, to name a few.

The project implementation enabled the local research community to complete the first stage of integration of fundamental and applied research with the university education. A number of leading chairs have been established as a joint effort involving JINR, “Atoll”, “Raduga”, “Soyuz”, etc. and now found an experimental and laboratory base at JINR.

Direct contacts and cooperation have been established with the university community from the US, Italy, Germany, China, and some other countries.

The University sees its mission in:

- transition towards the stage of research and innovation university which implies a leading position in Russia in certain priority avenues of advancement in research, technologies and engineering;
- targeted training of highly qualified cadres for organizations of the local research and engineering complex and the Russian Centre for Computer Science;
- considerable increase in the share of Masters, Postgraduates and future Doctors in Science at the University;
- transformation of the University into a principal training facility for the non-stop training in innovation, research, engineering and technology, including advanced training in the most demanded specialties.

In addition, it is envisaged to form at the University a system of laboratories, centers, business schools aimed at fundamental and applied research in the priority areas. It is planned, within the project framework, to advance the work on encouragement and support of start-ups founded by the University students and graduates.

As concerns qualitative indicators of its performance, the University views the project of a considerable increase in the share of graduates in data technologies, along with a simultaneous perfection of the respective training as its urgent priority.

The project provides for a close interaction with other Russian universities, which have excelled in training specialists in information technologies, for the sake of training experts for the Russian Centre for Computer Science. The University leadership is going to create a system of selection of Bachelors from the Russian-language high schools for a subsequent Master=s course with the University, with their parallel employment at IT companies. It is also intended to increase the number of the University graduates with the Master=s degree in IT up to 400-500 annually, thus meeting roughly at one-third needs of the companies under the Russian Centre for Computer Science.

The project "the Russian Centre for Computer Science"

The principal objective of the project is to foster the domestic IT production and secure its competitiveness on the national and world markets, boost the proportion of IT goods and services in the general structure of the nation's export.

While implementing the project, it is intended to establish an IT technopark in the town of Dubna and to concentrate there during next 5–7 years some 10,000 IT experts. As well, it is intended to boost the technopark's annual output up to USD 440 mln and to create a nationwide development and dissemination center with respect to the software design and sales culture.

The project provides for:

- establishment within the territory of the town of Dubna a settlement for some 30,000 IT staff with a total area of 465 hectares. The settlement will be located on the left bank of Volga;
- construction of a new industrial zone, to become home to serial and sample production facilities, on the right bank of Volga with the total area of 124 hectares.

The Concept of Supply of Cadres to the Dubna R&D Special Economic Zone

Presently, the local workforce is accounted for 38, 600, or 62.8% of the total local population. Of the total number of able-bodied population 81.9% (31,600) is employed in the economy, 11.0% is students, while 7.1% is currently unemployed.

By contrast with the employment structure of the Moscow oblast, in Dubna the greatest employment is noted in non-production sectors. Thus, 27.5% of the local population is employed in science and research, while every fourth appears employed in the industrial sector, which is a notable greater proportion vis-à-vis the rest of the region. The town boasts over 1,000 PhDs and some 300 Doctors in Science employed in the local economy.

According to the local employment agency, the number of those daily commuting mainly to Moscow to work there accounts for some

3,000 (including 1,000–1,200 specialists), while some 500 employees come to the town from the contiguous localities.

The officially registered unemployed do not outnumber 600.

It is envisaged to recruit labor resources for enterprises that will reside in the special economic zone among graduates from the “Dubna” university, as well as other Russia’s and CIS high schools and other local primary and secondary vocational training institutions, and through attraction of specialists residing in the town and currently employed elsewhere, residents from the contiguous localities, and specialists from other Russia’s regions and the CIS.

Staff Training in the Framework of the “Dubna” University Development Program

To train specialists, it is intended to increase enrollment mostly of Bachelors and specialists from other Russian and CIS high schools for the University’s Master=s course. It is envisaged that the of such post-graduates will be increased up to 500 annually. In parallel with that, there will be organized specialized commercial courses on the basis of contracts with potential employers and internships at such organizations.

It is suggested to organize admission to the Master=s courses and specialized courses and internships on the basis of long-term agreements with Russian and CIS universities and companies headquartering in Dubna.

Attraction of Qualified Specialists whoRreside in Dubna and are Currently Employed elsewhere

As mentioned above, presently their number is accounted for 1,000–1,2000. According to expert estimates and sampling surveys, it is possible to employ up to 70% of them in organizations that form the group of potential residents of the special economic zone.

Attraction of Residents from the Neighboring Localities

An additional source of workforce for the town may become Taldomsky district of Moscow oblast, with some 3,000 local residents now daily commuting to Moscow for work.

Traditionally, local organizations of the town employ residents from Kimry and Konakovo districts of Tver oblast. Should new job opportunities arise, the number of those residing in contiguous localities and willing to work in the town would grow substantially.

Within a close reach from the town there are settlements of Taldom district of Moscow oblast (the town of Taldom, urban settlements Zaprudnya and Verbilki), Kimry district of Tver oblast (the town of Kimry) and Konakovo district of Tver oblast (the town of Konakovo).

The overall number of the population within 35-km.-long radius from Dubna is 140–160,000, including 60–70,000 able-bodied individuals.

Attraction of Specialists from Russia and Near Abroad

It is intended to do it in two ways:

- attraction of young specialists – up to 20% of the overall need by this category;
- attraction of qualified specialists that meet the employees' requirements through staff recruitment agencies or by employer organizations themselves – up to 80% of the overall need in cadres by this particular category.

Stages and Timelines of the Strategy Implementation

The timetable for development and the respective material and engineering equipping of the R&D special economic zone and the contiguous territory was designed for the period between 2006 and 2010 and provides for placement of facilities in operation in two stages:

1st stage: 30,000 sq.m. of production and office facilities, main objects of social infrastructure and 100,000 sq.m. of housing –until January 1, 2008;

2nd stage: 340,000 sq.m. of production and office facilities and 495,000 sq.m. of housing – until January 1, 2011.

Financing the Strategy Implementation

The volume of costs associated with the establishment of the special economic zone in Dubna accounts for RUR 26, 257.1 mln, of which 3,739.0 mln is planned to fund from the federal budget (including 1.949.0 mln to be spent between 2006–2008), 972.7 mln – from the Moscow oblast budget (including 673.7 mln between 2006–2008), 554.5 mln – from the local budget of the town of Dubna (including 484.4 mln over 2006–2008), and 20,991.0 mln – from extrabudgetary sources (including 10,375.o mln between 2006–08).

The volume of costs associated with the SEZ's functioning through the whole period of its existence and over the period between 2006 and 2008 (in parentheses) accounts for RUR 9,506. 5 (78.7) mln in current prices, including: at the expense of the federal budget – 49.4 (1.8) mln, at the expense of the Moscow oblast budget 3,442. 6 (56.3) mln, at the expense of the local budget of the town of Dubna – 2, 855.8 (20.6) mln, and at the expense of extrabudgetary funds – 3,158.7 (59.7) mln.

The total volume of costs associated with the creation and functioning of the special economic zone in the town of Dubna accounts for RUR 35,763.6 mn. (including 13, 290.0 mln over the period between 2006 and 2008), including: at the expense of the federal budget – 3,788.4 (1,950.8) mln, at the expense of the Moscow oblast budget 4,415.3. 6 (730) mln, at the expense of the local budget of the town of Dubna – 3,410.2 (505.0) mln, and at the expense of extrabudgetary funds – 24,149 (10,794.7) mln.

Monitoring and Control over the Strategy Implementation

It is suggested to exercise monitoring of the Strategy implementation using the following control indicators:

1. Developing the SEZ infrastructure and the territories contiguous to the SEZ:
    1. placement in operation of production facilities (in sq.m., by years);
    2. housing construction (in sq.m., by years);
    3. construction of the road network (in sq.m., annually);
    4. reconstruction and construction of principal engineering facilities;
    5. reconstruction and construction of main engineering nets.
2. Performance by the SEZ residents:
    6. jobs created (in units, annually);
    7. volume of production of goods, works and services (in current and adjusted prices, annually);
    8. volume of exported goods, works and services (in current prices, annually);
    9. volume of revenues to the budgetary system of the Russian Federation (in current prices, annually).

Residents of the Special Economic Zone in Moscow Oblast (SEZ "Dubna")

So far as IT activities are concerned, the pioneer resident in the Zone has become "Luksoft-Dubna" company founded by IBS group. In 2005, it delivered services worth a total of a. RUR 1 bn. The company is going to quintuple the volume of its output by 2011, particularly, due to the creation of a computer science center, which will be servicing Russia, US and EU, as well as *Boeing, Motorola*, and other public and private customers.

The SEZ resident “Dubna-Systema” will focus on development of ion-plasmic technologies and introduction of nanotechnologies to production of new materials.

(b) Special R&D Economic Zone “Zelenograd”

The first site of the zone is located within the territory of the industrial site ‘Alabushevo”. The area of the site is 150 hectares. The Moscow government approved the design of the zone’s planning. The design comprises plans of the functional, construction and landscape zoning, and land development documentation. Because of the zone’s creation, the layout needs to be completed and should provide answers to several main questions, specifically:

- development of missing design and estimate documentation;
- correction of borders of the natural complex within the zone;
- provision of new housing to current residents of the future zone’s territory;
- demolition of some engineering facilities and buildings, including housing;
- construction of engineering, transport, energy supply and other communications and recreational area within the zone.

It is intended to create 15,000 new jobs within the zone.

It is planned to create research, production, auxiliary and recreational zones within “Alabushevo” site. It has been agreed that the federal center and the city of Moscow would invest, in equal shares, RUR 10 bn in creation of the local infrastructure in “Alabushevo”, while research and production facilities should be built at the SEZ residents’ expense. “Alabushevo” is designated for the implementation of the full cycle of R&D operations, that is, from development of materials, technology, etc. to an actual manufacture and sales of sample lots of produce.

The other area of R&D SEZ “Zelenograd” is formed by the territory of the innovation complex of Moscow Institute for Electronics with a total area of 5.15 hectares.

The territory currently accommodates a modern university innovation complex, which comprises a business incubator, a R&D park, 2 innovation centers, a regional center for technology commercialization and transfer, a multi-profile experimental factory, 8 training and research complexes, 6 sectoral centers for collective use.

The construction of Russia's pioneer Technological Village is close to completion. TV provides a cutting-edge research and production infrastructure for developing, mastering, producing in small series and testing on the market new electronic and microelectronic items that meet international standards.

The headquarters and facilities of the Village are constructed in stages. This year, the construction of 9,500 sq.m. of areas designated for R&D operations. In December 2007, it is planned to place the whole complex in operation.

Within this particular site, residents of the zone will focus on independent research and development, technical and development works, and provision of research and technical services to institutions, enterprises and organizations, which would reside in "Zelenograd", in the following areas:

1. Development of production of modern domestic electronic component base;
2. Development of production of microsystems devices on the basis of modern technologies of deep silicon profiling;
3. Development of production of integral optics, optoelectronics, intellectual navigation and control devices;
4. Electronic instrument making on the basis of mastering of a through cycle of superprecise assembly of electronic equipment and devices;
5. Targeted incubation of start-up innovation companies by avenues critical for the SEZ advancement.

It is intended to have the federal budget and the Moscow city budget allocate RUR 460 mn. in equal shares to create the infrastructure of the site

Expert assessments showed that by the end of the operational life of R&D zone "Zelenograd (2005) its residents' performance will be characterized by the following indicators:

- the residents' aggregate proceeds should account for RUR 30 bn, while the number of employees – 15,000;
- the overall economic effect from the creation of the zone should account for a. RUR 30 bn;
- the flow-out of budget allocations should discontinue since the 7th year of the zone's existence;
- the balance of budgetary funds (the inflow of budgetary funds less their flow-out) should turn positive in the 12th year of its functioning.

In parallel, it is planned to address a series of social challenges, of which the following ones deserve a particular attention:

- a maximum level of capitalization on the intellectual, research and engineering and technological capacity generated in Zelenograd over previous 48 years of the town's existence;
- future advancement of research and engineering and production operations will be secured by production facilities;
- the zone will enable one to solve the problem of local residents' employment and the transportation problem (commuting back and forth between Moscow and Zelenograd).

Main Objectives of SEZ "Zelenograd"

The main objectives of the R&D special economic zone "Zelenograd" are:

- generation of basic breakthrough technologies that bear a multiplying effect and form the basis for development and production of high-tech goods, which should be competitive both on the domestic and international markets;
- creation of favorable conditions for attraction of domestic and foreign investment in local highly technological and science-intensive production;
- development of an innovation infrastructure, creation of conditions for a successful implementation by residents of technical and promotional operations;
- production development and technical re-equipping of local electronic production in order to attain the modern technological level;
- an efficient capitalization on the existing production capacity and improvement of the local enterprises' financial sustainability;
- maintenance and increase of the capacity associated with highly qualified research, engineering and workers' cadres on the basis of

their profile training and retraining at enterprises and educational and training institutions and centers;
- commercialization of the local organizations and enterprises' research outputs;
- growth in local employment, due to new job opportunities;
- improvement of labor conditions and growth in salaries and wages;
- expansion of the local tax base and greater volumes of payments to the federal budget and the Moscow city budget, and to the extrabudgetary funds.

On July 13, 2006, the zone welcomed its pioneer resident, namely, JSC "Zelenogradsky innovatsionno-tekhnicheskiy tsentr". The enterprise's profile embraces development and creation of the domestic electronic component base; microsystem and microelectrotechnical equipment; data and telecommunication systems; radio-electronic equipment of a new generation (strapdown navigation systems; biomedical diagnostic systems; optical positioning systems; hardware-in-the-loop signal processing modules, among others).

The enterprise also provides services in the area of innovation business, including certification, quality management, marketing, business planning, project evaluation, support of foreign trade, facilities lease, lease of technologies and modern equipment, particularly on the basis of collective-use centers.

The envisaged project implementation timeline is 2021. The envisaged aggregate volume of funding is RUR 1 bn, providing it is allocated by the company itself, the Russian Fund for Technological Development, the Federal Agency for Research and Innovation, the Fund for Support of Small Forms of Enterprises in the Research and Engineering Sphere, and from commercial customers' payments.

The planned aggregate proceeds from sales should make up over RUR 6 bn, the planned aggregate net profit – RUR 3.1 bn, while contributions to budget of all levels – no less than RUR 1.1 bn. The internal profitability rate of the project should be 68%. The project should ultimately generate no less than 430 additional jobs, with JSC ZITT being ready to secure some 6,000 sq.m. of office space to become home to the SEZ residents.

The next resident in the zone became privately owned "Alfachip Ltd", which specializes in manufacturing of superscale integrations. The company's founders have a 7-year record of a successful cooperation with Motorola's Department for Semiconductor Devices.

Superscale integrations form the basis of the modern electronic and computer, communication and home electronic equipment.

(c) Special Economic Zone in St. Petersburg

A special engineering and promotion economic zone, is under creation in St. Petersburg, in compliance with Federal Act of July 22, 2005, "On special economic zones in the Russian Federation" No. 116-FZ and Government Resolution of December 21, 2005, "On establishment in the territory of St. Petersburg of a special economic zone of the research and development type". The territory of the future zone is 200 hectares, and it covers Petrodvorets district (the "Noiedorf" territory ("Strelna" settlement) and Primorsky district (a territory to the north to Novo-Orlovsky park).

The zone is being created for the sake of localization of organization and science-intensive production and generation of conditions of their development, as well as fostering the rise of the service sector in the high-tech area.

In compliance with the noted Act "On special economic zones in the Russian Federation", the R&D activities are understood as manufacture and sales of research and engineering products and their completion up to the stage of their industrial use, including production, testing and sales of sample lots, as well as development of software, data collection, processing and transmission, distribution computation systems, and delivery of services with respect to promotion and servicing of such products and the system.

According to potential residents' applications, it is intended to develop within the CEZ software; communication means and home radio-electronic equipment; automated technical process control systems; military and civic avionics; medical equipment; development of analytical devices, and production of sample lots.

According to the noted Act, the SEZ is created for the term of 20 years, while its regime allows:

– to produce export and import goods, following simplified procedures and thanks to introduction of a special customs regime;

– to lower the uniform social tax at 12% (the lower tax rate will be 14% in the event a private individual's annual salary is under RUR 280,000; alternatively, it can be lowered even further, due to the tax base).

Residents of the St. Petersburg SEZ

The pioneers in the SEZ became JSC "Tranzas: and JSC "Tranzas Tekhnologii".

Established in 1990, the founder corporation of JSC "Tranzas" currently boasts the staff over 1,200 worldwide and is going to move its HQ to the special economic zone.

JSC "Tranzas" holds some 30–40% of the world market for electronic cartographic systems and electronic maps for navigation and has supplied its systems to border guards and navy of several dozens of countries, including Russia, the US, Sweden, Germany, India, UK, Chile, Peru, Columbia, to name a few.

By last year 75% of the Russian civic aircraft has been equipped with TAWS (Terrain Awareness and Warning System) Tranzas had developed in full compliance with the recently adopted new ICAO standards.

Table XII-3

Preferences for the St. Petersburg Special Economic Zone

Taxes	General conditions	Within the SEZ
Uniform social tax	26%	14%
Customs duties	As per the customs tariff rate	no
Land tax	Max. 1,5%	0%
Property tax	2,2%	0%
Transport tax	Max. 200 RUR	0 RUR
Corporate profit tax	24%	20%

(d) Special Economic Zones in the City of Tomsk

Tomsk oblast is well prepared for the establishment of a special economic zone in the territory of the city of Tomsk. The following facts form a convincing evidence:

Development of the engineering and promotional activities in the Oblast's territory appears fully consistent with priorities of its socio-economic development, with a key priority declared in the Tomsk Oblast Development Strategy up to 2020 being securing a sustainable development of the region and growth in the population's welfare through generation of competitive advantages in the area of research and advanced technologies and shaping a qualitatively new economy, which rest upon an advanced research and educational complex, along with fast growing high-tech companies which would secure production of goods and services with a high value-added.

The city of Tomsk has a great capacity, so far as an intense development of high-tech innovation business is concerned:

- a high level of elaboration of technical aspects of creation of the SEZ;
- the territory ready to accommodate the zone is located within the city borders, which ensures its proximity to the mature engineering, transport and social infrastructure of the oblast capital;
- capacities of the local construction complex allow an efficient implementation of a project in the part of construction of the engineering, transport and research and production spheres of the future zone.

A high degree of the region and municipality's financial and economic sustainability minimizes risks associated with the financial aspect of the project.

The following avenues, which are most critical for Russia's and the world economies, have been picked as the most promising ones from the perspective of research, production and staff capacity:

Information and Telecom, and Electronic Technologies

Represented by such subsectors as telecom, production of electronic and electrotechnical equipment, IT services, the local ITC sector is one of the most fast growing industries of the oblast economy. A number of local ITC companies are among leaders on the domestic market, and their output also enjoys demand on such fairly saturated markets, as the US, Germany, UK, Japan, South Korea, and in the CIS countries.

The record of implementation of projects in the area of data, telecom and electronic technologies evidences that Russian technologies are competitive on the world market and the level of the ICT designs is confirmed by the existing demand for the local organizations' research and output. Thus, in 2004–2005, RUR 1,221 mln was invested in research into ICT and electronics (including industrial and medical instrument making) at research departments of local universities, academic institutions and research organizations.

Every year, over 1,000 highly qualified specialists in ICT graduate from local universities. Praised for its quality, a high level of training at the local universities is attributed primarily to the fact that R&D activities form an integral part of their curricula. Specifically, such practice is common at three local universities, 13 research centers and institutes under the universities (the Research Institute for Automation and Electromechanics; the ones for electric communication systems; electronic systems; radiotechnical systems; electronic technological equipment and communication systems; nuclear physics; high voltages; introscopy, applied mathematics and mechanics, biology and biophysics; the Electro-engineering Center; the Siberian Physics and Engineering Center, the Cybernetic Center), as well as at three institutes and a department of TNTS SO of the Russian Academy of Sciences (the Institute for Optics of Atmosphere; the ones for physics of solidity and science of materials; monitoring of climatic and ecological systems; and the department for informatization.

New Materials and Nanotechnologies

The pace of advancement of this avenue of research in the Oblast has been great lately, which can be evidenced by a considerable rise in output, as well as in the number of research and international recognition of the local products. Thus, according to the annual survey held by the prestigious US journal R&D Magazine, locally produced metal nanopowders have made it for the list of the Top-100 best science-intensive products presented at the US market in 2000, while ceramic nanofiber of aluminum oxide repeated this success in 2002 (www.nrel.gov). In 2002, likewise, at the Russian-American Technology Showcase (Menlo Park, California, Silicon Valley, after the respective evaluation IBM ranked the locally developed technology of compacting ceramic nanomaterials as one of the best products. In 2004, the locally produced filtering material on the basis of glassmicrofiber was proclaimed Product of the Year at the NASA's STHOF.

As of today, organizations of the local research and educational complex have received over 46 grants under various programs run by domestic government agencies, the Academy of Science and international organizations, such as TACIS, and conduct research by more than 25 huge contracts, including those with overseas counterparts. In 2004–05, over RUR 518 mln was invested in local institutions' works on new materials and nanotechnologies.

In Tomsk, there is the oldest and largest research school that deals with new materials and nanotechnologies, while some 450 specialists of this particular profile graduate annually from the local universities. The joint educational and research complex "New materials and nanotechnologies" comprises the Institute for Physics of Solidity and Science of Materials (IPSSM) of the Siberian Branch of the Russian Academy of Sciences and respective departments of research institutes of the Tomsk Research Center of the Siberian Branch of the Russian Academy of Sciences, Tomsk State University (TSU), Tomsk Polytechnic University (TPU) and Tomsk State Architectural and Construction University, and the Siberian Physics and Engineering Institute under Tomsk State University. The IPSSM became home to affiliates of 1 chair of TPU and two – of TSU. Every year, local academic institutions hold internships for over 100 students from Tomsk universities who specialize in new materials.

Biotechnologies and Medical Technologies

The local biotechnological complex constitutes a well-developed educational, research and production base, which comprises research centers, universities, pharmaceutical and biotechnological factories, as well as industrial enterprises that operate in the sphere of innovation biotechnology. A distinguishing feature of the local biotechnological complex is close connections between fundamental research and concomitant applied research. Thanks to this, the oblast has advanced and excelled in key segments of the market for biotechnology.

The potential volume of output in the local biotechnological sector by 2020 should account for over USD 2.5 bn, while the average increment in output may make up 27.1%, which is considerably greater vis-a-vis forecasted international growth rates in this particular area.

As noted above, Tomsk oblast enjoys a great research and educational capacity in the area of biotechnology. The annual number of graduates in profile specialties from the largest universities accounts for 1,000, including those from:

- Tomsk polytechnic university: graduates in chemical technology and biotechnology; biomedical engineering; biotechnologies; biotechnical and medical equipment and systems; chemical technology of high-molecular compounds;
- Tomsk State University: graduates in agronomy; plants protection; biology; medical physics. In 2005, the University established a training and research center for biotechnology and bioengineering;
- Siberian State Medical University: graduates in pharmacy; medical biology; medical biophysics; medical cybernetics.

The territory of the Tomsk R&D special economic zone covers 2 separate lots located within the precincts of the city. Their total area is 197 hectares.

The first site is located in one of the city's blocs called "Akademgorodok", which is also home to the complex of research facilities of the Tomsk Research Center of the Siberian Branch of the Russian Academy of Sciences. It also includes a housing area and small cottage settlements. The area is surrounded by urban woods spreading east- and southwards. It is envisaged that the site will accommodate all the basic material and engineering infrastructure of the zone.

The other site is located in the northern part of the city, in the territory of a large production hub, which has a great capacity in terms of development and promotion of science-intensive production aimed at innovation technologies.

Both sites were selected with account of the SEZ residents' needs – closeness to infrastructure, engineering communications, transport net, which will have possibilities for further expansion. Plus, there is an unoccupied territory available for erection of buildings and facilities, as proved by engineering and geological examinations.

Additionally, in the territory of the zone between 2006 and 2008 at the expense of extrabudgetary funds there will be established a number of back-up organizations, whose mission will be delivery of an ample spectrum of services, including information and educational ones, to resident companies.

To simplify the access to the diverse innovation infrastructure of the zone and to lower the administrative burden on its residents, it is provided for a mandatory introduction of the “single-window” mechanism, which implies that an investor (entrepreneur) will interact with a single special management company. This mechanism will be implemented by delegating a series of powers to a federal agency of the executive power authorized to exercise the special economic zone management functions.

According to the RF Ministry for Economic Development and Trade, a. 90 large Russian and foreign companies have already submitted their resident applications. It is envisaged that by late-2010 the annual turnover of the Tomsk SEZ residents should reach a. RUR 13 bn, with the share of the IT-sector accounting for RUR 5 bn and that of the bioengineering and medical products – RUR 4 bn.

Projects and potential residents’ applications are subject to a fairly long and thorough scrutiny. The first resident became “Nauchno-issledovatelskaya organizatsia “Sibur-Tomskneftekhim Ltd.”, whose profile is development of titanium-magnesium catalysts and organization on their basis of a model production of ultrarhigh-molecular polyethylene with unique characteristics. The resident has invested in the construction and placement in operation of a unique experimental plant. The plant was designed thanks to contributions by leading specialists of “Tomskneftekhim” Ltd., JSC “Sibur” and the Institute for catalysis of the Siberian Branch of the Russian Academy of Sciences.

The pioneer resident was followed by the Moscow-based federal public unitary enterprise “Microgen”, “Mikran” Ltd, JSC “Elesi”, “Elekard” Ltd. The Ministry for Economic Development and Trade had informed earlier that over 90 companies, including such giants as Cisco Systems and AFK “Systema” were going to become residents as well.

It is also worth noting that Singapore-based JTC, which manages 38 local and overseas technoparks with 7,000 companies operating there, has expressed its interest in the Tomsk SEZ.

Overall costs of creation of the SEZ infrastructure should make up a. RUR 1.9 bn, with the federal budget providing 74%, the Tomsk oblast budget – 22%, and the Tomsk city budget – 4% of the a.m. amount of funding. By preliminary estimates, by late-2010 the annual turnover of the SEZ residents should reach RUR 13 bn, of which the share of IT-sector would account for a. RUR 5 bn and that of the bioengineering and medical products – 4 bn.

It is envisaged that the zone would generate over 10,000 jobs by 2015, and by 2025 revenues from its operations to the budgets of all levels would make up RUR 70–90 bn. With initial plans modified, the Tomsk R&D SEZ, along with the Lipetsk and Elabuga ones, will grant regional tax benefits to its residents for the term of 10 years.

3. Special Economic Zones of Industrial Type

(a) Special Economic Zone in the Town of Yelabuga

General Information of Special Economic Zone "Alabuga"

At their meeting on November 28, 2005, the tender commissions under the RF Ministry for Economic Development and Trade and the Federal Agency for Special Economic Zones Management of RF on selection of applications for creation of special economic zones of research and development and industrial types ruled to establish a special economic zone of the latter type in the territory of "Alabuga" industrial site (Yelabuga district, Tatarstan) with a total area of 20 sq.km.

The territory of Yelabuga district's and the town of Yelabuga's performance in terms of industrial output per capita is at 42.7% greater vis-a-vis the average index across the Republic of Tatarstan and 3.1 times superior to the average nationwide level.

The territorial economy's profile is the industrial sector, agriculture, education and tourism.

The territory of the "Alabuga" SEZ is situated near the town of Yelabuga and within 25 km. from the town of Naberezhnye Chelny and 40 km. – from Nizhnekamsk.

On January 18, 2006, the RF Government, the Government of the Republic of Tatarstan and municipal administrations of Yelabuga district and the town of Yelabuga signed an agreement on establishment of the "Alabuga" special economic zone of industrial type. It is envisaged that the first stage of the Zone will start functioning in late-2006.

The management body of the Zone will be the territorial branch of the Federal SEZ Management Agency. In compliance with the RF Government's Resolution of December 13, 2005, No. 758, an Act on the Supervisory Board of the Zone has been approved. The Board's mission will be to control compliance with the agreement on creation of the zone and budgetary funds allocated for development of its territory. As well, it will approve and consider perspective SEZ development plans. A local (Republican) management company will be selected on the basis of tender procedures. These structures will coordinate interaction with the SEZ residents.

Preferences Granted to Residents of "Alabuga" SEZ

1. Companies registered in the territory of the Zone will be granted a series of preferences. More specifically, those are the free customs zone regime, under which foreign equipment is placed and used within the Zone without paying customs duties and VAT; abolition of export duties on exportation of locally manufactured goods. Resident companies are exempt from property tax since the moment of registration of their assets and from land tax from the moment the property right for a given site arises. In addition, Tatarstan has provided for special regional benefits for the SEZ resident companies: more specifically, the corporate profit tax rate has been lowered at 20%, and they are fully exempt from transport tax subject to collection to the Republic's budget.

Table XII-4

Main Preferences Granted to Residents of "Alabuga" SEZ

Tax	Tax rate (%)	Distribution across budgets (%)		
		Federal	Regional	Municipal
1. Corporate profit tax	24	6.5	17.5	-
For the SEZ residents	20	6.5	13.5	-
2. Property tax	2,2	-	1.1	1.1
For the SEZ residents (for 10 years)	0	-	0	0
3. Land tax 1.5%	-	-	1.5	
For the SEZ residents	0	-	-	0
4. Transport tax		Depending on the kind of vehicle and capacity of its engine	-	Depending on the kind of vehicle and capacity of its engine
For the SEZ residents	0	-	0	-

2. So far as their own fixed capital is concerned, corporate taxpayers that have obtained the SEZ resident status at “Alabuga” enjoy the right to apply a special coefficient to the basic depreciation norm, but not greater than 2.

3. Costs of R&D works (including those that fail to bring about positive outcomes) completed by the corporate taxpayers registered and operating in territories of special economic zones established in compliance with the RF law are recognized as equaling the amount of actual costs incurred during the reported (fiscal) period.

4. There are no restrictions with regard to the transfer of losses the “Alabuga” corporate residents reported over a previous fiscal period.

5. The procedures of registration of documentation on exercise of operations in the territory of “Alabuga” SEZ with the territorial branch of the Federal SEZ Management Agency imply the single window principle.

6. Presently the federal center and Tatarstan have provided funding for construction of the necessary infrastructure in the territory of “Alabuga” SEZ (20 sq. km.), including electric and heating supply systems, natural gas pipeline, an up-to-date telecommunication network, a customs office and a warehouse facility for temporary storage of customs cargo. These facilities should allow a considerable time saving on and minimization of costs of import-export cargo processing .

Registration of the SEZ Residents

To obtain the status of the SEZ resident, a company has to register itself in the territory of Elabuga district, sign an agreement with the SEZ management agency on conducting industrial and engineering operations and invest at least Euro 10 mln in its own production assets located in the zone, including 1 mln – in the first operational year.

The Zone in question is of a particular interest to foreign and domestic investors, as it can warrant competitive advantages associated to the following factors:

1. Tax and customs benefits.
2. Investors need not spend money on creation of costly communications, because all the necessary engineering infrastructure is already there: electricity and heating systems, a water purification plant, a natural gas pipeline, a railroad, a container terminal where 40-feet containers can be handled, an up-to-date telecommunica-

tion network equipped by “Alcatel” devices; plus, there is a customs office and a warehouse facility for temporary storage of customs cargo, which allow substantial time and costs saving, so far as processing and handling of import and export cargo are concerned.

3. In the territory of the zone there also are buildings and facilities at different stages of completion, which can be mobilized, at minimum costs and fairly promptly, to accommodate new production.
4. The region boasts qualified workforce and specialists with an employment record with companies with foreign investment; there also is a training center for their professional training.
5. At the industrial site, there is a team of managers and specialists in possession of necessary expertise in such areas as law, economics, negotiating skills available upright to help investors with development and implementation of investment projects.
6. The zone is conveniently located in the heart of Russia, close to highway M7 (Moscow – Nizhny Novgorod – Kazan – Ufa – Ekaterinburg), with an access to railroad, air- and water transportation hubs, which generates appropriate conditions of organization of an efficient logistics.

Residents of “Alabuga” Zone

To begin with, suffice it to mention JSC “Severstal-Avto”. Established in cooperation with FIAT, the company has invested RUR 4.4 bn in production of commercial vehicles, which would generate 1,700 jobs. The plant should be completely operational by March 2007. Additionally, the company focuses on another separate project, that is, construction of a plant with an annual output of 100,000 diesel engines.

Tarastan is currently negotiating with 30 domestic and foreign companies to become the zone’s residents. Potential residents’ plans are associated mostly with production of components for the automobile sector, and the Republic seems to be in full consent, as its leadership is keen to form an automobile cluster there. An additional benefit for potential investors in the automobile components production is that Tatarstan’s profile is deep oil refining and petrochemical production.

It is also planned to have the zone become home to “non-profile” agents, such as, for instance, companies operating in the light industry and construction sector.

(b) A special economic zone of industrial type in Lipetsk oblast

In compliance with Federal Act "On special economic zones" of July 22, 2005, No. 116-FZ, with its Resolution of December 12, 2005, No. 782, the RF Government ruled to establish in the territory of Lipetsk oblast a special economic zone of industrial type with the total area of 10 sq. km. It is planned that the first stage of the Zone will begin its operations in the 2nd quarter 2007.

This particular zone is established to foster manufacturing sectors, high-tech industries and production of new kinds of goods.

Its creation is regulated by the following main conditions:

- the term of its existence is 20 years;
- an investment project should imply capital investment of at least Euro 10 mln in RUR equivalent (with at least Euro 1 mn. invested within a year upon conclusion of the respective agreement) by the Bank of Russia's exchange rate;
- creation of the local engineering, transport and social infrastructure is funded from the federal budget and that of Lipetsk oblast, and from other sources;
- residents of the Zone will enjoy a government support.

Residents of "Kazinka" SEZ

- Bioethanol Ltd.: creation of an enterprise on wasteless production of bioethanol, with f RUR 2.8 bn invested in its establishment;
- Belon-Metakom Ltd.: production of sandwich panels and metal constructions, with the volume of investment totaling RUR 522mln;
- JSC "Saist-Lyuve" (Italy): manufacturing of assembly parts for refrigerating equipment, with the volume of investment totaling RUR 380 mln;
- CHSZ-Lipetsk Ltd.: construction of a plant to produce light glass tare fro the food-processing, chemical and medical industries, with the volume of investment totaling RUR 1.3-plus bn.

Enterprises that have confirmed their participation in the SEZ as its residents

- METR S.p.A – production of rotors and stators of electric engines;
- VERGOKAN – production of tote boxes;
- SIGNODE SYSTEM GMBH – production of packing systems with the use of steel band;
- Viterie Italia Cetrale – production of fastenings;

- EKINLER ELEKTRONIK – production of electric cables;
- Компания “BEEPLAST” – production of plastic assembly parts for home appliances;
- CIAMAGLIA – furniture production;
- INDESIT COMPANI – production of gas ovens and assembly parts for refrigerators and laundry washers;
- Electrolux – production of laundry washers;
- SEST – production of evaporators for refrigerated counters and windows;
- Pro-mould – production of rigging for manufacturing of plastic items;
- VERNIGLASS – production of glass gods;
- Elektrowerkzeuge – production of electric instruments;
- Odenwald Faserplattenwerk GmbH – production mineral fibre plates;
- B/S/H Bosch und Siemens Hausgerate GmbH – production of automobile spare parts, diagnostic equipment and electric instruments, home appliances, security systems and industrial equipment;
- Siemens GmbH – production of advanced equipment;
- Akzo Nobel – production of medicines, coatings and chemicals;
- Sisu Diesel – production of internal-combustion engines;
- Bundy Refrigeration – production of evaporators, condensers and other liquid-expansion cooling systems for refrigerators and home appliances.

Lipetsk oblast lately has been a donor to the federal budget and experts rank it as a region with the development level above average. Fitch Ratings Ltd. granted it a high credit rating and so did domestic rating agencies. It was the first Russia’s region to win Fitch’s national rating, which means it has displayed a good budgetary performance, absence of debt, a high credit capacity, and a sufficient degree of transparency of the economy and financial reporting. The experts also paid a special attention to the fact that the aggregate volume of foreign investment into the local economy had already exceeded indicators of its consolidated budget, which puts the Oblast even ahead of famous for the scale of its business Moscow. In Lipetsk oblast, the average annual increment of investment in fixed capital is 20%.

The SEZ territory of 1,027 hectares has practically all the necessary infrastructure: a local railroad, spur-tracks, an electric power plant, high-pressure gas pipelines, sewage facilities, while additional objects, such as engineering nets, water supply, canalization, substation transformers should be built shortly. The construction works are funded from the federal and region's budgets, which makes the territory increasingly attractive to private investors. However, in return they have to meet a number of conditions – thus, OEZ may not accommodate low-technology and environmentally aggressive production, nor there should be located mineral production and processing, housing or production and processing of excised goods (except for passenger cars and motorcycles).

In 2006 alone the volume of the project financing from the federal and regional sources was a. RUR 500 mln; it should consequently grow up to 1.7 bn in 2007 and make up 1.5 bn in 2008. According to some forecasts, the project implementation would allow attraction of some RUR 30 bn in investment (8.7 bn at the first stage, scheduled for 2006–08 and some 21 bn – at the second stage (2009–12).

According to some computations, the volume of the SEZ's output should become worth a total of RUR 11 bn by 2008 and 50 bn – by 2012. The zone should help create 12,000–13,000 jobs and attract over 50 different companies that produce home appliances and agricultural equipment, electronics and biofuel. These should help the zone avoid the trap of turning into a monostructural one.

SEZ will make higher demands of the professional level of its staff. With its 22 universities, 27 engineering high schools and 20, 500 students, it goes without saying that the Oblast displays a great capacity in this regard, however, even today some local companies complain of falling short of qualified workers, engineers and managers, while the local educational institutions so far have failed to supply specialists with an adequate level of expertise. It is envisaged that at the first stage the help will come from Italians, however the situation necessitates a comprehensive public staff training program, which should be built with account of SEZ needs, otherwise the regional labor market will experience imbalances, whichwill generate challenges to the SEZ.

4. Tourist and Recreational Special Economic Zones

Two Federal Acts: No. 76-FZ and 75-FZ of June 3, 2006, took effect as of July 9, 2006. The former Act modified provisions of Federal Act of July 22, 2005, No. 116-FZ "On special economic zones in the Russian Federation" (hereinafter referred to as Act No. 116-FZ). The respective modifications introduced a new type of special economic zones, that is, tourist and recreational special economic zones, the purpose of creation of which is development of and an efficient capitalization on national tourist resources. Act No. 75-FZ complemented some chapters of the Tax Code of RF by setting tax benefits for residents of such SEZs.

According to the RF Government Resolution, tourist and recreational zones are established for the term of 20 years. By contrast to industrial and R&D zones, they can be located in the territory of several municipalities and fully embrace parts of a city, district, oblast or krai. Plus, they can be established not only on publicly or municipally owned sites, but on the land owned by private individuals or legal entities. Furthermore, the sites that form such a zone can fall under the category of specially protected territories. Within such zones there can also be located objects owned by the government, municipality and private individuals, as well as housing objects.

To create a tourist and recreational zone, an RF Subject and a municipality (-ies) pretending to take part in a tender should submit a respective application to the RF Ministry for Economic Development and Trade. Procedures of completion and submission of such applications were approved by the RF Government with its Resolution of September 13, 2005, No. 564.

Concomitant with the application, the following documents should also be submitted: an accompanying letter drafted by a special form approved in compliance with Annex No. 1 to Resolution No. 564; and other documents enumerated in p.13 of the noted Resolution. Each applicant has a right to submit one or several applications, each of them complemented by a separate set of documents. The application and the concomitant documents are submitted in two copies.

Individual entrepreneurs and commercial organizations (except for unitary enterprises) may become residents of such zones. To this effect, they need to register themselves in the territory of the municipal entity in the borders of which the SEZ is located and to conclude with the SEZ management agency an agreement on exercise of tourism and recreational activities (below referred to as Agreement).

In compliance with p. 5.3.1. of Resolution of the RF Government of August 19, 2005, No. 530, SEZs are managed by the Federal SEZ Management Agency and its territorial branches.

The subject of the Agreement is mutual obligations of the SEZ resident and the SEZ management bodies. While the former assumes obligations to carry out in the SEZ territory tourist and recreational activities as per the Agreement, the SEZ management body assumes the obligation to conclude with the resident a land lease contract which concerns the site located within the SEZ territory and a lease contract on public or municipal property necessary for the exercise of activities by the SEZ resident.

Tourist and recreational activities are understood as operations on construction, reconstruction and maintenance of facilities designated for provision of sanatorium and rehabilitation services to citizens, as well as tourist activities and operations on development of entrails of mineral water, therapeutic muds and other natural therapeutic resources, their extraction and application, including activities with regard to sanatorium and rehabilitation treatment and preventive health care, medical rehabilitation, organization of citizens' vacations, and the industrial bottling of mineral water (p. 2.1. Art. 10 Act No. 116-FZ).

It is banned to delegate rights and obligations under the agreement to any third party. There also exist a number of effective bans on operations with the leased site. Thus, the leasing rights cannot be used as collateral, a contribution to the authorized capital, share in the production cooperative and it is prohibited to reassume rights and obligations under a given leasing agreement, including sub-lease of the site or its gratuitous use over a fixed time.

In compliance with Aprt. 31.2. of the noted Act, an entity willing to obtain the status of the SEZ resident, has to submit to the SEZ management agency an application for conclusion of the agreement which should contain the following data:

- on intended operations;
- on the area of the operational site;
- on the government and/or municipal property.

The applications should be submitted along with:

- a copy of the state registration certificate;
- a copy of the taxpayer registration certificate;
- copies of founding documents (for legal entities);
- business plan by a statutory form;
- an endorsement of the submitted business plan by a bank or a credit institution;
- other statutory documents for exercise of the tourist and recreational activities.

Within 10 days since the day of receipt of the documents, the SEZ management bodies make a decision and either notify the applicant of their approval of his business plan and of conclusion of the Agreement, or forward him a reasoned refusal to conclude the Agreement, which can be appealed in the court of law.

If there are no reasons to drop the application, the Agreement is made within 10 days since the day of approval of the respective decision.

An individual entrepreneur or a commercial organization is granted the status of the SEZ resident upon introduction of the respective entry into the register of the SEZ residents. Such an entry the SEZ management bodies make within three days upon signing of the Agreement.

The resident consequently has to submit to the SEZ management body for examination the project documentation necessary for realization of the business plan. The examination is conducted by authorized public executive agencies within 45 days upon submission of all the necessary documents. The examination is made at the applicant's expense.

Should the SEZ resident fail to honor conditions of the Agreement, the court of law can cancel that on the SEZ management bodies' request. More specifically, the court of law can cancel the Agreement in the event:

- the SEZ resident fails to meet set by the Agreement timelines with regard to submission for examination and approval of design documentation;
- he fails to secure capital investment in a volume and until the deadline, as per the Agreement;
- he conducts in the SEZ entrepreneurial operations that are not stipulated in the Agreement.

Furthermore, the court of law may cancel the Agreement in the event there is a negative aggregate expert conclusion on the design documentation, if the applicant fails to elaborate it and submit for a second evaluation in a reasonable time.

If the SEZ management bodies refuse to conclude a land lease agreement and/or an agreement on the lease pf public or municipal real estate, the SEZ resident has a right to appeal to the court with a request to cancel the Agreement or to force the counterparts to conclude the noted agreements.

The Agreement may also designate other acts by the parties, which they can recognize as a substantial violation of its provisions and which can constitute a reason for its cancellation.

In the event of an early cancellation of the Agreement through the SEZ resident's fault, the latter is bound to pay a penalty in the amount, as per the Agreement.

In addition to the reasons of the cancellation of the Agreement by the court of law, Act No. 116-FZ enumerates other reasons for its determination:

- its termination;
- cancellation by the parties' consent;
- termination of the land lease agreement (except for such a cancellation is a result of its redemption);
- deprivation of the SEZ resident of his status, because of his breach of the law;
- an early termination of the SEZ's existence.

Once the Agreement is terminated, the entity (individual) looses the status of the SEZ resident, while land and public and municipal real estate lease agreements are terminated, too.

In compliance with the Tax Code of RF modified by Law No. 75-FZ, residents of the tourist and recreational SEZ are granted additional guarantees and tax benefits. Thus, so far as corporate profit tax is concerned, they are entitled for:

- application to their own depreciated fixed capital units of a special coefficient added to the basic depreciation norm (but not greater than 2), that is, an accelerated depreciation (par. 4. p. 7 Art. 259 of TC of RF);

- recognition of costs of R&D works (including those that fail to bring about positive outcomes) in the reported (fiscal) when they were at the amount of actual costs (par. 4 p.2 Art. 262 of TC of RF);
- shifting the loss of the preceding fiscal period onto the current year in a full volume (while for other taxpayers it is set that the total sum of thus shifted loss in 2006 may not exceed 50% of the tax base calculated in compliance with Art. 274 of TC of RF (par. 4 p.2 .Art. 283 of TC of RF);
- lower corporate profit tax rate collectable to budgets of the RF Subjects and set by the respective regional acts; specifically, the RF Subject can lower the current 17.5% rate to the minimum 13.5% (Art. 284 of TC of RF).

Such benefits became effective as of July 9, 2006. In addition, since January 1, 2007, the SEZ residents were granted another benefit that concerns the property tax (exemption from it for the period of 5 years from the moment of registration of the property) (p. 17. Art.381 of TC of RF) with respect to the property:

- accounting in the balance sheet of an organization residing in the SEZ;
- created or purchased for the sake of conducting operations in the SEZ territory;
- located on the said territory.

These conditions should be complied with simultaneously.

As well, since 2007 SEZ residents will be exempt form land tax over the period of 5 years from the moment the property right for the site located in the territory of a given SEZ arises (p. 9 Art. 395 of TC of RF).

The territory of a tourist and recreational zone is subject to a special customs regime, that is, the free customs zone one. The regime is regulated by provisions of Art. 37 of Act No. 116-FZ, and it remains effective through the whole period of the zone's existence.

Only the goods that are placed in the territory of the zone and used by residents to conduct their operations may be placed under this particular customs regime.

The goods can be imported from the rest of Russia's territory, overseas or purchased in the SEZ territory from non-resident entities. Residents can use the goods at their discretion, except for operations the list of which will be approved by the RF Government.

Foreign goods imported into the territory of a tourist and recreational zone are exempt from import customs duties and VAT. In addition, the importation of goods into such a zone is not subject to restrictions and bans of economic nature provided for by the law on the government regulation of foreign trade.

Russian goods imported into the territory of a SEZ are likewise exempt from customs duties, while the VAT rate is zero.

Should the resident ship foreign goods from the territory of tourist and recreational zones to the rest of Russia, he is bound to pay customs duties, VAT and excise taxes. Russian goods in equal situation are exempt from customs duties.

While exporting foreign and Russian goods from the said territory to any location outside Russia, the exporter will have to pay only export customs duties.

Plus, in compliance with Art.38 of Act No. 116-FZ, during the whole period of effect of the Agreement, the government may not introduce any legal acts that may affect the SEZ residents' situation.

With its Decree of July 31, 2006, No. 212, the RF Ministry for Economic Development and Trade announced an open tender on selection of applications for creation of special economic zones of tourist and recreational type. The tender was held in 2006. The tender commission picked winners basing on an aggregate weighted score granted to every respective application with account of criteria set by the Act on conduct of a tender on selection of applications for creation of special economic zones the RF Government had approved earlier with its Resolution of September 13, 2005, No. 563.

The tender commission opened envelopes at its meeting on September 26, 2006. The commission ruled to let 18 applications run for approval, while another ten applications were declined as they failed to meet requirements to the tender documentation (the absence of a positive conclusion of the public environmental office, or a concomitant letter, or calculations by volumes of budgets of all the levels of the budgetary system of RF, and even minor failures to complete the territorial planning documents).

The applications were considered and evaluated by members of an expert council established under the tender commission in compliance with the Act on expert council approved by the Decree of the RF Ministry for Economic Development and Trade. The expert council was formed by representatives of ministries and agencies concerned, leading educational and research institutions, the RF Chamber of Trade and Industry, the Russian Union of Industrialists and Entrepreneurs, and business community.

The tender commission consequently convened twice, on November 23, 2006, and December 6, 2006, to select applications for creation of tourist and recreational zones and nominate the winners. Those became the applications with the highest marks by the aggregate weighted score, which is computed following requirements to the tender documentation.

The tender commission members agreed with the expert council's conclusions and nominated victors: those became applications submitted by administrations of Krasnodar krai, Stavropol krai, Irkutsk oblast, Republic of Buryatia, Altay krai, the government of Altay Republic, and Kaliningrad oblast. The commission acknowledged that these projects appeared the most interesting, conceptually elaborated and aimed at the comprehensive development of the tourist and recreational capacity of individual areas in RF.

The analysis of the submitted projects allows their "soft profiling": specifically, Irkutsk oblast will develop mostly business tourism, Republic of Buryatia – mountain-skiing and ecological tourism, Altay krai – water-, skiing-, recreational and speleo- tourism, while Altay Republic – mountain skiing and rehabilitation tourism. Establishment of tourist and recreational zones in Krasnodar krai and Kaliningrad oblast is aimed at developing sea resorts, while that in Stavropol krai – at creating recreational tourism with local balneological facilities.

Hence, the final list of regions and zones approved by the commission:

1. Altay krai – "Buryuzovaya Katun"SEZ;
2. Irkutsk oblast – SEZ in the precincts of Listvyanka settlement;
3. Republic of Buryatia – "Baikal" SEZ;
4. Altay Republic – a local SEZ;
5. Krasnodar Krai – a local SEZ;
6. Stavoropol krai – "Kavkazskiye Mineralnye Vody" SEZ;
7. Kalinigrad oblast – "Kurshskaya kosa" SEZ.

Establishment of tourist and recreational zones should give an impulse to development of the national resort and tourist industry, which recently has been on the decline. The world experiences evidence that tourism is able to mobilize colossal revenues to a national budget.

Yet Russia so far has not been able to have the pace of progress of its tourist sector catch up with other countries. This is often explained by the absence of necessary infrastructure and a low level of services against high prices, among other reasons. The tourist and recreational zones are expected to regalvanize this profitable business. Such zones should attract investors by means of preferences (primarily tax benefits) and generate favorable conditions and provide competitive advantages for the attraction of mass tourism.

By contrast to industrial and R&D zones, tourism and recreational zones should become of a particular interest to small- and medium-sized companies, for business therein is associated with the services sector.

According to the RF Ministry for Economic Development and Trade, until 2026 the federal center should spend on tourism and recreational zones RUR 44.5 bn, while business invest over RUR 270 bn. The zones should generate nearly RUR 260 bn in revenues. It is envisaged that the number of tourists visiting these territories should grow from 3 mln up to 9.7 mn. Already by 2016 the proportion of the tourist sector in GDP should grow from nearly zero up to 2% and with account of the multiplicative effect – up to 9%.

After the mechanism of creation of tourism zones has been worked out completely, the government should hold yet another tender on creation of tourist zones. However, Mr. Gref asserts it is not going to happen earlier than in 2 years.

(a) Special economic zone “Biryuzovaya Katun”.

The territory of the zone is situated on the left bank of Katun river, close to Krasny Kamen mountain. In its 32.3 hectare area the zone includes alpine meadows, mixed woods and a mountainous landscape.

The establishment of the zone constitutes the first stage of the formation of an organizational and economic environment for the creation and functioning in Altay krai of a tourist and recreational complex focused on a maximum capitalization on the local natural resources and peculiarities. The complex embraces territories of four districts of the krai, including precincts of the resort town of federal significance "Belokurikha" with the population of 92,000. The envisaged volume of investment should reach RUR 37.8 bn.

The complex promises to become unique, because of a series of economic and balneological factors and advantages, such as:

1. A great diversity of natural landscapes; the presence of water objects; the average annual air temperature +5° C; the height of snow blanket between 400 and 600 mm.; the number of sunny days a year no less than 235. All this creates conditions for an all-the-year-round provision of various combinations of tourist and recreational services;
2. Unique natural and medical and hydro-mineral resources, that is, ionized air, curative and drinking mineral water, and coniferous woods;
3. Esthetic and recreational value of the territory and tourist objects, including:
   - over 5,000 historical objects (archeological, architectural ones), museums, and traditional crafts;
   - natural complexes: suitable for rafting and swimming mountainous rivers, fishing and hunting areas.
4. Possibilities to organize versatile tourist routes of various categories of complexity: subwater and natural tourism, fishing and hunting, environmental, cultural and water (rafting, canoe and kayak), sports (mountain climbing), curative (climatotherapy, landscapotherapy), excursion (foot, horseback riding, skiing), tourism, mountain skiing, and speleotoursim.

With its two rivers suitable for rafting, Altay is very famous among water tourists, and the krai regularly hosts international tournaments in this kind of sports.

The krai is equally famous for its caves, which range from relatively shallow to a few deepest ones (340 m-deep and up to 2,500 m-long: these are "Geophysical", "Ecological" and "Altay" caves).

The krai also boasts an advanced tourist and recreational infrastructure. There are 126 local tourist agencies – their number has doubled vis-à-vis 2001. The number of tourist bases and other facilities has tripled since then and displays a clear trend to further growth. The number of beds accounted for 14,300 in 2005. There are some 8,000 local residents employed in the tourist sector.

The creation of the special economic zone should result in integration of local natural, rehabilitation and cultural and historic resources.

The concept for development of the special economic zone suggests two stages, of which “Biryuzovaya Katun” forms the first one.

At the second stage, it is intended to create in the krai a special enclave in the form of a resort and rehabilitation area formed by four districts: Charyshsky, Soloneshensky, Smolensky, Altaysky, and the resort town of Belokurikha.

It is intended to create the zone at the expense of all the sources of financing, with the total amount of funding of RUR 10.47 bn through 2026. Of the noted amount 6.93 bn should be allocated from the federal budget, 0.08 bn – from the local budget, and 3.16 bn – from extrabugetary sources. The budget funds should be spent on enhancement of the engineering infrastructure (a high-voltage line, a gas pipeline, a highway, a bridge passage, outdoor water-supply facilities, sewage facilities and canalization, communication facilities, and reconstruction of airports). It is planned to develop a wayside services infrastructure, too.

It is envisaged that main large residents of the zone should become JSC “Intourist” (Moscow), “Altay-Izvest” Ltd, “ANTE” Ltd.

By experts’ estimates, the tax revenues to budgets of all levels should grow up to RUR 31.7 bn by 2026, while the number of tourists should make up 1.1 mln.

The zone should create 3,000 jobs and with account of multiplicative effect in the supplier and consumer sectors – up to 7,000 jobs.

(b) Special economic zone in the territory of “Listvyanka” settlement

The concept of development of tourism in Irkutsk oblast suggests creation by 2026 a competitive world-class all-the-year-round resort for different segments of tourists from Russia, CIS and Europe on Baikal’s shore and mountainous areas near Listvyanka settlement (Irkutsk district).

It is intended to develop the resort by analogy with international ones. The project has been evaluated and received a positive conclusion by Ecosign (Canada).

The recreational capacity of the area is characterized by relatively favorable climate; there is a reservoir and an access to Baikal, which forms a prerequisite for development of various kinds of water tourism. A rich fauna of Baikal and its coastal areas, rare and endangered plants, affluence of natural (capes, rocks, caves, islands, etc.), as well as historical and cultural attractions, diverse hydro-mineral resources allows formation of a great (1,818.1 Thousand man-days annually) tourist and recreational capacity.

In Irkutsk district, there is a great number of resort bases, rehabilitation centers, tourist bases (a. 40), therapeutic and sports and rehabilitation institutions for children (a. 16), yacht clubs, bicycle and ski bases (a. 8). There also is a popular museum complex “Taltsy”. A part of the territory of the district is included in the “Pribaykalsky” national park; there also is the Kochegartsky sbale preserve of regional significance.

The settlement of Listvyanka is a cozy coastal resort area with the constant population of 1,5000. It is situated within 66 km. southeast to the city of Irkutsk and the head of Angara river, on a 5-km.-long coast of Baikal. A high-quality highway connects the settlement with Irkutsk. Presently Listvyanka functions as a summer coastal resort, and there are hotels, beaches and piers for pleasure and tourist boats there. The settlement boasts an arts gallery, the Baikal Limnologist Museum, a church, and an observatory.

The mountainous relief around the settlement is formed mostly by more than 700 m.-high mountain ridges that run northwards. The average gradient of their north-western flanks vary from 18 to 23%, thus making them ideal for mountain skiing and snowboarding. These relatively small mountains with 300-meter overfalls between them can form a basis for construction of a system of mountain-skiing routes and hoists, which can be simultaneously used by up to 4,000 tourists.

The upper part of the Krestovka river valley has a sufficient (a. 200 hectares) area to build a resort settlement infrastructure there – a complex of living, public and multi-purpose facilities, parking lots, highways and footpaths, which would ensure a daily presence at the resort of a number of tourists necessary to keep the routes and hoists busy. The area by the foot of the ridges is considerably greater than the size of a basic territory necessary for keeping a mountain-skiing center of such a scale occupied.

Should such a zone be created, it would allow not only a greater popularity of the existing in the oblast excursion, sanatorium and resort, recreational and mountain-skiing tourism, but a considerable improvement of the quality of the respective services and development of new kinds of tourism. That would boost the economic efficiency of tourism in the region, particularly by reducing seasonality, and turn the area into an international multi-profile all-the-year-round resort.

It is planned to build tourist objects in the territory of the zone in two stages: between 2007 and 2013 and 2017–2021, respectively. The construction should start on January 1, 2007. As construction is going to take 1-2 years on average, the zone will begin functioning in 2008.

While designing the plan of development of services with regard to accommodation of tourists in the zone, its authors examined relevant international experiences and that of the all-the-year-round Whistler resort (British Columbia, Canada) in particular.

Experts found out that the servicing of 1 mln of tourists annually necessitates building some 45–60 public catering objects with an average capacity of 50–100 seats. Such a need for catering facilities is explained by the fact that local hotels have their own restaurants that render their services to a considerable part of their guests.

It is intended to build 45 public catering objects, including 8 restaurants, 10 cafes and bars, 27 cafeterias and fast-food restaurants. The latter two would offer quality food at a relatively low price. They should be located in the main points of tourists concentration, that is: by the foot of the mountain and in the central part of the zone. It is envisaged that restaurants in the zone would offer different cuisines, including the national, European, Japanese and Asian. While one restaurant is to be located on the top of the mountain, two should be located by its foot and another five – in the central part of the zone. Restaurant should differ in terms of price categories, with that atop of the mountain being the most expensive one and offering, in addition to *haute cuisine,* a breathtaking panorama of Baikal. The other seven restaurants would be reasonably priced. One of the restaurants located in the central part of the town would be 3-storey building to host banquets and other functions.

The cafes would be situated in the central part of the zone and in the territory of the mountain-skiing complex.

The construction of the public catering objects likewise is planned to be completed in two stages, that is, between 2007 and 2012 and 2017–20. An analogous trend is noted in the dynamic of construction works at Whistler.

Irkutsk oblast is reach with mineral water – mineral-water wells outnumber 230 there. The local mineral waters allow treatment of a fairly comprehensive list of illnesses. By today 24 entrails have been found; in addition, there has also been found a great number of promising signs of the presence of mineral waters.

In the future, it is planned to develop, extract and bottle unique therapeutic mineral waters from the Munoksky deposit in Kazachinsky-Lensky district (an analogue to Matsesta resort in Sochi), “Natka” deposit in Tulunsk district and Nukutsky Matsesta (Ust-Ordynsky autonomous Buryatsky okru), and to build a balneological facility in the city of Irkutsk, among others.

In Olkhonsky district, there is Shara-Nur lake with therapeutic mud (very popular among local residents). It is necessary to examine the composition of the mud, its stock and balneological features. Ust-Kutsky district also has deposits of similar mud, which is widely applied by the regional resorts and sanatoria.

One of perspective avenues of the production of therapeutic mineral resources is extraction and bottling of the Baikal water from the depths of 500 and 1,700 m. The water from Baikal is famous as a model of purity and quality, and it has a positive influence on the human organism (the oxygen rate in the Baikal water is 12 mg/l, while its pH value equals to that of the human body).

Presently the bottling plant operates in Listvyanka settlement and two more plants are planned for constriction. Their daily output should be a. J1 ml., and each plant should cost a. USD 35 mln.

It is envisaged that the zone will be created at the expense of all the sources of financing, which should total RUR 15.04 bn until 2026. The federal budget should invest RUR 2.56 bn., the RF Subject’s one – 1.94 bn, the local budget – 0.22 bn, while extrabudgetary funds – 10.32 bn. It is planned to invest the budgetary funds in the construction of engineering infrastructure objects (a highway, communal and communication objects).

It is envisaged that the group of principal large residents of the zone will be formed by: the "Baikal Visa" association, "Grand Baikal" Ltd., JSC "Rosso Group", Nangtoon Company (China), "Impex" Ltd., "Real Group" Ltd, "Snowland" Ltd., "Gelion" Ltd., the "Russian mountain-skiing school" children's sports school, "The national trust for preservation and development of national landscapes", and "Erlinhot Company" (China).

Some experts estimate RUR 41.52 bn in tax revenues to the budgets of all levels by 2026, while the number of tourists to the zone should reach 1.0 mln. It is hoped that the zone should generate 17,000 new jobs and, with account of the multiplicative effect in the supplier/consumer sectors, – 41,000 ones.

(c) Special economic zone "Baikal"

To select a territory suitable for a tourist and recreational special economic zone in the Republic of Buryatia the local government hired JSC "Ektis" (Russia) and Ecosign Mountain Resort Planners Ltd., a renown international expert team in the area of design of mountain-skiing resorts.

Ecosign is headquartered in Whistler, B.C. (Canada) and has contributed to the design of over 250 big mountain-skiing resorts in 32 countries.

Ecosign has completed the following works to date:

- a preliminary technical evaluation and detailed analysis of the territory contiguous to Baikal (a. 20,000 sq.km.), including territories on the southern and eastern shores of the lake within the borders of the Republic of Buryatia. The evaluation was conducted with the use of Russian topographic maps and the region's climatic and natural data.
- In June 2006, the Ecosign expert team completed a study visit to the Republic for the sake of a visual evaluation of the territories most suitable for all-the-year-round mountainous resorts and produced a report on its findings.

The tourist and recreational zone “Baikal” is being created in an immediate proximity to Baikal, in Pribaikalsky district. Its territory will be over 70,000 hectares.

The future zone has all the necessary resources for creating a world-class mountainous and climatic resort: local mountains up to 1,771 m. and the vertical overfall up to 1.271 m.; their flanks are most suitable for mountain-skiing routes; a warm lake, mountainous rivers suitable for rafting and fishing, mineral wells and curative muds, flora and fauna, and the engineering and transport infrastructure within a close reach.

The concept of the zone suggests:

- creation of two all-the-year-round mountainous and climatic resorts with an advanced infrastructure and material base, including mountain-skiing complexes;
- creation of a center for water tourism;
- construction of basic infrastructure objects.

The existing natural and recreational, historical and cultural resources of the Republic and the potential importance of tourism to the regional economy allow positioning the future tourist and recreational complex as an international one.

Accordingly, the complex should offer top-notch services and all kinds of entertainment, sports, leisure and other services that should form all-the-year-round revenue sources. The high-season offer will be based upon sports, adventurous and ecological tourism, which now are the main local attractions. As concerns the all-the-year-round offer, it might be formed by a SPA- resort, therapeutic facilities, and entertainment.

The zone consists of three sites:

- The Southern site (the 1771 m-high alp and the contiguous territory);
- The Central site (Kotokelskoye lake and the contiguous territory);
- The Northern site (the 1,306 m-high alp and the coastal territory between Bezymaynnaya bay and cape of Katkov.

The Southern site suggests building a world-class all-the-year-round resort with an advanced infrastructure and a high density of various kinds of housing and sports and leisure facilities, as well as office and business centers, and trade and entertainment facilities, which should be situated in the territory with a total area of 525 hectares at the foot of and atop the 1,771 m.-high mountain.

At the basic territory, there would be located a 485 hectare golf field.

The Central site suggests construction of a center for water tourism covering an area of 240 hectares. It will be integrated into a joint tourist and recreational complex with the noted mountain-skiing resort of the Southern site.

The site will be situated on a picturesque shore of Kotokelskoye lake, and it will be formed by a yacht club, pier and embankment, an aquapark, a promenade, and a sports center with a multi-purpose sports arena, among other facilities.

The Northern site covers an area of 84 hectares and will comprise golf fields, a water resort, and a training center. By the foot of a 1,306 m-high mountain, there will be built a mountainous resort for inexperienced skiers and snowborders, which will occupy some 70 hectares.

The tourist facilities built throughout the territory of the zone will be capable to satisfy various demands of tourists of different categories and with different wallets. In the territory of the zone, there should also be built a huge center for SPA, balneological and oriental medicine services, and an international sports center.

The basic infrastructure in the territory of the zone suggests construction of two local 20- and 30 km.-long roads, which will cost RUR 1.4 bn.

To receive tourists from the neighboring regions and the city of Ulan-Ude, it is intended to restore a local airport in Goryachinsk settlement. This settlement and the neighboring Gremyachinsk settlement have helipads which also require reconstruction. It is also planned to restore a sea port in Turka village to regalvanize a sea route for tourists from Irkutsk oblast.

As the territory lacks electricity, it is planned to build a new high-voltage line (220 kilovolt) with two sub-stations with the capacity of 40 and 30 megawatt, respectively.

The site should be heated by means of electric boilers, and sun collectors to be constructed at the investors' expense; there should also be used non-traditional heating sources.

Water supply and drainage system will be environmentally safe, with water purification to be done with the use of activated carbon (biosorbing) and ozonization, and it should completely exclude chlorine. Such a technology meets all the environmental requirements to the Central Ecological Zone of Baikal.

The aggregate cost of the basic infrastructure will make up a. RUR 7 bn.

The advancement of the SEZ necessitates a further development of its external infrastructure, including: an extension of the runway at the Ulan-Ude international airport and reconstruction of the latter. Once it is done, the airport will be able to receive aircraft of all types and increase its annual capacity up to 1 mln passengers.

It is envisaged that the zone will be created at the expense of all the sources of financing. The overall volume of funding up to 2026 is estimated at the level of RUR 57.06 bn, with the federal budget contributing with 10.2 bn, the RF Subject's one – 3.05 bn, the local budget – 0.09 bn, and extrabudgetary sources – 43.72 bn. It is planned to use the budgetary funds on construction of the engineering infrastructure (the high-voltage line, highways and local roads, water supply and drainage systems, and reconstruction of the airports).

It is envisaged that the zone should attract numerous large residents, such as: "Buryatintur" Ltd., "Baikalkurort" Ltd., "Baikalfarm" Ltd., "Buryatgeopoject" Ltd., JSC "Continent", "Crystal Sibir" Ltd., "Trade House "Siberian Business Club" Ltd., JSC "Sibir Tour", "Restavratsia" td., JSC "Wistkom", JSC "Eurofinans", "Grand Baikal" Ltd., autonomous non-for- the-profit organization "Agentstvo kulturnykh initsiativ "Allegro", DVI Group, "Tan" Ltd., "Investment and Finance Company Metropol" Ltd., "Baikal-Puls" Ltd., JSC "Rimgeld", "V mire fantaziy" Ltd., "Piligrim" Ltd., JSC "Center Olympiyskoy Podgotovki "Yuniver-Baikal", and the Inter-regional trade-union of the production, research and science and management staff.

Some experts estimate RUR 41.55.04 bn in tax revenues to the budgets of all levels by 2026, while the number of tourists to the zone should reach 1.0 mln. It is hoped that the zone should generate 18,000 new jobs and, with account of the multiplicative effect in the supplier/consumer sectors, – 34,000 ones.

(d) SEZ in the territory of Altay Republic

For tourists, Altay is one of the most attractive territories – it boasts the untouched nature and is situated between several natural zones and cultural centers, including two public preserves and four public reserves, as well as five unique objects included in the UNESCO list, to say nothing of other local cultural and historical objects.

Over the past five years (1999–2005) the number of local tourist accommodation facilities grew from 36 up to 131, while the volume of tax revenues over the period in question rose several times. Every year, the Republic receives some 600–650,000 tourists.

So far as the recreational profile is concerned, the Republic's territory is formed by a system of multi-profile zones and therapeutic, rehabilitation, sanatorium, resort and tourist centers, of which the largest are Nizhnekatunsky, Bie-Teletsky, Nizhne-Uymonsky nd Ursulsky districts. The centers are shaped through integration into their composition of institutions designated for organization of recreational, therapeutic, as well as cognitive and sports and sanitary, kinds of activities.

Should the zone within precincts of a number of local municipalities be created, it would allow:

- organization of the functioning of a practical vehicle to boost development of depressive territories;
- securing the rise of a favorable entrepreneurial and investment climate and boost to the investment rating of the territory;
- encouragement of development of perspective sectors of the new economy by getting involved supplier/consumer sectors and territories of other municipalities outside those allocated for the creation of the SEZ.

The most promising location for the future SEZ may become certain sites in the territory of Mayminsky, Chemalsky, Turokchaksky and Ust-Koksinsky municipal districts. They are famous for favorable climate and weather conditions, are easily accessed and abundant with recreational resources; as well, there is noted a high concentration of infrastructure components of tourism.

The economy of the Republic should benefit greatly from the existence of such a unique natural object as Manzherokskoye lake with its relict endemic flora. The location allows construction of a world-class mountainous resort. It is envisaged that at the first stage of implementation of this particular project the Republic should focus on creation of a national mountainous and climatic sanatorium and tourist complex, which should provide a whole range of various services.

The creation of a modern highly efficient tourist industry in the area of the lake and Sinyukha mountain should provide an impetus to development of the local economy, increase the population's living standards and help solve socio-economic problems of the region.

The implementation of the first stage of the SEZ creation in the precincts of the "Mayminsky district" municipality in the area of the lake and Sinyukha mountain is determined by the fact that, on the one hand, land property documents are basically ready, and the local infrastructure is relatively developed there, on the other hand. Since 1986 the AR government has been repetitiously trying to build a mountain-skiing complex "Sinyukha". Back in 1993, this object had been included in the list of facilities of the 1993 Russian Sports Day and in the register of the federal targeted program "Development of tourism in the Russian Federation for 1995–97". However, because of numerous crises in the national economy, the federal budget and other sources have failed to ensure adequate funding.

Acting on behalf of the AR government, the Committee for Physical Culture and Sports of the Gorny Altay oblast commissioned a project of a mountain-skiing resort at Sinyukha mountain to the Moscow-based "Soyuzsportprojekt" institute and paid for the design. In 1993, the design was consequently submitted to the national Sports Committee and, as noted above, it was included in the federal targeted program. The AR government also commissioned the Moscow-based JSC "Soyuzprommekhanizatsia" to develop designs of a rope-way equipped with Austrian-made four- and two-seat hoists for the national Committee for Physical Culture and Sports.

To build a mountainous and climatic sanatorium and tourist complex, the RA government allocated a site of 31.6 hectares from the agricultural land owned by JSC "Karym". The site is located in immediate proximity to Manzherokskoye Lake, by the foot of Sinyukha mountain. Presently, another 69.3 hectares have been allocated to the site, thus extending the total up to 100.9 hectares.

The Federal Act "On special economic zones in the Russian Federation" reads that a special economic zone of tourist and recreational type can be situated in the precincts of several municipalities. That is why the envisaged mountainous and climatic and sanatorium and tourist complex at Sinyukha mountain can be regarded as the first stage of creation of a special economic tourist zone in the territory of the Altay Republic.

The noted steps with regard to the construction of the mountainous and climatic sanatorium and tourist complex may become possible only once the Federal SEZ Management Agency has completed a tender-based selection of RF Subjects in whose territories a special economic tourist zone will be created.

In the frame of the concept of creation of such a zone in AR it is planned to implement a complex of measures with respect to the world-class tourist accommodation and service infrastructure, including the noted mountain-skiing resort, a national sanatorium and tourist complex, the renewal of the local airport's operations, creation of the entertainment industry (sports and rehabilitation centers, casino, restaurants, aquaparks, etc.) to ensure their all-the-year-round loading. That is why apart from the noted territory by Manzherskoye lake and Sinyukha mountain, with regard to conclusions made in Chapter 2 of the Concept, the SEZ territory should also comprise the following territories: the one of the airport in the town of Gorno-Altaysk ("Mayminsky district" municipality); the sports and tourist complex "Seminsky pereval", with its perfect conditions for mountain-skiing and skiing activities ("Ongudaysky district) municipality; the coastal territory of Teletskoye lake ("Turachaksky district" and "Ulagansky district" municipalities); the Katun river coastal territory ("Mayminsky district and 'Chemalsky district" municipalities, and the territory of "Ust-Koksinsky district" municipality. These territories should be involved in the sphere of provision of a complex of various tourist services and their development is scheduled for phases 2 and 3 of the SEZ project implementation.

It is envisaged that the zone will be created at the expense of all the sources of financing. The overall volume of funding up to 2026 is estimated at the level of RUR 12.35 bn, with the federal budget contributing with 4.83 bn, the RF Subject's one – 0.78 bn, the local budget – 0.05 bn, and extrabudgetary sources – 6.69 bn. It is planned to use the budgetary funds on construction of the engineering infrastructure (natural gas pipeline, communal and communication facilities, and reconstruction of the local airport).

It is envisaged that the zone should attract numerous large residents, such as: AFK “Systema” (Moscow; JSC “Altay-West”; JSC “Stroitel”; JSC “Gornolyzhny complex ‘Manzherok”.

Some experts estimate RUR 13.9 bn in tax revenues to the budgets of all levels by 2026, while the number of tourists to the zone should reach 1.5 mln. It is hoped that the zone should generate 3,000 new jobs and, with account of the multiplicative effect in the supplier/consumer sectors, – 12,000 ones.

(e) SEZ in Krasondar krai

Looking for sites for future tourist SEZ that should allow a maximum effect at the first stage of implementation of respective projects, the regional administration has identified potential “points of growth” of the local tourist industry, namely, maritime territories at the Black sea and the sea of Azov, as well as in mountainous areas nearby the town of Apsheronsk and the city of Sochi. The territories display a considerable tourist and recreational capacity, thanks to diverse natural and climatic conditions, peculiarities of landscape and natural conditions. They have been long underdeveloped, with just a very few tourist facilities and private houses there. In cooperation with representatives of the respective municipalities, the krai administration selected 5 sites that best met the noted criteria of creation of a special tourist economic zone in the region:

1. “Blagoveschenskaya” – located in the precincts of the resort town of Anapa;
2. “Vysoky bereg”– located in the precincts of the resort town of Anapa;
3. “Krinitsa – Arkhipo – Osipovka” located in the precincts of the resort town of Gelendzhik”;
4. “Agriya” – located in the precincts of Tuapsinsky district municipality;
5. “Maly Akhun” in the precincts of the city of Sochi.

Thus the future SEZ is formed by five sites at the Black Sea with a total area of 1,730 hecrates. Each site and its future tourist products should focus on a certain targeted consumer segment. To ensure a comprehensive utilization of the region’s tourist and recreational capacity, the zone will be designated for development of the following kinds of tourism: beach; business; rehabilitation; water; sports.

The largest objects of the future tourist industry will become: several all-the-year-round world-class hotel complexes with the total capacity of 110,000 beds (3–5 – categories), along with cultural, entertainment and rehabilitation facilities; swimming pools, aquaparks, business centers, and yacht clubs.

It is envisaged that the zone will be created at the expense of all the sources of financing. The overall volume of funding up to 2026 is estimated at the level of RUR 181.66 bn, with the federal budget contributing with 15.98 bn, the RF Subject's one – 8.63 bn, the local budget – 4.35 bn, and extrabudgetary sources – 152.7 bn. It is planned to use the budgetary funds on construction of the engineering infrastructure (roads, natural gas pipelines, high-voltage lines, water supply, drainage and heating facilities, sewage facilities, and reconstruction of the local airports).

It is envisaged that principal residents in the SEZ would become: "Petra Sochi" Ltd; ""Purchase Center China"; "Mospromstroy" Ltd.; "Parus" Ltd.; "Alye Parusa" Ltd.; "Kubantelecom" Ltd.; "Businestsentr Sorduzhestvo" Ltd.; "Spetsstroykomplekt" Ltd.; "Chernomorsky Golf" Ltd.

Some experts estimate RUR 90.56 bn in tax revenues to the budgets of all levels by 2026, while the number of tourists to the zone should reach 3.2 mln. It is hoped that the zone should generate 26,000 new jobs and, with account of the multiplicative effect in the supplier/consumer sectors, – over 43,000 jobs.

(f) Special economic zone "Kavkazskiye Mineralnye Vody" (KMV)

This particular SEZ consists of four resort cities of the federal significance (Kislovodsk, Pyatigorsk, Essentuki and Zheleznovodsk), "Predgordny" municipal district, the town of Lermontov, and the town of Mineralnye Vody. These municipalities appear closely connected by transport routes and other infrastructure elements and united by mutually penetrating territories of sanitary-preserving areas of their joint basin of mineral waters. To crown the above, they form a mutually complementing set of natural, historical and cultural monuments and are situated within a fairly compact area of less than 4,000 sq. km.

To form a SEZ, there have been selected several sites with a total area of a. 2,000 hectares that mostly met the following requirements:

- Convenient location with respect to the existing transport network and settlement system in KMV;
- Existence of a tourist and recreational capacity (picturesque landscapes, proximity to main tourist flows or existence of unique resort opportunities, such as lakes, slopes, etc.);
- No legal charges and the existence of the owner's agreement to have the site be included into the SEZ;
- Closeness to basic infrastructure elements (primarily, gas and water supply pipelines, and highways);
- Size of the site appears sufficient and suitable for implementation of significant projects.

While identifying the list of sites, the emphasis was made on a fair degree of their diversity and dispersion across the region of KMV, for only providing this, the creation of a special economic zone would form a strong incentive to the general development of resorts within KMV.

It is intended to launch in the SEZ the following types of tourism: recreational and balneological; environmental; business, sports, and cognitive. The largest objects of the tourist sector should become: several world-class all-the-year-round 3 to 5* hotel complexes with an aggregate capacity of 17,000 beds, along with cultural and entertainment, and rehabilitation facilities; sanatoria, a clinic for innovation therapy; a sports and rehabilitation center, an aquapark, a children's rehabilitation center, the one for extreme tourism, and SPA-centers.

With all the above in place, the KMV's profile should also become innovation balneological technologies and novelties of the world SPA industry, including, among others:

- an accelerated neopsychological rehabilitation and elimination of personal and psychological post-surgery problems;
- modern therapeutic methods involving mineral waters from Batalinsky well of Zheleznaya mountain, which have a favorable effect on the organism;

- stone therapy on the basis of oriental medical practices, that is, treatment with igneous rocks, famous for their great thermal capacity and slow heat emission;
- Algotherm: the French methodology of five senses that suggests a comprehensive effect on the human senses from:
  - A therapy using muds from Tambukansly deposit;
  - German SPA- and French Yin-Yang devices;
  - Virtual diagnostic and treatment methodology;
  - Cellar therapy, which sometimes is called the medicine of the future;
  - Fitoaeroionization therapy and preventive methodologies.

It is envisaged that the zone will be created at the expense of all the sources of financing. The overall volume of funding up to 2026 is estimated at the level of RUR 52.06 bn, with the federal budget contributing with 2.54 bn, the RF Subject's one – 0.24 bn, the local budget – 0.28 bn, and extrabudgetary sources – 49.0 bn. It is planned to use the budgetary funds on construction of the engineering infrastructure (autonomous engineering power centers, electricity- and water supply facilities, roads, and reconstruction of the local airport).

It is envisaged that principal residents in the SEZ would become: UMACO, "RosEuroDevelopment", "HELIOPARK Group", "Wimm-Bill-Dann – Food Products", "Megapolis-Finans", "Svetprom" (under the guarantee by Sobinbank), "Northgas", Africa Israel Hotel Investments Ltd., "Insignia DEVELOPMENT", "Rigor-Stroy", "Renowa Stroy Group", "Waterhunters Holding Company".

By experts' estimates, by 2026 the zone should generate RUR 22.06 bn in tax revenues to the budgets of all levels, while the number of tourists to the zone should reach 2.8 mln. It is hoped that the zone should generate 11,000 new jobs and, with account of the multiplicative effect in the supplier/consumer sectors, – over 40,000 jobs.

(g) Special economic zone "Kurshskaya Kosa" (KK)

National park "Kurshskaya Kosa", perhaps, has no match among other Russia's national parks. Its area is 6,621 hectares, while the water area is 9,800 hectares. Its western border runs along the shore of the Baltic Sea, while the western one – along the shore of Kurshsky Bay.

Kurshskaya kosa is a sandy 98-km-long (of which Russia holds 48 km.) and 400 to 4,000 m-wide peninsula, which separates a shallow lagoon with fairly desalinated water, *aka* Kurshsky Bay, from the Baltic Sea.

By its size, length and the height of its dunes, as well as beauty of landscapes and affluent flora and fauna, KK stays unbeatable among suchlike spits in Europe. The local climate is mild in winter, while summer is usually moderately warm, autumn – warm, and spring – cool.

The local landscape formed not only by natural processes but human hands displays a model harmonious interaction between mankind and nature and illustrates evolution of the society and fishermen's settlements, in particular. KK still exists as a permanent cultural landscape, which retains an active social role and undergoes evolutionary processes. Meanwhile, it produces significant material evidence of its own evolution driven both by nature and man. Thus, there is a relict landscape there, whereat the evolution process had long been over, that is, the *Kursiai* tribe that once had resided there disappeared, but its ethnographic heritage is still there. The landscape of the fishermen's villages likewise can be found there under the sand dunes, for after the local woods were disforested, as many as 15 villages were buried in the sand.

The KK territory thus keeps cultural heritage objects:

- fishermen's villages;
- architectural monuments: unique protective facilities, which form an important cultural and historical objects;
- archeological objects: the aforementioned settlements of the indigenous population.

By the design, it is suggested to establish at KK, as a part of Zelenogradsky municipal district of the city of Kaliningrad, a special economic zone with the total area of up to 67 sq. km. In order to ensure a comprehensive utilization of the local tourist and recreational capacity, it is suggested to develop there the following types of tourism: environmental, rehabilitation, water- and bicycle, and excursion. The project involves construction of the following facilities: a children's rehabilitation center; an international environmental camp; an international educational center, and a glider school. In addition, there should be built the following major tourist objects: a boat pier, a congress center, an indoor aquapark, and a world-class bicycle route. It is planned to receive at KK to up to 4,000 tourists at once and provide accommodation to them.

It is envisaged that the zone will be created at the expense of all the sources of financing. The overall volume of funding up to 2026 is estimated at the level of RUR 7.62 bn, with the federal budget contributing with 1.5 bn, the RF Subject's one – 0.3 bn, and extrabudgetary sources – 5.82 bn. It is planned to use the budgetary funds on construction of the engineering infrastructure (electricity- and water supply facilities, coast-protecting structures).

It is envisaged that principal residents in the SEZ would become: "HELIOPARK Group", "Russkye Oteli" Ltd., JSC "Intersetotel", "VAK" Ltd., "Inter-invest" Ltd., JSC "TUTA Stroy",

By experts' estimates, the zone should generate RUR 4.7 bn in tax revenues to the budgets of all levels by 2026, while the number of tourists to the zone should reach 1.0 mln. It is hoped that the zone should generate 7,000 new jobs and, with account of the multiplicative effect in the supplier/consumer sectors, – 30,000 jobs.

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Conclusion

Special (free) economic zones have long been established in Russia's territory. The process of their creation and existence mirrored the transition towards market economy and the emergence of a new legal base. The lack of stability in the legal sphere, and asynchronicity between the federal and regional administrations' actions resulted in considerable tax risks. Legalization of free economic zone and a consequent deprivation of the RF Subjects of the right to grant tax benefits entailed the capital flight from Russia.

The enactment of the Federal Act "On special economic zones" constitutes a regular attempt of legal regulation. The Act provides for creation of special economic zones of two types, that is, industrial and R&D. Within their territory, an economic agent is allowed to carry out operations provided for by Act No. 116-FZ and the respective Resolution of the RF Government.

Procedures of inclusion of an organization into the register of residents of special economic zones suggest it complies with requirements stipulated in the aforementioned Act. For example, as per the agreement on exercise of industrial and production activities, a resident of a special economic zone is bound to complete capital investment in RUR equivalent in an amount no less that Euro 10 mn. (except for non-material assets) by the Central Bank of Russia's exchange rate as of the day of submission of the respective application for conclusion of the agreement. Act No. 16-FZ also provides for situations in which the resident of a special economic zone is deprived of his status.

One cannot help but take into account the fact that the noted Act became effective in the conditions of a relative economic stability. The Act reflected fundamentals of taxation and tax benefits in particular. Main tax benefits are provided for at the federal level. By contrast, the respective powers of the RF Subjects appear fairly restricted, primarily by provisions of the Tax Code.

All this to a certain extent excludes instability, which appeared so characteristic of free economic zones in the past. This equally excludes the opportunity to register a company within the territory of a special economic zone for the sake of tax dodging, as it often occurred in the past.

SEZ residents pay taxes as per general procedures, with certain exemptions set by the Tax Code of RF. More specifically, such exemptions are effective with respect to corporate profit tax, uniform social tax, corporate property tax, and land tax. The SEZ resident enjoys the right to switch to the simplified taxation system.

Free economic zones appear a promising enterprise worldwide, and at this point Russia is no exception. This can be proved by the pace of their development and aggregate output.

Whether or not the program of SEZ creation in Russia become a viable enterprise, depends on the degree to which the country will succeed in establishing in localized special zones an almost ideal economic system, that is, with strict rules of the game, minimum red-tape costs and maximum competitive environment, which should result in the most favorable investment climate therein.