

**TOWARDS TRANSFORMATION OF THE EXPORT PROCESSING ZONE REGIME
IN NAMIBIA: A CASE FOR REVIEW OF THE ENABLING LAW**

By

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ABSTRACT

Developing countries use EPZs as a policy strategy to transform from import-substitution industrialisation to export-led economic development. To make up for lack of comparative advantage, developing countries offer various incentives including better infrastructure, lax regulatory environment and tax exemptions, amongst others, to attract multinational corporations to invest in their countries. Although no specific international rules on EPZs exist, EPZs incentives such as tax exemptions and the relaxation of labour laws have been problematic at WTO and ILO, respectively. Like most countries, Namibia launched its EPZ programme following the promulgation of the EPZ Act 9 of 1995 with the objectives of attracting direct investments, creating employment, expanding exports, increasing foreign exchange earnings, and promoting skills and technology transfer. Generally, the Namibian EPZ programme has not been successful. Therefore, this study makes a comparative analysis of the EPZ Act as a policy instrument for the implementation of the EPZ programme in Namibia and the FIAS international best practice guidelines for the development of economic zones, to identify barriers to the achievement of the EPZ objectives and make a case for reform of the Namibian EPZ regime. The analysis identified a number of impediments to successful implementation of the EPZ programme, which includes a limited scope, absence of regulations, lack of private sector participation framework, conflicting roles of ODC, and the overly generous and WTO-inconsistent fiscal incentives. In the end, the study makes recommendations for the transformation of the Namibian EPZ programme into an effective policy instrument learning from international best practice guidelines for the development and management of economic zones.

LIST OF ABBREVIATIONS

ASCM	Agreement on Subsidies and Countervailing Measures
AGOA	Africa Growth and Opportunity Act
BITs	Bilateral Investment Treaties
CEACR	Committee of Experts on the Application of Conventions and Recommendations
COMESA	Common Market for Eastern and Southern Africa
EAC	East African Community
EBA	Everything But Arms
EPZs	Export Processing Zones
FIAS	Foreign Investment Advisory Service
FIRA	Foreign Investment Review Act
FDI	Foreign Direct Investment
FTZs	Free Trade Zones
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariff and Trade
GDP	Gross Domestic Product
GNI	Gross National Income
ILO	International Labour Organisation
MFA	Multi-Fibre Agreement
LaRRI	Labour Resource and Research Institute
LDCs	Least Developed Countries
NUNW	National Union of Namibian Workers
NIDA	Namibia Industrial Development Agency
NAFTA	North American Free Trade Agreement

NEPRU	Namibian Economic Policy Research Unit
OECD	Organisation for Economic Cooperation and Development
ODC	Offshore Development Company
RTAs	Regional Trade Agreements
PROEX	Export Financing Support Programme of Brazil
SACU	Southern Africa Customs Union
SADC	Southern Africa Development Community
SDGs	Sustainable Development Goals
SEZs	Special Economic Zones
SMEs	Small and Medium Enterprises
SZs	Specialised Zones
TRIMs	Agreement on Trade-Related Investment Measures
UNCTAD	United Nations Conference on Trade and Development
UNCTC	United Nations Centre on Transnational Corporations
UNIDO	United Nations Industrial Development Organisation
US	United States
USD	United States Dollars
VAT	Value Added Tax
WAEMU	Western African Economic and Monetary Union
WCO	World Customs Organisation
WEPZA	World Economic Processing Zone Association
WTO	World Trade Organisation
WWF	World –Wide Fund for Nature

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CHAPTER 1

BACKGROUND TO THE STUDY

1.1 Introduction

The past four decades or so have witnessed a proliferation of export processing zones (EPZs) as governments commonly use them as policy instruments to promote international trade and investment.¹ In Namibia, the EPZ programme was established following the promulgation of the Export Processing Zones Act 9 of 1995 (EPZ Act), as one of the policy instruments for industrial and economic development.² The main objectives of the EPZ Act are to promote the processing of goods targeting foreign markets, create employment for the masses, expand earnings from exports, and encourage technology and skills transfer.³ To achieve the set objectives, the enabling law offers numerous incentives, including infinite tax exemptions to attract investors into the EPZs. The intention behind generous tax exemptions was to make Namibia a ‘true tax haven’ in Africa.⁴ The Namibian government specifically anticipated that the incentives would attract foreign direct investment (FDI) to expand the manufacturing sector and create approximately 25 000 EPZ jobs.⁵ However, despite the incentives in place, an analysis conducted in 2010 has shown that the EPZ programme has not satisfactorily attracted export-oriented and labour-intensive manufacturing investments in Namibia.⁶

1.2 Research problem

Despite the existence of the EPZ programme for two decades, Namibia’s economic structure is still faced with numerous challenges, ranging from narrow manufacturing and export structures, high unemployment and poverty rates, as well as unequal distribution of income.⁷ More specifically, the country recorded a trade deficit of N\$ 39.2 billion in 2015, a 43 percent increase

¹ M Engman, O Onodera & E Pinali ‘Export processing zone: Past and future role in trade and development’ (2007) 8.

[http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?doclanguage=en&cote=td/tc/wp\(2006\)39/final](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?doclanguage=en&cote=td/tc/wp(2006)39/final) (accessed 15 November 2015).

² Offshore Development Company (ODC) ‘Annual report’ (2012/2013) 12.

³ Sec 3 of the EPZ Act.

⁴ Labour Resource and Research Institute (LaRRI) ‘Export processing zones in Namibia: Taking a closer look’ (2000) 41.

⁵ LaRRI (n 4 above) 8.

⁶ C Rosendahl ‘Industrial policy in Namibia’ (2010) 27-28; LaRRI (n 4 above) 10.

⁷ Ministry of Trade and Industry ‘Namibia’s industrial policy’ (2012) 4.

from the 2014 statistics.⁸ This trade deficit indicates that Namibia's imports for the period under review exceeded its exports in terms of the value of products.⁹ In addition, the export of mineral products contributed 72 percent of total exports in 2015.¹⁰ This is an indication that Namibia's export structure is still dominated by primary commodities without any value addition. These statistics, although just the tip of the iceberg, are a sign that the EPZ programme as a policy instrument for industrial and economic development, has not lived up to its expectations of expanding the export-orientated manufacturing structure.

The issue is that the EPZ Act, which is the implementation instrument for the EPZ programme in Namibia, is outdated and has a limited scope as it targets traditional labour-intensive and export-oriented light manufacturing enterprises, despite the fact that cheap labour and preferential trade arrangements that were responsible for the EPZs' boom in the 1980s and early 1990s have dwindled. This law also offers extensive fiscal incentives, amongst others, which are problematic under the international trade rules. Therefore, there are compelling reasons to revise the EPZ Act. It is for this reason that this study reviews the EPZ Act as the legal and policy framework underpinning the EPZ regime in Namibia, with a view to identifying and addressing shortcomings in the enabling law, that hinder the achievement of the EPZ objectives. The aim is to make a case for the transformation of the EPZ programme into an effective policy instrument taking a cue from the guidelines for the establishment of economic zones as recommended by the World Bank Group's Foreign Investment Advisory Service (FIAS).

As the literature review below will show, the question whether economic zones such as the EPZs are the best policy instrument for promoting economic growth has not been settled. However, there is a convergence of views that economic zones have the capacity to act as stimulants for broad economic reforms and lead to the economic growth of developing countries if they are properly established and managed.¹¹

⁸Tralac 'Namibia annual trade statistics bulletin 2015' <http://www.tralac.org/news/article/9278-namibia-annual-trade-statistics-bulletin-2015.html> (accessed on 30 March 2016).

⁹Analysing Namibia's 2015 trade statistics' *New Era* 22 March 2016 <https://www.newera.com.na/2016/03/22/analysing-namibias-2015-trade-statistics/> (accessed 30 March 2016).

¹⁰Tralac (n 8 above).

¹¹D Madani 'A review of the role and impact of export processing zones' (1999) 7-8.

Indeed, it is important to note that a combination of factors, including a comprehensive legal framework, have to be in place for EPZs to be successful. However, while the presence of a comprehensive legal framework does not guarantee success, its absence can contribute to the EPZs programmes' failure.¹² Thus, the law should provide a solid basis and evolve to meet changing economic needs for the effective implementation of EPZ programmes.¹³ This study, therefore, argues that shortcomings in the legal framework hinder the effectiveness of the EPZ policy.

1.3 Research questions

The main question that this study seeks to answer is: what are the shortcomings that should be addressed in the EPZ Act to transform the EPZ programme into an effective policy instrument for Namibia? In addressing the main question, the following sub-questions will also be answered:

- (i) What is the nature and context of EPZs?
- (ii) Do international rules have implications on EPZs?
- (iii) How is the current EPZ programme regulated in Namibia, and what are the shortcomings in the enabling law that are impeding the achievement of its objectives?
- (iv) What lessons can Namibia learn from the FIAS guidelines for zone development to transform the EPZ programme into an effective policy instrument for socio-economic development in Namibia?

1.4 Thesis statement

This study argues that the EPZ Act has shortcomings that hinder the EPZs from attracting requisite direct investments into the country. It further argues that the revision of the EPZ Act would lead to the transformation of the EPZ programme into an effective policy tool for socio-economic development in Namibia.

¹² T Farole *Special economic zones in Africa: Comparing performance and learning from global experiences* (2011) 9.

¹³ Farole (n 12 above) 166.

1.5 Justification

This study will provide a long overdue systematic legal review of the Namibian EPZ Act and make recommendations to the Namibian government to transform the EPZ programme into an effective policy instrument. Therefore, from the Namibian government's perspective, this study will prove to be a cost and time-saving exercise for the reason that it will provide free analysis and recommendations on the EPZ Act based on academic research.

Additionally, from the academic point of view, this study will be an input into the on-going debate on the merit of the EPZs as a policy choice for African countries. It will, in particular, supplement the limited legal literature on the Namibian EPZs.

1.6 Literature review

Whereas EPZs have been successful in Central America, the Caribbean, and East Asia, the use of EPZs as policy instruments for trade and investment in Africa is relatively unsuccessful.¹⁴ Literature has shown that there is an unsettled debate on the impacts of EPZs on the economy of developing countries. According to Baissac¹⁵, the debate on the contribution of EPZs to the economic development has been intense for approximately four decades and there is no sign of it abating.

One school of thought views economic zones as less effective policy instruments for trade and investment in comparison to economy-wide liberalisation, while the other school considers economic zones to have the potential to conquer market failure, and become stimulants for economic reforms.¹⁶

Proponents of economic zones, such as Baissac,¹⁷ argue that successful examples from East Asia and Mauritius indicate that the EPZs have the potential to turn developing economies into 'export power houses', with significant economic benefits. However, Baissac has argued this point from the perspective of economic impacts and did not deal with the question of

¹⁴ C Baissac 'Introduction to export processing zones' (2003) 17
www.nccur.lib.nccu.edu.tw/bitstream/140.119/33936/7/93303407.pdf (accessed 1 November 2015).

¹⁵ C Baissac 'Maximising the developmental impact of EPZs: A comparative perspective in the African context of need accelerated growth' (2003) 1.

¹⁶ Farole (n 12 above) 2.

¹⁷ n 15 above, 7.

whether the shortcomings in the legal framework underpinning EPZs hinder the EPZs' performance.

Similarly, Haywood¹⁸, in support of economic zones, argues that the economic zones concept has transformed from a static conventional enclave to a more dynamic, enabling, and integrated economic development tool. Furthermore, Haywood¹⁹ refutes a United Nations Conference on Trade and Development (UNCTAD) report, which describes the EPZ development drive as attracting low-quality jobs, light value addition, marginal profit, high market uncertainty, and an uncertain and volatile investment environment. He argues that the statistics indicate that export manufacturing industries are the most stable sectors in developing countries. Haywood's argument is debatable considering the investments flight, particularly from African EPZs, following the dismantling of the Multi-Fibre Agreement.²⁰ However, the argument whether or not EPZ industries are more stable than other industries falls outside the subject of this study.

Another school of thought, such as that of Engman *et al*, consider EPZs as 'suboptimal policies', in promoting FDI, creating employment and enhancing economic growth in less developed countries in comparison with general trade and investment liberalisation.²¹

Madani²² holds the same view as Engman *et al*, that EPZs are far from being the optimal policy choice. Nevertheless, she is of the view that zones can be instrumental in the development process of their host countries if they are appropriately established, well-managed, their incentives are compatible with the World Trade Organization (WTO), and are used as part of a general reform agenda, and not as barriers to the reform process. Madani's viewpoint on the role of economic zones goes to the core of this study which aims to review the Namibian EPZ legal framework to ensure that zones are developed and managed in line with international best practice, compliant with international rules, and they promote integration of zones with the host economy to enhance national economic growth.

¹⁸ R C Haywood 'Free zones in the modern world' (2000) 1 <http://www.wepza.org> (accessed 1 November 2015).

¹⁹As above.

²⁰ T Fontaine 'End of quotas hits African textiles' *International monetary Fund (IMF) Survey Magazine* 05 July 2007 <https://www.imf.org/external/pubs/ft/survey/so/2007/NEW075A.htm> (accessed 21 April 2016).

²¹ n 1 above, 6.

²² D Madani (n 11 above) 7-8.

In a study on Southern Africa, Jauch²³ argues that EPZs do not provide solutions to unemployment, and neither do they increase foreign exchange earnings or lead to any significant skills transfer. In his view, EPZs create second class jobs, deepen dependency on foreign capital, and affect local industries negatively and thus, do not lead to sustainable economic development.²⁴ He further argues that, instead of benefiting from EPZs, host countries suffer losses due to tax exemptions, as well as through the development of EPZ infrastructure and the provision of subsidised services.²⁵ In other words, Jauch sees EPZs as a burden rather than a solution. However, although EPZs have not flourished in most African countries, there are success stories with EPZs in countries such as Mauritius and in East Asia.²⁶ Therefore, Jauch's position is not without a counter argument as far as the performance of EPZs is concerned.

Meanwhile, Farole²⁷ has somewhat neutralised the debate by submitting that economic zones may be facilitators for economy-wide liberalisation if all prerequisites are put in place, otherwise, their economic impact would be miniscule and short-lived, or they become archaic welfare-reducing enclaves, which impede reform.

Although, from the above literature review, the debate on whether EPZs are the best policy instruments for promoting economic growth has not been settled, there seems to be convergence of views that economic zones, in general, have the potential to act as agents for economic reforms and lead to the growth of developing economies if they are properly established and managed. However, the literature has not addressed the issue of whether or not the shortcomings in the legal framework impede the effective implementation of the zone programme. This study, therefore, argues that shortcomings in the EPZ legal framework impede on the effectiveness of the EPZ policy. This is done by analysing the legal framework underpinning the EPZ programme in Namibia with a view to identifying shortcomings which hinder the effective implementation of the EPZ programme.

The reality is that all African countries need to graduate from commodity dependency by diversifying their economies. For this reason, a policy instrument, whether or not it is a second-

²³ H Jauch 'Export processing zones and the quest for sustainable development: A Southern African perspective' (2002) 14 *Environmental & Urbanisation* 111.

²⁴ As above.

²⁵ Jauch (n 23 above) 102.

²⁶ Baissac (n 114 above) 17.

²⁷ n 12 above, 5.

best option, is an indispensable tool for most African countries insofar as it enhances economic diversification. On this basis, the writer agrees with Haywood's metaphor that 'if a craftsman does not sharpen his saw and it fails to cut, it is not the saw's fault, but the craftsman's'.²⁸ This means that zones fail not because they are a bad concept, but because countries do not develop increasingly progressive policies for their zones.²⁹ To this end, the legal framework underpinning economic zones need to be regularly revised and adapted to the changing economic environment to facilitate the effective implementation of the zone programme.

1.7 Research methodology

This study is desktop based, relying on both primary and secondary sources. Primary sources include the Namibian EPZ Act and international cases and agreements. Secondary sources include books, journal articles, policy papers, reports and online materials. The information will mainly be processed through historical and analytical approaches. A comparative approach is also used to determine the extent to which the Namibian EPZ programme is in line with guidelines for the establishment of economic zones, and the prescriptive approach is used by making recommendations on the way forward. The guidelines for the establishment of economic zones as devised by the FIAS are chosen as appropriate benchmarks for Namibia as they are based on a comprehensive study of different zones around the world. Thus, these guidelines are embodiments of international best practice in zone development and management.

1.8 Limitations of the study

While economists have written extensively on the costs and benefits of economic zones and their impacts on host countries' economies, there is a noticeable scarcity of legal literature on EPZs and economic zones in general.

In addition, to the extent that this study is desktop based, it was difficult to obtain up-to-date information on the Namibian EPZ programme as information is not extensively publicised.

²⁸ n 18 above, 3.

²⁹ As above.

1.9 Overview of chapters

Chapter 1 provides an introduction to the study by outlining the problem statement, thesis statement, research questions, the significance of the study, and the research methodology. Chapter 2 explains the nature and context of the EPZs and economic zones in general. Chapter 3 discusses the implications of international agreements on EPZs. Chapter 4 analyses the legal framework governing EPZs in Namibia. Chapter 5 discusses the guidelines for the establishment of the economic zones as benchmarks for transforming the Namibian EPZ regime. Finally, Chapter 6 concludes and makes recommendations.

CHAPTER 2

THE NATURE AND CONTEXT OF EXPORT PROCESSING ZONES

2.1 Introduction

The first chapter introduced the study and provided the background to the research topic by outlining the problem statement and the justification for reviewing the law underpinning the EPZ programme in Namibia. This chapter gives a detailed background of EPZs. In particular, it puts EPZs into context by explaining what EPZs are, analysing definitions of various international organisations, and giving a brief historical background of the evolution of EPZs from the global perspective. It further explains the different types of economic zones and discusses the EPZ trends in certain African countries with respect to EPZ policies. Lastly, this chapter deals with the economic significance of the EPZs by explaining EPZ policy objectives and the incentives commonly offered to attract investors in the EPZs.

2.2 Contextualization of EPZs

Around the 1960s, many developing nations embarked on the transformation of their industrialisation strategies from import-substitution to export-oriented economic development by employing the EPZ concept as a tool of choice.¹

2.2.1 What are EPZs?

In order to answer the question of what EPZs are, the study analyses definitions of EPZs by different international organisations, as compiled by Baissac:²

The United Nations Industrial Development Organization (UNIDO):

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.

¹ UNIDO 'Economic zones in the ASEAN: Industrial parks, special economic zones, eco industrial parks, innovation districts as strategies for industrial competitiveness' (2015) 28.

² C Baissac 'Introduction to Export Processing Zones' (2003) 6
<http://nccur.lib.nccu.edu.tw/bitstream/140.119/33936/7/93303407.pdf> (accessed 27/11/2015).

The World Bank:

An EPZ 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.

The International Labour Organisation (ILO) and the United Nations Centre on Transnational Corporations (UNCTC):

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 export benefit from a certain number of fiscal and financial incentives.

The United Nations Conference on Trade and Development (UNCTAD):

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 production are not subject to customs duty.

The definitions of EPZs by the World Bank, ILO and UNCTC, and UNCTAD are more or less similar to UNIDO's definition. The common features from these definitions are an enclave or geographically defined area, with the main objective of promoting exports, coupled with the provision of special incentives.³ However, these definitions are narrow as they do not take into consideration the fact that EPZs have evolved and that some countries, including Mauritius, allow EPZ firms to be set up in any part of the country without being restricted to a specific geographical area.⁴ Additionally, other countries, including Mexico and Kenya, allow domestic sales of EPZ products.⁵ Thus, the entire EPZ production in some countries is not necessarily destined to the foreign markets as per the definition of UNCTAD, for example.

On the other hand, the World Economic Processing Zone Association (WEPZA) defines EPZs as:

³ M Engman, O Onodera & E Pinali 'Export processing zone: Past and future role in trade and development' (2007) 10.
[http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?doclanguage=en&cote=td/tc/wp\(2006\)39/final](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?doclanguage=en&cote=td/tc/wp(2006)39/final)
(accessed 15 November 2015).

⁴ D Madani 'A review of the role and impact of export processing zones' (1999) 13.

⁵ As above.

All government authorized areas such as free ports, free trade zones, custom free zones, industrial free zones or foreign trade or any other type of zone, as the Council may from time to time decide to include.⁶

Save that WEPZA defines an EPZ as a government authorised area, the definition is too wide, and fails to highlight the outstanding characteristics of an EPZ. This is, especially, the case considering that WEPZA uses the term as an all-embracing term and not as a particular model.

Meanwhile, Engman *et al.*⁷ define EPZs as:

A government policy to promote exports of goods and/or services by offering a more competitive business environment through provision of special incentives, including in particular tariff exemptions to inputs either in a geographically defined area or through a specification process.

The definition espoused by Engman *et al.* is more comprehensive as it is adapted to include both traditional EPZs which are described as “fenced-in areas” or “enclaves” and the modern type EPZs which allow single factories, yet it excludes other forms of economic zones such as special economic zones (SEZs) and freeports.

2.2.2 Historical development of the EPZs

The use of economic zones as policy instruments for economic development by both developing and developed countries is not new. Literature traces the economic zones concept to as far back as 300 BC.⁸ Additionally, UNIDO estimates that the zones concept has existed in international trade for over 2500 years.⁹

According to the Organisation for Economic Co-operation and Development (OECD), the first types of economic zones were freeports, situated inside seaports, which provided trade and storage facilities.¹⁰ These later transformed into customs-free zones, performing processing and light manufacturing.¹¹ After customs-free zones, the next generation was the EPZs, where more complex manufacturing operations took place for export.¹² The SEZs, which offer a broader

⁶ Baissac (n 2 above) 10.

⁷ n 3 above, 11.

⁸ Baissac (n 2 above) 1.

⁹ n 1 above, 27.

¹⁰ OECD ‘Towards best practice guidelines for the development of economic zones’ (2009) 4.

¹¹ As above.

¹² As above

range of sectors, including services and manufacturing for both domestic and foreign markets, are the most recent form of economic zones.¹³

The Irish Shannon Free Zone,¹⁴ set up in 1959, is generally recognised as the first contemporary EPZ.¹⁵ Since then, several countries including Puerto Rico, India, Chinese Taipei, the Republic of Korea and Malaysia established EPZs modelled on the Shannon Free Zone in the 1960s and 1970s, respectively.¹⁶ In Africa, Senegal, Liberia, Ghana and Mauritius set up their EPZs in the early 1970s.¹⁷

In 1980, China introduced a dramatic new concept broader than EPZs, the SEZs, to experiment with the open economy policy.¹⁸ The Chinese SEZ programme has been hugely successful in enticing FDI and has made China a leading beneficiary of FDI and the world's number one exporter of industrialised products.¹⁹ Since China's introduction of the SEZs, the concept has swiftly shot to fame, with most developing countries, including African countries, adopting SEZ policies in anticipation of replicating China's exceptional and robust economic growth over the last two decades.²⁰

The ILO reported a sharp increase in the number of countries with EPZs from 25 in 1975 to 116 countries in 2002.²¹ In 2015, the number of countries rose to 140, with approximately 4500 zones in existence.²² Without a doubt, the number recorded by both the ILO and UNIDO is inclusive of all types of economic zones, and not necessarily the EPZ model. However, the increase in zones establishment is an indication of how countries especially, developing countries, value the economic zones concept as a vital policy tool for economic development.

¹³ As above.

¹⁴ The purpose was to save about 1500 jobs for workers employed at Shannon Airport that were at risk of being lost due to advanced aviation technology which made refuelling of transatlantic flights at Shannon redundant. The Airport was then turned into a duty-free manufacturing zone to create employment for retrenched workers. See Baissac (n 2 above) 2.

¹⁵ As above.

¹⁶ Engman *et al.* (n 3 above) 12.

¹⁷ As above.

¹⁸ Engman *et al.* (n 3 above) 11.

¹⁹T Farole *Special economic zones in Africa: Comparing performance and learning from global experiences* (2011) 36.

²⁰Farole (n 19 above) foreword.

²¹ Engman *et al.* (n 3 above) 12.

²² UNIDO (n 1 above) 26.

2.2.3 Typology of economic zones

The zone concept has evolved over the years as countries adapt their zones to suit their developmental objectives.²³ Various names have been used to designate economic zones in different countries. In Ireland, for example, they are called export-free zones or industrial-free zones; in Mexico they are famously known as the *maquiladoras*; in the Republic of Korea they are called free export zones or duty-free export processing zones; in the Philippines they are called EPZs; while in China they are popularly known as SEZs.²⁴ According to UNCTAD, the ILO has listed approximately 30 different names used to designate economic zones around the world.²⁵

Despite the variety of names and types, zones have at least three essential features in common, save that all the three features may not necessarily be displayed at the same time.²⁶ These are:

- (i) Economic zones are demarcated geographical areas, which are governed by more liberal rules than applicable in the rest of their host countries.
- (ii) The zones' administration has a committed governance structure to ensure efficiency of the programme.
- (iii) The zones are provided with general infrastructure such as estates, roads, telecommunication, water and electricity to support the activities in the zones.²⁷

The most commonly used types of economic zones are:²⁸

- a) **Free trade zones (FTZs)** (also known as commercial free zones or free zones)²⁹ are 'small, fenced-in, duty-free areas, offering warehousing, storage, and distribution facilities for trade, transshipment, and re-export operations, normally located in most ports of entry around the world.'³⁰ FTZs are recorded as the oldest and the most widespread form of economic zones, usually falling directly or indirectly under the

²³ UNIDO (n 1 above) 27.

²⁴ Engman *et al.* (n 3 above) 11.

²⁵ UNCTAD 'Enhancing the contribution of export processing zones to the sustainable development goals: An analysis of 100 EPZs and a framework for sustainable economic zone' (2015) 3.

²⁶ Farole (n 19 above) 25.

²⁷ As above.

²⁸ OECD (n 10 above) 4.

²⁹ As above.

³⁰ FIAS 'Special economic zones: Performance, lessons learned and implications for zone development' (2008) 10.

ports authority, and their operations include sales, exhibitions and light processing activities.³¹

- b) **Export processing zones** are ‘industrial estates offering special incentives and facilities for manufacturing and related activities aimed mostly at export markets.’³² Originally, EPZs targeted manufacturing for foreign markets while investments were limited to foreign capital, but most EPZs have developed since, and various activities are now allowed.³³
- c) **Single factory processing zones**, also referred to as enterprise zones or free unit zone, may be located anywhere in the country as they are intended to revive either distressed rural or urban areas in their host country by providing financial grants and tax incentives.³⁴ The Mexican *maquiladoras* are of this genus.³⁵
- d) **Special economic zones** are bigger areas which can cover an entire city and could be considered cities on their own as they permit on-site residence.³⁶ They mimic several features of EPZs, export processing units, and freeports, but they are distinct as they accommodate a broad range of economic sectors, including agriculture, construction, manufacturing, public utilities, finance and tourism. Firms receive similar incentives to those offered in the EPZs.³⁷ China is the pioneer of this approach.³⁸
- e) **Specialised zones (SZs)** are zones that target specific economic activities or sectors, such as science or technology parks. The infrastructure is usually sector tailor-made, and access to these zones by companies in non-priority sectors is restricted.³⁹

Whereas the FIAS⁴⁰ and Farole⁴¹ include ‘freeports’ in their classifications of economic zones, they excluded SEZs. However, their descriptions of freeports overlap with that of SEZs as

³¹ Farole (n 19 above) 27.

³² FIAS (n 28 above) 10.

³³ Farole (n 19 above) 28.

³⁴ FIAS (n 30 above) 11.

³⁵ Farole (n 19 above) 28.

³⁶ OECD (n 10 above) 4.

³⁷ H Stein ‘Africa, industrial policy and export processing zones: Lessons from Asia’ in A Noman, K Botchwey, H Stein & JE Stiglitz (eds) ‘*Good growth and governance in Africa: Rethinking development strategies*’ (2012) 325.

³⁸ As above.

³⁹ OECD (n 10 above) 5.

⁴⁰ FIAS is an investment climate advisory service of the World Bank Group. See n 30 above, 10.

described by the OECD⁴² and Stein.⁴³ On the other hand, the OECD does not include ‘freeports’ in its classification. This makes it difficult to distinguish between the two types of zones. It can only be assumed that the rationale for leaving out SEZs as a type of economic zone by the FIAS and Farole is because they have used SEZs as a generic name in their literature.

Very often phrases such as EPZs, FTZs and SEZs have been used interchangeably in literature as generic names encompassing other forms of economic zones. This is somewhat confusing, especially in determining whether the term is used as a generic name or as a specific economic zone model.

Notwithstanding the confusion due to the interchangeable use of the zones’ names, authors such as Johansson cited by Madani,⁴⁴ support the interchangeable use of the zones’ names on the basis that the concept of all zones is fundamentally the same. While this argument may be true, there are specific zones which have fundamental distinctions. These include the FTZs which comprise of EPZs, but, not all EPZs are FTZs.⁴⁵ Similarly, EPZs and SEZs are not mutually exclusive but have sufficient distinct objectives, investment requirements, and approaches, to warrant differentiation.⁴⁶

Therefore, although the phrases EPZs, SEZs and FTZs have been used interchangeably as generic names in literature, they are used in this study as specific economic zone models and not as generic names. Where the context dictates the use of a generic name, the phrases ‘economic zone(s)’ or ‘zone(s)’ are used to denote a reference to all forms of economic zones and to dispel confusion.

2.3 Africa’s experience with the EPZs

Countries such as Liberia, Senegal and Mauritius introduced EPZs on the continent in the early 1970s to transform their import-substitution industrialisation policies to export-oriented

⁴¹ n 19 above, 27.

⁴² n 10 above, 4.

⁴³ n 37 above, 325.

⁴⁴ n 4 above, 12.

⁴⁵ As above.

⁴⁶ T Farole & G Akinci (eds) ‘*Special economic zones: Progress, emerging challenges and future direction*’ (2011) 3.

development strategies.⁴⁷ However, the establishment of economic zones in Africa has only multiplied between 1990 and 2000.⁴⁸

Evidence has shown that the EPZs in African countries, with the exception of the Mauritian EPZs, have not performed according to expectations, particularly, in terms of employment creation, generating high levels of export and FDI, and leveraging forward and backward linkages.⁴⁹ The poor performance of African EPZs is largely attributed to, in the first place, the fact that many zones have been driven by aid agencies and preferential market access through arrangements such as the Multi-Fibre Arrangement (MFA), which expired in 2005; the Everything But Arms (EBA); and the African Growth and Opportunity Act (AGOA).⁵⁰ Stein⁵¹ blames the underperformance of the African zones on what he terms ‘a faulty neoclassical notion’ of the World Bank that sees EPZs as, simply, an inferior solution to overall trade and investment liberalisation, as opposed to seeing the zones concept as part of the broader industrial policy. Other contributory factors to the failure of African zones are, amongst others, poor infrastructure, inadequate water and electricity supply, poor zone planning and management, lack of institutional coordination, lack of private sector participation, weak governance, and lack of integration of the zone with the domestic economy.⁵²

The EPZ model adopted by most African countries has also been criticised for having a limited scope in the wake of growth in other sectors such as services, agro-processing, and global and regional trade integration.⁵³ According to Farole and Akinici,⁵⁴ the increasing costs of labour and the contracting trade preferences render the conventional EPZ model unsustainable. Of late, a number of countries, including Tanzania,⁵⁵ South Africa⁵⁶ and more recently Kenya,⁵⁷ have

⁴⁷S Woolfrey ‘Special economic zones and regional integration in Africa’ (2013) 8

⁴⁸ UNCTAD ‘Economic development in Africa, intra-Africa trade: Unlocking private sector dynamism’ (2013) 113.

⁴⁹ Woolfrey (n 47 above) 13 .

⁵⁰ H Stein ‘Africa, Industrial policy and export processing zones: Lessons from Asia’ in Noman *et al.* (n 37 above) 323.

⁵¹ As above.

⁵² Woolfrey (n 47 above) 13.

⁵³ As above.

⁵⁴ n 46 above, 4.

⁵⁵ **Tanzania** established its EPZs in 2002 following the enactment of the EPZ Act 11 of 2002 to attract export-oriented investment in order to promote competitiveness. In 2006 the government introduced the SEZs policy and enacted the SEZs Act 2 of 2006. The purpose is to target investment industries, focusing both in the local and foreign market. There are no export performance requirements under the SEZs Act. (see Woolfrey (n 47 above) 11).

⁵⁶ **South Africa** initially established the industrial development zones through the Manufacturing Development Act 187 of 1993. The purpose was to attract FDI and promote the export of value-added products. The programme has

reviewed their EPZ policy and legislative frameworks to adopt the SEZ concept with the hope to improve the performance of their zones.

2.4 Economic significance of EPZs

While some countries adopt EPZ policies in the initial phases of economic development to jump-start their industrialisation process, others employ EPZs to strengthen their manufacturing and exports industries.⁵⁸ According to Baissac,⁵⁹ EPZs are useful instruments for economic development during the early stages of industrialisation, but cautions against sole reliance on the policy as the main driver for economic development in the long term, as it loses significance when higher levels of development are attained.

2.4.1 Common policy objectives for EPZs

Different countries have different policy objectives for establishing EPZs. Nevertheless, there is consensus from the literature that the most common objectives for establishing EPZs in developing countries are:

- a) *To attract FDI*: Most developing countries, some of which may be endowed with natural resources, lack capital and capacity to produce at a regional and global competitive level, so these countries establish EPZs to attract foreign capital and technology to produce goods targeting the export markets.⁶⁰ However, EPZs have been criticised for attracting footloose industries which only trail the incentives and usually relocate when tax incentives expire.⁶¹
- b) *To create large-scale employment*: This was the case with the Ireland's Shannon Free Zone which was predominantly created to save jobs that faced imminent risk of being lost

generally not yielded the expected outcomes, mainly due to its lack of special incentives. The underperformance of the IDZs led to the government reviewing the programme and formulating a SEZ policy in 2012, culminating in the enactment of the SEZs Act 16 of 2014. (Woolfrey (n 47 above) 10).

⁵⁷ Kenya established the EPZ regime in 1990 to transcend from import substitution to export-led economic growth. Recently, the government reviewed the EPZ policy and adopted the SEZ policy to plug the loopholes in the EPZ regime by targeting infrastructure, business challenges, and restriction of domestic sale, as well as addressing the WTO incompatibility. The Kenyan SEZ policy is also flexible enough to permit operations such as agro-processing and the tourism sector. (Woolfrey (n 47 above) 10).

⁵⁸ Madani (n 4 above) 18.

⁵⁹ n 2 above, 5.

⁶⁰ Engman *et al.* (n 3 above) 16.

⁶¹ Engman *et al.* (n 3 above) 37.

due to advanced technology in the aviation industry.⁶² The Mexican *maquiladoras* were also established to address unemployment resulting from the termination of the United States (US) Bracero Programme.⁶³

- c) *To increase exports and foreign exchange earnings from export goods:* EPZs offer exporting companies that do not have access to competitive inputs due to high tariffs and bottlenecks in the general business environment, duty-free access to inputs, as well as efficient administrative support and high-standard infrastructures, to capacitate them to participate in international trade.⁶⁴ Generally, countries that import most of their products and export less than they import risk facing trade deficits and a shortage of foreign exchanges. Thus, EPZs are employed to offset these challenges. However, in Madani's⁶⁵ view, benefits of foreign exchange earnings may have been exaggerated, because for foreign companies, gains from foreign exchange may only ensue when these companies convert foreign exchange earnings into local currency at an official rate to pay for local wages and expenses, otherwise, they repatriate their profits.
- d) *To promote technology and skills transfer:* Investments in the EPZs, especially by foreign investors, can lead to technology and skills transfer into the domestic market.⁶⁶ Skills and technology transfer occurs when non-EPZ enterprises and prospective entrepreneurs are able to learn and copy from foreign investors.⁶⁷ However, skills and technology transfer in the EPZs may be limited because EPZs do not usually attract skills-intensive or advanced technology investments.⁶⁸

2.4.2 Frequently offered incentives in the EPZs

In an effort to lure investors into the EPZs, developing countries usually offer various benefits to investors to make up for their lack of a comparative advantage. Countries compete with their neighbours to attract foreign investors by offering generous incentives resulting in the infamous

⁶² See n 14 above.

⁶³ Farole (n 19 above) 57.

⁶⁴ Engman *et al.* (n 3 above) 22.

⁶⁵ n 4 above, 23.

⁶⁶ Engman *et al.* (n 3 above) 16.

⁶⁷ Madani (n 4 above) 29.

⁶⁸ FIAS (n 30 above) 36.

‘race to the bottom’ as desperately generous incentives consequently erode the actual benefits that could be derived from the EPZs.⁶⁹

EPZs are considered to have the potential to move up the value chain by attracting industries that can add value to the natural resources of less developed countries or simply by attracting industries which can produce higher value-added products.⁷⁰ Thus, there is a good reason to lure investors.

The incentives offered in the EPZs may be divided into three categories⁷¹:

- i) *Financial incentives*: These may be direct in the form of grants and soft loans to EPZ investors or indirect in the form of physical infrastructures, such as telecommunications, transport and logistical networks, factory cells, housing and school facilities, and special grants for education and training.⁷² The supply of water and electricity at a rate lower than the market rates also falls in this category.⁷³
- ii) *Fiscal incentives* include waiving import duties on inputs, customs fees and charges and value-added tax on goods or services exported, and on resources and services sourced from the domestic market, which are used in the course of production, in the EPZs.⁷⁴ Duty drawbacks and exemptions from corporate tax are also part of fiscal incentives which are usually contingent on export performance.⁷⁵
- iii) *Regulatory incentives* consist of relaxed rules on labour, environment, foreign exchange regimes, lease or purchase of land, foreign business ownership, as well as the provision of a one-stop shop services.⁷⁶

Although incentives may play a role in a decision to locate in another country, they are not the only factors investors have to consider, as other factors such as access to a large market, availability of skilled labour and raw materials, and macroeconomic stability, are equally

⁶⁹ UNIDO (n 1 above) 30.

⁷⁰ As above.

⁷¹ OECD (n 10 above) 8.

⁷² Engman *et al.* (n 3 above) 17.

⁷³ As above.

⁷⁴ OECD (n 10 above); Engman *et al.* (n 3 above) 17.

⁷⁵ Engman *et al.* (n 3 above) 17.

⁷⁶ As above.

important.⁷⁷ According to UNCTAD, FDI is determined by a combination of a liberal FDI policy framework, favourable economic factors, and the ‘ease of doing business’ in the country concerned.⁷⁸ This is testimony that incentives alone are not sufficient for multinational corporations to invest in a country, as other factors are equally, if not more significant.

2.5 Conclusions

This chapter has shown that EPZs are policy instruments implemented by governments, especially of developing countries, with the main goals of attracting FDI; creating employment; promoting the export of goods; increasing foreign exchanges earnings; and promoting the transfer of skills and technology in exchange for special incentives.

However, incentives are not the only factors which investors consider before making a decision to locate to a foreign country, as other factors, such as access to a larger market, availability of skilled labour and raw materials, macroeconomic stability and the ease of doing business, are equally important in influencing the decision of investors to invest abroad.

The next chapter will discuss the implications of international rules on the EPZs. At the core of the next chapter are the international trade rules which have implications on fiscal incentives offered and performance requirements imposed under the EPZs programmes.

⁷⁷ As above.

⁷⁸ UNCTAD ‘The role of international investment agreements in attracting foreign direct investment to developing countries’ (2009) 5.

CHAPTER 3

INTERNATIONAL RULES AND THE EPZs

3.1 Introduction

The previous chapter provided a background of EPZs by explaining what they are and how they evolved over the years. It also discussed the common objectives for EPZs, and the incentives offered to attract investors to the EPZs. This chapter focuses on the relationship between international rules and the EPZs. In particular, it explains the effects of the World Trade Organization (WTO) agreements, such as the Agreement on Subsidies and Countervailing Measures (ASCM), the General Agreement on Trade in Services (GATS), and the Agreement on Trade-Related Investment Measures (TRIMs), on EPZs. It further discusses the treatment of EPZs under regional trade agreements (RTAs), as well as the implications of the ILO's standards on EPZs. Finally, this chapter concludes by providing a brief discussion of the impacts of the recently launched Sustainable Development Goals (SDGs) on EPZs.

3.2 EPZs and the international trade rules

Although EPZs are considered to be outside their countries' customs territories in terms of the Revised Kyoto Convention, they are nevertheless subject to the general laws of their host countries unless validly exempted. Thus, EPZs are subject to international laws and agreements which are binding upon their host states. For this reason, there is an obligation upon member states to ensure that their EPZ programmes are consistent with international instruments, such as the WTO agreements, the Kyoto Convention, and the ILO conventions, among others, in order to avoid the violation of international rules.

3.2.1 The Revised Kyoto Convention

The World Customs Organization (WCO) acknowledges the use of free zones as an economic policy to attract investment and facilitate trade.¹ Thus, it provides guidelines with respect to customs regulations in the economic zones under Chapter 2 of Annex D to the Revised Kyoto Convention. In that chapter the phrase 'free zone' is defined as 'a part of the territory of a

¹ S Creskoff & P Walkenhorst 'Implications of WTO disciplines for special economic zones in developing countries' (2009) 12.

contracting party where any goods introduced is generally regarded in so far as import duties and taxes are concerned as being outside the customs territory.² It also lists a number of standards to govern customs regulations applicable to the free zones.³ One of the standard requirements for the establishment and control of free zone under Chapter 2 of Annex D is that the domestic legislation should define the criteria for the development of economic zones, the types of goods permissible, and the nature of the processes such goods have to undergo within the zones.⁴ However, the Revised Kyoto Convention has a narrow focus on economic zones as it only provides for treatment of the zones products under customs regulations as opposed to regulation of zones in general.

3.2.2 EPZs and the WTO agreements

The ASCM

The WTO does not have specific rules on economic zones in any of its agreements.⁵ Despite this fact, there are certain WTO rules which have impacts on the EPZs. Of major concern with respect to the EPZs, are financial and fiscal incentives, which are offered to lure investors into the EPZs. Some of these incentives, such as the financial assistance by the host government and the tax holidays, fall within the definition of the term ‘subsidy’ as defined in Article 1 read with Annex I of the ASCM.⁶ Article 1 of the ASCM defines a subsidy as ‘a financial contribution by a government or a public body which confers a benefit to the recipient.’ In terms of this Article, loans, grants, equity infusions, loan guarantees, or forfeited government revenues qualify as financial contributions if they are made by a government or a public body. Article 3.1 of the ASCM proscribes two categories of subsidies: i) subsidies dependent on export performance and ii) subsidies dependent on the use of local over foreign goods. This means that financial benefits, either in the form of monetary grants or tax exemptions which some countries give to EPZ

² Specific Annex D to the Revised Kyoto Convention, Chapter 2
http://www.wcoomd.org/en/topics/facilitation/instrument-and-tools/conventions/pf_revised_kyoto_conv/kyoto_new/spand.aspx (accessed 01 February 2016).

³ As above.

⁴ As above.

⁵ Creskoff & Walkenhorst (n 1 above) 9.

⁶ Creskoff & Walkenhorst (n 1 above) 34.

investors on condition that the enterprise will export all or most of its products, qualify as export subsidies prohibited under the ASCM.⁷

The Panel in the *Australia - Subsidies provided to producers and exporters of automotive leather (Australia – Automotive Leather II case)* found that the grant payment in terms of the agreement between the Australian government and Australian Leather Holdings Ltd was a ‘subsidy contingent upon export performance within the meaning of Article 3(1)(a) of the ASCM’.⁸ On a similar matter, the Panel also found that the Export Financing Support Programme of Brazil (PROEX) payments for the export of Brazilian regional aircraft were ‘subsidies within the meaning of Article 1 contingent upon export performance within the meaning of Article 3(1)(a) of the ASCM’.⁹ Although the above-cited cases did not arise from the EPZs, they are an indication of how similar subsidies may be challenged.

Other subsidies, such as exemptions from import charges for products destined for the EPZs, municipal taxes value-added tax, stamp duties and transaction taxes, though not prohibited, they may nevertheless be contested by other WTO members through the WTO dispute settlement process on the basis of Article 5 of the ASCM on actionable subsidies.¹⁰

EPZs by nature are export-oriented. Therefore, any subsidy given to EPZ companies is likely to be deemed to be based on export performance requirements. Consequently, subsidies dependent on export performance should be eliminated in accordance with Article 27 of the ASCM.

Article 27 of the ASCM makes provision for special and differential treatment for developing countries with respect to prohibited export subsidies as follows:

⁷ RC Haywood & M Ouya ‘Economic processing zones incentives and the WTO agreement on subsidies and countervailing measures’ (2001) 2.

⁸ *Australia-Subsidies provided to producers and exporters of automotive leather* Report of the Panel WTO WT/DS126/R (25 May 1999) para 10.1 https://www.wto.org/english/tratop_e/dispu_e/1343d.pdf (accessed 16 March 2016).

⁹ *Brazil-Export financing for aircraft* Report of the Panel WT/DS46/R (14 April 1999) para 7.14 https://www.wto.org/english/tratop_e/dispu_e/46r.pdf (accessed 16 March 2016).

¹⁰ Commonwealth ‘Trade hot topics: Export processing zones and the WTO agreement on subsidies and countervailing measures’ Issue No. 4 <https://www.oecd-ilibrary.org> (accessed 25 January 2016).

- In terms of Article 27(2)(a) read with Annex VII (a), least developed countries (LDCs) that are categorised by the United Nations as such,¹¹ are automatically exempted from the proscription of export subsidies.¹²
- The countries listed in Annex VII (b) are excused until their Gross National Product (GNP) per capita surpasses USD 1000 at 1990 dollar value for three successive years.¹³
- Developing countries that are not mentioned under Annex VII were given until 1 January 2003 to phase out their export subsidies. However, members that met certain criteria for the extension of the transitional period were granted an extension up to the end of 2007, which was then further postponed to the end of 2015.¹⁴

It is worth noting that the phasing out period for developing countries not listed in Annex VII to the ASCM has passed. This means that developing countries that are not exempted under Annex VII are now obliged to cease providing subsidies conditional on export performance or use of local materials to comply with the ASCM. However, the so-called schedule VII countries have also to start redesigning their EPZs in preparation for their graduation from the LDCs' status. This is of particular importance considering that some WTO members, especially the developed countries, have already made proposals for revision of the ASCM to expand the list of prohibited subsidies under the on-going Doha Development Agenda.¹⁵

The GATS

Contrary to the WTO agreements applicable to trade in goods, the discussion on subsidies pertaining to trade in services is still a subject of on-going negotiations under the Doha Development Round.¹⁶ Thus, there are no prohibited subsidies relating to trade in services. On

¹¹ As of 11 December 2015 the United Nations has designated 48 countries as least developed countries (34 are WTO members). The LDCs status which is reviewed every three years is determined based on three criteria: 1) Per capita income, 2) Human assets, and 3) Economic vulnerability. (www.unctad.org/UN recognition of LDCs) (accessed 29 January 2016).

¹² Art 27(2)(a) & Annex VII(a) of ASCM.

¹³ Creskoff S & Walkenhorst (n 1 above) 23.

¹⁴ Creskoff S & Walkenhorst (n 1 above) 35.

¹⁵ Creskoff S & Walkenhorst (n 1 above) 24.

¹⁶ M Engman, O Onodera & E Pinali 'Export processing zone: Past and future role in trade and development' (2007) 49.

[http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?doclanguage=en&cote=td/tc/wp\(2006\)39/final](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?doclanguage=en&cote=td/tc/wp(2006)39/final) (accessed 15 November 2015).

the other hand, subject to exemptions and commitments in terms of the GATS, preferential treatment of services or service providers from a particular country over those from other WTO members in the EPZs may contravene the most-favoured-nation treatment principle under Article II of the GATS.¹⁷ Similarly, preferential treatment of local services or service providers over foreign services or service providers in the EPZs may contravene the national treatment principle under Article XVII of the GATS.¹⁸ Therefore, in order to remain consistent with the GATS, there should be equal treatment of services and service providers in the EPZs, irrespective of nationality.

The TRIMs

The TRIMs relates only to trade in goods.¹⁹ Article 2 of the TRIMs proscribes the use of trade-related investment measures that are incompatible with Article III on National Treatment or Article XI on General Elimination of Quantitative Restriction of the General Agreement on Tariffs and Trade (GATT). Measures such as the domestic materials and trade balancing requirements, as well as foreign exchange restrictions as illustrated in the Annex to the TRIMs, are common in the EPZs.²⁰ According to Engman *et al.*,²¹ EPZs by nature constitute a trade-related investment measure as it fits the definition of both 'investment measure' and 'trade-related', with EPZs' core objectives being to attract FDI and to promote exports. Therefore, WTO members whose EPZ programmes have requirements for 'local content, trade balancing, or foreign exchange restrictions' are inconsistent with the TRIMs.²² These countries are required in terms of Article 5 of the TRIMs to notify the Council of Trade in Goods of all such non-conforming measures and to consequently eliminate the same within two years after entry into force of the TRIMs.

¹⁷ As above.

¹⁸ Creskoff S & Walkenhorst (n 1 above) 31; Engman *et al.* (n 16 above) 49.

¹⁹ Article 1 of TRIMs.

²⁰ Engman *et al.* (n 16 above) 49.

²¹ As above.

²² W Milberg & M Amengual 'Economic development and working conditions in export processing zones: A survey of trends' (2008) 30.

3.2.3 EPZs and the RTAs

Akin to EPZs, regional trade agreements have also multiplied over recent years, resulting in most countries subscribing to more than one agreement (the famous ‘spaghetti bowl’) to promote trade and investment.²³ Whereas EPZs attract FDI, increase exports, and enhance economic growth, RTAs, on the other hand, lead to increased trade and promote integration between members to an RTA.²⁴

The existence of EPZs in countries which are part of RTAs is a contentious issue, mainly due to EPZs tariff-related incentives which have trade-distorting effects.²⁵ According to Madani,²⁶ the role which EPZs play in regional integration is not clearly defined. However, three conditions may arise: firstly, investors may be attracted to the EPZs because of the host country’s membership to an RTA that has preferential access to non-members’ markets²⁷ such as access by Southern Africa Development Community (SADC) members to the European market. Secondly, investors may be attracted to the EPZs because of an expanded market created by the formation of an RTA.²⁸ The third scenario is that investors in the EPZs will suffer if their host country is excluded from an RTA.²⁹

RTAs have implications on EPZs, especially, when an RTA creates a customs union whereby several customs territories are merged into a single customs territory. A customs union turns the regional markets into a single market.³⁰ This has the effect that the EPZ’s products that used to be exported to the customs union members’ markets can no longer be regarded as exports as those markets are converted into a common domestic market.³¹ Thus, the EPZ companies have to find other export markets to meet the export performance requirement of the EPZs or risk losing the EPZ status.

²³ S Woolfrey ‘Special economic zones and regional integration in Africa’ (2013) 1.

²⁴ T Farole & G Akinci (eds) *Special economic zones: Progress, emerging challenges and future direction* (2011) 127.

²⁵ Farole & Akinci (n 24 above) 128.

²⁶ D Madani ‘A review of the role and impact of export processing zones’ (1999) 58.

²⁷ As above.

²⁸ As above.

²⁹ As above.

³⁰ Farole & Akinci (n 24 above) 137.

³¹ As above.

Although there are no multilateral guidelines or rules on the treatment of products from the EPZs, at the regional level, rules varies from RTA to RTA. Whereas some RTAs have not made any provision for EPZs, others have incorporated special provisions on the treatment of EPZ products, into their RTAs.³² The North American Free Trade Agreement (NAFTA) for example, prohibits entry of EPZ products while the Western African Economic and Monetary Union (WAEMU) allow the granting of a certificate of origin on condition that import duties are paid on inputs.³³ Other RTAs, such as the Common Market for Eastern and Southern Africa (COMESA) and the Southern Africa Development Community (SADC) have no special provision for EPZs.³⁴ As a result, they rely on the rules of origin to control entry of EPZ products, whereby a specified ratio of the local materials used on an EPZ product would determine the eligibility of the product for duty-free market access in these RTAs.³⁵ However, the lack of regulation of EPZs in the RTAs may create a window for trade circumvention as EPZs' products enter the local markets duty-free through the territories of other RTA members.³⁶

According to Farole and Akinci,³⁷ when RTAs and EPZs coincide, synergies may be generated to reduce regional trade barriers, enhance the realisation of economies of scale of production, and attract both domestic and foreign investments in member states. Thus, there is a case for RTA members to harmonise EPZ policies in order to take full advantage of regional integration. The East African Community (EAC), recognising the potential benefits, has taken a step to harmonise EPZ policies in its configuration by establishing a common regulatory framework for EPZs in the region.³⁸ However, it remains to be seen how harmonisation of the EPZ policies within the EAC would generate the requisite synergies.

³² Engman *et al.* (n 16 above) 51.

³³ Farole & Akinci (n 24 above) 138.

³⁴ As above.

³⁵ As above.

³⁶ P Gibbon, S Jones & L Thomsen 'An assessment of the impact of export processing zones and an identification of appropriate measures to support their development' (2008) 51.

³⁷ n 24 above, 127.

³⁸ Farole & Akinci (n 24 above) 138.

3.3 EPZs and international labour standards

Employment creation is at the heart of EPZ policies. However, labour standards and relations in the EPZs have been dubious as host countries tend to relax national labour regulations as a way of enticing investors into their EPZs.³⁹ This practice has led to some workers' rights activists labelling EPZs as 'the brutal face of globalisation', mainly because of alleged violations of workers' rights by EPZs enterprises.⁴⁰ Despite some studies indicating that employment conditions within some EPZs are better than within the domestic industries, there are still concerns with respect to health and safety of workers, working hours, wages, freedom of association, the right to collective bargaining, and the special needs of female workers, especially considering that most EPZs are dominated by female workers.⁴¹

The ILO, being the international labour standards' 'watchdog', monitors EPZs in its member countries with an eagle eye due to the EPZs' impacts on the labour markets.⁴² Although the ILO acknowledges that EPZs have created high employment levels in some countries, including China, Malaysia, and Mauritius, it nevertheless stresses that the capacity of EPZs to improve employment environments, develop skills, and become competitive is weakened by the relaxation of labour legislations to restrict unionisation of the zones and the lack of enforcement of labour regulations.⁴³

To this end, the ILO's Committee of Experts on the Application of Conventions and Recommendations (CEACR) has since 1998 commented on legislation and the practices of some signatory States as pertains to the inconsistencies of their legislation and practices with the fundamental conventions ratified by them.⁴⁴ This is especially the case concerning the right to organize and join associations of choice (Nigeria, Namibia, Dominican Republic, Panama, Togo, Bangladesh), the right to collective bargaining (Turkey, Dominican Republic, Panama, Bangladesh), and the right to strike (Panama, Turkey).⁴⁵ Furthermore, the ILO Committee on

³⁹ ILO 'Employment, labour relations and working condition in EPZs'

http://training.ilo.it/actrav_cdrom1/english/global/iloepz/reports/epzre/2_2.htm (accessed 29 January 2016).

⁴⁰ Chu Yun Juliana Nam 'Competing for foreign direct investment through the creation of export processing zones: the impact on human rights' in O De Schutter (ed) *Transnational corporations and human rights* (2006) 161.

⁴¹ ILO 'Employment and social policy in respect of the export processing zones' (2003) 10.

⁴² n 41 above, 1.

⁴³ n 41 above, 7.

⁴⁴ As above.

⁴⁵ As above.

Freedom of Association have made recommendations to concerned member states on EPZ-related cases in connection with, amongst others, denial of the right to organise (Philippines), the right to establish or to memberships of associations of choice (Honduras), and the right to collective bargaining (El Salvador).⁴⁶

However, the ILO can only make comments or recommendations to member countries and hope that they will comply with the fundamental conventions as it lacks the necessary enforcement mechanisms to impose sanctions on non-compliant member states, in comparison to the WTO.⁴⁷

3.4 EPZs and environmental regulations

FDI is seen as a panacea for economic development in developing countries as it brings about much-needed technology, expertise and capital to assist developing countries in being part of the global economy.⁴⁸ However, increased FDI inflow may impact negatively on the ecosystem of the host country.⁴⁹

There is a perception that a substantial number of investors, especially polluting industries which invest in developing countries, are attracted to less stringent environmental regulations in developing countries ('pollution haven theory') where they can maximise their gains.⁵⁰ This theory essentially entails that polluting industries relocate to developing countries where there are no strict environmental regulations, and thus it is cheaper for them to comply with those lax regulations.⁵¹

Developing countries have less strict regulatory requirements, either due to lack of regulation or enforcement ('regulatory chill theory') or due to the fact that governments relax standards, especially, applying to the environment and labour, in order to compete with other countries in attracting FDI ('race to the bottom theory').⁵² This is agreeable considering that

⁴⁶ ILO (n 41 above) 8.

⁴⁷ Chu Yun Juliana Nam 'Competing for foreign direct investment through the creation of export processing zones: The impact on human rights' in De Schutter (n 40 above) 172.

⁴⁸ RK Gray 'Foreign direct investment and environmental impacts: Is the debate over' (2002) 11(3) *REICEL* 306.

⁴⁹ As above.

⁵⁰ As above.

⁵¹ European Commission 'Strict environmental law does not necessarily create pollution havens' http://ec.europa.eu/environment/integration/research/newsalert/pdf/199na2_en.pdf (accessed on 01 February 2016).

⁵² Gray (n 48 above) 306.

some developing countries see their environmental laws as soft targets. Thus, the strictness of the environmental regulations, although not determinative, influences certain investors to locate in a foreign country.⁵³

3.5 EPZs and the SDGs

Although the debate on the impacts of economic zones on the economies of developing countries is still a subject of research, it is an irrefutable fact that many developing countries regard economic zones as vital to economic development.⁵⁴ This is despite the fact that EPZs are seen by some as not being the best policy option to achieve sustainable economic development as compared to general trade and investment liberalisation.⁵⁵

Most developing countries build their EPZs around fiscal incentives, as well as lax environmental and labour regulations. These incentives have become problematic not only in relation to international trade rules but also with respect to the United Nations' SDGs.

The SDGs are a set of universal goals adopted by the United Nations in September 2015, building on the Millennium Development Goals (MDGs), to *inter alia* fight poverty, inequality and climate change.⁵⁶ UNCTAD identified Goals 8, 9, and 12⁵⁷ to be of particular significance in the context of EPZs.⁵⁸ Factors such as cheap labour and poor environmental practices ascribed to EPZs are not consistent with SDG 8. Although most SDGs can be related to EPZs in positive or negative terms, Goal 13⁵⁹ has also implications on EPZs policies, more particularly with regard to impacts of industrial pollution on the environment and climate change in general.

⁵³ As above.

⁵⁴ UNCTAD 'Enhancing the contribution of export processing zones to the sustainable development goals: An analysis of 100 EPZs and a framework for sustainable economic zone' (2015) 4.

⁵⁵ Engman *et al.* (n 16 above) 22.

⁵⁶ UN 'Sustainable development goals' <http://www.undp.org/content/undp/en/home/sdgoverview/post-2015-development-agenda.html> (accessed 11 May 2016)

⁵⁷ 'Goal 8: Promote inclusive and sustainable economic growth, employment and decent work for all; Goal 9: Build resilient infrastructure, promote sustainable industrialisation and foster innovation; and Goal 12: Ensure sustainable consumption and production patterns.' <http://www.un.org/sustainabledevelopment/sustainable-development-goals/> (accessed 01 February 2016).

⁵⁸ n 54 above, iii.

⁵⁹ 'Take urgent action to combat climate change and its impacts.

<http://www.un.org/sustainabledevelopment/sustainable-development-goals/> (accessed 01 February 2016).

On this basis, UNCTAD, having analysed 100 EPZs in 2015, recommends the restructuring of EPZs to fit in with the developments in the global arena.⁶⁰ Accordingly, UNCTAD proposes a ‘role reversal’ for EPZs to switch from the provision of inferior environmental and labour standards to centres of excellence and facilitators for sustainable economic development.⁶¹ It further recommends a framework for ‘sustainable economic zones’ to enhance the performance of labour, environment, health and safety, and economic linkages.⁶² This shows that the EPZs cannot continue to operate ‘business as usual’ in a changing environment. They have to fit in with the SDGs to remain sustainable and contribute to sustainable development.

3.6 Conclusions

This chapter discussed the implications of international rules on EPZs. Except for the WCO, which provides guidelines for the customs regulations with respect to goods produced in the economic zones, there are no specific international rules governing the EPZs in general. However, it emerged that the ASCM and TRIMs have implications on the fiscal incentives given by host countries to attract investors, and certain performance requirements imposed on EPZ investors, respectively.

The discussion on the impacts of RTAs on EPZs has also shown that treatment of EPZs under RTAs varies, with some RTAs making special provisions for EPZs’ products while others rely on the rules of origin to regulate the entry of products from the EPZs. Be that as it may, there is a case for RTA members to harmonise EPZ policies in order to maximise the benefit of regional integration.

In addition, the ILO’s conventions related to the right to organise and join associations of choice have impacts on the EPZs. Countries have a tendency to relax labour and environmental regulations in the EPZs to attract investors. This practice has led to the ILO making recommendations to member States to ensure compliance with its conventions. Thus, the ILO member States have a duty to ensure that their EPZs’ labour standards are consistent with the ILO’s conventions. This sentiment was echoed by UNCTAD in its framework for sustainable

⁶⁰ n 54 above, 23.

⁶¹ n 54 above, 1.

⁶² UNCTAD (n 54 above) 21.

economic zones, where it encourages countries to reform EPZs from being cost-saving programmes, through the provision of inferior environmental and labour standards, to centres of excellence and facilitators for sustainable economic development.

The next chapter will undertake a specific review of the legal framework underpinning the EPZ programme in Namibia. The focus will be on the Namibian EPZ Act to identify the shortcomings which hamper the achievement of the EPZ objectives in Namibia.

CHAPTER 4

THE UNDERPINNING LAW OF EPZs IN NAMIBIA

4.1 Introduction

The preceding chapter examined the implications of the WTO, the ILO, RTAs, and SDGs, amongst others, on the EPZs. In particular, it has shown that fiscal incentives and the relaxation of labour and environmental standards by developing countries as a way of attracting investments in the EPZs are not consistent with the WTO rules, the ILO standards, as well as the SDGs. This chapter examines the underpinning law of EPZs in Namibia. It commences with a discussion on the rationale for the establishment of the EPZ programme in Namibia to put the EPZs into the Namibian's socio-economic context. It also examines Namibia's experience with the EPZs, looking at the performance thus far. The crux of this chapter is the analysis of the Namibian EPZ Act as the policy instrument for the implementation of the EPZ programme in Namibia, so as to identify barriers to the achievement of the EPZ objectives. Finally, this chapter examines the compatibility of the performance requirements and fiscal incentives under the EPZ Act with the WTO rules.

4.2 Rationale for establishing the EPZ programme in Namibia

Namibia is a country of 2.403 million people and is an upper middle-income economy with a Gross National Income (GNI) per capita of US\$ 5.630, according to the World Bank's 2014 classification.¹ The GDP composition by sector is made up of 9% for agriculture and fishing, 12.3% for manufacturing, 12.3% for mining and quarrying, and 60% for services.² The country's economy depends significantly on mining activities, with the exports of minerals, predominantly diamonds, making up more than half of total exports.³ Considering the size of the population, Namibia has a relatively small domestic market.

The Labour Resource and Research Institute (LaRRI) reported in 2000 that the government was convinced that export-oriented industrialisation is the only feasible strategy for sustainable

¹ World Bank 'Namibia' <http://data.worldbank.org/country/namibia> (accessed 18 February 2016).

² Namibia trade information portal 'Economic outline' <https://www.namibiatradeinformationportal.gov.na/invest-in-namibia/economic-outline.php> (accessed 18 February 2016).

³ UNDP 'Integrating globally: Namibia's aid for trade framework and strategy' (2011) 18.

economic development given the country's small domestic market.⁴ Thus, the implementation of the EPZ programme was one of the government's strategies to expand the industrial sector and at the same time address high unemployment rates.⁵

Although EPZ programme targets manufacturing activities for exports, meat and fish processing are not eligible for EPZ status.⁶ The exclusion of meat and fish processing from the EPZ is presumed to be influenced by the Namibian Economic Policy Research Unit (NEPRU) report of 1993 on the relevance of EPZs to Namibia, that the 'non-food manufacturing sector' was the one not performing in terms of export.⁷ On the other hand, processing of minerals is eligible for EPZ status provided that an independent enterprise is registered for mineral processing or beneficiation purpose.⁸ The mineral processing companies have to be independent of the mining companies because the latter are liable for the tax and therefore, not eligible for EPZ status.⁹

The government anticipated that the EPZ programme would contribute to a diversified economy, increased exports of manufactured goods, reduction of large-scale unemployment, increased investments, and transfer of technology and skills.¹⁰ The government, in particular, expected the EPZs to create approximately 25 000 jobs between 1997 and 1999.¹¹ The benefits anticipated to flow from the EPZs are usually common to EPZs in general as explained in chapter 2 of this study.

The objective of promoting export-led industrialisation is further buttressed by Namibia's Vision 2030¹² and the Industrial Policy¹³ whereby the government envisions the manufacturing

⁴ LaRRI 'Export processing zones in Namibia: Taking a closer look' (2000) 40.

⁵ LaRRI (n 4 above) 39.

⁶ Namibia Investor Guide 'Export processing zone industrial development strategy: Harnessing Namibia's manufacturing and exporting potential' 3

<http://www.embassyofnamibia.org.br/investments/Namibias%20Export%20Processing%20Zone.pdf> (accessed 21 March 2016).

⁷ R Sherbourne 'Export processing zones and their relevance to Namibia' (1993) 22.

⁸ Namibia Investor Guide (n 6 above) 5.

⁹ As above.

¹⁰ Section 3 of the Export Processing Zone Act 9 of 1995.

¹¹ LaRRI (n 4 above) 41.

¹² 'A document that clearly spells out the country's development programmes and strategies to achieve its national objectives' see <http://www.gov.na/vision-2030> (accessed 12 March 2016).

¹³ Ministry of Trade and Industry 'Namibia's Industrial Policy (2012).

sector to contribute at least 70 percent of total export by the year 2030.¹⁴ Thus, the EPZ programme fits in the national industrialisation strategy.

4.3 Namibia's EPZ experience

In order to determine whether or not the EPZ programme has achieved its objectives, it is important to assess the performance against the set objectives. In 1996, approximately 100 EPZ enterprises were registered.¹⁵ However, in 1999, there were only nine EPZ enterprises in business which employed roughly 400 people.¹⁶ In 2007, there were 20 EPZ companies in operation, of which nine were involved in manufacturing and the remainder were involved in the processing of minerals, altogether employed 5173 people.¹⁷ The Offshore Development Company (ODC) reported that in 2012 there were 23 EPZ companies which employed 2532 people.¹⁸ However, EPZ jobs increased up to 10 000 in 2004 due to the Ramatex investment.¹⁹ The sharp decline in the number of jobs between 2007 and 2012 can be attributed to the closure of Ramatex operations in 2008. Generally, the EPZ performance from the perspective of job creation is disappointing considering that the target was to create 25 000 EPZ jobs between 1997 and 1999.²⁰

In terms of investment, there were also a large number of withdrawals of EPZ status as the number of enterprises dropped from 100 enterprises in 1996 down to only 23 in 2012. Nevertheless, ODC reported diverse investments in activities such as manufacturing, assembling and processing.²¹ The investment value has also been reported to have doubled from N\$5.0 billion in 2011 to N\$12.7 billion in 2012, credited mainly to huge investments by Areva Processing, and reinvestments by Namzinc and Dundee Precious Metals Tsumeb.²² However, despite the huge investments by these mineral processing companies, the number of enterprises and the quality of investments in the EPZs are still worryingly low.

¹⁴ Office of the President 'Namibia Vision 2030: Policy Framework for long term national development' (2004) 16.

¹⁵ C Rosendahl 'Industrial policy in Namibia' (2010) 23 24.

¹⁶ LaRRI (n 7 above) 8.

¹⁷ Rosendahl (n 15 above) 24.

¹⁸ ODC 'Annual Report'(2012/2013) 13.

¹⁹ H Jauch 'Africa's clothing and textile industry: the case of Ramatex in Namibia' in H Jauch & R Traub-Merz (eds) *The future of textile and clothing industry in sub-Saharan Africa* (2006) 215.

²⁰ LaRRI (n 4 above) 41

²¹ ODC (n 18 above) 13.

²² As above.

Part of the objectives is to increase exports and expand foreign exchange earnings. The ODC reported that exports increased from N\$7.6 billion in 2011 to N\$8.2 billion in 2012.²³ Although gross exports may be impressive, the actual contribution to foreign exchange earnings may be minimal considering the value of imports into the EPZs. According to LaRRI, nearly all EPZ enterprises import machineries, raw materials, and inputs into the EPZs.²⁴ Therefore, the gains from foreign exchange earnings in case of foreign EPZ enterprises are only realised when the enterprise exchanges foreign currency into local currency to pay for wages and services provided by local companies.²⁵ This is agreeable considering that, in Namibia, foreign enterprises are allowed to maintain foreign currency bank accounts and to repatriate their capital and profit without restrictions.²⁶ However, the reinvestments by Namzinc and Dundee Metals mean that the raw materials are sourced in Namibia and thus it also plays a role in increasing the net exports, as well as foreign exchange earnings. By and large, the absence of trade deficit between exports and imports in the EPZs is an indication that the Namibian EPZ contributes to the country's overall exports, albeit marginally.

In terms of technology and skills transfer, benefits are negligible, as there is no evidence of imitation or copying of products by workers who left the EPZ companies or shareholding by Namibians in foreign EPZ companies.²⁷ Lack of evidence makes the assessment of this objective inconclusive.

On the other hand, ODC reported backward linkage in the form of procurement of local goods and services such as transport and logistics, utilities, information technology, auditing, cleaning, security, and insurance.²⁸ However, since the achievement from backward linkage reported by ODC is not quantified, it makes it difficult to conclude on the extent of backward linkage into the domestic economy.

On the whole, the performance of the Namibian EPZ has not been satisfactory, because even where positive growth has been recorded, such as for exports contribution, the growth is

²³ n 18 above, 13.

²⁴ n 4 above, 9.

²⁵ D Madani 'A review of the role and impact of export processing zones' (1999) 24.

²⁶ Namibia Investor Guide (n 6 above) 4.

²⁷ Rosendahl (n 15 above) 25.

²⁸ n 18 above, 13.

miniscule. This is why critics such as Jauch²⁹ condemns EPZs for not providing solutions to unemployment as they only create second class jobs, and do not increase foreign exchange earnings or lead to any significant skills transfer. Therefore, it can be safely concluded that the EPZ programme in Namibia has not satisfactorily succeeded in attracting quality investments, creating large-scale employment, and there is also no evidence of technology and skills transfer.

The RAMATEX investment

One cannot review the Namibian EPZ regime without making reference to the Ramatex investment. The Ramatex investment provides lessons that could inform future dealings with investors to avoid a repeat of past mistakes. Ramatex, a Malaysian clothing and textile company, set up its EPZ plants in 2001 in Windhoek, whereby it sourced cotton from West Africa and exported its finished products to the US under the US preferential trade arrangement granted to Namibia under AGOA.³⁰ In order to attract Ramatex to Namibia, the government made generous concessions, in addition to those already provided for under the EPZ Act.³¹ Such concessions include heavily subsidized water and electricity, land use tax exemption for 99 years, and tailored infrastructure development.³²

Ramatex employed approximately 8000 people, of which 6000 were Namibian nationals.³³ This was the largest number of employment created by a single EPZ investor since the inception of the EPZ programme. Therefore, huge costs incurred by the government to secure the Ramatex investment were justified considering the number of jobs created.³⁴

However, the Ramatex investment was short-lived. The company started to close down some of its factories in 2005 due to lack of orders, and eventually terminated its entire investment in 2008, allegedly due to competition from China.³⁵ Ramatex was characterised by controversies surrounding unfair labour practice, poor working conditions, and low wages, amongst others, which led to fierce resistance from trade unions and workers and resulted in a

²⁹ H Jauch 'Export processing zones and the quest for sustainable development: A Southern African perspective' (2002) 14 Environmental & Urbanisation 111.

³⁰ Rosendahl (n 15 above) 25.

³¹ Jauch (n 19 above) 216.

³² As above.

³³ Rosendahl (n 15 above) 25.

³⁴ Jauch (n 19 above) 216.

³⁵ Rosendahl (n 15 above) 25.

number of strikes.³⁶ It also emerged that the costs in terms of social as well as environmental side-effects far exceeded the benefits of the investment.³⁷ Consequently, Ramatex left behind far-reaching environmental damages³⁸ and a huge ‘white elephant’ in the form of big factory buildings.

Ramatex investment was a classic example of how transnational corporations use their bargaining powers to get disproportionate concessions from developing countries that are desperate for FDI.³⁹ Thus, according to Jauch,⁴⁰ one crucial lesson that should be learned from the Ramatex investment to avoid similar mistakes in the future is that national laws should guide future negotiations with foreign investors to assist the government to choose investments which enhance to the sustainable economic development.

4.4 An overview of the Namibian EPZ Act

4.4.1 The scope and objectives

The EPZ Act regulates ‘the establishment, development, and management of EPZs in Namibia’.⁴¹ The objectives are to promote the processing of goods targeting foreign markets, create employment for the masses, expand earnings from exports, and encourage technology and skills transfer.⁴² These are typical objectives for traditional EPZs, as discussed in chapter 2 above. On the whole, these objectives target export-oriented enterprises. The model name ‘export processing zone’ says it all. This means that the objective is to process for export purposes. According to Farole and Akinici,⁴³ this conventional EPZ model can no longer be sustained when the labour costs become high or the preferential market access is eroded. On this basis, the scope of the EPZ regime is too narrow to accommodate rapidly changing socio-economic conditions, both at national and global levels.

³⁶ As above.

³⁷ Rosendahl (n 15 above) 25.

³⁸ Africa Files ‘Namibia: Who will clean up after Ramatex’ <http://www.africafiles.org/article.asp?id=13872> (accessed 19/03/2016).

³⁹ Jauch (n 19 above) 225.

⁴⁰ H Jauch ‘The Ramatex closure in Namibia: Hard lessons to be learned’ *The Namibian* 14 March 2008. <http://www.namibian.com.na/index.php?id=46344&page=archive-read> (accessed 14 March 2016).

⁴¹ Long title to the EPZ Act.

⁴² Section 3 of the EPZ Act.

⁴³ T Farole & G Akinici (Eds) *Special economic zones: Progress, emerging challenges, and future directions* (2011) 4.

4.4.2 What is an EPZ under the EPZ Act?

Section 1 of the EPZ Act defines an export processing zone as ‘an export processing zone established under section 2 or by section 19.’ Whereas, section 2 of the EPZ Act deals with the establishment of EPZs in any part of the country, section 19, on the other hand, specifically establishes the Walvis Bay EPZ. Therefore, according to this definition, an EPZ in Namibia can only be that which has been established in accordance with either section 2 or 19 of the EPZ Act.

4.4.3 Establishment of EPZs in Namibia

The Minister responsible for trade and industry (the Minister), in consultation with the Minister responsible for finance, has the power to establish EPZs and determine their locations, extents and borders in any part of the country.⁴⁴ An EPZ may contain one factory entity or a cluster of factories in terms of section 2(2) of the EPZ Act. This means that Namibia adopted a hybrid EPZ model, whereby single factory enterprises, as well as the traditional EPZ in a specific enclosed area, may be established. The rationale behind the promotion of a single factory unit is to allow existing enterprises that desire to benefit from an EPZ status to do so in their current locations so as to avoid costs of relocating to EPZ parks.⁴⁵ It also allows enterprises to set up factories close to factors of production such as raw materials or labour. However, single factory enterprises may not enjoy the luxury of high standard infrastructures and streamlined administrative services available to enterprises located within the zones.⁴⁶

While all other EPZs may be established in terms of section 2 of the EPZ Act, the Walvis Bay EPZ is specifically established in terms of section 19 of the EPZ Act. This is the first EPZ established in Namibia and also the most strategically located as it is situated near the main harbour. This makes it an attractive location for investors with respect to the costs of transportation of their products.

⁴⁴ Sec 2(1) of the EPZ Act.

⁴⁵T Farole *Special economic zones in Africa: Comparing performance and learning from global experiences* (2011) 29.

⁴⁶ HCAW Schulz ‘The free-trade-zone programmes of Namibia and Mauritius and the latest developments in Europe: Lessons for South Africa’ (1999) 32 *Comparative and International Law Journal of Southern Africa (CILSA)* 172.

4.4.4 Admission of EPZ investors

To set up its investment in the EPZ, an investor must first apply for a certificate to establish or conduct an enterprise in the EPZ from the EPZ management company responsible for a specific EPZ.⁴⁷ In terms of section 14(2) of the EPZ Act, the management company has to consult with the Minister, the Minister of Finance, and the Central Bank before it approves or rejects the application. On the other hand, an applicant for a single factory EPZ enterprise's certificate has to apply directly to the Minister in terms of section 2(3) of the EPZ Act.

An EPZ certificate cannot be issued if the investment activities pose a danger to the environment; the investor will use any prohibited material or produce prohibited goods; the investment will not create employment or increase export earnings; the applicant has no intention of engaging in manufacturing, exporting and importing in the EPZ; the applicant plans to conduct a retail business in the EPZ; or the applicant does not comply with any other requirements as may be determined by the regulations.⁴⁸ Some of the condition precedents for an EPZ certificate, especially the export performance requirements, are contentious at the WTO. This is discussed later in this chapter.

4.4.5 Restrictions on goods produced in the EPZs

Except with the requisite approvals, conducting a business or selling goods imported or manufactured in the EPZs; consuming goods manufactured in the EPZs; or removing goods manufactured in the EPZs, except for exporting outside Namibia, is prohibited.⁴⁹ These restrictions proscribe the sale of EPZ products into the domestic market, justifiably to prevent unfair competition between domestic companies and EPZ enterprises that produce competing products, considering that domestic companies pay import duties and other taxes while EPZ companies are exempted. EPZ companies have to export all or at least 70 percent of their products, which means that only 30 percent of their products may be allowed into the domestic market, provided prior approval is obtained.⁵⁰

⁴⁷ Sec 14(1) of the EPZ Act.

⁴⁸ Sec 14(5) of the EPZ Act.

⁴⁹ Sec 4(1)(a) of the EPZ Act.

⁵⁰ Namibia Investor Guide (n 6 above) 4.

The restriction of the sale of the EPZ manufactured goods in the domestic market is an impediment to the successful implementation of the EPZ programme. This is so, especially, with respect to small and medium enterprises (SMEs) that have no capacity to export to global markets but that can export into the Southern Africa Customs Union (SACU) market. However, since the SACU market is regarded as part of the domestic market because of the common external tariffs, exports in the context of the Namibian EPZ is only considered to be export outside the SACU market. Had domestic sale not been restricted, SMEs would invest in the EPZs and take advantage of infrastructural and fiscal incentives to create employment and promote the competitiveness of the local businesses.

4.4.6 Incentives under the EPZ Act

Namibia, like most developing countries, offers incentives to lure investors into the EPZs. The incentives offered under the EPZ Act include fiscal or tax incentives, as well as other incentives such as regulatory and financial incentives.

4.4.6.1 Fiscal incentives

Sales tax, additional sales duty, and value-added tax

Section 5(1)(a) of the EPZ Act exempts payment of sales tax on goods imported into the EPZs, as well as on services delivered in the EPZs. Additionally, section 5(1)(b) of the EPZ Act exempts payment of additional sales duty payable in terms of section 5 of the Additional Sales Duty Act 11 of 1993 on goods imported into or manufactured in the EPZs. The Sales Tax Act 5 of 1992 and the Additional Sales Duty Act 11 of 1993 are repealed in whole by the Value Added Tax Act 10 of 2000 (the VAT Act).⁵¹ However, according to Kellaway,⁵² the repeal of a law, the provision of which are incorporated in another law (incorporating law), does not automatically repeal the provisions of the incorporating law, except if the repealing law has expressly repealed the provisions of the incorporating law. Since the VAT Act (the repealing law) does not repeal or amend the relevant provisions of the EPZ Act (the incorporating law), the exemptions from sales tax and additional sales duty still stand, although it became redundant since the sales tax and

⁵¹ Schedule VII to the VAT Act.

⁵² EA Kellaway *Principles of legal interpretation of statutes, contracts and wills* (1995) 248.

additional sales duty are no longer applied in Namibia after the repeal of the enabling laws by the VAT Act.

The VAT Act makes provision for levying and payment of VAT on goods and services. In Namibia, persons, including enterprises, pay 15 percent value-added tax on all taxable goods or services.⁵³ However, EPZ enterprises and EPZ management companies are exempted from paying VAT on goods or services within an EPZ.⁵⁴

Customs and excise duty

Goods produced in or imported into the EPZs are exempt from customs and excise duty payable in terms of the Customs and Excise Act 91 of 1964.⁵⁵ However, goods moved from the EPZs into the domestic market are considered to be goods imported into Namibia hence are subject to taxation in accordance with the Customs and Excise Act.⁵⁶ The Customs and Excise Act 91 of 1964 is repealed by the Customs and Excise Act 20 of 1998.⁵⁷ However, since the latter Act does not amend the EPZ Act, the customs and excise duties exempted are, as in terms of Act 91 of 1964 and not in terms of Act 20 of 1998.⁵⁸

Where goods manufactured in the EPZ conform to the criteria for local content, the process involved in manufacturing and the cost of production as prescribed, the Commissioner of Customs and Excise shall certify such goods as originating in Namibia.⁵⁹ This is especially significant considering that most RTAs require goods qualifying for preferential treatment to meet specified originating criteria.

Stamp and Transfer Duties

In terms of section 5(1)(c) of the EPZ Act, specified legal instruments relating to lease, hypothecation, or transfer of movable and immovable properties within the EPZ are exempted from payment of stamp duty payable on such instruments in terms of section 3 of the Stamp Duty Act 15 of 1993 read with schedule 1 to that Act. Similarly, transfer duty payable in terms of

⁵³ Sec 6 of the Value Added Tax Act.

⁵⁴ Sec 6(4) of the VAT Act.

⁵⁵ Sec 5(1)(b) of the EPZ Act.

⁵⁶ Sec 5(3) of the EPZ Act.

⁵⁷ Schedule 9 to Customs and Excise Duty Act.

⁵⁸ See n 52 above.

⁵⁹ Sec 6(3) of the EPZ Act.

the Transfer Duty Act 14 of 1993 is also exempt in terms of section 5(1)(d) of the EPZ Act with respect to the purchase of immovable properties located in the EPZs.

Income Tax

Whereas ordinary companies in Namibia currently pay 32 percent income tax,⁶⁰ EPZ management companies and enterprises are exempt from payment of income tax payable in terms of the Income Tax Act 24 of 1981.⁶¹ Usually, incentives such as exemption from income tax are offered for a limited period, known as ‘tax holiday’.⁶² However, the income tax exemption in terms of the EPZ Act is indefinite. This means that EPZ enterprises need never pay income tax for as long as their EPZ certificates remain valid.

4.4.6.2 Other Incentives

Application of the Labour Act to the EPZs

The EPZ Act initially suspended the enforcement of the Labour Act 6 of 1992, in the EPZs.⁶³ The government deemed the suspension necessary to allay investors’ fear of potential labour unrests.⁶⁴ However, the suspension led to a public outcry, especially, from the labour unions, which resulted in the National Union of Namibian Workers (NUNW) threatening to challenge the constitutionality of the concerned provision of the EPZ Act.⁶⁵ However, before legal battles commenced, the government and the NUNW reached a compromise to amend the EPZ Act.⁶⁶ Subsequently, section 8 of the EPZ Act was amended by section 1 of the EPZ Amendment Act 6 of 1996 to the effect that the Labour Act 6 of 1992 was applicable in the EPZs, but employers and employees in the EPZs were prohibited from partaking in the lock-outs and strikes, respectively, for a period of five years.

⁶⁰PWC ‘Republic of Namibia’ <http://www.pwc.com/gx/en/services/tax/corporate-tax/worldwide-tax-summaries/downloads.html> accessed (21 March 2016).

⁶¹ Sec 7(2) of the EPZ Act.

⁶²M Engman, O Onodera & E Pinali ‘Export Processing zone: Past and future role in trade and development’ (2006) 17

[http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?doclanguage=en&cote=td/tc/wp\(2006\)39/final](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?doclanguage=en&cote=td/tc/wp(2006)39/final) (accessed 15 November 2015).

⁶³ Sec 8 of EPZ Act before the amendment.

⁶⁴ LaRRI (n 4 above) 54.

⁶⁵ As above.

⁶⁶ As above.

Nonetheless, in terms of section 8(10) of the EPZ Act, the provisions of section 8 of the EPZ Act as amended would be deemed to be repealed if the legislature does not revive it within a period of five years after the commencement of the EPZ Amendment Act. Since the provision of section 8 has not been revived, it is now deemed to have been repealed as of 25 June 2001, and therefore has ceased to exist in the EPZ Act. This means that from 25 June 2001 the Labour Act 6 of 1992 became fully applicable to the EPZs in Namibia. The Labour Act 6 of 1992 has since been repealed by the new Labour Act 11 of 2007, which is also fully applicable to the EPZs since it is deemed that the EPZ Act no longer restricts the application of the Labour Act to the EPZs.

The exclusion of the entire Labour Act, and the consequent amendment outlawing strikes under the EPZ Act, led to the CEACR making several observations and direct requests for the government to bring the provisions of the EPZ Act concerned in compliance with the Freedom of Association and Protection of the Right to Organize Convention, 1948 (No. 87); and the Right to Organize and Collective Bargaining Convention, 1949 (No. 98), ratified by Namibia.⁶⁷ However, section 8(10), the deeming provision, became effective before the government could heed the CEACR's recommendations to repeal the concerned provisions of the EPZ Act.

The lesson learned from these types of incentives is that national policy instruments should always take into consideration the country's international obligations.

Training of Namibian citizens

The government committed itself to refund the EPZ management companies and enterprises 75 percent of expenditures incurred directly in providing training to Namibian citizens employed by EPZ management companies or enterprises.⁶⁸ However, refunding only takes place if training

⁶⁷ Observation (CEACR) - adopted 1997, published 86th ILC session (1998); Observation (CEACR) - adopted 1998, published 87th ILC session (1999); Observation (CEACR) - adopted 1999, published 88th ILC session (2000); Observation (CEACR) - adopted 2000, published 89th ILC session (2001); Observation (CEACR) - adopted 2002, published 91st ILC session (2003); Observation (CEACR) - adopted 2004, published 93rd ILC session (2005) Direct Request (CEACR) - adopted 1997, published 86th ILC session (1998); Direct Request (CEACR) - adopted 1999, published 88th ILC session (2000); Direct Request (CEACR) - adopted 2001, published 90th ILC session (2002) http://www.ilo.org/dyn/normlex/en/f?p=1000:13100:0::NO:13100:P13100_COMMENT_ID:2165926 (Accessed 26 February 2016.)

⁶⁸ Sec 25(1) of the EPZ Act.

was approved in accordance with section 25(2) of the EPZ Act. This is an incentive offered by the government to promote the objective of skills transfer and human development.

Expropriation and compensation

Foreign investors are most concerned about the safety and security of their investments, especially in host states with an unstable political environment. Fortunately, Namibia is politically stable. In addition to a politically stable environment which offers an investment friendly climate, Namibia guarantees EPZ investors' properties protection against expropriation without compensation.⁶⁹ Expropriation of EPZ investors' properties has to be done in accordance with the provision of Article 16(2) of the Namibian Constitution and procedures laid down in the Expropriation Ordinance 13 of 1978.⁷⁰ Accordingly, compensation for expropriated properties must be 'just, paid without undue delay and in freely convertible currency'.⁷¹

Compensation has been a controversial issue under international law as there are no uniform international standards on compensation.⁷² However, the trend, especially in the bilateral investment treaties (BITs), is that states often adopt the Hull Formula of 'prompt, adequate and effective' compensation, as it is regarded as being of a high standard of protection, especially by developed states.⁷³ The standard on compensation in terms of the EPZ Act, except for the use of the term 'just' as opposed to 'adequate', is not different from the Hull Formula. In any case, according to Nikiema,⁷⁴ various writers argue that the terms are interchangeable. Therefore, the standard of compensation in terms of the EPZ Act is of an international standard and thus an incentive to investors.

Settlement of Disputes

It is appealing to foreign investors if they are guaranteed that investor-host state disputes would be settled by an impartial body located in a third party state.⁷⁵ In terms of section 17 of the EPZ Act, disputes concerning compensation for expropriation or the validity of certificates between

⁶⁹ Sec 16 of the EPZ Act.

⁷⁰ Sec 16(1) of the EPZ Act.

⁷¹ Sec 16 of the EPZ Act.

⁷² M Sornarajah *The international law on foreign investment* (2010) 208.

⁷³ Sornarajah (n 72 above) 211.

⁷⁴ SH Nikiema 'Compensation for expropriation' (2013) 10.

⁷⁵ Sornarajah (n 72 above) 102.

the holders of EPZ management companies or EPZ enterprises certificates may either be settled through arbitration or local remedies. For a dispute to be settled through arbitration, the certificate holder has to select arbitration during the application for a certificate so that the certificate specifies that arbitration is the method of dispute settlement.⁷⁶ The certificate is proof of consent between the government and certificate holder to abide by arbitration.⁷⁷ An arbitration award is final and binding on the holder of a certificate and the government, respectively.⁷⁸

Even though arbitration may be the method of choice in terms of the certificate, the government, and the certificate holder may agree to have the dispute resolved in a competent local court.⁷⁹ Similarly, where the certificate does not indicate arbitration as a method of dispute settlement, a dispute can be settled in a local court with jurisdiction.⁸⁰ This means that EPZ investors are at liberty to choose their preferred dispute settlement method and are not restricted to local remedies if they do not have confidence in the local institutions. However, the Namibian judiciary is considered to be free from political interferences and effective in enforcing property rights.⁸¹ Furthermore, the *Kessl v Ministry of Lands, Resettlement and others and two similar cases (Kessl case)*,⁸² where the court found in favour of the three German nationals with respect to the expropriation of their farms by the government, was a test for the credibility and impartiality of the Namibian judiciary.

It is also important to note that a certificate may not have specified arbitration as a method of dispute settlement. However, a dispute between the holder of an EPZ certificate and the government may nevertheless be decided through arbitration, if the EPZ certificate holder's home country and Namibia have entered into a BIT which provides for arbitration. On this basis, the flexibility with respect to the settlement of host states investor disputes is an advantage to foreign investors.

⁷⁶ Sec 17(1) of the EPZ Act.

⁷⁷ Sec 17(2) of the EPZ Act.

⁷⁸ Sec 17(3) of EPZ Act.

⁷⁹ Sec 17(4)(b) of the EPZ Act.

⁸⁰ Sec 17(4)(a) of the EPZ Act.

⁸¹ U.S. State Department 'Namibia Investment Climate Statement' (2015) 8

<http://www.state.gov/documents/organization/241886.pdf> accessed on (15 March 2016).

⁸² *Kessl v Ministry of Lands, Resettlement and others and two similar cases* 2008 (1) NR 167 (HC).

4.4.7 Development and management of EPZs

In terms of section 10(1) of the EPZ Act, development and management of each EPZ is to be carried out by an EPZ management company appointed by the Minister. The powers, duties, and functions of the management companies include: establishment of adequate fencing, walls, enclosures or demarcation; identification and securement of EPZ to the satisfaction of the Minister; subdivision of an EPZ into plots, streets, and construction of buildings for leasing; supplying of water and electricity; and the imposition and charging of levies.⁸³ Management companies have the same roles as the local authorities within the EPZ in relation to planning, zoning, and subdivisions.⁸⁴

A foreign-owned company that satisfies the conditions set by the Minister may be appointed as an EPZ management company since there is no requirement that the management company should be Namibian owned.⁸⁵ Similarly, a private or public company may be appointed to develop and manage an EPZ.

Conditions for the appointment of management companies may be made by the Minister in the regulations or the Minister may simply determine and specify such conditions in the agreement with the management company so appointed.⁸⁶ Since there are no regulations setting out conditions for the appointment of management companies in accordance with section 10(1)(a) of the EPZ Act as of yet, the Minister has unfettered discretion when appointing management companies.

Although there are several EPZs in the country, only one management company, the Walvis Bay EPZ Management Company, exists.⁸⁷ Other EPZs are developed and managed by the ODC.⁸⁸ This means that, except for the Walvis Bay EPZ, the ODC is monopolising the development and management of EPZs in the country. This is an anomaly for the ODC to play the role of EPZ developer, manager and at the same time, the regulator of the EPZ regime. The lack of clear rules and procedure for the appointment of EPZ management companies and ODC's

⁸³ Sec 13 of the EPZ Act.

⁸⁴ Sec 5 (1)(e) of the EPZ Act.

⁸⁵ LaRRI (n 4 above) 44.

⁸⁶ Sec 10 (a) and (b) of the EPZ Act.

⁸⁷ ODC (n 18 above) 24.

⁸⁸ LaRRI (n 4 above) 44.

involvement in the development and management of EPZs are likely to discourage private companies from participating in the development and management of EPZs.

4.4.8 Administration and regulation of EPZs

Appointment of the Offshore Development Company

Section 26(1) and (3) of the EPZ Act empowers the Minister to appoint a private company as the Offshore Development Company (ODC) to be responsible for promoting, marketing, coordinating and monitoring approved activities in the EPZs.

To achieve the overall purpose, the ODC has to:

- provide an ‘umbrella service’ to all companies approved to invest in the EPZs;
- adopt and execute a promotional and marketing plan for the EPZ;
- advise the Minister on all issues, activities and developments related to EPZ management companies and enterprises, and other offshore enterprises both locally and internationally;
- advise the Minister on the need to amend existing laws or draft new laws to govern the EPZs; and
- coordinate and cooperate with other government ministries to ensure the development of human capital and infrastructure.⁸⁹

In terms of section 27(2) of the EPZ Act, the government has to hold at least 9% of the total equity in the ODC and at least one representative on the board. The use of the phrase ‘at least’ implies that the government can have more than 9% shareholding and more than one representative on the ODC board. However, due to the fact that ODC has to be a private company in terms of section 26(1) of the EPZ Act, it means that government may not have the majority shareholding and representation in the ODC. In 2000, LaRRI⁹⁰ reported that the government held 15% shares in ODC in. In 2010, the government had 95% of shares in ODC,

⁸⁹ Sec 26(3) of the EPZ Act.

⁹⁰ LaRRI (n 4 above) 43.

allegedly, due to due to lack of interest in ODC's shares from the private sector.⁹¹ Recently, Cabinet approved the Ministry of Industrialisation, Trade and Small Medium Enterprises Development to acquire the remainder of privately owned shares of 1.1525 in ODC.⁹² The acquisition is necessitated by the government's decision to merge the ODC with the Namibia Development Corporation (NDC) into a new agency, the Namibia Industrial Development Agency (NIDA), to cut the costs of running the two entities.⁹³ The merger would be formalised once the current draft NIDA Bill is passed into law. NIDA is expected to assume the responsibilities of both the ODC and NDC in terms of the EPZs Act⁹⁴ and the NDC Act 18 of 1993, respectively.⁹⁵ This means that NIDA will oversee the entire national industrial policy.⁹⁶ Since the study of the implications of NIDA on the EPZ is not part of this study, suffice to say that the amalgamation of ODC and NDC would have implications on the EPZ considering that the EPZ will not have a dedicated administrative and regulatory body.

The powers, functions and duties of the ODC

In terms of section 29 of the EPZ Act, the ODC may, with the approval of the Minister:

- partner with other entities to advance the establishment and development of EPZs;
- facilitate and promote the establishment of facilities and services to support the EPZ enterprises; and
- determine charges or levies to be paid by enterprises and to establish criteria for management and operation of EPZs.

In addition, the ODC is also responsible for developing and leasing industrial and business sites and factory units to other businesses outside the EPZs.⁹⁷ It is not clear where this mandate for the

⁹¹ Rosendahl (n 15 above) 23.

⁹² 'NIDA to swallow ODC and NDC' *New Era Newspaper* 22 May 2015
<https://www.newera.com.na/2015/05/22/nida-swallow-ndc-odc/> (accessed 15 March 2016).

⁹³ As above.

⁹⁴ Sec 35(1) of the draft NIDA Bill 2015 (1) would repeal section 26(1) of the EPZ Act which deals with the appointment of ODC, Sec 27 on the incorporation of ODC and sec 28 on public disclosure. Sect 35(2) stipulates that NIDA will assume ODC's powers, duties and functions under the EPZ Act.

⁹⁵ Sec 34 of the draft NIDA Bill 2015 (1) would repeal NDC Act in whole.

⁹⁶ Sec 3 of the draft NIDA Bill 2015 (1).

⁹⁷ Ministry of Trade and Industry 'Offshore Development Company' www.mti.gov.na/odc.html (accessed 17 March 2016).

ODC is drawn from considering the fact that the Minister has not made any regulations to vest the ODC with additional powers in terms of section 26(4) of the EPZ Act.

While the ODC's role in terms of the EPZ Act is that of the coordinator, promoter, administrator, advisor, and regulator in terms of sections 26 (3) and 29(d) of the EPZ Act respectively, the ODC is also acting as a management company for the rest of the EPZs in the country. According to the FIAS, this practice of regulators being involved in zone development and management leads to a conflict of interests as they compete with the private sector.⁹⁸ Clearly, the ODC has conflicting roles with the EPZ management companies, especially with regard to the development and operating of EPZs as it plays roles of EPZ developer, manager, administrator, as well as the regulator.

The ODC's engagement in development and management of EPZs makes these aspects of EPZs less attractive to the private sector as they fear unfair competition due to the lack of a level playing field. Therefore, the absence of a clearly defined private sector participation framework for zone development and operation contributes to the non-participation of the private sector.

Regulations relating to the EPZs

The Minister is empowered to make regulations for the effective implementation of the EPZ Act.⁹⁹ Matters which are required to be determined under the regulations include the conditions for the appointment of management companies and the conditions to be met by applicants for EPZ certificates in terms of sections 10(1)(a) and 14(5)(e) of the EPZ Act. However, to date, the Minister has not made any regulations in terms of the EPZ Act.

The absence of regulations, especially with respect to the application of the certificate for EPZ management companies or enterprises in terms of sections 10 and 14 of the EPZ Act respectively, brings uncertainties regarding the procedures and criteria employed by the government in this process. It also raises the question of transparency, which discourages potential investors from applying for appointment as EPZ management companies. Thus, the absence of regulations thwarts the attractiveness of the EPZs to the private companies due to uncertainties and lack of transparency.

⁹⁸FIAS 'Special economic zones: Performance, lessons learned and implications for zone development' (2008) 21.

⁹⁹ Sec 24 of the EPZ Act.

4.5 Compatibility of the EPZ Act with WTO rules

Namibia's membership of the GATT dates as far back as 15 September 1992, and it subsequently joined the WTO on 1 January 1995.¹⁰⁰ The consequence that flows from such membership is the respect for international obligations assumed under the WTO agreements. Thus, as far as the EPZ Act is concerned, the provisions that have to be tested for compatibility with the WTO rules are the ones that prescribe measures that have trade-distorting effects. The most controversial as discussed in chapter 3, are the fiscal or tax incentives and performance requirements, which are not consistent with the ASCM and the TRIMs, respectively.

4.5.1 The EPZ Act and the ASCM

As a general rule, subsidies based on the use of local materials over imported materials, or conditional on exports, are prohibited in terms of the ASCM.¹⁰¹ A subsidy is defined as 'a financial contribution by a government or a public body which confers a benefit to the recipient.'¹⁰² Loans, grants, equity infusions, loan guarantee, or forfeited government revenues qualify as financial contributions if made by a governmental or a public body.¹⁰³ The EPZ Act makes provision for the government to forfeit revenue which it could otherwise receive or collect in the ordinary course of business. In particular, sections 5 and 7 the EPZ Act forfeits customs and excise duties, stamp duty, transfer duty, and corporate tax. These fiscal incentives are financial contributions given by the government in the form of forgone government revenue in the context of Article 1 of the ASCM. Since they are given on condition that the investor will export its products, they fall within the definition of export subsidies, which are prohibited in terms of Article 3 of the ASCM. Therefore, the fiscal incentives offered in terms of sections 5 and 7 of the EPZ Act are not consistent with the WTO rules on subsidies.

Needless to say, the inconsistencies of these incentives with the WTO rules could bring uncertainties to investors as multinational corporations may be cautious to invest in a regime where their investments may be negatively affected if such incentives were to be challenged.

¹⁰⁰ WTO 'Namibia and the WTO' www.wto.org/english/e/country/e/namibia (accessed 06 March 2016).

¹⁰¹ Art 3 of the ASCM.

¹⁰² Art 1 of the ASCM.

¹⁰³ As above.

Therefore, fiscal incentives under the EPZ Act may be barriers to the achievement of the EPZ objective of attracting quality FDI.

4.5.2 The EPZ Act and the TRIMs

The question here is whether or not export performance requirements imposed by the EPZ Act violate the Agreement on TRIMs. Section 14(5)(d) and (e) of the EPZ Act expressly stipulate that an investor would not be issued with an EPZ certificate except if its investment will create employment; result in export earnings; or conduct a business of manufacturing, exporting or importing into EPZs, respectively. This provision makes the export performance a compulsory requirement for EPZ investors. Although not stipulated in the EPZ Act, EPZ investors are required to export all or a minimum of 70 percent of their products beyond the borders of the SACU market.¹⁰⁴

Some WTO members such as the US have consistently opposed the export performance requirement, citing that it has trade-distorting effects.¹⁰⁵ However, in 1984 the Panel in the *Canada-Administration of the Foreign Investment Review Act (FIRA) case*,¹⁰⁶ where the US alleged that undertakings to export made by foreign investors to the Canadian government in terms of the FIRA, violate Article XVII of the GATT, found that the GATT does not forbid countries from imposing export performance requirements. Consequently, during the Uruguay Round negotiations, WTO members, especially developing countries, refused to recognise export targets as trade-related investment measures under the TRIMs.¹⁰⁷

However, the most problematic measures under the TRIMs are ‘the local content requirement, trade balancing requirements, and foreign exchange restrictions, which are inconsistent with Articles III and XI on National Treatment and Quantitative Restrictions’, respectively.¹⁰⁸ Since Namibia does not impose the use of local materials, trade balancing

¹⁰⁴ Namibia Investor Guide (n 6 above) 4.

¹⁰⁵ Sornarajah (n 72 above) 112.

¹⁰⁶ *Canada-Administration of the Foreign Investment Review Act (FIRA)* Report of the Panel adopted on 07 February 1984 (L/5504 – 305/140) case para 5.18 https://www.wto.org/english/tratop_e/dispu_e/82fira.pdf (accessed 16 March 2016).

¹⁰⁷ WTO ‘Agreement on trade-related investment measures’ https://www.wto.org/english/tratop_e/invest_e/invest_info_e.htm (accessed 16 March 2016).

¹⁰⁸ Appendix I to the TRIMs.

requirements or foreign exchanges restrictions, the Namibian EPZ regime is consistent with the TRIMs.

4.6 Summary of shortcomings in the Namibian EPZ regime

From the foregoing analysis, it has emerged that the EPZ Act has shortcomings and impediments which hamper the successful implementation of the EPZ programme in Namibia. The following are identified as being vital to the effective implementation of the EPZ programme:

- The EPZ Act has a number of outdated provisions, in particular with reference to repealed statutes.
- The scope of the EPZ Act is narrow as it focuses on manufacturing for export and does not make provision for the development of other types of zones focusing on other sectors such as services.
- There is no clearly defined regulatory framework for the participation of the private sector in the development and operation of EPZs.
- The ODC, which is vested with regulatory authority over the EPZ programme, is also involved in the development and operation of EPZs, leading to a conflict of interests and conflicting roles.
- The lack of integration of the EPZs with the domestic market hinders forward and backward linkages.
- Finally, the EPZ offers overly generous and WTO-inconsistent fiscal incentives.

4.7 Conclusions

The theme of this chapter is the review of the legal framework underpinning the EPZ programme in Namibia. To put the Namibian EPZ into perspective, the experience of Namibia with the EPZs was discussed and revealed that the EPZs has not lived up to its expectations of attracting quality FDI, creating large-scale employment, and aiding transfer of skills and technology. An analysis of the EPZ Act identified a number of impediments to the effective implementation of the EPZ programme in Namibia. These include the limited scope of the EPZ Act, which focuses on the traditional export-oriented model; the absence of regulations; lack of private sector participation

framework; conflicting roles of ODC; and the overly generous and WTO-inconsistent fiscal incentives.

It is indisputable that there is a need to promote the manufacturing sector to compensate for the depleting natural products and promote economic development. However, while policy tools such the EPZ may not necessarily be a panacea or a ‘silver bullet’ to many of the developmental challenges, it may be useful to spur economic development if implemented effectively.

The next chapter will discuss the guidelines for the establishment of economic zones, compiled by the FIAS from best practice of economic zones around the world. The purpose of reviewing these guidelines is to draw lessons for Namibia to transform its EPZ regime in line with international best practice.

CHAPTER 5

TOWARDS TRANSFORMATION OF THE NAMIBIAN EPZ LANDSCAPE: APPLYING FIAS BENCHMARKS AS BEST PRACTICE GUIDELINES FOR THE ESTABLISHMENT OF ECONOMIC ZONES

5.1 Introduction

The previous chapter analysed the EPZ Act as a policy instrument for the implementation of the EPZ programme in Namibia. The analysis has identified a number of shortcomings which impede the achievement of the EPZ objectives. This chapter discusses the best practice guidelines for the establishment of economic zones, pioneered by the FIAS. The purpose is to draw lessons for Namibia to reform its EPZ programme. The discussion navigates around the essential elements of legal and policy frameworks in the planning phase of economic zones. A comparison between the FIAS guidelines and the Namibian EPZ regime is then made to determine the extent to which the Namibian EPZ policy instrument is consistent with the FIAS guidelines and to delineate areas for reform. Finally, this chapter provides guidelines on how to achieve a WTO-compliant EPZ programme.

5.2 Guidelines for the establishment of economic zones: Legal and policy aspects

The starting point is to explain what the FIAS guidelines for the establishment of economic zones are.

5.2.1 What are FIAS guidelines for the establishment of economic zones?

These are guidelines developed by the FIAS in 2008 after an extensive study of zones practice, development patterns, and impacts on their host economies.¹ The FIAS is a World Bank Group's investment climate advisory body responsible for guiding developing countries on how to reform their investment policies and laws in order to attract investors.² The guidelines are intended to guide policymakers in the planning and evaluation phases of their zone programmes, with a view

¹ FIAS 'Special economic zones: Performance, lessons learned and implications for zone development' (2008) 1 http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2008/10/07/000334955_20081007064814/Rendred/PDF/458690WP0Box331s0April200801PUBLIC1.pdf (accessed on 24 February 2016).

² Investment Climate Advisory Services <https://www.wbginvestmentclimate.org/advisory-services/> (accessed 19 April 2016).

to establishing economic zones that are beneficial to both the host states and investors.³ These guidelines were consequently acknowledged by the OECD in 2009 when it recommended them to the OECD-Middle East and North African (MENA) countries as ‘best practice guidelines for the development of economic zones’.⁴ Accordingly, in this study, the phrases ‘FIAS guidelines’, ‘best practice guidelines’, and ‘international best practice’ are used interchangeably. Although these guidelines are not legally binding on states, they are useful tools for countries contemplating to establish new or transform existing zones, considering that they were developed based on the practice of various zones around the world. Thus, these guidelines are embodiments of international best practice in zone development and management. However, it should be noted that the success of the zone programme depends largely on the general trade and investment environment prevailing in the host country and the level of integration of the zones with the domestic industries.⁵

5.2.2 Essential elements of zone planning and evaluation

The FIAS highlighted six elements that have to be considered when planning or evaluating the zone programme.⁶ These elements are essential as they shape the structures of the zones’ policy and legal frameworks. These are: ‘the type of zone to be promoted; core policy framework; incentive framework; regulatory framework; institutional framework; and physical development and management of zones’.⁷ Each of these elements is discussed below.

(i) Type of zone to be promoted

As explained in chapter 2, there are several types of economic zones in existence. Thus, when deciding the type of economic zone to be promoted, the policymakers have to consider two important factors: the scope and the extent of private sector involvement.⁸ The scope of the zone should not be too narrow so as to restrict the zone to a few sectors, as is the case with traditional EPZs in contrast to SEZs.⁹ The guidelines recommend the adoption of a zone model that is

³ FIAS (n 1 above) 1.

⁴ OECD ‘Towards best practice guidelines for the development of economic zones’ (2009) 3. <https://www.oecd.org/mena/competitiveness/44866585.pdf> (accessed on 24 February 2016).

⁵ OECD (n 4 above) 10.

⁶ FIAS (n 1 above) 51-57.

⁷ OECD (n 4 above) 10.

⁸ OECD (n 4 above) 10.

⁹ As above.

flexible enough to accommodate a variety of trade and industrial activities and which allows zone and non-zone businesses to be situated in the same areas.¹⁰

Moreover, the OECD observed that the global trend is shifting towards the consolidation of traditional EPZs into SEZs to cover a broad variety of sectors encompassing services, commercial and manufacturing operations.¹¹ According to Farole and Akinci,¹² the era for traditional EPZs when countries used to rely on cheap labour to attract investments in light manufacturing sectors, has ended. Thus, countries have to strive to remain competitive by adopting programmes that promote investments in high value-added activities. Generally, SEZs cover a much bigger area, a wide range of economic activities, and permit the sale of goods produced in zones into the domestic market without quantitative restrictions but subject to import duties and all applicable charges.¹³ However, the FIAS cautions that the SEZ model is demanding with respect to administration and regulation, and thus requires government commitment and necessary institutional and technical capacity in order to prosper.¹⁴

The second factor to be considered when deciding on the type of zone to be promoted relates to the public-private partnership or private ownership of economic zones.¹⁵ The FIAS estimates that half of the world's economic zones are run by the private sector, a trend sparked mainly by the perception that privately-run zones are more effective than government-run zones.¹⁶ Although there is no conclusive evidence that private sector operated zones are more successful than their counterparts,¹⁷ there is a consensus that private zones offer high standard infrastructure, better facilities, and more efficient services because they are run on a cost-recovery basis.¹⁸ Moreover, private sector involvement decreases the burden on public funds and brings about the effectiveness of zones.¹⁹

¹⁰ FIAS (n 1 above) 51.

¹¹ n 4 above, 10.

¹² T Farole & G Akinci (eds) *Special economic zones: Progress, emerging challenges and future direction* (2011) 6.

¹³ FIAS (n 1 above) 16.

¹⁴ n 1 above, 52.

¹⁵ OECD (n 4 above) 10.

¹⁶ n 1 above, 18.

¹⁷ T Farole *Special economic zones in Africa: Comparing performance and learning from global experiences* (2011) 189.

¹⁸ FIAS (n 1 above) 46.

¹⁹ OECD (n 4 above) 10.

Participation of private entities in the development of zones may be in the form of ‘management contracts, concession agreements, build-own-operate, build-operate-transfer, or build-own-operate-transfer arrangements’.²⁰ However, in order to facilitate the development of private zones, it is imperative that there should be a legal framework clearly outlining the rights and obligations of various parties involved.²¹ Where private and public zones co-exist, the legal framework should ensure fair competition by avoiding discriminatory advantages in favour of public zones.²² Nonetheless, the fact that the private sector owns zones should not be understood to relieve governments of their obligations to develop general off-site infrastructure, provide institutional support, and create a favourable investment climate.²³ Therefore, it is vital to put a legal framework that clearly defines the roles of each stakeholder in place in order to avoid uncertainties.²⁴ To this end, the best practice guidelines support the promotion of private as opposed to public zones as the former increases the chances of success.²⁵

(ii) Streamlining the policy framework

International experience has shown that the best practice is to have the policy and incentive framework streamlined and harmonised so that the zones compete against each other based on the quality of the amenities, infrastructure, services and facilitation they offer to investors, rather than on overly generous tax incentives.²⁶ According to the FIAS, the best practice policy framework has the following key features:²⁷

- a) **Extra-territoriality:** As per the revised Kyoto Convention, the economic zones are treated as outside the customs territories of their host states, but the goods manufactured in the zones should qualify for a certificate of origin from the host state to allow them to take part in trade and to benefit from preferential trade agreements.²⁸
- b) **Development of private zones:** Where private zones development is promoted, the rights, obligations, and benefits for private developers, as well the role of the government

²⁰ FIAS (n 1 above) 19.

²¹ FIAS (n 1 above) 52.

²² FIAS (n 1 above) 53.

²³ Farole (n 17 above) 193.

²⁴ Farole (n 17 above) 194; FIAS (n1 above) 52.

²⁵ FIAS (n 1 above) 51.

²⁶ FIAS (n 1 above) 52; OECD (n 2 above) 12.

²⁷ n 1 above, 52-53.

²⁸ FIAS (n 1 above) 52.

need to be clearly defined.²⁹ Additionally, where private zones and public zones co-exist, public zones should not be unfairly benefited to the detriment of private zones to ensure fair competition between public and private zones in attracting investors.³⁰

- c) **Criteria for designation of zones:** Zone development standards and criteria, such as the zone plan; environmental standards; technical and financial records for the development companies; and equity requirements should be clearly defined to guide the application process for zone development.³¹
- d) **Eligibility criteria:** These are requirements that determine which investments qualify for zone status. International experience has shown that it is best that the zone should be open to a variety of permissible economic activities and should not impose export performance requirements, such as is common with EPZs.³² Additionally, there should be no restriction on ownership of zone enterprises or discrimination between national and foreign investments.³³ It is also recommended that local firms should be given duty-free benefits on inputs supplied to zone firms so as to enhance backward linkage with the local economy to promote economic development.³⁴
- e) **Labour standards:** Labour standards in the zones should be consistent with the ILO standards as it has been shown from international experience that the competitiveness of the zone is not linked to sub-standard employment regulations, but to the quality and productivity of the workers.³⁵ This calls for the harmonisation of the labour standards in the zones with the national labour standards so that they do not violate host states international labour obligations.

²⁹ As above.

³⁰ FIAS (n 1 above) 52.

³¹ FIAS (n 1 above) 52; OECD (n 2 above) 12.

³² FIAS (n 1 above) 53; OECD (n 2 above) 12.

³³ FIAS (n 1 above) 52.

³⁴ OECD (n 4 above) 12.

³⁵ FIAS (n 1 above) 53.

(iii) Planning an effective incentive framework

Different types of incentives offered by states to attract investors into their zones are already discussed in chapter 2. So far, this study has shown that the fiscal (tax) incentives associated with EPZs are contentious, especially within the multilateral trading system. However, literature is not conclusive on whether or not fiscal incentives are indeed effective in attracting FDI in a specific country.³⁶

According to Morisset and Pimia,³⁷ fiscal incentives need to co-exist with other equally important factors such as quality infrastructure, political and macro-economic stability, good governance, and streamlined procedures, in order to attract FDI and bring about expected spillovers. On the other hand, tax incentives are regarded as subordinate in attracting FDI, to more critical aspects such as the extent of the market, and the availability of natural resources and labour skills.³⁸ However, being attracted to incentives also depends on the type of investment an enterprise intends to make, as footloose export-oriented enterprises may consider tax incentives sufficient for them to invest in a certain country.³⁹ Nevertheless, there is significant evidence that suggests that fiscal incentives given by developing countries to zone investors are not effective, as they strain government revenues.⁴⁰

Not only are fiscal incentives ineffective in contributing to the success of the zones, but they are also problematic within the multilateral trading system due to their trade distortive effects. Though the WTO does not have specific rules for economic zones, there is overwhelming convergence that fiscal incentives which are dependent on export performance, foreign exchange earnings, or use of local inputs, are inconsistent with the WTO rules.⁴¹

³⁶ B Pangioti, 'Effects of Tax incentives on Investment decisions of Transnational Enterprises in an integrated world: A literature review' 3 <http://www.eefs.eu/conf/athens/papers/607.pdf> (accessed 21 March 2016).

³⁷ J Morisset & N Pimia 'How tax policy and incentives affect FDI: A review' (2000) 22 <http://213.154.74.164/invenio/record/12651/files/morisset.pdf> (accessed 21 March 2016).

³⁸ UNCTAD 'Tax incentive and foreign direct investment: A global survey' (2000) 11.

³⁹ As above.

⁴⁰ FIAS (n 1 above) 54.

⁴¹ As above.

In light of the above, to be effective, a zone incentive framework should be designed in line with the following guidelines:

- Corporate tax for zone enterprises should be harmonised with the national policies on other promoted industries.⁴² The best practice is the maintenance of performance-based tax exemptions in the national tax law, as opposed to the EPZs legislation.⁴³ Additionally, where tax incentives are offered, there should be a cut-off time as indefinite or long-term tax incentives defeat the intent and purpose of zones.⁴⁴ Countries can take advantage of zone programme reforms to harmonise zone tax regimes with national tax regimes.⁴⁵
- Zones programmes may be used to de-regulate and de-monopolize utilities such as telecommunication and others, as may be necessary.⁴⁶
- The incentive framework should be consistent with the WTO disciplines. This can be achieved by eliminating the export requirement to permit the sale of zone products in the domestic market, subject to import duty.⁴⁷

(iv) Legal and regulatory framework

The zone programmes are founded on the legal framework.⁴⁸ Therefore, it is vital that the legal framework should be solid, and comprehensively outline the rules and procedures for zone development, management, and operation.⁴⁹ Even though the presence of a solid legal framework does not guarantee success, its absence or lack of comprehensiveness has proven to have unsatisfactory outcomes in the past.⁵⁰ Zhen⁵¹ likened the implementation of a zone programme without a thorough legal framework to ‘putting a cart before a horse’ and cautions that it brings uncertainties, unpredictability, and lack of transparency, which deter prospective investors.

⁴² FIAS (n 1 above) 17.

⁴³ FIAS (n 1 above) 54; OECD (n 2 above) 13.

⁴⁴ OECD (n 4 above) 13.

⁴⁵ FIAS (n 1 above) 54.

⁴⁶ As above.

⁴⁷ FIAS (n 1 above) 55.

⁴⁸ Farole (n 17 above) 163.

⁴⁹ As above.

⁵⁰ Farole (n 17 above) 165.

⁵¹ DZ Zeng ‘Global experience with special economic zones – with a focus on China and Africa’ (2015) 9.

In addition, regulatory aspects are crucial to the success of the zone programme, and therefore, administrative procedures such as investment screening and approval, issuing of work permits, and customs procedure should be as simplified and streamlined as possible.⁵² The following guidelines are helpful in developing an effective regulatory framework for the zones:

- The adoption of a simplified business registration process can be achieved by allowing a single government office to deal with application of licences; publishing a negative list of prohibited investment activities and criteria for approval or rejection of the application; and making provision for automatic approval in the event of a decision not being made within the stipulated time.
- Empowering the zone authority, instead of various ministries or agencies, to issue additional permits for land, labour, building, and health and safety, amongst others, would expedite the process.
- Establishment of specific rules for customs and the implementation of computerised customs systems would simplify customs procedures in the zones.⁵³

(v) *Institutional framework*

The autonomy of the institution charged with the supervision of the operation of the zone programme (zone authority), with respect to personnel management, budget control, and policymaking, is of utmost importance to the success of the zone programme.⁵⁴ The zone's authority must have an autonomous board consisting of relevant high-ranking government and private sector representatives with the private sector being represented in the majority representation to ensure result-driven administration.⁵⁵ It is critical that the zone authority is not allowed to own, develop or operate the zones, in order to prevent conflict of interests.⁵⁶ The enabling legislation should establish a one-stop shop system to vest the zone authority with the requisite powers over other government agencies in primary areas, in order to streamline

⁵² FIAS (n 1 above) 55.

⁵³ FIAS (n 1 above) 56.

⁵⁴ OECD (n 4 above) 14.

⁵⁵ FIAS (n 1 above) 56.

⁵⁶ OECD (n 4 above) 14.

administrative procedures while allowing the zone authority to delegate, outsource or privatise the non-core functions to focus on the crucial tasks.⁵⁷

(vi) Physical development and management

According to FIAS, the physical location and the manner in which the zones are established and managed have a role in the success of the zones.⁵⁸ The OECD added that the location of the zone is crucial as it determines the degree to which the government would spend funds on common infrastructure.⁵⁹ It goes without saying that zones which are located near ports, roads, and water and electricity sources would not require excessive public funding.⁶⁰

Therefore, for zones to conform to international best practice for physical development and management, they should be developed and managed along the following guidelines:

- Land use planning and zoning rules should be implemented to guide the development of zones in suitable locations for industrial and commercial activities.⁶¹ This would also prevent mushrooming of zones.⁶²
- Criteria for zone development should be well-defined in the enabling law to ensure that private zones are situated in the designated area to minimise government expenditure on infrastructural development in underdeveloped regions.⁶³
- Zones should be operated on a cost-recovery basis, as opposed to a subsidised basis, in order to enhance efficient management.⁶⁴
- A unit responsible for zoning and development of infrastructure should be established to ensure that there is coordinated planning and infrastructural development.⁶⁵

⁵⁷ FIAS (n 1 above) 57.

⁵⁸ As above.

⁵⁹ n 4 above, 15.

⁶⁰ As above.

⁶¹ FIAS (n 1 above) 57; OECD (n 4 above) 15.

⁶² Zeng (n 51 above) 6.

⁶³ FIAS (n 1 above) 57.

⁶⁴ As above.

⁶⁵ FIAS (n 1 above) 57; OECD (n 4 above) 15.

5.3 Is the Namibian EPZ regime in line with FIAS guidelines?

The Namibian EPZ regime is put on the scale in this section in order to determine the extent to which it is up-to-date with international best practice. The review of the EPZ Act in chapter 3 has identified a number of shortcomings. This section, therefore, highlights those shortcomings through the lens of the FIAS guidelines. To the extent that the FIAS guidelines are based on the lessons learnt from zones around the world, they are useful benchmarks for countries such as Namibia which are operating EPZs for decades, without success.

5.3.1 The scope of the EPZ Act

The analysis of the EPZ Act in chapter 3 revealed that the Act has a narrow scope as it targets traditional export-oriented and labour-intensive industries. This conventional EPZ model has become redundant, especially in light of increasing costs of labour, mounting erosion of trade preferences, and developing multilateral trading rules.⁶⁶ The global trend indicates a shift towards adoption of the SEZ model.⁶⁷ The SEZ model is increasingly preferred because it can accommodate a wide range of sectors and has the potential to spur economic transformation.⁶⁸ As discussed in chapter 2, a number of sub-Saharan countries that initially implemented EPZs, including Kenya, Tanzania, and South Africa have already adopted legal frameworks for SEZs. Since these countries are still in early stages of implementation, it is yet to be seen how African SEZs will fare. Be that as it may, Namibia needs to reflect on the type of zone that should be promoted to keep abreast with international best practice, going forward.

5.3.2 Fiscal incentives

In terms of sections 5 and 7 of the EPZ Act, Namibia exempts EPZ enterprises from liability to pay income tax, sales tax, customs and excise duties, and stamp and transfer duties. Additionally, EPZ enterprises are also exempt from VAT in terms of section 6 of the VAT Act. These tax exemptions are indefinite as they are meant to lure investors to invest in the Namibian EPZs. However, international experience has demonstrated that overly generous tax benefits are not effective as they promote transfer pricing, discourage financing for investment capital, and have

⁶⁶ Farole & Akinci (n 12 above) 6.

⁶⁷ OECD (n 4 above) 10; Farole & Akinci (n 12 above) 6.

⁶⁸ FIAS (n 1 above) 51.

a tendency to attract footloose industries.⁶⁹ Best practice suggests that instead of competing in terms of fiscal incentives, zones should rather compete on the basis of facilities, infrastructure, services, and facilitation.⁷⁰

Another aspect related to fiscal incentives is its inconsistency with the WTO agreements. There is an overwhelming consensus that fiscal incentives that are linked to export performance amount to prohibited export subsidies. The tax exemptions offered by Namibia are linked to export performance. Therefore, these incentives are not consistent with the ASCM and need to be discontinued. As discussed in chapter 2, the transitional period for the elimination of prohibited export subsidies by WTO members not listed in schedule VII to the ASCM expired in 2015.⁷¹ Namibia is not listed in schedule VII to the ASCM. Therefore, Namibia has a legal obligation to eliminate prohibited export subsidies as they are not only inconsistent with the best practice guidelines but most importantly, with WTO rules.

5.3.3 Private sector participation

The EPZ Act under section 10 implicitly allows the appointment of private companies to develop and manage EPZs. This flexibility is in keeping with best practice guidelines which recommend the promotion of private businesses involvement in zone development and management because of the evidence that private zones tend to be more successful than their counterparts.⁷² However, even if the EPZ Act is flexible enough to allow private sector participation, the EPZ Act does not clearly define the eligibility criteria and procedures for application to be appointed as an EPZ management company. The best practice guidelines, on the other hand, requires selection criteria, and benefits of private development and management companies to be clearly outlined in the legal framework.⁷³ Similarly, where a public-private partnership is promoted, a framework that clearly designates the rights and obligations of the public and the private sector parties should be developed to avoid confusions over responsibilities.⁷⁴ These requirements enhance transparency and accountability. In light of the above, the EPZ Act is in line with best practice guidelines insofar as it makes provision for private sector involvement in development and

⁶⁹ FIAS (n 1 above) 50.

⁷⁰ FIAS (n 1 above) 52.

⁷¹ See para 3.1.2 of chapter 2.

⁷² FIAS (n 1 above) 51; OECD (n 4 above) 10.

⁷³ OECD (n 4 above) 11.

⁷⁴ Farole (n 17 above) 194.

operation of zones. However, the EPZ legal framework lags behind in terms of clearly outlining criteria for selection and the tender process.

5.3.4 Institutional framework

The guidelines for zone development recommend that the zone authority should as far as possible be independent in respect of personnel management, budget control and policymaking.⁷⁵ The board of the zone authority must have sufficient powers and an independent board composed of key public and private sector representation, with the private sector represented in the majority to ensure result-oriented and customer-focused administration.⁷⁶ It is also important that the zone authority is not involved in ownership, development and operating of zones to prevent conflict of interest.⁷⁷ In Namibia, the ODC is the EPZ authority appointed in terms of the EPZ Act.⁷⁸ Although in terms of the Act, ODC should be a private company, today the government is the majority shareholder in ODC.⁷⁹ As if that is not enough, ODC is currently awaiting to be merged with another institution into a new statutory body which would place it under full control of the government. In addition, ODC is not only responsible for regulatory and administrative roles, but it is also involved in developing and operating EPZs. This practice offers an uneven playing field for prospective private zone developers, and thus is also not in keeping with best practice with regard to the institutional framework.

5.3.5 Integration of zones into the domestic economy

According to FIAS, the extent to which the zone programme will succeed depends largely on the level of integration with the domestic economy.⁸⁰ The traditional fenced-in zones do not promote the requisite interaction between the zones and the host economy as zones are secluded, and the movement of goods to and from the zones is tightly controlled.⁸¹ However, the traditional concept has undergone a transformation over the past decades, due to the speed of globalisation and evolution of international trading rules which have compelled states to re-assess the zones

⁷⁵ FIAS (n 1 above) 56.

⁷⁶ FIAS (n 1 above) 57.

⁷⁷ FIAS (n 1 above) 56.

⁷⁸ See Chapter 3 para 3.2.7.

⁷⁹ As above.

⁸⁰ n 1 above, 52.

⁸¹ FIAS (n 1 above) 14.

objectives and their impact on the host economies.⁸² This is why there is growing emphasis to integrate the zones into local economies. Integration can be achieved through, amongst others, allowing zone and non-zone enterprises to co-locate in industrial zones⁸³ extending duty-free access to local firms that supply input to zone firms; sub-contracting and joint venturing;⁸⁴ and allowing unrestricted sale of the zone products into the domestic market subject to import duties.⁸⁵ Integration of the zones into the local economy promotes skills and technology transfer which enhance backward and forward linkage between zone firms and local firms.⁸⁶

On the other hand, the EPZ Act promotes secluded zones which may consist of a group of factory units or a single factory unit.⁸⁷ With respect to goods imported from the domestic market to the zone, the EPZ Act stipulates that duty or tax paid on any such goods is non-refundable.⁸⁸ This means that domestic enterprises do not have duty-free access to inputs supplied to the EPZ enterprises. Furthermore, the EPZ Act proscribes the sale and consumption of EPZs products in the domestic market or within the EPZs, except with the written authorization of the Minister in consultation with the Minister of Finance.⁸⁹ However, only 30 percent of the goods produced in the EPZs may be sold in the domestic market (SACU market).⁹⁰ These sections of the EPZ Act are, amongst others, indications that the EPZ Act is not up to date with international best practice on the integration of zones with the host economy.

5.4 Achieving WTO compliant economic zones

According to Creskoff and P Walkenhorst,⁹¹ in order to achieve a WTO-compliant economic zone programme, members should review their programmes to identify all measures that are likely to contravene WTO rules, notify such measures to WTO accordingly, and develop and implement an elimination schedule for such inconsistent measures.

⁸² As above.

⁸³ FIAS (1 above) 5

⁸⁴ FIAS(n 1 above) 42.

⁸⁵ FIAS (n 1 above)16.

⁸⁶ FIAs (n 1 above) 42.

⁸⁷ Sec 2 of the EPZ Act.

⁸⁸ Sec 5(2) of the EPZ Act.

⁸⁹ Sec 4(1)(a) of the EPZ Act.

⁹⁰ See ch 3 above, para 3.3.4.

⁹¹ S Creskoff & P Walkenhorst 'Implications of WTO disciplines for special economic zones in developing countries' (2009) 36.

The general consensus is that the economic zones regime without export performance and local content requirements, or maintenance of foreign exchange balance, is consistent with the WTO rules.⁹² The most problematic aspects of the EPZs programme are the fiscal or financial incentives which are contingent on the export performance and sometimes on the use of domestic content requirements or maintenance of foreign exchange balance. Such measures are not consistent with the WTO rules.

Waters⁹³ is of the view that the elimination of fiscal incentives and export performance requirements would make EPZ legislation consistent with WTO rules in that the removal of fiscal or financial incentives eliminates the ‘subsidy’, while the removal of the export performance requirement will place the measure outside the purview of Article 3(1)(a) of the ASCM.⁹⁴ The emphasis is that both elements should be eliminated because the elimination of export performance requirement while maintaining fiscal or financial incentives will only shift the measure from being a prohibited export subsidy to an actionable subsidy, which is still inconsistent with the ASCM.⁹⁵

Similarly, the maintenance of local content requirements while removing fiscal or financial incentives would shift the measure from the purview of the ASCM to that of the TRIMs. However, even if a country eliminates export performance and local content requirements in the EPZs but still maintains the fiscal incentives, such incentives may still be considered to be export subsidies due to the export-orientated nature of the EPZs. Thus, reform to bring the EPZs into conformity with the WTO rules should target fiscal incentives, financial assistance, export performance, and the local content requirement.

Nevertheless, fiscal incentives cannot just be removed without considering the investors who already committed their investments based on the existing incentives regime as that would lead to legal disputes between investors and host countries.⁹⁶ In this regard, Creskoff and Walkenhorst⁹⁷ are of the view that countries may eliminate prohibited export subsidies by doing

⁹² FIAS (n 1 above) 54.

⁹³ JJ Waters ‘Achieving world trade organization compliance for export processing zone while maintaining economic competitiveness for developing countries’ (2013) 63.481 *Duke Law Journal* 502.

⁹⁴ Waters (n 93 above) 502.

⁹⁵ As above.

⁹⁶ Creskoff & Walkenhorst (n 91 above) 37.

⁹⁷ n 91 above, 37.

away with the minimum export requirement to allow the domestic sale of EPZs products subject to duty and by extending similar fiscal incentives to non-zone enterprises so as to make such subsidies not specific to export-oriented enterprises.

Waters⁹⁸ encourages countries to limit actions based on *de facto* export subsidies by taking initiatives which allow EPZs companies to sell their products in the domestic market, and to target workers' advancement and employment creation as the main goals as opposed to generating exports or foreign exchange earnings. He also proposes the replacement of the term 'export' in the phrase 'export processing zones' with a more neutral term.⁹⁹ Without a doubt, if countries remove minimum export requirements and harmonise the tax regime with other promoted industries, a WTO-compliant economic zone would be achieved.

5.6 Conclusions

The FIAS has devised guidelines for the development of zones based on lessons learnt from the review of zones around the world. These guidelines are equally useful to countries establishing new or reforming existing zone programmes. When planning or reviewing a zone programme, six key elements as discussed above, have to be considered in order to give the policy and legal frameworks appropriate structures.

The comparison between the Namibian EPZ regime and the FIAS guidelines in this chapter indicates that the Namibian EPZ regime falls short of the international best practice with respect to the scope of the EPZ programme, fiscal incentives, rule and procedure for private sector involvement, integration with the host economy and institutional framework. These are the areas that need to be reformed.

This chapter has also shown that the traditional EPZ model has become redundant and that the world is shifting to the SEZ model, which is considered to be flexible as it accommodates a wide range of sectors and has the potential to spur economic transformation through greater integration with the host economy.

⁹⁸ n 93 above, 504.

⁹⁹ Waters (n 93 above) 504.

However, the success of the zone programmes depends largely on the general trade and investment environment prevailing in the host country, as well as the degree to which there is an integration of the zones with the local economy.¹⁰⁰ Therefore, it should be noted that the zone programme is not an end in itself but a component of the national socio-economic development strategy.

The following chapter, which is the final chapter for this study, will provide an overall conclusion of the discussions in the preceding chapters and make recommendations on how Namibia can transform its EPZ programme into an effective policy instrument.

¹⁰⁰ OECD (n 4 above) 10.

CHAPTER 6

CONCLUSIONS AND RECOMMENDATIONS

6.1 A recap of the research agenda

This mini-dissertation reviewed the Namibian EPZ Act as the policy instrument for the implementation of the EPZ programme in Namibia. The review was necessitated by the fact that the EPZ programme has not achieved its set objectives in its two decades of implementation. The issue is that the Namibian EPZ continues to target labour-intensive and light manufacturing investments despite the fact that cheap labour and special preferential trade arrangements, which drove the EPZs in the 1970s and 1980s have dwindled. It is on this basis that this study has analysed the EPZ Act in order to identify impediments to the achievement of the EPZ objectives and make a case for the transformation of the EPZ programme into an effective policy instrument for socio-economic development in Namibia.

6.2 Summary of the findings

Chapter 1 set the pace by introducing the study and highlighting the research problem, which is the unsuccessful implementation of the EPZ programme in Namibia. Chapter 2 placed the EPZs into context by analysing various definitions of EPZs by international organisations and providing a historical background of EPZs. It also highlighted the fact that EPZs are trade and investment policy instruments adopted mainly by developing countries to shift from import-substitution industrialisation strategies to export-led industrialisation. The common EPZs' objectives include attracting FDI, creating employment, expanding exports and foreign exchanges earnings, and creating linkages with the domestic economy through skills and technology transfers. This chapter also examined the common incentives that are offered by developing countries to attract FDI. These are classified into fiscal, financial and regulatory incentives. Additionally, Chapter 2 has shown that there is a trend to shift from EPZs to SEZs, with some sub-Saharan countries including Kenya, Tanzania and South Africa, that initially established EPZs having already adopted the SEZs policy and legal frameworks.

Chapter 3 discussed the implications of the WTO, RTAs and ILO standards on the EPZs. It has shown that even though the WTO does not have specific rules on economic zones, there are

certain WTO disciplines which have an impact on the EPZs measures. At the forefront are fiscal incentives given in the form of tax exemptions to the EPZs firms. Because the EPZs firms are given these exemptions on condition that they export their entire or a substantial part of their production, or that they would use local materials in their production, these incentives qualify as prohibited subsidies under the ASCM. A number of WTO members were given an extended period to phase out their prohibited subsidies. That period expired in December 2015, and the implication is that all WTO members that are not listed in schedule VII to the ASCM were expected to be in compliance with the ASCM by 01 January 2016. Another aspect concerning the EPZs is the performance requirements, especially the use of local contents or maintaining trade balancing or foreign exchange restrictions. These requirements are inconsistent with the TRIMs.

In addition, a discussion on international labour standards has shown that the ILO made several recommendations to its member states that limited the EPZs workers' the right to organise and join associations of choice, collective bargaining rights, and the right to strike in their EPZs as a way of attracting investors.

Chapter 4 undertook a review of the law underpinning the EPZ programme in Namibia. In the preliminary, this chapter provides a brief overview of the Namibian economic structure to appreciate and put the EPZ into the Namibian perspective. It also examined the Namibian experience with the EPZs, where it has shown that the EPZ programme has failed to achieve its objectives set out in section 3 of the EPZ Act. In this regard, the number and quality of foreign investments in the EPZs and employment created thus far are clear testimonies that the EPZ programme is not a success story in Namibia. The analysis of the EPZ Act identified various shortcomings in the Act which the author is convinced, are barriers to the achievement of the set objectives. These includes the limited scope of the EPZ Act which is based on the traditional export-oriented model, absence of regulations, lack of private sector participation framework, conflicting roles of ODC, and the overly generous and WTO-inconsistent fiscal incentives. Without a doubt, there is a case for the transformation of the EPZ regime in Namibia.

Chapter 5 discussed the FIAS guidelines for the establishment of economic zones. These guidelines are an outcome of the extensive study of economic zones' experience, development patterns and impacts on their host economies, conducted by the FIAS with the aim of compiling

best practice with regard to zone development and management. Thus, these guidelines are an embodiment of international best practice in the zone development and management. They provide guidance to policymakers when establishing new or reforming existing zone programmes. These guidelines are used in this study as benchmarks to compare to the Namibian EPZ regime in order to identify areas of the Namibian EPZ programme needing reform. The guidelines identified six core elements which form the basis for policy and legal frameworks for the zone programme and have to be considered by policy-makers during planning or evaluation of a zone programme. A comparison of the Namibian EPZ regime with the FIAS guidelines has shown that the Namibian EPZ programme falls short of the international best practice with respect to the scope of the EPZ programme, fiscal incentives, rule and procedure for private sector involvement, integration with the host economy, and institutional framework. Therefore, there is a case for the transformation of the EPZ programme in Namibia.

6.3 Conclusions

This study identified shortcomings in the EPZ Act, which is the legal and policy framework underpinning the EPZ programme in Namibia. The author has argued how each of the identified shortcomings hinders the achievement of the EPZ objectives rendering the EPZ programme ineffective in the process. Without a doubt, a case is made for the transformation of the Namibian EPZ. Therefore, at this stage, the question that has to be posed is ‘how can Namibia transform its EPZs regime into an effective policy instrument? As this study has shown, there is no single answer to this question. A number of factors have to be considered and investigated in order to turn around the failing EPZ programme. However, what is certain is the fact that the EPZ programme in its current form and approach will continue to disappoint. This is because the EPZ model is outdated and is no longer relevant in the wake of increasing costs of labour and contracting trade preferences, which were factors responsible for EPZs’ boom in the 1980s and early 1990s.

In contrast, this study has shown that the world is shifting from an EPZ model to the SEZ model because it covers a wide variety of sectors and promotes better linkage with the domestic economy. Thus, the SEZ is a better facilitator for economic reform.

6.4 Recommendations

It is imperative that Namibia considers adopting an SEZ model which should progressively absorb the current EPZ regime.

Namibia should, as far as possible, streamline and harmonise regulatory procedures in order to facilitate the process of business registration and application for zone status. It is also recommended that the power to issue all the necessary permits be vested in a single authority in order to cut the bureaucratic red tape.

In order to promote private sector participation in the zone development and operations, the government should ensure that the procedures and selection criteria for the application to be appointed as a management company are clearly outlined in the enabling law and that all the rights, obligations and privileges are defined.

There is also need to review the fiscal incentives offered under the existing EPZ programme to ensure that the incentive framework does not violate the WTO rules on subsidies. This can be achieved by harmonising the tax exemptions offered in the EPZs and in the domestic market under the national tax law to apply equivocally to all promoted industries. In this way, the tax incentives will not be specific to certain sectors or industries. This has to be done with caution in order to avoid host state-investor disputes, considering the fact that existing investors have already committed their investments based on the incentives currently in operation. Similarly, the minimum export requirements must be eliminated by allowing the sale of zone products in the domestic market subject to payment of import duties.

The zone regulatory authority should be given requisite powers to regulate the operation of the zone programme. In particular, the authority that would be vested with an oversight responsibility for the reformed zone programme should have an independent board made up of high-ranking government and private sector representatives. It is advisable that the private sector should have a majority representation to ensure result-driven administration. The zone regulatory authority should not be allowed to take part in the development and management of zones to prevent conflict of interests, and more so to ensure an even playing field for the private management companies.

There should be a clearly defined zone designation and development criteria in order to prevent mushrooming of zones and to also preserve government funds on general infrastructure.

To this end, it is important that the EPZ Act be reformed by adopting a comprehensive legal framework for the reformed zone programme which should embody the following aspects:

- The zone legislation should clearly define the rules and procedures related to, among others, selection of suitable locations; criteria for investments screening and approval; licensing requirements; and physical development and environmental standards.
- The legislation should be flexible to adapt to changing economic conditions. The institutional framework should be consolidated and harmonised by the new legislation to avoid overlapping responsibilities and institutional conflicts.
- A one-stop shop system should be established in the new law to vest authority in one institution to carry out core administrative and regulatory activities related to the operation of the zone enterprises.
- The legal framework should design special rules and regulations for customs informed by the WTO and WCO rules to simplify customs procedures in the zones.
- The roles and obligations of all relevant participants (government, zone owners, developers, managers or operators) in the development, management and operation of the zone should be clearly defined in the legal framework. This brings about the certainty of responsibilities and enhances accountability.

It should, however, be noted that for a zone programme to succeed, the legal framework needs to be complemented by other factors, including effective implementation of the programme and improvement of the general business climate in the country.

Namibia should capitalise on the reform of the EPZ programme to get all aspects in order, right at the strategic planning stage to ensure smooth implementation of the reformed zone programme.

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