



Free Trade Zones and trade in ODS



WHAT IS A FREE TRADE ZONE?

“Free Trade Zones” (FTZ), are specifically defined areas within a country where goods may be imported/landed, handled, processed, assembled, manufactured or reconfigured, and re-exported with the companies deriving a wide range of benefits, for example, exemptions from duty and taxes, simplified administrative procedures and duty free imports of raw materials, machinery, parts and equipment. They are generally located around major ports, international airports, and national borders and locations with geographic advantages for trade.

The relaxed regulations, limited taxes and reduced oversight in FTZs provide considerable opportunities for businesses and they now play a critical role in global trade, driving economic growth and facilitating increased international trade and investment. FTZs are intended to “stimulate export ... to motivate production and competition, to attract foreign direct investments, to reduce regional inequalities, to encourage technology diffusion and economic development”¹. FTZs are also known by a number of different names (see box).

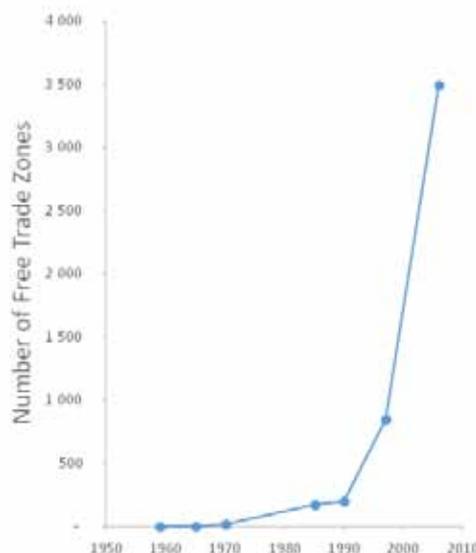
Also known as...

Free Trade Zones are called different names around the world, including:

- Free Zones
- Duty Free Zones
- Free Ports
- Foreign-Trade Zones
- Export Processing Zones
- Special Economic Zones
- Industrial Free Zones
- Export Free Zones
- Qualifying Industrial Zones
- Duty Free Export Processing Zones

THE GROWTH OF FREE TRADE ZONES

Currently there are about 3,500 FTZs located in 135 countries around the world, employing more than 66 million workers worldwide (mostly in manufacturing). Most FTZs are located in developing countries. The largest FTZs are situated in China, Singapore and the United Arab Emirates. For example, the largest FTZs in China, the Shanghai Free Trade Zone established in 2013 - has the area of 11 km² and contains 4,600 companies (including 280 foreign enterprises).²



Source: United Nations and ILO data, reported in Bolle and Williams, 2013²

CONTROL OVER MOVEMENT OF GOODS TO AND FROM FREE TRADE ZONES

The Kyoto Convention (The International Convention on the Simplification and Harmonization of Customs Procedures)³ defines FTZs as a particular class of “Special Economic Zones” and “a part of the territory of a World Customs Organization (WCO) Contracting Party where any goods introduced are generally regarded, insofar as import duties and taxes are concerned, as being outside the Customs territory”. The Convention further states that:

- *“National legislation shall specify the requirements relating to the establishment of free zones, the kinds of goods admissible to such zones and the nature of the operations to which goods may be subjected in them” and that*
- *“Customs authorities shall have the right to carry out checks at any time of the goods stored on the premises of any person introducing goods into a free zone”*

Around the world there is little consistency in the approach to monitoring and control of trade in

FTZs and a common misconception often exists that FTZs are ‘extraterritorial’ and not subject to national customs or customs laws. This inconsistency and confusion can lead to a situation that enables unlawful activities to flourish in some of these zones. The WCO has tried to address this issue by providing guidelines in the Revised Kyoto Convention. These include: explicit customs jurisdiction over FTZs, rules on origin of goods, and customs transit and transshipment procedures. However few countries have implemented the provisions of the Revised Kyoto Convention.

“Along with the recent global proliferation of FTZs has come increasing vulnerability to a wide range of abuses by criminal actors who have taken advantage of relaxed oversight, softened Customs controls and the lack of transparency in these zones”

- International Chamber of Commerce⁴

FREE TRADE ZONES AND THE MONTREAL PROTOCOL

Ozone depleting substances (ODS) controlled by the Montreal Protocol, specifically hydrochlorofluorocarbons (HCFCs) as well as equipment containing or relying on HCFCs, are susceptible to illegal trade due to the restrictions on their import and export in many countries and the continued high demand for many of these substances. Many shipments of ODS pass through FTZs as part of international trade.

Lack of proper oversight and controls in some FTZs can create an environment where illegal trade in ODS can proliferate. This can allow the import and export of ODS without proper licenses and not adhering to quotas set by countries as required under the Montreal Protocol. Transshipment fraud through FTZs is one of the most common methods of ODS smuggling; the ODS consignments are officially destined to legitimate markets, but go through FTZs and are then diverted to the black market. There is also evidence of counterfeiting of ODS packaging and containers while shipments transit through FTZs.

Although consideration of the issue of problems arising from trade provisions of the Montreal Protocol related to FTZs is under the mandate of the Protocol (the mandate of the OEWG was extended by decision III/15 to include this), the issue has not been considered to any great extent by the Parties.

Occasionally the issue of trade through FTZs is raised in the Meeting of the Parties and the Implementation Committee as a potential reason for the difference between reported export and import of ODS and lack of clarity identifying the countries of origin of imports. FTZs are occasionally referred to in the information reported to the Ozone Secretariat on illegal trade in ODS. The Article 7 data reporting guidelines state that countries having FTZs inside their territories should make a special effort to include in their data reporting production, import and export figures for such zones.⁵

Over the years the issue of the role of FTZs in the illegal trade in ODS has been discussed many times by concerned countries in meetings of UNEP’s Regional Networks of Ozone Officers, flagging this as a potential problem in monitoring and controlling illegal trade and ensuring accurate data reporting. The UNEP OzonAction Customs training manual highlights FTZs as being “often sources of illegal trade in ODS”.

“Very often, non-producer countries and free-trade zones are abused as transit points for further distribution of ODS thereby by-passing the Montreal Protocol licensing system.”

- WCO Secretary General Kunio Mikuriya⁶



Examples of customs regulations in Free Trade Zones

In most countries general legal provisions related to trade through FTZs are included in national customs regulations. However, in some countries specific laws on FTZs have been developed to enhance oversight and strengthen monitoring and control of trade through FTZs.

European Union (EU)

In the EU there are currently 93 FTZs located in 23 Member States. In the EU, legal provisions which regulate trade in FTZs are part of the Community Customs Code established in 2008, which state, inter alia, that:

- The perimeter and entry and exit points of the area of free zones shall be subject to customs supervision
- Persons, goods and means of transport entering or leaving a free zone shall be subject to customs controls
- Any activity in a free zone shall be subject to notification, in advance, to the customs authorities
- Licencing of the import and re-export of ODS and products and equipment containing or relying on ODS through a FTZ located in the EU territory is not required if the goods stay in the FTZ for less than 45 days. If imported goods are later released for free circulation in the EU, an import license is needed. (EC Regulation No 1005/2009)⁷
- ODS (or products and equipment containing or relying on ODS), which are banned in the EU, are not permitted to enter a FTZ located in the EU territory.

Singapore

In Singapore there are currently five FTZs, all are located at the Singapore seaport. Singapore is one of the few countries where a specific Free Zones Act has been established⁸. According to the Act:

- Goods of any description, except those specifically prohibited by law, may be brought into a free trade zone, be removed from the free trade zone, destroyed, or sent into customs territory or into another free trade zone in the original package or otherwise and, unless otherwise directed by the authority, be stored, sold, exhibited, broken up, repacked, assembled, distributed, sorted, graded, cleaned, mixed, or otherwise manipulated, or be manufactured. However, when the goods are exported from a free zone, standard customs procedures apply.
- Any activity carried out in a free zone must be notified to its authority in order to obtain permission
- The authority shall permit customs offices to be established in a free trade zone and shall provide adequate facilities for officers of customs whose duties require their presence within or at the perimeter of the zone

United Arab Emirates (UAE)

In the UAE there are currently more than 38 FTZs. 20 FTZs are located in Dubai. The UAE Provisions related to FTZs are contained in the Gulf Cooperation Council Customs Law. This includes the following provisions:

- FTZ management shall present to the State Authorities, upon their request, a list of goods which were brought into or taken out of the FTZ
- Gulf Cooperation Council Member States may make a list of goods that are not allowed to enter the FTZ
- The customs office may carry out inspections in the FTZ for prohibited goods and may review documents and examine goods when there is suspicion of smuggling.

IMPORTANT POINTS FOR OZONE OFFICERS

- The Montreal Protocol provides no leeway for exempting parts of a Party's territory, such as a FTZ, from any of its requirements.
- Since all countries are now Party to the Montreal Amendment, those which do not regulate the import and export of ODS into and out of FTZs are by definition not in compliance with their obligations under the Protocol.
- Countries may need to enhance their control measures to ensure that import and export of ODSs through FTZs does not lead to discrepancies in Article 7 data reporting, including uncertainty in the origins of the material.
- Lack of proper oversight of FTZs may provide a route for ODSs to be traded outside any form of monitoring or regulation.
- Countries may wish to take extra monitoring and control measures to prevent the import and export of counterfeit and mislabelled ODSs through FTZs.
- National customs administrations may consider adding export of ODSs from FTZs as a specific risk factor in their risk profiling systems.



Additional information

- 1 Export Processing Zones and the Law of the World Trade Organization, M.C. Almeida, <http://www.sielnet.org>
- 2 M. J. Bolle, B. R. Williams, US Foreign-Trade Zones – Background and issues for Congress, November 12, 2007, Congressional Research Service, 7-5700, www.crs.gov, R42686
- 3 Text of special Annex D of “International Convention on the simplification and harmonization of customs procedures (as amended)” called also “revised Kyoto Convention” http://www.wcoomd.org/en/topics/facilitation/instrument-and-tools/conventions/pf_revised_kyoto_conv/kyoto_new/spand.aspx
- 4 Controlling the zone: Balancing facilitation and control to combat illicit trade in the world's free trade zones, International Chamber of Commerce Publication, May 2013, <http://www.ip-watch.org/weblog/wp-content/uploads/2013/05/FTZ-report.pdf>
- 5 Report of the 3rd Meeting of the Parties, UNEP/OzL.Pro.3/11, pg 74. http://ozone.unep.org/Meeting_Documents/mop/03mop/3mop-11.e.doc
- 6 OzonAction Special Issue 2009. http://www.unep.fr/ozonaction/information/mmcfiles/3139-e-OASI09_2010andThen.pdf
- 7 Regulation (EC) No 1005/2009 of the European Parliament and of the Council of 16 September 2009 on substances that deplete the ozone layer (recast), <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:286:0001:0030:EN:PDF>
- 8 Singapore Free Trade Zones Act (2014), <http://www.customs.gov.sg/topNav/leg/act/Free+Trade+Zones+Act.html>

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