

Danube Free Zones – between Desiderata and Achievements

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Abstract: The notion of free zone, appears frequently in commercial discussions, as being the place where you can develop a business, due to several facilities offered to both importers and exporters - facilities of a customs, fiscal and commercial nature. Many companies use the advantages of the free zone regime, as a good tool for fiscal optimization of costs. Under the conditions of globalization, it is becoming increasingly important to use tools that optimize the flow of goods. In this sense, free zones are the most suitable tools for optimizing both the flows of goods and the financial ones of companies. With so many advantages it presents a free area related to a waterway, such as the Danube River. Our study aims to analyze the opportunities and achievements of the free zones related to the Danube, in Romania; the addressability of this analysis is both to the business environment and to the academic one. The analysis methods are by excellence qualitative, thematic, comparative, applying the study, the expertise. Our study can be useful both to business people, as well as to researchers, students in the economic field; therefore, any suggestions for improvement will be welcome.

Keywords: international trade; transit zones; free ports; foreign trade; economic impact

JEL Classification: F6; K19; K20; K33

Motto:

“The distance between Regensburg and Vienna seems long, when you follow the meanders of the Danube. However, on the nearly four hundred and seventy-five kilometers waterway, cities of some importance are rare”.

(Jules Verne - The Pilot on the Danube)

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1. Introduction

Since antiquity, governments, emperors, kings and queens have been providing traders and investors with special sites offering respite from normal import-export tax regimes and regulations in return for a steady stream of much needed revenue for the public purse. Before modernity, such places were concentrated in the Mediterranean basin, at Delos in Greco- Roman times and in Venice, Genoa and Marseilles during the Middle Ages. By the 19th century, they had spread to Southeast Asia. But it was not until the latter half of the 20th century that so-called free zones made their mark as deliberate tools of economic development, most notably in China in 1979 when one of the most famous free zones of all was set up at Shenzhen.

"Free zones are like a heart that helps many countries learn how to operate economically, technically and politically in the world"¹. They appeared in antiquity, no doubt in close connection with water transport, in the form of open ports, located on the most important commercial routes. The first such port was Carthagina, mentioned in 1814 BC and it was followed by many others positioned from the Mediterranean Sea, the Baltic Sea (where the role of the Hanseatic League is mentioned) to ancient China. In 1860 the notion of free zones was used for the first time. It was happening in Italy, for Haute - Savoie. At the end of the 19th century, the city of Genoa, the Italian port with an unmistakable international resonance, became the free zone, followed by Copenhagen in Denmark and Thessaloniki in Greece, just as important. The concept of a free zone is a generic one. Currently, in the specialized literature and international documents, more than 20 different terms are used, which are also recognized in association with the idea of processing or handling some products intended for export (Enache, 1998). The Danube river did not remain outside the area of interest so, in turn, free zones were established in Belgrade, Pancevo, Budapest, Vidin, Ruse. In Romania, in 1870, Sulina was declared a free port by the Ottoman Empire within the European Commission of the Danube, due to its favorable geographical position, on the Danube's discharge into the Black Sea.

Nowadays there are several hundred free zones around the world and the MENA region has a fair share of successes, from Dubai's media and Internet cities that caught the early wave of the e-economy, through Egypt's Gulf of Suez all the way to the Tangier Free Zone.

¹ www.tehnopress.ro.

Operators in every free zone in the world aim to energize international trade, as international trade is recognized as the engine of global economic growth. In the last 50 years, trade worldwide has increased 17 times, while global production has increased 4 times, and the income / inhabitant doubled.

The liberalization of international trade has taken a big step forward, by the conclusion of the Uruguay Round and the signing of the Final Act in Marrakech in April 1994. Through this document, the customs duties were significantly reduced and were abolished the quantitative obstacles at the borders of the 140 signatory countries, including Romania. However, the trend of continuous development of international trade it has been and is still curbed by the restrictive customs regimes of the states. On this fund, the suspensive (favorable) import regimes were developed under the following forms: customs warehouses; temporary imports; transit operations; re-exports; free economic zones.

Many companies use the advantages of the free zone regime, but in the following article you will see what these are and how your company can run profitable businesses through a free zone. Businesses whose main component is import-export operations and, in particular, trade relations with countries outside the European Union can be used as a good tool for tax optimization of costs. From this point of view, the Galati Free Zone is one of the points of local, but also national economic interest on the eastern border of the European Union. We all know that in the European Union there are free zones in Europe. What are these? The free zones are parts of the customs territory of the Community or premises located in this territory, separated from the rest of it, in which:

- a) the non-Community goods are considered, as regards the application of import rights and the measures of commercial policy on import, as not being located in the customs territory of the Community, as long as they are not released for free circulation or placed under another customs regime, neither used or consumed in conditions other than those provided for in the customs regulations
- b) Community goods, for which there is such a provision in accordance with the Community legislation regulating specific fields, benefit from the measures usually related to the export of the goods, based on their placement in a free zone or a free warehouse. Free zone - the place where you can develop a business. What kind of business? Well, pretty much any kind of business from production to trade or just transit of goods. Of course, the free zone regime can benefit more those companies / businesses that are related to international trade. Even global, we could say. Why?

The current global economy has already changed the way goods are produced. Currently, components manufactured in one country are increasingly being assembled in another and then sold in a third country. In these new conditions of globalization, the use of tools to optimize these commodity flows is becoming more and more important. In this sense, free zones are the most suitable optimization tools for both commodity and financial flows of companies.

2. Related Work

Kumar, (2008) examines 30 years of experience in zones, reviewing development patterns and economic impacts of zones worldwide. The experience shows that while zones have been effective in addressing economic growth and development objectives, they have not been uniformly successful; successes in East Asia and Latin America have been difficult to replicate, particularly in Africa and many zones have failed. Moreover, since the onset of zone development in developing countries, concerns have been raised about the impact of zones on employment (in terms of gender, wage levels and benefits, worker rights and work conditions), the environment and related social factors.

Tiefenbrun, (2013) precised that in the free zones, domestic or foreign enterprises buying products from abroad can store goods in a customs-free facility prior to shipment into the country where the zone is located. Storage can result in substantial savings in financing charges and increased cash flows. Some importers depend upon free trade zones to package, label, sort, assemble, process or manufacture finished goods prior to re-exporting their duty-exempt finished products.

De Jong, (2013) appreciates that: “As Free Zones mostly operate as specific entities within a larger administration, it is important that roles are clearly distributed. In the case of State aid for example, the host MS needs to report to the EC on activity within the region, but is often dependent on auditing and reporting done by the region itself. This is a sensitive issue as some might perceive Free Zones as reducing trade in competing "normal" jurisdictions, whereas, on the other hand, local constituencies could perceive enquires to be intrusive”.

Zeng, (2015) provides a brief overview of the different SEZ experiences in China and Africa, the key lessons that Africa can learn from China, as well as the recent Chinese zones in Africa. For this purpose, the paper is structured in the following way: section 1 starts with definition of SEZs, then followed with the Chinese

experiences, African experiences the lessons that Africa can learn from China, Chinese zones in Africa and then concludes.

Lavissière and Rodrigue, (2017) analyzed a collected free ports data that enabled the identification of three constitutive factors of evolution: an external factor (the jurisdiction), an internal factor (the services provided) and a linking factor (the orientation of flows). Based on these three factors a model of free ports was designed with a typology of thirteen types of free ports, an explanation of their evolution and their future prospects.

Cirera and Lakshman, (2017) precise that different zones provide different types of incentives, depending on the existing domestic market conditions, ability to attract Foreign Direct Investment (FDI) and the type of sectors targeted to be attracted to the zone. This makes the comparison across Export Processing Zones difficult. In general, they can separate the main set of incentives in three categories: tax, infrastructure and regulation.

Moberg, (2017) examines in this book SEZs from a political economy perspective, both to dissect the incentives of governments, zone developers, and exporters, and to uncover both the hidden costs and untapped potential of zone policies. Costs include misallocated resources, the encouragement of rent-seeking and distraction of policy-makers from more effective reforms. However, the zones also have several unappreciated benefits. They can change the politics of a country, by generating a transition from a system of rent-seeking to one of liberalized open markets. In revealing the hidden promise of SEZs, this book shows how the SEZ model of development can succeed in the future.

Çal, Kandemir, Saygılı, Bayraktar, (2018) made an interesting and comprehensive analysis of the 18 free zones of Turkey, with their minus and plus.

Chaisse and Hu, (2019) offered in their volume a sort of assistance to the future development of Economic Zones around the world, offering analysis of this dynamic phenomenon across legal, economic, investment, regulatory and policy matrices. The book offers a careful examination of theory and practice and its comprehensive approach to developing best practices and the lessons from case-studies which will reward all interested and ever-more important area of law and economics.

3 Problem Statement

a) The fierce competition for finding new product markets, as well as the need to harness the economic potential of a region by attracting it of foreign capital, led to the emergence of an element of interest in the structure economy of a country: Free Zone. Defined as a complex form of suspensive customs regime, the free zone constitutes within a well-defined perimeter of the territory of a country, in which goods may be introduced for processing and marketing to third parties markets, without the application of tariff and non-tariff restrictions of the customs regime in comparison with the national territory. The purpose of setting up a free zone is to promote development economic by attracting foreign capital investments. At the same time, the free zones serve to encourage international trade, stimulating the industrial bases of local communities.

b) The experience of the free zones worldwide has shown that an element that hinders the launch and later their development is the exaggerated shift of their profit towards the storage activity, to the detriment of the industrial processing activities oriented towards export. The presentation of free zone as "glorified deposits" proves a service together with the striking similarity of the commercial and financial advantages offered:

- exemptions from customs duties on the access of the imported products in the area, provided they are re-exported or of the products resulting from the processing outside the national customs territory, of the reduction or exemption of taxes during the period of determination
- tariff concessions for the provision of services and the provision of financial assistance. It is considered that only those areas have survived, which, based on the initial advantages offered, have been oriented consistently to the development of processing activities for export. On the other hand, the industrial free zones have proved viable only insofar as the services offered by the existing organizational structure have been maintained through quality, operability and selectivity at the level of the increase of the users' requirements in these areas. The concept of the free zone has been modified and adjusted in many ways. Trade promotion has always led to the creation of a secure physical environment and a set of laws and rules for trading business. Without them, the cost and the risks would make the trade unfavorable. From a commercial point of view, the increase of the regulations presents both advantages and disadvantages
- improving communications

➤ new forms of business organizations facilitate the growth of trade by reducing uncertainty in transactions. Trade regulations and import taxes, on the other hand, have a negative impact on trade.

c) What is the situation about the proposals and the results of these, in our days – this is what our study intend to present.

4. Concept and Terms

What is Porto Franco? Porto franco (free port) is a port located in a "free economic zone with a more relaxed jurisdiction, compared to the country where it is located. This usually means being exempt from customs duties or having a customs regime, especially with favorable customs regulations.

The Concept of Free Zones

The free zone is the most complex form of the suspensive customs regimes. By law, it is provided that in a free area well defined of the national territory goods may be introduced for processing and marketing, on third markets, without the application of tariff and non-tariff restrictions of the customs regime in comparison with the national territory, corresponding to the area reserved for the free customs area.

The concept of Free Zone is a useful political tool for countries that intend to develop an export-oriented production sector, but which do not have the administrative and technical capacity necessary to develop a national system that allows exporters to import duty-free equipment and materials. In international practice, customs facilities are associated with fiscal facilities. The free access of goods in the area, in conjunction with the more liberal regime of taxes on the profit realized in the area, represent favorable premises for attracting foreign capital in the free zone. These are necessary conditions for stimulating foreign investments, but not enough. In order to ensure success, in addition to the facilities granted to the free zone, there must be favorable conditions for combining capital with other factors of production (labor force, raw materials), as well as an appropriate infrastructure.

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How to Organize and Manage Free Zones

The free zone represents a geographical space in the territory of a country except from its customs regime, where no import duties are levied and where a special fiscal policy is applied. “Free zones generally fall into one of four categories: free trade zones, export processing zones, special economic zones, or industrial zones”¹.

On the Romanian territory there are currently 6 free zones: Sulina Free Zone, Constanta-South Free Zone and Basarabi Free Zone (both under single administration), Galati Free Zone, Braila Free Zone, Giurgiu Free Zone, Curtici-Arad Free Zone.

It is based on the exclusive role of the state in the creation and administration of free economic zones. As long as the state does not have the means to invest and develop the free zones, and their administrations are invested only with supervisory and control functions, without real levers of asset management, attraction of financial funds and investors, incentives for promotion and development of the respective areas, it is difficult to ensure their high efficiency. And worldwide experience suggests that ZELs organized on entrepreneurship / commercial principles, developed and managed by private entities or on the principle of public-private partnership, are more efficient and better achieve the goals pursued by their creation.

Advantages of the Free Zones

Free zones have emerged on the scene as a planning tool to help boost economic development. They have their advantages, but their policy pitfalls too.

Benefits of using the Free Zone are as follows: the free zones offer more facilities for importers and exporters, customs, fiscal and commercial facilities. Thus, *importers* who bring goods through the free zone enjoy advantages such as:

- approaching the goods of own market
- the possibility to buy various goods from the free zone, after they have been subjected to processing that increase their value and make them more suitable to the internal beneficiaries

¹ OECD Observer, 9 September 2019

➤ the possibility of having stocks of goods nearby, for situations when the international market situation is unfavorable, without having to pay prices to sub-suppliers and without making the necessary efforts in connection with the payment of goods and customs duties related to the importation of large lots

For *exporters* using the free zone, the advantages are:

➤ elimination of the obligation to enter the customs value of customs duties, offered to imported components and materials, thus avoiding the blocking of important amounts

➤ the possibility to respond promptly to the demands of the nearby markets and to sell the goods at the optimum time

➤ the possibility of organizing permanent exhibitions in the area for sale

➤ the possibility of storing the goods in the area without limit and without payment of customs duties, until the moment of the export

➤ tax exemption on turnover for goods sold in areas and re-exported

➤ obtaining important benefits from the difference of transport taxes for the goods brought in bulk and re-exported from the area, after processing

➤ obtaining the certificate of origin of the country in the territory of which there is a free zone, for the goods processed in the area and in which a certain percentage of the products of the respective country has been incorporated (about 50% manpower and indigenous materials)

➤ the possibility to bring subassemblies and component parts from different countries, to process them in the area and to re-export them as a finished product

➤ the right to contribute to the arrangement, endowment, use of the free zone on the basis of cooperation, following that the investments are recovered through the services of area administration.

Types of Industries Attracted to the Free Zones

Most of the industries that meet in the free industrial zones of the world are industries belonging to the textile and clothing industry, consumer electronics, simple household equipment, plastic products, furniture, food and beverages, which need relatively low capital investment. There are also free industrial areas of export, located especially in the developed and emerging countries, which host the heavy

industry and are dominated by refineries and petrochemicals, by bauxite processing companies in aluminum and by car manufacturers, generally located outside the perimeter of "enclave" type, on the initial territory of the enterprise, declared free zone (USA, Hungary, UAE). The development of the heavy industry in the free industrial zones of export is related both to the natural resources of the country of residence (oil, gas, bauxite) and to the semi-manufactured products produced from local raw materials (steel, aluminum, basic chemicals, wood). In this respect, some successful examples in developing countries are relevant:

- companies producing rubber gloves in the free zones of Malaysia, rely on the internal resources of natural rubber
- companies producing automotive components in the free zones of Mexico, based on the use of locally produced steel
- food and cigarette processing companies in free zones in Latin America, based on local raw materials.

5. Analysis of Results

The general objective of the industrial free zones is the promotion of industrialization oriented towards export. The specific objectives consist in attracting foreign capital, creating new jobs, increasing foreign exchange earnings, promoting the transfer of technology and improving the competitiveness of the products, as well as favoring relations with the economy of the country on whose territory the free zone is located. Most of the foreign investors from the Romanian free zones are for now interested in using areas as warehouses for storing products on near term. Interest in processing imported goods to be re-exported, as is the case in most of the existing free zones worldwide, it is in its infancy. Insufficient infrastructure and facilities so far, thanks the non-involvement of the state in such investments does not stimulate the placement of units industrial, though some investors in Japan have expressed interest in creation of fish processing units in the free port of Constanta-Sud and some South Korean investors have expressed interest in arranging some consumer electronics companies in the free area near Turnu-Severin, for the production of products to be exported. As it is known from international practice, the creation of an area free imposes substantial investments. The volume of initial investments, which should be in principle realized by the host country, is on average \$ 5000 / job and usually runs for 5-10 years. Attracting significant investment foreigners are possible only inside this interval.

6. Conclusion

Comparisons between the legislation in the field in Romania and other countries that have remarkable successes (China, Hungary, Egypt and all other treated countries) in the first phase of the study lead to the conclusion that the incentives provided by Romania is not enough to attract investors and the arrangements in the areas free are in the early stages and insufficient. There is formally a law in Romania, which it provides standard incentives and facilities for free zones, as they are provided for in the legislation of the countries competing with their free zones. But while other countries, either developed or developing, that they have free zones, they compete in offering as many and diversified incentives as possible to foreign investors, depending on the field of activity, their power and the magnitude of the investments, in Romania the investors are confused, there is the impression the reduction of incentives and facilities and, therefore, their discouragement.

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