ZONE-ABILITY:

Unlocking the Potential of the Atlantica Region with Special Economic Zones

BARRIE B. F. HEBB

October 2009

Atlantic Institute for Market Studies

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CONTENTS

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Barrie Hebb joined the Atlantic Institute for Market Studies in January, 2008, as a research economist. Prior to joining AIMS, he worked as an economist in the former Soviet Union and in Canada and currently resides in Ottawa and works as a Fiscal and Economic Policy Officer in a Federal Political Party.

Barrie was programme coordinator for the Aga Khan Development Network`s University of Central Asia (UCA) based in Bishkek, Kyrgyzstan. The position involved research on the development of the world`s first internationally chartered institution of higher education; one university, three campuses, three republics, all located in remote mountainous regions in Central Asia. In addition to offering access to high quality educational programmes, UCA focuses on issues involving sustainable development in remote rural, non agricultural, mountainous communities. Barrie worked primarily on curriculum development, economic outlooks for the Central Asian region, staff and student recruitment strategies, and integrating ethics across the curriculum.

He first arrived in the former Soviet Union in 1998 as a visiting fellow in economics with the Civic Education Project. This position primarily focused on promoting reforms in higher educational institutions, lecturing in economics and conducting research on the transition economies. He spent his first year in Tashkent, Uzbekistan, and following three years in Kazakhstan, Kyrgyzstan, and Ukraine. He has also held positions in Economics Departments in Canada at St. Francis Xavier University, St. Mary's University and the University of Alberta. He spent an additional year with the Academic Fellowship Programme in Odessa, Ukraine.

Barrie is originally from Halifax. He received an honors BA from Queen's University (1996) and an MA from the University of Alberta (1998), both in economics. He currently holds a Foreign Government Award from the Russian Federation and is continuing to work on his PhD/Candidate of Sciences degree at St. Petersburg State University when time permits.

INTRODUCTION

Finding agreement on a policy at the national level is difficult for any state. This is especially true in a country as geographically large and economically diverse as Canada and especially for trade issues. Different regions face different conditions, they have different industries and are linked to different degrees with different trade partners in various global networks. They will naturally have different, and often strongly opposing, views about the types of trade policies they would like to see Ottawa adopt at the national level. Imposing a single one-size-fits-all policy from Coast to Coast is likely to be successful only on a few issues shared in common across such a diverse nation and doomed to failure as many regions find they never get what they want and need. A Federal policy that could allow for greater flexibility to reflect diverse trade policy preferences would allow, ironically, regions greater freedom to pursue their interests while at the same time fostering national unity by avoiding a major source of discord. A well designed Federal Special Economic Zone (SEZ) Policy would give Canada's regions the flexibility they need when it comes to trade policy to pursue their interests.

Special economic zones offer a way to improve competitiveness and generate benefits from the flow of trade through a region.[1] SEZs come in various shapes, sizes, and labels, such as free trade zones or export processing zones, but they share a set of common features. An SEZ is a defined space where laws and regulations, especially those related to trade, are more liberal than in the rest of a country. Typically, the territory set aside as an SEZ is considered outside a country's customs regime. This makes the area more attractive for trade activities, since those operating in the zone avoid burdensome tariffs, excise taxes, and usually value-added taxes, such as the goods and services tax (GST). Beyond this relief, the clustering of activities in an SEZ makes it easier to design relevant infrastructure for them, to recover costs through operating fees, and to entice further entrants to the zone through incentives such as tax holidays. Often, within such zones, different levels of government are combined in a single administration, further reducing red tape and, therefore, costs, and improving the competitive advantage of operating inside the zone.

Canada is the only member of the G-8 that does not have an SEZ in the form that is meant here. The closest examples are a combination of two programs. Canada's Duty Deferral Program, implemented in 1996, opened the possibility that some businesses under specific conditions could avoid paying tariffs and excise taxes. Then, in 2001, the *Excise Tax Act* was amended and under the Export Distribution Centre program, activities that would qualify for a similar

[1] For a brief overview of how SEZs function, see Rhee (1994); for more on the types of SEZs and evidence from around the world, see FIAS (2007).

exemption of GST and the federal portion of the harmonized sales Tax (HST) were expanded.[3] Under these initiatives, authorized businesses (those holding certificates for each program) can avoid paying trade-related taxes, replicating some of the benefits businesses receive in SEZs in other countries.

These two programs do not, however, cover the full range of advantages of SEZs, but apply only to businesses operating in Canada that mostly re-export whatever they import into the country and that get back the taxes they pay on imports in tax credits after re-exporting anyway. These programs simply permit participating businesses to avoid paying taxes and having to recollect them, which saves on cash flows related to taxes paid. This is not only a very limited part of the benefits of SEZs, but these programs are complex, require paperwork, apply to a very select list of businesses, do not apply to manufacturing or those selling to the Canadian market, and appear not be well advertised or readily available on either the Canadian Revenue nor Canadian Border Services Agency websites. In short, they do not replicate the benefits of SEZs elsewhere in the G-8 or rest of the world. Thisplaces trade-related activities in Canada and some of its regions, like the Atlantic in particular, at a serious competitive disadvantage because burdensome national trade policies cannot be relaxed to permit a region to trade in the way it might like to, or need to.

The growing complexity and importance of trade means that regions like Atlantica must take advantage of opportunities that will help it to compete and to prosper. An SEZ offers a strategy that would help the region achieve greater potential. Canada, however, lacks a framework that outlines the kinds of special zones that can be created where and how, so it is not possible to predict accurately how such a zone might be established in the Atlantica region or what it might look like. Nonetheless, it is useful to explore the basic concept of SEZs around the world, what they are used for, what the broad costs involved are, and how to create a framework within which to establish them.

The emphasis in this paper is on the implications of an SEZ for the Atlantica region — particularly for the Port of Halifax to stimulate a much needed debate about the need for a flexibility in trade and what types of exceptions might need to be made to allow the region to pursue further trade-related opportunities. Once in place, a well-designed successful SEZ framework would likely foster the creation of other zones across the country. Each of these zones could be tailored to the needs and aspirations of the region in which it is located, and made ready to seize new trade-related opportunities.

[3] Some Canadian airports, such as Vancouver's, have so-called free trade zones, but these are in reference to holders of an EDC certificate. See . http://www.cra-arc.gc.ca/E/pub/gm/b-088/README.html

A NOT SO UNUSUAL CONCEPT

The Importance of a Not-So-Unusual Concept

The first step in discussing making exceptions to national trade policies for parts of a country involves recognizing that societies rarely apply one-size-fits-all rules and regulations. Despite the name, there is nothing really all that "special" about the concept of special economic zones (SEZs). They generally involve making an exception to a set of rules, and society does this all the time. Within a city, for example, there are plenty of rules regulating what can take place within certain municipal zones – speed limits are adjusted upwards and downwards for different traffic zones because one speed would not fit all conditions. Society also makes exceptions for certain behaviours – for example, the consumption of alcoholic beverages is generally permitted, but not, say, while driving, or by those below a certain age, or in certain places. What makes special economic zones "special" is that they are exempted from certain general rules that apply to a country's trade regime that are preventing a region from reaching its potential.

Exceptions to general rules also make sense. They allow society to avoid extreme choices and tailor rules to fit far more diverse conditions than it could do otherwise. To take liquor laws as an example, a society that made no exceptions would face two choices: either to permit all alcohol consumption under any conditions or to forbid it under all conditions. In the first case, there would be no restrictions on consumption by age or while driving; in the second, while prohibition might lessen the incidence of alcohol-related harmful behaviour, it would deny alcohol to those who simply wish to consume it without causing others harm. A society that permits exceptions, however, can choose from a range of options that allows it to satisfy conflicting goals.

The creation of special zones that are exceptions to the country's normal set of trade policies is just a matter of choice, as it is with respect to other issues. As for the rationale for such a policy choice, it is extremely difficult for a country as large and diverse as Canada to develop trade policies that satisfy the interests of all of its regions — what helps one region might well harm another. An SEZ, however, would allow the development of policies tailored to meet a region's particular conditions and goals.

The 1965 Canada-US Auto Pact

The 1965 Auto-Pact between the United States and Canada demonstrates the difficulty of finding a policy that satisfies Canadian "national" interests from coast to coast[2]. US auto companies,

[2] For more information on the Auto Pact, see Canada, "Key Economic Events: 1965, Canada–United States Auto Pact"; available at Web site:
<http://canadianeconomy.gc.ca/english/economy/1965canada_us_auto_pact.html>.

such as Ford, had been producing vehicles in both countries prior to 1965, but Canada typically imported more cars from the United States than it exported to the US market, resulting in a trade deficit in terms of cars. The Auto Pact permitted free trade in autos and components between the two countries, which served to integrate both their markets for their production of vehicles. The Pact also included some protectionist elements[3]. For example, for every car sold in Canada, one (not necessarily the same one) had to be manufactured in Canada, and 60 percent of components had to be Canadian. This condition served to protect Canadian jobs in this sector and to encourage further investments in Canadian production plants in order to sell to the Canadian market and avoid tariffs.

At first glance, the Pact might seem to have been politically and economically good for Canada. It encouraged North American integration, reduced some trade barriers, and gave strong incentives for large (US) auto companies to invest in Canada while offering protection to jobs and creating many more. By 2002, the auto industry accounted for some 12 percent of the manufacturing sector's contribution to Canada's gross domestic product (GDP). Without the pact, most of those jobs and that production would have been south of the border.

But what did the Auto Pact, the vast bulk of the Canadian jobs generated by which were in central Canadian plants, do for the rest of the country? It is a question often repeated in the fall of 2008 and winter of 2009 as hundreds of millions of taxpayers dollars were spent on the so-call auto industry bailout.

Without the Auto Pact, there likely would have been less auto manufacturing in Canada, no preferential treatment for US-made cars over cars from other countries, more consumer choice, and lower prices for non-North American cars. Much larger volumes of foreign imports would likely have flowed into the Canadian market through ports on the east and west coasts and they would be earning more from the increased auto trade between Canada and the rest of the world today. In short, the Auto Pact might have benefited Central Canada, but at the cost of fewer jobs on the coasts in terms of shipping, prep work, possible assembly plants, and distribution centres. The Auto Pact is a prime example of a national trade policy that influenced the subsequent course of development encouraging one type of activity in one part of Canada, auto manufacturing, while discouraging another type, auto shipping and related trade activities, elsewhere.

[3] Japanese auto manufacturers have repeatedly complained that the discriminatory preferences given to North American automakers contradict Canada's international trade commitments.

THE GLOBAL SPREAD OF SEZS

The creation of enclaves with liberal barriers to exchange, in order to attract trade flows, pursue growth, and create jobs is by no means a new strategy. City-wide free zones were in place in Gibraltar in 1704, Singapore in 1819, Hong Kong in 1848, Hamburg in 1888, and Copenhagen in 1891. Despite the liberalization of trade since World War II, the use of SEZs to seize new opportunities in global markets has exploded. In 1986, there were 176 such zones in 47 countries (FIAS 2007); by 2003, the numbers had grown to 3000 zones in 135 countries, employing more than 68 million people and producing more than $500 billion in trade-related, value-added activities. The United States enacted legislation on Foreign-Trade Zones in 1934, but until 1960 there were only ten zones (Da Ponte Jr. 1995). Today, the United States has more than 200 such zones of various sizes and shapes, which handled US$17 billion in exports in 1994 (Da Ponte Jr. 1995).

The recent growth in trade zones, which seek to liberalize trade, should appear ironic, especially in an era often dubbed as one of trade liberalization. In the Post WW II period, trade agreements have been endorsed, tariffs have fallen, and technology has permitted far more rapid and wide ranging trade activities to take place to a greater degree than ever before. Special zoning should appear to be unnecessary. So why should SEZs have become so popular worldwide at a time when Western nations have been engaged – through multilateral and bilateral agreements, free trade deals, common markets and other commitments – in opening their borders to flows of goods, services, and capital? Should the need for SEZs not be decreasing in an era of liberalized trade?

In spite of efforts to liberalize trade in recent years, the fact is that many other barriers to trade remain while others have been erected. Trade is encumbered not only by government regulation and taxes, but also by technological limitations and geography. A hundred years ago, considerable effort had to be expended to export wheat, fish, and meat from Canada in ships that were slower, less reliable, and lacking modern communications. Today’s technology gives people access to quicker, lower-cost ways to communicate and more economical ways to transport goods, services, and people farther and more quickly. As trade has become physically easier, however, it has begun to encounter far more complex mixes of costly red tape associated with the growth in levels and complexity of government. For example, a foreign firm wishing to locate a new branch in Halifax must look at municipal, provincial, and federal codes and regulations, and a host of international agreements that have freed trade in some areas and made it more difficult in others. Costs rise as more items cross more levels of government in more jurisdictions around the world, amid complex webs of rules, regulations, standards, procedures, forms, certificates, and fees. So while it is true that in some ways trade has been freed, in other ways it has not. Governments may have also moved to open access to their markets in some sectors in exchange for reciprocal access to certain sectors in foreign markets, but they have also kept some sectors protected at the same time as erecting new barriers. It is probably more accurate to label the Post WW II era as one of increasingly complex strategic trade.

SEZs are a way to deal with this new combination of greater trade potential and more complex webs of trade barriers and their recent growth is probably their ability to simplify and reduce costs efficiently in an increasingly complicated global trade newtworks. They vary, however, in shape and form, according to the challenges different countries face in global markets, and their varying domestic environments, government regulations, and goals. As a result, there is no generic model of an SEZ that can simply be replicated anywhere with the expectation of success. This is evident from the different types of SEZs that are currently in use around the world:

- ***Free ports***. These are usually large areas covering both commercial and residential parts of a city tied to a port; they typically use broad-based incentives to attract trade-related activities to the zone.

- ***Export processing zones***. These are territories primarily focused on producing exports for foreign markets. Typically, they have relaxed rules on importing needed inputs duty free, as well as simplified customs and administrative procedures, which lower their costs of production and increase their attractiveness to foreign investors. This type of zone is common in regions with access to low-wage manufacturing labour, usually in developing countries, with the hope that export activity will foster industrialization, the acquisition of higher skills, and much needed export earnings and investment.

- ***Free trade zones***. Also referred to as commercial free zones, these are small, fenced-in areas offering warehousing, storage and distribution, transshipment, and re-export facilities.

- ***Urban enterprise zones***. These focus on revitalizing distressed urban or rural areas by providing simplified administration, often dominated by local control, coupled with tax incentives to attract economic investment.

- ***Specialized zones***. These usually facilitate a specific type of activity in a region by encouraging the clustering of such activities and/or by reducing or removing administrative barriers to those activities. Russia, for example, has tourist zones with a simplified administration and other incentives, making it easier for tourists to travel to the zone and tourism industry investors to cluster their activities in special areas that are likely to attract tourism. Such zones also enhance the ability to monitor and enforce standards that might be necessary for property and security protection and the environment. Some zones offer special technical subzones and logistics parks.

Most zones fit in one or more of these categories. Whatever the purpose of an SEZ, however, its primary goal should be to open a set of trade-related possibilities that could not exist in a more restrictive environment. A well-designed framework would allow the zone the freedom to combine benefits and costs with enough flexibility to make adjustments to seize the best possible outcome at the lowest possible cost.

Although zones vary in their objectives, they usually seek some combination of the following benefits:

- ***To attract foreign direct investment (FDI)***. In developing countries, SEZs are used to attract much-needed FDI. Due to low national income, there is often a lack of domestic capital available to self-finance industrialization, infrastructure, or other necessary investments, such as education to acquire skills. Targeting a specific region within the country allows the government to cluster activity in one place, making it potentially easier to finance whatever infrastructure investments are necessary more effectively while offering a trade regime within the zone that is highly attractive to foreign investors. A similar rationale could apply in the case of distressed regions in developed countries, which share many of these same fundamental conditions.

- ***To serve as pilot projects***. Rather than risk exposing the entire economy to a new trade policy regime or liberalization or to severe shocks, a country can use an SEZ to experiment with new policies and to learn from its successes and mistakes in forming a future nationwide policy. China used this rationale as it started to move from command and control to free market regimes. Specific regions were targeted as SEZs and allowed to liberalize their trade regimes and to experiment with free market reforms. A similar rational has been used in many of the other transition economies following the collapse of the communist bloc, but it can also be applied in developed countries in cases where the consequences of new policies are uncertain and some time may be required to adjust (Litwack and Qian 1998).

- ***To increase export earnings***. Low-income countries are often burdened with paying high prices for imports and earning very little from their low-priced exports. Governments in poor countries often lack a domestic tax base and are limited to taxes on trade. SEZs offer a way to provide relief for foreign investors from the costs and risks they might otherwise face in a developing nation and to encourage them to locate their operations there and produce goods primarily for export. Typically, such export processing zones are treated as though they were outside the country for customs purposes, resulting in little or no import duties for manufacturing materials and very lax regulations concerning production. This allows for very low cost production that is much more likely to be competitive on global markets and earns the country much-needed income from exports.

- ***To create jobs***. SEZs can provide strong incentives to locate production in areas with high unemployment. In such zones, trade restrictions, both domestic and international, can be relaxed, customs and excise duties reduced or removed, and tax holidays granted along with a host of other incentives that serve to lower the cost and risk of investment.

- ***To serve as substitute for broader policy***. Rather than pursue liberalization nationwide, some nations choose SEZs as a convenient way to keep the rest of the economy isolated from foreign competition, while still having zones in which exposure to global markets takes place (FAIS 2007).

- ***To simplify administration***. Whether a business is domestic or foreign, the environment within a nation may be complex beyond the issue of tariffs and taxes on trade. If the business is trade oriented, it faces an array of regulations and standards imposed by various levels of government in each market in which it operates. Countries also abide by combinations of multilateral and bilateral trade agreements that can impose high costs on businesses in meeting their information-collection and other bureaucratic obligations. A business in such a country might find itself at a competitive disadvantage compared to firms in countries, or in SEZs, where conditions are far more relaxed and simplified. SEZs typically have only a single administrative window, which serves to simplify the bureaucracy and therefore reduce costs. In developed countries, in fact, this reduction in bureaucratic costs is likely to far outweigh the benefits of simplified customs procedures, and has been cited in countries such as India as one of the major incentives for drafting new SEZ legislation[4].

- ***To encourage overall growth and development***. SEZs are often used to pursue a country's overall growth and development. Poor countries facing highly competitive markets and a very limited tax base can use SEZs to offer relaxed trade and customs conditions, tax incentives, and supporting infrastructure to promote foreign investment in a region. Clustering activity within a zone also provides the benefit that developing countries can focus their limited infrastructure funds more effectively rather than spreading them thinly across the nation. It is also easier to monitor and enforce regulations and standards when businesses are geographically concentrated. A well-designed SEZ can also provide spillovers into the domestic market as domestic businesses learn from the presence of major foreign companies, are permitted to compete with foreign inputs into production within the zone, and potentially develop related links to SEZ activities. A textile firm might, for example, be able to rely on locally produced spare parts over time.

- ***To provide a competitive edge***. A reduction in transport costs, the liberalization of borders, and improved communications have served to widen and deepen markets to a degree unlike ever before. Developed countries are now competing with developing countries more directly to attract and retain firms and create jobs. The higher wages and complex red tape in developed countries, however, places these nations at a competitive disadvantage. Just as some regions simplify their tax codes and regulations to make themselves more competitive, so an SEZ can be used to improve a region's competitive trade position.

The costs of implementing an SEZ depend on the type of zone, but, broadly, zoning involves some combination of the following (see FIAS 2007):

[4] http://www.sezindia.nic.in/

- ***Labour costs***. Operating an SEZ requires the employment of some workers in the zone authority to manage, enforce regulations, and undertake other duties. In addition to the salaries of these workers, there are some additional costs to government bodies at all levels for those who have to dedicate some of their time to SEZs.

- ***Infrastructure costs***. Infrastructure costs incurred will depend on the activities of the SEZ, the current state of its available infrastructure, and the need for other links to networks outside the zone. Some infrastructure costs, of course, are likely to be incurred with or without an SEZ, and some of the investment can be recovered through fees levied on businesses operating inside the zone.

- ***Lost tax revenue***. Because an SEZ typically is considered outside a country's customs regime, some loss of tariff and excise tax revenues can be expected. The extent of this cost varies according to the number of businesses that relocate to the zone to avoid taxes. On the other hand, governments often receive fees from zone activities that compensate for some of this loss.

- ***Socioeconomic costs***. The large number of zones worldwide has furnished clear evidence of the different ways zones can operate on many levels. Some zones have been associated with labour exploitation and with little regard for international standards, while others follow standard labour and other conventions. The presence and degree of these costs really depend on how well the zone is organized, how its rules are established and enforced, and what activities are undertaken there. Although a zone might be considered outside a country for customs purposes, that does not mean anarchy can be allowed to prevail there, as most businesses would find it difficult and costly to operate in a lawless state.

- ***Unfair competition costs***. The ability of businesses to operate in an SEZ's lower-cost environment gives them a competitive advantage over businesses in higher-cost areas. Within a country, the difficulty businesses operating outside the zone might have in competing with those inside the zone could harm development. Steps can be taken to level the playing field and minimize these costs, however, by permitting similar businesses outside the zone to be governed by the same privileges[10] and by authorizing activities in the zone that are likely to have far more positive than negative spillover effects.

[10] In the United States, this is called a sub-zone, and it must be affiliated with a registered zone.

From Russia with trade

Russia, the newest member of the G-8 and facing a serious economic downturn in the 1990s, began experimenting with economic zones as a way to stimulate economic growth, create jobs, and foster modernization. In some respects, Russia sought to replicate some of the success of China's experiment with SEZs as part of its free market reforms to move away from a command economy. In addition to providing tax holidays and a host of other incentives to locate in certain areas, the primary benefits Russian SEZs targeted had much more to do with burdensome government policies. According to Natalya Kuznetsova, to open a new business in Russia, some 200 authorizations are required compared to 40 to 50 in Poland and 5 to 7 in Scandinavia (Alexandrova, 2008). This, in addition to widespread instability and a wide variety of socio-economic problems associated with transition, served to make the country extremely unattractive at a time when the country was really desperate to attract foreign investment, adopt new techniques, and generate employment. SEZs were seen as a way to focus attention on areas with potential and make it administratively easier to operate by lessening red tape coupled with other incentives. Clustering activity in the zones also allowed the government to experiment with new market oriented policies and demonstrate stable governance.

Like any other country considering implementing Special Economic Zoning as a way to make a region more attractive for economic activity, Russia has had to overcome several hurdles. The first set involves recognizing that there are areas with greater potential that are being held back, typically by restrictive trade laws, administrative barriers, poorly designed infrastructure, and a host of other hindrances. The second hurdle involves realizing that these are not all beyond repair. A burdensome administrative regime with lots of red tape can be simplified, taxes on trade reduced or removed, and investments can be made in better infrastructure. The third hurdle is finding a strategy to do this as far as possible and in choosing SEZs, there is a wide variety of models to choose from that vary in degrees of success all over the world. Decisions have to be made about which activities will be permitted, where, and for how long, what the rules are, who will enforce them, how people can set up an SEZ, which types of incentives will be required to make it attractive, and how the territory will be governed, to name but a few. In 2005, after making all of these types of decisions, the Government of the Russian Federation introduced SEZ legislation[5] and established a Ministry in charge of processing, monitoring and enforcing SEZs across the country. There are now over 10 SEZs underway out of a larger pool of applicants.

A successful SEZ framework gives regions the flexibility to implement the type or shape of zone that best serves their interests. Being aware of the costs and benefits, even broadly, is useful in reducing the imposition of criteria and restrictions that affect them and that can serve unintentionally to hinder or prevent a viable zone from taking shape.

Countries have opened their doors to SEZs in different ways around the world, which means there is no single template for Canada to follow; instead, the implementation of a zone depends

5. See http://eng.www.rosoez.ru/oez/evolution/

on the country-specific reasons for its creation. Nevertheless, most zones share some common features or considerations that can help inform an SEZ policy for Canada, including the following:

- ***The existence of a demonstrated opportunity***. The primary reason for permitting the establishment of an SEZ is to allow a region to pursue specific economic opportunities that it otherwise cannot due to barriers that have been placed in its way. Once both the opportunities and barriers have been identified, the specific type of SEZ can be tailored to a country's needs. Ideally, different regions should have a voice in drafting a national SEZ framework that is adaptable to their needs, but that should not deter a particular region, such as Atlantica, from taking the firsts steps, rather than waiting for other regions to lead the way potentially excluding the type of SEZ that might be best for the region..

- ***A policy framework***. Decisions have to be made about which activities will be generally permitted to take place in a special zone and where, which exemptions and incentives will be provided and for how long, and which standards will have to be met. These decisions must be based on the benefits the zone is expected to pursue and the broad costs involved.

- ***Governance characteristics***. Administering the zone involves deciding who operates it, who gets to locate in it, how decisions are made over which areas, how utilities are operated and financed, how standard rules and regulations are enforced, and who will be held accountable. The United States, for example, has a Foreign-Trade Zone Board; in Russia, there is a ministry in charge of SEZs. Generally, involving the private sector in the design and operation of a zone makes it easier to tailor the zone specifically to fit specialized needs, thereby attracting higher-value activities (FIAS 2007)

- ***Infrastructure.*** Since most SEZs require some form of infrastructure, the framework must address how decisions will be made concerning infrastructure investments, how they will be financed, and who will own them and be accountable for their maintenance and basic operation. There is a wide variety of ways in which this is done around the world, ranging from completely government owned, operated, and financed to completely privately owned, operated, and financed.

- ***Legislation.*** Each country's framework is, to a degree, unique. Once the desirable size, shape, and procedures of the SEZ are clearer, it is easier to identify which levels of government need to be involved and what legislation is needed to permit their creation and operation. In Canada's case, in addition to the two policies already in place, amendments to the *Excise Tax Act* would be required to permit exemptions over broader ranges of activities and to provide the ministers who issue exemptions some form of authority over the creation and monitoring of SEZs. Canada likely would tailor legislation to ensure that the zone adheres to international standards with respect to labour, the environment, and free zones to which it is a signatory.[11]

Three examples follow that highlight the fundamental similarities in strategies to target a distressed area and provide incentives to locate there primarily by relaxing trade and administrative procedures. The examples also challenge the common perception that SEZs are used only in Third World countries to manufacture low-cost goods for export using low-skilled, low-cost labour.

Shenzhen, China

One of the most successful SEZs, and one that has gathered attention worldwide, is in Shenzhen, China.[12] That country initiated the use of SEZs during the early stages of its transition from a command economy to a more market-oriented one. SEZs were seen as a way to pilot new market-based reforms, attract FDI, create jobs, acquire export earnings, and foster development strategies that might eventually spread nationwide if successful. China targeted specific regions that looked promising and treated them as enclaves outside the rest of the economy. This allowed China the ability to avoid exposing the entire country to the shock of free market reforms and global competition and the government to take a much more cautious role in managing the painful transition process.

Before 1979, Shenzhen, in South China not far from Hong Kong, was a small fishing village with fewer than 30,000 people. Chosen by Chinese leader Deng Xiaoping to be the first SEZ in China in 1980, a portion of Shenzhen was demarcated as a special economic zone and labelled the Shenzhen SEZ (see Ota 2003). Today, Shenzhen is a thriving metropolis of more than 17 million people; its GDP in 2006 was US$73.82 billion, an increase of 15 percent from the year before. Shenzhen's port, which handled 18.47 million TEUs[13] in 2006, up 14 percent from the previous year, now ranks second in China after Shanghai and fourth in the world after Singapore, Hong Kong, and Shanghai. Shenzhen is also home to some of China's most successful hi-tech companies, such as Huawei and ZTE, and foreign manufacturing companies such as Foxconn, which manufactures iPods and laptops for Apple.

After Shenzhen, China established other zones in Zhuhai, Shantou, and Xiamen, along its southeast coast, and designated the entire province of Hainan as a special zone. China has further expanded the concept throughout the nation and by 2006 there were at least 15 free trade zones, 32 state-level economic and technological development zones, and 53 new and hi-tech industrial development zones. Thus, China appears to use SEZs to target specific areas and as pilot reform projects and to have a combination of the goals mentioned above.

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[11] See World Customs Organization, *Kyoto Convention* (Brussels), chap 2, annex D; available at Web site: <http://www.wcoomd.org/kybodyspand.htm>.

[12] Research by the Atlantic Institute for Market Studies (AIMS) on SEZs — in particular, Shenzhen — was initiated by AIMS' researcher, John Huang, an importer-exporter from that city.

[13] A TEU is a 20-foot equivalent unit of cargo space; thus, the standard 40-foot cargo container is 2 TEUs

Bedford, Indiana

In the United States, urban enterprise zones (UEZs) offer a prime example of the diverse ways people are exploring to relieve particularly distressed areas of cumbersome bureaucracy and to pursue economic improvement. Typically, distressed areas have disincentives to entice new economic activity to locate there. They often lack the right infrastructure, good local schools, or other factors that are typically needed to attract development. Moreover, because the distressed area is not developed, it does not have the income to afford those items that attract businesses and development to the region — the trap of not being able to develop because of a lack of development. Making matters worse, distressed urban areas often face numerous levels of government and other bureaucratic obstacles to improving their prospects. They often lack the political clout to have their voices heard, let alone to change their futures.

In 1983, to focus on this problem by stimulating local development, the state of Indiana passed legislation enabling the creation of local UEZs that would combine incentives for development to locate in a distressed region while empowering the local community to take charge of implementing projects that made sense and avoid the cumbersome bureaucratic process that all too often leaves distressed regions behind.

One such zone was established in Bedford, Indiana.[14] Firms locating in the zone save about 64 percent of the funds they would typically pay in state taxes if they were located outside the zone. This tax incentive entices firms to locate there and to accept some of the risk. Of the monies paid, a very small portion goes to the state while the rest goes to the local UEZ's association. The zone's board is comprised of local stakeholders (businesses, citizens, and other community groups) who decide collectively how to spend the money to satisfy local needs, interests, and goals. The Bedford zone's guiding goal is simply stated on its Web site: "Our mission is to improve the quality of life for all area stakeholders."

This zone highlights the fundamental similarity of all special economic zoning around the world in the sense that distressed areas increasingly face a cumbersome and costly bureaucratic set of obstacles that make it difficult to entice activities to locate there rather than somewhere else. Bedford offers an example, however, of an SEZ that can simplify bureaucratic obstacles while providing a mix of incentives for economic progress. Bedford also shows how an SEZ can be tailored to fit the specific set of circumstances in which a region finds itself stuck.

Latvia

The small republic of Latvia, formerly part of the Soviet Union, is conveniently situated along the Baltic coast between European markets and the large, resource-rich, Eurasian landmass. Traditionally, Latvia had been a transportation and commercial hub along Asian and European trade routes, but during the post–World War II Soviet era, its ports had a largely military focus.

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[14] For more information on Bedford's Urban Enterprise Zone, see its Web site: <http://www.bedfordenterprise.com/>.

After regaining independence in 1991, Latvia wasted little time in moving forward despite its small size, and began experimenting with SEZ policy in the late 1990s as a way to reinvigorate its role in trade, create jobs, attract investment, and reform the heavy bureaucracy, a holdover from the Soviet era, to become simpler, more trade friendly, and ultimately attractive for commercial trade-related activity. Although it has been economically distressed for different reasons, there are parallels between this small nation and Atlantica in terms of positioning between large markets.

There are four SEZs in Latvia:[15]

- ***Riga Free Port***. This SEZ is located near the capital, Riga, has year-round navigation and can handle 20 million tonnes of cargo per year. Well situated along the Baltic, linking several important international markets, the Riga FP has its sights set on becoming one of the leading ports in the region, providing distribution, warehousing, and acquisition services. The emphasis on creating the SEZ, as in most such cases, stressed enabling the port to participate more freely in international trade, attract investment, encourage production, and create jobs.

- ***Ventspils Free Port***. This free port was created for similar reasons as that of Riga — indeed, Ventspils has a larger capacity and the largest crude oil and oil product and liquid chemical transshipment terminals in the Baltic Sea. It also houses the second-largest potash transshipment terminal in the world, is connected to crude oil pipelines, and linked to the rail network of the former Soviet Union.

- ***Rezekne SEZ***. This is located in the southeast of the country, close to the Russian border, and is mostly aimed at the production of wood products for eastern European markets.

- ***Liepaja SEZ***. This zone with some 95,000 people along the southwest coast, covers a large portion of the city and includes a port, airport, industrial centres, and an old military base.

These are only a few examples of the thousands of zones that are being used around the world under varying conditions as tools to pursue opportunities that might not otherwise be possible. There are enough examples to suggest not only that this strategy can work, but also that the framework is flexible enough to meet the goals of any new environment. Neither Canada nor the Atlantica region has to move forward blindly.

[15] For more information on Latvian SEZs, see the Web site: <http://www.lowtax.net/lowtax/html/latvia/jlvfree.html>.

OPPORTUNITIES FOR ATLANTICA

The central argument for an SEZ is that it offers trade opportunities that a region might not be able to pursue otherwise due to the presence of barriers that would be relaxed in an SEZ. To make the case for an SEZ in Atlantica, therefore, one needs to present evidence that these trade opportunities are both real and large, particularly for the Port of Halifax, and held back by barriers that need to be, and could be, relaxed.

Figure 1 indicates the extent to which trade has grown. While there was a general trade flow collapse early in 2009, the forecast is a levelling of the decline and then gradual growth[6]. Before this general decline, export growth had been remarkably high around the world, and typically outpaced the growth of GDP. That means that exports grew faster than the size of economies and, thus, that larger portions of economies are tied to trade than before. Moreover, trade has increased not only in volume but also in complexity, and has shifted away from goods to inputs; in today's world, goods production takes place across many borders – that is, people in a number of different countries are involved in the various stages of production of a single good or service. Infrastructure can handle trade flows only within certain limits, however, and as trade flows grow in volume and complexity over wider areas and require quicker delivery, the pressure on existing infrastructure increases. New routes will appear, connecting new links or replacing old links, and some links will shrink while others expand.

Figure 1 – Worldwide Growth Trends of Exports

Growth in Percent	1990-2000	2000-2005	2006	2007	2008
World Exports	6.9	5.7	10.1	9.2	7.6
USA	7.1	1.9	8.4	7.8	8.5
Japan	4.4	5.9	9.6	6.5	4
Euro Area	6.9	3.6	9	11.9	7.2
East Asia	11.7	15.4	17.7	17.8	15.2
Europe and Central Asia	0.9	9.1	10.3	9.2	8.5
Latin America	8.1	5.3	7.8	4.8	5.5
Middle East, North Africa	4.4	6.1	9.5	4.3	3.8
Sub-Saharan Africa	4.7	5.4	4.4	5.7	7.3

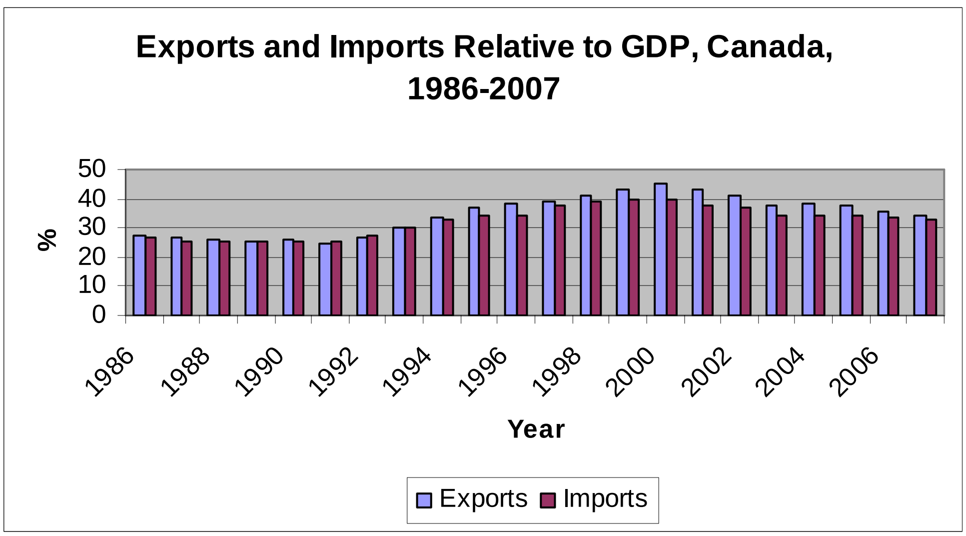
Note: Figures for 2006 and after are estimated and forecast.
Source: World Bank

[6] OECD International Trade Statistics, 15 July 2009

For the Atlantica region, these global trends spell opportunity. The region finds itself well positioned between North American centres of production and consumption and all of these global markets engaging in trade. Further, existing trade routes linking these markets are nearing capacity and require massive infrastructural investments to handle increases in volumes at a time when shippers are increasingly using post-Panamax ships that require deep harbours, which are few and far between. Halifax, as noted, has such a harbour, as well as excess capacity, and could find itself picking up where other routes leave off. The shipping trade itself also has spillover effects into other areas of the regional economy, such as providing local producers and consumers access to more markets, a greater variety of jobs, and new services to supply trading activities.

As world exports have grown in volume, the Canadian economy has become more engaged in world trade, as Figure 2 shows. Trade between Canada and other countries has increased not only as a portion of GDP but also in volume. Thus, trade-related activities in the economy are growing in importance, and those areas of the country that are on trade routes are becoming increasingly important to the Canadian economy and will likely see more activity as the economy becomes even more involved in global markets.

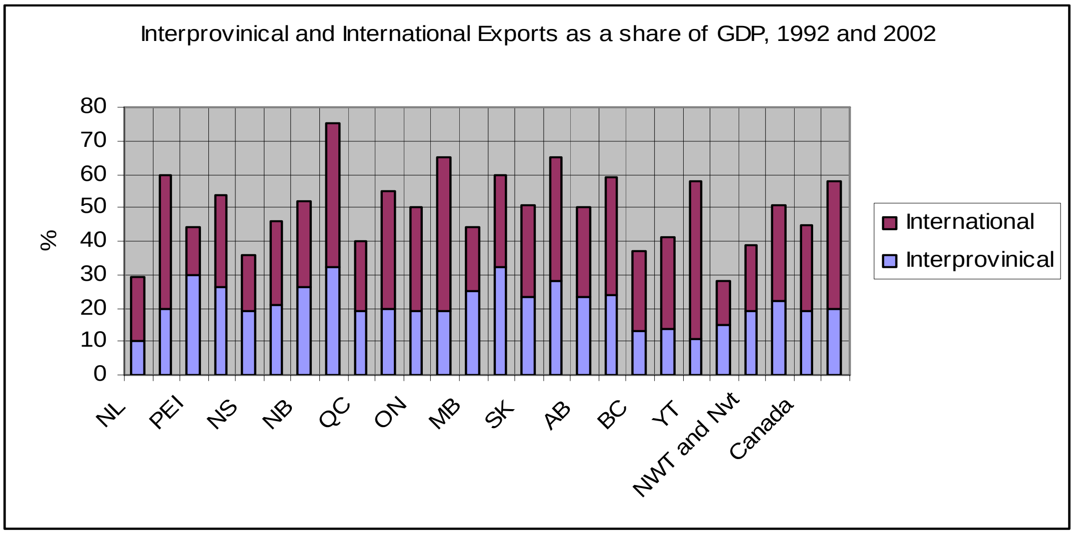
Figure 2



Source: Economic Indicators, International Trade Canada, Bureau of Chief Economist

Figure 3 breaks down exports, both international and interprovincial, at the provincial level for the ten-year period 1992 to 2002. There are several key trends here that are important in terms of opportunities for the Port of Halifax and the greater Atlantica region. First, trade among the provinces is significant in itself, which shows how their economic prosperity is tied together. Second, every province has a significant level of its economy tied to exports to other countries and, in general, that portion has increased across the country. Third, although the relative portions of interprovincial and international exports in each province vary, this can be explained in large part by geography. The very large Ontario and Quebec economies can access the outside world most economically only via the west or east coasts or through the United States. If any of these routes becomes congested, Ontario's trade flows naturally will be pushed in other directions.

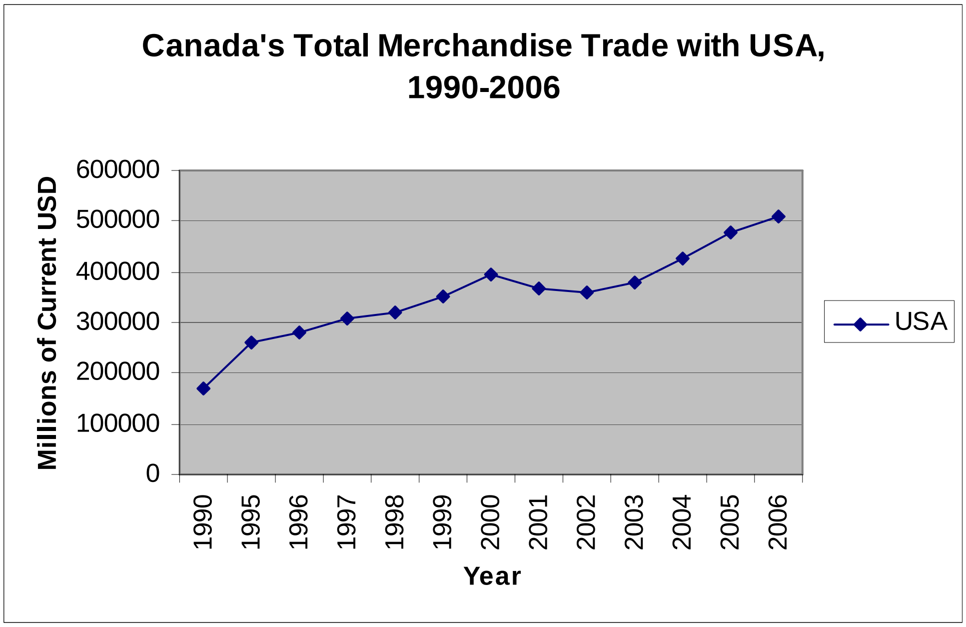
Figure 3



Source: Input Output Division, Statistics Canada

At the same time as exports have grown among the provinces and between the provinces and the outside world, trade flows between Canada and its partners to the North American Free Trade Agreement (NAFTA) have also increased dramatically, as Figures 4 and 5 show. These figures, however, draw attention to yet another set of relationships. The Canadian economy has grown more integrated as provinces trade more among each other at the same time as Canada has become more enmeshed or integrated with global markets. Figures 3 and 4 understate the degree of integration, however, because they do not address the complexity of these trade ties, only the volume.. There are, furthermore, several important implications from these trends. First, they highlight the growing strength of trade relationships and the ties that bind provincial economies in new ways to other economies continentally and globally. Second, much of this trade within North America has been huge, complex, and to an extent unanticipated. So far, the transportation infrastructure has handled this massive web of trade flows, but it has done so reluctantly and now requires not only maintenance, but significant upgrades to handle any further increases (Blank et al. 2006). Third, it should encourage people to think about the way the continent is connected both within itself and between itself and the outside world. From this vantagepoint, Nova Scotia is not just a gateway to central Canada, but to all of North America, and from North America to global markets.

Figure 4



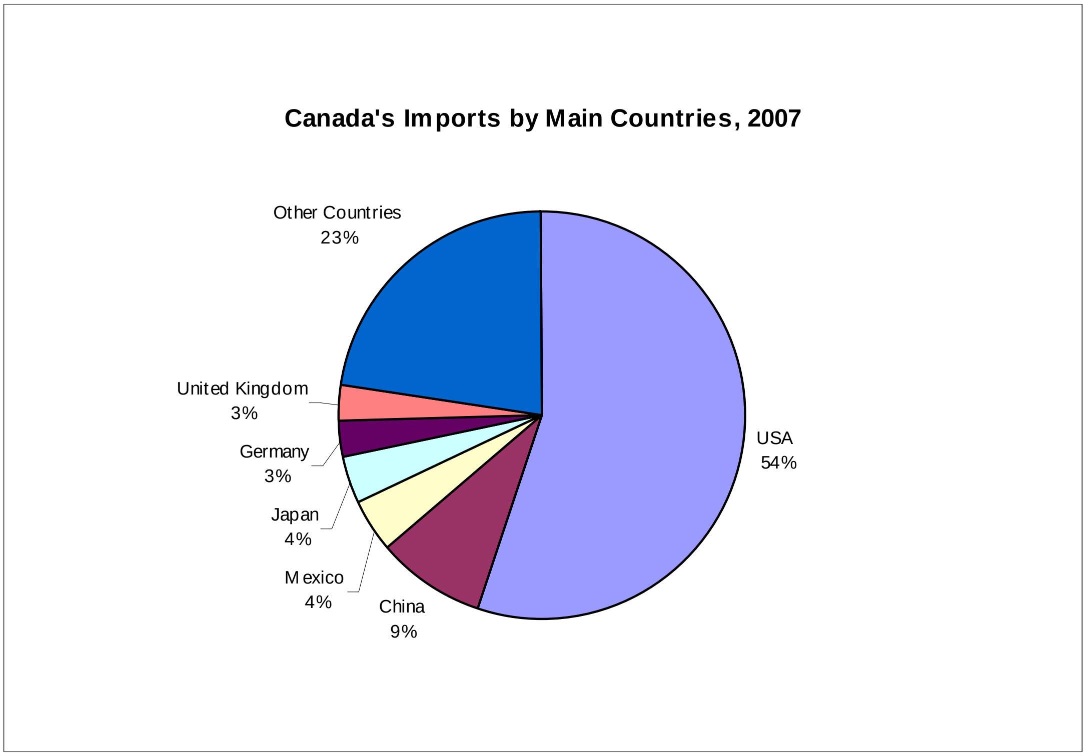
Source: North American Transportation Statistics Database

Figure 5

Source: North American Transportation Statistics Database

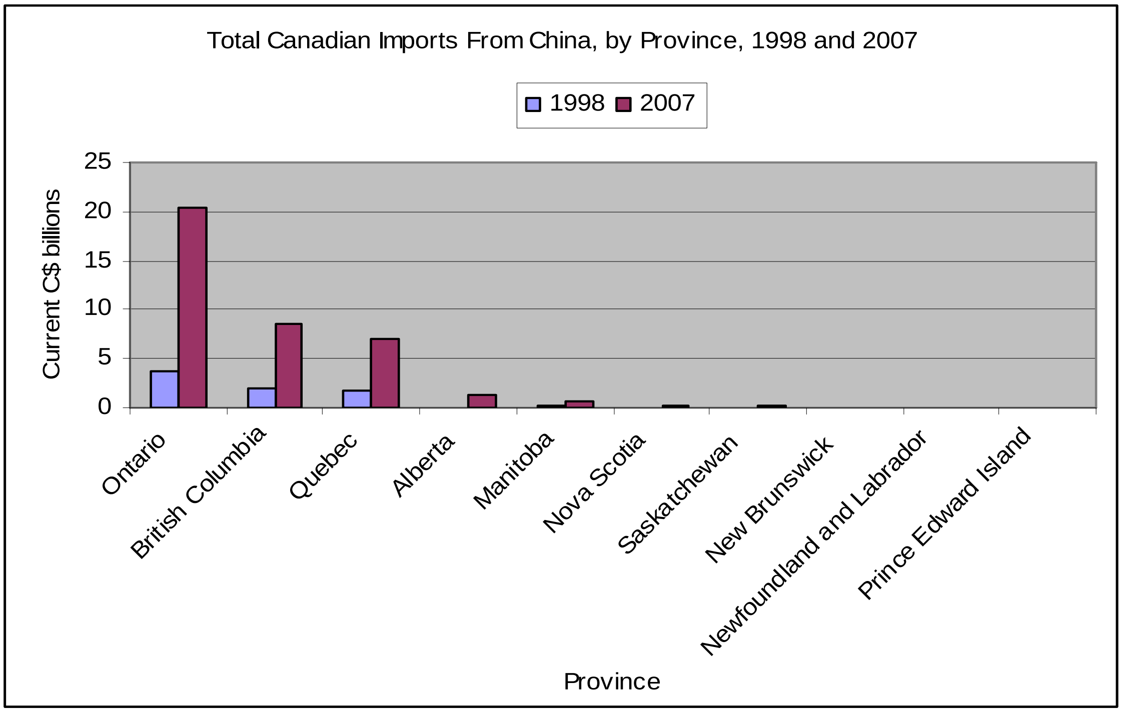
Figure 6 shows the main sources of Canada's imports from around the world in 2007. There should be little surprise about the dominance of the United States. The Canada-US trade relationship, moreover, is complex, since about 70 percent of the trade moving across the border is within related firms, rather than a simple exchange of "US" for "Canadian" goods and services. Also notable is the relative importance of China and Mexico, imports from which outweigh those from Japan, Germany, and the United Kingdom combined. China is now the largest source of Canada's imports after the United States, and this relationship is likely to continue to grow in absolute size, relative importance, and degree of complexity. Figure 6, which breaks down Chinese imports to Canada by province for the years 1998 and 2007, might suggest that Nova Scotia, or Atlantica more generally, has no role to play in Chinese-Canadian trade, since the vast majority of imports flow to other provinces — particularly British Columbia, Ontario, and Quebec — with negligible volumes bound for the east coast. But trade flows to central Canada mostly have to go through other provinces or states, and as those flows increase in volume, opportunities for a port such as Halifax will also increase. Furthermore, this is not the only potential trade flow to consider. Figure 8 shows another example, involving imports into Canada from Latin America, excluding Mexico, for 1998 and 2007 by province. Here, the overall trend is similar to that for Chinese imports, presenting yet another opportunity for Atlantica ports to benefit from increased trade volumes.

Figure 6



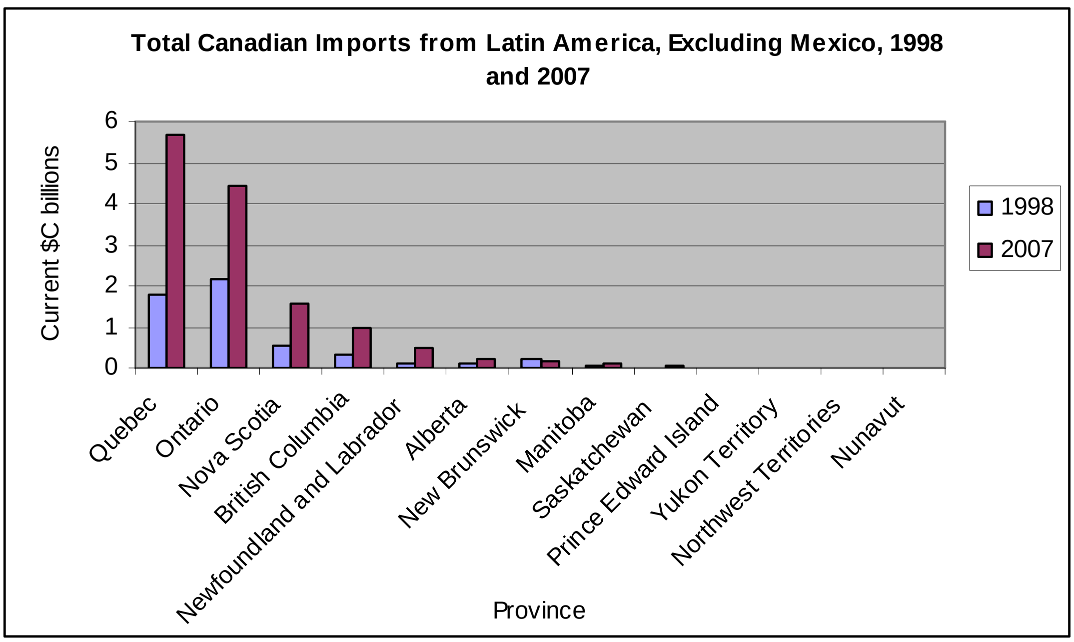
Source: Transport Canada, adapted from Statistics Canada, International Trade Database, February 2008

Figure 7



Source: Industry Canada, Strategis Database

Figure 8



Source: Industry Canada, Strategis Database

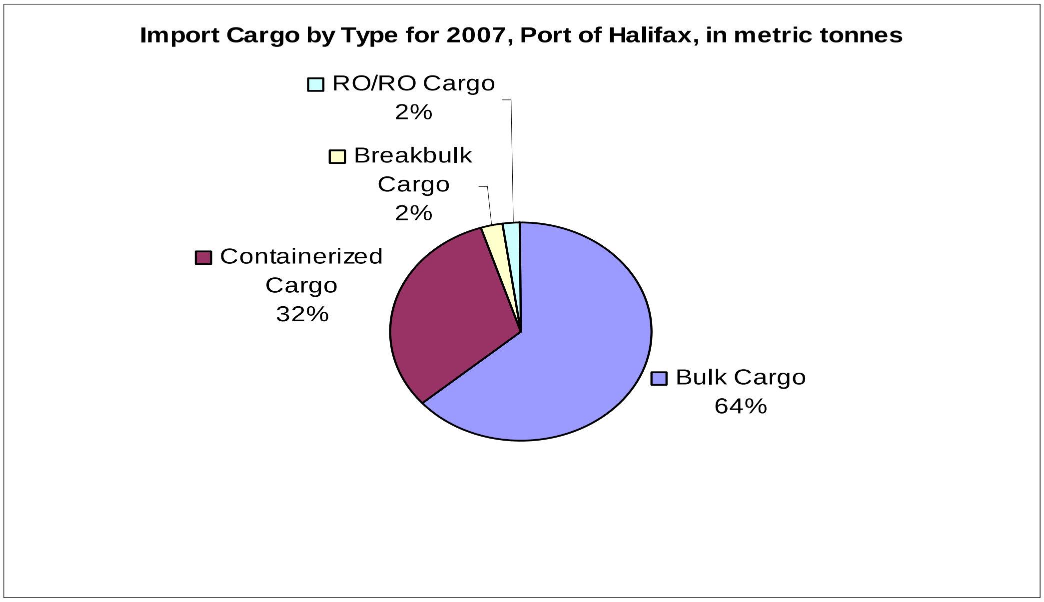
A map may clarify Atlantica's advantageous position along the east coast of North America and the potential for Halifax to act as a point of entry and exit in the flow of trade between the continent and global markets. Figure 9 shows the freight traffic flowing along the eastern side of North America by rail. It looks like a set of veins connecting the coast with the deep inland through a set of networks ranging in size from small capillaries to large arteries. An equivalent map for trucking would show a similar view. Much of this flow has become congested to the further south of Atlantica in recent years. Note, however, that Halifax is well situated at the mouth of entry into North America and also bear in mind that its ice-free harbour is one of the few that is deep enough to handle the larger post-Panamax ships that will play a much larger role in connecting major port hubs around the world.

Figure 9 – Total Rail Traffic Through EBTC in Tonnes

Source: Eastern Border Transportation Coalition

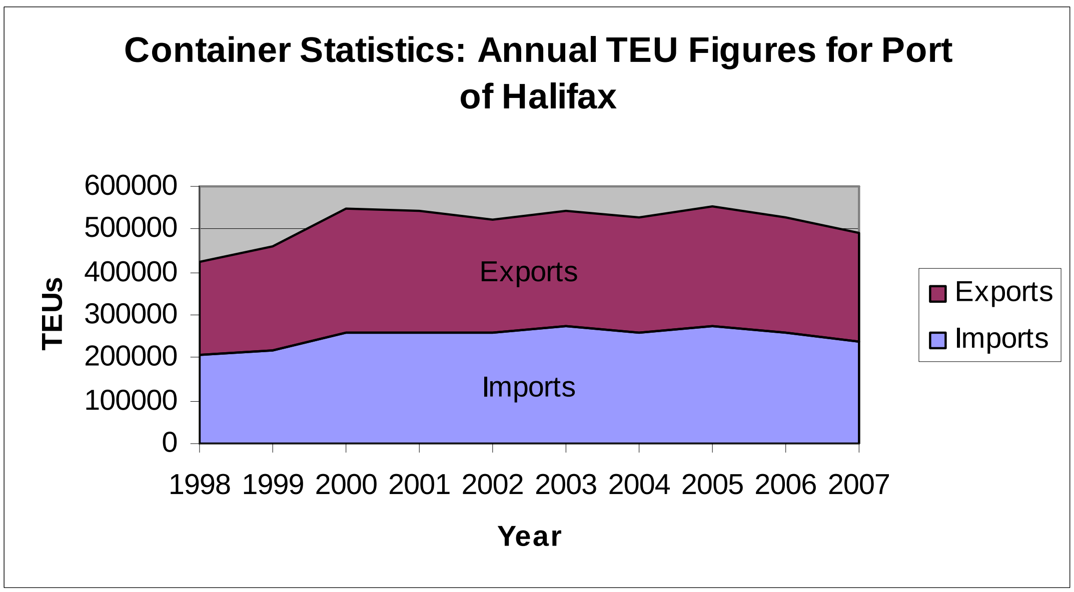
Given the dramatic increase in trade flows, internationally, within North America, and between provinces, and given Halifax's advantages, as just described, one might expect to have seen an increase in the volume of traffic flowing through the Port of Halifax and through Nova Scotia. Figure 10 shows that, in 2007, the largest shares of cargo by type were of bulk cargo and containerized cargo, while Figure 11 shows a very gradual increase, then a decline, in container traffic through Halifax over the 1998–2007 period. Clearly, Halifax has not reaped the benefits of increased trade flows and this begs the question, in light of the evidence, of why it hasn't.

Figure 10



Source: Port of Halifax Statistics

Figure 11



Source: Port of Halifax Statistics

Several reasons are popularly given for explaining what is wrong with Halifax, Nova Scotia, and with the Atlantica gateway concept in general, and, more to the point,why this region is not attractive as a major shipping route.

- ***Existing capacity does not require it***. The large flows of trade have been absorbed by the already existing transportation infrastructure elsewhere. Although further increases in cargo might stretch many of the existing routes beyond their limit, flows have not yet reached this point.

- ***The distance to the hinterland is too great***. Although Halifax is closer by water than are other east coast ports to other ports around the world, it is too far from the inland markets of North America. Marine transportation is cheaper than inland shipping, which puts the region at a competitive disadvantage compared to ports that are closer to inland destinations.

- ***Its infrastructure is inferior***. Although Halifax can handle bulk, container, and other forms of cargo and has connections to air, rail, and trucking to move goods to their inland destinations, infrastructure at competing ports might be more effective at moving cargo between various modes more quickly, reliably, and cost effectively.

- ***It is outside the usual supply chains***. Halifax might be well situated and able to handle increases in trade volumes between North America and global markets, but the competition is not between regions but between supply chains. Shippers do not look solely at the attractiveness of a port in deciding which ones to use to get their goods to their destinations. They also look at the financial cost, travel times, and risk in moving freight between the point of origin and the destination. They are interested in the entire set of links in transportation. The cost of shipping to Halifax might be cheaper, but there are several other modes of transportation required to get to the final destination. A port along the US east coast might be farther and slightly more costly, but it might be better linked to lower-cost, more reliable rail and trucking lines. Shippers are likely to increase their volumes along reliable existing lines with which they already feel comfortable before they risk switching to an alternate route with unknown characteristics.

- ***It is too small***. Halifax is too small to compete with larger, already-established regions that handle much larger flows of trade. Its small size also makes it difficult to reach the capacity needed for the shipping industry to spread the cost of capital over large volumes.

All these reasons have some truth to them. Halifax, for example, though well situated, is far away from other markets. There are, however, two problems with this way of thinking. First, if the geographic advantages on the one hand are more than mitigated by the disadvantages on the other, it would appear that there is little we can do. We cannot move Halifax closer to Chicago or New York. Ports closer to those areas will always be closer and Halifax will always lose the location battle. But many of these disadvantages can be remedied by building better and more reliable links at a time when these other ports also face costly upgrading expenditures to handle additional volumes. Second, these disadvantages are only part of the story. The Port of Halifax and the Atlantica region are in fact well positioned and have a great potential. It is the institutional, policy, setting that is holding them back from further potential expansion.

NO STRENGTH OF DIRECTION

To claim, early in the twenty-first century, that governments in the developed world have been erecting barriers to trade over the past 50 years is generally a great way to raise eyebrows at cocktail parties. Not only has the government of Canada been signing free trade deals (especially in past few years),multilateral and bilateral agreements and treaties, and extending national treatment and most-favoured-nation status to a long list of countries, but people are confronted every day with examples of globalization. Trade flows have increased in leaps and bounds, bringing something from virtually every corner of the earth to the local store even in remote towns and villages. European chocolates, Danish flatware, Swedish furniture, Persian rugs, Middle Eastern canned goods, and Indian aryuvedic toothpaste can be purchased almost anywhere. Halifax's Saturday market features Russian cranberry juice, Japanese caviar, Moscow salami, Indian and Mexican cuisines, and Greek cheeses. There is ample visual evidence that the barriers to trade are falling, and trade flows wide and free.

A sober second thought, however, might change this skewed impression if Canadians turn their attention to what they do not see on their store shelves, in their theatres, or on television. Bollywood produces a lot more films per year than Hollywood, but this is hardly the impression one gets from the local cable network. Variety seems limited in terms of TV programming and in government-controlled alcohol retailing as well. Government bureaucracy means that people who want to move or travel face the need for a wide array of visas and work permits, and softer issues such as health insurance and coverage restrictions. There are restrictions on where people can invest their hard-earned money. Workers are much less free to move across borders today than they were 100 years ago, even though it is much easier and less costly to do so. Here we have one of the strangest paradoxes of the modern era: trade has been made easier and more difficult simultaneously.

It would be more accurate to label the post–World War II era as one of strategic trade rather than focusing purely on one side, liberalization, or on the other, an increase in trade restrictions. Countries have signed agreements committing to reduce tariffs on trade and open up to foreign imports — typically, however, with specific countries, after negotiating on a sector-by-sector or good-by-good basis (see Dymond and Hart 2008). This has allowed countries to trade access to their domestic market in exchange for access for their exports to foreign markets, while protecting some key sectors from foreign competition. As pressure to reduce tariffs has increased, countries have also become much cleverer at finding ways to justify non-tariff barriers to protect sectors of the domestic market — agriculture, for example — from foreign competition. Add to this a myriad different codes, standards, regulations, fees, certifications, and so on.

As a result, what we have today is a mixture of improved access to world markets in some sectors, for some goods, to a degree unlike ever before, and restricted access to other markets in other sectors to a degree unlike ever before. While some parts of Canada have industrialized and enjoyed, as well as prospered from, the protection that the federal government might have provided them, other, far more trade-oriented regions have been unable to engage in trade as widely as they might like or in sectors that are restricted for the benefit of other parts of the country.

A complete list of all of barriers to trade would be long and complicated, but a review of the major tariff and non-tariff barriers provides some idea, first, of how extensive and strange the restrictions are in a supposed era of "trade liberalization" and, second, of how burdensome they are. It also gives some idea of what might holding Atlantica back from engaging in the widest possible trade flows and what the establishment of an SEZ might do to unlock the region's potential.

Tariffs and Quota Barriers

Significant progress has been made since the 1930s toward reducing and removing many tariffs and quota barriers between countries, particularly in the developed world. Many foreign goods and companies are now treated on a par with domestic firms. Almost half of all goods entering Canada do so duty free; with NAFTA, almost 100 percent of imports from the United States and almost 94 percent of those from Mexico enter duty free.

These, however, are averages. Some sectors of the Canadian economy are well insulated from foreign competition and hidden in these broad averages. The average rates also are higher in Canada than they are in the European Union, Japan, or the United States. General tariff rates that apply to imported goods remain at about 35 percent. Among the products that face import tariffs are agricultural products, textiles, footwear, chemicals, plastics, and some wood products. Several products in Canada continue to be supply managed by federal and provincial marketing boards as well as supplier associations (United States 2004). In some of these categories, a limited amount of imports may permitted through import licences and controls, but amounts beyond the quota often face much higher tariffs, if they are permitted at all. Table 2 shows the contrast.

Figure 12: 2003, In- and Out-of-Quota Tariff Rates for Selected Products

Product	Out-of-Quota Tariff %	In-Quota Tariff %
Cream	292.5	7.5
Ice Cream	277	6.5
Beef and Veal	26.5	0
Other Dairy	250.5	6.5
Fluid Milk	241	7.5
Yoghurt	237.5	6.5
Margarine	218	7.5
Wheat Flour	$139.83/tonne	$2.42/tonne

Source: Beckman et al. 2006, 7.

The continued presence of tariffs in some areas and for some goods and services might seem trivial, but they should not be underestimated. Collectively, the damage they cause is considerable. For one thing, they reduce the flow of goods and services through corridors to a level below what it could be, which hinders the ability of some areas to reach threshold levels of capacity or to specialize in the shipment of some goods and services — for example, container-size restrictions on imported fruits and vegetables can prevent bulk imports of, say, US-grown blueberries. In addition, these restrictions reduce specialization internationally and prevent consumers and producers from accessing the best the world has to offer at the best possible prices. Finally, in a world where many parts of products are combined at different stages in many different regions, a restriction limiting any one of these products could serve to restrict possible spillovers into other sectors. A limit on blueberries sounds trivial, but it could prevent juice production, blends, and other related products from being produced and combined elsewhere for shipment to other markets. It is certainly not trivial for people who would like access to the best product at the most competitive price.

These tariff barriers, moreover, are determined at the national level of government and are based on “national interests” or to favour richer, more populated regions. By themselves, the Atlantic provinces and the northern New England states lack the political clout to argue for trade liberalization that favours their region. Within an SEZ, however, tariffs that are particularly bothersome to the Atlantica region could be cut even if they remain in place elsewhere in the country.

Non-Tariff Barriers

In addition to the remaining complex web of tariffs and quotas is the all-too-often-ignored realm of non-tariff barriers (NTBs).[16] In fact, it is really this long list of barriers that continues to hinder trade flows in the developed world, since most trade liberalization in the post–World War II era has focused primarily on reducing and removing tariff and quota barriers between countries on a bilateral and multilateral basis. Even if all tariff barriers were removed and a country entered into complete free trade, there would still be an argument in favour of specialized economic zones, since they could offer ways to further liberalize barriers beyond those posed by tariffs.

The following is by no means an exhaustive list of all of the NTBs in existence. Instead, the list is meant to show that the traditional justification of SEZs has shifted from providing relief from taxes on trade to the wide variety of NTBS that continue to increase costs and impose substantial burdens on the access of producers and consumers to the best the world has to offer.

- ***Trade disagreements***. Trade agreements themselves pose a significant barrier to trade by adding a complex web of preferential treatment between countries, which gives some high-cost nations access to a country while protecting other sectors from foreign competition. Disagreements, however, typically involve only those nations that were

[16] This section relies heavily on information reported in Compass Inc. (2004); United States (2004); and Beckman et al. (2006).

party to an agreement, even though a dispute might affect non-parties as well. Nations can also simply refuse to honour commitments or to offer access to other sectors as compensation. The inability to resolve trade disputes in a timely and predictable manner makes the current system riskier, adds costs, and poses an extra barrier to free flows across borders. A nation caught in the middle could make decisions involving disputes that benefit some parts of the country at the expense of other parts (see Dymond and Hart 2008).

- ***Cabotage***. This set of laws restricts the transportation of cargo and passengers between two domestic points to domestic carriers. This originally applied to marine shipping, but has been extended to cover other modes such as road, rail, and air. Despite recent moves to allow foreign operators to carry Canadian passengers between two Canadian points within Canada, liberalization of the Canadian air industry has a long way to go. The most onerous restriction on trade is short sea shipping, which prevents foreign vessels from carrying cargo or passengers between two domestic points (see Brooks 2005). The many ships thus carrying empty cargo space along their routes artificially causes shipping costs to be spread over fewer tonnes of cargo. It also forces an over-reliance on existing roads and rail crossings and presses them close to capacity. These restrictions pose a serious limit the Port of Halifax's potential, since its harbour is one of the few along the east coast deep enough to handle the large post-Panamax ships. Halifax could be a major hub, with many short sea shipping spokes spread along the coast of Canada and the United States, if it were not for these cabotage restrictions.

- ***Border thickening***. Since 9/11, heightened security concerns on the US side of the border have generated additional paperwork, restrictions, and delays, all of which have served to increase the cost of crossing the border and to hinder the relative competitiveness of transportation corridors on the Canadian side into the US market versus an entirely US route. It has also affected transportation between Canadian points via corridors that temporarily pass through the United States. As an example, rail freight from Atlantic Canada destined for Quebec that travels through Maine comes with a US government requirement for a complete and detailed cargo manifest for sealed rail cars. This route is more geographically direct, but the extra administrative costs involved are an incentive to use all-Canadian routes where possible to avoid them.

- ***Port governance restrictions***. The *Canada Marine Act* limits Canadian ports' ability to raise capital just when new investments to increase capacity to competitive levels are needed (see Atlantic Ministers of Transportation 2008, 15). There are limits on the amounts ports can borrow, and changes to limits are processed through the federal minister of transport, which can take considerable time. Proposed amendments to the Act would provide for a more commercially based borrowing regime. Moreover, US ports also have access to funding and loan guarantees from their federal government, whereas Canadian ports do not, which places them on a less than equal footing.

- ***Interprovincial trade restrictions***. Differences in regulations, standards, and tax codes across provinces make it more difficult and costly to engage in interprovincial trade. Although there are no apparent border crossings, crossing from one provincial jurisdiction to another involves many different licensing and highway codes and professional restrictions, for example. Provincial governments have also typically given preference to provincial operators in government procurement. Although some progress has been made since the 1995 signing of the Internal Agreement on Trade and the following Council of the Federation in 2003, internal trade barriers, which are non-tariff, remain problematic. This imposes many extra costs on regions such as Atlantica, where trade flows are likely to pass through several provincial jurisdictions en route to destination markets.

- ***Government procurement preferences***. Governments in Canada spend a significant portion of Canada's GDP each year. When they give preference to domestic contractors, they in effect impose a barrier to foreign competition for a potentially large portion of the Canadian economy. Making matters more complex, both the federal and provincial levels of government typically give preference to suppliers within their jurisdictions, which serves to impose interprovincial and international trade barriers. These restrictions not only mean that there is less competition for government contracts, forcing the public to pay higher prices, but also that Canadian and provincially based contractors have less access to other provinces, states, and countries. This issue persists despite the Internal Agreement on Trade, which sought to make the provinces reduce and remove provincial preferential treatment, and international agreements on government procurement through the World Trade Organization.

- ***Administrative complexity.*** Canadian consumers and producers face a complex set of rules and regulations spread across multiple levels of government, as well as a web of multilateral and bilateral trade arrangements. Extra sets of rules and restrictions come into play for foreign-owned versus domestic operations. Different complex tax arrangements and added paperwork increase operating costs, especially for businesses operating in a number of jurisdictions. As an example, Canada maintains a long list of controlled items that includes broiler and hatching chickens, turkeys, margarine, hemp, nuclear equipment, ice cream, and medical devices. Cut roses and rose buds from Israel, however, have duty-free access through a new Canada-Israel Free Trade Agreement.

- ***Investment restrictions***. Canada has a bewildering array of provisions for the notification and review of foreign investments in all sectors above certain thresholds. Additional review conditions target uranium production, transportation, and the financial and cultural industries. There are ownership limitations for the fisheries, air transportation, book publishing and distribution, periodical publishing, and broadcasting. The federal minister of industry has 45 days to determine whether or not to allow a proposed investment and can extend this unilaterally by 30 days if notice citing reasons is given to the foreign investor. In telecommunications, there is a 46.7 percent limit on foreign ownership for facilities-based telecommunications service suppliers, but this does not apply to fixed satellite or submarine cables (United States 2004, 67). At least 80 percent of the members of the boards of basic telecommunications facilities must be Canadian citizens. A wide array of restrictions prevents foreign funds and significant management control in a variety of sectors, which serves to make the Canadian market overall less competitive, to cause particular industries to face great difficulties in raising capital, and to discourage foreign investment activity. These restrictions also place an undue burden on a region like Atlantica, which would likely welcome foreign investment, ideas, and input, as well as imported goods and services.

ATTRACTING TRADE TO ATLANTICA

A discussion about strategy starts with an outline of a vision of where a region can go and which obstacles need to be overcome. The status quo, however, is not an option; sitting still with sails furled as winds and currents change means merely accepting one's fate. There are trade opportunities that look favourable for the Atlantica region — in particular, the Port of Halifax. The trade has to flow through somewhere, and if Halifax does not take measures to capture it, it will go through a competing set of links, taking all the benefits with it. A special economic zone would give Atlantica the ability to seize these trade opportunities, by:

- ***Removing or reducing trade barriers***. The region could set its own trade agenda by relaxing within an SEZ those barriers to trade that are particularly in its way. This would serve to remove many of the negative incentives to trade through the Atlantica corridor.

- ***Enhancing incentives to invest***. With a special zone, the region could implement positive incentives, and remove negative ones, to attract investment. Ownership and control restrictions that prevent Canadians from investing where they want and foreigners from investing in Canada where they want could be relaxed. In addition, tax reductions, tax holidays, and a wide variety of other incentives could be used in a non-discriminatory way to increase the benefits of locating here. Time, however, is of the essence, and the economically distressed Atlantica cannot afford simply to wait for the world to discover the region.

- ***Simplifying administration***. Canada's multiple levels of government are complex and cumbersome. Zoning would allow the combining of complex bureaucracies into a single window unit, which would retain standards while lowering the cost of dealing with bureaucracy and red tape. Indeed, since tariffs have already been reduced considerably, reducing the costs of bureaucracy is perhaps one of the greatest benefits of zoning in developed countries, especially for regions attempting to attract complex trade links. This benefit likely explains in part the growing popularity of Foreign-Trade Zones in the United States. Reducing bureaucracy would also simplify administration of the zone itself and allow it seize opportunities without having to face a maze of government programs and permissions.

- ***Improving transportation and infrastructure investment***. An SEZ would allow the region to cluster activities together to foster intermodal transportation links and give them a greater say in the kinds of infrastructure investments they need. It would allow the region to tailor limited social spending much more effectively to meet regional needs and attract outside funds and cost-recovery financing. In the modern trade era, where parts of goods are transported across many borders, in different modes of transport, and in complex ways, anything that helps to develop transport links that fit the market more effectively will increase a region's attractiveness.

- ***Improving Atlantica's competitiveness***. Atlantica — in particular, the Port of Halifax — faces the same choices as other ports and transportation hubs around the world. All are looking at the same basic trends and are having to decide what investments to make to improve their competitive edge. Several are already using SEZs to improve their ability to capture a larger portion of increasing trade flow and the benefits that are derived from doing so. Atlantica should pursue a similar strategy.

Among the benefits an SEZ would bring to Atlantica are the following:

- ***Improved market access***. Compared with those in a similar-sized region less open to trade, producers and consumers in this region would have far broader and deeper access to goods, services, capital, and inputs from around the world at more competitive prices.

- ***Job creation***. Attracting increased volumes of trade flows through the region — including opening the door to high-value-added trade flows in niche areas — would create jobs tied directly to the handling trade, which is growing in complexity, in addition to spinoff activities. Labour market conditions in Atlantica should widen and deepen as the region is opened to more trade, in more areas, with more countries.

- ***Program and reform testing and piloting***. A simplified administration with its interests tied more closely with those of residents would make it easier for new programs and reforms to be tested in the region. As trade and security face new tradeoffs in the post–9/11 world and US links become even more important, an SEZ could pilot new customs clearance projects that would be mutually beneficial to this region and to destination markets. It could also make it easier to pilot new training, research, and educational programs in logistics support, linked financial services, and other trade-related activities.

- ***Growth and development***. A well-designed SEZ would attract trade flows and spinoff activities well tied to spread effects both inside and outside the zoned area. Building and maintaining infrastructure likely would increase the demand for locally or regionally provided support services, specialized equipment, and labour services. Opening up to world markets would also provide a wider export market and lower-cost inputs that could be combined in new ways regionally.

The main purpose of this paper is to advocate a general framework to permit the creation of SEZs in Canada and to discuss what such a framework could mean for Atlantica. The goal, in particular, should be to open the door to the creation of possibilities that currently do not exist, rather than to argue for a specific size, shape, or form of an SEZ for the Port of Halifax. Once the door is open, people can decide which benefits they think are worth pursuing, and an SEZ can be designed to capture what global markets have to offer. Nonetheless, some speculation about what an SEZ in this region might look like is worthwhile, if only to suggest what would be possible if greater zoning opportunities were permitted. An SEZ in the Port of Halifax might entail the following features:

- ***Territory***. An SEZ likely would encompass all of the port's facilities, rail terminals, the airport, and the roadways connecting them. To broaden the scope of its activities, it might also cover distribution and trans-loading parks, possible retail zones, and industrial or business parks.

- ***Administration***. There would be a local zone administration in charge of operations, governance, rules enforcement, and dealing with complaints and appeals — ultimately accountable to some outside higher authority. This body would function much like a municipal government, but have relevant authority over combinations of other levels, such as trade, customs, and the collection of taxes and fees. Criminal justice, for example, would remain outside this administration's control.

- ***Customs***. The zone would be considered outside of Canadian customs, and would operate within standard international conventions, such as the World Customs Organization. It would still have to provide security and support for importing from the zone into Canada and potentially the United States (if US customs clearance could be organized within the zone).

- ***Activities***. Canada's current policies related to SEZs are very restrictive and do not allow for much value-added activity or for manufacturing and re-export to other destinations in Canada. Within the zone, however, manufacturing could be permitted, with access to lower-cost imported inputs, local production for zone businesses, transloading, distribution centres, and, potentially, retail operations in addition to trade support and logistics services.

CONCLUSION

Great opportunities are not thrown in one's direction every day. When they are, the first step is to recognize the chance and the second step is to consider what needs to be done to seize these opportunities and move forward. Global trade flows are highly influenced by geography coupled with many other factors within the domain of intelligence, such as building and designing the right infrastructure to ship cargo effectively from its point of origin to its destination. This means that people can make their geographical location more attractive by focusing on these other factors, within their control, that affect the costs involved with trade.

Technology has made the world smaller and opened up regions in all corners of the world to the benefits of trade to a degree unparalleled in the past. A hundred years ago, the cost of geography tolls and tariffs were the biggest challenges to trade and commerce over vast distances. Today it has a lot more to do with infrastructure and institutional design, or public policy. The administrative infrastructure that trade flows through also has an important, if not vital, role to play. If it is cumbersome, complex, and costly to deal with, when other jurisdictions are finding innovative ways to increase their attractiveness, thought has to be given to improving a region's governance, just like improving the design of a bridge or road. Although we have trade infrastructure and it is currently being used, the complexity of rules, regulations, treaties and other policy instruments has become such an important and costly trade barrier today that this likely explains why so many regions are using SEZs in an era labelled as "free trade" to pursue the best world markets have to offer.

Waiting for National trade policy to deal with these issues is unlikely to be of much use in a country as large and diverse as Canada. Regions are also unlikely to have the clout they need to influence national trade policy in ways that make sense for their economic interests. A one size fits all approach will only achieve national consensus on a few issues while leaving most regions dissatisfied and unable to make the most of what they have to offer. We need a framework that allows greater flexibility for Canada's regions to pursue their diverse trade interests not only for national unity, but for regional economies to prosper: an SEZ policy would provide the kind and degree of flexibility that Canadian regions need.

It is the complex web of multilateral and bilateral agreements, trade deals, and tariff and non-tariff barriers that limits flows, in other words. The Port of Halifax and Atlantica are well positioned along major routes linking distant markets around the world at a time when other well-travelled routes are near capacity and require significant additional investments to handle further increases or the larger post-Panamax ships. A well-designed special economic zone could give the region the competitive edge it needs to attract trade flows and to make the most of a unique set of opportunities. Other regions will seize these opportunities if Atlantica does not.

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