



# ENHANCING THE CONTRIBUTION OF EXPORT PROCESSING ZONES TO THE SUSTAINABLE DEVELOPMENT **GOALS**

An analysis of 100 EPZs  
and a Framework for  
Sustainable Economic Zones



# Enhancing the Contribution of Export Processing Zones to the Sustainable Development Goals

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## Preface

Over the past decade, the popularity of Export Processing Zones (EPZs) has grown in many countries across the global south. There are now over 4,000 EPZs, which is over 3,000 more than 20 years ago. Some countries have made the promotion of such zones central to their economic development strategies, while others have questioned their contribution to national development. Meanwhile, the increasing implementation of international trade rules mean that some of the traditional incentives for EPZs, such as tax breaks for exports, are no longer in line with WTO rules. In that context EPZs, also called Special Economic Zones (SEZs), need to innovate new means of maintaining and developing their competitiveness.

Factory collapses and fires, worker unrest and pollution-related industrial tragedies in developing countries provide stark reminders of the need for high standards of environmental and worker protections around the world, and for multinational enterprise (MNEs) to exercise corporate social responsibility (CSR) throughout their supply chains. In a rapidly changing global marketplace, how can EPZs located in developing countries best position themselves to remain attractive and relevant over the longer term to MNEs and their suppliers?

Building on UNCTAD's recognition of the role of EPZs in the World Investment Report of 2013, this report explores the proposition that EPZs positioned and structured as centres of excellence and innovation both in terms of conventional commercial performance, and also with respect to performance in support of environmental and social objectives, may respond better to the evolving global marketplace.

This work fits into the broader context of the launch of the Sustainable Development Goals (SDGs) and UNCTAD's Investment Policy Framework for Sustainable Development. Across a wide range of investment promotion practices, a new generation of policies is emerging that pursues a broader and more intricate development policy agenda, while building or maintaining a generally favourable investment climate. "New generation" investment policies place inclusive growth and sustainable development at the heart of efforts to attract and benefit from investment. In this context, the present report is intended to stimulate further discussion and exploration of the proposition that a "new generation" of EPZ policies could viably reposition EPZs as centres of excellence in corporate sustainability, attracting investment and contributing to the SDGs.

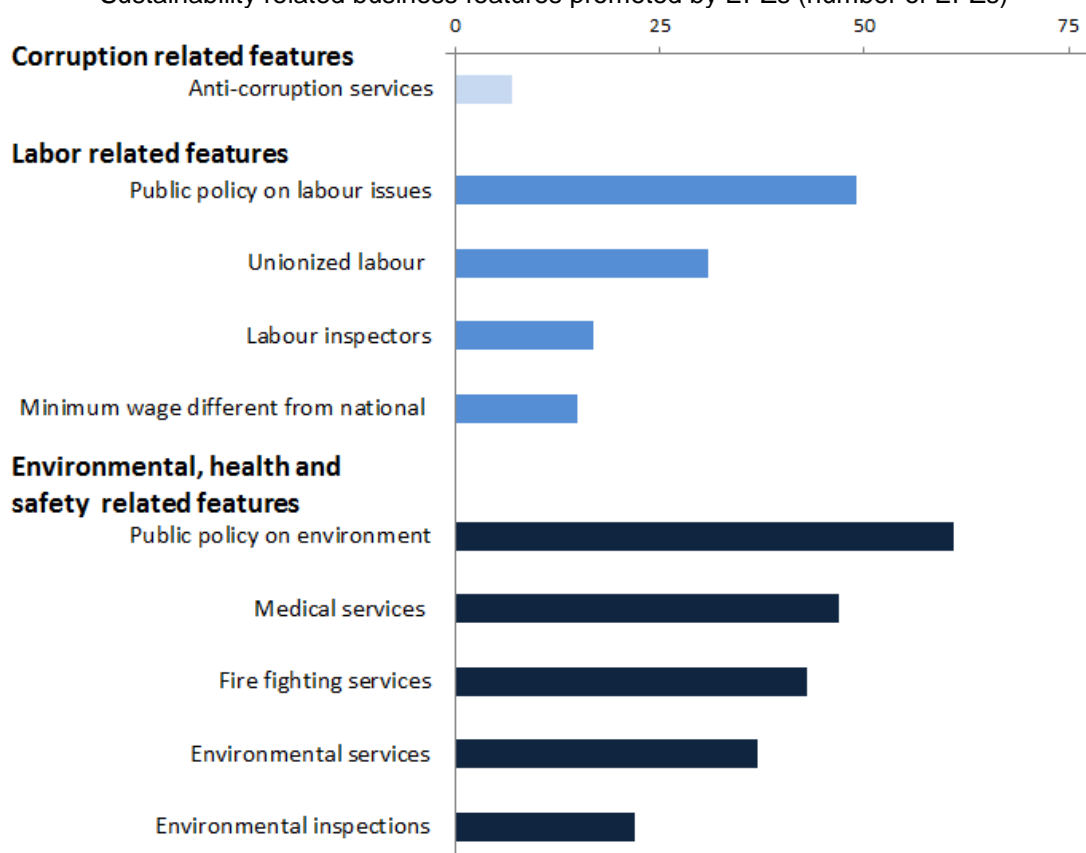
## Key messages

This exploratory report suggests that changes taking place in the global market mean that Export Processing Zones (EPZs), and Special Economic Zones (SEZs) more generally, can be restructured as centres of excellence for sustainable development. Such restructuring would increase the appeal of EPZs to multinational enterprises (MNEs) and their suppliers, while simultaneously contributing to the implementation of the Sustainable Development Goals (SDGs), also known as ‘Global Goals’. The report argues:

- **EPZs face a strategic challenge** as traditional tax incentives for attracting companies into zones become incompatible with international trade law and exemptions for developing countries expire.
- **EPZs can enhance competitiveness through a ‘role reversal’: switching from a narrow focus on cost advantages and lower standards to become champions of sustainable business.** EPZs can find new grounds for competitiveness through meeting the growing expectations on MNEs and their suppliers to exercise good social and environmental practices. “Next generation” EPZs can gain a competitive advantage by not only providing conventional commercial benefits (such as modern infrastructure and expedited permitting), but by also providing cost-effective support for good environmental and social practices for firms operating within their boundaries.
- Although some EPZs are making the transition to more of a sustainable development orientation (demonstrating proof of concept), an UNCTAD survey of 100 EPZs’ public information undertaken as part of this report suggests that **most EPZs are not promoting prominent environmental and social features.** Given changes to conventional means of attracting investment into EPZs, this lack of engagement with corporate sustainability could become a missed opportunity for both sustainable development and for EPZ investment promotion.

### Most EPZs are not yet promoting environmental and social features

Sustainability related business features promoted by EPZs (number of EPZs)



Source: UNCTAD review of public information on 100 EPZs

- **EPZ management agencies can develop services to help firms’ cost-effective compliance with international Corporate Social Responsibility (CSR) standards**, including provision of training and monitoring, as well as health, safety and waste management services to enable a circular economy.
- Governments and investment promotion strategies should **promote competitiveness through enabling efficient performance on all issues that matter to business success, including economic, social and environmental issues**, rather than exempting zones from their own national laws on labour practices or the environment. They could require zones to promote economic linkages with their wider economies of host countries and assess progress towards that aim.
- EPZs operating as centres of excellence for sustainable development could act as pilot projects. **Lessons learned from these “Sustainable Economic Zones” could be applied and scaled up by developing country governments at a regional and national level.** This can be part of the development of backward and forward linkages to the wider economy so that zones are catalysts of wider development. In that way, **EPZs could play a catalytic role in helping nations achieve, *inter alia*, SDG 8, on employment and decent work, 9, on sustainable production, and 12, on sustainable industrialization.**
- **A ‘Framework for Sustainable Economic Zones’ is offered to guide consideration of EPZ standards, infrastructure and administrative assistance** to enhance sustainability performance.

**Framework for Sustainable Economic Zones**  
Key elements for promoting sustainable EPZs

	Policies/Standards	Infrastructure assistance	Administrative assistance
<b>General Approach</b>	Create multi-stakeholder partnerships to identify opportunities and develop an action plan		
	Maintains and enforces policies and standards, including:	Provides services or specialists to insure compliance/offer assistance, including:	Provides guidance and training to companies, covering how to:
<b>Labour</b>	<ul style="list-style-type: none"> <li>• minimum wage</li> <li>• working hours and benefits</li> <li>• respecting right of unions to be active within the zone</li> <li>• gender equality and related issues</li> <li>• incentives for third-party certifications</li> </ul>	<ul style="list-style-type: none"> <li>• labour inspectors</li> <li>• conflict resolution specialists</li> <li>• reporting hotlines</li> <li>• gender focal points</li> </ul>	<ul style="list-style-type: none"> <li>• improve labour conditions</li> <li>• engage in social dialogue</li> </ul>
<b>Environment</b>	<ul style="list-style-type: none"> <li>• emissions</li> <li>• waste disposal</li> <li>• energy use</li> <li>• incentives for third-party certifications</li> <li>• promoting circular economy</li> </ul>	<ul style="list-style-type: none"> <li>• centralized effluent treatment</li> <li>• water reclamation systems</li> <li>• recycling services</li> <li>• hazardous waste management services</li> <li>• alternative energy sources</li> <li>• reporting hotlines</li> <li>• enabling circular economy</li> </ul>	<ul style="list-style-type: none"> <li>• further reduce natural resource use</li> <li>• reduce waste</li> <li>• increase recycling</li> <li>• improve energy efficiency</li> <li>• adopt renewable energy</li> </ul>
<b>Health &amp; Safety</b>	<ul style="list-style-type: none"> <li>• employee health and safety protection</li> <li>• incentives for third-party certifications</li> </ul>	<ul style="list-style-type: none"> <li>• medical clinic</li> <li>• fire brigade</li> <li>• reporting hotlines</li> </ul>	<ul style="list-style-type: none"> <li>• prevent health and safety emergencies</li> </ul>
<b>Corruption</b>	<ul style="list-style-type: none"> <li>• anti-corruption standards and policies</li> </ul>	<ul style="list-style-type: none"> <li>• hotlines</li> <li>• information on reporting corruption</li> </ul>	<ul style="list-style-type: none"> <li>• build capacity to detect and avoid corrupt business practices</li> </ul>
<b>Economic Linkages</b>	<ul style="list-style-type: none"> <li>• employer support for staff training and development</li> </ul>	<ul style="list-style-type: none"> <li>• assistance with local sourcing</li> </ul>	<ul style="list-style-type: none"> <li>• identify and upgrade local suppliers</li> </ul>

Source: UNCTAD

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# 1. Introduction

Historically, the relationship between industrialization, international trade and sustainable development has been varied.<sup>1</sup> Launched by the United Nations in 2015, the Sustainable Development Goals (SDGs) demonstrate the commitment of member states to make that relationship entirely positive. In particular, Goal 8 seeks “full and productive employment and decent work for all,” while Goal 9 is to “build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation” and Goal 12 aims to “ensure sustainable consumption and production patterns”.<sup>2</sup> In many developing countries, Export Processing Zones (EPZs), also called Special Economic Zones (SEZs), are seen as important tools for national industrialization and development.<sup>3</sup> How EPZs enable socially and environmentally responsible industrialization and international trade will therefore be key to national progress on SDGs 8, 9 and 12 and therefore sustainable development more broadly.

In addition to being significant features of international trade, EPZs need to be recognized by scholars and policy makers as novel and important arrangements in the relationship between territory, authority and rights.<sup>4</sup> That relationship continues to evolve today, with rapid changes in EPZ ownership, nature of work, trade rules and market sentiments. If these dynamics are misunderstood by EPZ management agencies, investors and regulators, there could be significant costs and missed opportunities for both investment promotion and sustainable development.

To help develop more effective strategies and policies, this report explores whether EPZs can undergo a ‘role reversal’: repositioning themselves to more systematically support the environmental and social objectives of sustainable development (SD), and by doing so assist in addressing “governance gaps”<sup>4</sup> in the regulation of markets and enable trade and investment to more closely align with the SDGs. This involves a significant ‘role reversal’: transforming EPZs from a largely single-minded focus on increasing exports through lower social and environmental standards and conventional commercial benefits such as fiscal incentives (“first generation” EPZs); to instead creating zones that provide cost benefits but are also centres of excellence for sustainable development, in alignment with international social and environmental standards (“second generation” EPZs, or “Sustainable Economic Zones”).

In the first two sections of the report (“Introduction” and “Global context”), the rapid rise of EPZs in international trade is explored, as well as the implications of international trade law for the future competitiveness of such zones. In the third section (“EPZs and services”), the results of a survey undertaken by UNCTAD for this report evaluating 100 EPZs are summarized in terms of the conventional and more sustainability-oriented features they provide. The fourth section of the report (“Framework for Sustainable Economic Zones”) contextualizes the survey results in the context of wider scholarship on the current and potential of EPZs to support sustainable development and offers some initial recommendations, including a simple framework to guide EPZ managers, investors, regulators and stakeholders. In the final section (“Conclusions”) the report reflects on the

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<sup>1</sup> Bendell, J and I. Doyle (2014)

<sup>2</sup> UNSC (2015)

<sup>3</sup> Lu, Xia (2014)

<sup>4</sup> Sassen (2008)

important competitive reasons for promoting a 'role reversal' among EPZs (moving from low-cost, low-standards zones to cost-effective sustainability zones) and suggests some next steps for future multi-stakeholder action.

## 2. EPZs and their global context

### 2.1 Background: definition and purpose of EPZs

“Export Processing Zones,” “Special Economic Zones,” “Free Trade Zones” (FTZs), “Free Zones,” “Enterprise Zones,” and similar terms and phrases are used to describe geographically limited and specially administered areas within a country that are established to attract local and foreign direct investment (FDI), trade, employment and industrial development.<sup>5</sup> Those operating within such zones (generally referred to as EPZs in this report) are typically provided with certain advantages granted by government or others that those operating outside the zone do not possess. The exact nature of the advantages used to attract investment can vary considerably from one zone to another. Common advantages or benefits provided in EPZs include preferential tax or duty treatment or exemptions from restrictions on the repatriation of profits, direct subsidies and enhanced physical infrastructure, as well as expedited permitting and related services.<sup>6</sup>

These industrial zones may be administered by national, regional or local governments, by the private sector, or in some form of partnership. The OECD describes EPZs as “a policy tool for development and export oriented growth”.<sup>7</sup> EPZs have been a popular policy tool to attract export-oriented FDI.<sup>8</sup> Most EPZs are located in developing countries and focus on light manufacturing activities.

The ILO identifies nearly 30 unique forms of EPZs ranging from zones in China which encompass entire provinces to much smaller fenced-in economic zones.<sup>9</sup> In addition to playing an important role in global value chains and providing a vehicle for FDI, EPZs can act as a mechanism for host countries to develop light manufacturing skills and a competitive industrial labour force.<sup>10</sup> In effect, EPZs can provide a platform for developing the infrastructure and regulatory environment in a country that enables concentrated business activity to take place in a geographically limited area. EPZs offer policy makers a more manageable scale, when compared with the challenges associated with developing the infrastructure of industrial activity and concomitant regulatory environment to operate on a region or country-wide basis. From a development perspective, a positive initial experience at the EPZ level can be scaled up to be adopted on a more widespread basis across a region or a country.<sup>11</sup> In essence, EPZs can be regarded as laboratories for application of new approaches to be applied on a limited basis before more widespread application elsewhere in a country.<sup>12</sup> Thus, it has been argued that improved infrastructure found within

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<sup>5</sup> There is no single authoritative definition of “export processing zones” or the variations on this nomenclature noted above. The description and discussion of the key characteristics of EPZs provided in this report is consistent with the definition of Special Economic Zones provided in World Bank, “Special Economic Zones: Performance, Lessons Learned, and Implications for Zone Development” (2008).

<sup>6</sup> Lang (2010)

<sup>7</sup> OECD (2007) p. 11

<sup>8</sup> UNCTAD (2004)

<sup>9</sup> ILO (2007) p. 24

<sup>10</sup> Siroën and Yücer (2014)

<sup>11</sup> UNCTAD (2004)

<sup>12</sup> World Bank, 2011, op cit., p. 4

EPZs does, in some cases, spill over to other parts of the country as economic development progresses.<sup>13</sup>

Aside from direct fiscal incentives, EPZs can provide a variety of other benefits such as pooled resources for infrastructure that enhances the efficiency and effectiveness of operations within the zone (e.g. centralized waste management, a reliable electricity/energy supply, and seamless internet services), as well as administrative management assistance (e.g. “one-stop” processing of business licenses, and in-house customs offices).<sup>14</sup> All of these benefits are intended to improve the ease of doing business within the zone.

## 2.2 The evolution of EPZs

It has been said that the first modern industrial “Free Zone” was established in Shannon, Ireland in 1959.<sup>15</sup> Since the 1970s, most zones have been created in developing countries. In 1986, the ILO’s database of Special Economic Zones listed 176 zones in 47 countries,<sup>16</sup> but by 2006 the number had grown to 3,500 zones in 130 countries.<sup>17</sup> There are now claims of over 4,500 EPZs existing worldwide.<sup>18</sup> Today, those economies with the highest levels of EPZ based exports tend to be developing economies, including China, Egypt, Indonesia and the Philippines, although EPZs in New Zealand, Ireland and the United States are also among the largest by export quantity.<sup>19</sup> Some countries have made the development of these zones central to their renewed efforts at economic growth. Another way of understanding the global presence of EPZs is through EPZ intensity within a given economy. Research by the ILO has found that developing economies have a much higher intensity of EPZ activity than developed markets.<sup>20</sup>

Reflecting on the popularity of Zones, in 2015 *The Economist* magazine warned that the enthusiasm for zones needs to be balanced with an understanding of what makes them work positively for development, and what can go wrong:

“[EPZs] are often flops. Africa is littered with white elephants. India has hundreds that failed to get going, including more than 60 in Maharashtra state alone in just the past few years. Nor are these efforts cost-free. The incentives offered to attract investors mean forgone tax revenues (at least in the short term). [...] To ensure that these costs are more than offset by jobs and investment, governments must learn from the failures.”<sup>21</sup>

Debates remain about the economic impact of Zones on host countries. Some analysis shows that they are enclaves of economic activity with limited linkages to economic development outside the zones, whereas other analysis shows that they can act as catalysts for development outside of zones. Such catalytic effect involves forward and backward economic linkages with other firms in a national economy, as well as skills transfer into the wider society. The positive impact of a zone therefore appears to be dependent on how a

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<sup>13</sup> ILO (2008) p. 3.

<sup>14</sup> Torres (2007)

<sup>15</sup> World Bank (2011) op cit., p. 3.

<sup>16</sup> World Bank (2011) op cit., p. 5.

<sup>17</sup> ILO (2007)

<sup>18</sup> The Economist (2015)

<sup>19</sup> ILO (2007)

<sup>20</sup> ILO (2008) p. 6

<sup>21</sup> The Economist (2015)

zone is designed and managed.<sup>22</sup> As more evidence emerges of the varying success or failure of EPZs, policy makers and investors are better able to design and manage zones to promote sustainable development. It is important therefore, to consider the latest trends in zones and their global competitive and regulatory context.

### 2.2.1 The changing focus and ownership of EPZs

In addition to their expanding presence, the nature of work taking place within EPZs has also evolved. The trend has been for EPZs to move away from being exclusively locations for business processes using low skilled labour (such as through simple garment manufacturing) to locations for a variety of more complex business processes requiring more highly skilled labour such as that associated with finance and logistics centres. For example, in 2013, the Shanghai Free Trade Zone opened for business, with a focus on attracting the insurance industry.<sup>23</sup> One reason for this trend from use of lower to more highly skilled labour in EPZs has been the phase-out of the Multi-fibre Arrangement (MFA), and the subsequent move away from the quota based system which led companies to source apparel from around the globe. While apparel continues to represent a large percentage of work conducted within EPZs, some countries (notably India, China and several countries within the Caribbean) have developed specialized EPZs focusing on services, electronics, communication technologies and even finance.<sup>24</sup>

Another way in which EPZs have evolved over time is with respect to the increasingly significant role played by the private sector. In a 2008 study, the World Bank noted that perhaps the most notable trend in EPZs over the previous 15 years was the growing number of privately owned, developed and operated zones worldwide.<sup>25</sup> The study found 62% of the 2,301 zones in developing and transition countries were private sector developed and operated. This contrasted with the 1980s, when less than 25% of zones worldwide were in private hands. The World Bank study speculated that a key factor behind the rise of private zones was “the realization that such facilities can be profitably operated on the part of developers, and that the burden such SEZs place on government resources can be reduced.”

The growth in number and diversity of EPZs was noted by UNCTAD in its 2013 World Investment Report when recognizing role in global value chains.<sup>26</sup> That growth has also led to the creation of organisations that seek to network EPZ agencies and their stakeholders, for the purposes of sharing best practices and networking relevant suppliers. These organisations include the World Export Processing Zones Association (WEPZA)<sup>27</sup> and the World Free Zones Organization (WFZO).<sup>28</sup> The growth of such networks could enable the rapid evolution of EPZ strategies in line with international trade and investment trends, and significant changes in the global regulatory environment.

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<sup>22</sup> Winiarczyk (2014)

<sup>23</sup> Yang and Ai (2014)

<sup>24</sup> ILO (2008)

<sup>25</sup> World Bank (2008)

<sup>26</sup> UNCTAD (2013)

<sup>27</sup> [www.wepza.org](http://www.wepza.org)

<sup>28</sup> [www.worldfzo.org](http://www.worldfzo.org)

### 2.2.3 Changing WTO rules applying to EPZs

The competitive landscape for EPZs is changing in part due to an adjustment in the WTO's *Agreement on Subsidies and Countervailing Measures* (SCM) regime that seeks to phase out the use of certain fiscal subsidies for EPZs from the start of 2016.<sup>29</sup> Trade agreements such as the SCM are systems of rules established through the WTO that typically have the objectives of open, fair and undistorted competition across participating jurisdictions.<sup>30</sup> To achieve these objectives, the agreements restrict the ability of member countries to adopt measures that impede the free flow of trade, unless the measures take an approved form and/or can be justified as compatible with certain identified public policy objectives.

Pursuant to Article 3 paragraph 1(a) of the SCM, governments are prohibited from providing direct fiscal subsidies contingent upon export performance (as are sometimes offered to firms operating within an EPZ). As a WTO authored paper explains: "Prohibited subsidies are those which are either contingent upon export performance or upon the use of domestic over imported goods; these subsidies are commonly referred to as export subsidies and import substitution subsidies."<sup>31</sup> The reason that governments restrict tax incentives to EPZ-located firms focused on export is otherwise their products would unfairly compete domestically with firms outside the EPZ that have to pay more tax. However, by restricting tax exemptions to exports, such fiscal incentives can be regarded as a form of subsidy on exports and thus a 'distortion' to international trade. Yet this approach is widespread among EPZs and has been central to their current competitiveness strategy. As a WTO authored paper explains:

"The majority of free-zone schemes have some specific rules on the sale and export of items produced in the free zone into the customs territory of the country. In many cases these rules establish restrictions on the quantities that may be sold or 'exported' to the customs territory of the country. A restriction on the sales to be made domestically is at the same time a requirement for the enterprise to export a portion of its production, thus turning the benefits received by enterprises in the free zone into export subsidies."<sup>32</sup>

The geographical extent of application of this principle is changing, to affect more developing countries. Pursuant to Article 27 paragraph (2)a of the SCM, certain developing countries are not subject to the Article 3 paragraph 1(a) prohibition, if they are "Annex VII" countries.<sup>33</sup> In 2007, a WTO deadline of December 31, 2015 was set for ending the practice of granting exemptions to developing countries that did not meet either of the two conditions set out in Annex VII.<sup>34</sup>

Five countries have transitioned from Annex VII status and are subject to the general Article 3(1)(a) prohibition as of December 15, 2015,<sup>35</sup> and another eight countries have been identified as being within a few hundred dollars of reaching the \$1,000 threshold.<sup>36</sup> Thus,

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<sup>29</sup> See Article 27.4 of the SCM Agreement, and Waters (2013)

<sup>30</sup> This discussion of trade agreements draws substantially on Webb and Morrison (2004)

<sup>31</sup> Torres (2007) p. 217

<sup>32</sup> Torres (2007) p. 219

<sup>33</sup> Annex VII states that countries identified as either a "least-developed country" by the UN or countries with an annual GDP per capita of less than \$1,000 are exempt from the prohibition on export subsidies. The following discussion is based on J. Waters, *op cit.*, esp. p. 484 – 485.

<sup>34</sup> Waters (2013) p. 485.

<sup>35</sup> The Dominican Republic, Egypt, Guatemala, Morocco, and the Philippines, per Waters, p. 485.

<sup>36</sup> The Congo, Cameroon, Guyana, Honduras, India, Indonesia, Senegal, and Sri Lanka, per Waters, p. 485.

several countries will no longer be able to offer subsidies to corporations operating within EPZs at the end of 2015. In this regard, for those countries transitioning from exempt status at the end of 2015, their EPZs will need to provide benefits for corporations operating within their boundaries that take a form other than direct subsidies. As a WTO-authored paper explains:

“They would need to get rid of all aspects that could make a free zone a prohibited subsidy. The aspects that may turn free zones into prohibited subsidies include: (1) requirements to use domestic over imported goods; (2) requirements to export a certain amount of the production; (3) limitations in sales and exports into the national customs territory (including the payment of certain taxes on those sales). These requirements together with the benefits provided put free zones in the prohibited subsidy category of the SCM Agreement.”<sup>37</sup>

One option might be for EPZs to change tax incentives into simple ‘drawback’ schemes, whereby firms apply for rebates on import taxes they have paid on the amount of product involved in producing their exports. However, that may be complicated to administer and conformity with WTO rules is unclear. In March 2015 the WTO composed a dispute resolution panel to hear the complaint of the EU on Brazil’s tax system, which initially included concern on how taxes are administered in EPZs in compliance with the SCM agreement. It was the first dispute ever brought that mentioned fiscal incentives in zones, and may indicate what lies ahead for EPZs.<sup>38</sup>

Does this evolution of international trade law mean the end of an era for EPZs? What options are there for countries that still seek to use EPZs as part of their economic development strategies? In some cases, governments are considering a relaxation of certain regulations, for instance on restrictions on foreign ownership, in the hope this will boost attractiveness to business. Such regulatory relaxation needs to be considered carefully so as not to contradict governments’ international commitments on social, environmental and human rights standards, as well as their existing domestic commitments to such issues. Furthermore, some regulatory relaxations on firms in EPZs, such as on the national minimum wage, could possibly be questioned as a form of export subsidy, if that meant less tax payments would be made by a firm per employee.

Some commentators have suggested that conditioning fiscal incentives within EPZs upon operators meeting internationally-recognized standards of CSR could enable countries to comply fully with SCM requirements while maintaining the economic competitiveness of their EPZs.<sup>39</sup> Leveraging private standards in this way is something UNCTAD has explored in previous studies.<sup>40</sup>

The WTO-authored paper notes that competitiveness for EPZs can arise from factors other than low cost. The attractiveness of EPZs to foreign investors “lies not just in the tax incentives that they may offer. It also lies in the synergies that can be created by having a group of enterprises, including SMEs, in close proximity and with access to improved infrastructure, research and development institutions, an educated workforce and trade

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<sup>37</sup> Torres (2007) p. 220

<sup>38</sup> WTO Dispute DS472: “Brazil — Certain Measures Concerning Taxation and Charges”

<sup>39</sup> *Ibid.*, at p. 486.

<sup>40</sup> Bendell, J., A. Miller, and K. Wortmann (2011)



facilitation programmes.”<sup>41</sup> It is this aspect of EPZs competitiveness that will need to be explored and enhanced and is a key reason for this report. Fortunately the wider trends in global markets provide some opportunities for a new era of EPZ competitiveness.

### 2.2.4 Increasing expectations of and by MNEs, to exercise CSR throughout their supply chains

International CSR standards<sup>42</sup> are indicative of increasingly formalized expectations for MNEs to maintain good social and environmental practices in all their activities. These expectations extend to supplier operations located in developing countries, and therefore to EPZs located within developing countries. A key tenet of the “Protect, Respect, Remedy” framework of the UN Guiding Principles on Business and Human Rights is recognition that only through a combination of government action (duty to protect), business action (responsibility to respect) and multipartite efforts to provide redress, might “governance gaps” be addressed.

MNEs have become increasingly sensitized to the need to respect human rights and adopt sustainable business practices throughout their supply chains.<sup>43</sup> The reason for this includes eight commercial reasons for performing well and often above legal compliance that have been documented by extensive research on CSR (Figure 1).

**Figure 1: Commercial Drivers of Corporate Sustainability**

Studies on the commercial reasons for companies to actively comply with national laws and international standards on social, environmental and ethical issues, and to exceed them, have identified eight key drivers:

<b>Eco-efficiency</b>	Reducing costs, through operational efficiency gains, such as eco-efficiency;
<b>Supplies</b>	Sustained resource base for raw materials, and healthy and secure environment for consumers and staff;
<b>Employees</b>	Enhanced employee relations, thereby improving recruitment, motivation, retention, customer service, learning and innovation, and productivity;
<b>Communities</b>	Enhanced licence to operate from stronger relationships with communities;
<b>Consumers</b>	Improved consumer relations, through reputation and branding, by avoiding negative news and appealing to interests;
<b>Innovation</b>	Connections with voluntary groups, networks and interests of wider society that generate innovative ideas and enable access to new markets;
<b>Finance</b>	Improved relations with the financial sector, including responsible investors and lenders.

Source: Bendell and Doyle (2014)

<sup>41</sup> Torres (2007) p. 223

<sup>42</sup> For example: the ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy (updated in 2014); and the UN Guiding Principles on Business and Human Rights (endorsed in 2011); as well as numerous derivative standards or guidance documents such as the International Organization for Standardization’s ISO 26000 Guidance Standard on Social Responsibility (published in 2010), the OECD Multinational Enterprise Guidelines (revised in 2011) and the IFC Sustainability Framework and Performance Standards (revised in 2012).

<sup>43</sup> UNCTAD (2011a)

Cost-effective implementation of CSR is particularly challenging in international contexts and with SME suppliers at the lower ends of the value chain.<sup>44</sup> One of the critical challenges for MNEs wishing to exercise CSR in all their operations is limited government capacity in many developing countries. Upholding social and environmental protections requires a sufficiently resourced regulatory infrastructure (e.g. trained inspectors) and physical infrastructure (e.g. waste treatment facilities) the widespread implementation of which can exceed the limited resources of some developing countries. EPZs present an opportunity for governments and others to concentrate resources at a manageable and affordable scale to create centres of excellence for sustainable business practices and realise the commercial benefits highlighted in Figure 1.

Can such commercial benefits be sufficient to maintain the competitiveness of EPZs in attracting FDI, given the ending of some fiscal incentives within EPZs? Chapter 3 of this report provides examples of where EPZs appear to be succeeding by enabling CSR. Nevertheless, more research is required on the extent to which benefits from CSR will outweigh a reduction in fiscal incentives.

UNCTAD's 2011 Report to the G20<sup>45</sup> and its World Investment Report 2011 explore the increasingly broad scope and range of CSR codes and standards being developed and used by MNEs and other organizations. While acknowledging the growing importance of voluntary codes and standards to address social and environmental activities of MNEs, there is also recognition that voluntary approaches may not be sufficient to achieve the necessary scale for making widespread improvements (Bendell and Doyle, 2014; UNCTAD 2011b). Thus a combined market and regulatory approach may be the most efficacious way of addressing global governance gaps within and outside EPZs, aligned with the aforementioned UN "Protect, Respect, Remedy" framework.

International commitments to sustainable development, renewed in 2015 as the UN Sustainable Development Goals, also point to the increased focus on aligning investment and industrialisation with social and environmental aims. Goal 9 is to "Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation." One target for Goal 9 is to "Promote inclusive and sustainable industrialization and, by 2030, significantly raise industry's share of employment and gross domestic product".<sup>46</sup> Specifically the text on indicators elaborates that "by 2030, upgrade infrastructure and retrofit industries to make them sustainable, with increased resource-use efficiency and greater adoption of clean and environmentally sound technologies and industrial processes."

Goal 12 is to "ensure sustainable consumption and production patterns." One of the targets for Goal 12 is "by 2020, achieve the environmentally sound management of chemicals and all wastes throughout their life cycle, in accordance with agreed international frameworks, and significantly reduce their release to air, water and soil in order to minimize their adverse impacts on human health and the environment." These goals provide additional policy contexts for governments to take initiatives to increase EPZs contributions to sustainable development.

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<sup>44</sup> UNCTAD (2012b)

<sup>45</sup> UNCTAD (2011c)

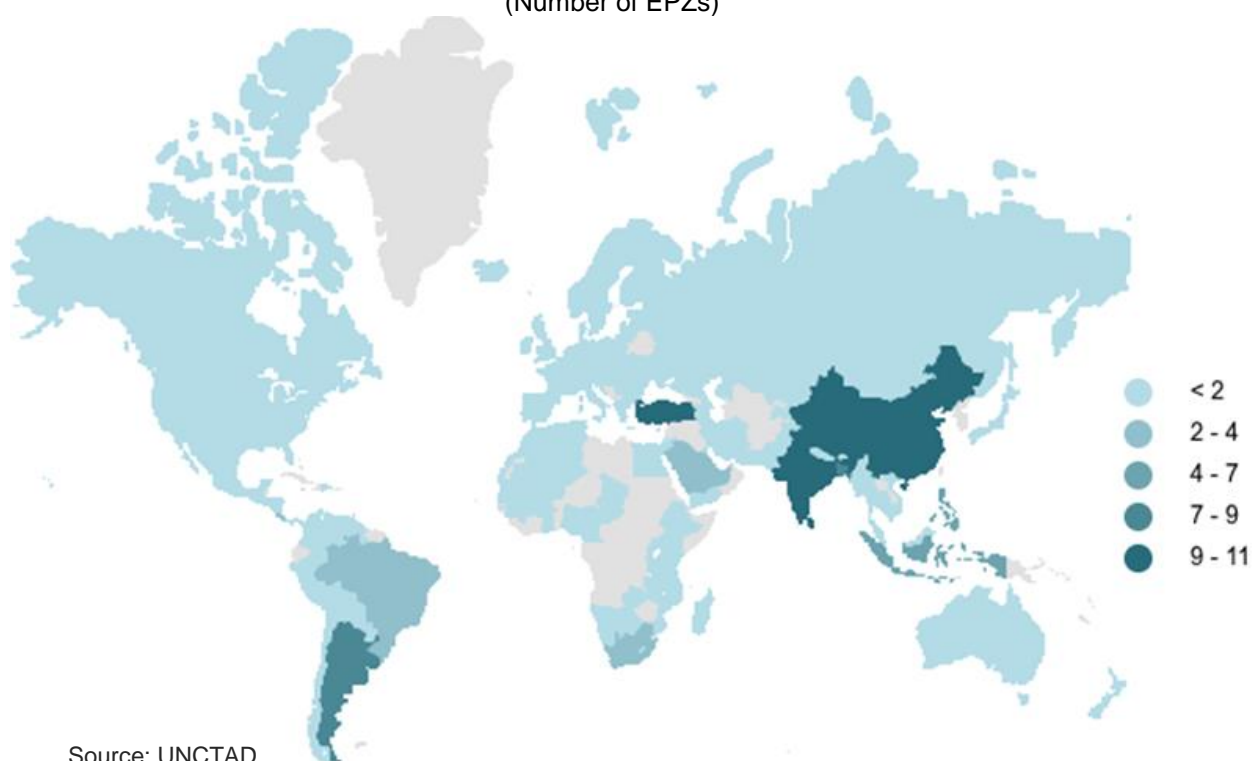
<sup>46</sup> UNSC (2015)

### 3. EPZs and services: analysis of 100 EPZs

Most EPZs provide a variety of services and infrastructure benefits to companies operating within their zone. The extent to which these services and infrastructure benefits enable performance on social and environmental issues will give insight into how well prepared zones are to embrace the new basis for competitiveness described above. Therefore, this section provides an overview of the types of services and infrastructure benefits available to companies functioning within a surveyed grouping of diverse EPZs.<sup>47</sup>

UNCTAD's research was focused on government run industrial parks. These are broadly defined to encompass a variety of geographically limited territories where industrial activity is encouraged, such as export processing zones, special economic zones, etc. To evaluate the role of sustainability services within EPZs a sample of 100 EPZs from around the world were surveyed, using publicly available information. Following an initial focus on developing countries of the G20 the research was broadened to search for best practices from additional countries around the world (see Figure 2 for geographical distribution and Appendix B for a list of EPZs). The methodology of the UNCTAD EPZ survey is described in Appendix A and a list of data points collected is shown in Appendix C.

**Figure 2: Geographic spread of EPZs covered in UNCTAD survey**  
(Number of EPZs)



The data collection focused on the extent to which traditional business services, such as those related to customs, licensing, communications and tax, are promoted by EPZs, as well as sustainability-related services. While the study of public information cannot determine with certainty whether or not these services exist in the zones, the study does provide an accurate indication of what EPZs publicly promote or talk about having in their zones. The

<sup>47</sup> For a complete description of the methodology, see Appendix A.

main elements considered for sustainability-related services were anticorruption, labour issues, environmental issues, and reporting on sustainability policies and performance. Discussion of the results in the following sections has been broken down into two groups: 3.1) conventional business services; and 3.2) sustainability-related services.

### 3.1 EPZs and conventional business services

Most of the EPZs surveyed offer a variety of conventional business services which simplify the processes for companies establishing their business in a particular zone. In terms of policy advantages, many EPZs offer favourable customs and tax policies, which have long been noted as a primary advantage of operating in an EPZ. These services are provided by different actors, including private companies as well as through local and national governments.

In terms of infrastructure, the surveyed EPZs typically offer in-house customs and tax processing. Nearly all EPZs are located in proximity to regional or international transportation hubs to facilitate rapid transfer of goods at lower costs. This infrastructure includes shipping ports, especially large roads, or direct linkages to airports. Within the EPZ, key infrastructure includes stable electrical and water supplies, which can be a challenge to maintain in many developing nations. Most surveyed EPZs also offer world-class telecommunications options such as full telephone and fibre optic/internet connectivity. In addition to these infrastructure benefits, many EPZs offer management assistance to companies operating within the zone. For example, as EPZs are typically geared towards foreign investment, leading EPZs offer assistance to investors during the business licensing application procedures. Over one third of EPZs surveyed offer assistance to incoming investors in obtaining business licenses.

**Figure 3. Traditional business features provided by EPZs**  
Results of study of 100 EPZs. (Number of EPZs).



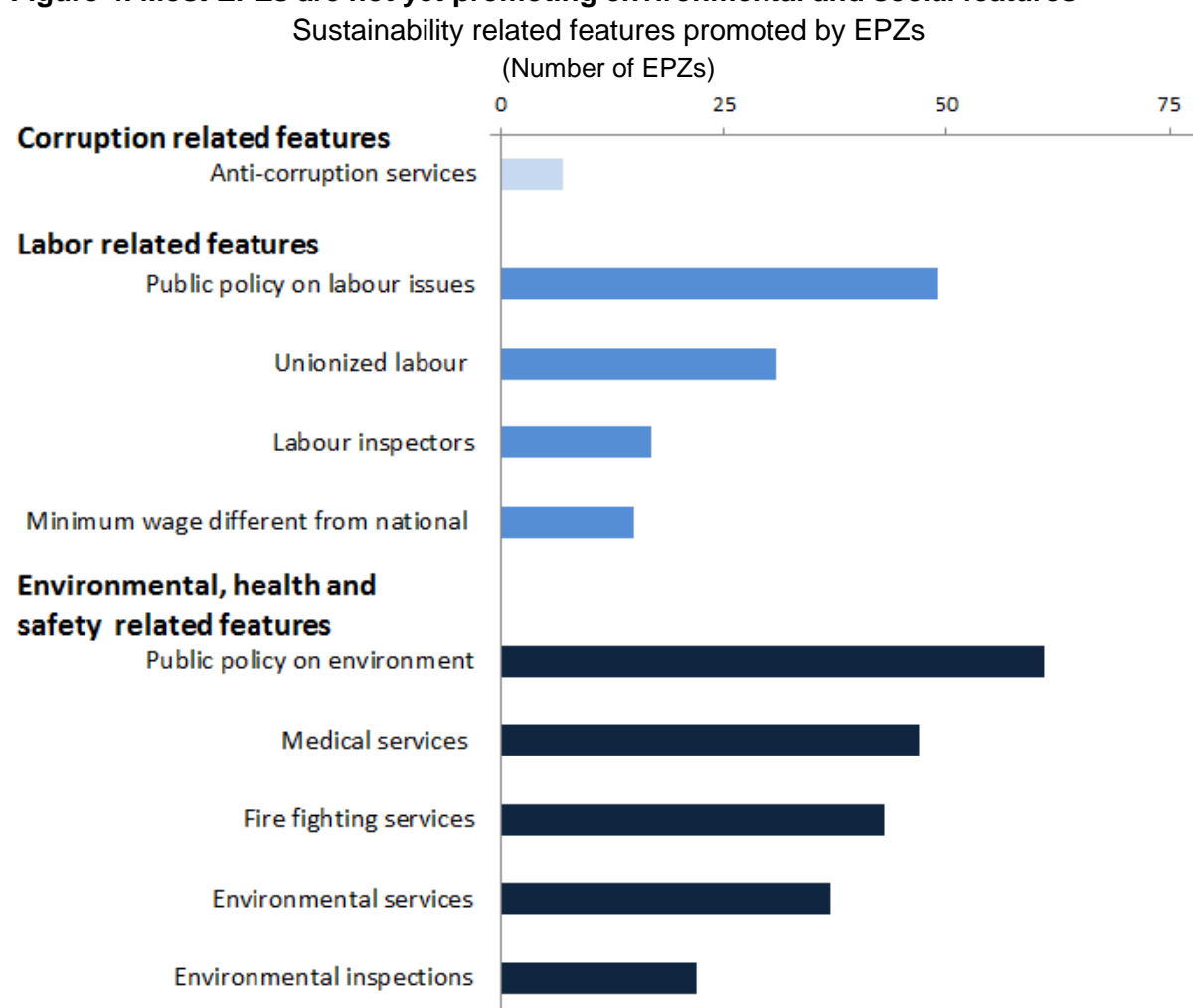
Source: UNCTAD review of public information on 100 EPZs

The offering of this suite of conventional business services assists companies in fulfilling government requirements and is often promoted as a “one-stop-shop.” While not all EPZs surveyed explicitly stated that they offer all of the above services, well over half of the EPZs detailed their services in one or more of these areas. Another type of assistance that is provided is in regards to taxes and customs, with three quarters of surveyed EPZs offering assistance to companies when filing their taxes. The extent of EPZ provision of such traditional business services is shown in Figure 3. A key lesson from this analysis is that specialized support for commercial activities is a normal approach for many EPZs around the world.

### 3.2 EPZs and sustainable development-oriented services

Sustainable development-oriented services can consist of policies, infrastructure and administrative support provided to companies to assist with and promote improved social and environmental practices. The UNCTAD EPZ survey found that such services within EPZs are not widely promoted or available and not all EPZs approach these issues in the same way. In fact, the survey revealed that the majority of EPZs examined promote only a limited scope of sustainable development-oriented services if they offer any at all. The currently partial extension of business support services into the sustainability field is summarized by Figure 4.

**Figure 4. Most EPZs are not yet promoting environmental and social features**



Source: UNCTAD review of public information on 100 EPZs

The implications of this limited engagement with sustainability issues are addressed in section 4 below, where they are connected to reports of variable social and environmental performance, and the wider changes in market expectations. The UNCTAD EPZ survey did find that several EPZs are already providing some SD-oriented services, and there are a handful of leading examples of EPZs that offer services across multiple areas of sustainable development. These few pioneering practices serve as proof of concept for more wide-scale adoption by other EPZs. The rest of this section looks more closely at the survey findings on EPZ engagement of different sustainability-related issues.

### 3.2.1. Promoting responsible labour practices in EPZs

Many EPZs provide some assistance with labour related issues to companies operating within their zone. This assistance comes in a variety of forms and ranges including from provision of infrastructure (such as labour inspectors), to management assistance (such as having an on-site Labour and Human Resources Bureau which assists in resolving labour disputes). The majority of zones which address labour concerns provide modest policy related services such as reiterating the legal obligations of employers towards their employees or recognizing trade unions.

Some EPZs set out clear standards on labour practices for companies operating within their zones, addressing minimum wages, hours, and conditions for the operation of unions. In most cases these stated labour standards conformed to local and national laws but in a few situations (including EPZs in China and India) the EPZ standards were *higher* than those required at the state or national level.

Very few EPZs expressly indicated that inspection services would be available to assist firms in meeting labour standards and policies, but some EPZs did indicate that labour inspectors were present within the EPZ.<sup>48</sup> One Chinese EPZ indicated that it provided an on-site Labour and Human Resource Bureau, which could be an example for others to consider. The Zona America, in Uruguay, provides administrative assistance services through skills training to employees as well as training on business ethics.

### 3.2.2. Promoting environmental sustainability in EPZs

While many zones make little or no mention of environmental concerns, more than half have policies on environmental standards and regulations, and some adopt international environmental management system standards. Policy-related sustainability services have varying degrees of detail and can include standards concerning land, air, and water pollution, waste, noise and the use of energy. Just over half of EPZs examined by UNCTAD set out an environmental policy, including statements surrounding climate change and pollution control. In some cases, these policies are further developed or controlled through a dedicated committee. It is not uncommon for zones to have relatively well developed environmental reporting requirements under which companies are required to report their anticipated amounts of wastes, pollutants, and the decibel level of noise that is expected to be produced. This is the case in approximately half of the zones in Turkey, two of the three zones in South Africa, several in India, Morocco, United Arab Emirates, and to a degree in zones in Argentina and China. A small number of surveyed EPZs explicitly reserved the right to remove a company from the EPZ in the event of failure to uphold standards set forth by the committee.

In addition to policies, leading EPZs provide technical assistance, institutional mechanisms and physical infrastructure to assist companies and promote compliance with standards. Most notable is the availability of hazardous waste management systems, including methods for how waste should be disposed of properly, which can be found in EPZs in, for example, Argentina, Saudi Arabia, South Africa, South Korea and Turkey. This type of service is

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<sup>48</sup> However, few EPZs communicate the specific functions of the labour inspectors or how they may be used by companies operating in the EPZ.



particularly important since most EPZs focus on manufacturing related activities which often generate significant hazardous waste. While numerous EPZs provide services related to the disposal of hazardous waste, only a few EPZs provide recycling services (Saudi Arabia, South Africa, two in South Korea, Turkey and Uruguay). Some will deal with the problem of hazardous waste by simply stipulating the type of firms they allow in their zone. Examples in South Korea restrict the companies in the zone by the types of waste produced by their manufacturing process.

To complement standard energy services, a few EPZs offer alternative energy services to the companies operating within their zone. For example, a few EPZs from Saudi Arabia, South Africa, South Korea and Turkey offer alternative energy sources including solar and wind technologies within the EPZ. In China and South Korea, some EPZs employ alternative energy sources or more sustainable use of traditional energy sources throughout residential and commercial areas which are connected to the EPZs. The Zona America in Uruguay compliments environmental services with management assistance through programs for natural resource reduction and effluent treatment.

Some EPZs located in China's 'low carbon cities' provide environmental services including the development of alternative sources of energy, enhanced waste management systems, grey water recycling and recycling systems connected to a circular economy logic. This is an unsurprising finding, given the emphasis on promoting circular economies in these zones, as discussed in more depth in section 4 of the report.

In addition, several EPZs around the world have been certified to the ISO 14001 environmental management system standard, including locations in China and India. The export processing zone authority of Kenya launched a strategic plan to achieve ISO 14001 certification for all of the zones in that country. The use of these standards within EPZ management also impacts companies operating within the zone and helps to guide management processes towards responsible business practices. One EPZ in India goes further by actively encouraging all companies operating within the zone to become ISO 14001 certified.

### **3.2.3. Promoting worker health and safety in EPZs**

Very few EPZs offer policy or administrative assistance services for worker health and safety. A notable exception comes from Zona America, in Uruguay, which offers "labour risk prevention" programs. The majority of services for health and safety are infrastructure based, e.g. clinics. That said, less than half of all the EPZs studied mention medical clinics or onsite medical personnel in their public information. The medical services mentioned typically offer assistance during medical emergencies as well as routine medical exams.

While firefighting services are suspected to be in place in most EPZs around the world, less than half of the EPZs studied made any mention of it in their public information. Given the international attention paid to deaths from factory fires in many global value chains, it is noteworthy that EPZs do not place more emphasis on this service.

### **3.2.4. Promoting good governance: combating corruption in EPZs**

Almost no EPZs offer any explicit services to assist companies in combatting corruption. One EPZ from South Africa has a clear “no tolerance” policy for corruption, and offers contact phone numbers for companies to raise complaints. However, the phone service is not geared exclusively for corruption related complaints.

As summarized in Figure 4, it appears that EPZ management agencies report more support for firms on environmental performance issues than either anti-corruption or labour issues. The research did not explore the extent to which EPZ agencies encourage or require firms to generate wider economic benefits for the host country, such as through local sourcing, staff development, and technology transfer. That could be addressed in future research.

While provision of sustainability services is relatively low in the sample studied, there are nevertheless some existing good practices which provide a proof of concept and set an example for promoting more sustainable EPZs. The next section discusses these good practices and compiles them together in a framework for what a sustainable EPZ might look like.



## 4. Framework for Sustainable Economic Zones

The UNCTAD EPZ Survey's findings on the limited scale of EPZ action on social and environmental issues suggests a missed opportunity and strategic risk for some EPZs, given the concerns that have been reported about practices in some zones. This section reviews the wider scholarship on EPZ performance on these issues. Drawing upon the analysis in Section 2 on the changing competitive context, and the analysis in Section 3 on existing practices, this section outlines some areas for strategy and policy development, including the outline of a "Framework for Sustainable Economic Zones".

### 4.1 Mixed profile of EPZs on sustainable development issues

The survey for this report did not analyse social and environmental outcomes in EPZs, as the focus was to analyse the extent of public commitments to corporate sustainability by EPZs, to indicate the extent of their preparedness for a new competitive context and their potential to contribute to the SDGs. To contextualize these findings, it is important to draw on wider scholarship on performance by EPZs, and case studies of what some zones have been able to achieve. This section focuses on labour and then environmental issues, before a wider discussion of strategic and policy implications.

Firms within EPZs are major employers, and traditionally lower labour costs have been a factor in EPZ competitiveness. The UNCTAD survey of EPZs found limited evidence of publically reported proactive efforts by zones to enable good labour standards. What might the realities be like on the ground? Drawing on studies by the ILO, the WHO, and others, Lang describes situations concerning non-compliance with labour rights and health and safety protections in EPZs,<sup>49</sup> noting the ILO's findings such as "excessive overtime is consistently a problem in EPZ workplaces"<sup>50</sup> and the WHO's conclusions that "EPZs have been associated with high levels of machine-related accidents, stress, and intense exposure to toxic chemicals."<sup>51</sup>

Legislation in most developing countries pertaining to industrial relations,<sup>52</sup> health and safety and environmental protection stipulates that businesses operating within their borders (including those operating in EPZs) must meet the environmental and social requirements embodied in these laws. The ILO has suggested that the "strength of national legislation is often not a good indicator of actual labour conditions because weak government agencies are unable to enforce the law."<sup>53</sup> In some countries, labour inspectors lack transportation to visit EPZs and never conduct preventative inspections.<sup>54</sup> Thus despite the existence of environmental and social requirements enshrined in national legislation, there is limited assurance that those requirements are effectively implemented within EPZs.

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<sup>49</sup> As discussed in Lang, *op cit.*, esp. pp. 18 ff.

<sup>50</sup> ILO (2008)

<sup>51</sup> Loewenson (2001)

<sup>52</sup> ILO (2012) p. 8. For example, pertaining to freedom of association, the right to collective bargaining, non-discrimination, equal pay between men and women, the abolition of forced labour, and the elimination of child labour.

<sup>53</sup> ILO (2008) p. 59

<sup>54</sup> ILO (2012) p. 14

Research on labour and human rights practices within EPZs has shown mixed results. The ILO has noted that “[t]here are very few preventative initiatives undertaken by labour inspectorates within EPZs, for example efforts to reduce accidents, work related diseases or strategies to prevent any unfair labour practices. Being reactive, inspectorates only intervene once a standard has been violated or an accident has occurred, whether the intervention is initiated ex-officio or through a complaint from a worker.”<sup>55</sup> This suggests the need for innovative approaches, incentives and administrative infrastructure to ensure that good environmental, social and governance (ESG) practices are maintained in EPZs. In particular, such approaches should involve local groups, including local civil society and trade unions, working with employers and government to strengthen the role of monitoring compliance with standards. Voluntary international CSR codes can also play a role, guiding MNE relations with members of its value chain located in EPZs.

Overall, information concerning labour inspections within EPZs is limited and inconclusive, and both the ILO as well as several other UN bodies have called for improvements in this area.<sup>56</sup> Of particular concern to some commentators is that some government administrations have used zones as a means of providing firms with exemptions from national labour laws.<sup>57</sup>

On the other hand, there is some evidence that labour practices may also be better inside some of the zones, compared to practices elsewhere. The OECD has noted that several studies have pointed to improved labour benefits within some EPZs.<sup>58</sup> There are instances where EPZs have provided opportunities for governments, employers and workers to come together to develop tri-partite solutions to social issues. A good example comes from the Tripartite Agreement that is in place in Nicaragua’s Free Trade Zone System.<sup>59</sup> The Agreement has been described as “creating an ongoing dialogue among the industry’s main stakeholders about how to preserve and increase Nicaragua’s competitiveness while simultaneously ensuring that workers benefit from the industry’s growth.”<sup>60</sup> In 2010, a Tripartite Labour Commission was established to institutionalize dialogue and cooperation among the stakeholders.

It has been reported that problems with labour relations have decreased as a result of concerted work with the private sector, CNZF/government ministries, and unions:

“The conflicts that had been more frequent, those related to union formation and collective agreements, have significantly been reduced in number. Before 2007 it was typical that free-zone representatives would ask for a list of workers that were in the process of forming a union. Employers would use this list to fire workers before the union got to be created. Now, there is

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<sup>55</sup> ILO (2012) p.14

<sup>56</sup> ILO (2012) p. 16

<sup>57</sup> The Economist (2014)

<sup>58</sup> OECD (2007) p. 31

<sup>59</sup> The following account draws primarily on Gereffi and Bair (2010)

<sup>60</sup> In Nicaragua, the Free Trade Zone system is governed by the National Commission of Free Trade Zones (CNZF), originally established in 1976 by government decree. In 2009, the CNZF took a leadership role leading to the signing of tripartite “Economic and Labour Agreements” (involving business organizations, unions, and government ministries as tripartite partners) addressing specified improvements for workers. For example, with the stated objectives of saving jobs and promoting labour stability, and attracting responsible investment that guarantees the creation of more and better jobs, the Tripartite Agreements require specified annual increases in the minimum wage over several years, detailed steps towards improved living conditions including construction of 1,000 low income houses over a three year period, provision of 40,000 food packages, creation of recreation centres, and establishment of savings and loan cooperatives.

an effective level of protection of labour rights. The level of conflict has been significantly reduced. Furthermore work relations have improved since the social dialogue was initiated.”<sup>61</sup>

A 2013 report indicated that “Nicaragua’s EPZs have continued to grow with this agreement”<sup>62</sup> and that “employment in EPZs continues to increase and the Tripartite Labour Commission’s efforts on behalf of workers has brought stability to labour relation issues.”<sup>63</sup> The above-described situation illustrates the potential for EPZs to become centres of excellence on social issues.

In Sri Lanka, the Ministry of Labour introduced an integrated inspection system where a multidisciplinary team of inspectors visited a factory to carry out an overall evaluation of all aspects of compliance including labour, health and safety, and environmental considerations.<sup>64</sup> Similarly, the ILO has also called for engagement in CSR initiatives and employer-led audit schemes, which includes better integration of labour inspection programmes with existing public private programmes and schemes, such as the ILO/IFC Better Work programme, and other similar initiatives.<sup>65</sup>

The economic contribution of zones to host countries is cited by some as a reason for lowering standards or expectations on labour issues, including on wages. However, studies on the economic contribution of zones over decades have found that cheap labour is a poor basis for maintaining a zone’s competitiveness and enhancing its contribution to wider development. For instance, twenty years after EPZs were introduced to Poland, detailed analysis shows that while there have been a range of economic benefits from increased FDI, the zones have not overcome the sustainable development challenges of the regions where the zones are located. One study suggests that the nature of the incentives used to attract firms influences the type of firms and activities in that EPZ which then shapes its industrial culture.<sup>66</sup> It is not straightforward for firms and EPZs that are focused on cost savings via tax incentives to evolve their competitive advantage. Analysis of zones over 20 years suggests that unless there is a coherent proactive approach to develop local employee capabilities and evolve the strategies and approaches of firms in EPZs, then the contribution of an EPZ to a region’s development may be fundamentally limited.<sup>67</sup> Likewise, the potential of a zone to act as a catalyst (rather than an enclave) of economic development may be supported through the pursuit of good social and environmental practices in a zone.

Environmental issues are also a key part of the new SDG agenda, particularly Goals 9 and 12, which recognize the need to integrate environmental concerns into economic development strategies. The UNCTAD survey of EPZs found that while environmental services are still not widespread among zones, the subject is more actively addressed by EPZs compared to labour issues. Other studies on environmental performance in EPZs show mixed results. The OECD has noted that there is not strong evidence for differing environmental standards within EPZs and in the regions outside of zones.<sup>68</sup> There is also some indication that foreign companies may be demanding improved environmental

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<sup>61</sup> Ibid., p. 51.

<sup>62</sup> Per: J. Waters, op cit., at p. 522, fn 236.

<sup>63</sup> Ibid.

<sup>64</sup> ILO (2012) p. 16

<sup>65</sup> ILO (2012) p. 27

<sup>66</sup> Winiarczyk (2014)

<sup>67</sup> Ibid.

<sup>68</sup> OECD (2007) p. 29

practices in EPZs and the OECD has also noted cases where governments have put in place stronger environmental standards because of industry concentration and national policies on sustainability.<sup>69</sup>

Particular lessons could be learned from Chinese industrial parks that are not classified as EPZs, but which are zones focused on industrial development. Referred to as Eco-Industrial Parks, they have been designed since the early 2000s to be based on circular economy principles, so that the wastes of one firm can be the raw material input or energy source for another firm in the same zone.<sup>70</sup> China was not the first to develop these approaches, often called industrial ecology, or the circular economy, but China has taken the concept to a new level of scale and design and is showing what developing countries are able to achieve.<sup>71</sup> The survey presented in Section 3 above found only a few EPZs reporting that they sought to promote pro-competitive eco-efficiencies through enabling a circular economy between companies in an EPZ. This suggests a missed opportunity for many EPZs at this time.

Meanwhile, as part of their efforts at environmental management, many Chinese Eco-Industrial Parks have been aiming to achieve ISO 14001-certifications for entire parks.<sup>72</sup> There are three significant aspects to the Chinese approach. First, a government has made environmental management a founding principle for the design of an industrial zone or park, so as to design-out, or minimize as much as possible, waste from industrial processes at the start. Second, it is significant that the Chinese government has implicitly endorsed of the use of the ISO 14001 certification standard (an international management system standard) as an important part of their eco-park program. Third, the fact that the ISO 14001 certification applies to the park as a whole, thus providing some assurance to firms located in the park, as well as supply chain partners (such as MNEs) and others that an internationally recognized environmental management system standard is in place for activities undertaken by the park management.

A similar approach appears to have been implemented in Kenya. The Kenya Export Processing Zones Authority has committed to control its services and operational activities in order to minimize negative environment impacts and to comply with applicable environmental laws. To achieve these ends it aims to: set up and achieve environmental objectives and targets through monitoring, reporting and review; train staff; and adopt the environmental management system established by ISO 14001.<sup>73</sup>

This analysis of wider scholarship on EPZs and sustainable development suggests that there remain concerns about social and environmental performance in some zones. A lack of EPZ engagement on these issues, therefore, does not help to bolster the attractiveness of the zones to MNEs committed to CSR. However, the positive examples profiled here show that some zones are already making sustainability a central aspect of their strategies for international competitiveness and so more EPZs could learn from that experience to align economic development with national commitments to the SDGs.

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<sup>69</sup> OECD (2007) p. 29

<sup>70</sup> UNEP (2013)

<sup>71</sup> Geng and Doberstein (2008)

<sup>72</sup> Shi et al (2012)

<sup>73</sup> Kenya Export Processing Zone Authority website: [www.epzakenya.com](http://www.epzakenya.com)

## 4.2 Implications for policy and strategy

The changes to international trade rules and growing international business interest in CSR, mean that EPZ management agencies and investment promotion agencies have a need and opportunity to explore investment promotion strategies that relate to social, environmental and governance performance, rather than cheap labour, exemption from regulations or broadly-applied tax breaks.

Governments and local authorities typically understand that obligations on social and environmental issues that have been agreed at an international level shall continue to apply to all their territories without exemption, including within EPZs. Any regulatory exemptions for enhancing EPZ competitiveness should be restricted to matters not governed by international treaty nor affecting worker protection, the environment or ethical conduct. For instance, exemptions in areas such as percentage of foreign ownership of an enterprise could be considered but not exemptions on minimum wages or pollution levels.

Seeking exemptions to national regulations as a basis for competitiveness would be a misleading starting point if it means the potential of EPZs to promote good governance is overlooked. EPZs in developing countries are locations where there is a critical mass of government, employer, worker and civil society actors who can come together to innovate approaches that deliver for all stakeholders. A key characteristic of these miniature governance ecosystems is that they more readily enable consent amongst stakeholders. It has been suggested that “consent is the most effective form of governance.”<sup>74</sup> That is, there is the opportunity for parties to come together to voluntarily accept and construct the overall structure and operation of the regime in which they operate. Therefore, EPZ management agencies could play a key role in developing practices which are supported by all involved in the successful operation of companies in an EPZ, including the enabling of corporate sustainability.

Given the changing demands of MNEs and their suppliers, a ‘hassle free’ zone is not one that ignores basic labour rights or environmental standards, but is one that makes the achievement of such standards as simple and cost-effective as possible. Therefore, EPZ management agencies could develop new services for the cost effective implementation of actions to help firms meet international CSR standards, for instance by provision of relevant training, monitoring and improved infrastructure related to health, safety and waste management. EPZ management agencies and investment promotion agencies could also explore strategies to develop clusters of firms that can operate in a circular economy, using each other’s wastes and by-products as inputs, and thus achieving high eco-efficiencies.

In particular EPZs can learn from the past decade of experience in China where Eco-Industrial Parks have been developed to achieve greater circularity. As Accenture's Global Managing Director for Sustainability explains, “EPZ agencies have the opportunity to curate a circular economy among firms that operate in their zone. Firms can benefit from cost

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<sup>74</sup> Purchase (2004)

savings on waste, cheaper inputs, and a higher sustainability profile in markets that seek, and pay for, environmental quality.”<sup>75</sup>

The overall relevance of EPZs, and the rationale for governments to permit or enable them, depends on how they contribute to wider economic development in the host country. Therefore the promotion of that wider impact must be a key part of a sustainable EPZ agenda. There are a range of activities that EPZ management agencies could undertake to promote such positive impact. They could set standards for employers to provide support for staff training and development, so the workforce can progress into higher value work. They could provide information services for enabling more local sourcing and the sharing of knowledge with firms outside the EPZ. They could provide information to firms on the schemes for increasing their investments in CSR and related innovations, especially those that require more up-front investment, such as renewable energy systems.

On the basis of the analysis in this report, a simple ‘Framework for Sustainable Economic Zones’ is offered here, to guide initial consideration of EPZ standards, infrastructure assistance and administrative assistance to enhance performance on labour, environment, anti-corruption and health and safety (Figure 5). This framework is presented to provoke further discussion on what elements need to be in place to create true Sustainable Economic Zones. Further research is needed to assess the cost implications for EPZ agencies to provide the support described in the framework, and how the relative value delivered to companies in the zone will compensate for a reduction in fiscal or other incentives. Clearly some measures, such as provision of services to enable social auditing, will require less upfront investment from either a zone or a firm, than measures such as renewable energy generation or waste treatment. The Framework does not prioritise issues, but invites comprehensive attention and reporting on efforts towards sustainable zone management.

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<sup>75</sup> Peter Lacy, Global Managing Director, Accenture. Personal communication with Professor Jem Bendell, Cumbria University, June 2015.



**Figure 5. Framework for Sustainable Economic Zones**

Key elements for promoting sustainable EPZs

	Policies/Standards	Infrastructure assistance	Administrative assistance
<b>General Approach</b>	Create multi-stakeholder partnerships to identify opportunities and develop an action plan		
	Maintains and enforces policies and standards, including:	Provides services or specialists to insure compliance/offer assistance, including:	Provides guidance and training to companies, covering how to:
<b>Labour</b>	<ul style="list-style-type: none"> <li>• minimum wage</li> <li>• working hours and benefits</li> <li>• respecting right of unions to be active within the zone</li> <li>• gender equality and related issues</li> <li>• incentives for third-party certifications</li> </ul>	<ul style="list-style-type: none"> <li>• labour inspectors</li> <li>• conflict resolution specialists</li> <li>• reporting hotlines</li> <li>• gender focal points</li> </ul>	<ul style="list-style-type: none"> <li>• improve labour conditions</li> <li>• engage in social dialogue</li> </ul>
<b>Environment</b>	<ul style="list-style-type: none"> <li>• emissions</li> <li>• waste disposal</li> <li>• energy use</li> <li>• incentives for third-party certifications</li> <li>• promoting circular economy</li> </ul>	<ul style="list-style-type: none"> <li>• centralized effluent treatment</li> <li>• water reclamation systems</li> <li>• recycling services</li> <li>• hazardous waste management services</li> <li>• alternative energy sources</li> <li>• reporting hotlines</li> <li>• enabling circular economy</li> </ul>	<ul style="list-style-type: none"> <li>• further reduce natural resource use</li> <li>• reduce waste</li> <li>• increase recycling</li> <li>• improve energy efficiency</li> <li>• adopt renewable energy</li> </ul>
<b>Health &amp; Safety</b>	<ul style="list-style-type: none"> <li>• employee health and safety protection</li> <li>• incentives for third-party certifications</li> </ul>	<ul style="list-style-type: none"> <li>• medical clinic</li> <li>• fire brigade</li> <li>• reporting hotlines</li> </ul>	<ul style="list-style-type: none"> <li>• prevent health and safety emergencies</li> </ul>
<b>Corruption</b>	<ul style="list-style-type: none"> <li>• anti-corruption standards and policies</li> </ul>	<ul style="list-style-type: none"> <li>• hotlines</li> <li>• information on reporting corruption</li> </ul>	<ul style="list-style-type: none"> <li>• build capacity to detect and avoid corrupt business practices</li> </ul>
<b>Economic Linkages</b>	<ul style="list-style-type: none"> <li>• employer support for staff training and development</li> </ul>	<ul style="list-style-type: none"> <li>• assistance with local sourcing</li> </ul>	<ul style="list-style-type: none"> <li>• identify and upgrade local suppliers</li> </ul>

Source: UNCTAD

## 5. Conclusions

EPZs remain an important part of many countries' economic development strategies. However, their future competitiveness is in question, as the increasing application of international trade rules removes the possibility of attracting companies through tax breaks. In addition, serious questions remain about the utility of zones in promoting sustainable development in their host countries via economic linkages and other forms of positive engagement. Therefore, both new grounds for competitiveness need to be found and new means for zones to make contribution to their host countries. Some countries are responding to this challenge by considering relaxing the application of certain laws in EPZs. However, past research has demonstrated that those zones focused primarily on providing cost savings for firms, rather than a broader range of business success factors, often do not succeed in contributing to a host nation's sustainable development priorities. In addition, a process that splinters the application of national laws across territories could pose new political risks. This would also detract from the recent commitment of member states to the SDGs, which involve a renewed promise to ensure that industrialization, trade and investment align with broader social and environmental aims. Therefore, countries that are making zones central to their industrialization today need to develop a strategy that attracts firms that seek competitiveness on the basis of factors beyond low costs and tax breaks.

This report has identified the need for a 'role reversal' for EPZs: switching from a narrow focus on cost advantages and lower standards to become champions of sustainable business. The report has mapped out a strategy for the future competitiveness of EPZs that enable their contribution to the SDGs. That strategy is based on a recognition of the growth in commitment to CSR by multinational enterprises. Such enterprises, and their suppliers, seek reassurances that national laws are complied with and relevant international standards are met. The proposed strategy involves EPZ management agencies seeking to leverage their governance capabilities to enable the efficient and cost-effective performance of firms on social, environmental and ethical issues. The review of research on EPZs, as well as the UNCTAD survey of 100 EPZs, found a number of examples where EPZs are making social and environmental excellence part of their investment promotion strategies. From China to Uruguay, some zones are already demonstrating this strategy can work.

However, it appears that most EPZ management agencies are not prepared for this new competitive context. The review of existing studies on the social and environmental performance of EPZs showed that current performance is varied, with concerns raised about social, environmental and ethical performance. Therefore a strategic leap is required, to move beyond first generation EPZs and pursue 'Sustainable Economic Zones'.

This paper recommends that policy makers and EPZ owners and operators adopt the 'Framework for Sustainable Economic Zones' as a starting point for thinking about how enhanced sustainability services can strengthen their ability to attract investment. Such rethinking about the competitive role of EPZs could usefully take place within the broader context of UNCTAD's Investment Policy Framework for Sustainable Development.<sup>76</sup>

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<sup>76</sup> UNCTAD (2012c)



The potential for EPZs to contribute to the new 'Global Goals' is not only through achieving higher standards of social and environmental performance themselves, but also in demonstrating what is possible to the rest of a country. Therefore, while supporting leadership by EPZs on social and environmental performance, national governments can reiterate their commitment to, and develop strategies for, the achievement of regulatory compliance and sustainable development across all their territories. The destination must not be a two-tier economy with differing standards, but a positive contribution of zones to the wider progress of their host countries.

## 5.1 Next steps

To help EPZs consider, adopt, apply and promote their efforts in line with the Framework for Sustainable Economic Zones, other stakeholders have a role to play. Below are suggested next steps for stakeholders to help EPZs enhance their approach to sustainable development:

- (1) **International environmental, social and trade and investment bodies** such as the ILO, UNCTAD, UNEP, WHO and standards/certification bodies such as the Fair Labour Association, the International Organization for Standardization (ISO), and SA 8000 could increase their outreach to EPZs. Resultant partnerships could enhance the ability of the participating EPZs (and firms operating within those EPZ) to consistently behave in a socially responsible manner by tapping into expertise and resources external to the EPZ.
- (2) **Organizations involved in CSR standards** could develop specialised international certification standards and associated implementation regimes tailored to apply to EPZs meeting good environmental and social practices. Such specialized international certification standards and implementation regimes could address the social and environmental attributes of particular geographically limited areas, and the associated governance and accountability regime for these areas. Such specialized EPZ standards/certification regimes may offer economies of scale in terms of approaches to implementation, infrastructure and administrative services not available to individual firms operating independently, so that by grouping together they would reduce the shared overall operating costs within a zone.
- (3) **National, regional and global associations of EPZs** should encourage more information sharing between EPZs on the means for developing competitive advantage through excellence in corporate sustainability. Such associations could promote the adoption of environmental and social principles and standards by their members. Membership of associations could become contingent upon meeting agreed upon environmental and social standards, and on reporting compliance with the standards. The grouping together of such EPZs would allow for "brand differentiation" and competitive advantage for those EPZs meeting high environmental and social standards, and would make it easier for CSR-oriented MNEs to identify "good actors" to partner with in terms of where they would want their supply chain partners to be located.
- (4) **Funders of research** could support independent studies on the social, environmental and corporate governance implications of changing EPZ strategies in response to new trade agreements, to further inform EPZ management and governance, as well as future policies on international investment and trade. This research could also re-examine the

overall contribution of zones to the development of their host countries in the new trade-law context. A useful next step might be a conference bringing together relevant stakeholders to explore options such as those described in this report.

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## Appendix A: Survey methodology

### Sample

In order to evaluate the infrastructure and services currently being promoted by Export Processing Zones a survey of the public information of 100 different EPZs was conducted. As there is no readily available list of EPZs, it was necessary to generate a sample of EPZs to be studied. This study focused on emerging market economies from within the G20, as well as a variety of countries chosen on the basis of available information, geographic diversity and the importance of EPZs as a national policy tool, specifically:

- Argentina
- Bangladesh
- Brazil
- China
- Costa Rica
- El Salvador
- India
- Indonesia
- Jordan
- Mexico
- Morocco
- Namibia
- Panama
- Philipians
- Saudi Arabia
- South Africa
- South Korea
- Sri Lanka
- Turkey
- United Arab Emirates
- Uruguay

### Process

A list of approximately ten EPZs per country was generated, although some economies have fewer EPZs, for a complete list of EPZs studied, see Appendix B. This paper uses the International Labour Organization definition for an EPZ, namely: “industrial zones with special incentives set up to attract foreign investors, in which imported materials undergo some degree of processing before being (re-) exported again”.<sup>77</sup> Websites of EPZs were surveyed and an analysis of the infrastructure and services offered as well as stated policies was conducted. A structured survey was conducted with a total of 63 questions, ranging from services related to customs to the presence of a medical clinic. For a complete list, see Appendix C.

### Limitations

- *Limited public information.* One challenge with this method is a lack of public information on EPZ internet pages. To mitigate this, the research team directly contacted EPZs in the study to receive additional information as necessary. Following an analysis of the EPZ list, research was broadened to search for best practices in sustainability of EPZs.
- *Public information versus actual practice.* The report is based on publicly available information, so some initiatives on CSR and sustainability may have been overlooked. Moreover, while the study of public information cannot determine with certainty whether or not specific services exist in the zones, the study does provide an accurate indication of what EPZs publicly promote or talk about having in their zones.
- *Limited sample size.* This survey is necessarily exploratory rather than conclusive. The growth of EPZs to well over 4,000, means that this report is based on a comparatively small sample of 100 EPZs.

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<sup>77</sup> ILO (2003)

## Appendix B: List of EPZs studied

Argentina EPZ 1: La Plata  
Argentina EPZ 2: San Luis  
Argentina EPZ 3: Tucuman  
Argentina EPZ 4: Cordoba  
Argentina EPZ 5: Mendoza  
Argentina EPZ 6: General Pico  
Argentina EPZ 7: Comodoro Rivadavia  
Argentina EPZ 8: Salta  
Argentina EPZ 9: Puerto Iguazu  
Bangladesh EPZ 1: Adamjee  
Bangladesh EPZ 2: Dhaka  
Bangladesh EPZ 3: Mongla  
Bangladesh EPZ 4: Ishwardi  
Bangladesh EPZ 5: Comilla  
Bangladesh EPZ 6: Uttara  
Bangladesh EPZ 7: Chittagong  
Bangladesh EPZ 8: Karnaphuli  
Brazil EPZ 1: Teofilo Otoni  
Brazil EPZ 2: Parnaiba  
China EPZ 1: Changschu Export Processing Zone  
China EPZ 2: Baoding High-tech Industrial Development Zone  
China EPZ 3: Tianjin Port Free Trade Zone  
China EPZ 4: Qingdao Export Processing Zone  
China EPZ 5: Shanghai Integrated Free Trade Zone  
China EPZ 6: Qinhuangdao Export Processing Zone  
China EPZ 7: Hangzhou Export Processing Zone  
China EPZ 8: Kunshan Free Trade Zone  
China EPZ 9: Lianyungang Export Processing Zone  
China EPZ 10: Wuxi  
Costa Rica EPZ 1: Zona Franca del Este  
Costa Rica EPZ 2: Global Park Free Zone  
Costa Rica EPZ 3: Metro Free Zone  
El Salvador EPZ 1: International Free Zone  
India EPZ 1: Adani Port SEZ (Mundra)  
India EPZ 2: Kandla SEZ  
India EPZ 3: Andhra Pradesh Special Economic Zone  
India EPZ 4: Cochin Special Economic  
India EPZ 5: Maharashtra Industrial Development Corporation Ltd, (4 zones total: Mumbai, Pune, Nagpur, Nanded)  
India EPZ 6: Madras Export Processing Zone  
India EPZ 7: Falta Special Economic Zone  
India EPZ 8: Visakhapatnam SEZ  
India EPZ 9: Seepz Special Economic Zone  
Indonesia EPZ 1: Batam FTZ  
Indonesia EPZ 2: Bintan FTZ  
Indonesia EPZ 3: Karimun FTZ  
Indonesia EPZ 4: PT. Kawasan Berikat Nusantara (Persero)  
Jordan EPZ 1: Aqaba Special Economic Zone  
Mexico EPZ 1: Puerto Devera Cruz:  
Morocco EPZ 1: Tanger Free Zone  
Namibia EPZ 1: Walvis Bay  
Panama EPZ 1: Colon Free Trade Zone  
Philippines EPZ 1: Mactan I  
Philippines EPZ 2: Mactan II  
Philippines EPZ 3: Free Port Area of Bataan (SEZ)  
Philippines EPZ 4: Cavite  
Saudi Arabia EPZ 1: King Abdullah Economic City

Saudi Arabia EPZ 2: Prince Abdulaziz Bin Mousaed (PABMEC)  
South Africa EPZ 1: Coega Industrial Development Zone (Port Elizabeth)  
South Africa EPZ 2: East London (ELIDZ)  
South Africa EPZ 3: Richards Bay Industrial Dvlpt Zone Company  
South Korea, EPZ 1: IFEZ, Incheon Free Economic Zone  
South Korea, EPZ 2: SGFEZ, Saemangeum (Gunsan FTZ)  
South Korea EPZ 3: BJFEZ, Busan-Jinhae  
South Korea EPZ 4: GFEZ, Gwangyang Bay Area FEZ  
South Korea EPZ 5: Yellow Sea Free Economic Zone  
South Korea EPZ 6: DGFEZ, Daegu-Gyeongbuk FEZ Authority  
South Korea EPZ 7: Daebul Free Trade Zone  
South Korea EPZ 8: Gunsan Free TRade Zone  
South Korea EPZ 9: Masan FTZ  
South Korea EPZ 10: Donghae FTZ  
Sri Lanka EPZ 1: Katunayake  
Sri Lanka EPZ 2: Biyagama  
Sri Lanka EPZ 3: Koggala  
Sri Lanka EPZ 4: Mawathagama  
Sri Lanka EPZ 5: Polgahawela  
Sri Lanka EPZ 6: Mirigama  
Sri Lanka EPZ 7: Horana  
Sri Lanka EPZ 8: Seethawaka  
Sri Lanka EPZ 9: Kandy  
Sri Lanka EPZ 10: Malwatta  
Sri Lanka EPZ 11: Wathupitiwela  
Turkey EPZ 1: Antalya Free Zone  
Turkey EPZ 2: MESABAS, Mersin Free Zone Operator Inc.  
Turkey EPZ 3: ESBAS Aegean Free Trade Zone  
Turkey EPZ 4: Trabzon Free Zone  
Turkey EPZ 5: Gaziantep / Gasbas  
Turkey EPZ 6: İstanbul Thrace Free Zone  
Turkey EPZ 7: Izmir Menemen Leather Free Trade Zone  
Turkey EPZ 8: DENSER - Denizli  
Turkey EPZ 9: Toros Adana Yumurtalık Free, TAYSEB  
Turkey EPZ 10: Kayser / Kaiser  
United Arab Emirates EPZ 1: Jebel Ali Free Zone  
United Arab Emirates EPZ 2: Sharjah Airport Int'l Free Zone  
Uruguay EPZ 1: Zona America  
Uruguay EPZ 2: Zona Franca de Colonia (Grupo Continental S.A.)  
Uruguay EPZ 3: Zona Franca Colonia Suiza  
Uruguay EPZ 4: Zona Franca Floridasur (Florida S.A.)  
Uruguay EPZ 5: Zona Franca Libertad (Lideral S.A.)  
Uruguay EPZ 6: WTC Free Zone  
Uruguay EPZ 7: Parque de las Ciencias



## Appendix C: List of survey questions

### **A. General questions about EPZ**

- 1 Number of companies
- 2 Number of workers
- 3 Trade volume (US\$ per year, latest figures)
- 4 Industries represented in EPZ

### **B. Traditional business services offered by EPZ**

- 5 Customs assistance
  - 5.1 Government provides customs service
  - 5.2 Private Sector provides customs service
  - 5.3 Unclear who provided
- 6 Business license issues
  - 6.1 Government provides business license service
  - 6.2 Private Sector provides business license service
  - 6.3 Unclear who provided
- 7 Tax services
  - 7.1 Government provides Tax service
  - 7.2 Private Sector provides tax service
  - 7.3 Unclear who provided
- 8 Provides ITC infrastructure (internet / phone)

### **C. Sustainability related services**

#### Corruption related services / issues

- 9 Assistance in dealing with corruption
  - 9.1 Government provides assistance with corruption
  - 9.2 Private Sector provides assistance with corruption
  - 9.3 Unclear who provided

#### Labour related services / issues

- 10 Labour inspectors
  - 10.1 Government provides labour inspectors
  - 10.2 Private Sector provides labour inspectors
  - 10.3 Unclear who provided
- 11 Does the EPZ have any public policy on labour issues?
- 12 Is there evidence of unionized labour within the EPZ?
- 13 Is the minimum wage in the EPZ different from national min wage?
  - 13.1 Greater
  - 13.2 Less than

#### Environmental, health and safety related services / issues

- 14 Environmental inspections
  - 14.1 Government provides environmental inspectors
  - 14.2 Private Sector provides environmental inspectors
  - 14.3 Unclear who provided
- 15 Does EPZ have any public policy on environment?
  - 15.1 On climate change?
  - 15.2 On energy efficiency?
  - 15.3 On recycling?
  - 15.4 On hazardous waste management?
- 16 Is there any evidence of environmental services provided through EPZ?

- 16.1 Recycling services
- 16.2 Alternative energy services
- 16.3 Hazardous waste management services

- 17 Firefighting services
- 18 Medical services (e.g. clinic, hospital)

***D. Reporting requirements for firms within EPZ***

20 Required to report sustainability standards at point of application?

- 20.1 Land pollutants
- 20.2 Air pollutants
- 20.3 Water pollutants

21 Required to report sustainability standards on an annual basis?

- 21.1 Land pollutants
- 21.2 Air pollutants
- 21.3 Water pollutants