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**THE FREE ZONES AND THE CASE OF FREE ZONE
IN TRNC**

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ABSTRACT

All the countries aim at developing their international trade with a scope of increasing the foreign currency revenues. In order to reach this objective the states need to create an environment of local and foreign investment under liberal economic conditions to enhance export oriented development. Free zones and ports are designated areas within the national boundaries of a country which are considered to be outside the local system where special investment incentives, lower tax rates, and free of any entry or exit barriers. Investors enjoy relaxed regulations, incentives and lower costs and hence freely operate their production or service units in these designated areas. Free zones are in existence for many centuries and has especially developed since after 1980s when the liberalization movement started all over the world.

Famagusta Free Zone was established soon after the liberalization of the Turkish Cypriots from many years of suppression under the Greek dominance.

1. Introduction

States are in a continuing competition all the time. The reason for competing is to obtain political and economic superiority. Foundation of political or any other superiority is the economic strength. Such as a man needs money to obtain their needs, and those who have more money can do this better, the states also need adequate reserves to accomplish their objectives. Currency earning activities is very important for a healthy economy. There are a few instruments that can create currency earning, these are: exports, tourism revenues, and foreign investments. Free ports and zones are especially designated areas that provide especial advantages to the investors to enable them to operate their export oriented businesses. Especial rules and regulations in the free zones reduce the costs and bureaucracy. Free Zones are defined as special sites within the country but deemed to be outside of the customs border and they are the regions where the valid regulations related to foreign trade and other financial and economic areas are not applicable, are partly applicable or new regulations are tested in. Free Zones are also the regions where more convenient business climate is offered in order to increase trade volume and export for some industrial and commercial activities as compared to the other parts of country. (Bağrıaçık, 2002, pp.1)

Free Ports are harbors in which the vessels of all nations may enter and load or unload without payment of import duty. Charges are made for harbor services only. Goods unloaded may be reshipped elsewhere on payment of a transit duty or may be admitted to that country for consumption upon payment of import duty. More common than the free port is the free zone maintained in many ports. New York City port has a free zone on Staten Island in New York Bay. Rotterdam and Singapore are other famous free ports. Mersin port also have free

port facilities and free zone attachment. A similar arrangement is also present in TRNC.

The basic objective of the free zones is to attract foreign investment and increase the currency earnings. The Turkish law 3218 sets the objectives of the free ports as "attract increasing amounts of foreign investment and currency earning". The free ports, to reach these objectives, allow free movements in and out of the zone with minimal entry and exit barriers. (Alacaklıoğlu, 1998, pp.1)

When the free zones function according to the aims and objectives the host country flourish with higher GDP per capita and higher employment rates. Since the input costs are lower in the free zones the host country is likely to end up with lower priced goods and services.

The following study will be a study of the free ports and zones. The study will be under three main section. The first part will be about the general concept of free zones and its application in Turkey. The second part will focus on the free zone activities in the Gazi Magusa of TRNC. The final part of the study will be the conclusion and the recommendations.

2. Free Zone Concept

Free Zones are defined as special regions within the country that are deemed to be outside of the customs border and where the valid regulations related to foreign trade and other financial and economic areas are either not applicable, are partly applicable or in which new regulations are tested. Free Zones are also the regions where a more convenient business climate is provided in order to increase trade volume and export for certain industrial and commercial activities as compared to other parts of country. (DTM, 2002, pp2)

Free Zones Law numbered 3218 was issued in 1985 with the objective of increasing export-oriented investment and production in Turkey, accelerating the entry of foreign capital and technology, procuring inputs into the economy in an economic and orderly fashion and increasing the utilization of external finance and trade possibilities.

Free Zones Law No. 3218 was put into effect in 1985 and since then the Mersin and Antalya Free Zones became operational in 1988, the Aegean and Istanbul Ataturk Airport Free Zones in 1990, the Trabzon Free Zone in 1992, the Istanbul-Leather Free Zone in 1995 and commercial activities have been conducted in the Mardin and Eastern Anatolian Free Zones since October, 1995. (Toroslu, 2000, p.3)

On the other hand, a new implementation, the Istanbul International Stock Exchange Free Zone which is expected to commence its activities in the second half of 1996 and whose main objective is to create an international finance center, will operate in the field of stock purchasing-selling, stock barter, maintenance and in the field of other transactions within the body of Istanbul Stock Exchange, one of the most intensive stock exchange in this region of

the world that foreigners carry out their transactions when it become operational.

The 15th International Conference of Free Zones and Export Processing Zones and the 8th General Assembly Meeting was held between October 8 and 11, 1995 in Rio de Janeiro, Brazil by the World Export Processing Zones Association (WEPZA) which the General Directorate of Free Zones (Undersecretariat for Foreign Trade) has been a member since 1991. During the 8th General Assembly Meeting, held with the participation of 32 countries, Turkey's representative, the Director of the General Directorate of Free Zones was elected unanimously by the members of the General Assembly for 4 years to the membership of the WEPZA Council, which is the highest body of WEPZA. (Turgay, 2003, p.21)

Moreover, it was decided that the 17th International Conference of Free Zones and Export Processing Zones and the 9th General Assembly were to be held in Istanbul, Turkey in 1997.

In addition, the General Directorate of Free Zones assists at project and technical levels in studies on the establishment of free zones in the country's region and provides the necessary documentation for their legal arrangements.

Turkish Free Zones, as far as their legislation, infrastructure and volume of trade are concerned, provide a good example in our region. In this context, technical and project assistance have been given to the countries in the region to help to establish their free zones. A joint protocol was signed between the Turkish and Georgian Governments on October 31, 1995 in Tbilisi to carry out technical and feasibility studies to establish the Georgian Free Zones and also to prepare the required legislation for this purpose.

2.1 Definition and objectives of the Free Zones

The free trade zones are defined as special areas and considered as the parts of the customs territory of Turkey where the goods not being in the free-circulation are placed not subject to the customs formalities and not in the release for free circulation provided that they are not used or consumed in the circumstances prescribed in the customs legislation; however, are deemed not being on the Turkish customs territory in respect of import duties and commercial policy measures and exchange policy; are the premises in which the goods released for free circulation are placed to benefit from the normal export procedure (Alacaklıoğlu, 1998, pp.1-3).

Free Zones are also regions offering a more convenient business climate in order to increase trade volume and exports for certain industrial and commercial activities, in contrast to the remainder of the country. In general, all types of activity may be performed in Turkish Free Zones, such as manufacturing, storing, packing, general trading, banking and insurance. Investors are free to construct their own premises, although these zones also possess available office space, workshops, or warehouses available on a rental basis with attractive terms. All fields of activity open to the Turkish private sector are also open to foreign joint ventures. Private companies also operate free zones in Turkey.

With the objective of increasing export-oriented investment and production in Turkey, accelerating the entry of foreign capital and technology, procuring the inputs of the economy in an economic and orderly fashion and increasing the utilization of external finance and trade possibilities, Free Zones Law numbered 3218 was issued in 1985. Since then Mersin (1987), Antalya (1987), Aegean (1990), İstanbul Atatürk Airport Free Zones (1990), Trabzon (1992), İstanbul Leather and Industry (1995), Mardin (1995), Eastern Anatolia (1995), İstanbul

International Stock Exchange (1997), İzmir Menemen-Leather (1998), Rize (1998), Samsun (1998), İstanbul Thrace (Çatalca) (1998), Adana-Yumurtalik (1998), Kayseri (1998), Europe (1999), Gaziantep (1999) Free Zones became operational. İstanbul International Stock Exchange Free Zone's main objective is to make İstanbul an international finance center where underwriting-trading, stock barter activities are carried out in a tax-free environment.

In general all kind of activities can be performed in Turkish Free Zones such as manufacturing, storing, packing, general trading, banking and insurance. Investors are free to construct their own premises, while zones have also available office spaces, workshops, or warehouses on rental basis with attractive terms. All fields of activities open to Turkish private sector are also open to joint-ventures and foreign companies.

Turkey has realized Customs Union with EU countries on January 1, 1996 and Free Zones are one of the topics to be harmonized during the Customs Union Period. During the negotiations with EU officials it was observed that although the legislation unity was provided in order to minimize the implementation differences, the full harmonization has not yet been achieved in the Community Free Zone Implementations. There are still some differences in Community Implementations and uniformity of these differences could not be realized in a short term and the Community has to take into consideration the free zone legislation of member states which were put into force according to their National Laws before the full membership. Within this context as a result of Community Officials' evaluations on the Turkish Free Zones Legislation, it was observed that both legislation are substantially similar, so Turkey does not need a new legal arrangement on this subject and the current situation can be carried on during the Customs Union period.

Turkish Free Zones as far as their legislation, infrastructure and volume of trade are concerned, constitutes a good example in our region. In this context, technical and consultancy assistance have been given to the countries in the region especially to the CIS countries to help to establish their free zones. Moreover, the 17th International Conference of World Export Processing Zones' Association (WEPZA) - a non-profit international organization set up under the auspices of UNIDO and which has 50 members in 40 countries was realized in Istanbul, on October 5-8, 1997 under the theme "The Global Network of Free Zones In the 21st Century". This organization indicates that Turkish Free Zones are considered among the most successful free zones in the world.

There are various different applications regarding the free zones and these are named in alternative ways as follows (Koçver, 2001, p.12)

- free zone
- free port
- customs free zone
- export processing zone
- free economic zone
- free production zone
- free trade zone
- industrial free zone
- maquiladora
- special economic zone
- tax free trade zone
- customs free airport.

Today there are around 850 free zones operating in 105 countries including the USA, Mexico, Brasil, Argentina, Germany, England,

Spain, Bulgaria, Romania, India, China, South Korea, Indonesia, Iran, and Urdun (Koçver, 2001, p.23).

The free zones are not limited to the developing countries. The developed countries also use the free zones as an economic concept. Some use free zones just for the customs purposes. The host country has no influence on the free zones. Developed countries such as the USA and Germany are using the free zones for their advantages. Likewise the developing countries such as Korea and China are making use of free zones in very similar manner. Basic objectives of the free zones are summarized as follows.

- to increase the foreign trade and investment
- to empower the local producers to obtain inputs at competitive prices from the foreign markets.
- To support and give incentives to the export oriented organizations
- To increase the currency earnings.
- To increase employment
- To attract latest technologies in management and productions.

2.2 Advantages of the Free Zones

In the free zones, the regulation provisions regarding the tax, dues, toll, customs and foreign exchange obligations are not applied. The firms are exempted from all income, institutional and value added taxes regarding the income they obtain from their activities at the zone.

Also, the price of workmanship is low, since no income taxes are paid for the salary of the workers. The validity period of an operating license is maximum 10 years for tenant users, and 20 years for users who wish to build their own working spaces in the zone; If the

operating license is for production, these terms are 15 and 30 years for tenant users and investors, respectively (Bağrıaçık, 1999, p.2).

The incomes and revenues obtained from the activities at the free zone can be transferred abroad or to Turkey without being subject to any kind of tax or permission. Even if the income and revenues obtained by the full and limited real and juridical persons in Turkey obtained from the activities at the free zone are brought to Turkey in accordance with the foreign currency regulations, they will be exempted from income and institutional taxation.

There is no limitation on the proportion of foreign capital participation in investment within the Free Zones. In contrast to most Free Zones in the world, sales into the domestic market are allowed. Trade conducted between Turkish Free Zones and Turkey is subject to foreign trade regime. (Sales to the domestic market are subject to a fee of 0.5 % of the transaction value.) (Bağrıaçık, 1999, p.3)

Since the status of free circulation of the Turkish or EU origin goods or goods at free circulation in these countries brought to the free zone have not changed, no customs taxes are to be paid during the entrance of these goods to Turkey or during the entrance of the third country origin goods to the free zone or during the delivery of these goods to third countries apart from Turkey or the EU member countries. However, for the third country origin goods which are not in free circulation and which are sent to Turkey or the countries of the EU from the free zone, customs taxes are paid from the rates designated by the common Customs tariff.

Since the free zones are accepted to be within the "Turkey - EU Customs Union Customs Region", the Turkish and EU - origin goods and the goods in a state of free circulation in Turkey can be sent to the countries of the EU from the free zones by preparing a A - TR document.

The firms carrying out activities at the free zone can benefit from the investment incentive designated by the Council of Ministers at the investment and production phases.

All native and foreign firms benefit equally from the incentives and advantages provided at the free zone. The goods can stay at the free zone without any time limitations.

After a free zone becomes active, strikes and lock - outs cannot be applied for a period of 10 years. The Supreme Arbitration Council shall resolve any disputes occurring within the context of collective bargaining during this period. The authorities delivered to the state foundations and institutions regarding the prices, quality and standards are not applied at the free zones.

All kinds of payments regarding the activities carried out at the free zone are made in foreign currencies.

No restrictions have been imparted on the sale of commodities (import) towards Turkey from the free zones and on the trade in the form of exchange of goods to be made between the free zone and the other countries.

An activity license up to a period of 99 years can be granted. During the period of application and activity, the bureaucratic transactions have been minimized. The private sector companies operate the free zones. At the free zones, the provisions of the Municipality Law numbered 1580 (excluding paragraph 5, 22, 25, 32 and 47 of Article 15), the Passport Law numbered 5682, Law 5683 regarding the residing and traveling of foreigners in Turkey, Law 2007 regarding the arts and services assigned for the Turkish Citizens in Turkey and the annexes and modifications, Law 2677 regarding the execution of the duties and services at the airports, seaports and border gates, the General Accountancy Law numbered 1050, the Audit Court (Office) Law numbered 832, the State Tender Law numbered 2886 and

the other laws which are contrary to the Free Zones Law are not applied. (Bağrıaçık, 1999, p.2)

The free zones are established at locations near the EU and the Middle East markets, which are also near to the major seaports at the Mediterranean, Aegean and the Black Seas, to the international airports, to the highway networks and to the culture, tourism and entertainment centers.

The infrastructures of the free zones are at the same standards with similar zones of the developed countries. The rentals for the open and closed areas are lower than those of the other countries.

The firms carrying out activities at the free zone are exempted from all taxation including income tax, institutional tax, value added tax and the property tax and from all the dues and tolls valid in Turkey. However, the transactions to be carried out by these firms in Turkey and the purchasing of goods without being subject to foreign trade regulations, are subject to dues and tolls in accordance with the other regulations regarding VAT. In a more general expression, the incentives and exemptions provided by the Free Zones Law numbered 3218 are only valid within the boundaries of the free zone but there is a possibility of enlarging these boundaries for the transactions carried out outside the boundaries of the free zone concerning the free zone activities.

In the Turkish Free Zones, Municipality Law, Passport Law, Foreign Investment Law, Foreign Investment and Encouragement Law, and all other articles of laws contrary to the provisions of the Free Zones Law, shall not be applicable.

Free zones are attraction points for foreign direct investment. One sixth of the total free zone companies in Turkey is made by the foreign investors. In other words the foreign investment made in the free zones of Turkey is in the excess of 500 million dollars. The

portion of foreign investment in Turkish free zones in money terms is 30 percent.

The success of the free zones in attracting foreign investment is due to incentives and tax exemptions. Following are some of the incentives used in the free zones of Turkey (Seçen, 2001, p.34)

- In contrast to most Free Zones worldwide, sales to the domestic market are allowed in Turkish Free Zones.
- Free Zones are exempted from all kinds of taxes including income, corporate, payroll and value-added tax.
- The existing industrial settlement in the various regions offers a large pool of qualified employees. Since companies located in the zone do not pay taxes, they benefit from a reduction of between 25% to 35% in labour related costs.
- For a period of 10 years following the commencement of operations in these zones, strikes and lockouts shall not occur.
- Energy costs are 30% lower due to tax advantages.
- Free Zone earnings and revenues may be freely transferred to any country, including Turkey, without prior permission, and are not subject to any taxes, duties or fees.
- There is no limitation on the proportion of foreign capital participation in investment within Turkey's Free Zones.
- Foreign investors can obtain an operating licence without setting up a new company in Turkey.
- There is no limitation on stocking periods.
- Infrastructure of the Turkish Free Zones meets international standards. Turkish Free Zones are adjacent to major Turkish Ports on the Mediterranean, Aegean and Black Seas. In addition, they were established within easy access to international airports and highways.

- Red tape and bureaucracy have been minimized during application and operational phases by authorizing only one agency to oversee these procedures.
- As transactions within the zone are performed with convertible foreign currencies, the domestic inflation rate will not influence purchasing and selling activities and accounting procedures in general.
- The validity period of an operation license is a maximum of 10 years for tenant users, and 20 years for users wishing to establish their own offices in the zone. Where the operating license is issued for production, the terms are 15 and 30 years for tenant users and investors, respectively. The requested operation license period may be prolonged to 99 years.
- The status of the free zones provides the exclusivity and security of title-deed ownership in investment.
- In Turkish Free Zones, Municipality Law, Passport Law, Foreign Investment Law, and all other articles of law contrary to the provisions of the Free Zones Law, do not apply.

2.3 The negative Impact of the Free Zones on the Economy

Since the goods can be imported with no customs duty to the free ports, the importers will prefer to use the benefits of the free zones instead of importing to the inland. This will lead in revenue losses to the state (Toroslu, 2000, s.67)

Since the multinational companies will prefer lower cost inputs they are likely to import most of their inputs from the third countries. This means that as the export from the free zones will increase so will the imports from the third countries.

The multinational companies and foreign investors in the free zones will become competitors of the local producers. Therefore

importers of the foreign countries will import from the free zone companies rather than the local companies. This will mean business loss for the local companies.

As part of the incentives to the foreign investors in the free zones there are restrictions on the labor movements. Strikes are usually forbidden in the free zones. This leads to ill-treatment against the employees. Most of the organizations in the free zones are likely to exploit the human resources.

One important danger of the free zones is the possibility of smuggling goods from the free zone to the local markets. Unless carefully controlled the goods imported to the free zone without any duty or tax may be sold in the local markets. This will create revenue cost to the state as well creating unfair competition to the local importers.

2.4 Economic Benefit of the Free Zones

- Companies that produce goods with imported inputs will be able to import low price inputs from anywhere in the world.
- Incentives and easiness of formalities will increase the exports and currency earnings
- Since the goods will be imported in big quantities there will be lower costs. The free zones can be used for bulk import and transfer of the imports to the local markets as smaller quantities.
- There will be more jobs and increased welfare to the surrounding communities.
- The firms in the free zones will first look for inputs at the nearest places to them. This will mean more business to the surrounding local businesses.
- Transfer of new technologies by the big foreign investors

- The free zones can be used as test areas for new economic policies.

In order to see the economic benefits of the free zones we only need to look at the developments in Turkey. Since passage of the Turkish law on free zones in 1985, ten zones have commenced operations and another three are under preparation. The zones are open to a wide range of activity, including manufacturing, storage, packaging, trading, banking and insurance. Foreign products enter and leave the free zones without payment of any customs or other duties. Activities in the zones are exempt from taxation, quota restrictions, licensing and standardization regulations. Revenues generated in the zones are also exempt from income taxes. On the other hand, goods and revenues transported from the zones into Turkey are subject to all relevant import regulations.

The trade volume of Turkey's free zones in 1997 was USD 5.5 billion, or about 7.5 percent of Turkey's total trade volume. There are no restrictions on foreign firms operations in the free zones.

According to treasury data, as of April, 1998, 4,135 foreign firms had invested and were operating in Turkey. Total authorized capital was USD 22.6 billion and aggregate actual inflows reached USD 10.7 billion from 1980 through 1997. EU countries accounted for 67.4 percent of cumulative foreign investment, OECD countries accounted for 91.4 percent and Islamic countries for 4.7 percent. France (18.5 percent) is the top source of foreign investment, followed by the U.S. (14.7 percent), Germany (12.4 percent), and the Netherlands (12.3 percent). Note that, because of the absence of a bilateral tax treaty until 1998, much U.S.-origin capital has been invested in Turkey through third-country subsidiaries. By unofficial

estimates the U.S. is actually the largest source of foreign investment in Turkey.

In 1997, about 56.8 percent of foreign investment was in manufacturing, 40.5 percent in services, 1.6 percent in agriculture and 1.1 percent in mining. Of the foregoing, some of the larger sub-sectors include banking (15 percent), vehicle production (9 percent), food processing (8 percent), financial services (7 percent), tobacco products (4 percent), hotel services (4 percent), and chemicals (4 percent).

Turkey's largest foreign investors include Renault, Toyota, Fiat, Castrol, Enron Power, Citibank, Pirelli Tire, Unilever, RJR Nabisco, Philip Morris, FMC, Honda, Hyundai, Bosch, Siemens, Mercedes, Chase Manhattan, AEG, Bridgestone, Cargill, Ciba-Geigy, Coca Cola, Colgate-Palmolive, General Electric, General Motors, ITT, Ford Motor Co., Lockheed, Gillette, Goodyear, Hilton International, Hoechst, McDonald's, Nestle, Mobil, Pepsi, Pfizer, Procter and Gamble, and Shell.

Currently, there are 951 firms in the Turkish Free Zones of which 178 are foreign and 773 are local. These zones employ approximately 6000 personnel.

When the breakdown of volume of trade by countries as of the end 1995 is evaluated, it is seen that the volume of trade realized with EU countries was 15 percent, with the other OECD countries 6 percent, with the other European countries 2 percent, with CIS countries 13 percent, with the Middle East Countries 4 percent, with the other countries 1 percent and with Turkey 50 percent.

In 1995, free zones exports to Turkey reached \$545.5 million US which constitutes 21 percent of the free zones' total volume of trade. On the other hand, free zones imports from Turkey was \$969 million US, representing 34 percent of the free zones' total volume of trade.

As of the end of 1995 industrial products constituted 74%, agricultural and livestock products 23% and mining products 3% of free zones' trade volume.

When the sectoral breakdown of volume of trade is studied, industrial products are seen to be made up of textiles and garment products with \$884 million US, machinery industry products with \$227 million US, motor vehicles with \$201 million US, electric-electronic and optical products with \$192 million US, chemical products with \$184 million US respectively. (DTM, 2003, p.42)

In general, a great variety of activities can be performed in Turkish Free Zones such as manufacturing, storing, packing, general trading, banking and insurance. Investors are free to construct their own premises, while zones also have available office spaces, workshops, or warehouses on a rental basis at attractive terms. All fields of activities open to the Turkish private sector are also open to joint-venture or foreign companies.

2.5 Types of Free Zones

Different countries have different expectations from the free zones. The free zones are not exactly the same around the globe, there are variations. The main types of the free zones are summarized below (Toroslu, 2000, pp.7-10):

2.5.1 Free Trade Zone

Free trade zones are usually designated areas within or near a sea port. There are limited permissions in this area to stock goods, assemble and prepare for export. A simple description is that the free

trade zones are facilitation of re-export and transit trade. There are no industrial activity in such places.

2.5.2 Free Production Zones

Unlike the free trade zones the free production zones are facilities for production purposes. Production and assembly facilities are provided for export oriented firms. Electronics and clothing are main users of the Free Production Zones.

2.5.3 Free Ports

Any one port of a country can be organized to provide services as free port. Free ports are useful for re-exporting purposes. Free trade is also possible within the free ports.

2.5.4 Enterprise Zones

Enterprise zones are designed to attract investments in regions which are not well developed and lack behind the other regions. Such arrangements are more for the local investors than the foreign ones.

2.5.5 Free Banking and Off-shore Banking

The free banking and Off-shore banking facilities are designed to capture international finance. Offshore banking is the banking activity outside the normal banking business of that country. They work and serve to clients outside the local markets. There are many exemptions to these banks. For example they do not have to deposit at the Central Bank for security purposes. There are also tax incentives

for offshore banking. There are however strict regulations against operations within the local markets.

2.5.6 Free Export Zone

Free export zones are designated for export purposes only. Firms wishing to produce goods for export purpose can get places in these areas and import the inputs without any restriction. Most of the organizations in these zones are subsidiaries of the multinational organizations (Toroslu, 2000, p.7)

2.5.7 Bonded Warehouses

Bonded warehouses are under the control of the Customs and excise offices. These are the warehouse that the goods subject to customs duty and taxes are temporarily placed without any cost. The goods from the warehouses can be imported to the local market or exported to a new destination. The bonded warehouses provide a great opportunity for smaller firms who lack the financial means to import and pay duty on big quantities. By making use of the bonded warehouses they can import big quantities and place them at the warehouses and then draw them in small quantities.

2.5.8 Free Zones and the EU

Since both Turkey and TRNC are aiming to become part of the European Union it is important to look into the system of free zones in the EU. The free zones are operated within the EU by a Customs code accepted in 1993. This code was later amended and updated. The code lists the factors on the basis of which import and export duties and other measures prescribed in respect of trade in goods are applied.

These are: the Customs Tariff of the European Community and the tariff classification of goods, their origin (preferential or non-preferential) and their customs value.

The code lists the provisions applicable to goods brought into the customs territory of the Community until they are assigned a customs-approved treatment or use. It covers the entry of goods into the customs territory of the Community, presentation of goods to customs, summary declaration and unloading of goods, the obligation to assign them a customs-approved treatment or use, and their temporary storage. Special provisions apply to non-Community goods which are moved under a transit procedure.

A major section of the code covers customs-approved treatment or use. It sets out rules for placing goods under a customs procedure, release of goods for free circulation, suspensive and other arrangements and customs procedures with economic impact, export and internal transit. Special provisions cover the position of free zones and free warehouses (which are part of Community customs territory but are separate from the rest of it) and the re-exportation, destruction and abandonment of non-Community goods.

The section on "Privileged operations" sets out provisions for reliefs from duty, returned goods, and products of sea-fishing and other products taken from the sea. Another on "Customs debt" sets out rules on providing security for customs debt, specifies when the debt is incurred and provides for its recovery.

The code provides for a two-stage right of appeal: in the first instance to the customs authority, then to the national courts. It establishes a Customs Code Committee with responsibility for examining any matter relating to customs Regulations. The code also sets out the legal effects in a Member State of measures taken, documents issued and findings made in another Member State.

Regulation (EC) No 2700/2000 modernises customs procedures and simplifies import and export declarations. As soon as it enters into force, methods of checking free zones will become more flexible. This Regulation introduced a new definition of "good faith" and attendant provisions. A balance was achieved between safeguarding the Community's financial interests and importers' responsibility to demonstrate their good faith, while observing the conditions for implementing preferential arrangements

There are two different identifications of the goods in trade within the EU. These are the goods originated within the EU and the Goods from outside the EU.

A product not originating from a Customs Union country, but from a third party country is not obliged to pay any taxes, and may move freely within the zone. If goods have been manufactured using materials of a third party country, only the common customs tariff is payable. For such goods, a Circulation Certificate (ATR) can be organized. With this certificate (ATR) these goods may be exported to markets within the Customs Union. Goods originating in markets within the Customs Union may enter Turkey without payment of any Customs Duties. Following Turkey's entry into the Customs Union, free zones have encouraged production, and appropriate incentives are provided.

There are two laws on the free zones in Turkey, the law 4458 and 3218. since the law 4458 was adapted from the EU code it is considered to be appropriate for EU members. Free zones operating under this law are considered to be inside the boundaries of the EU trade region.

2.5.9 Prospect of the Free Zones

The free zones around the world are playing an increased role in the world trade. The successful free zones in the countries such as the USA and Korea are become more specialized in certain aspects.

As is well known, the main function of free trade zones is to provide favorable conditions in which traders and processors can gain easy access to duty free equipment and raw materials for warehousing, re-packing, processing and export. There are, of course, other formulas, such as the duty drawback system, a duty remission or suspension system, and bonded manufacturing system, which allow exporters duty free access to imported materials. But the free trade zone/EPZ is the most efficient arrangement from a manufacturer's point of view. In addition to providing duty free access to equipment and materials, a free trade zone usually provides a bureaucracy-free environment for investors.

Free trade zones have therefore been an extraordinary mechanism for fostering export-led industrialization worldwide. They promote economic development by attracting investment and generating employment and foreign exchange earnings. Especially in the case of large and unbalanced developing economies, free trade zones can be used as a means of reducing regional imbalances. All these effects can be observed from the growing international experience with free trade zones development.

This is the conventional wisdom regarding free trade zones development. The additional point I would like to make, that has been extremely important from Latin America's point of view, is the role of free trade zones in the trade liberalization process in goods and services. In East Asian countries there was a realization first, in the early 1970s, that one can pursue an immediate and locally controlled liberalization through the creation of free trade zones rather than

promoting a general and uniform liberalization across all products and economic sectors. The second strategy takes time and may have a number of undesired short term implications.

Initially, the free zones served rather as bonded warehouses in turkey but the semi-finished goods assembled there now find their way, in increasing amounts every day.

The fact that the total volume of trade in Turkey's free zones is increasing by an average of 50% a year is arousing growing interest among investors; in their ten years of operation, they have become among the most productive such zones in the world. Seven new zones are also in the process of being set up and a large number of applications are piling up. Strikes are banned in these enclaves for the first ten years after their opening, but their workers enjoy similar social security cover to their counterparts outside and, since the companies pay no taxes, wages tend to be higher.

2.6 Factors Influencing the Investment decisions to the Free Zones

Main ambition of the investor in any business is to make profit. Taking part in a free zone brings many advantage in respect of input costs (Alpar, 1985, p.28). The investors, especially the bigger ones, have many option as to which free zone to invest to. Since there are hundreds of free zones all around the world they have many options to chose from. So, what does an investor look for in free zone:

- a. Social, political and economic stability: Investors do not like stability. Change of governments for example should mean changes in policies such as new taxes, restrictions of obstacles. Some of the countries who gives importance to free zones and foreign investments sign contracts so to guarantee that there will be no unexpected changes.

- b. Accessibility: How accessible is the zone. Is it on the trade routes of different countries. There should be easy and practical system of cooperation and trade with the outside markets.
- c. Cost of the human resources and rights: investors look for cheap labor. They do not like paying high amounts of wages and they do not want to face strikes and demonstrations.
- d. Transportation costs: Since the free zones are export oriented and since most of the inputs are also imported, the international transportation costs are very critical for the investors.
- e. Physical and Managerial infrastructure: The zones should have all the infrastructure such as the roads, electricity, water and so on. They should also be cleverly managed.

3. FREE ZONE CONCEPT IN THE TRNC

The Government of TRNC is keen to encourage foreign capital investment either in the form of joint-venture or independently through capital commitment or introduction of improved technology in all sectors. The Free Port and Zone situated at Magosa (Famagusta) is considered to be an ideal place for all kinds of business and investment (Serbest Liman Yasası, 2003).

Magosa Free Port and Zone covering an area of 115 acres, offers to foreign investors excellent opportunities for transit trade as well as manufacturing opportunities for middle-east and near-east countries. Among the activities, assembly and repair of any kind of ships, banking and insurance services, transshipment and re-export activities, manufactures of all kinds of industrial products are through to be suitable investment fields. Free Port and Zone is totally exempt from controls and regulations regarding trade and finance, which are applicable within the TRNC.

Following are some of the benefits of the Famagusta Free Port:

- Open Port to All Flags.
- Expert and Friendly Service.
- Geographically excellently positioned.
- Strategically located with convenient regional and international air links
- 24 Hours Service rendered if and when requested.
- Highly qualified and very competitive operating cost.
- International Safety Standard Observed.
- An Ideal Port for all functions i.e. Docking transshipment and as a Feeder Port especially for neighboring Middle East Countries and Turkey.
- Not Port Congestion problems and / or delays.

- No Storage Charges, for the first 7 days.
- First 15 days no storage charges for full container.
- First 30 days no storage charges for empty container.
- Less formality.
- No limitation on the proportion of Foreign Capital participation.
- No limit on Repatriation of Profit and Capital.
- Exemption from Corporate tax and Income tax.
- Exemption from Customs Duties and Indirect taxes.
- A pleasant working and living environment including the lowest crime rate in Europe.

3.1 Legal framework of the Famagusta Free Zone

The Free Port and Zone Law states that only 'Approved Enterprises are entitled to operate and erect concerns in the Free Port and Free Zone Areas'. An "Approved Enterprise" is defined as one which has received approval from Free Port and Zone Council to function in the Free Port and Zone Areas. Applications for "Approved Enterprise" status are to be submitted to the Free Port and Zone Council on forms supplied by this body.

Operations and activities permitted in the Free Port and Zone Areas are as follows:

- Engaging in all kinds of industry, manufacturing and production.
- Storage and export of goods imported to the Free Port and Zone Areas.
- Assembly and repair of goods imported to the Free Port and Zone Areas.
- Building, repair and assembly of all kinds of ships.

- Banking and Insurance services.
- Any other kind of activity approved by the Council of Ministers.

Investors applying to the above activities are charged a fee up to 1000 \$, this fee being changeable according to the activity undertaken.

Incentives provided to businesses established in the Free Port and Zone are as follows:

- All income derived from activities and operations undertaken by investors in the Free Port and Zone are exempt from Corporate and Income Tax. This exemption does not apply to the exports of goods and services not manufactured and undertaken in the Free Port and Zone and that are directed to the TRNC.
- No limit on repatriation of profit and capital.
- Exemption from custom duties and indirect taxes.
- Permission to employ foreign expert, engineer and technical personnel.

In addition to the above incentives there is ample supply of skilled and unskilled labour and wages are reasonable. The Port's handling charges are much lower than the other neighbouring ports. The port, which is geographically well located, offers sufficient covered storage area, experienced stevedoring and good security. A sound and receptive civil service, coupled with minimum of formalities, provides investors and dealers with a favourable working climate. All types of port machineries (fork-lifts, cranes etc) are available.

3.2 Privatization efforts of the Free Port

The Famagusta Free port cannot be claimed to be very successful. There need to be an increased effort to improve the conditions. In a recent statement, just before the elections, the Minister for economy Mr. Coşar announced that the part of the unused free Port of Magusa will be privatized. He suggested that this would be the only way to provide progress in the zone. The company which was successful in obtaining the license for developing the free zone area was a company called Doba. The directors of the company, which is a specialized company in the free zones management has claimed that not only they will improve the Famagusta free port but they will also clean up the Denizli mine waste region and turn into a free zone as well. If this is achieved the TRNC will be freed from the main environmental problem. Free zone in this region will also help for the development of the region.

3.3 Impact of Famagusta Free Port on the Economy

There has been \$350,000.- imports and \$880,000 exports from the Famagusta Free Port in the year 2002. The export from the region contribute to 1% of the total exports of the country. The imports into the free port contributes to 0.1% of the total country import. When we look at the profitability of the port we can observe that the port made profits of \$62,000, in 1993, \$257,000 in 1994, \$990,000 in 1995, and 337,000 in 2002. It is estimated that the profits for the 2003 will not exceed \$130,000. In 1995 there were 48 firms operating in the port. 37.5% of these were Turkish Cypriots, 20.8% Turkish, and nearly 40% were third parties. In 2002 the total number of the firms in the region were 37. 59.5% of the firms are Turkish Cypriots, 18.9% Turkish, 8.1% are Turkish and Turkish Cypriot partnership, and 13.5% are the

foreign investors. Out of the 5 foreign investors in the region 4 are Syrians and 1 Macedonian.

From the above information and additional information from various sources it is evident that the Famagusta Free Port has not reached its objectives and cannot be considered as successful. The place has not been able to attract foreign investment, it has not been able to increase the exports and it has not been contributing to employment. The profitability of the free port is also in a decline.

4. CONCLUSION AND RECOMMENDATIONS

International trade is becoming more and more important in the globalizing world economy. The barriers are diminishing in the international trade and new economic waves are spreading in the form of sanal trade. The TRNC organizations are aiming to take their place in this new environment of international trade. Free ports and zones are just some of the instruments that can help to improve the international trade to and from the country.

When the pros and cons of the free zones are evaluated the free zones are found to be important instruments and systems to improve the international trade provided that they are well managed. Free zones are places where the bureaucracy is at the minimum, and there are tax and duty exemptions.

There are also states as a whole, who operate like the free zones. Such countries abolish all the customs duties and taxes and allow free trade. Overall the business life is made easy and simple as well as less costly. Financial freedom and minimal bureaucracy are other characteristics of these countries. Starting a business or planning to invest in these countries is so welcomed the investors need only to apply to one specific centre and the rest of the formalities will be handled by the application point.

In small countries such as TRNC the formalities of establishing a business or making an investment should be reduced to a mere formality of a few pages regulations. All the bureaucracy should be lifted and all the restrictions should be abolished in front of the international trade.

There are arguments recently about the declaration of the TRNC as a free trade country. A well organized country with no restrictions and easy formalities is certain to attract foreign attention. Transit

trading, assembly manufacturing, packaging industry, banking and insurance are the first lines of businesses to attract foreign investment. As these investments grow there will be new entries into business. A lively international trade, high employment rate, increased foreign currency earnings will mean prosperity and better life standards for the local community. It will also mean better income for the people in the agricultural sector. Construction industry will prosper since there will be need for new factories, depots and housing.

There is already a small free zone in Cyprus which is operating under the law 45/77. This law can simply be amended to cover the whole island. However there should be a caution since the free zone of Magusa has not proved to be successful. When established in 1977 the main objective of the free port was to increase international trade, and hence increase the currency earnings, contribute to employment and to the overall economy. Since its establishment the number of the firms established businesses in the zone range between 16-22. The number of the employees never exceeded 280 (Sancarlı, 1997, p.50)

The basic reason behind the failure of the Famagusta Free Zone is the political uncertainty in TRNC. The long Cyprus problem not being solved the investors decline from coming to invest in the TRNC. Lack of the infrastructure, financial difficulties, excessive bureaucracy, and inappropriate human resources are other problems.

The above problems must be solved in order to provide any success for the zone. Privatizing the free port is a positive step, but this is not enough on its own. The state must be more decisive about supporting the free enterprises and they need to introduce better incentives.

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