Date of Hearing: April 21, 2015

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT, AND THE ECONOMY
Eduardo Garcia, Chair
AB 1444 (Eduardo Garcia) – As Introduced February 27, 2015

SUBJECT: Foreign-trade zones

SUMMARY: Expands the type of applicants California law recognizes under the federal Foreign Trade Zone Act of 1934 to include applications submitted by a federally recognized tribal government.

EXISTING FEDERAL LAW, the Foreign-Trade Zones (FTZ) Act of 1934, establishes a process for a public corporation and a private corporation to become designated as a FTZ. The implementing federal regulations require, among other things, that the eligibility of grant applicants be supported by enabling legislation from the state in which the FTZ is to be located, indicating that the applicant, individually or as part of a class, is authorized to apply.

EXISTING STATE LAW authorizes public and private corporations to apply for a FTZ designation. A public corporation is defined as the state, any political subdivision thereof, any incorporated municipality therein, or any corporate municipal instrumentality of the state, or of this state and one or more other states. Private corporations must be formed for the specific purpose of establishing, operating, and maintaining a FTZ.

FISCAL EFFECT: None

POLICY ISSUE FRAME:

This bill proposes to change state law to more clearly reflect the sovereignty of tribal governments relative to their application for FTZ designation. By practice, the FTZ Board has approved a number of FTZ designations involving tribal government applicants by using the public corporation category. Multiple models have been used, including direct designation authority, as seen in Washington and Oregon, and having the FTZ located on tribal lands with another entity having the operational responsibility, as in Oklahoma.

While a tribal government is a public entity, a tribal government is a separate public entity from the state or states in which their lands are surrounded. Existing state law says that the public corporation applicant must be the State of California, a political subdivision of the state or a municipality. AB 1444 establishes a second public entity category, which more accurately reflects tribal government sovereignty.

The Comments section of the analysis includes the author's statement, information on FTZ, the importance of foreign trade to the California economy, and related legislation.

COMMENTS:

1) **Author's Purpose**: According to the author's statement, "By practice, the FTZ Board has approved FTZ designations that have been applied for by tribal governments using the public corporation category. Multiple models have been approved by the FTZ Board, including direct designation authority, as seen in Washington and Oregon, and having the FTZ being located on tribal lands with another entity having the operational responsibility, as in Oklahoma. Tribal governments are,

however, not a political subdivision of the state nor municipality. AB 1444 updates California's law to reflect the sovereignty of tribal governments."

2) **Background on FTZs**: The FTZ program is a federal economic development tool, which is used to attract manufacturing and product assembly that may otherwise be undertaken in a foreign country. In addition, FTZs strengthen the competitiveness of U.S. companies to participate within global supply chains.

   Businesses benefit from special FTZ custom procedures, which allow domestic activity involving foreign items to take place prior to its official entry into U.S. Customs. Among other advantages, duty-free treatment is accorded items that are re-exported and duty payment is deferred on items sold in the U.S. market. When merchandise is manufactured in zones, users have the option of paying duties at the finished product rate.

   Another FTZ advantage is the exemption from state and local ad valorem taxes. This applies to tangible personal property imported from outside the U.S. and held in a zone for the purpose of storage, sale, exhibition, repackaging, assembly, distribution, sorting, grading, cleaning, mixing, display, manufacturing, or processing, and tangible personal property produced in the U.S. and held in a zone for exportation, either in its original form or as altered by any of the above processes.

   Taken together, the FTZ custom treatment and state and local tax provisions are designed to help offset advantages available to overseas producers who compete with producers located in the U.S.. There are 250 FTZ in the U.S. with 16 located in California.

3) **Application Procedures**: Each zone is managed locally by the "grantee" organization, which is generally a public or non-profit organization focused on trade or economic development. Designation authority is awarded by the Foreign-Trade Zone Board (Board), which is comprised of the U.S. Secretary of the Treasury and the U.S. Department of Commerce, who serves as chair.

   Among other evaluation criteria, the Board is required to base its evaluation on such factors as market conditions, price sensitivity, degree and nature of foreign competition, intra-industry and intra-firm trade, effect on exports and imports, ability to conduct the proposed activity outside the U.S., and net effect on U.S. employment and the U.S. economy.

   Once the FTZ authority is granted by the Board, the grantee must submit an application to the U.S. Customs and Border Protection which is responsible for overseeing the local port of entry. This second process is referred to the FTZ activation process and generally includes steps such as background checks, a written procedures manual, posting a bond with the U.S. Customs and Border Protection, as well as a review of the security of the site(s) and the proposed inventory control methods. On a day-to-day basis, the U.S. Customs and Border Protection is responsible for overseeing activities within the FTZ.

4) **Magnet Sites and Subzones**: As initially implemented, the boundaries of most FTZs included seaports or airports, as well as some industrial parks. The FTZ operated as a magnet site which could be used by multiple businesses. Subzones were developed as unique usage-driven sites, which are approved for a specific company. Designations of a subzone may also include the use of an "Alternative Site Framework," which is described by the Board as being a quicker and simpler process for designating a subzone at a specific company's facility, usually a manufacturing or processing plant.

In addition to the 250 FTZs, there are 500 subzones in the U.S. The largest industry subsector currently using zone procedures is the petroleum refining industry. Significant zone manufacturing also occurs in the automotive, electronic, and pharmaceutical product areas. California's 16 FTZs have 37 related subzones operated by the following companies: Chevron, Hewlett-Packard, National RV, Skechers USA, LLC, Sony Electronics, Inc., and Valero Refining Company-California

5) **Importance of Trade to the California Economy**: A key driver of California's $2.2 trillion economy is trade is the production and delivery of goods and services within an expanding global marketplace. California's 2013 GDP places it as the eighth largest economy in the world. When the 2014 GDP numbers are formally released by the California Department of Finance in June 2015, some anticipate that California will rank seventh.

   In 2014 California exported $174 billion in products as compared to $168 billion in 2013 and $162 billion in 2012. Mexico remained California's largest export market, where the value of exports totaled $25.4 billion in 2014. After Mexico, California's top export markets in 2014 were: Canada ($18.2 billion); China ($16.0 billion); Japan ($12.3 billion); South Korea ($8.6 billion); Hong Kong ($8.5 billion); Taiwan ($7.5 billion); Germany ($5.4 billion); the Netherlands ($5.4 billion); and India ($5.3 billion).

   California's top five exports in 2014 were: Computer & Electronic Products ($42.7 billion); Transportation Equipment ($18.7 billion); Machinery, Except Electrical ($14.9 billion); Miscellaneous Manufactured Commodities ($14.6 billion); and Chemicals ($14 billion). It is important to note that significant portions of these five export categories include parts and semi-assembled products, which underlies both California's importance within and dependence on global supply chains.

   Another important component of global supply chains are the ability of states to import products quickly and efficiently. China is the largest source of imports into California. The 2014 value of Chinese imports was $137.7 billion, followed by Mexico ($41.3 billion); Japan ($38.3 billion); and Canada ($27.9 billion).

6) **Related Legislation**: Below is a list of bills from the current and prior sessions.

   a) ***AB 311 (V. Manuel Pérez) I-Bank California-Mexico Border Assistance***: This bill would have expanded the role of the I-Bank to include facilitating infrastructure and economic development financing activities within the California and Mexico border region. Status: Died in the Assembly Committee on Appropriations, 2014.

   b) ***AB 337 (Allen) Economic Development: International Trade and Investment Strategy***: This bill adds specificity to the development and content of the state international trade and investment strategy (ITI Strategy), which is an existing report requirement of the Governor's Office of Business and Economic Development (GO-Biz). This bill requires the ITI Strategy to be based on current and emerging market conditions and the needs of investors, businesses, and workers. Specific new content requirements include the addition of a framework, which can be used by GO-Biz to evaluate the changing needs of business during the five-year term of the ITI Strategy. Status: Signed by the Governor, Chapter 776, Statutes of 2014.

   c) ***AB 886 (Allen and Ian Calderon) Importer-Exporter Tax Credit***: This bill would have authorized a five-year $500 million tax credit program for importers and exporters that increase cargo through in-state airports and seaports, hire additional staff, or incur capital costs at a California cargo facility. Status: Held on the Suspense File of the Assembly Committee on Appropriations, 2013.

d) ***AB 1137 (V. Manuel Pérez) Small Business Assistance and Attracting Private Investment:*** This bill would have facilitated local economic development and job creation by assisting small businesses to access new export markets for their goods and services, updating the law relating to FTZs, and authorizing the use of new federal funds under the Small Business Jobs Act of 2010. Status: Held in Senate Committee on Appropriations, 2012.

e) ***AB 1400 (Assembly Committee on Jobs, Economic Development, and the Economy) Export Document Certificates***: This bill modifies the state's Export Document Program to accept requests electronically, expedite approval of existing labels, and extend the term of the export labels from 180 days to 365 days, in order to alleviate backlog of exports of food, drugs, and medical devices. Status: Signed by the Governor, Chapter 539, Statutes of 2013.

f) ***AB 2012 (John A. Pérez) Economic Development Reorganization***: This bill transfers the authority for undertaking international trade and foreign investment activities from the Business, Transportation and Housing Agency to the Governor's Office of Business and Economic Development. Status: Signed by the Governor, Chapter 294, Statutes of 2012.

REGISTERED SUPPORT / OPPOSITION:

Support

None received

Opposition

None received

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