

Date of Hearing: April 25, 2017

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT, AND THE ECONOMY

Sharon Quirk-Silva, Chair

AB 1727 (Committee on Jobs, Economic Development, and the Economy) – As Introduced March 21, 2017

SUBJECT: Foreign trade and investment

SUMMARY: Makes technical changes to update the content and the statutory placement of the codes relating to Foreign Trade Zones (FTZs) and the California Foreign Investment Program.

EXISTING STATE LAW:

- 1) Establishes GO-Biz to serve as the state's primary agency for issues of economic and business development. Among other entities within GO-Biz' oversight are the California Business Investment Services Program, the Office of the Small Business Advocate, the International Trade and Investment Program, and the California Infrastructure and Economic Development Bank.
- 2) Establishes the California Foreign Investment Program within GO-Biz to oversee the state's participation in the federal EB-5 foreign investment visa program. Among other things, this office sets the terms and conditions regarding the designation of targeted employment areas, as related to the EB-5 visas.
- 3) 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.

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.

FISCAL EFFECT: Unknown

POLICY FRAME:

Since the demise of the California Technology, Trade and Commerce Agency, in 2003, the Legislature and Governor have been in an extended dialogue about the appropriate role of the state in issue areas relating to economic and business development, including international trade and foreign investment. Some of these discussions were specific, as to under what conditions is it appropriate for the state undertake promotional activities in a foreign county, and in other situations, the economic development programs were part of a larger reorganization to better serve the needs of the state.

This bill makes technical changes to update the content and the statutory placement of the codes relating to FTZs and the California Foreign Investment Program. It is the authors' intent that this bill will serve as a code maintenance bill and be available for other nonsubstantive changes.

The analysis includes information on the California global economy, FTZs, and the California Trade and Investment Program.

COMMENTS:

- 1) **Consolidating Trade Codes:** Between 1986 and 2004, the Technology, Trade and Commerce Agency was the government entity responsible for promoting economic development, international trade, and foreign investment in California. When the agency was eliminated due to its poor administrative performance and a possible savings of money, the authority for all state trade activity was also struck from statute.

Beginning in the 2005-06 session, several legislative measures were introduced to reinstate the state's trade authority. No measures were successful until a compromise was negotiated by the JEDE, SB 1513 [(Romero), Chapter 663, Statutes of 2006]. SB 1513 assigned international trade authority to the Business, Transportation and Housing Agency (BTH).

Several years later and a new administration, an agreement was made to re-establish a separate state-level economic development entity. In signing legislation to codify GO-Biz, Governor Brown also issued a letter outlining his continued interest in expanding the role of GO-Biz for the purpose of better focusing the state's multiple economic development activities, AB 29 (John A. Pérez), Chapter X, Statutes of 2011. The Governor reiterated this policy when he released his proposed 2012-13 budget.

On March 30, 2012, the Governor also submitted a reorganization plan to the Little Hoover Commission, which operationalized his earlier statements. Among other things, the reorganization plan, eliminated BTH and transferred the following programs to GO-Biz.

- The Small Business Loan Guarantee Program;
- The California Travel and Tourism Commission;
- The California Film Commission;
- The Film California First Program; and
- The Infrastructure and Economic Development Bank (IBank).

Also during 2012, Speaker John A. Pérez authored legislation to transfer the official operation of the trade-related activities to GO-Biz, AB 2012, Chapter 294, Statutes of 2012. While the authority was transferred, the code sections remained isolated in the former code sections related to BTH.

By renumbering Government Code Sections 6315-6315.3 to Sections 12100.50.- 12100.53 AB 1727 recasts – with no policy changes - the California Foreign Investment Program within CHAPTER 1.6. Governor's Office of Business and Economic Development

- 2) **Legacy Code Sections for the Foreign Trade Zones:** California adopted implementing statute to participate in the federal FTZ Program in 1943. The structure of California Law and has changed in the succeeding 70 years. AB 1727 makes technical and nonsubstantive changes to codes.
- 3) **California's Global Economy:** International trade and foreign investment are very important components of California's \$2.4 trillion economy supporting 4.4 million California jobs. The importance of trade to the California economy is increasing as a percentage of California jobs tied to trade more than doubled from 1992 to 2011, 10.6% v. 22.0%.

California receives more foreign direct investment (FDI) than any other state in the U.S., which is significant since the U.S. is the largest receiver of FDI in the world. The California economy benefits from FDI in many ways, some of which include assisting in the creation of jobs, boosting worker wages, increasing exports, bringing in new technology and skills, and generally strengthening the state's manufacturing base.

The top 5 regions with the highest foreign owned and affiliated businesses are: Gateway Cities (796 establishments), South Bay-LAX (741 establishments), San Fernando Valley (725 establishments), San Gabriel Valley (698 establishments), and West Side (415 establishments). The top 5 cities with the highest concentration of foreign owned and affiliated businesses are Los Angeles (1591 establishments), Torrance (310 establishments), Long Beach (212 establishments), Santa Monica (134 establishments), and Pasadena (127 establishments).

The federal International Trade Administration estimates that in 2012 over 602,800 California workers benefit from jobs with foreign-owned firms, which accounts for 4.8% of all private sector jobs in the state. California has had the highest level of employment in foreign-owned firms in the nation since at least 1997. Along with employment, foreign-owned firms own more property, plants, and equipment in California than in any other state.

California's largest industry sector by employment is Trade, Transportation, and Utilities, which encompasses everything from major retail outlets, to import-export businesses, to transportation and warehousing. California leads the nation in export-related jobs. The U.S. Department of Commerce estimates that 775,320 jobs were directly supported by the export of products in 2014, including 665,000 manufacturing jobs. Workers in trade-related jobs earn on average 13% to 28% higher wages than the national average. California leads the nation in export-related jobs. The U.S. Department of Commerce estimates that for every one million dollars of increased trade activity, eleven new jobs are supported. Workers in trade-related jobs earn on average 13% to 28% higher wages than the national average.

California's land, sea, and air ports of entry served as key international commercial gateways for the \$573 billion in products entering and exiting the U.S. in 2015. If California were a country, it would be the 28st largest exporter and the 12th largest importer in the world, based on 2015 trade numbers. California's two-way trade represented 15.3% of total U.S. imports and exports. In 2015, exports out of California were valued at \$165.3 billion and represented 11% of total U.S. exports. Imports into California were valued at \$408.1 billion and represented 18.2% of total U.S. imports in 2015.

In 2016, California exported \$163.6 billion in goods. The *Chart* below shows export data on the state's top five trade partners, based on origin of movement. Other top-ranking export destinations not shown on the chart include Hong Kong, Taiwan, Germany, the Netherlands, and the United Kingdom.

California Exports 2011 to 2016 (billions of dollars)							
	<i>Partner</i>	<i>2011</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>	<i>2016</i>
	World	159.4	161.7	168.0	174.1	165.3	163.6
1	Mexico	25.8	26.3	23.9	25.4	26.7	25.2
2	Canada	17.2	17.4	18.8	18.2	17.2	16.1
3	China	14.2	13.9	16.2	16.0	14.3	14.3
4	Japan	13.1	13.0	12.7	12.2	11.7	11.7
5	Hong King	7.6	7.8	7.7	8.5	8.7	9.6

6	South Korea	8.4	8.2	8.3	8.6	8.6	8.2
Source: International Trade Administration, accessed 04/11/2017							

The International Trade Administration estimates that in 2015, approximately 11.5 million U.S. jobs were related to the export of goods and services. Statewide, 707,000 California jobs are dependent on exports, 11% of all U.S. export related jobs. Texas is reported to have the largest number of jobs related to exports (1 million). Manufacturing is responsible for the largest number of trade-related California jobs (469,000).

In today's globally linked economy, manufacturing utilizes products from across the U.S., as well as from other nations. In 2012, 61% (\$1.3 trillion) of the products imported into the U.S. were inputs and components intended for use by American producers. In addition, U.S. imports often include components or have benefited from services provided by U.S. firms, including many California companies. The Wilson Center estimates that Mexican imports and Canadian imports contain 40% and 20% U.S. components, respectively.

The federal International Trade Administration estimates that in 2013 over 631,500 California workers benefitted from jobs with foreign-owned enterprise (FOE) firms, which accounts for 10.3% of all FOE jobs in the U.S. California has had the highest level of employment in foreign-owned firms in the nation since at least 1997. In 2013, California FOE-related jobs represented 4.1% of all private sector jobs in the state. According to the Business Roundtable, there are:

- 110,000 companies in California that are headquartered in Japan;
- 78,500 companies in California that are headquartered in the United Kingdom;
- 59,200 companies in California that are headquartered in France;
- 58,900 companies in California that are headquartered in Switzerland.

As noted previously, foreign-owned firms own more property, plants, and equipment in California than in any other state.

- 4) **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 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 over 250 FTZ in the U.S., of which 181 were active in 2015.

California has 17 FTZs, with 14 reported as being active in 2015. FTZs were responsible for the employment of over 33,000 people. California FTZs received over \$75 billion in merchandise and over \$1 billion in exports, resulting in total shipment value of between \$33 and \$34 billion in 2015. The largest categories of foreign product processed by value were oil/petroleum (37%), vehicles (13%), and other electronics (9%).

- 5) **Designation of the Foreign Trade Zones:** 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.

- 6) **The Modern Foreign Trade Zone:** As initially implemented, the boundaries of most FTZs included seaports or airports, as well as some industrial parks. These FTZs are operated as a magnet site, which could be used by multiple businesses. Subzones were later 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 17 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.

- 7) **Related Legislation:** Below is a list of bills from the current and prior sessions.
- a) **AB 29 (John A. Pérez, Feuer and V. Manuel Pérez) Office of Business and Economic Development:*** This bill establishes the Governor's Office of Business and Economic Development (GO-BIZ), to be administered by a director appointed by the Governor. The bill would also moves the Office of the Small Business Advocate to the Office of Economic Development. Status: Signed by the Governor, Chapter 475, Statutes of 2011.

- b) ***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 on File

Opposition

None on File

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