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Jurisdictional Uncertainty: The American Foreign Trade Zone

by Mark B. Bader*

I. Introduction

Since the days of ancient Greece and Carthage, the free port has played an important role in international commerce.¹ As the nations of the world grow more economically interdependent, and the worldwide volume of foreign commerce increases, conditions ripen for an expansion of that role.

The United States entered the field of international free ports with the passage of the Foreign Trade Zones Act² in 1934. This Act and its subsequent amendments³ represent a congressional attempt to encourage the use of American labor and facilities in foreign commerce.⁴

Although the use of foreign trade zones is on the upswing,⁵ their potential has not yet been fully realized, due largely to businesses' uncertainty regarding jurisdiction over zones and over activities within the zones. Both the federal government and the states have arguable claims to jurisdiction over property and activities within zones, and the inability to predict accurately the application of federal and state authority in a foreign trade zone diminishes the utility and attractiveness of conducting business within the zone.

This article focuses on the issue of jurisdiction in a foreign trade

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¹ R. THOMAS, *FREE PORTS AND FOREIGN TRADE ZONES* 11-12 (1956). The historical beginnings of foreign trade zones have been the subject of some debate. Professor Thomas traces their inauguration to the city-states of the Mediterranean region, while Professor Lomax argues the free port came into being in 1189 with the exemption of the city of Hamburg from payment of customs duties on the lower Elbe river. A. LOMAX, *THE FOREIGN TRADE ZONE* 8 (1947).

² Foreign Trade Zones Act of 1934, ch. 590, 48 Stat. 998 (codified as amended at 19 U.S.C. §§ 81a-81w (1976 & Supp. V 1981)).

³ The Foreign Trade Zones Act has been amended twice. In 1950, Congress enacted the Boggs Amendment, ch. 296, 64 Stat. 246 (1950), to permit manufacturing and exhibition in a zone. Minor changes were also made by the Foreign Trade Zones Act Amendment of 1970, Pub. L. No. 91-271, § 309, 84 Stat. 274, 292 (amending 19 U.S.C. § 81c (1976)).

⁴ *See* S. REP. NO. 905, 73d Cong., 2d Sess. 1 (1934) [hereinafter cited as SENATE REPORT]; S. REP. NO. 713, 70th Cong., 1st Sess. 1 (1928).

⁵ The Foreign Trade Zones Board reported the increase of eight new zones or sub-zones in fiscal 1979, increasing to 47 the number of communities with zones at that time. 41 U.S. FOREIGN TRADE ZONES BOARD, *ANNUAL REPORT* 1 (1979).

zone. After a brief discussion of the zone concept, procedures within a zone, and the strengths and weaknesses of the zones, the jurisdiction of the Foreign Trade Board is examined, as is federal jurisdiction and the application of federal statutory law, state regulatory jurisdiction, and most importantly, the question of state and local taxing authority over zone inventory and activities. It is hoped that a thorough look at jurisdictional concerns will ease business uncertainty about operation in a foreign trade zone and pave the way for continued growth in zone utilization.

II. The Foreign Trade Zone Concept

A. *Concept and Procedures*

The zone concept itself is a simple one. Congressman Emanuel Celler, sponsor of the Foreign Trade Zone Act, described a zone as an isolated, enclosed and policed area in or adjacent to a port of entry, without a resident population, furnished with the necessary facilities for lading and unloading, for supplying fuel and ship stores, for storing goods, and for reshipping them by land and water—an area within which goods may be landed, stored, mixed, blended, repacked, manufactured, and reshipped without payment of duties and without the intervention of customs officials.⁶

The purpose of a free zone is to encourage and expedite foreign trade by eliminating the payment of customs duties unless and until foreign merchandise is imported into U.S. customs territory. By definition, a zone is not within U.S. customs territory.⁷ Thus, the payment of customs duties is deferred until any processing in a zone is completed and the foreign goods are imported into the United States.⁸

A foreign trade zone is an enclosed area and must be located at a port of entry.⁹ Any foreign or domestic merchandise can be brought into a zone and there “stored, sold, exhibited, broken up, repacked, assembled, sorted, graded, cleaned, mixed with foreign or domestic merchandise, or otherwise manipulated, or . . . manufactured. . . .”¹⁰ Although the U.S. Customs Service constantly supervises foreign trade zones, the manipulation and processing of goods in a zone occurs without the administrative procedures and customs expenses generally associated with operations in a U.S. port.

The regulations of the Foreign Trade Zones Board (Board) author-

⁶ 78 CONG. REC. 9853 (1934).

⁷ 19 U.S.C. § 81c (1976 & Supp. V 1981).

⁸ *Id.*

⁹ *Id.* § 81b(a). Although the term “port” traditionally connoted a seaport, its use today extends to a variety of situations. In the area of foreign-trade zones, a port of entry denotes one of the more than 300 Customs ports of entry located in the United States. A broadening of the scope of the term is attributable to U.S. CONST. art. I, § 9, cl. 6, which prohibits legislation favoring the ports of one state over those of another.

¹⁰ 19 U.S.C. § 81c (1976 & Supp. V 1981).

ize general purpose foreign trade zones and special purpose sub-zones.¹¹ The major distinction between a foreign trade zone and a special purpose sub-zone is that a sub-zone is accessible to use by only one firm.¹² A qualifying business need not physically relocate to an existing zone. Instead, the business simply designates that part of its facilities which will comprise the sub-zone. Indeed, sub-zones were specifically designed for companies wishing to utilize the zone concept but unable to relocate to an existing zone.¹³ The Board's regulations state that a special purpose zone or sub-zone may be authorized upon a Board finding that "existing or authorized zones will not serve adequately the convenience of commerce with respect to the proposed purposes."¹⁴

The application procedures for both foreign trade zones and sub-zones are similar. Applications to operate a zone may be submitted by either public or private corporations, depending on applicable state law.¹⁵ The corporation submits an application to the Board showing the "location and qualifications of the area in which it is proposed to establish a zone."¹⁶ The Board is empowered to grant an application if it "finds that the proposed plans and location are suitable for the accomplishment of the purpose of a foreign trade zone. . . ."¹⁷ The Board may also prescribe rules and regulations necessary to establish and conduct these zones.¹⁸ The grantee of the zone becomes, in effect, the lessor to businesses which use zone facilities.¹⁹

Operation in a foreign trade zone or sub-zone offers several unique advantages. The most obvious and important advantage is the elimination of customs duties on goods that enter a zone and are later transhipped or reexported without entering U.S. customs territory. Another advantage is the opportunity to bring foreign goods into a zone, with customs duties determined only on finished products imported into the United States. Customs savings will be significant if the duty on the imported raw material is greater than that on the finished product, and no customs duties are paid on materials which eventually become waste. In addition, cash flow is increased through deferral of customs duties on zone merchandise until importation. Prospective purchasers can ex-

¹¹ 15 C.F.R. § 400.304 (1983).

¹² *Id.* See also *Armco Steel Corp. v. Stans*, 303 F. Supp. 262 (S.D.N.Y. 1969), *aff'd*, 431 F.2d 779, 788-89 (2d Cir. 1970).

¹³ See Atkins, Doyle & Schwidetzky, *Foreign Trade Zones: Sub-Zones, State Taxation and State Legislation*, 8 DEN. J. INT'L L. & POL'Y 445, 448 (1979); Da Ponte, *Foreign Trade Zones: An Update*, AM. IMPORT & EXPORT BULL., April 1977.

¹⁴ 15 C.F.R. § 400.304 (1983).

¹⁵ See *infra* notes 63-83 and accompanying text.

¹⁶ 19 U.S.C. § 81f(a)(1) (1976).

¹⁷ *Id.* § 81g.

¹⁸ 15 C.F.R. § 400.200(b) (1983). For example, the Board's regulations state that a grantee of a zone or sub-zone must "maintain the structures and other facilities within the zone in good condition and so as not to endanger the life and health of the employees of the United States and others who may be required to enter the zone." 15 C.F.R. § 400.900 (1983).

¹⁹ See A. LOMAX, *supra* note 1, at 17.

amine zone goods and place orders, assuring sale prior to payment of duties. A zone operator is also able to release the goods at the most advantageous marketing moment. Finally, insurance rates in a zone may be lower, as the nonpayment of customs duties decreases the insurable value of a zone operator's goods.²⁰

One possible disincentive built into the Act is the Board's express power to prohibit the manufacture or zone processing of any goods "that in its judgment [are] detrimental to the public's interest, health or safety."²¹ Such reclassification is unlikely to occur, however, as the case of a Puerto Rican meat packing sub-zone demonstrates. In response to the creation of the sub-zone, the American Cattleman's Association complained to the U.S. Department of Agriculture (USDA) that because meat produced abroad but packed in the sub-zone did not count against U.S. meat import quotas, sub-zone packed meat could be used by foreign meat producers to avoid the U.S. quotas. The USDA responded by filing with the Board a request that meat packing be declared not in the public interest when occurring in a zone or sub-zone. Before the Board could rule on the request, however, the USDA changed its own regulations so that meat produced abroad and packed in a sub-zone counted against U.S. meat import quotas. This regulation change solved the problem, and the Board abandoned its investigation of the USDA's complaint.²² The meat packing episode demonstrates that activities which are not in the public interest can often be more easily dealt with by the agency responsible for regulating those activities, wherever they take place. Hence, the Board's power to prohibit such activities in a zone is largely redundant.

The foreign trade zone concept is sound. Foreign trade zones provide many advantages and only one significant disincentive. The application procedures are relatively straightforward, and with the veritable plethora of advantages available through zone operation, it is unclear why zone utilization, despite the recent increase, remains depressed.

B. Legal Challenges to the Foreign Trade Zone Concept

Despite its historic antecedents, the foreign trade zone concept, as used in the United States, has been legally challenged. The most serious challenge was presented in *Armco Steel Corp. v. Stans*,²³ where Armco sought a declaratory judgment in federal district court to set aside an order by the Board which authorized the Commissioners of the Port of New Orleans to operate a sub-zone. The sub-zone's purpose was to per-

²⁰ See generally Note, *Foreign-Trade Zones: "Everything Except the Customs?"* 31 U. FLA. L. REV. 725, 737-39 (1979).

²¹ 19 U.S.C. § 810(c) (1976).

²² 39 U.S. FOREIGN TRADE ZONES BOARD, ANNUAL REPORT 11-12 (1977). The author is indebted to Marshall Miller, President of the Foreign Trade Association, Kansas City, Kansas, for directing his attention to this example.

²³ 431 F.2d 779 (2d Cir. 1970).

mit a rival shipbuilder to construct barges with Japanese steel. The high duty on the Japanese steel could be avoided by bringing the steel into the sub-zone and exporting the barges. In a full-scale assault on the zone concept, Armco argued that a zone cannot be used to avoid customs duties if such avoidance results in an unfair competitive advantage over nonzone operators. Armco further alleged that the sub-zone could not be operated as a public utility as required, as only one company would benefit by using the entire sub-zone for its own operations.²⁴ The district court rejected these arguments, granting defendant's motion for summary judgment.²⁵

In a ringing affirmation of the foreign trade zone and, specifically, the sub-zone concept, the Second Circuit upheld the district court's decision.²⁶ The court began by recognizing that Congress gave the Board wide latitude to determine when a zone would aid the domestic economy. This discretion was not abused when authorizing this particular sub-zone.²⁷ This sub-zone was also held not to violate the "equal treatment" requirement of the Act,²⁸ as the Port of New Orleans had offered to establish a similar sub-zone for whomever requested one under the correct conditions.²⁹

The court's most significant action was its dismissal of Armco's implied challenge to the zone concept itself. As the Act was specifically designed to confer a competitive advantage on zone operators, Armco's assertion that a sub-zone could not be granted when an operator received such an advantage struck at the heart of the Act. In response to this argument, the court held that this "multi-faceted assault on the New Orleans Foreign Trade Zone (a Sub-Zone) involved arguments of policy which are better designed for consideration by the Congress than by a federal court."³⁰ The Second Circuit upheld the zone concept and clearly expressed its opinion that any change in that Act's concepts, purposes, or policies must come from Congress rather than the judiciary.

The congressional decision to place foreign trade zones outside the United States customs territory has also been challenged. In *Hawaiian Independent Refinery v. United States*,³¹ a refinery located in a sub-zone used its own imported refined oil to heat distillation equipment. In a dispute over the nonpayment of duties on the oil used in the sub-zone, plaintiff argued that this oil never entered customs territory. The Government, on the other hand, relied on the general rule of dutiability of goods enter-

²⁴ 303 F. Supp. 262, 268 (S.D.N.Y. 1969), *aff'd*, 431 F.2d 779 (2d Cir. 1970).

²⁵ 303 F. Supp. at 272.

²⁶ 431 F.2d 779 (2d Cir. 1970).

²⁷ *Id.* at 788.

²⁸ See 19 U.S.C. § 81n (1976), requiring that the zone grantee "afford to all who may apply for the use of the zone . . . uniform treatment under like conditions"

²⁹ 431 F.2d at 789.

³⁰ *Id.* at 784.

³¹ 460 F. Supp. 1249 (Cust. Ct. 1978).

ing the United States.³² The court held for plaintiff, stating that the Government's general rule applies only to items entering U.S. customs territory. Congress specifically exempted foreign trade zones from customs territory in section 3 of the Act.³³ The exemption is supported by the legislative history of the Act and its amendments.³⁴ The court's holding clearly validated the congressional scheme of customs duty exemption on foreign goods in a zone.

Armco Steel and *Hawaiian Independant Refinery* demonstrate the legal strength of the foreign trade zone concept. Indeed, commentators now seem to have no doubt about the integrity of foreign trade zones.³⁵ Yet, the business community remains uncertain as to the utility of these zones. This uncertainty is focused on the unsettled application of federal and state laws to zones, and the jurisdictional problems inherent therein. The jurisdictional problems revolve around three entities: the Foreign Trade Zone Board, the Federal Government, and state governments.

III. Jurisdiction

A. Foreign Trade Zones Board

The Foreign Trade Zones Board has one of the few clear jurisdictional mandates. The Board's function is to perform the executive roles necessary to implement the Act.³⁶ The Board grants to both public and private corporations the privilege of establishing, operating, and maintaining zones, and has the power to prescribe such rules and regulations as it deems necessary to establish and conduct such zones.³⁷ The Board basically coordinates and manages foreign trade zones on a nationwide basis.

Despite the seemingly clear legislative delegation of power to the Board, the Board's jurisdiction has not gone unchallenged. One such challenge was presented in *Oklahoma ex rel. Blakenship v. South*,³⁸ where the plaintiff requested a declaratory judgment and injunction to halt proceedings before the Board and the Secretary of the Interior. The proceedings contemplated the establishment of an oil refining sub-zone. Plaintiff's principal allegation was lack of jurisdiction in the Board and

³² This rule states that all articles imported into the United States are subject to a tax (a duty) if the tariff schedule so specifies. See 19 U.S.C. § 1202(1) (1976).

³³ See 19 U.S.C. § 81c (1976 & Supp. V 1981).

³⁴ See S. REP. NO. 1107, 81st Cong., 1st Sess. 1 (1949), reprinted in 1950 U.S. CODE CONG. & AD. NEWS 2533. See also 78 CONG. REC. 9853 (1934) (remarks of Rep. Celler); 78 CONG. REC. 9763 (1934) (remarks of Rep. Welch).

³⁵ Commentators have universally agreed on the integrity of foreign trade zones. Scholarly research has dealt primarily with business, and to a lesser extent legal, problems inherent in zone operation. See, e.g., Atkins, Doyle & Schwidetzky, *supra* note 13; Landry & McGinnis, *Foreign Trade Zones in Florida: Legal Considerations for Foreign Business Interest*, 10 LAW. AM. 41 (1978); Note, *supra* note 20.

³⁶ 19 U.S.C. § 81h (1976). See 15 C.F.R. § 400.200 (1983).

³⁷ 19 U.S.C. §§ 81b(a), 81h (1976). See 15 C.F.R. § 400.200(b) (1983).

³⁸ 312 F. Supp. 770 (W.D. Okla. 1970).

in the Secretary to entertain the applications before them.³⁹

The court disagreed with plaintiff's contentions and granted defendants' motion to dismiss.⁴⁰ The court found that Congress had clearly delegated to each defendant jurisdiction to examine the applications.⁴¹ Delegation of jurisdiction to the Board seems clear from the words of the Act granting wide discretion to the Board to hear such applications.⁴² The *Blakenship* decision squarely confirms the power of the Board to hear controversies concerning zone applications in accordance with the congressional scheme.

*Sinclair Oil Corp. v. Smith*⁴³ raised a similar challenge to the Board's jurisdiction. In *Sinclair*, the plaintiff claimed that the Secretary of the Interior and the Board were exceeding their constitutional and statutory authority in entertaining an application for an oil refining sub-zone. Plaintiff's main argument against the Board's jurisdiction was founded on a notion that the Board lacked jurisdiction to create a sub-zone which was "an integral part of a plan to obtain an oil import license which the Secretary lacks power to grant."⁴⁴

The District Court for the Southern District of New York refused to intervene in the on-going administrative proceeding.⁴⁵ The court held that the Secretary of the Interior clearly had the power to consider oil import license requests, and that Occidental Petroleum had properly applied for a license. The argument of lack of jurisdiction of the Board was derivatively based on a claim of a lack of jurisdiction of the Secretary. As the Secretary had jurisdiction, the assertion that the Board did not falls of its own weight. The court deemed the question of Board jurisdiction unworthy of extended discussion, as the Board clearly had the power to entertain zone applications before it.

As illustrated by the cases, the jurisdiction of the Board is solidly established. Assuming certain threshold criteria are met,⁴⁶ the Board has the power to act on zone applications and, in general, to supervise and administer the national foreign trade zone structure.⁴⁷ There should be no uncertainty in the business community as to the effect of Board actions. In conjunction with the previous cases upholding the zone concept, any potential zone applicant apparently can rely on the application and administrative procedures embodied in the Foreign Trade Zones Act.

³⁹ *Id.* at 771.

⁴⁰ *Id.* at 771-72.

⁴¹ *Id.* at 771. The court based this finding on "an examination of the applicable laws," citing *Sinclair Oil Corp. v. Smith*, 293 F. Supp. 1111 (S.D.N.Y. 1968).

⁴² See 19 U.S.C. § 81b (1976).

⁴³ 293 F. Supp. 1111 (S.D.N.Y. 1968).

⁴⁴ *Id.* at 1114.

⁴⁵ *Id.* at 1115.

⁴⁶ See 19 U.S.C. § 81f (1976); 15 C.F.R. §§ 400.600-609 (1983).

⁴⁷ 19 U.S.C. § 81f (1976).

B. Federal Jurisdiction

The Foreign Trade Zones Act does not empower a particular body to decide legal disputes arising from zone operations. Such disputes are left to be heard by the judiciary. Hence, a serious question arises as to what disputes are appropriate for federal courts, and what powers, if any, the several states have over zone operations.

The threshold issue is whether a foreign trade zone is subject to exclusive federal jurisdiction as a "federal enclave." The issue was first raised in *American Dock Co. v. City of New York*.⁴⁸ *American Dock* involved a taxpayer's action to invalidate a zone operating contract between the City of New York and a private corporation. The New York State court held, *inter alia*, that neither the Foreign Trade Zones Board nor the United States was a necessary party to the action. While the issue of federal versus state jurisdiction was not explicitly discussed, the court held that the resolution of the case did not involve any right or interest of the United States, eliminating the need for the Board as a party.⁴⁹ The state court reached the merits of the case, suggesting zones may be subject to state jurisdiction and are not "federal enclaves" subject to exclusive federal jurisdiction.⁵⁰

A more explicit rejection of the "federal enclave" theory occurred in *Fountain v. New Orleans Public Service, Inc.*⁵¹ Plaintiff brought a wrongful death action in federal court with the only possible basis for federal jurisdiction being that the accident occurred in a foreign trade zone. The Fifth Circuit affirmed the district court's dismissal of the action for lack of subject matter jurisdiction. The court prefaced its holding by noting that the Foreign Trade Zones Act by its terms does not confer federal jurisdiction.⁵² The court also held that the suit did not deal directly with the construction of federal law, as neither the Constitution nor the rights of the United States were involved. Thus, no federal question was properly before the court.⁵³

Fountain and *American Dock* appear to reject the idea that a zone is a "federal enclave" for jurisdictional purposes. On the other hand, suits involving questions of federal law in zones remain within the scope of federal jurisdiction. The legislative history of the Act strongly supports continued federal jurisdiction over federal question lawsuits arising within the zones. In response to concerns about zone operations Congressman Cellar said, "[A foreign trade zone] is subject...to all the laws relating to public health, vessel inspection, postal service, labor condi-

⁴⁸ 174 Misc. 813, 21 N.Y.S.2d 943 (Sup. Ct. 1940), *aff'd per curiam*, 261 A.D. 1065, 26 N.Y.S.2d 704, *aff'd per curiam*, 286 N.Y. 658, 36 N.E.2d 696 (1941).

⁴⁹ *Id.* at 817-18, 21 N.Y.S.2d at 950-51.

⁵⁰ *Id.*

⁵¹ 387 F.2d 343 (5th Cir. 1967).

⁵² *Id.* at 344.

⁵³ *Id.*

tions, immigration, and indeed everything except the customs."⁵⁴ One can readily infer an intent on the part of the bill's sponsor, speaking in Congress, to continue the reach of federal law in foreign trade zones, and subsequent federal court decisions support the inference.

The application of federal patent laws to zone operations was examined in *G.D. Searle & Co. v. Byron Chemical Co.*,⁵⁵ which involved a patent dispute in which the defendant Byron admitted the validity of the plaintiff Searle's patent. Byron had bought the patented drug from a German company which shipped it to a foreign trade zone in New York. Byron subsequently placed the drug aboard a carrier for shipment to Japan. When Searle sued on the patent, defendant Byron argued that the transaction had occurred totally in foreign commerce and therefore was outside the reach of U.S. patent laws. Relying in part on the legislative history of the Foreign Trade Zones Act, the court rejected defendant's contentions and found applicable jurisdiction.⁵⁶ The court held that federal laws regulating business activity, including the U.S. patent law, apply with full force in a zone.

The *Searle* decision followed the previously decided but unreported case of *American Cynamid Co. v. Bolone*.⁵⁷ The defendant in *American Cynamid* had agreed to a decree enjoining further infringement on plaintiff's patent on the drug sulfadiozone. In an attempt to avoid the consent decree, the defendant imported sulfadiozone into a foreign trade zone for transshipment to foreign countries. The court held the defendant in contempt of the previous decree, further supporting the application of U.S. patent laws in a zone.

The Lanham Trademark Act⁵⁸ has also been held to apply in a zone. In *A.T. Cross Co. v. Sunil Trading Corp.*,⁵⁹ Sunil imported bogus Cross pens into a zone with the intention to transship them for sale in the Canary Islands. By bringing the pens into a zone, Sunil could avoid customs duties and legally stamp the pens "Made in U.S.A.," increasing their resemblance to legitimate Cross pens. In a federal trademark action brought by Cross, Sunil asserted lack of subject matter jurisdiction as a defense.⁶⁰

The court rejected Sunil's argument and found jurisdiction over the cause of action, granting Cross's request for a preliminary injunction. The court construed congressional intent to render the Lanham Act's jurisdictional predicates coextensive with those of the Commerce Clause.⁶¹ As such, the Act would reach not only interstate commerce but

⁵⁴ 78 CONG. REC. 9853 (1934).

⁵⁵ 223 F. Supp. 172 (E.D.N.Y. 1963).

⁵⁶ *Id.* at 174.

⁵⁷ No. 992-60 (C.D.N.J. April 18, 1962).

⁵⁸ 15 U.S.C. §§ 1051-1127 (1976 & Supp. V 1981).

⁵⁹ 467 F. Supp. 47 (S.D.N.Y. 1979).

⁶⁰ *Id.* at 48-49.

⁶¹ *Id.* at 51. See U.S. CONST., art. I, § 8, cl. 3.

also foreign commerce. In construing the jurisdictional provisions of the Foreign Trade Zones Act, the court made the following analysis:

There is absolutely no indication in the Foreign Trade Zones Act that Congress ever intended to exclude goods therein from regulation under United States laws by the Federal Courts. Indeed, the totality of the evidence indicates the contrary

Consequently, since the Commerce Clause extends into the foreign trade zone, and the jurisdictional reach of the Lanham Act is coextensive therewith, the only possible conclusion is that, absent an express repudiation of federal jurisdiction (which is not contained in the Foreign Trade Zone Act), the jurisdictional parameters of the Lanham Act reach within the foreign trade zone.⁶²

The idea that federal acts with jurisdictional parameters coextensive with the Commerce Clause reach into foreign trade zones was previously applied in *United States v. Yaron Laboratories, Inc.*⁶³ In *Yaron*, the Food and Drug Administration's (FDA) administrative powers were at issue. Yaron Labs processed raw materials from Italy into the drug PAX in a foreign trade zone, and reexported the drug. PAX had neither been filed with, nor approved by, the FDA.⁶⁴ Upon examination of the FDA's enabling legislation, the court held that federal jurisdiction in a zone existed under the Pure Food and Drug Act.⁶⁵ The court found that the jurisdiction conferred was coextensive with the congressional power under the Commerce Clause and, therefore, extended to both interstate and foreign commerce.⁶⁶

The lack of a jurisdictional predicate fully coextensive with the Commerce Clause was fatal to the government's case in *United States v. Prock*.⁶⁷ Prior to the effective date of Texas anti-gaming laws, defendant sent slot machines from Texas to a foreign trade zone in New Orleans. Federal authorities arrested him on a charge of violating the federal law prohibiting interstate shipment of gaming devices.⁶⁸

At trial, the district court sustained the defendant's motion for acquittal, noting that the statute prohibited only interstate transport of gaming machines. The market was not in interstate commerce, but in foreign commerce, as the slot machines went to a foreign trade zone. The court held that only transfer from a place in one state to a place in another state or in the District of Columbia qualifies as interstate transportation.⁶⁹ The *Prock* opinion suggests that a zone is not a "place in another State," but a foreign outpost for the purposes of the law regulating interstate commerce. More importantly, the opinion demonstrates

⁶² *Sunil*, 467 F. Supp. at 51.

⁶³ 365 F. Supp. 917 (N.D. Cal. 1972).

⁶⁴ *Id.* at 919.

⁶⁵ See 21 U.S.C. § 332(a) (1976).

⁶⁶ *Yaron*, 365 F. Supp. at 919-20.

⁶⁷ 105 F. Supp. 263 (S.D. Tex. 1952).

⁶⁸ *Id.* at 264. See 15 U.S.C. §§ 1171, 1175 (1976).

⁶⁹ *Prock*, 105 F. Supp. at 264.

that an act which regulates only interstate commerce does not apply in a foreign trade zone.

The preceding decisions illustrate a dichotomy in the applicability of federal acts to zone operations. Those acts providing for jurisdiction over foreign commerce apply in foreign trade zones, and those where jurisdiction is limited to interstate commerce do not apply. Acts which regulate business activity regardless of whether the market is in interstate or foreign commerce, and acts which regulate activities regardless of the commercial output will operate in zones. Those acts which are limited to regulation or prohibition of actions solely in interstate commerce probably do not apply in foreign trade zones.

This dichotomy is in harmony with the purposes behind foreign trade zones. A major reason for the existence of zones is to encourage the use of American facilities in the reexport and transshipment of trade.⁷⁰ Clearly, this trade is almost exclusively in foreign commerce. To regulate such commerce by laws aimed at domestic interstate commerce would weaken the incentives provided by the Act. Trade between a domestic point and a foreign trade zone should also be considered not to be in interstate commerce for jurisdictional purposes. A zone, in many cases, merely acts as a stopping-off point for goods to be exported from a domestic point. Congress intended to encourage such zone utilization through the Act, in order to increase the use of American facilities and labor. Subjecting goods transferred to a zone to all laws regulating interstate commerce would restrain such zone use and weaken the Act's potential. A foreign trade zone is designed to encourage business entities engaged in foreign commerce.⁷¹ In consonance with that design, only federal laws reaching foreign commerce should reach foreign trade zones.

The idea that foreign trade zone activities are part of foreign commerce has also been used offensively to give rise to federal jurisdiction over traditional state functions in limited circumstances. In *United States v. Yoppolo*,⁷² defendants appealed their conviction for theft of scotch which was being transported from Glasgow, Scotland to Cincinnati. The scotch was stolen from a trader in a Toledo, Ohio foreign trade zone. On appeal, the defendants argued that their convictions in federal district court were invalid due to a lack of jurisdiction.⁷³ The Sixth Circuit disagreed, finding federal jurisdiction as the goods were still moving in foreign commerce. The goods thus were still subject to federal regulation exclusively, and federal courts had the power to enforce criminal sanctions.⁷⁴

The *Yoppolo* holding appears to establish a basis for federal jurisdic-

⁷⁰ See SENATE REPORT, *supra* note 4.

⁷¹ See *id.* at 1.

⁷² 435 F.2d 625 (6th Cir. 1970).

⁷³ *Id.* at 626.

⁷⁴ *Id.*

tion whenever merchandise is stolen from a foreign trade zone. As the previous decisions dealing with the reach of federal acts into zones make clear, zone activities are considered to be in foreign commerce. Therefore, theft of merchandise from a zone would appear to be the theft of goods in foreign commerce.

A look at the jurisdictional parameters of specific federal statutes should give a relatively clear picture of which statutes apply in foreign trade zones. For example, given the jurisdictional rationale behind the earlier cases, the National Labor Relations Act (NLRA)⁷⁵ should apply in foreign trade zones. Because the NLRA applies to corporations acting in foreign commerce,⁷⁶ it probably grants federal jurisdiction over labor matters arising in zones.

A foreign trade zone operator should be able to determine which statutes apply to zone operations. The jurisdictional reach of federal statutes eliminates the possibility of conducting activities in a zone which generally would be prohibited under federal law.⁷⁷ A zone operator, however, is probably not subject to federal acts which regulate only interstate commerce. This dichotomy, although somewhat cumbersome, adds predictability to zone operation and, by doing so, should reduce some of the present business uncertainty about zone usage.

C. State Jurisdiction

With the rejection of a foreign trade zone as a "federal enclave," zones became subject to concurrent state and federal jurisdiction. The limits of state jurisdiction are somewhat unclear. Indeed, one of the basic uncertainties about zone operations involves the question of state power in zones. Certain basic parameters can be discerned, however.

In *During v. Valente*,⁷⁸ a New York court held that a state does not have the power to regulate commercial activity in a foreign trade zone. *Valente*, a breach of contract action, is the only reported decision on this issue. In *Valente* the plaintiff alleged that the defendant had employed and authorized him to sell foreign liquor stored in a zone, and that the plaintiff had procured a buyer. The defendant, however, refused to carry out the sale.⁷⁹ At trial, the court upheld the defendant's motion to dismiss on the grounds that the complaint failed to allege plaintiff had a solicitor's permit as required by New York alcoholic beverage laws.⁸⁰

The New York appellate court reversed the lower court ruling and

⁷⁵ 29 U.S.C. §§ 151-169 (1976 & Supp. V 1981).

⁷⁶ *Id.* § 152(6) (1976).

⁷⁷ For example, a zone could not be used to evade the requirements of federal securities laws, because the jurisdictional reach of these laws is coextensive with the Commerce Clause. *See, e.g.*, Securities Act of 1933, § 2(7), 15 U.S.C. § 77b(7) (1976).

⁷⁸ 267 A.D. 383, 46 N.Y.S.2d 385 (1944).

⁷⁹ *Id.* at ___, 46 N.Y.S.2d at 386-87.

⁸⁰ *During v. Valente*, __ Misc. ___, 42 N.Y.S.2d 11 (1943). *See* N.Y. ALCO. BEV. CONT. LAW § 93 (McKinney 1970).

held for plaintiff. The court observed that a local zone was established through the exclusive and plenary power of Congress to regulate commerce with foreign nations. Imposition of a complicated set of state liquor regulations was held not only to interfere with the exclusive control of Congress over foreign commerce, but also to seriously impair, if not defeat, the purposes for which trade zones were established. Mere importation and geographical location of the goods within New York State in a zone was held not to constitute importation into the state. The sale of the goods was therefore not subject to state regulation.⁸¹

In the years since the *Valente* decision, no court has questioned its holding. Indeed, *Valente* is regularly cited for the proposition that foreign trade zones were created through the plenary power of Congress over foreign commerce.⁸² Therefore, it seems well-established that state regulatory encroachment into zones would be impermissible as an attempt to regulate foreign commerce. State regulation would also defeat the purposes of foreign trade zones. Companies involved in reexport and transshipment activities would be severely shackled if forced to comply with the state regulations, and the encouragement of the use of American labor and facilities in foreign commerce intended through zone authorizations would be severely hampered if such zones were subject to the vagaries of local regulation.

State legislation does directly affect applications for foreign trade zone operations. The Foreign Trade Zones Act delineates certain limited situations where an act of the state legislature is required before the Board can accept an application.⁸³ Further, the Act states that a zone may be operated by a public or private corporation,⁸⁴ with preference given to public corporations.⁸⁵ States play an integral role in the process by defining public corporations, and by designating which public and private corporations are authorized to make a zone application. States designate appropriate applicants in a variety of ways; most often by specifying which public corporations may apply.

State definitions of a "public corporation" vary greatly, with some state definitions as broad as that in the Act itself.⁸⁶ Others define "pub-

⁸¹ *Valente*, 267 A.D. at ___, 46 N.Y.S.2d at 387.

⁸² See, e.g., *A.T. Cross Co. v. Sunil Trading Corp.*, 467 F. Supp. 47, 50-51 (S.D.N.Y. 1979).

⁸³ See 19 U.S.C. § 81b(d) (1976). State legislation is required whenever a state contains two types of ports of entry, one where harbor facilities are controlled by the state and the other with facilities controlled by a municipality. This provision evidently was intended to deny states an advantage over municipalities. While a state could make an application for a zone at its port of entry at once, a municipality might be forced to approach the state legislature for bonding authority. This section puts both entities on the same time footing by requiring a state legislative act. This issue is beyond the jurisdictional purview of our present discussion, and will not be discussed further. For an in-depth look at this provision and the situations where state legislative action is required see *Atkins, Doyle & Schwidetzky, supra* note 13.

⁸⁴ 19 U.S.C. §§ 81a(d), 81b(c) (1976).

⁸⁵ *Id.* § 81b(c).

⁸⁶ *Id.* § 81a(e).

lic corporation" in terms of a particular government entity. The Virginia foreign trade zone statute illustrates the former, less restricted definition:

The term "public corporation" for the purposes of this chapter, means the State of Virginia or any political subdivision thereof or any incorporated municipality therein or any public agency of this State or of any political subdivision thereof or of any municipality therein, or any corporate municipal instrumentality of this State or of the State and one or more States.⁸⁷

The Louisiana foreign trade zone statute is typical of a more restrictive definition of a public corporation for zone application purposes, stating: "The [Board of Commissioners of the Port Districts] may make application to the Secretary of Commerce for the purpose of establishing, opening and maintaining foreign trade zones. . . ."⁸⁸ Michigan uses the presence or absence of public funding as the criterion for determining which public entities may apply.⁸⁹

Many states also define those private corporations which may apply for a zone grant. Statutes range from total exclusion of private applicants to statutes allowing almost any private corporation to apply. An example of the exclusionary approach is that of Hawaii.⁹⁰ Considering the Act's specific preference for public corporations,⁹¹ this approach may appear more realistic. Given the time and political constraints on state and local governments, however, more efficient use of the zone concept could come from private corporations. A public corporation operating in a zone may compete for funds with other governmental entities, such as school districts, thereby hampering efficient operation of the zone. Although the Act requires a private corporation operating a zone to operate as a public utility,⁹² the profit motive could easily act as an impetus to use the zone and encourage more efficient business practices in zone administration.

Some states have recognized the problem of governmental inertia and allow private corporations to apply. Many states authorize private corporations expressly organized for zone operation. For example, the New Jersey statute states: "Corporations may be organized in this State for the purpose of establishing, operating and maintaining foreign trade

⁸⁷ VA. CODE ANN. §§ 62.1-159 (1982). California also defines "public corporation" in the broadest possible terms. See CAL. GOV'T CODE § 6300 (West 1980).

⁸⁸ LA. REV. STAT. § 51:62 (Supp. 1983).

⁸⁹ The Michigan statute reads, in pertinent part: "'Public corporation' means the state, or any county, township, city or village within the state, or any State or municipal authority or similar organization financed in whole or part by public funds." MICH. COMP. LAWS ANN. § 21.302(1)(b) (1967).

⁹⁰ See HAWAII REV. STAT. §§ 212-2 to -3 (1976). Section 212-2 defines a "public corporation" as "the state of Hawaii, any political subdivision thereof, and municipality therein, or any public agency of the state." Section 212-3 limits applicants for foreign trade zones to "any public corporation which is duly designated and approved by the governor."

⁹¹ 19 U.S.C. § 81b(c) (1976).

⁹² *Id.* § 81n (1976).

zones. . . .⁹³ Georgia has a similar provision.⁹⁴ These statutes allow for private operation, but are not as helpful as possible. By requiring the establishment of a separate corporation for zone operation, the element of governmental inertia is reinstated.

Still other states have adopted a broader approach and allow basically all private corporations to apply for zone status. A typical statute is that of Delaware, which provides: "All public and private corporations shall have the power to apply to the proper authorities of the United States government for a grant, and when such a grant is issued, to establish and operate foreign trade zones. . . ."⁹⁵ Arizona embraces this approach and also provides that public and private corporations may combine to operate a zone.⁹⁶ By allowing free private access to the zone, these states have encouraged utilization of the zone concept. Some would argue that this approach goes too far, as private corporations would have no incentive to operate in the public interest.

As a compromise system, a state could provide by statute for a contractual relation whereby a public corporation acts as a grantee and contracts with a private corporation to operate a zone at the latter's expense. While the Act clearly states that "the grant shall not be sold, conveyed, transferred, set over nor assigned,"⁹⁷ the early case of *American Dock Co. v. City of New York*⁹⁸ acknowledged the validity of such a contractual relation. The Washington State statutory scheme uses this compromise approach:

A city or town, as a zone sponsor, may apply to the United States for permission to establish, operate and maintain foreign trade zones: *Provided*, that nothing herewith shall be construed to prevent these zones from being operated and financed by private corporation(s) on behalf of a city or town as zone sponsor.⁹⁹

The compromise approach appears to be the most efficient. It combines the business expertise and profit motive of a private corporation with the public concern of a governmental entity. While the approach does not eliminate the problem of government inertia, the added presence of a private organization urging governmental action could lessen the problem. By using a contractual relationship between a public corporation grantee and a private corporation operator, a foreign trade zone can be operated more efficiently, and with an eye toward protecting the public interest.

For a business interested in operating and maintaining a foreign trade zone, a statutory scheme allowing private zone operation can rep-

⁹³ N.J. STAT. ANN. § 12:13-3 (West 1979).

⁹⁴ GA. STAT. ANN. § 52-10-3 (1981).

⁹⁵ DEL. CODE ANN. tit. 6, § 7502 (West Supp. 1982).

⁹⁶ See ARIZ. REV. STAT. ANN. § 44-6501 (West Supp. 1982).

⁹⁷ 19 U.S.C. § 81g (1976).

⁹⁸ 174 Misc. 813, 21 N.Y.S.2d 943 (1940), *aff'd per curiam*, 261 A.D. 1065, 26 N.Y.S.2d 704, *aff'd per curiam*, 286 N.Y. 658, 36 N.E.2d 696 (1941).

⁹⁹ WASH. REV. CODE ANN. § 35.21.850 (Supp. 1983).

resent a profitable opportunity. Private management could also be beneficial to the affected state, by lessening the problem of governmental inertia in the initial zone organization, and by providing greater flexibility to deal with changing business conditions. In turn, better management could encourage greater zone usage to the ultimate benefit of the state through greater utilization of its facilities and labor force.

To a business which seeks only to operate within a zone, state jurisdiction should provide little uncertainty. An operator would not be subject to state regulatory schemes, particularly regulations for licensing zone applicants. While the full limits of state jurisdiction are unclear, the lack of regulatory jurisdiction provides a boon. Operation in a foreign trade zone adds no state regulation and may result in avoiding state regulation in significant areas.

IV. Taxation

The most significant unsettled issue of state and federal jurisdiction over foreign trade zones is that of the validity of state *ad valorem* personal property taxation of zone merchandise. The existence of state and local taxation of zone goods could provide a powerful disincentive to a businessman wishing to begin zone operation. At this time no clear answer exists as to the validity of such taxation, but recent decisions have opened up this area for comment.

A recent set of cases dealt with the issue of state taxation over imports, although not in the context of a foreign trade zone. The Supreme Court considered this issue in *Michelin Tire Corp. v. Wages*,¹⁰⁰ where state *ad valorem* personal property taxes were assessed against Michelin by a county in Georgia on tires imported from France and Nova Scotia. Michelin brought a federal action seeking to have the tax invalidated as an "impost or duty" in violation of the Import/Export Clause of the United States Constitution.¹⁰¹

The Supreme Court ruled that a nondiscriminatory *ad valorem* property tax is not prohibited as an unconstitutional impost or duty. The Court held that such property taxes are the method by which states apportion the cost of services among beneficiaries according to respective wealth, and that no reason exists to accord imported goods preferential treatment. The Court went on to state:

It is obvious that such nondiscriminatory property taxation can have no impact whatsoever on the Federal Government's exclusive regulation of foreign commerce, probably the most important purpose of the [Import/Export] Clause's prohibition. By definition, such a tax does not fall on imports as such because of their place of origin. It cannot be used to create special protective tariffs or particular preferences for certain domestic goods, and it cannot be applied selectively to encourage or discourage any importation in a manner inconsistent with federal

¹⁰⁰ 423 U.S. 276 (1976).

¹⁰¹ *Id.* at 278-79. See U.S. CONST. art. I, § 10, cl. 2.

regulation.¹⁰²

The Court in *Michelin* has shifted the focus of judicial analysis concerning the validity of state and local taxes on imported goods to the question of whether the tax in question discriminates based on the foreign origin of the goods, regardless of the status of the goods as imports. The Court seems to be indicating that a state or local tax on imported goods is permissible if nondiscriminatory. Should the rationale apply to foreign trade zones, a nondiscriminatory *ad valorem* personal property tax would appear permissible.

The *Michelin* approach was applied in *Zee Toys, Inc. v. County of Los Angeles*,¹⁰³ which dealt with imported goods in warehouses in much the same fact situation as in *Michelin*. The county had taxed plaintiff's goods which were manufactured outside the United States. Plaintiff taxpayer filed for a tax exemption under California statutes exempting goods brought through the state and transshipped outside the state.¹⁰⁴ The California court struck down this tax exemption, holding that selective exemption of foreign goods gives them a competitive advantage over intrastate goods. Such an exemption would be a regulation of interstate foreign commerce and thus a violation of the Import/Export Clause. The court went on to say that goods manufactured in a foreign country and imported are subject to *ad valorem* taxes under like conditions as interstate goods and tax discrimination is impermissible.¹⁰⁵

The point had also been raised in *American Smelting and Refining Co. v. County of Contra Costa*¹⁰⁶ in which the county assessed taxes against goods held in a bonded warehouse, a duty-free enclave.¹⁰⁷ The California Court of Appeals upheld the tax, saying congressional intent in authorizing bonded warehouses was to relieve the processor only of customs duties until goods enter United States customs territory, not to grant an exemption from state and local taxation. The case is of little value, however, when evaluating state taxation of goods in a foreign trade zone. The court specifically held the law regarding zones was not controlling and suggested the Foreign Trade Zones Act was a "broader statute" than the statute authorizing bonded warehouses.¹⁰⁸

In reliance on these cases, proponents have argued that nondiscriminatory taxation of zone merchandise is permissible.¹⁰⁹ However, it is im-

¹⁰² *Michelin*, 423 U.S. at 286.

¹⁰³ 85 Cal. App. 3d 763, 149 Cal. Rptr. 750 (1978), *aff'd sub nom.* Sears, Roebuck & Co. v. County of Los Angeles, 449 U.S. 1119 (1981).

¹⁰⁴ *Zee Toys*, 85 Cal. App. 3d at 767-769, 149 Cal. Rptr. at 752-54.

¹⁰⁵ *Id.* at 772-77, 149 Cal. Rptr. at 756-59.

¹⁰⁶ 271 Cal. App. 2d 437, 77 Cal. Rptr. 570 (1969), *cert. denied*, 396 U.S. 273 (1970).

¹⁰⁷ *See generally* 14 U.S.C. § 1555 (1976) (authorizing bonded warehouses).

¹⁰⁸ *American Smelting*, 271 Cal. App. at ___, 77 Cal. Rptr. at 599.

¹⁰⁹ *See, e.g.*, Note, *North Carolina Foreign-Trade Zones: Problems & Perspectives*, 5 N.C.J. INT'L L. & COM. REG. 521, 525-28 (1980). Because nontaxation of zone merchandise gives imported goods a competitive advantage over domestic goods, state refusal to tax zone merchandise could arguably be unconstitutional as an infringement upon Congress' sole authority to regulate foreign commerce. *See* U.S. CONST., art. I, § 8, cl. 3; Note, *supra*, at 526-28.

portant to note that none of the cases dealt with goods in a foreign trade zone. It is difficult to conceive of a state personal property tax which would not be discriminatory towards the foreign origin of zone goods. Most zone goods would not be within the physical boundaries of a state were it not for the existence of a foreign trade zone. This is particularly true of goods in the transshipment and reexport trade. To levy state and local personal property taxes against such goods would be to levy taxes on goods due to their foreign origin, and could not be termed nondiscriminatory.

Also, the previously mentioned cases did not deal with the usual zone situation of goods in foreign commerce. In all of the cases, the taxed goods had come to rest in a particular state and were destined for interstate commerce. As discussed earlier, federal statutes regulating only interstate commerce do not generally apply to zone activities.¹¹⁰ In *Michelin* the state tax was held applicable to imported goods which were destined for interstate commerce. The distinction between interstate and foreign commerce weakens the precedential effect of *Michelin* where zone merchandise is involved.

A stronger argument for the lack of state tax jurisdiction in foreign trade zones revolves around the Commerce Clause.¹¹¹ If goods in a foreign trade zone are in foreign commerce, state taxation may conflict with the plenary power of Congress over foreign commerce, and hence may be unconstitutional. The Import/Export Clause and the Commerce Clause are not coterminous in scope,¹¹² and taxation which does not violate the former could violate the latter. Thus, even if the Import/Export Clause does not bar state and local taxation after *Michelin*,¹¹³ the Commerce Clause could still prohibit such taxation.

The Commerce Clause was raised against state taxation in *McGoldrick v. Gulf Oil Corp.*,¹¹⁴ in which the state of New York attempted to impose taxes on fuel oil in a bonded warehouse. Gulf imported the oil from foreign sources and sold it to ships for consumption as fuel in foreign commerce.¹¹⁵ The Supreme Court held the tax violated the Commerce Clause. By authorizing bonded warehouses, Congress was held to have intended to confer a competitive advantage for those using such warehouses in foreign commerce. The question then became whether the tax conflicted with this congressional policy. The Court held that it was evi-

¹¹⁰ See *supra* notes 67-69 and accompanying text.

¹¹¹ U.S. CONST., art. I, § 10, cl. 3.

¹¹² See *Richfield Oil Corp. v. State Board of Equalization*, 329 U.S. 69 (1946). The Court here explained that the invalidity of a state tax under the Import/Export Clause derives from the prohibition of state taxes on imports or exports, while the invalidity of a state tax under the Commerce Clause does not turn on whether the article taxed was or ever has been an import or export. The Court further noted that the Commerce Clause is not cast as a tax prohibition, but rather as a power on the part of Congress to regulate commerce.

¹¹³ 423 U.S. 276 (1976).

¹¹⁴ 309 U.S. 414 (1940).

¹¹⁵ *Id.* at 422.

dent this purpose would fail if the states were free, at any stage of the transaction, to impose a tax which would lessen this competitive advantage. The congressional regulation, read in light of its purpose, was held tantamount to a declaration that this oil was not to become part of the common mass of taxable property within the state, and therefore was not subject to state taxation.¹¹⁶ The state tax thus had to fail as an infringement on congressional regulation of commerce. While *McGoldrick* dealt only with goods intended for reexport, the previously discussed decision in *During v. Valente*¹¹⁷ considered all zone goods part of foreign commerce.

Taken together, these decisions stand loosely for the proposition that state or local taxation must fail if it thwarts a legislatively expressed congressional policy regarding commerce. The Foreign Trade Zones Act represents such a policy. The Act is designed to encourage the use of American labor and facilities in foreign commerce, an area exclusively reserved to Congress. To allow state and local taxation of zone merchandise would thwart this objective by raising costs to business, whether the zone goods are destined for reexport or for eventual importation. Congress certainly could have distinguished between these two categories of merchandise when enacting the Foreign Trade Zones Act, but chose not to do so, which suggests that Congress sought to encourage foreign commerce in zones regardless of the ultimate destination of the goods. By authorizing zones, Congress expressed a clear policy in favor of certain foreign commerce.

State taxation also conflicts with the desire of Congress to simplify matters through the Foreign Trade Zones Act.¹¹⁸ Bonded warehouses and drawback provisions,¹¹⁹ providing the same duty-free status as zones, never received great usage due to their complexity. Recognizing the failure of these provisions, Congress adopted the new simpler format of foreign trade zones. State taxation would complicate zone usage, both in terms of accounting and in terms of the varying taxation of the several states.

North Carolina has exempted foreign trade zones from *ad valorem* personal property taxation by amending the 1975 Act authorizing the establishment of foreign trade zones in the state.¹²⁰ The amendment accomplished two desirable ends. First, it made North Carolina foreign

¹¹⁶ *Id.* at 429.

¹¹⁷ 267 A.D. 383, 46 N.Y.S.2d 385 (1944). *See supra* text accompanying notes 78-81.

¹¹⁸ The complexity of the drawback system and the bonded warehouse were major factors in the passage of the Act. *See* 78 CONG. REC. 9853 (1934) (remarks by Rep. Celler discussing the "irksome provisions" of using a bonded warehouse).

¹¹⁹ Drawback provisions allow the reimbursement of up to 94% of customs duties paid on goods reexported or transshipped in foreign commerce. *See* 19 U.S.C. § 1313 (1976 & Supp. V 1981).

¹²⁰ *See* Act of June 28, 1977, 1977 N.C. Sess. Laws 782 (codified at N.C. GEN. STAT. §§ 55C-4, 105-275(23) (1982)) (amending North Carolina Foreign Trade Zone Act, 1975 N.C. Sess. Laws 983 (codified at N.C. GEN. STAT. §§ 55C-1 to -4 (1982))).

trade zones more attractive to business through relief from personal property taxes.¹²¹ Second, the amendment removed a major point of uncertainty for prospective zone operators,¹²² thus eliminating one of the main causes for companies foregoing zone operation. North Carolina has led the way in this area.

There has been no clear, judicial expression on the issue of the validity of state and local taxation of merchandise held in a foreign trade zone. Such taxation is arguably no longer prohibited by the Import/Export Clause after *Michelin*. However, such a result is not mandated by *Michelin* and significant distinctions exist between the *Michelin* situation and foreign trade zones. In any event, the Commerce Clause looms as a serious obstacle to state and local taxation of zone goods. If the Foreign Trade Zones Act is held to reflect a congressional policy regarding foreign commerce, state taxation would conflict with this policy. As a hindrance to a legislatively expressed congressional policy, state taxation would be considered unconstitutional. Persuasive policy reasons also exist in opposition to the imposition of *ad valorem* personal property taxes.

The best way to alleviate the uncertainty surrounding the taxation issue is for states to follow the lead of North Carolina and expressly evidence an intent not to assess *ad valorem* taxes against zone merchandise. In this era of tightening state budgets, such a move could be politically unpopular. However, by eschewing this taxation, states would encourage zone usage and possibly increase employment and tax revenues from zone employees' wages and personal expenditures. The purposes of the Foreign Trade Zones Act also would thus be encouraged.

V. Conclusion

A modicum of uncertainty about jurisdiction in a foreign trade zone remains. The uncertainty is minor, however, when compared with the advantages gained by operation in a zone. Zone usage is on the increase and deservedly so. Few other business locations offer the advantages inherent in a foreign trade zone, particularly to a businessman involved in the export-import trade, or one manufacturing from imported raw materials. With some semblance of order to the jurisdictional issues surrounding foreign trade zones, zone usage should increase, leading to a fuller utilization of the zone concept.

¹²¹ See Note, *supra* note 109, at 526.

¹²² *Id.* The amendment removed the constitutional cloud surrounding the original act by exempting zone merchandise from personal property taxes, thus avoiding the question whether zone merchandise could constitutionally be subject to the tax. See N.C. GEN. STAT. § 105-273(23) (1982).