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FTZ Board Proposes Significant Revisions to Foreign Trade Zones Regulations

Introduction

The Foreign Trade Zones (FTZ) Board recently issued a [notice of proposed rulemaking](#) which proposes a major overhaul in the substantive and procedural rules (15 CFR Part 400) for the authorization of Foreign Trade Zones (FTZs) and the regulation of activity that occurs inside those zones. Key revisions in the proposed rule pertain to activities in FTZs in which an imported component is combined with one or more other components to create a different finished product, as well as expedited access to FTZ benefits for U.S. manufacturers for export-oriented activity.

A summary of the key provisions of the proposed rule which will likely have an impact of U.S. importers and exporters follows below:

- “Production” term would replace current manufacturing and processing categories – In the proposed rule, the FTZ Board recognizes that the current FTZ regulations divide activity into two categories – “manufacturing” or “processing”, depending on whether the activity involves “substantial transformation” of the component – and apply procedures that can differ between the two categories. Under the current regulations, manufacturing involves a substantial transformation of the component, while processing involves a change in customs classification or in its eligibility for entry (that does not amount to a substantial transformation). The proposed rule would eliminate these two categories and instead apply a unified

concept of “production” with a single set of procedures pertaining to that type of activity. The FTZ Board proposes defining “production” activity as “any activity which results in a change in the customs classification of an article or in its eligibility for entry for consumption; regardless of whether U.S. customs entry actually is made on the article resulting from the production activity.” The proposed rule would make a universal change to the regulations and provide a single set of procedures pertaining to production activity.

- Approval No Longer Required for Most Export Manufacturing – The proposed rule would eliminate the general advance approval requirement for most export manufacturing. Advance approval from the FZ Board would be limited to situations in which a production input is subject to an antidumping/countervailing (AD/CVD) duty order, a Section 337 order, or quantitative restriction (quota).
- Approval Required for U.S. Market Goods if Potential Adverse Impacts – The proposed rule would limit the general advance approval process to specific types of FTZ benefits that could potentially impact other domestic manufacturers:
 - Tariff inversion - if a lower U.S. duty rate will be applied to the component through its incorporation into a downstream product in the FTZ);
 - AD/CVD duties or quotas – if a foreign article would be subject to an

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antidumping or countervailing duty order (AD/CVD) or otherwise would be subject to suspension of liquidation under AD/CVD duty procedures under an order of the International Trade Commission under Section 337 or under quota; or

- Certain scrap or waste – duty avoidance on scrap or waste resulting from the production activity.

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- “Public Utility” Requirements Proposed for FTZs, Including Fee Rates

– The proposed rule would establish specific standards for compliance with the statutory requirement that any organization licensed by the FTZ Board to serve a particular region is operating the zone as a public utility. For example, any rate or charge (fee) imposed on zone participants must be based on costs incurred by the grantee and would need to

be directly related to the service provided by the grantee (for which the rate or charge recovers costs incurred) to the zone participants. Rates or charges could incorporate a reasonable return on investment, but could not be tied to the level of benefits derived by zone participants. The FTZ Board recognizes that some grantees’ existing business arrangements may not comply with the proposed public utility requirements. Thus, the FTZ Board is proposed that the effective date for compliance with such requirements be delayed for up to two years after the date of publication of the final rule.

- Uniform Treatment for Contracts to be Required for all Zone Users – The proposed rule includes uniform treatment requirements including :

- standard contractual provisions,
- agreements to be made in writing directly with the grantee,
- neutral evaluation criteria, and
- justification for differing treatment.

- Proposed Rule Implements Statutory Authority for Fines and Penalties – The current FTZ regulations contain no provisions pertaining to statutory fining authority. The proposed regulations would authorize fines for certain violations of not more than \$1,000 for each day which a violation continues constituting a separate offense. Parties that could be fined include the zone operator, grantee or agent of the grantee. Proposed offenses include:

- failure to request advance approval or notification for each finished product or foreign component when required; or
- production involving any finished product, foreign component, or combination thereof authorized by

the FTZ Board at a level exceeding the plant's authorized or notified capacity;

- failure to submit a complete and accurate annual report; or
- each day during which an agent of the grantee performs functions that are a conflict of interest.

The proposed rule would also authorize CBP to suspend activated status of a zone, if instructed, when a fine has not been paid within specified time period or if there is a repeated and willful failure to comply with a prohibition or restriction. The proposed rule contains a new provision allowing for the "prior disclosure" of violations of the FTZ Act or regulations.

The FTZ Board is soliciting comments from interested parties on the proposed new rule. All comments must be received on or before April 8, 2011. Please contact a Barnes/Richardson attorney with any questions or if you would like assistance in preparing comments for the FTZ Board.