UNC SCHOOL OF LAW

NORTH CAROLINA JOURNAL OF INTERNATIONAL LAW AND COMMERCIAL REGULATION

Volume 14 | Number 3 Article 7

Fall 1989

Nissan Motor Manufacturing Corp. v. United States: An Update in Foreign Trade Zone Law

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NOTES

Nissan Motor Manufacturing Corp. v. United States:[1] An Update in Foreign Trade Zone Law

A foreign trade zone is a special area within the United States designated to be outside U.S. customs territory.[2] As a result, foreign merchandise can be brought into a zone without payment of duty.[3] Foreign trade zones are authorized for general purposes such as assembling, repackaging, and storing foreign merchandise.[4] The Foreign Trade Zones Board, established pursuant to the Foreign Trade Zones Act of 1934,[5] governs the operation of foreign trade zones by public and private corporations. The zone operator leases space within a zone to various companies to conduct business.[6] A subzone, on the other hand, is an area independent of an established foreign trade zone that is authorized for a specific purpose, yet it retains zone benefits.[7] Subzone activity is typically carried on by a single

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[1] 693 F. Supp. 1183 (Ct. Int'l Trade 1988), *aff'd*, 884 F.2d 1375 (Fed. Cir. 1989). This Note examines the decision of the Court of International Trade. After this Note was ready for publication, the United States Court of Appeals for the Federal Circuit affirmed the holding and the reasoning of the Court of International Trade.

[2] 15 C.F.R. § 400.101 (1988). A "foreign trade zone" is defined as follows:

> [A]n isolated, enclosed, and policed area, operated as a public utility, in or adjacent to a port of entry, furnished with facilities for lading, unlading, handling, storing, manipulating, manufacturing, and exhibiting goods, and for reshipping them by land, water, or air. Any foreign and domestic merchandise, except such as is prohibited by law or such as the Board may order to be excluded as detrimental to the public interest, health, or safety may be brought into a zone without being subject to the customs laws of the United States governing the entry of goods or the payment of duty thereon . . . .

Id. The establishment of foreign trade zones is authorized pursuant to 19 U.S.C. § 81b(a) (1982). "The Board is authorized . . . to grant to corporations the privilege of establishing, operating, and maintaining foreign-trade zones in or adjacent to ports of entry under the jurisdiction of the United States." *Id.*

[3] 19 U.S.C. § 81c(a) (Supp. V 1987).

[4] *Id.*

[5] 19 U.S.C. §§ 81a-81u (1988).

[6] 19 U.S.C. § 81n (1982).

[7] 15 C.F.R. § 400.304 (1988).

> The establishment of a zone, or a sub-zone in an area separate from an exisitng zone, for one or more of the specialized purposes of storing, manipulating, manufacturing, or exhibiting goods, may be authorized if the Board finds that existing or authorized zones will not serve adequately the convenience of commerce with respect to the proposed purposes.

Id.

company.[8]

In *Nissan Motor Manufacturing Corp. v. U.S.*, the Court of International Trade addressed the question of whether machinery imported to produce merchandise within a subzone is subject to U. S. Customs duty.[9] In holding the production machinery dutiable, the court refused to extend previous case law[10] liberally interpreting the Foreign Trade Zones Act. This Note examines the extent to which the *Nissan* decision is inconsistent with previous foreign trade zone law and how it updates the limited case law by echoing current congressional antizone sentiment.

Statement of the Case

In 1981 the Metropolitan Nashville Port Authority applied to the Foreign Trade Zones Board (Board) for permission to establish a foreign trade subzone at Nissan's manufacturing plant in Smyrna, Tennessee. Pending Board approval, Nissan requested a ruling from the Customs Service (Customs) regarding duty on capital equipment to be imported for use in production within the subzone. Customs determined that the machinery was dutiable. Because of uncertainty on the part of Nissan as to which machinery it would ultimately use, assessment of duties was deferred until the machinery was actually installed and tested.[11]

After the Board approved the subzone application in 1982, Nissan imported over $116 million worth of machinery. The amount of duties assessed on the imported equipment exceeded $3 million. Nissan filed the machinery entries in 1983, and liquidated the entries as entered in 1986.[12] Customs denied the liquidations in 1987. In

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[8] deKieffer and Thompson, *Political and Policy Dimensions of Foreign Trade Zones: Expansion or the Beginning of the End?*, 18 VAND. J. TRANSNAT'L L. 481, 492 (1985).

[9] 693 F. Supp. 1183, 1184 (Ct. Int'l Trade 1988).

[10] *E.g.*, Hawaiian Indep. Ref. v. United States, 460 F. Supp. 1249 (Cust. Ct. 1978). The United States Customs Court is the predecessor of the United States Court of International Trade. In 1980, Congress amended 28 U.S.C. § 251 to change the name of the court from the United States Customs Court to the United States Court of International Trade. Customs Courts Act of 1980, Pub. L. No. 96-417, § 501(2), 94 Stat. 1742 (codified throughout chapter 11 of 28 U.S.C.).

[11] Nissan Motor Mfg. Corp. v. United States, 693 F. Supp. 1183, 1185 (Ct. Int'l Trade 1988).

[12] Liquidation is the "final computation or ascertainment of the duties . . . accruing on an entry." 19 C.F.R. § 159.1 (1988).

Nissan was attempting to avoid the payment of duty by treating the production equipment as "privileged foreign merchandise" within the meaning of 19 C.F.R. § 146.41 (1988). "Foreign merchandise which has not been manipulated or manufactured so as to effect a change in tariff classification will be given status as privileged foreign merchandise on proper application . . . ." *Id.* § 146.41(a). Duty on "privileged foreign merchandise" is determined or "liquidated" when the merchandise enters the zone. *Id.* § 146.65(a)(1). No duty is actually paid on privileged foreign merchandise, however, until the merchandise actually enters U.S. Customs territory. 19 U.S.C. § 81c(a) (Supp. V 1987). Thus, if the Nissan machinery had qualified as "privileged foreign merchandise," duty would have been liquidated when the equipment entered the subzone. Nissan would never have paid

response, Nissan initiated this action and moved for summary judgement requiring Customs to reliquidate the entries of production machinery and to refund the $3 million in duties. The Government moved for summary judgement affirming Customs' assessment of duty. The court granted the Government's motion, holding the production equipment dutiable.[13]

In reaching its conclusion, the court relied first on the statutory language of the Foreign Trade Zones Act providing that foreign merchandise may, without being subject to U.S. Customs laws, be brought into a foreign trade zone and may be "stored, sold, exhibited, broken up, repacked, assembled, distributed, sorted, graded, cleaned, mixed with foreign or domestic merchandise, or otherwise manipulated, or be manufactured except as otherwise provided in this chapter, and be exported, destroyed, or sent into customs territory of the United States . . . ."[14] The court found that the capital machinery in dispute was "actively used or intended to be used to produce motor vehicles."[15] The machinery, the court reasoned, was thus not used for one of the activities permitted by the Act. The court relied on the general rule of statutory construction that "the expression of one thing is the exclusion of the alternative."[16] Therefore, because the "exhaustive" list of activities permitted by the statute does not include installation and operation of production machinery, such machinery must be dutiable.

Next, the court relied on legislative history of a 1950 amendment to the Foreign Trade Zones Act stating that the amended proviso "would not authorize consumption of merchandise in a zone . . . without the payment of liquidated duties."[17] From this the court reasoned that use of production machinery is analogous to "consumption" and therefore not excluded from duty.[18]

The court also relied on a Customs Service Decision (CSD) on production machinery imported for use in another zone.[19] In that CSD, Customs relied both on Congress' rejection of proposals to permit entry of production equipment into zones free from duty and on the comprehensive nature of the section 81c(a) list of permitted activities to conclude that production equipment in a zone is

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any duty on the equipment, however, because Nissan had no intention of ever importing the equipment into U.S. Customs territory.

[13] *Nissan*, 693 F. Supp. at 1184.

[14] 19 U.S.C. § 81c(a) (Supp. V 1987).

[15] *Nissan*, 693 F. Supp. at 1186.

[16] *Id.*

[17] S. REP. No. 1107, 81st Cong., 2d Sess. (1949), *reprinted in* 1950 U. S. CODE CONG. SERVICE 2533, 2536.

[18] *Nissan*, 693 F. Supp. at 1186, 1188.

[19] C.S.D. 79-418, 13 Cust. B. & Dec. 1627 (1979). A Customs Service Decision is an administrative decision of the U.S. Customs Service.

dutiable.[20]

The court found further support for its conclusion in the legislative history of a 1984 amendment to the Foreign Trade Zones Act[21] stating that an exemption from duty under the Act as amended in 1950 "does not apply to machinery and equipment that is imported for use (for manufacturing and the like) within a foreign trade zone."[22] Although this amendment was enacted after the Nissan machinery entered the subzone, the court justified its reliance on the 1984 statement by noting that the statement refers to the Act as it existed at the time of the disputed entries.[23]

Nissan had relied on *Hawaiian Independent Refinery v. United States*[24] to argue that the machinery should be exempt from duty.[25] *Hawaiian* held that imported refined crude oil used as fuel within a subzone was exempt from duty. The *Nissan* court distinguished the Nissan situation from *Hawaiian*. Specifically, the *Nissan* court classified refined crude oil as "merchandise within the meaning of the Foreign Trade Zones Act."[26] The test the court used for determining what qualified as such merchandise was whether the article was used for one of the activities permitted in the section 81c(a) list. Based on this test, the court concluded that production equipment is not "merchandise within the meaning of the Foreign Trade Zones Act" because it does not comply with the comprehensive list of permissible uses for duty-free articles.[27]

Finally, the court asserted that as a matter of public policy Congress did not intend to place domestic manufacturers of production machinery at a competitive disadvantage to foreign manufacturers by allowing the foreign manufacturers to send equipment into foreign trade zones free from duty and undersell domestic manufacturers.[28] The court thus concluded that Congress could not have intended to

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[20] *Id.* at 1627-30.

[21] Foreign Trade Zone Act of 1930, ch. 590, 48 Stat. 998 (1934) (codified as amended at 19 U.S.C. §§ 81a-81u (1988)).

[22] S. REP. No. 308, 98th Cong., 1st Sess. 35, 36 (1983), *reprinted in* 1984 U.S. CODE CONG. & ADMIN NEWS 4910, 4945.

[23] *Nissan*, 693 F. Supp. at 1186.

[24] 460 F. Supp. 1249 (Cust. Ct. 1978).

[25] *See infra* notes 51-56 and accompanying text.

[26] *Nissan*, 693 F. Supp. at 1187.

[27] *Id.*

[28] *Id.* at 1187-1188. Before a foreign manufacturer can sell its goods in the United States, the manufacturer must pay a duty. The cost of this duty is added to the price of the goods when they are sold in the United States. Thus, duties have the effect of raising the price of foreign merchandise sold within the United States. By raising the price of foreign goods without similarly raising the price of domestic goods, duties give domestic manufacturers a cost advantage over foreign manufacturers. If foreign equipment was allowed to enter foreign trade zones exempt from duty, domestic equipment manufacturers would lose the competitive edge provided for them through duties. Thus, exempting foreign equipment entering a subzone from duty would put domestic manufacturers at a "competitive disadvantage" to foreign equipment manufacturers with respect to sales to companies operating in foreign trade zones or subzones.

nullify existing customs protection for domestic capital equipment manufacturers.[29]

Background

Congress first authorized foreign trade zones in the Foreign Trade Zones Act of 1934.[30] This act provided for the establishment of a Foreign Trade Zones Board[31] with authority to grant to private and public corporations the privilege of establishing and operating foreign trade zones in or adjacent to U.S. ports of entry.[32]

The idea of duty-free importation is neither peculiar to foreign trade zones nor did it originate with the 1934 Act. Free ports have existed since the days of Ancient Greece and Rome.[33] In the United States prior to 1934, duties on goods that were later re-exported could be avoided through the use of bonded warehouses[34] or refunded through a process known as drawback.[35] At the time of its enactment, the Foreign Trade Zones Act was viewed as a method of minimizing the procedural formalities involved with the use of bonded warehouses or drawback while still maintaining the benefits of these earlier procedures.[36]

The congressional purpose behind the Foreign Trade Zones Act was twofold. First, trade zones were intended to facilitate the re-export of foreign goods from the United States by exempting them from import duties.[37] Second, trade zones allow foreign goods into U.S. territory so that U.S. citizens can be involved in and financially

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[29] *Id.* The Government asserted an alternative argument that the Foreign Trade Zones Board conditioned the grant of Nissan's subzone on an implicit promise in the subzone application to pay duty on the production machinery. Similarly, the Government argued that Nissan waived its right to challenge Customs' entry requirement by paying the assessed duties. The court rejected these arguments as unfounded. *Id.* at 1189.

[30] Foreign Trade Zones Act of 1934, ch. 590, 48 Stat. 998 (codified as amended at 19 U.S.C. §§ 81a-81u (1988)).

[31] The Board consists of the Secretaries of Commerce, Treasury, and the Army. 19 U.S.C. § 81a(b) (1982).

[32] 19 U.S.C. § 81b(a) (1982).

[33] Jayawardena, *Free Trade Zones*, 17 J. WORLD TRADE L. 427, 427 (1983). The purpose of these early free ports was to promote trade. *Id.*

[34] 19 U.S.C. § 1555 (1982). Bonded warehouses are designated structures within the United States into which foreign merchandise may be brought without the payment of duty. The merchandise can be imported from the bonded warehouse into U.S. Customs territory upon payment of duty or it can be exported to a foreign country without ever being subject to duty. *Id.* § 1555(a).

[35] 19 U.S.C. § 1313 (1982). Drawback is the refund, upon exportation, of a duty assessed or collected on foreign merchandise when it entered the United States. *Id.*; 19 C.F.R. § 191.2(a) (1988). *See also* deKieffer and Thompson, *supra* note 8, at 485-86 & n.14.

[36] In 1934, Secretary of Commerce Daniel C. Roper described the Act as "little more than the minimizing of the official limitations and costs involved in the formalities of entry into bonded warehouses and drawback." H.R. Rep. No. 1521, 73d Cong., 2d Sess. 3, 4 (1934) (excerpt from letter by Secretary Roper).

[37] *See* A. T. Cross Co. v. Sunil Trading Corp., 467 F. Supp. 47, 50 (S.D.N.Y. 1979). Foreign trade through these transshipment centers is facilitated by the elimination of duties unless and until foreign merchandise is imported into U.S. Customs territory. Bader,

profit from breaking down, repackaging, and relabelling such goods.[38] A foreign trade zone is not designed to be a profit-making venture for its sponsor.[39] Instead, it is to be operated as a public utility—available uniformly to all who apply for its use—to provide economic benefit to the local and national economies by encouraging transshipment trade.[40]

The 1934 Act did not permit manufacturing within foreign trade zones because of congressional concern that such activity might adversely affect domestic industry.[41] As originally intended, foreign trade zones served for many years primarily as transshipment centers for foreign merchandise. As trade zone use increased in the late 1940s,[42] however, Congress became concerned with the inconsistency of permitting "manipulation" within zones while disallowing "manufacture."[43] In 1950, Congress passed the Boggs Amendment, allowing "manufacturing" within zones, to correct this discrepancy.[44] The Boggs Amendment was intended to be a mere technical clarification as opposed to a substantive change.[45] Extensive manufacturing within zones was not expected because the high cost of land within zones would make large scale manufacturing prohibitively expensive.[46]

The Foreign Trade Zones Board removed this natural limit on zone manufacturing in 1952, however, when it authorized "zones for specialized purposes."[47] This regulation authorized the establishment of special purpose zones or subzones if existing trade zones did not adequately serve the "convenience of commerce" with respect to the subzone's proposed use.[48] Because a subzone is generally used by a single firm, the practical effect of authorizing subzones was to

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Jurisdictional Uncertainty: The American Foreign Trade Zone, 8 N.C.J. INT'L L. & COM. REG. 239, 240 (1983).

[38] *A. T. Cross*, 467 F. Supp. at 50.

[39] Note, *Foreign-Trade Zones: "Everything Except the Customs"?*, 31 U. FLA. L. REV. 725, 736 (1979).

[40] 19 U.S.C. § 81n (1982). "Each zone shall be operated as a public utility . . . and the grantee [zone operator] shall afford to all who may apply for the use of the zone and its facilities and appurtenances uniform treatment under like conditions . . . ." *Id.* *See* Note, *supra* note 39, at 736.

[41] S. REP. No. 905, 73d Cong., 2d Sess. 2, 3 (1934); *see also* Note, *U.S. Foreign Trade Zone Manufacturing and Assembly: Overview and Update*, 13 LAW & POL'Y INT'L BUS. 339, 343 (1981).

[42] For a summary of the historical development of foreign trade zone law and use during the 1930s, 1940s, and 1950s, see Note, *Foreign-Trade Zone Manufacturing: The Emergence of a Free Trade Instrument*, 9 VA. J. INT'L L. 444, 448-55 (1969).

[43] *See* Note, *supra* note 41, at 343.

[44] Act of June 17, 1950 (Boggs Amendment), ch. 296 § 1, Pub. L. No. 81-566, 64 Stat. 246 (codified at 19 U.S.C. § 81c(a) (Supp. V 1987)).

[45] Note, *supra* note 41, at 344.

[46] deKieffer and Thompson, *supra* note 8, at 490.

[47] Foreign Trade Zones Board Order No. 29, 17 Fed. Reg. 5316 (1952) (codified at 15 C.F.R. § 400.304 (1988)).

[48] *Id.*

allow existing business operations to take advantage of zone benefits without physically relocating to a general purpose zone.[49] As a result of the Boggs Amendment and the 1952 regulation, foreign trade zones are no longer merely transshipment centers as originally envisioned in 1934. Instead, today's foreign trade zones and subzones are the sites of major manufacturing facilities.[50]

Prior to *Nissan*, the sole case on dutiability in connection with subzone manufacturing was *Hawaiian Independent Refinery v. U.S.*[51] *Hawaiian* involved a subzone refinery using partially processed foreign crude oil as a secondary fuel source for subzone operations. The U.S. Customs Court defined the issue in that case as "whether foreign merchandise which is used as an integral part of a permissible manufacturing process within a zone, but which never enters the customs territory of the United States, is subject to duty under the Tariff Schedules of the United States."[52]

The *Hawaiian* court exempted the crude oil from duty, relying primarily on the argument that foreign trade zones are physically distinct from U.S. customs territory.[53] Because the crude oil never entered customs territory, it was not subject to duty. The court explained that exemption from duty for zone merchandise is the rule, and any exception to this rule must be specifically provided for in the Foreign Trade Zones Act. In reaching this conclusion, the court rejected the Government's argument that because the Act does not specifically authorize "consumption" within a zone, such merchandise is subject to the general principle that all foreign merchandise imported into the United States is subject to duty.

The *Hawaiian* court also rejected the theory that foreign merchandise consumed in a zone is constructively transferred to customs territory at the time of its use. The court held that Customs has no authority to require such involuntary constructive transfer.[54] The court recognized the Foreign Trade Zones Board's ability to refuse to grant a zone permit or impose specific conditions on such a permit to prevent unauthorized activity within a zone. The permit in *Hawaiian*, however, was not conditioned on the use of duty-paid fuel. The zone was designed to be self-contained and intended to compete with foreign refineries which do not use duty-paid fuel.[55] In resolv-

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[49] Note, *supra* note 39, at 731.

[50] For example, cars, bicycles, and televisions are manufactured in foreign trade zones and subzones today. *See* deKieffer and Thompson, *supra* note 8, at 508-09 nn.110-12 & 117.

[51] 460 F. Supp. 1249 (Cust. Ct. 1978).

[52] *Id.* at 1251.

[53] *Id.* at 1253-55. "[A] patent distinction is drawn between the boundaries delineating the geographical territory of the United States and the customs territory of the United States." *Id.* at 1253. *See also* 19 C.F.R. 146.1(c) (1988).

[54] *Hawaiian*, 460 F. Supp. at 1256.

[55] *Id.* at 1255-57.

ing the *Hawaiian* duty dispute, the court was careful to avoid the issue of what constitutes permissible zone activity.[56]

Significance

The immediate significance of *Nissan* is that it rejects the arguments accepted by the *Hawaiian* court ten years earlier. The *Hawaiian* court stressed the fact that the activity in dispute occurred within a subzone; it did not focus on the nature of the activity or whether the activity complied with the section 81c(a) list. In *Hawaiian*, an underlying concern of the court was the desire to maintain foreign trade zones on a par with foreign manufacturing conditions to facilitate zone competition in the world market.[57] In *Nissan*, however, the court's primary motive was to ensure domestic industry the maximum protection from zone competition.[58] This change in judicial consideration is at odds with the original purpose for which zones were established—to facilitate the shipment of foreign goods through U.S. ports.[59] That goal is thwarted when burdensome duties designed to protect U.S. producers in the domestic market are imposed upon zone manufacturers trying to compete in an international market. *Nissan* also contradicts the legislative history supporting expansion of foreign trade zones.[60]

Although *Nissan* is inconsistent with prior case law and the legislative history of the Foreign Trade Zones Act, its result is not surprising. The *Hawaiian* court took painstaking care to limit the holding in *Hawaiian* to the particular fact situation involved.[61] Soon after the *Hawaiian* decision was announced, the Customs Service issued a ruling stating that production equipment may not be brought into a foreign trade zone free from duty.[62] In that ruling, Customs carefully distinguished *Hawaiian* as not involving capital equipment and specified that the *Hawaiian* ruling would be strictly limited to its fact situation.[63] Thus, the principles of *Hawaiian* have not been extended to exempt production equipment used in foreign trade zones from duty.

Despite its inconsistency with the basic concept of foreign trade

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[56] *Id.* at 1256. "From the History of the Act no indication appears that Congress intended this court to become the arbiter of permissible and/or nonpermissible intra-trade zone activity." *Id.*

[57] *Id.* at 1257 n.11.

[58] Nissan Motor Mfg. Corp. v. United States, 693 F. Supp. 1183, 1187-88 (Ct. Int'l Trade 1988).

[59] *See supra* notes 37-40 and accompanying text.

[60] *See supra* notes 41-50 and accompanying text.

[61] *Hawaiian*, 460 F. Supp. at 1251 n.1. "It must be emphasized at this juncture that the determination which the court makes in the instant action is limited to the subject matter merchandise, that is—non-privileged foreign merchandise." *Id.*

[62] C.S.D. 79-418, 13 Cust. B. & Dec. 1627 (1979).

[63] *Id.* at 1630.

zones—facilitation of world trade through U.S. transshipment centers—*Nissan* is still not whithout justification. The modern foreign trade zone is extremely different from the zone envisioned by Congress in 1934. Foreign trade zones are physically more expansive than originally anticipated. The physical limitation on zones to "ports of entry" has been eradicated by improved transportation. For example, as a result of air travel, any U.S. location can now be a "port of entry." In addition, the emergence of the subzone concept has drastically expanded the physical limits of any existing zone.[64]

The greatest transformation in foreign trade zones has been their development from transshipment storage centers, where merchandise underwent minor changes, to major industrial production facilities.[65] Today inland subzones, like the one encompassing the Nissan plant in Tennessee, are seen not as U.S. stopovers for foreign merchandise on its way to other international markets, but as a means for foreign manufacturers to minimize costs of merchandise intended for U.S. consumption.[66] The judiciary has recognized this "hole in the tariff wall" available to manufacturers utilizing foreign trade zone production facilities and has validated this result as supported by the Foreign Trade Zones Act.[67]

Foreign trade zones and subzones provide many advantages for operators choosing to locate within such facilities. Importers receive cash flow benefits because no duty must be paid until merchandise is sold and actually enters customs territory.[68] No duty is ever paid on zone exports, damaged merchandise, or waste.[69] Foreign trade zone storage facilitates compliance with quotas, while zone manufacture bypasses quotas altogether.[70] Manufacturers can take advantage of inverted tariff structures to reduce duties by transforming higher-duty components into lower-duty products prior to importation into customs territory.[71] Most-favored-nation tariff rates can be realized

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[64] *See supra* notes 47-50 and accompanying text.

[65] *See supra* notes 41-50 and accompanying text.

[66] deKieffer and Thompson, *supra* note 8, at 492-99.

[67] Armco Steel Corp. v. Stans, 431 F.2d 779, 784-85 (2d Cir. 1970). In *Armco*, the court recognized the possibility that

> manufacturers, through utilization of Foreign Trade Zones, may take advantage of differentials built into the tariff rate structure. If a "hole" is thereby rent in "the tariff wall," Congress intended it, for the Foreign Trade Zones Act clearly contemplates that trade zone users may take advantage of differing rates in tariff schedules and thereby, depending on what form a product might take when imported from the zone into the U.S. customs territory, save on customs duties.

Id.

[68] Note, *supra* note 41, at 355.

[69] *Id.* at 357, 359-60.

[70] *Id.* at 365-66. Quota goods can be transformed into nonquota goods within foreign trade zones and then imported into U.S. Customs territory. *Id.*

[71] *Armco*, 431 F.2d at 784-85. This result is facilitated by electing between "privileged" status for imported merchandise whereby duty liability is assessed when merchandise enters the zone, 19 C.F.R. §§ 146.41, 146.65(a)(1) (1988), and "non-privileged"

for non-favored Communist products by transforming them within a zone.[72] Additionally, zone operators receive tax advantages[73] and insurance savings.[74]

Zone operators benefit from increased profits through proper timing—such as zone storage of merchandise until the market is more favorable.[75] Also, duties can be minimized because costs attributable to zone operations are not included in the determination of the dutiable value of the imported product.[76] Finally, increased duty resulting from an increase in the market value of merchandise while it is stored within a zone can be avoided by fixing duty when the merchandise enters the zone.[77]

By offering these advantages to foreign manufacturers, foreign trade zones undermine the protection Congress has provided for domestic manufacturers by imposing duties and quotas on foreign goods entering the United States. Because of this threat, domestic manufacturers and members of Congress have developed antizone sentiments.

Despite their antiprotectionist effects, foreign trade zones still offer important benefits to the U.S. economy. Foreign trade zones, once viewed as a relatively insignificant contribution to U.S. participation in world trade, are now seen as vehicles to generate additional jobs and stimulate local economies.[78] The most important goal associated with the establishment of foreign trade zones today is the protection of U.S. jobs.[79] Zones prevent marginally competitive U.S. industries from being entirely lost to foreign competition.[80] Domestic manufacturers view zones as "halfway house alternatives" to

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status whereby duty liablity is assessed upon import into customs territory, 19 C.F.R. §§ 146.42, 146.65(a)(2) (1988). By electing "non-privileged" status for higher-duty components, duty is actually paid at the lower final product rate upon importation.

[72] Note, *supra* note 41, at 360.

[73] Zone merchandise is not subject to U.S. excise taxes. *See generally* 26 U.S.C. §§ 4061-4227 (1982). The Trade and Tariff Act of 1984 exempts from state and local *ad valorem* taxes all foreign and domestically produced merchandise within a zone which is destined for exportation. Act of Oct. 30, 1984, Pub. L. No. 98-573, 98 Stat. 2948 (codified at 19 U.S.C. § 81o(e) (Supp. IV 1986)). In addition, some states have legislation expressly exempting zone merchandise from state taxation. *See, e.g.*, N.C. GEN. STAT. § 55c-4 (1988).

[74] Note, *supra* note 41, at 361. Insurance costs are reduced because merchandise has a lower insurable value prior to duty payment and Customs Service protection of zones decreases the risk of damage to zone merchandise. *Id.*

[75] Note, *supra* note 39, at 738.

[76] 19 C.F.R. § 146.65(b)(2) (1988).

[77] *Id. See also* Note, *North Carolina Foreign-Trade Zones: Problems and Prospects*, 5 N.C.J. INT'L L. & COM. REG. 521, 522-24 (1980).

[78] Note, *supra* note 39, at 733.

[79] deKieffer and Thompson, *supra* note 8, at 504-05.

[80] *Id.* Zone manufacture is especially necessary to compete with "border industry" plants—foreign plants which allow duty-free entry of articles of U.S. origin which, after further fabrication, are subsequently returned to U.S. customs territory. "Border industry" facilities provide duty reduction benefits similar to foreign trade zones, yet they generally employ foreign workers. *Id.*

either becoming importers themselves, switching to offshore operations, or going out of business entirely.[81] Because of these advantages, foreign trade zones should and probably will continue to exist.

In response to the changing nature of foreign trade zones, congressional attitudes toward foreign trade zones have changed. Congress has demonstrated a willingness to infringe upon what was once known as the "wide latitude of judgement" delegated to the Foreign Trade Zones Board.[82] Similarly, the judiciary has affirmed congressional action contrary to the Foreign Trade Zones Act where the discrepancy can be attributed to the facilitation of a different congressional purpose.[83] As a result, the Foreign Trade Zones Board has changed its decision making process when evaluating zone applications.[84] The primary concern of the Board is whether a proposed zone will benefit public interest. In the past, this standard was easily met because the creation or retention of jobs which might otherwise go overseas sufficed as a public benefit.[85] While the creation of jobs is still a valid consideration in evaluating zone applications, it is no longer the primary criterion. Today the political consequences of granting a zone application are important considerations as well. Faced with domestic resistance to a zone application, the Board must consider whether zone activity will undermine a remedial action or program in effect because of an unfair trade practice, or whether such activity will materially or substantially harm an existing domestic industry.[86] Modern Board decisions tend to minimize adverse political consequences, perhaps in an attempt to avert congressional curtailing of the zone program.[87] These changes reflect an awareness by Congress and the Foreign Trade Zones Board of the need to resolve the conflict between strong protectionism and the desire to continue the economic advantages provided by foreign trade zones.

The *Nissan* decision reflects an attempt by the court to compromise between these two competing ends. By subjecting the foreign equipment to duty, the *Nissan* court maintains tariff protection for

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[81] *Id.* at 504.

[82] Armco Steel Corp. v. Stans, 431 F.2d 779, 788 (2d Cir. 1970).

Faced with domestic resistance to a subzone bicycle plant, Congress amended the Foreign Trade Zones Act to exempt bicycle components from zone benefits unless reexported. Act of Oct. 30, 1984, Pub. L. No. 98-573, 98 Stat. 142 (codified at 19 U.S.C. § 81c(b) (Supp. V 1987)).

[83] Klockner Inc. v. United States, 590 F. Supp. 1266 (Ct. Int'l Trade 1984). In *Klockner*, the court upheld an "Arrangement" entered into by the European Coal and Steel Community and the United States which defined the "U.S.A." as including both U.S. customs territory and foreign trade zones. The court upheld this "discrepancy" with the Foreign Trade Zones Act as necessary to aid the domestic steel industry. *Id.* at 1273.

[84] Note, *supra* note 41, at 349.

[85] *Id.*

[86] deKieffer and Thompson, *supra* note 8, at 503.

[87] *Id.* at 509.

domestic manufacturers who sell production equipment to companies operating in foreign trade zones. The court thus supports some degree of protection for U.S. manufacturers. At the same time, however, the court does not infringe upon the other benefits available to subzone manufacturers.[88] The court thus advances protectionism without seriously curtailing foreign trade zone benefits.

Conclusion

Foreign trade zones, once seen as a relatively insignificant method of facilitating the age old problems of international transshipment, have become a means of reducing or avoiding duties on foreign merchandise entering the United States.[89] Recognizing this transformation in function and the corresponding development of antizone sentiment, Congress, with court approval, has begun to whittle away at foreign trade zones.[90] Realizing the political sentiment against zone usage—especially zone manufacturing—the Foreign Trade Zones Board has similarly limited authorization of zone usage through the exercise of its broad discretion.[91]

The *Nissan* decision updates case law to reflect the current conflict between protectionism and foreign trade zone law. Because of the enormous changes foreign trade zones have undergone since first authorized in 1934, continued adjustments will be needed in order to reconcile differences between the Foreign Trade Zones Act and the trade zones it is designed to regulate. As a result, constriction of foreign trade zone law is likely to continue through actions of both Congress and the Foreign Trade Zones Board, probably with court approval.

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[88] *See supra* notes 68-77 and accompanying text.
[89] *See supra* notes 65-77 and accompanying text.
[90] *See supra* notes 82-83 and accompanying text.
[91] *See supra* notes 84-87 and accompanying text.