

**SENATE COMMITTEE PRINT. 65TH
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ZONES IN PORTS OF THE UNITED
STATES: LETTER FROM THE UNITED
STATES TARIFF COMMISSION**

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Letter from the United States Tariff Commission by Various

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SENATE COMMITTEE PRINT

FREE ZONES IN PORTS OF THE UNITED STATES

LETTER FROM THE
UNITED STATES TARIFF COMMISSION

131

TRANSMITTING

IN COMPLIANCE WITH THE REQUEST OF THE SENATE
COMMITTEE ON COMMERCE A REPORT UPON THE
POLICY OF ESTABLISHING FREE ZONES IN PORTS OF
THE UNITED STATES, TOGETHER WITH AN ANALYSIS
AND COMMENT CONCERNING THE BILL (S. 4153) TO
PROVIDE FOR THE ESTABLISHMENT, OPERATION, AND
MAINTENANCE OF FREE ZONES IN THE PORTS OF THE
UNITED STATES, AND FOR OTHER PURPOSES



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1918



UNITED STATES TARIFF COMMISSION.

Office: 1822 New York Avenue.

WASHINGTON, D. C.

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F. W. TAUSSIG, Chairman.

THOMAS WALKER PAGE, Vice Chairman.

DAVID J. LEWIS.

WILLIAM KENT.

WILLIAM S. CULBERTSON.

EDWARD F. COSTIGAN.

WILLIAM M. SYDNEY, Secretary and Statistician.

LETTER OF TRANSMITTAL.

UNITED STATES TARIFF COMMISSION,
Washington, November 20, 1918.

HON. DUNCAN U. FLETCHER,
Chairman, Committee on Commerce, United States Senate.

SIR: In accordance with your request of May 3, 1918, the Tariff Commission respectfully submits herewith a report concerning the policy of establishing free zones in ports of the United States, together with comment concerning Senate Bill 4153.

Respectfully,

UNITED STATES TARIFF COMMISSION,
F. W. TAUSSIG, *Chairman.*
THOMAS WALKER PAGE, *Vice Chairman.*
DAVID J. LEWIS.
WILLIAM KENT.
W. S. CULBERTSON.
EDWARD P. COSTIGAN.

PREFACE.

The act of September 8, 1916, creating the United States Tariff Commission (sec. 702) declares:

It shall be the duty of said commission to investigate the administration * * * of the customs laws of this country * * *, to investigate the operation of customs laws, * * * and to submit reports of its investigations.

The duty of investigating the administration of the customs laws carries with it a consideration of the bonded warehouse, bonded manufacturing warehouse, and drawback systems as instrumentalities for assisting reexport in foreign trade. The free zone, as an alternative and supplementary device to this end, requires consideration. Specific request for investigation and report on this subject was made by the chairman of the Ways and Means Committee August 16, 1917.

On May 4, 1918, the following request was also received:

COMMITTEE ON COMMERCE, UNITED STATES SENATE,

Washington, D. C., May 3, 1918.

Sir: I am directed by the Committee on Commerce to refer to you the inclosed bill, S. 4153, and to request you to furnish the committee with such suggestions as you may deem proper touching the merits of the bill and the propriety of its passage.

I am,

Very respectfully,

DUNCAN U. FLATCHEAD, *Chairman.*

Hon. F. W. TAUSING,
Chairman United States Tariff Commission.

S. 4153 (identical with H. R. 10892) entitled "To provide for the establishment, operation, and maintenance of free zones in the ports of the United States, and for other purposes," was introduced in the Senate March 21, 1918, and in the House March 20, 1918.

In the course of the investigation—

Hearings were held in San Francisco, New York, and Philadelphia by members of the commission;

Information and data were sought through investigation by representatives of the commission in New Orleans and Galveston;

A questionnaire was sent out to several hundred merchants and shippers;

Study was made of the history and working of the free ports or free zones in Europe and of the laws and regulations controlling them;

Interviews were had with those familiar with free zone practice; and

Information as to recent foreign development was secured through the Department of State.

From data thus obtained the following report is compiled.

PART I

DEFINITION AND PURPOSE OF A FREE ZONE.

The word "free" in connection with "port" or "zone" is apt to be misleading. It is proper to note, therefore, that the term has no relation either to port charges or to any policy of "free trade" or "protection" in this case. Conventional nomenclature is in this case misleading. A "neutral" zone would be more properly descriptive. A free port or free zone is a place, limited in extent, that differs from adjacent territory in being exempt from the customs laws as affecting goods destined for reexport; it means simply that, as regards customs duties, there is freedom, unless and until imported goods enter the domestic market.

A free zone may be defined as an isolated, inclosed, and policed area, in or adjacent to a port of entry, without resident population, furnished with the necessary facilities for lading and unloading, for supplying fuel and ship's stores, for storing goods and for reshipping them by land and water; an area within which goods may be landed, stored, mixed, banded, repacked, manufactured, and reshipped without payment of duties and without the intervention of customs officials. It is subject equally with adjacent regions to all the laws relating to public health, vessel inspection, postal service, labor conditions, immigration, and indeed everything except the customs.

The purpose of the free zone is to encourage and expedite that part of a nation's foreign trade which its government wishes to free from the restrictions necessitated by customs duties. In other words, it aims to foster the dealing in foreign goods that are imported, not for domestic consumption, but for reexport to foreign markets, and for conditioning, or for combining with domestic products previous to export.

Although the free zone is naturally conceived to be on deep water, and is commonly regarded as in many ways an extension of the open sea, there is none the less a possibility of its establishment in an interior location where rail and inland waters may bring about the assembling of foreign and domestic goods destined for export. It is pertinent to note that Switzerland is contemplating the establishment of a free zone at Basle, which is close to the industrial districts of France, Italy, Austria-Hungary, and the German Empire.

THE POLICY OF THE UNITED STATES.

The policy of the United States has not been unfavorable to the kind of commerce that the free zone is designed to promote. On the contrary, it has been the obvious intention of the Government to relieve reexport trade from the restrictions incident to the admin-

istration of the tariff and customs laws, and to that end three institutions have been devised.

- (1) The bonded warehouse, where goods intended for reexport may be entered and held free of duty.
- (2) The bonded manufacturing warehouse, where without payment of duty imported goods may be handled, altered, or manufactured solely for export, either with or without the admixture of domestic materials and parts.
- (3) The drawback, which is a repayment of 99 per cent of the duties paid on imported goods when they are exported.

The provision and retention of these three devices show clearly that it has not been the purpose of the United States Government to place unnecessary obstacles in the way of its citizens when engaged in international trade. That such obstacles have arisen is due to the fact that the three devices mentioned were inadequate wholly to relieve foreign commerce from the regulations and restrictions placed upon the importation of foreign goods for domestic consumption. It would therefore involve no change of policy to supplement these devices by a system of free ports or free zones such as have proved singularly effective in other countries.

INADEQUACY OF BONDING AND DRAWBACK.

There are certain features in the present bonded warehouse and drawback systems which detract from their usefulness in facilitating foreign commerce. Some of these features are inherent in the nature of the case; others consist of seemingly unnecessary hardships which can be ameliorated by a revision of the customs laws and the regulations accompanying them.

In accordance with the mandate of the law creating the United States Tariff Commission, we have studied the customs administrative laws, to the end of securing simplification and granting relief from what seems unnecessary procedure, and reported on August 26, 1915, our findings and recommendations. In so far as changes suggested in that report affect the procedure under bonding and drawback attention is called to the footnotes herein.

The purposes of the bonded storage warehouse are to relieve importers from the payment of duty on foreign products that in unchanged form are destined for reexport, and also to permit the postponement of payment of such duties until the time when, during a period of three years the owner desires to remove them. It can not aid in expediting the entry and

clearance of shipping or the handling of merchandise, for vessels must submit to the same formalities and requirements, whether they bring dutiable goods or goods to be placed in bond, and the goods themselves, whatever their destination, must be valued, sampled, weighed, and tested before removal from the dock. Much of the delay necessarily incident to the proper assessment of duties on imports for domestic consumption is equally imposed on goods destined to be reshipped.¹

(a) To protect the public revenue from unauthorized entry of goods into domestic trade, the owner of the goods is required, under present procedure, to give bond in double the amount of the duty, which is forfeited if the goods are stolen, lost, destroyed, or fraudulently removed.²

(b) Even draysage between dock and warehouse must be done under bond.

(c) In addition, from the time they enter port until they are reshipped the goods are under constant customs control and supervision.

(d) While in the warehouse they must be placed and arranged in accordance with certain well-defined regulations, so that they may at any time be checked and inspected by special agents of the Treasury Department.

(e) Permits must be obtained for their reception and delivery, and strict accounts must be kept of all warehouse transactions.

(f) Except during the usual business hours the warehouse is closed by a Government lock, and to enter it at any other time requires special permission and payment for the overtime presence of a customs agent.

(g) Handling, sorting, mixing, or repacking of the goods is prohibited; only where serious damage is threatened can the original package be opened, and even then it must be done by special permission and under customs supervision.³

(h) Subject to these regulations, the expense of which it should be noted is made a charge upon the goods, an owner may leave his merchandise in bond for three years, but at the end of that time if duties are not paid they are considered, to use a technical expression, as "abandoned to the Government," to be sold by the Government, accruing charges and expenses deducted, and the remaining proceeds turned over to the owner.⁴

The usefulness of the bonded warehouse is sometimes further restricted by the tariff practice of the country to which bonded goods are reexported. Thus, the Canadian law treats goods that have been held in American bonded warehouses exactly as if they had entered American domestic commerce.

¹ In the case of a ship loading part of its cargo in an American customs port and desiring to continue its voyage with the remainder of its cargo in a foreign port, the practice and the regulations make entry of such dutiable goods an arduous and simple matter.

² In the case of a vessel entering a port having part of its cargo destined for reshipment to a foreign port, it can transport its remaining cargo to another vessel through bonded lighters, with merely nominal customs procedure.

³ The suggested revision of the customs laws relieves the owner of the goods of this specific bonding, and locks to the owner of the bonded warehouse for safeguards against such removal.

⁴ The proposed revision provides permission for repacking, mixing, blending, cleaning, sorting, and in fact practically every process short of actual manufacture.

⁵ Under the proposed revision the President is given the power to extend this three-year term under war or any other emergency.

When imported from this country to Canada, such goods are assessed for duty at the foreign value increased by the amount of the duty they would have paid if they had entered the United States for domestic consumption. The effect of this regulation finds illustration in the business of a certain American firm dealing in foreign embroideries. In order to fill a Canadian order, this firm found it necessary to send goods from a bonded warehouse in New York to England where the goods were re invoiced and thence shipped direct to Canada.

BONDED MANUFACTURING WAREHOUSE.

The mere statement of the regulations sufficiently indicates the limited usefulness, so far as export trade is concerned, of the bonded storage warehouse. Even more stringent are those applying to the bonded manufacturing warehouse. In the latter institution foreign materials may be entered free of duty and worked up into manufactures ready for consumption.

(a) Production can be carried on in such a warehouse for export only. With a few special exceptions, the output can not be disposed of in the domestic market, even on payment of duty.¹ The most important exceptions are metal from ore smelted in bond, and cigars "made in whole from tobacco imported from one country." Minor exceptions are found in a provision for the entry of Mexican peas, or Garbanzo, which have been cleaned at such warehouses, and in the permission to sell for domestic consumption by-products and waste arising in the manufacture of goods for export, provided duty is first paid on such articles as if imported from abroad.

(b) Before beginning operations the proprietor must file with the Treasury Department and with the collector of customs a statement of all the articles he intends to manufacture, giving the names of the articles, the exact kind and quantity of ingredients, and the formula of manufacture, and he must adhere rigidly to the formula set forth.

(c) He must also give bond in double the value of the goods he intends to produce.

(d) From beginning to end materials and operations are under strict customs supervision. A multitude of restrictions make the procedure intricate and expensive, and the penalties for violation are very heavy. Only in the most highly standardized industries is it possible to avoid frequent disputes and misunderstandings.

DRAWBACK.

The law authorizing what is known as drawback permits an importer, instead of placing his goods in bond, to pay duty on their entry and then to draw back from the Treasury on their reexportation 99 per cent of the amount paid. This provision, of course, can not any more than the bonded warehouse relieve commerce from the delays and other burdens incident to customs enforcement. The intent of the law is to aid production for foreign markets by relieving from customs dues imported materials that are manufac-

¹ The proposed revision permits withdrawal for consumption of all goods produced from bonded manufacturing warehouses.

tured or finished in this country and then shipped abroad. But the relief thus afforded, except in the sugar and tin-plate industries, has been relatively small, as may be seen from the following table:

Principal imported articles used in the manufacture of articles exported upon which drawback was paid.

(For years ending June 30.)

Articles.	Tariff act of 1897.		1900.		1901.		1902.		1903.		1904.		1905.		1906.	
	1897	Per cent of total.	1900	Per cent of total.	1901	Per cent of total.	1902	Per cent of total.	1903	Per cent of total.	1904	Per cent of total.	1905	Per cent of total.	1906	Per cent of total.
Aluminum.....	965,880	1.90	616,601	0.94	819,099	1.06	893,704	4.74	826,804	6.09	836,125	8.02	841,109	3.05	875,092	0.49
Wheat flour.....	46,370	.91	50,153	.73	157,762	2.71	180,479	2.81	147,313	3.24	69,846	3.00	26,273	.35	52,845	.34
Cotton manufactures.....	16,524	.34	44,295	.68	27,069	.44	45,720	.65	59,288	1.33	25,983	.79	16,291	.22	34,800	.23
Fruits and nuts.....	22,915	.45	23,775	.35	37,439	.60	14,167	.22	33,013	1.14	53,745	1.00	53,279	.79	70,243	.44
Hides of cattle.....	977,897	19.56	848,423	12.78	924,001	13.35	364,020	4.32	67,000	2.23	160	.00	33	.00	10	.00
Tin plates.....	1,225,203	24.01	1,334,490	20.24	1,329,558	20.73	1,491,479	23.32	48,271	.99	24,400	0.48	451,246	6.14	23,473	.14
Lead ore and bullion.....	306,020	6.12	368,351	5.60	395,014	4.30	428,202	6.39	461,330	10.59	373,013	11.84	181,596	2.51	98,902	.64
Oils (trapped and others).....	33,000	.66	49,499	.74	33,122	.39	83,792	.87	61,130	1.34	48,403	1.53	44,471	.60	30,797	.20
Sugar and molasses.....	1,381,328	27.64	1,195,200	18.72	1,303,027	13.26	3,900,134	31.23	1,443,387	31.77	552,319	36.79	6,412,620	72.74	13,776,431	90.19
Rice.....	44,798	.89	37,684	.56	40,521	.49	136,723	2.12	60,969	2.20	183,114	5.15	41,968	1.11	59,008	.39
Optics and manufactures.....	88,100	1.76	149,549	2.21	10,001	.11	544	.008	296	.007	1,108	.03	22,817	.30	372,878	2.44
Chemicals, drugs, and dyes.....	35,700	.71	37,684	.56	40,521	.49	141,460	.84	25,315	1.14	26,844	1.17	43,267	.58	126,000	.85
Glycerine.....	36,445	.73	52,553	.80	54,178	.57	52,872	.80	34,200	.86	15,900	.80	30,294	.80	58,384	.38
Total.....	5,444,151	100.00	6,897,600	100.00	4,182,375	100.00	6,402,638	100.00	4,543,590	100.00	3,145,902	100.00	7,339,290	100.00	16,576,898	100.00

It is obvious from these figures that scores of industries in this country that now use foreign materials to produce goods for export do not exercise the drawback privilege at all. The reason is that, for the prevention of fraud, the privilege is so hedged about with exacting and intricate regulations that the amount of the drawback very often does not pay for the labor and cost of collecting it.

(a) To prove the identity of goods on which drawback is claimed requires a minute checking of imported elements entering into the manufacture, with the right and oftentimes with the need of examining into factory management sometimes threatening the disclosure of trade secrets of importance. So complicated is the procedure in making claim and proving identity that many producers do not find it worth while to apply for drawback at all. Large-scale industries, like sugar refineries and those compelling the use of large quantities of tin plate, go to the expense of employing experts permanently to look after their drawback interests.

(b) Every step must be taken subject to customs inspection, and oaths are required from importers, superintendents, and exporters.

(c) Even after reshipment, before drawback can be recovered, evidence must be given of the actual landing of the goods in a foreign country.¹

(d) At best, under the smoothest operation of the law, that part of the owner's capital advanced in payment of duties is tied up in the Treasury from the time the goods are imported until 30 days after they are reshipped.

ILLUSTRATIONS OF THE INADEQUACY OF THE PRESENT SYSTEM.

At the hearings conducted by the Tariff Commission and in the replies to its questionnaire numerous instances were adduced illustrating the inadequacy of the bonding and drawback system. To a few of these attention may be here directed.

Rice milling is an industry for the successful prosecution of which all conditions appear to be favorable

in the United States except a sufficient supply of raw material. The industry is now limited almost entirely to the preparation of the domestic product for domestic consumption, and this does not furnish full employment. It requires expensive specialized machinery and much skilled labor that must be engaged by the year. But testimony was presented showing that the largest mills are idle much of the time, because the domestic crop can keep them in operation for only half the year. Efforts have been made to use the idle months in cleaning and milling oriental rice, the supply of which is very large, for reexport to the West Indies and Spanish America. To do this work profitably the rice must be imported in full ships' cargoes and handled in bulk through grain elevators. These cargoes usually are about 6,000 tons, and as there is an average duty of one-half cent a pound on rice, the duty that must be paid on a full cargo is \$60,000. The importer, of course, would be entitled to a drawback on such quantity of the rice as was reexported; but it was the unanimous testimony of the mill officials interviewed that the business had to be discontinued because of the difficulty, delay, and expense of securing the drawback.

Again, it was found that imported flowers and feathers and imitation feathers are extensively used in this country for trimming women's hats, the model or frame of which is an article of domestic production. Also Panama and imitation Panama hats for the use of both men and women are imported from Central and South America and finished in the United States with the use of domestic materials. The industry has been almost entirely limited to supplying the domestic market, for our manufacturers have found themselves hampered in competing for foreign markets by the restrictions of our bonding and drawback system.

The effect of these systems on dealers in highly finished goods is perhaps best seen in the case of laces and embroideries. These are manufactures for which Spanish America offers a large and lucrative market which heretofore has been almost entirely supplied from Europe. Commodities of this character are apt to be included in the same order with a variety of other goods, and the order naturally goes to the dealer who can fill it as a whole at the lowest price, in the

¹ Under the proposed revision of the customs laws, the landing certificate requirement is abolished, excepting when, in specific instances for reasons assigned, the Secretary of the Treasury shall call for such procedure.