MILLER: THE MOSES OF THE FOREIGN TRADE ZONE MOVEMENT
Streamlining applications means "the binder business has gone away."

CALL OF DUTY-FREE

REFORM OF THE FOREIGN TRADE ZONE PROCESS MAKES IT EASIER FOR SMALL COMPANIES TO WIN BIG-COMPANY ADVANTAGES

[BY WILL SWAIM]

YOU KNOW THOMAS JEFFERSON as an American founder, a president, a thinker and inventor. You might also know that he was a major Virginia planter, and it's reasonable to speculate that his appreciation for the natural cycles of the earth shaped his observations about government. Writing a couple of centuries ago—about the time the White House was taking shape in a swamp, before he became the nation's third president—Jefferson noted that the "natural progress of things is for liberty to yield and government to gain ground."

Once they get power, in other words, governments almost never voluntarily relinquish it. Governments grow. So what to make of the recent, radical deregulation of the federal foreign trade zone program?

"I've seen things happen in the last four years that I've never seen before," says Adrienne Turner, FTZ administrator for the city of San Diego. "It's amazing. I've seen remarkable things."

Listening to Turner and others is like hearing of a Greek god unbound. They speak of their surprise in the speed of the changes, and the fact that those changes were kick-started by President Barack Obama, a man more noteworthy for his expansion of federal authority over healthcare than for aggressively trimming government red tape. They talk of their astonishment at seeing federal officials slash the application required of companies eager to expand their exports through the FTZ program but daunted by the prospect of getting too close to government. They describe

▲ "DEFINITELY SEEING BENEFITS FROM THE CASH-FLOW SIDE."
Wheat Group CEO Chad Grismer opens the firm's Foreign trade zone warehouse with former San Diego Mayor Jerry Sanders, November 2012.

a White House-backed requirement that the major federal bureaucracies (Commerce and Customs) overseeing the FTZ process limit actually working together.

And they note the subsequent skyrocketing performance of American companies that take advantage of a process that may seem at first absolutely inconsequential.

Mostly, they all seem completely shocked by the very recognition that this administration reversed what Jefferson called "the natural progress of things," that in the case of foreign trade zones, government got it right.

TO UNDERSTAND THE CLEANUP AND WHAT IT MEANS FOR YOU, it's best to go back about 80 years. In the late 1920s, with the world economy slipping into recession, many nations responded by erecting tariffs and drafting trade laws to shield their native industries from competition. In the U.S., that shield appeared in the form of the now-notorious Smoot-Hawley Tariff Act of 1930.

Historians agree that Smoot-Hawley—named for Willis Hawley, a congressman from Oregon, and Utah's Sen. Reed Smoot—triggered a dramatic decline in global trade. By some calculations, the act that bears their name raised tariffs on a few thousand U.S. goods; more conservative estimates put the number at several hundred.

Confronted with a massive increase in the tariff on goods shipped into the U.S., foreign governments retaliated. Canada raised tariffs on 30 percent of all U.S. exports into that country. Great Britain, "the bulwark of free trade, tried its best to resist," one historian has observed. "But the impact of the U.S. tariff proved too much for it to handle. Saddled with debt and faced with a vanishing market for its goods, Great Britain had to resort to protection in 1931." France, he notes, "eventually reacted to the collapse of trade with a particularly devastating quota system."

Historians disagree about whether Smoot-Hawley drove the world into a global depression or was merely one of myriad contributing blunders. But most would likely agree with the *Economist*. Writing in December 2008, after the first shock of the second Great Depression, the magazine (which calls itself a newspaper) said the U.S. tariff hike "added poison to the emptying well of global trade."

If the Smoot-Hawley Tariff Act seems dangerously stupid—its disastrous yield somehow inevitable—consider that many countries went further still. In post-1933 Germany, for instance, Adolf Hitler declared that his country would no longer cooperate in the global economy; self-sufficiency (or autarky, as it was sometimes called) seemed somehow more heroic to the Nazi Party than the prospect of sellers and buyers meeting voluntarily in the global marketplace—and seemed a surer way to protect scarce cash reserves. Germany, the Nazi party decreed, would manufacture for itself everything it needed. In the short term, that produced something like full employment. But when self-sufficiency failed to satisfy German demand for jobs, land and some products, Germans invaded and looted their neighbors.

HE'S IN THE ZONE
Obama has been the president with the surprise inside when it comes to slashing government regs around foreign trade zones.

But until the war, for much of the 1930s, Hitler's Germany looked to many, including some in the U.S., like the brightest possible future, a glorious new world of productivity, efficiency and prosperity. By contrast, soup lines curling around urban neighborhoods seemed to indicate America was falling behind.

In that world, American companies began relocating business units offshore, behind the rising walls of foreign tariffs where they would be treated as locals. They went native. That produced further job losses at home.

Prodded by Franklin D. Roosevelt, Congress responded with the Foreign Trade Zone Act of 1934.

It'd be great to report that the act changed everything. It did not. In fact, for the first several years, foreign trade zones were little more than real estate developments located near ports of entry. And for years after the Second World War, when the U.S. stood nearly alone in the midst of fallen industrial powers—Asia and most of Europe in ruins, architecturally and sometimes politically—foreign trade zones seemed hardly worth the trouble; U.S. products and services were everywhere necessary and therefore triumphant, and hardly needed the slim advantages afforded by a foreign trade zone.

NOW WE COME TO THE POINT IN THE STORY when things begin to change radically, if over the course of decades. With the rise of Japanese and European competition in the 1970s, there was pressure on the federal government to act. U.S. companies looking to reduce labor costs that constituted the American dream and the seeds of its own decline eyeballed offshore manufacturing. By 1980, the feds allowed companies in foreign trade

IN THROUGH THE OUT DOOR
Wheat Sicon accessories move from China to San Diego and onto cruise ships without pausing to pay duties

zones to import component products for manufacturing or refining with no additional tax—if the final product was shipped out of country.

"When you treat a facility in Detroit or Alabama or Mississippi as outside the country, but you employ people here who would (otherwise) be working in another country, it's pretty cool," says Marshall Miller, an attorney with the Missouri-based consulting firm that bears his name. Miller says the 1980 changes led to "explosive growth," like "a 45-degree angle on the graphs."

"Cool" is an interesting choice of words for Miller, a man many regard as "the father of the modern trade zone," one of the architects of its recent reforms, its Moses. He seems humbled by the accolades, and admits to a kind of geek love of this obscure part of the business—says he "kind of fell in love with the whole concept of trade zones" while in law school at the University of Virginia, back when Richard M. Nixon was in the White House.

Miller notes that the 1980 reforms left two features unchanged. First, becoming a certified participant in a foreign trade zone still took time—a year or more. And that took money, usually in the form of a legal expert hired to fill out redundant/complex/overlapping/contradictory forms from the U.S. Customs Service (then a part of the Treasury Department) and the Commerce Department. The fruit of their labors was a thick, complex document—"a binder," Miller calls it—proving that a company was right for a foreign trade zone.

The second challenge: If you wanted to take advantage of a foreign trade zone designation, you had to move into a foreign trade zone facility.

"It used to be the animals had to come to the zoo," says Miller. "A city or a port authority would say, 'We have a piece of property, it's near a port or airport, and we want you to use it. If you want to play, you have to come to our property.'"

Those two problems—the time/money nemesis that bedevils all of mankind, and the need to actually move an operation into a specific piece of real estate—made foreign trade zones the playground of richer companies.

Then came the second Great Depression—the financial collapse of late 2008—and with it a new president and popular calls for jobs, or tariffs, or maybe both.

Barack Obama entered office in January 2009 and almost immediately issued an order that, Miller says, told agencies in the Departments of Commerce and Homeland Security (where Treasury moved after the September 11 attacks), "We need you to reduce paperwork, to make things easier for companies to access foreign trade zones, to have less regulation—and we want you to talk first about industry. They must have an opportunity for input."

"This was not a White House initiative, but it was an administration that would listen," says Miller.

There is no huge win for the White House in pushing for foreign trade zone reform, Miller suggests. The board overseeing foreign trade zones "is terribly small," viewed by some as the smallest federal agency. Its total staff is seven—not even a line item in the federal budget. "And it's always operated quietly because they had no funding. It just wasn't a big deal. It was a good thing, always a good thing, but a very small thing that nobody was going to get terribly excited about.

"This is just not an easy area to get a lot of visibility with. It's very narrow in scope, very technical. It would have gotten nowhere if the timing wasn't what it was, and you didn't have responsive people."

If the political dividends for reform were meager, the payoff to global companies is huge. When the work of cutting and pasting and going online was completed in 2012, officials predicted they had cut the application process from a year or so "to 120 days." The reality was even better.

"I just received FTZ Board approval for a new warehouse/distribution center in only 10 days," says city of San Diego's Turner.

When he "was first involved in the 1970s," Miller says, "the applications had 13 exhibits. The applications were probably three to five inches thick. Now it's all online. And the binder business has gone away. The questions are simple and straightforward. And the time reduced is up to 75 percent."

EVEN THOSE WHO BEGAN THE APPLICATION PROCESS just before the 2012 revamp felt the tailwind of imminent change.

"It took us eight to nine months," said Paul Brown, CFO of The Wheat Group, which picked up its certification in November 2012. "From what I'm hearing, it sounds like it's a lot easier now."

His San Diego-based firm imports apparel and accessories it

manufactures ("mostly in China and some in Indonesia") for such high-profile brands as Hurley, Puma and Skull Candy. Most of the product arrives tariff-free at the company's Otay Mesa, California, warehouse, just north of the Mexican border—but well within the service area of the city of San Diego's foreign trade zone.

Brown says the key advantage is cash flow. Before certification, his company "paid the duty right on delivery;" following re-export of those same goods—to cruise ships operating in international waters, for example, or to Canada—the Wheat Group chased a refund of the duty through byzantine federal bureaucracies. Now, he says, there's no cash expense for duty. "The product comes into the foreign trade zone and leaves, but because it never technically hits the U.S. there's no payment and so no refund request.

"We hired someone basically to track all that, and we're definitely seeing great benefits from the cash-flow side," Brown says.

Then too there's the faster speed of Customs processing, Brown says. Participating in the foreign trade zone, the Wheat Group submitted to a background check. Its containers are now fast-tracked through the Port of Long Beach because "Customs knows more about you. Our goods clear through customs much quicker."

As part of the deal, Customs requires stricter accountability at the company's warehouse, of course. Brown calls the federal agency "very detail-oriented where inventory tracking is concerned." He's not complaining: The agency's compelling interest in the destination of all goods moving through a foreign trade zone forced The Wheat Group to step up its inventory-management game. Simple theft of merchandise, for instance, is suddenly a federal offense. Lost inventory is no longer just a nuisance; it could jeopardize a company's certification.

Turner, the city's foreign trade zone administrator, points to The Wheat Group's experience as evidence of even better things to come. The slimmed-down app process is bringing smaller companies—not just the petroleum industry giants who import crude and export refined fuel.

"We're just very fortunate in the FTZ world," Turner says. "A very forward-looking group of people" looked at a system that was "onerous," "expensive" and "difficult," at "regulations that hadn't been updated for decades, and they found the best way to improve exports is to just stop the old, ridiculous application process."

In seeing that, we'd tell Thomas Jefferson, we have seen a small group of forward-looking people reverse "the natural progress of things."

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