Export FTZ Advantages

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Foreign-Trade Zones (FTZs) are restricted access sites authorized by the Foreign-Trade Zones Board. Foreign and domestic merchandise may be admitted into zones for storage, exhibition, assembly, manufacture or other processing. The usual formal Customs entry procedure and payment of Customs duties is required on the foreign merchandise **only if** it enters Customs territory for domestic consumption. No Customs duties are ever paid on exported material. Domestic merchandise is allowed in a facility for any authorized activity. Exemption from ad valorem, state and local personal property taxes is provided under certain circumstances in the Act. The Foreign-Trade Zones Board may restrict activities on public interest grounds.

As structured by Congress, the Program encourages US investment and jobs, as opposed to similar activity in foreign countries. As of July 1, 1998, there are 225 general-purpose foreign-trade zones and 391 foreign-trade subzones with 27 pending applications.

One of the two primary reasons for the Foreign-Trade Zones Act of 1934 was the promotion of exports. The role of the FTZ as a facilitator of exporting has been greatly increased by subsequent amendments to the Act. In 1997 about $20 billion worth of merchandise was exported from FTZs. Foreign-trade zones in the US offer many advantages for the manufacturing and warehousing of exports. For most exporters, no other mechanism is as effective in reducing the costs of exporting operations as a FTZ.

Advantages over Drawback/ Bonded Warehouses

Other duty savings mechanisms available to exporters do not provide the cost savings of a FTZ and require a significant paperwork burden. Use of a FTZ has advantages over drawback. The greatest zone advantage is avoiding the immediate payment of Customs duties and at a later date seeking its recovery. As a result of the recent total change in the drawback regulations, the complexity of the process and the potential Customs penalties significantly change the nature of the drawback process. Drawback permits the recovery of 99% of the duties paid for imported material that is exported. The duty refund obtained under drawback is not recovered until the exportation. Actual recovery of duties under a drawback claim necessitates compliance with strict documentary requirements and careful accounting of the foreign material. Many exporters are only able to claim drawback on a limited number of foreign parts due to the complexity of the drawback procedure. The drawback procedure for exports to Canada is particularly restrictive. The financial recovery through drawback is often further reduced by the 10% - 30% commission due to the drawback consultant. Drawback is only applicable to merchandise that is exported within a limited number of years. An operator of a FTZ, on the other hand, enjoys cash flow savings by never making the duty payments that drawback claimants try to recover.

Most types of bonded warehouses cannot be used for manufacturing. Those that can, are only permitted to use foreign merchandise in the manufacturing process. Only a FTZ allows a manufacturer to combine both foreign and domestic material to produce a product for export. Additionally, bonded warehouses must be used for the storage of foreign merchandise only, often limiting flexibility of storage space and requiring fencing and other expenses. No physical separation of domestic and foreign merchandise is needed in a FTZ.

Avoidance of Customs Entry

Because a FTZ is not part of the Customs Territory of the US, imported material can be admitted into a FTZ without filing a Customs entry. This results in many advantages for exporters. Customs duty payments are avoided on foreign sourced finished goods, material used to manufacture products and spare parts. A very significant advantage is that antidumping/countervailing duties are also avoided on exported merchandise. There is no other US Customs mechanism where these additional duties are not paid by US firms. Drawback is not available to recover AD/CVD duties. US quota restrictions are avoided in foreign-trade zones, either when the material is exported in its original condition or when used in manufacturing for export. Voluntary restraints and orderly marketing agreements enforced by foreign countries may not be avoided for shipments to the US into a FTZ.

Merchandise exported from the US to foreign customers and returned, can be admitted to a FTZ for storage, repair and re-export. This methodology is much simpler than the traditional approach of making Customs entry when foreign customer returns occur. Zone use reduces the cost and the chance for errors in Customs entry. Because merchandise is not subject to Customs entry, regulatory requirements of many federal agencies are not applied to merchandise admitted to a foreign-trade zone. Merchandise can be held in the zone and re-exported without compliance with many federal agency laws.

By not filing Customs entries, many of the expenses associated with the entry of foreign material are either greatly reduced or eliminated. Customs brokerage fees for Customs entries will be eliminated. The US Customs Service Merchandise Processing Fee paid on each Customs entry is eliminated. Collectively, these expenses can be significant.

NAFTA

While a foreign-trade zone is not part of the US Customs territory, a foreign-trade zone is, by definition in the NAFTA treaty and statute, part of the NAFTA territory. Therefore, production within a foreign-trade zone qualifies as production in the US for the purpose of NAFTA qualification. This is a most important FTZ financial savings opportunity, as it provides the ability to combine domestic and foreign materials to create a NAFTA-qualified finished product. For exports to Canada now and to Mexico beginning in 2001, shipments must be the subject of a Customs entry whereby, before exportation, duties will be paid on the non-NAFTA material equal to the US duties less the amount of duties that will be owed to Revenue Canada upon entry into Canada.

A major financial savings is found in warehousing operations. In a FTZ, finished goods may be admitted from foreign countries and re-exported without the payment of Customs duties to Canada or Mexico. In duty drawback to a NAFTA country, there are very strict inventory control structures in place now that limit drawback claims for such merchandise. The financial savings can be very significant.

Tax Advantages

The Foreign-Trade Zones Act provides that foreign and domestic property held in a foreign-trade zone for export are exempt from state and local ad valorem personal property taxes. This provides, in certain states, a significant financial advantage. Sixteen states and Puerto Rico also provide other tax incentives for companies located within existing foreign-trade zones.

Foreign based companies that wish to store their merchandise in the US for exportation may avoid US tax liability. The foreign companies' merchandise can be held in a foreign-trade zone in such a manner that the company does not have a permanent establishment in the United States for tax purposes. Title can be transferred from the foreign company to the purchaser and shipped directly from the zone to overseas locations.

Production Machinery

The Foreign-Trade Zones Act permits the assembly of parts of machines into finished production machinery in the foreign-trade zone. Customs duties are paid on the finished machinery when it is capable of full-scale production or on the parts if they have a lower duty rate. Since many parts of machines carry a higher Customs duty rate than the finished machine, the FTZ advantage is significant. Not only does this activity result in the lowering of Customs duties, but there is a significant deferral of Customs duty payments pending the completion of all equipment.

Non-Financial Considerations

There are a number of non-financial advantages that should be seriously considered. With the reduction of Customs entries comes the reduction of the overall paperwork burden. Since merchandise held in a foreign-trade zone is not subject to country of origin marking, there may be significant savings in US Customs inquiries concerning marking. The FTZ can be used, once the final destination is known, to apply the correct marks and labels for the destination country. This obviates the need for inventory segregated by destination and products that are pre-determined for fixed markets. Since merchandise can be admitted in bond quickly to a foreign-trade zone, the normal delays found in Customs entries can be avoided. The reduction in cycle time will result in the overall reduction of inventory levels for merchandise being held in the US for export markets.

Conclusion

Exporters enjoy a significant advantage by utilizing a FTZ. Companies involved in exporting should consider whether the cost of their exporting operations could be reduced through the use of a FTZ.

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