

## Extending Foreign Trade Zone Status to a Single Manufacturer

By Troy Post, CECd

### THE ECONOMIC DEVELOPER'S ROLE IN THE SUBZONE DESIGNATION PROCESS

Subzone designation, a Foreign Trade Zone (FTZ) classification existing under the auspices of the U.S. International Trade Administration (a division of the U.S. Commerce Department), can be a critical tool in maintaining the viability of American manufacturers that import components for a finished good. Although the designation has been available for a number of decades, subzones may not be known to many small and mid-size manufacturers in the U.S. economy. This article explains the FTZ program and the subzone designation. It suggests actions that a local economic development organization can take to ensure that its local manufacturing base takes advantage of the benefits afforded by this program.

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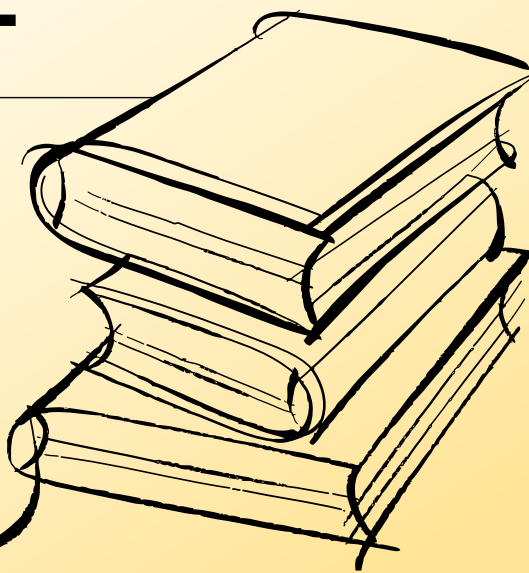


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# extending foreign trade

## ZONE STATUS TO A SINGLE MANUFACTURER

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### INTRODUCTION

As communities across the nation grapple with the increasing challenges of helping businesses stay competitive, especially those in the manufacturing sector, local economic developers should leverage tools and programs already available for use. One such program, which has been in existence for decades, is **Foreign Trade Zone (FTZ)** status under the U.S. International Trade Administration (ITA). By operating within such a zone, a manufacturing or assembly operation can defer part, or even all, duties charged on the import of components for manufacturing – a result which can better position the firm for competition in the global market, while increasing its viability in the local economy. This article provides a brief overview of the FTZ program and outlines the steps that a local economic developer can take to assist a company seeking subzone classification under the program.

### WHAT IS A FOREIGN TRADE ZONE?

The FTZ program, as regulated by the U.S. Commerce Department through the ITA, was created in 1934 specifically to aid American-based companies competing in international trade. Today, there are more than 250 general purpose FTZs in the nation.<sup>1</sup>

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import tax or restrictions on the number and type of materials brought into a country – the FTZ program makes imported materials (such as raw materials or finished goods considered as components) duty-free, provided that they are used in the manufacturing process to produce a “new” good. Thus, an assembler of automobiles could import certain goods or finished products like drivetrains or engines made abroad and avoid paying an import tax, as long as those goods and component products were used to manufacture a new good – in this case, an automobile.

But mere proximity to a FTZ does not allow a company to enjoy the benefits of the program. The manufacturing or assembly activity utilizing these imported components must operate within a designated FTZ area, hence the nomenclature “zone.”

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### THE ECONOMIC DEVELOPER'S ROLE IN THE SUBZONE DESIGNATION PROCESS

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These zones are geographical areas considered by the federal government to be, in effect, outside the bounds of the U.S. Customs & Border Protection (CBP) office and its taxing authority,<sup>2</sup> although the CBP is involved in FTZ monitoring and compliance. Within that designated zone area, select categories of merchandise can be imported without undergoing formal U.S. Customs protocol for the payment of import taxes.

Duty-free status may also be accorded to certain items salvaged, repackaged, cleaned, or processed in an FTZ.<sup>3</sup> In those cases, duty payments are not levied until goods are brought out of the FTZ designated area and shipped for sale in the domestic market.

Operating within an FTZ can have other benefits for a manufacturer or assembly operation, such as:

- Reducing or eliminating duties on materials subject to defect, damage, waste, or scrap;
- Providing unlimited time for inventorying finished goods without a duty payment, thus allowing the firm to determine the best time for introducing goods to a market;
- Reducing or eliminating delays in clearances from the CBP;
- Identifying sub-standard goods to be destroyed or returned without duty payments, through quality control inspections while goods are within an FTZ;
- Alleviating duties owed on the intra-FTZ transfer of merchandise; and
- Suspending federal quotas or restrictions on certain imported products, in some cases.<sup>4</sup>

With each benefit listed above, the FTZ program can yield immediate savings and directly impact the cash flow of a manufacturing operation. But beyond aiding a particular company, the presence of a FTZ can benefit the local community as well. Being aligned with a FTZ is an important consideration used by many manufacturing firms to determine whether to locate or expand within a particular community. The presence of an FTZ, or affiliation with one, can demonstrate to prospect firms that a community has companies actively engaged in the global economy. That, in turn, can help brand the communi-

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ty as an international business location and potentially drive more commerce to the area.

## IS A “FREE TRADE ZONE” THE SAME AS A “FOREIGN TRADE ZONE?”

Occasionally, the word “free” is substituted for “foreign” in discussions on FTZs. However, a **free trade zone** generally refers to an area occupied by U.S. companies abroad, in which quotas for goods or taxes on goods imported into foreign nations are eliminated or relaxed due to less regulation by those state governments.<sup>5</sup> These free trade zones are designed to encourage capital investment in those countries, which can lead to greater job and income opportunities for its citizenry. Firms can move into a free trade zone, produce a product, then distribute the finished good – either domestically or internationally – without being taxed or restricted in the number of goods produced.

While a free trade zone is similar in concept to that of an FTZ, the word “foreign” should be used when discussing the attributes of the ITA’s program for manufacturers. This distinguishes it as a domestic program, applicable to lands and territories located within the U.S. and regulated by the CBP.

## GENERAL PURPOSE ZONE

There are two types of foreign trade zone classifications in the United States. The first is a **general purpose zone**, or GPZ, which may be sponsored by a state or local government, a transportation authority, or even an economic development group.<sup>6</sup> Once an application for this classification has been approved by the U.S. Foreign Trade Zones Board, the sponsoring entity becomes the “grantee” of the designation and is permitted to operate an FTZ.<sup>7</sup>

These GPZ designations may cover multiple facilities within a particular area, although the size (in acres or square feet) can vary. They may also include public facilities or developments used by more than one company, such as an industrial park or a seaport.

In the city of Savannah, Georgia, for example, the Savannah Economic Development Commission operates FTZ #104, which includes space within the Savannah International Airport complex, along with locations scattered among existing buildings and available land in several adjoining counties in Georgia.<sup>8</sup> It is a general purpose zone used by multiple firms to ship product in and out of the port facilities in Savannah, the local airport, and through the highway corridors surrounding that particular metro area.

## THE ROLE OF THE CBP

Integral to the operation of the FTZ program is the oversight provided by the U.S. Customs and Border Protection (CBP) Office. The CBP is responsible for monitoring activity within a designated FTZ. In that regard, the CBP reviews every application for a zone designation. And since all goods and merchandise located within a zone fall under the control of the CBP, it may conduct on-the-spot inspections and reviews to determine compliance with federal regulations, once an application has been approved. For more information on the CBP, visit [www.cbp.gov](http://www.cbp.gov).

In 2009, the U.S. Commerce Department instituted a new, optional management process for FTZs, known as the Alternative Site Framework (ASF), which essentially produced two types of GPZ site designations.<sup>9</sup> One of those designations, **magnet site** (or magnet GPZ site), refers to an area or building property or properties pre-designated by a FTZ grantee to serve multiple operators.<sup>10</sup> Magnet sites include industrial parks and logistics centers, and can vary greatly in size. In Indiana, for example, magnet sites range from more than 4,800 acres at the Indianapolis International Airport Complex to 123 acres contained within the Eagle Point Business Park in the city of Anderson, located to the northeast of Indianapolis.<sup>11</sup>

These sites are attractive to distribution and warehousing firms in particular, since they are not required to go through a formal application process for FTZ participation, given that the site has already been qualified by the grantee for FTZ benefits. Manufacturers may also take advantage of a magnet site, but a separate application to the regulatory body (the U.S. Foreign Trade Zones Board) is required for those users, referred to as “production authority.”<sup>12</sup> Regardless, the process for a manufacturer applying for FTZ program participation in a magnet site can still be less time consuming and less costly than seeking a subzone designation, the second classification of FTZs in the U.S. and one described later in this article.

The second type of GPZ site designation, **usage-driven sites** (or usage-driven GPZ sites), are areas dedicated to a specific company. Rather than accommodating multiple users scattered throughout many spaces inside a defined service area – as in the case with magnet sites – the usage-driven site is tied to one company and its affiliates. It is limited to the space solely needed by that company for the activities permissible within an FTZ.<sup>13</sup> Such was the case for an electrode manufacturing company in the city of Peoria, Arizona, which received approval in 2014 for a user-driven site within a 120,000 sq. ft. facility under FTZ #277.<sup>14</sup> These user-driven sites provide greater flexibility for firms that cannot move to space within a magnet site and are most often used by companies for warehousing product and operating distribution hubs.

Photo Credit: Farm Assist



*Syngenta crop protection products.*

## WHAT IS A “FREE PORT?”

To reduce business costs, some states offer personal property tax incentives for manufacturers. Operating within a “free port” area can make it possible for manufacturers located within a particular state to reduce or eliminate personal property taxes levied by local or state governments on products made in that state and stored for shipment outside the borders of that particular state. Though similar to a FTZ’s ability to defer or exempt taxes, “free ports” do not provide relief from federal tariffs or duties. Read how Macon County, Georgia, uses this incentive at: <http://www.maconcountygga.gov/freeport-exemption.cfm>.

## THE SIXTY MILES OR NINETY MINUTES RULE

Establishing a general purpose zone involves several requirements. Two key criteria include the proximity of the proposed GPZ to a port of entry into the U.S. and the submittal to the U.S. Foreign Trade Zones Board of a “demonstration of benefit,” showing the economic impact of a FTZ on the community where such a designation would be granted.

Since the FTZ program is centered upon the import of products and goods into the U.S., all FTZs must be located within a certain radius of an international port of entry (typically an air or seaport) staffed by a CBP office. This provision aids personnel in conducting their work as inspectors and enforcers of import laws and regulations.

Known as the **Sixty Miles or Ninety Minutes Rule**, a FTZ must be located within either sixty (60) miles from the closest CBP port of entry, or within a ninety (90) minute drive.<sup>15</sup> Although some discretion remains with CBP officials to determine precisely what constitutes a 90-minute drive (depending upon speed limits, highway infrastructure, and congestion/traffic patterns), it is likely that any community located substantially more than 60 miles *by roadway* from a CBP office will have difficulty in establishing a FTZ.<sup>16</sup>

If the distance rule can be met, then a **Demonstration of Benefit** statement must be created. Typically, this document describes the local economy, including the identification of firms or clusters of firms that are engaged in international trade or could be interested in such activity, but for the existence of the FTZ program.<sup>17</sup> It also details how the FTZ would impact the community through those firms, but not adversely impact U.S. commerce practices.<sup>18</sup> The local economic developer can be especially helpful in providing information on the local economic base to an entity seeking the FTZ designation.

## THE SUBZONE PROGRAM

A second type of foreign trade zone in the U.S. is the **subzone**, or SZ classification. A SZ is a special purpose FTZ site for use by one company for a limited purpose, such as the assembly of a product or the manufacturing of a line of products.<sup>19</sup> In Louisiana, for example, a recently-approved subzone application covers a facility used by the global agribusiness firm Syngenta for producing crop protection products, such as herbicides and insecticides.<sup>20</sup>





Cargo ships at Port Canaveral, Florida.

The subzone status offers all the advantages of the FTZ program, but – unlike a user-driven GPZ site – involves a single firm's location, where the relocation of that manufacturer to a GPZ site is not practical or desired. (User-driven sites, though tied to one company, can exist in more than one area.) Today, there are more than 400 subzones located throughout the U.S.<sup>21</sup> In some FTZs, a number of subzones exist; in others, like FTZ #136 in Port Canaveral, Florida – which has six GPZs – there are only two SZ operators.<sup>22</sup>

To establish a subzone, requests are made directly to an existing GPZ, which in turn, files a request with the U.S. Foreign Trade Zones Board, asking for permission to reorganize the GPZ's boundaries to include the new proposed service area or site. The request to the GPZ identifies the proposed service area and describes how it complies with the Sixty Miles or Ninety Minutes Rule. If the proposed area has the potential of being served by more than one CBP office, then it is advised that the U.S. Foreign Trade Zones Board be contacted for guidance on determining which port of entry (and hence, which GPZ) should be listed.

Applying for a new SZ consists of several requirements, beginning with a **letter or executive summary**, which identifies the company and explains why the application would benefit the company and the U.S. economy.

A **statement of economic justification** provides a compelling economic reason for why the existing GPZ should modify its service area. There is no template for this, but generally it details the company's operation and its industry, including:

- Challenges and strengths facing the firm;
- Employment size and market share;
- Why the operation could not be supported elsewhere;
- Whether the company has other plant sites or locations in the U.S. or overseas;
- How the designation would affect purchasing plans;

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- Current annual production at the plant site seeking the designation;
- Identification of major competitors and the industry's competitive factors; and
- Estimated total savings to be realized by operating under the designation.<sup>23</sup>

In short, the equivalent of a corporate business plan is provided, much as if the firm was seeking financial assistance from a conventional lender.

Augmenting this economic justification statement, **information on the local economy** provides an overview of current trends and developments affecting it. This identifies the local economy's strengths and weaknesses, and how the designation would help the region maintain economic vitality.

A **site description** identifies the proposed SZ's acreage or square footage (if a single structure), improvements upon the land (i.e., buildings), and any planned or existing activities at the site.<sup>24</sup> This also includes a legal description of the property to be designated; a survey is recommended.<sup>25</sup>

In lieu of a survey, **mapping data** can be submitted, showing the boundaries of the property and its adjoining uses.<sup>26</sup> This need not be U.S. Geological Survey (topographic) map data, but rather mapping that shows major roadways, landmarks, and communities.

### A SUBZONE EXAMPLE

The LEEVAC shipyard facility in Jennings, Louisiana, is an example of a subzone. Located on the west bank of the Mermentau River, the site has a total operating area of 180 acres, and is fully equipped to handle the construction of tugboats, barges, and other offshore supply vessels. The company, which dates to 1913, operates three shipyards in Louisiana. For more information on LEEVAC and its Jennings operation, visit the firm's website at [www.leevac.com](http://www.leevac.com).

The *operation and financing of the SZ* details the security measures to safeguard the firm's products and guarantee that no non-zone items are moved to the designated area.<sup>27</sup> This is especially critical, since the SZ will be subject to code enforcement by the closest CBP office, which has a legal obligation to ensure that zone boundaries and records are properly maintained.

The applicant must also certify that it has the authority to request the designation, which includes evidence that the organization is a legal entity and is permitted by law to participate in the FTZ program. In most states, a secretary of state's office can provide a **certificate of corporate standing** to validate the entity's existence. Resolutions from the applicant, citing the firm's duly appointed representatives and its ability to make program commitments, are suggested.<sup>28</sup>

Lastly, the applicant provides **information on the type of products and components** that will be stored within the proposed designated area. This includes finished products that will be made, along with finished goods intended for export to international markets. The Harmonized Tariff Schedule of the U.S. (HTSUS), the source for determining customs duties on goods brought into the country, contains the HTSUS codes for goods that would be stored in the SZ.<sup>29</sup>

### THE ROLE OF AN ECONOMIC DEVELOPER IN A SUBZONE APPLICATION FOR A MANUFACTURER

Given the tax-deferred advantages of the FTZ's subzone designation to a manufacturer, it should be the task of every economic development official to determine if the program could be used to help manufacturers in the economic developer's specific service area. Beyond networking with the local manufacturing base – and knowing which firms might benefit from the designation, given the amount of imported materials used – the initial determination for community participation should be based upon the compliance with the Sixty Miles or Ninety Minutes Rule, regarding proximity to a CBP port of entry.

This determination is relatively easy for a local economic developer to make, given that all such CBP office locations are identified on the agency's website.<sup>30</sup> In some cases, a potential SZ located outside the Sixty Miles or Ninety Minutes radius may still qualify if

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**For additional information** on the FTZ program specifically and on similar free trade zones worldwide, visit these websites:

<http://enforcement.trade.gov/ftzpage/> - U.S. Foreign Trade Zones Board, U.S. Commerce Department, International Trade Administration

[www.naftz.org](http://www.naftz.org) - National Association of Foreign Trade Zones

[www.freezones.org](http://www.freezones.org) - World Free Zones Convention

[www.cbp.gov](http://www.cbp.gov) - U.S. Customs & Border Protection

the port director at the closest CBP office determines that proper oversight of import administration procedures is possible.<sup>31</sup>

Next, the local economic developer should identify and contact a FTZ that could potentially expand its service area to include a new SZ. This necessitates research on existing FTZs in a particular state and correspondence with a FTZ to determine its interest in receiving a SZ application.<sup>32</sup> If more than one FTZ could service the local economy, the local economic developer should contact the U.S. Foreign Trade Zones Board for direction.

Communicating the advantages of the program to the community's existing manufacturing base should be the next task for an economic development office (EDO). That might include hosting networking events between local companies and officials from an existing FTZ or conducting seminars on FTZs, to increase awareness of the program. It could also involve communicating updated information on the FTZ program, as new regulations or changes are introduced.

Costs are involved in filing a SZ application. In determining a manufacturer's interest in proceeding, the local EDO could assist a prospective applicant with understanding the fees required. The local economic developer might even help the company identify private sector consultants in the field, individuals or firms that provide expertise in the application process, particularly for applicants unfamiliar with federal programs or the documentation typically required. Many of these consultants provide services after the application process has been completed, helping the company monitor and manage its SZ once designation has been received.

If a company wants to proceed with submitting a SZ application, the local economic developer could assist the company with several aspects of that process, most notably through data compilation for the statement of economic justification and the report on the local economy. In this regard, generating a written **economic assessment** on the local economy – a task that all EDOs should engage in periodically – should provide the applicant with the relevant information to document the current state of the local economy and the impact that the SZ status could have on it. These assessment reports generally include notations on:

- Local economic conditions (select statistical information on the market);
- Current economic activity (recent local business activity, including new business announcements);
- Future local trends and developments (a forecast of expected or planned developments);
- Community attributes (the area's "quality of place"); and
- Development capacities (resources/incentives available to induce business investment in the area).<sup>33</sup>

Another key role that the local economic developer plays in the application process is help with assembling letters of support from affected jurisdictions and other community partners concerned with the area's economic vitality. These provide evidence to the FTZ that the economic impact of the designation would extend beyond a single company. The request for letters might also help spread awareness of the FTZ program, further increasing the likelihood that other companies in the community would learn of the program's advantages.

The FTZ, as part of its application review process, may ask the EDO to assist it with surveying existing manufacturers in an area, to determine the level of export activity currently existing in the community. This is a critical part of the FTZ analysis, given that it must make a case before the U.S. Foreign Trade Zones Board to amend its service area to accommodate the applicant business. Considering the interaction typical between an EDO and the local business community, this is the type of information that an EDO has readily available, if it practices ongoing networking efforts and retention programs.

In fact, helping a company obtain a SZ designation should be part of a larger service offered by an EDO – assisting companies in developing an export program. When firms export, they import money into the local economy. To facilitate this, the EDO can offer an export assistance program for firms on how to develop markets internationally and how to use tools like FTZ status to

The FTZ program can be very beneficial to manufacturers or assembly operations that import raw material or components used in producing a finished good, by deferring or avoiding tariff duties. One option, instead of creating a new FTZ, is to work through an existing FTZ to have a site-particular designation of a subzone (SZ) – a designation which permits a company to enjoy the benefits of being located within an FTZ.

make exporting activities competitive. In this regard, the EDO could coordinate information from a number of program providers, from state international trade offices to federal agencies (such as the U.S. Export-Import Bank), and make it available to local firms.

## CONCLUSION

The FTZ program can be very beneficial to manufacturers or assembly operations that import raw material or components used in producing a finished good, by deferring or avoiding tariff duties. One option, instead of creating a new FTZ, is to work through an existing FTZ to have a site-particular designation of a subzone (SZ) – a designation which permits a company to enjoy the benefits of being located within an FTZ. The role of an economic developer is to determine if a SZ is attainable and then to assist a manufacturer or assembler seeking the designation with the application process. If a SZ designation is awarded, the money saved by a firm will likely be reinvested into the company, thereby improving its market position and retaining – if not creating – jobs for the local economy. 🌐

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