

Foreign Trade Zones

IN THE ELECTRONICS INDUSTRY



**Logistics &
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Powerful Impact:

How 3PLs with Foreign Trade Zone Capabilities Can Reduce Operating Expense and Increase Cash Flow

A WHITE PAPER BY ATC LOGISTICS & ELECTRONICS (ATCLE)

Introduction

Gaining an advantage over industry peers is the goal for every business. In today's highly competitive global economy, companies are seeking every advantage to dominate the marketplace. With reliance on foreign manufacturing for many industries, pursuing markets in the United States and North America equates to significant import duties, taxes and other fees. As such, it is a natural area to explore for cost cutting measures.

Foreign Trade Zones (FTZ) were created by the U.S. Congress in 1934, to stimulate commerce, facilitate trade and boost employment as a result of the elimination or reduction of import expenses. They are specific areas considered outside the territory of the U.S. to conduct storage, distribution, manufacturing, assembly, inspection and testing, as well as repackaging of goods.

FTZs are more viable now than ever as evidenced by sizable gains in the value of shipments that have entered them throughout the last decade. According to annual reports from the Foreign Trade Zones Board to the U.S. Congress, the combined value of shipments into FTZs jumped from \$177.8 billion in FY 1997 to \$502 billion in FY 2007. That is a staggering increase of 182 percent, with no apparent slowdown in sight.

The benefits of FTZs are obvious for the reduction of import charges alone. However, to take full advantage of FTZs, and the services permitted within them, third-party logistics (3PL) providers that conduct kitting & packaging, light manufacturing, 'last-mile' finishing and testing services offer an even greater advantage. Plus, by working with a 3PL, fixed costs for labor, transportation and administrative operations can be avoided and instead "variablized"¹, making the partnership an attractive option for many companies.

3PL providers with these capabilities are in a unique position to not only transport and process inventory, but also assemble, test and package products within the zone to accelerate the overall supply chain. When coupled with an advanced 3PL partner, manufacturers have a tremendous amount to gain from an FTZ without the investment otherwise required for going it alone.

¹ [Click here](#) to download "Logistics Insight: How the Electronics Industry Can Flourish in a Down Economy with Outsourced Variable Cost Platforms."

FTZ Benefits

Merchandising Processing Fees Reduction

Merchandising processing fees (MPF) can be a huge drain, especially for high volume products such as electronics. Under current regulations, a fee must be paid on every importation through Customs (both devices and accessories) based on .21 percent of the value, with a maximum fee of \$485 per import shipment. These charges can quickly accumulate for medium-sized shipments, creating a major residual expense.

With an FTZ, the MPF can be consolidated on a weekly basis, known as a “Weekly Entry Process” (WE), which allows products to be imported 24/7/365 requiring only a single weekly payment, peaking at \$485 for each transaction, or an annual maximum of about \$25,000. Many companies pay hundreds or thousands of dollars in MPF under standard import procedures. A quick calculation of current MPF spend versus the annual FTZ payment of \$25,000 reveals the often considerable savings in this category alone.

Duty Savings

From duty deferrals and reductions, to outright elimination, an FTZ makes an immediate bottom line impact on import expenses that improve a company's cash flow.

- **Deferral:** Devices that are within an FTZ will only be charged import duties once they are withdrawn from the zone and enter the United States. What's more, they can stay within the FTZ indefinitely.
- **Reduction:** Outside an FTZ, an import duty can be applied to each component, as well as the device, such as a cell phone and batteries. If the phone, battery and other components are packaged into a single unit within an FTZ, there is only one duty charge upon export, as opposed to multiple fees.
- **Elimination:** In the event that a device is within an FTZ and shipped outside of the United States, there is no duty whatsoever. If merchandise and material enter the FTZ and later become scrap, there are no duties.

Reduced Inventory Tax

For states with inventory taxes, goods in inventory may incur business/personal property taxes. With an FTZ, however, foreign goods never officially enter the commerce of the U.S., and are therefore not subject to this tax, unless the inventory remains in the state for sale. The tax on units headed to other destinations is avoided altogether. This makes doing business in states with inventory taxes far more cost effective, while still benefitting from preferable geographic locations.

Accelerated Supply Chain

A 3PL operator of an FTZ can create a host of efficiencies in supply chain operations that can reduce overall costs and improve speed to market, thereby increasing sales. Port delays can be avoided by bypassing Customs at the port(s) of arrival into the U.S., moving merchandise directly into an FTZ. For example, if goods are being air shipped from China to an international airport, they can be directly delivered to an FTZ. Customs clearance isn't required until the goods leave the FTZ, which saves import processing time.

A 3PL with advanced capabilities such as kitting & packaging and test & repair further enhances the value of an FTZ. With these services in place, time sensitive foreign components can be flown in bulk from overseas while low-value bulk packaging materials can be sourced locally to reduce freight costs. Accessories and components, such as batteries and chargers, with higher rates of duty than the core devices, can be admitted, stored, and kitted in the FTZ to avoid, defer or 'invert' tariffs. This also offers the flexibility to alter packaging or conduct software reflashing to increase marketability.

Savings Scenario: Utilizing a 3PL with an FTZ Offering

In a hypothetical situation, a leading consumer electronics manufacturer with a strong North American market presence and high volumes of goods, sought to reduce its import expenses. The company has a partnership with a Texas-based FTZ-approved 3PL provider that possesses centrally located facilities in the DFW Metroplex, in close proximity to international air and an inland ports. The Texas location is essential, as it provides direct access to key markets throughout the continent. Most importantly, the 3PL partner offers advanced kitting & packaging, and testing & repair services.

With the combination of location and strategic distribution, as well as kitting & packaging and testing & repair services, the manufacturer was able to harness the full savings power of an FTZ. It all started by shipping units in bulk from APAC via airfreight to maximize load capacity and avoid transporting packaging materials.

The primary unit was shipped directly into an FTZ to defer tariffs, keeping expenses low, and saving precious time in speed to market. The 3PL imported accessories, including batteries and chargers, and procured packaging materials locally to further reduce operating costs. Additionally, testing & repair could be performed by the 3PL for last minute software upgrades or reflashing. Packaging could also be customized to coincide with actual order destinations and/or special promotions, along with seasonal surges such as the "Black Friday" holiday.

The flexibility of packaging and updating software on site greatly improved the manufacturer's ability to adapt to shifting market demands, which helps enhance relationships with retailers and boost sales. Beyond the FTZ cost reductions, the 3PL saves the customer approximately two dollars per unit by shipping in bulk and conducting packaging processes within the zone. As for direct benefits from operating in an FTZ, in the first full year of implementation, savings from duty reductions, lower MPF and the avoidance of Texas' inventory tax, has been dramatic:

OVERALL VOLUME	5 Million Units
Duty (INVERTED TARIFF THROUGH MANUFACTURING)	~\$416,000
MPF	~\$58,000
Inventory Tax	~\$166,000
TOTAL SAVINGS	~\$640,000

Savings are expected to grow as volume increases as a result of the financial benefit from the FTZ and specialized 3PL services. With growth in volume and greater market penetration, sales are anticipated to increase accordingly.

Tips for Selecting a 3PL/FTZ Partner

Selecting a 3PL/FTZ partner is a critical decision not to be taken lightly. Manufacturers must rely upon their partner to be in full compliance with Customs regulations on their behalf to avoid serious financial penalties (\$1,000 per day for each violation). They are also entrusting valuable inventory that must be closely managed to prevent loss or damage in transport or within the FTZ.

When choosing a partner, closely consider the following:

- A partner should have a complete understanding of FTZ polices and the ability to dissect an entire supply chain to generate the maximum amount of savings for customers.
- To obtain the full financial benefit from an FTZ, the 3PL should possess specialized services, including kitting & packaging, testing & repair and transportation management, etc.
- Location of the FTZ is critical. To streamline supply chain and improve speed to market, the partner should be located in close proximity to an international airport and/or inland port. Preferably both.
- Because theft within an FTZ is a felony and considered smuggling, “Best-in-Class” security and inventory measures are essential to avoid liability:
 - *Especially important for small electronic devices due to high value and compact size that could potentially contribute to theft.*
- A partner should have rigorous personnel controls in place, supported by thorough background checks to confirm legal status and reveal any criminal history for those with direct access to inventory.
- Comprehensive administrative capability, with broad understanding of Customs processes and procedures.

Looking Ahead...

As the global economy continues to expand, forward-thinking manufacturers must explore every avenue to reduce import cost as they pursue new markets. But the strategy for success doesn't stop with utilizing an FTZ. Establishing a partnership with a sophisticated 3PL provider that offers the

flexibility of direct bulk shipping and advanced services such as kitting & packaging and test & repair, can reduce cost even further. This will allow companies to avoid fixed supply chain costs, while taking advantage of an FTZ in an accelerated timeframe without the administrative burden.

About ATC Logistics & Electronics

ATC Logistics & Electronics (ATCLE), is a premier provider of third-party logistics (3PL) and supply chain services. The company also operates a Foreign Trade Zone (FTZ) at its facility in Fort Worth, Texas. ATCLE specializes in forward logistics, reverse logistics, asset recovery, test & repair, kitting & packaging, transportation management and value-added services for high velocity, high-tech devices, in addition to other equipment and components. Industry focus includes wireless, broadband, electronics, medical, industrial and automotive. ATCLE's knowledge, expertise, IT capabilities and 99.5 percent service and quality levels enable its customers to streamline supply chain efficiency and enhance growth and profit. With a customer roster including AT&T, GM, LG, Pantech and TomTom, ATCLE raises the standard for quality, service and performance.

For more visit: www.atcle.com.