

Rapid City/
Black Hills
Region
Foreign Trade
Zone
Feasibility
Study

Interim Report to Mayor Sam Kooiker on the Feasibility of a Foreign Trade Zone in
Rapid City, South Dakota, or the Black Hills of South Dakota

To:

Sam Kooiker, Mayor of Rapid City South Dakota
Economic Development Leaders in the Black Hills and Upper Plains Region
Business Leaders in the Black Hills and Upper Plains Region
Business Leaders Considering Relocation to the Black Hills Region
Interested Members of the Community

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<i>Executive Summary</i>	2
<i>Introduction</i>	5
<i>Theoretical Discussion</i>	5
Definition of a Foreign Trade Zone	5
History	6
Benefits	6
Current Situation in Rapid City, SD and the Black Hills of South Dakota	7
<i>Data Acquisition</i>	8
<i>Procedures</i>	9
<i>Data Presentation</i>	10
Importing Companies	10
Data from Similar Sized Cities within Approximately 400 miles	12
<i>Analysis</i>	14
<i>Discussion of Overall Results</i>	14
<i>Assess the Results</i>	15
<i>Conclusions and Recommendations</i>	15
<i>Citations and Bibliography</i>	16

Executive Summary

A **project was conceived** at the request of Mayor Sam Kooiker of Rapid City, SD, and fellow community leaders to investigate the feasibility of obtaining Foreign Trade Zone (FTZ) status for a geographic location in Rapid City, or the Black Hills of South Dakota. The effort was initially spearhead by John C. Quinn through the Center for Business and Economics but after he passed away it was taken over by a subset of the members of the Task Force and they have been performing due diligence, prior to committing city funds leading to FTZ status.

Eighty separate companies or individuals were identified as having imported something into the Black Hills in 2012. Nine of the largest importers, concentrated within ten miles of downtown Rapid City were selected to determine their levels of imports, duties paid,

and any prospective operational savings accruing to the individual importer by using an FTZ. Only one company was identified as having significant import \$ values, (\$321,130.71) which was **not** located within the Rapid City metro area. That company was located in Pine Ridge and judged to be too much of an outlier to be relevant to the purposes of the project.

The minimum cost of having a Customs and Border Patrol (CBP) officer in residence is about \$150,000 per year. There are additional costs of administration, for an FTZ operator, segregating FTZ goods from non-FTZ goods, and the additional strict record-keeping requirements of having goods in an FTZ. These additional costs could quite easily add another \$25,000 to the costs of having a CBP officer, and bring the bare bones expenses of operating an FTZ to \$175,000 per year.

Obtaining sub-zone status of an existing FTZ, in the Black Hills Region, was investigated. And while CBP is fairly flexible in providing service, they are not willing to support a sub-zone that is located 340 miles from the nearest FTZ (Sioux Falls). And from previous experience, one of the authors of this report has determined that 100 miles from an FTZ is about the outer limit at which CBP is willing to dispatch an officer for inspections and related duties.

The largest \$ value of imports of any company on the list was **\$1,572,748.79**. This value was a one-off situation, and would not be repeated again, in any subsequent year.

The second largest \$ value of imports was: **\$1,011,930.31**. This company's imports were relatively stable over time. Their highest duty rate was 3.2% on any goods imported. This company does no remanufacturing of imported products, and imported products are immediately shipped directly to customers at various locations across the U.S. No cost saving opportunities was discovered for this company to operate inside an FTZ.

The **highest duty rate** any company in the survey was paying was **3.2%**.

At that rate **no company surveyed would save money by using an FTZ.**

During the due diligence process, it gradually became apparent that growing our already substantial Tourism Industry by **obtaining a CBP officer to clear passengers on internationally originating flights** may have a better chance of succeeding in developing the economy of Rapid City and the Black Hills Region than obtaining FTZ status.

To that end, we are engaged in performing the due diligence to determine the feasibility of getting a **CBP agent assigned to the Rapid City Regional Airport**, for passenger clearance of incoming international flights, and for local residents returning from outside the U.S. Due to CBP regulations, the largest number of passengers one CBP agent can clear alone is 20. While this limits the size and number of aircraft that can be cleared at

one time, it presents the opportunity to save money in infrastructure costs by having the CBP Customs Clearance located in the facilities of one of our privately owned **Fixed Base Operators (FBO)**.

Our current recommendation is to cease any efforts regarding obtaining FTZ status, and instead concentrate on determining if economic justification can be made for obtaining a CBP officer for passenger clearances, at Rapid City Regional Airport.

We further recommend working with other municipalities and stakeholders within the Black Hills Tourism Industry to determine their needs, and to obtain buy-in for a CBP officer at Rapid City Regional Airport. And to determine if funds can be obtained from these interested parties for startup costs and ongoing operating costs for a certain period, probably not more than three to five years.

We are currently working with our **largest Fixed Base Operator (FBO), airport management, and the Chicago Customs Office** to determine what options are available to the City of Rapid City for passenger clearance services.

A final report, with final recommendations is anticipated within the first half of 2014.

Introduction

This project was conceived at the request of Mayor Sam Kooiker and fellow community leaders to investigate the feasibility of obtaining Foreign Trade Zone (FTZ) status for a To Be Determined site in Rapid City or the Greater Black Hills Area of South Dakota. The effort was initially spearheaded by John C. Quinn through the Center for Business and Economics, but after he passed away in January 2013 it was taken over by a subset of the members of the Task Force and additional volunteers. The approach includes:

1. Contact Rock Nelson, Director of South Dakota's International Trade Center, to determine what Sioux Falls has done with their FTZ and airport customs clearance facilities.
2. Visit Sioux Falls FTZ and airport customs clearance facilities.
- 3... Survey top management of companies in the immediate area that are currently importing products from outside the U.S.
4. Determine their level of Import Duties being paid and, whether operational savings would accrue through use of a Foreign Trade Zone (FTZ).
5. Survey cities of a similar size within an approximately 400 mile radius to determine if they have an FTZ, the volume of transactions entering and leaving the FTZ, and whether the FTZ is self-supporting.
6. If the similar sized city does not have an FTZ, determine whether the city has investigated obtaining FTZ status, and why the city chose not to obtain FTZ status.

Theoretical Discussion

Definition of a Foreign Trade Zone

"A foreign-trade zone (FTZ) in the United States is a geographical area, in (or adjacent to) a [United States Port of Entry](#), where commercial merchandise, both domestic and foreign receives the same Customs treatment it would if it were outside the commerce of the United States. Another definition of an FTZ states that it is an isolated, enclosed and policed area operated as a public utility, furnished with facilities for loading, unloading, handling, storing, manipulating, manufacturing and exhibiting goods and for reshipping them by land, water or air. Merchandise of every description may be held in the Zone without being subject to [Customs duties](#) and other [ad valorem taxes](#). This tariff and tax relief is designed to lower the costs of U.S.-based operations engaged in [international trade](#) and thereby create and retain the employment and [capital investment](#) opportunities that result from those operations. These special geographic areas – Foreign-Trade Zones – are established "in or adjacent to" U.S. Ports of Entry and are

under the supervision of the [U.S. Customs and Border Protection](#) under the [United States Homeland Security Council](#). Since 1986, U.S. Customs' oversight of FTZ operations has been conducted on an audit-inspection basis known as Compliance Reviews, whereby compliance is assured through audits and spot checks under a surety bond, rather than through on-site supervision by Customs personnel.

There are over 230 Foreign-Trade Zone projects and nearly 400 Subzones in the United States.⁽¹⁾

History

"The U.S. Foreign-Trade Zones program was created by the Foreign-Trade Zones Act of 1934. The Foreign-Trade Zones Act was one of two key pieces of legislation passed in 1934 in an attempt to mitigate some of the destructive effects of the [Smoot-Hawley Tariffs](#), which had been imposed in 1930. The Foreign-Trade Zones Act was created to "expedite and encourage foreign commerce" in the United States.

Through [World War II](#), manufacturing activity was allowed only on a very limited basis. In 1950, the original act was amended to open up FTZ's to manufacturing, but it had little impact until 1980. In that year, Congress again amended the act so that products manufactured in the zones would not be assessed on U.S. value-added. This ensured that the only tariffs a producer inside the zone selling to U.S. customers would pay would be on the raw materials imported into the zone. This "integrated" model, which replaced the previous "island" model, spurred growth in the U.S. Foreign-Trade Zones program." (1)

There are two options for a company wanting to use the benefits of an FTZ.

1. Locate some or all of the company's operations within an existing FTZ.
2. Establish a sub-zone within the company's facilities.

There are advantages to each, but both options require strict physical control and record keeping, and the ability to pass a CBP audit at any time. These advantages come with costs. Examples are:

1. Expenses associated with moving goods in and out of the zone.
2. Managing the paperwork and records to ensure customs regulations are met.
3. Support (wages, benefits, training, etc.) of the CBP agent.

Benefits

"US Foreign-Trade Zones (FTZ's) pose multiple benefits, other than duty deferred and inverted tariff, which companies can use to benefit their bottom line. However, a majority of companies are not utilizing FTZ's to their full potential because sometimes the unknown creates uncertainty.

Some of the benefits of operating a **FTZ** include:

- Improved inventory management

- Automated recordkeeping and document storage
- Increased visibility of the supply chain
- Improved cash flow
- Improved company compliance “ (1)

Current Situation in Rapid City, SD and the Black Hills of South Dakota

Rapid City and the Black Hills region has grown up around, and to this day are still dependent upon, four distinct industries: Mining, Forestry, Agriculture, and Tourism.

Since World War II, the economy of Rapid City and the surrounding region has also benefitted from the proximity of Ellsworth Air Force Base (EAFB), a federal facility that injects significant monies into the local economy. There have been efforts on the Federal level to close EAFB. The region has been fortunate in that new missions have been found for EAFB, and it is currently in operation. That may not be the situation in the future. Any closure or downsizing of EAFB would have immediate and significant economic consequences to the entire region.

In an effort to diversify the local economy, the Mayor of Rapid City has put together an informal consortium consisting of city officials and volunteers from the community. The group is charged with investigating economic development opportunities for the city and region, and to report back to the Mayor.

One of the possible opportunities that arose during these meetings was the formation of an FTZ in the Black Hills Region.

This report is the (interim) result of the due diligence performed in determining the feasibility of an FTZ in the Black Hills Region.

Data Acquisition

During Fall of 2012, it was determined that the first step in the due diligence process should be to focus on the FTZ because it seemed to provide the potential economic benefits that would support and justify a Customs and Border Protection (CBP) agent assignment to the Black Hills area.

Sioux Falls Experience:

The first activity was to invite Rock Nelson, Director of South Dakota's International Trade Center, to speak to a group of Rapid City business members about Sioux Falls FTZ and airport customs clearances. He explained the benefits and differences between the FTZ and the airport customs clearances CBP and the current status. A follow up site visit to Sioux Falls was made by Jim Quinn to tour the FTZ facilities within Nordic Warehousing (Dave Lyng), visit the Sioux Falls airport facilities and meet with Rock Nelson and the CBP agent (Mike Horan) responsible for both facilities. A separate trip report has been provided for this activity but in summary:

1. The FTZ was not heavily utilized and the only had one company using it and it was limited to only 600 SF within the Nordic 480k SF facility
2. Most of the activity and requirements for the CBP agent were centered on customs clearances of private aircraft. They are clearing between 10 and 15 flights per month.
3. Rosenbauer America, Inc was actively pursuing an FTZ subzone designation within their manufacturing facility because they felt there are sufficient economic benefits to support the additional administrative burden and costs. They are importing components and assembling fire trucks for export which is ideal because all import duties can be avoided and they can control all materials directly within their facilities. The CBP agent only would provide regular inspections when required to verify imports and that controls are being maintained.

Survey of Regional Importers:

The second activity was related to trying to quantify the economic benefits of the FTZ and survey current importers in the Region to determine three key factors:

1. Dollar Value of imported goods.
2. Duty Rate on imported goods.
3. Whether the importer could cut operating expenses by using the services of an FTZ.

We contacted a commercial provider of ocean import data (PIERS, a subsidiary of JOC Group <http://www.joc.com/group/joc-group>) and inquired as to the availability of statistics for importers in the Black Hills Region. The report was very small (only about 80 separate listings) and PIERS provided that information to us free of charge. (Thanks to Joe Davis, 415-947-6362, jdavis@piers.com)

The report was for 2012, and was in Excel format, which made it easy to sort on the most relevant categories.

We sorted the spreadsheet on the \$ value of imported goods. That sort provided a ranked list of importers by \$ value. The top importer on the list imported \$1,572,748.79 worth of goods into the United States. The smallest imported \$338.84.

Cities represented on the list include: Belle Fourche, Black Hawk, Custer, Deadwood, Ellsworth AFB, Fruitdale, Hermosa, Hill City, Hot Springs, Nemo, Piedmont, Pine Ridge, Rapid City, Spearfish, Sturgis, Wall, and Whitewood.

Due to cost of travel, and geographical concentration considerations, it was arbitrarily decided to contact the top 9 companies in import dollar value in Rapid City and Piedmont. The company at the number 9 position represented just a little under \$200,000.00 of import dollar value. By this point, we had determined from talking with the Sioux Falls FTZ that the annual cost of an FTZ would probably be in excess of \$150,000, and that any company importing less than 2X that amount would probably be a poor candidate for an FTZ, because they would not be able to generate enough savings to justify the added costs of FTZ participation. The largest importer NOT close to Rapid City was in Pine Ridge and represented \$321,130.71 in import value.

Procedures

The top 9 companies were contacted by phone and email. The appropriate employee was identified, and an explanation was provided regarding our mission, and how the individual could be of assistance to us. All but one of the participants were very helpful and generous with their time and sensitive company data. Data gathering was conducted either in a face to face interview or during a phone call.

One of the promises we made to the participants was we would do everything possible to protect their company data. In that vein, we gave each participant power of veto on any data that will be included in this report. Each participant has had the opportunity to view the entry for his company, and has given approval to the information for his/her company as presented in this report. To protect confidentiality, companies will not be identified by name.

Data Presentation

Importing Companies

Company # 1: \$1,572,748.79 in Import Value

A one time purchase of automotive related equipment. The company does not intend to do any more importing. Little or no opportunity for benefitting from an FTZ

Company # 2.: \$1,274,278.38 in Import Value

Imports manufactured building materials; panels, etc. from China.
Highest duty rates are 3.2%.
Goods usually go immediately to customer Distribution Centers, not held in inventory in Rapid City.
Savings not high enough to offset the cost of FTZ expenses.

Company #3: \$1,011,930.31 in Import Value

Imports electronics, steel enclosures, mostly from China.
Duty rates are very low and included with the invoice sent from their freight forwarder.
The only advantage of an FTZ for them would be in the time value of money.
Would not outweigh the expense of an FTZ.

Company #4: \$686,627.53 in Import Value

Imports electronics, fiberoptic light guides, nonwoven garments, medical gloves into North Carolina and South Dakota.
Duty rates are very low (1% - 2%) and the dollar values are “relatively small”.
The only advantage of an FTZ for them would be in the time value of money.
Would not outweigh the expenses of an FTZ.

Company #5: \$430,034.74 in Import Value

Imports children’s toys. Shipments usually go immediately to their distributors, some inventory held in Rapid City.
Duty rates are either very low or 0%.
Savings not enough to offset the cost of FTZ expenses.

Company # 6: \$357,506.84 in Import Value

Imports assembled furniture.
Was unwilling to participate.

Company # 7: \$253,047.06 in Import Value

Imports manufactured wood components; furniture, cabinet, retail items, etc. from China, Europe and South America.

Highest duty rates are 3.2%.

Goods usually go immediately to customer Distribution Centers, very little held in inventory in Rapid City.

Savings not enough to offset the cost of FTZ expenses.

Company # 8: \$246,399.52 in Import Value

They import jewelry, watches, jewelry boxes, etc to supply all of their stores (53) from Montana to Minnesota and North Dakota to Oklahoma.

Rapid City is their central distribution point for all their stores.

They import using UPS as a turn-key freight forwarder and importer.

Their shipping quantities are relatively small and everything comes in as air freight through UPS.

Participant did not know the duty rates or range for the items they are importing.

However, he did offer to provide us his contact with UPS so that we could further investigate the duties and procedures for their imported items. (Following up on this invitation resulted in a misunderstanding with the UPS rep in Sioux Falls, and was subsequently abandoned as not worthwhile).

Participant was not sure of the value of imports they had on an annual basis.

They are also importing gems (diamonds) and specialty metals for their manufacturing of jewelry.

They do not export any of their finished products from the factory. The retail stores sometimes export items for tourists.

Company # 9: \$197,730.67 in Import Value

Unable to contact.

With such a low level of Import Value, it would be nearly impossible to justify the estimated minimum cost of \$150,000 for an FTZ.

Data from Similar Sized Cities within Approximately 400 miles

As part of the due diligence process, we have communicated with several similar sized cities in a radius of approximately 400 miles. In depth conversations were held, both face to face and in tele-conferences. Some of these cities have an established FTZ, and some have investigated the option and decided against obtaining FTZ status. None are currently in the process of obtaining FTZ status.

The cities are as follows:

Sioux Falls, SD

1. South Dakota's only designated Point of Entry.
2. Has one CBP officer and an FTZ.
3. Officer clears both passengers and freight. FTZ has one user, and another user at a sub-zone in Lyons, SD.
4. CBP is requiring the airport to upgrade their facilities to meet Post-9/11 Dept. of Homeland Security regulations. Will cost the airport around \$2.5 million to provide a compliant facility, **in the airport terminal.**

Casper, WY

1. Wyoming's one and only designated Port Of Entry.
2. CBP agent only clears passengers, no freight.
3. There is an FTZ, but it is currently not being used.
4. CBP is requiring the airport to upgrade their facilities to meet Post-9/11 Dept. of Homeland Security regulations. Will cost the airport around \$500,000 to remodel an existing facility, i.e.: the old airport restaurant.

Bozeman, MT

1. Customs Clearance Fee airport. No FTZ. CBP officer clears passengers only, no freight.
2. Customs Clearance Fees after about one year of operation cover about 70% of expenses. The remaining 30% is paid by the city and a nearby resort that benefits from tourists being able to clear Customs at Bozeman.

Billings, MT

1. Has no CBP officer.
2. **Has** investigated the feasibility of an FTZ, and has decided against it.

Williston, ND

1. An International Airport and Port Of Entry airport with one CBP officer.
2. No FTZ. CBP officer clears passengers only, no freight.
3. Airport is in the process of relocating about 7 miles away from current facility. Incremental cost of adding a Customs Clearance facility **in the terminal building** is estimated at \$2.5 million.

Dickinson, ND

1. Has no CBP officer.
2. Has **not** investigated the feasibility of obtaining FTZ status.

Bismarck, ND

1. Has no CBP officer.
2. **Has** investigated the feasibility of an FTZ, and has decided against it.

Analysis

The companies that import to the Black Hills area regularly can be characterized as follows:

1. Very low level of imports relative to their overall business.
2. Very low level of duties paid. The highest duty rate encountered for goods being imported was 3.2%.
3. Very little dutied material held in inventory. The vast majority is distributed immediately to customers, or other stores or branches within the company.
4. The incremental cost of participating in an FTZ would be far greater than the projected savings for ALL the surveyed participants. NOT ONE of the surveyed companies was a good candidate for participation in an FTZ.

There are costs for bonding a carrier to move the goods from the port of entry to the FTZ.

There are strict CBP controls and documentation required in moving goods in and out of the FTZ.

You need to have a warehousing agent to manage the goods for customers, if you have a centralized FTZ, or the company has to manage the record keeping and controls for a CBP agent inspection if you establish a sub-zone within a company's facilities.

Establishing a **sub-zone of an existing FTZ** in the Black Hills Region is impractical due to the extensive time and travel costs required of the CBP agent.

Discussion of Overall Results

The Mining, Forestry and Agriculture industries import very little of their raw materials and machinery. And Manufacturing, one of the biggest users of FTZ's in other regions of the U.S. is a very small percentage of the Black Hills Region's business community. The vast majority of machinery and raw materials used in Manufacturing in the Black Hills Region is sourced domestically, leaving very little opportunity for cost savings via an FTZ.

Duties are very low on the items being imported.

No companies are importing, processing, and subsequently re-exporting any goods; activities which would support the costs of an FTZ or sub-zone

Assess the Results

There are currently no companies, or industries, within the Black Hills Region that are importing, and paying high duties on, a sufficient quantity of goods to economically justify the added costs of an FTZ.

Barring any significant changes to this equation, the committee sees no economic justification for spending the money to obtain FTZ status anywhere in the Black Hills region at this time.

Conclusions and Recommendations

While an FTZ could be useful for attracting more manufacturing businesses to the Black Hills Region, it is not justified at this time.

There are, however, some advantages of seeking a Customs and Border Protection agent in the region. Many local companies with aircraft at Rapid City Regional Airport would benefit from having local customs clearance services. Combining this demand with our regional tourism industry would seem to be a logical avenue to pursue to help justify the costs associated with securing a Customs and Border Protection agent.

This agent would be tasked with clearing both local residents returning from outside the US and providing Customs Clearance for foreign nationals arriving in the Black Hills for business, and tourism to take advantage of the unique recreational activities in the area including: Mount Rushmore, Black Hills National Forest, Custer State Park, numerous tourist related attractions, and the Sturgis Motorcycle Rally.

We recommend ceasing any efforts regarding obtaining FTZ status, and instead concentrate on determining if economic justification can be made for obtaining a CBP officer for passenger clearances, at Rapid City Regional Airport.

To that end, we are engaged in performing the due diligence to determine the feasibility of getting **a CBP agent assigned to the Rapid City Regional Airport**, for passenger clearance of incoming international flights, and for local residents returning from outside the U.S. Due to CBP regulations, the largest number of passengers one CBP agent can clear alone is 20. While this limits the number of aircraft that can be cleared, it presents the opportunity to save money in infrastructure costs by having the CBP Customs Clearance located in the facilities of one of our privately owned **Fixed Base Operators** (FBO).

We **further recommend** working with other municipalities and stakeholders within the Black Hills Tourism Industry to determine their needs and obtain their buy-in to support a CBP officer at Rapid City Regional Airport. They would be asked to provide funds to cover a portion of startup costs and ongoing operating costs for a certain period, probably not more than four to five years.

We are currently working with our **largest FBO, airport management, and the Chicago Customs Office** to determine what options are available to the City of Rapid City for passenger clearance services.

A final report, with final recommendations is anticipated within the first half of 2014.

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Citations and Bibliography

1. http://en.wikipedia.org/wiki/Foreign_trade_zone