

FIRST SALE PERSPECTIVE

Five Things to Know About First Sale to Lower Your Duty & Tax Costs

The First Sale Rule enables U.S. companies to significantly reduce landed costs to capture duty and tax savings. Why does it remain an untapped resource? Those who are familiar with First Sale view it as a complex process of documentation and filings. To some, First Sale is almost taboo. That shouldn't be the case. Here's a look at five key things you should understand about the First Sale rule to get started reducing your duty costs.

What is it?

The First Sale rule applies to importers of goods involving multiple handoffs — where the product is bought and sold multiple times overseas. According to this rule, importers only apply duty to the price paid at the very first sale of goods — rather than paying duty on the final price paid by the importer, which has been marked up. It is particularly valuable in industries where product is subject to higher duty rates, such as apparel.

Examples of First Sale Benefits:

- Reduce customs duties: An \$8 item moves from manufacturer to a middleman and is marked up to \$10 before reaching the importer. Assuming a 15% duty fee, the importer pays \$1.50 on the \$10 item. Based on First Sale, the 15% duty fee is applied to the \$8 value of the item, reducing the duty to \$1.20.

- Generate significant savings: A well-known luxury brand imports \$100 million FOB annually. Total duty based on a 15% rate is \$15 million. A 10% reduction in duty through First Sale generates \$1,500,000 in savings.

What steps and documentation are necessary?

According to Sandler, Travis & Rosenberg, who helped establish the law in 1988, once it is determined that the basic requirements are met, a clear documentation trail must be set up. The importer asserting first sale must be able to show a purchase order (PO) from the importer to the vendor, a PO from the vendor to the factory, an invoice from the vendor to the importer, and invoice from the factory to the vendor (provided with the shipment at the time of importation), payment from the importer to the vendor, and payment from the vendor to

According to the United States International Trade Commission, when goods are sold more than once before they are actually imported (in sales involving middlemen), the First Sale rule allows an earlier sale to be used in declaring customs value as long as that sale can be documented as a sale for exportation to the United States and the importer meets all other Customs requirements.

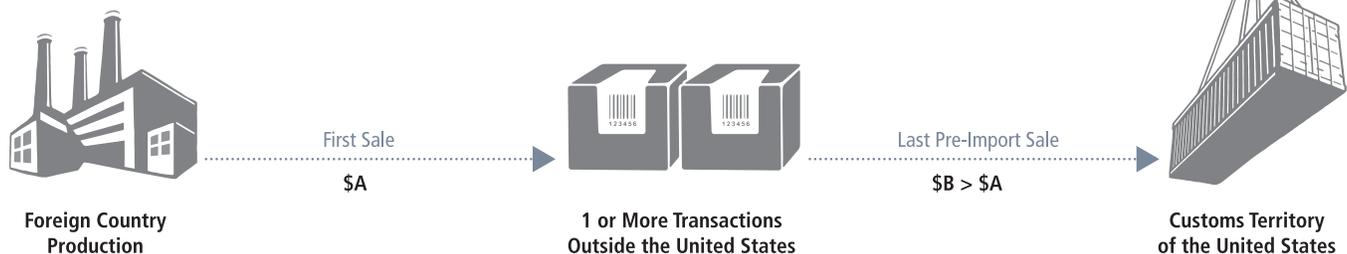
the factory. Depending on the complexity of the transaction, the paper trail can be even more involved.

Why don't more companies take advantage of First Sale?

There are multiple reasons why companies have delayed taking advantage of the First Sale rule:

1. Cost of setting up the program: certify suppliers, establish the documentation and other requirements.

FIGURE 1: Example of a series of transactions for which the First Sale rule might be applicable



2. Managing the process: There are legal requirements, complexities and documentation headaches. Companies implement First Sale to capture savings. But implementing is a manual process. ERP only manages the transaction between the importer and the middleman. It does not manage the First Sale transaction between the middleman and the factory. These are two separate transactions with two separate parties.

Executing First Sale involves manual processes between disparate systems.

- First Sale requires clearance using the first sale documents.
- Second sale is another set of documents that needs to be reviewed and reconciled by the importer or their designed party, such as a broker.
- The first sale data needs to be entered into the system for clearing instead of the 2nd sale data.

The challenges are significant:

- Manual processes
- Risk of errors and non-compliance
- Time consuming
- Not scalable

The common response to First Sale is to throw bodies and paper at it. But this is not scalable. While First Sale is a huge opportunity to generate savings, the current approach to deployment is misguided.

For example, one apparel brand identified significant savings through a First Sale program with a piloted group of suppliers, and was looking to triple the number of suppliers in the program to increase their duty savings. However, they were planning to manage their First Sale program in a manual environment. The documentation process was so cumbersome that the brand never deployed First Sale, leaving significant savings on the table.

Another challenge adding to the complexity is ensuring only the right people see the documentation and data. Dealing with sensitive data surrounding export and duty costs requires a tight handle on processes.

The processes behind First Sale need to be electronic, automated, and secure to deliver the most value. With the right infrastructure in place from both a legal and technical perspective, First Sale is a very achievable program that can generate significant savings. When documentation and process flows are automated and all parties are connected in an electronic environment, the challenges are greatly reduced.

Automating Processes behind the Scenes

Replacing paper and manual processes with an automated environment is the key starting point. An automated platform can house purchase orders, invoices and other

trade documents to streamline the workflow. More importantly, a platform approach can connect multiple parties. This eliminates the headache of extracting documents from two separate systems and removes manual steps for aligning information for processing First Sale transactions.

The good news is, many companies already have access to these tools. Businesses using cloud platforms for procure-to-pay, for example, have the core foundation already in place — a central data hub that delivers multi-enterprise collaboration.

Recommendations for Taking Advantage of First Sale:

- Talk to a specialist or consultant, such as Sandler Travis, KPMG, Deloitte or E&Y to determine the necessary legal structure for a First Sale program.
- Remove paper and manual tasks from the First Sale process by automating workflows for document review, matching and approval.
- Talk to your procurement, finance or supply chain team to find out if a source-to-settle or procure-to-pay platform is already in use at your business. It may serve as an easy extension for taking advantage of First Sale.