Developing an Agile Tariff Strategy While Preparing for an Economic Downturn

Trade & Customs Services

In the last several years, importers have had to rapidly adjust to the fluid global trade environment. After many years of static duty rates, the trade tensions with China taught us how quickly the status quo could be disrupted. Now, as importers are facing a global economic slowdown companies are focusing on minimizing costs and maximizing liquidity. This may be especially true for importers who, in the face of the Section 301 punitive tariffs, made significant capital investments to relocate out of China, speculating that the costs would be recouped because the economy was so hot. Now, with supply chains disrupted globally and consumer demand softening, the return on investment (ROI) of these projects may be much more extended than originally anticipated. Even importers who were not significantly impacted by the China-U.S. tensions or who aggressively managed the imposition of the tariffs will still likely feel the pinch of decreased demand.

As we enter a period of heightened need for liquidity, companies are looking at all possible ways to identify cash and streamline operations—including examining duty spend, which is included in the cost of goods. There are a number of strategies companies should consider to help exclude, mitigate, recover, and defer tariffs during a period of uncertainty. While selecting the right savings programs is driven by a number of factors, including the return on investment, the time to implementation, and a company's long-term priorities, each can be a powerful lever in reducing above-the-line costs. Further, when the right programs are combined, the savings can be magnified.

Tariff elimination

Eliminating tariffs altogether eliminates a significant cost for companies. There are several different strategies companies should consider in today's tariff environment that may completely remove duty spend on certain imported products to gain a competitive advantage. However, understanding the requirements of each opportunity is critical to maximizing and complying with the opportunity.

China product exclusions (Section 301)

Importers could request product exclusions from the United States Trade Representative (USTR) for their products subject to the Section 301 China tariffs by demonstrating that, among other considerations, tariffs on the products would cause harm to the U.S. Although the exclusion application process is closed, the USTR is still issuing decisions. Once granted, any company can take advantage of the exclusion providing its imports meet the exact specifications listed in the exclusion. Product exclusions are retroactive to when the punitive tariff was imposed and valid for one year. Importers should take a hard look at existing exclusions to assess whether their products satisfy both the HTS and product description. If so, importers will receive immediate relief from the Section 301 tariffs as well as a potential recovery.

The tariff classification for rear-view mirrors is under HTSUS subheading 7009.10.0000. However, in February 2020, an exclusion was granted for the following product:

"Rear-view mirrors of convex glass for motor vehicles, each measuring not less than 1.75 mm and not more than 2.4 mm in thickness, not less than 125 mm and not more than 210 mm in length, not less than 97 mm and not more than 180 mm in width, weighing not less than 74 grams and not more than 188 grams"

The product description is actually narrower than the description in the HTS. For a company to benefit from this exclusion, it must import rear-view mirrors that meet also the exact parameters of the description, not only the classification.

e-Commerce shipments

Goods imported by one person on one day valued at $800 or less may qualify for duty-free treatment under Section 321. The Trade Facilitation and Trade Enforcement Act (TFTEA) increased the de minimis

amount from $200 to $800, creating an opportunity for importers to lower their overall duty spend. This is especially true for retailers with a strong online presence who are moving away from brick-and-mortar stores and ship directly from outside the United States to customers. Although there may be initial challenges in monitoring shipments to ensure the maximum threshold is not exceeded, in many cases, it may be worth the systems investment to obtain this visibility.

Medical product exclusions (Section 301)

Companies that produce goods used to combat COVID-19 may be eligible to submit comments to the USTR to obtain an exclusion from the Section 301 China tariffs of 7.5 percent–25 percent. This process is different from the exclusion requests that were previously available as it appears that the USTR will be making decisions on an expedited basis. Further, the requirements for a potential exclusion are focused on how the product will be used to fight COVID-19 instead of the nexus with China. Additionally, exclusions appear available for both manufacturers of finished goods or components that will be incorporated into a medically necessary good. Comments may be submitted until at least June—and it is likely that this date will be extended. Importers are well advised to review their products to assess if they may be used in medical goods.

Aluminum and steel exclusions (Section 232)

Importers of steel and aluminum may be eligible for exclusions to the Section 232 tariffs of 25 percent and 10 percent, respectively. These exclusions are valid for a year and retroactive from the date the exclusion was submitted. To obtain an exclusion, the requester must demonstrate that the product is not available in a sufficient quantity or quality in the United States. Although making a submission can be time intensive, it is the only way to eliminate the Section 232 tariffs because, unlike the Section 301 tariffs, exclusions are company specific. For impacted companies, consideration should be given to submitting a request.

Tariff recovery

The next best option if you can't eliminate that tariff is to potentially recoup some or all of the duty payments. Although these strategies don't eliminate duty payments, these programs are accessible to a wider number of companies in various industries and countries.

Duty drawback

Duty drawback allows an importer to reclaim 99 percent of duties and fees on imported goods that are subsequently exported. Although duty drawback is a long-standing program, it was streamlined under TFTEA, making it more user friendly. These changes include fully automated filing in ACE as well as permitting claims for up to five years from the time of import and three years from the time of export. Further, data analytics and blockchain have enhanced importers' ability to match imports and exports and to accelerate claims. Companies should not be deterred if they are not the exporter; it is still possible to receive a duty refund if the export data is available. Duty drawback remains one of the most effective programs to reclaim duties.

Retroactive exclusion recoveries

Importers can recover duties paid on punitive tariffs once an exclusion is in place through various procedural mechanisms. For example, the CBP Reconciliation Program allows importers to make entry corrections up to 21 months from the date of the entry summary. Many importers will wait until the end of their fiscal year to file Reconciliation so that all entries can be closed at once. However, importers with pending exclusions can easily flag those entries to prevent liquidation and to facilitate easy correction if the exclusion is granted. It should also be noted that CBP allows importers to request an extension of liquidation deadlines for pending exclusions and file Post Summary Corrections—for those importers not in the Reconciliation program. If the entries are liquidated, a timely protest can recover the punitive tariff. Taking these very simple steps can protect a company's ability to reclaim punitive tariffs.

Duty minimization

Minimizing duty payments by lowering entered value allows cash to remain with the company instead of outlaying it and then seeking a refund. This means that the savings can be allocated immediately without follow-up with CBP.

First Sale for Export

First Sale for Export allows importers with multitiered transactions to claim for customs purposes the value of the sale between the foreign factory and the foreign middleman instead of the middleman and the importer. This program has long been very popular with apparel retailers who have historically had high duty rates. As the China-U.S. tensions intensified, nonapparel retailers implemented this program because of the continual, year over year savings. During an economic downturn, First Sale is a strong program to help manage costs and to free cash. Additionally, a phased implementation approach can be taken, allowing the company to evaluate its impact before comprehensively rolling it out.

Valuation unbundling

Certain costs can be lawfully removed from the dutiable value of goods, thereby lowering the total entered value. Many of these costs are included in the total invoice price and the importer does not initially have visibility into them. In some cases, the importer may not even be aware that they are included. However, these fees can add up, substantially

increasing the dutiable value of imports on an annual basis. Stripping out costs related to handling charges paid to the supplier, fuel charges and foreign inland freight can lead to dramatically reduced values. Additionally, international freight and insurance may also be deducted from the dutiable value when certain incoterms govern the transaction and the importer knows the actual (not estimated) values. Given the economic downturn and ongoing supply chain disruption, removing nondutiable costs may provide considerable savings.

Post-import repair costs (Defective value allowances)

When an importer must make repairs to products that were damaged at the time of import, the declared value of the good may be reduced. As a result, the importer may request a duty reduction equal to duty paid on the diminution in value, or repair costs. This is an important opportunity for high-value importers who do not inspect their products until after import. Historically, the automotive industry has relied heavily on this program, but other importers should consider revising the value of imports when damage is discovered.

Transfer pricing adjustments

Most importers are aware of the impact that transfer pricing adjustments can have on customs declarations. In cases where an upward price adjustment occurs, additional duty may potentially be owed if the corresponding value of the goods increases. However, when a downward price adjustment is made and the value of the goods is lowered, duty may have been overpaid. In certain jurisdictions, a refund may be possible. Importers should evaluate their transfer pricing policy to understand where downward adjustments will be made and then prioritize those countries where a refund is possible. Importers may also consider optimizing their transfer pricing strategy to prevent an overpayment of customs duties. In doing so, the company would set the right price for both tax and customs purposes and would not have to chase refunds.

Duty deferral

Softening demand has resulted in excess inventory that must be stored and managed, causing many importers to scramble for warehouse space. Additionally, duty is being paid on this inventory although consumers may not be purchasing at the same speed as they were previously. However, there are certain customs solutions that allow an importer to both increase warehouse space and manage cash flow.

Bonded warehouses

A bonded warehouse is a designated area where imported goods may be stored, manufactured, or manipulated without paying duties for up to five years. One of the advantages of a bonded warehouse, in addition to deferring duties, is that additional warehouse space can be obtained quickly.

Foreign-trade zone

Similar to a bonded warehouse, a foreign-trade zone (FTZ) not only allows importers to defer duty payments but also offers additional benefits. An FTZ is a designated area that is considered outside of U.S. customs territory. Importers may admit goods into an FTZ without paying duty. The goods may stay indefinitely in the FTZ until they are needed. At that time, they would be entered and duty paid. When manufacturing occurs within the FTZ, the importer receives the benefit of an inverted tariff; if the duty rate on the finished product is less than the components, then the lower duty amount may be paid. Additionally, many importers realize customs broker savings because only one entry a week is filed instead of multiple entries. During an economic downturn, one of the benefits of a FTZ is that space can be designated as part of the zone but not activated until it is needed. This provides a level of flexibility to companies that may need to quickly expand their warehousing capabilities.

Conclusion

In sum, there are a number of levers that can be pulled to properly manage tariffs. The first step to developing a tariff strategy is to assess those strategies that are both available to the company and operationally feasible. Once a return on investment is conducted, a determination can be made regarding implementation goals over the long and short terms. The right program or combination of programs may potentially provide lasting savings even when the economic downturn ends.

Contact us

To further discuss tariff mitigation strategies, please contact your local tax adviser or the contacts listed below.

Andy Siciliano
Partner and Trade & Customs Services National Leader
E: asiciliano@kpmg.com
T: 631-425-6057

Doug Zuvich
Partner and Global Practice Leader
E: dzuvich@kpmg.com
T: 312-665-8363

John McLoughlin
Principal and East Coast Leader
E: jlmcloughlin@kpmg.com
T: 267-256-2614

Christopher Young
Principal
E: christopheryoung@kpmg.com
T: 312-665-3229

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