taxnotes® international

Volume 101, Number 12 ■ March 22, 2021

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Reprinted from *Tax Notes International*, March 22, 2021, p. 1547 tax notes international®

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In this article, the authors examine tariff mitigation strategies companies can take to create substantial short- and long-term savings.

I. Introduction

Just as taxable income is used to determine income tax, the customs value is similarly used to calculate duty liability. To calculate an accurate customs value, companies must factor in some dutiable additions and should consider non-dutiable deductions. Because tariff rates are assessed against an imported good's dutiable value, increases or decreases to the value can materially affect a company's duty liability. In today's environment, tariff mitigation strategies are top of mind for many companies because reducing the tariff liability can provide substantial short- and long-term savings. This article will discuss several often-overlooked non-dutiable charges that may, with proper planning, reduce a good's declared customs value.

II. Determining U.S. Customs Value

The United States follows the valuation hierarchy established by the WTO and lays out six valuation methods. The preferred valuation for most importers is transaction value. For U.S. importers, this is defined as "the price actually paid or payable for the merchandise when sold for exportation to the United States,"[1] plus some enumerated statutory additions. The price actually paid or payable is the "total payment . . . made, or to be made, for imported merchandise by the buyer to, or for the benefit of, the seller."[2] Transaction value requires an arm's-length sale between the seller and the buyer, which is assumed when the parties are unrelated. Transaction value may still be appropriate when the seller and buyer are related, but additional steps must be taken to validate the purchase price. The buyer must be able to demonstrate that the relationship between the parties did not influence the transaction, which may be accomplished through a circumstance of sale analysis. When the sale does not occur at arm's length, or transaction value is inappropriate for other reasons, an alternate valuation method must be used. The valuation methods are applied in a hierarchical order until an appropriate method is found.

Some importers who qualify for transaction value simply declare the price listed on the commercial invoice, assuming that is the custom value for the goods. However, several enumerated additions to the price must be added if they are not reflected in the invoice price to satisfy transaction value requirements. The added costs that form part of the customs value include:

- packing costs;
- selling commissions the buyer pays;
- assists;
- royalty or license fees that the buyer pays either directly or indirectly as a condition of sale; and
- proceeds of a subsequent resale that accrue directly or indirectly to the seller of the imported merchandise.[3]

An assist, one of the enumerated additions, is an item (such as a material, tool, or design)

[1] 19 U.S.C. section 1401a(b)(1).

[2] 19 U.S.C. section 1401a(b)(4)(A).

[3] 19 U.S.C. section 1401a(b)(1).

provided for free or at a reduced cost by the buyer to the seller that will be used in the production or the sale for export to the United States of the imported goods. In some industries, providing assists is common, requiring the importer to closely track the assist's value to ensure that the correct price is declared to U.S. Customs and Border Protection (CBP). Assists include the following:

- materials or other components;
- tools, dies, and molds;
- merchandise that is consumed during the production of the imported goods; and
- engineering, development, artwork, and design work that is undertaken outside the United States.[4]

Importers should also keep in mind that under the *Generra* presumption, CBP presumes that any payments made by the buyer to the seller, or a party related to the seller, are dutiable. This presumption was established when the Federal Circuit found that the importer is responsible for demonstrating that payments to a seller are unrelated to the imported goods.[5] While this presumption can be rebutted, the burden is on the importer to demonstrate why the additional payment is not associated with the imports. As a result, importers should be aware of any payments made by the buyer that occur outside the commercial invoice. While there will be circumstances in which additional payments are not dutiable, these situations should be carefully analyzed, and the rationale supporting the determination that the payments are not dutiable should be fully documented.

III. Eliminating Non-Dutiable Charges

While additions to customs value are more commonly known, permissible value exclusions or deductions are often missed. In fact, in some instances the statute and regulation directly identify deductions or exemptions. The term "price actually paid or payable" contains a carveout for specific charges. It states that the "price actually paid or payable" is "exclusive of any costs, charges, or expenses incurred for transportation, insurance, and related services incident to the international shipment of the merchandise from the country of exportation to the place of importation in the United States."[6] This means that in some circumstances, the cost of international freight and related costs may be deducted from the transaction value.

It is not simply the cost of freight and incidental services that may be deducted — a number of other deductions and exclusions may be taken associated with foreign taxes and fees or defective products discovered after import. Understanding if and how they apply to the business can round out any duty-mitigation program.

IV. Eight Overlooked Non-Dutiable Charges

For importers using transaction value, the following savings opportunities should be considered. While some of these programs provide ongoing savings and some are only used in specific circumstances, they all may play a role in reducing the tariff spend.

1. Freight and Insurance

Foreign inland freight, international freight, and insurance costs may be deducted from the transaction value if particular requirements are met. More specifically, with accurate International Commercial Terms (Incoterms) and supporting costs and documentation, this long-term cost-savings strategy can be an easy to implement. In fact, the regulations themselves outline what is required.

19 C.F.R. section 152.103(a)(5) provides guidance around foreign inland freight and other charges "incident to the international shipment of . . . merchandise." It states that when ex-factory terms of sale govern (in which the buyer is responsible for moving the goods once the seller makes them available, usually at the factory), the cost of foreign inland freight or other incidental charges do not have to be added to the invoice price. Further, when alternative Incoterms govern the transaction, these costs can be deducted from the declared value if specific requirements are met. In a transaction not governed by ex-factory

[4] 19 U.S.C. section 1401a(h)(1)(A).

[5] *Generra Sportswear Co. v. United States*, 905 F.2d 377 (Fed. Cir. 1990).

[6] 19 U.S.C. section 1401a(b)(4)(A).

Incoterms, the importer must ship the goods on a through bill of lading, and the costs must be separately identified and occur after the goods are sold for export to the United States.[7]

Importantly, importers must verify that they are deducting the actual, not estimated, costs and that the supporting documentation is adequate. CBP has found that a through waybill is essential as evidence to support this exclusion. It has denied claims in which there was not a "through shipment from the factory to the United States documented by a through bill of lading" even when the importer could demonstrate that the goods moved from the foreign port to the United States.[8] International freight may also be deducted from the entered value when the actual costs of the freight are available and separately itemized. This proves challenging for some importers because sometimes an estimated value is used at the time of shipment and then reconciled later. In those circumstances, it is not acceptable to claim a deduction.

Further, insurance costs may be deducted from the entered value when they are separately itemized, and the actual costs (not estimated) are claimed. It is important to verify with sellers that they are providing actual costs because CBP will reject deductions based on estimates, even when the importer paid more than it claimed on the entry.[9]

When assessing whether to make a deduction, the fees should be shown in the commercial documentation, although not necessarily on the invoice. Acceptable documentation may include a freight or insurance bill or a written contract that separately lists the fees.[10] While there may be some initial, upfront work to validate that these charges are appropriately deducted, eliminating these costs from the declared value will, in most cases, be a source of substantial savings.

2. Supply Chain ('Origin') Costs

International transportation costs typically include some other fees — often referred to as "origin costs." In many cases, CBP considers these origin costs to be "incident to the international shipment of merchandise" and, therefore, possibly excluded from the customs value. While each fee must be assessed individually, several groups of fees that CBP has previously determined are not part of the price actually paid or payable may be excluded:

- *Security Charges*. The security charges that generally may be deducted from the transaction value include a port security charge and supply chain security fee.
- *Documentation Fees*. There are several common fees that importers incur associated with the cost of producing and issuing the documentation required for international transport. The deductible fees may include:
  - Carrier agent booking fee and carrier bill of lading.
  - Freight cargo receipt/house bill of lading issuance.
  - Costs associated with the Automated Manifest System (AMS), which is the electronic information transmission system CBP operates.
  - Importer security filing (ISF) management fee, commonly referred to as the "10+2." The ISF is a CBP-mandated requirement in which specific trade data must be provided to CBP in advance of the vessel's U.S. arrival.
- *Logistics Fees*. Additional fees are usually incurred from the third-party service provider that is preparing the goods for international shipment. Many of these fees are not included in the transaction value and, where properly supported, may be excluded from the value declared to CBP at the time of entry. Some of these fees include:
  - container freight station receiving;
  - customs clearance;
  - container yard monitoring;
  - equipment management fee;
  - less than container load (LCL) handling;
  - terminal handling charge; and
  - wharfage and container seal fees.[11]

[7] 19 C.F.R. section 152.103(5)(ii).

[8] HQ H312640 (Oct. 27, 2020).

[9] HQ H548068 (Apr. 5, 2002).

[10] HQ H229700 (Jan. 30, 2013).

[11] HQ H229700 (Jan. 30, 2013).

Per shipment, these miscellaneous fees may appear insignificant. But they can result in a significant annual expense for the company by driving up duty payments. Implementing processes to compliantly remove these expenses from the declared value of the imports can make an ongoing material difference in duty payments. As a general rule, the importer must deduct the actual costs, validate that commercial documentation meets all requirements, and understand when services are being provided. However, once these steps have been taken, it is likely that little additional work will be required to realize ongoing savings.

3. Warehousing Costs

CBP has found that when warehousing costs are paid by the buyer to third parties, they are not included in the price actually paid or payable for the imported merchandise. However, the CBP has distinguished this scenario from cases in which the seller, or a party related to the seller, provided this same service and the warehousing costs were included in the price actually paid or payable. The payments in those cases were found to be dutiable under the *Generra* presumption and could not be deducted.[12] Importers that are interested in using this opportunity should conduct a careful review of payments and terms of sale to validate that the transaction meets all of CBP's criteria before taking this deduction.

4. Inspection or Testing Fees

Before shipment, an importer will often arrange for products to be inspected or tested to validate that they satisfy a buyer's quality standards. Under some conditions, these inspection or testing fees may be excluded from the dutiable value when they are paid to third parties unrelated to the seller of the goods.[13] For example, some products require additional safety testing before they can be imported, and the testing fees, if structured properly, should not be part of the price actually paid or payable.

By contrast, CBP has clearly stated that when the seller or a party related to the seller is conducting the inspection or testing, the payments form part of the price actually paid or payable. It's also important to understand that testing that is "essential to the production of that merchandise" is dutiable. In those cases, CBP would consider payments to unrelated third parties for these services as assists that are part of the transaction value.[14]

Importers who rely on the seller to perform inspection or testing services should conduct an analysis to assess the return on investment for engaging a third party to perform these services.

5. Latent Defect Allowances

In some circumstances, importers may be able to reduce dutiable value after importation based on repair costs attributable to manufacturing or design defects. For importers with high-value products, such as those in the automotive industry, repair costs can be substantial, and this allowance in value provides an opportunity to manage those costs by reclaiming duty. While customs regulations allow for deductions based on latent defects, several requirements must be satisfied:

- the importer contracted for defect-free merchandise;
- the merchandise was defective at the time of importation and can be linked to specific entries; and
- the value of the defect can be established for each item.[15]

In many cases, CBP will request specific documentation supporting each element of the claim to validate that the post-importation value allowances comply with applicable regulations. However, with proper planning, a program can be implemented to help ensure the importer does not overpay duty on goods that were defective at the time of import. This program is often used by automobile importers because of the ability to meet the requirements and the large volume of post-importation repair costs incurred.

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[12] HQ 547534 (Jan. 19, 2001).

[13] HQ H308695 (Feb. 25, 2020).

[14] HQ H301764 (June 10, 2019).

[15] *See Volkswagen of America Inc. v. United States*, 532 F.3d 1365, 1374 (Fed. Cir. 2008); *Fabil Manufacturing Co. v. United States*, 237 F.3d 1335 (Fed. Cir. 2001); and *Samsung Electronics America Inc. v. United States*, 106 F.3d 376 (Fed. Cir. 1997); *see also* HQ 548507 (Jan. 25, 2005); HQ 548390 (Jan. 12, 2004); and HQ 546761 (Sept. 23, 1999).

6. Instruments of International Traffic — Reclassification of Packaging

Pallets, cartons, hangers, and other packaging material may sometimes be considered instruments of international traffic (IIT), exempting them from duty. The customs statutes provide that "instruments of international traffic . . . shall be excepted from the application of customs laws,"[16] and the CBP commissioner may designate additional articles as instruments of international traffic.[17] In so designating, these articles may be released without the payment of duty. To qualify as an IIT, CBP has determined that the article must meet several criteria, including that it is "substantial, suitable for and capable of repeated use, and used in significant numbers in international traffic."[18] Further, the article must be used in commercial shipping or transportation more than twice to qualify as an IIT.[19]

For importers, whose supply chains include the reuse of specified containers or other materials used to transport international goods, it may be valuable to assess whether these goods qualify as IIT and are therefore duty free. While additional steps may be necessary to confirm that the containers qualify, this opportunity presents the possibility of substantial, ongoing savings.

7. Post-Importation Price Adjustments

When companies make post-importation price adjustments they may be entitled to a duty refund on the amount adjusted. This usually occurs when transfer pricing adjustments are made between related parties, causing a change to the products' customs value.

When a downward price adjustment is made, resulting in a price reduction from the foreign seller to the related importer, the importer may be eligible for a duty refund. Obtaining this refund is predicated on meeting CBP's five-factor "formulaic pricing" test and establishing that the post-adjusted price is at arm's length from a customs perspective. Validating that the company meets these requirements before claiming a refund will be central to maintaining compliance. Also, importers who anticipate price adjustments should consider joining CBP's reconciliation program to facilitate reporting price changes, as it generally provides importers up to 21 months after initial entry to true-up the final customs price. For companies that routinely make retroactive transfer pricing adjustments, having the documentation in place to support a refund can have a powerful effect on duty spend.

8. Taxes and Other Fees

Companies may be entitled to deduct VAT or goods and services taxes from the declared value of the imports when these payments are refunded. Not only should importers maximize their refunds when possible, but in doing so they create another opportunity for savings.

The U.S. Court of International Trade has found that when VAT is remitted by the U.S. importer to the foreign seller, separately identified and refunded to the importer, then the refunded amount is not included in transaction value.[20] Importers should team with their tax departments and foreign suppliers to determine if VAT refunds have been obtained and create documentation that reflects separate itemization of the refunded VAT.

Similarly, when the seller is responsible for paying duties, such as in a transaction with delivered duty paid Incoterms, anti-dumping and countervailing duties (ADD/CVD) may be deducted from the transaction value when they are separately itemized. This is permissible because one of the exclusions to transaction value is "the customs duties and other Federal taxes currently payable on the imported merchandise by reason of its importation."[21] CBP has found that ADD/CVD are considered "customs duties and other Federal taxes" within the meaning of the statute.[22] As a result, when separately itemized they may be deducted. By deducting the ADD/CVD from the transaction value, the overall duty payment will be lower. While this savings

[16] 19 U.S.C. section 1322(a).

[17] 19 C.F.R. section 10.41a.

[18] HQ H300587 (July 5, 2019).

[19] HQ H300587 (July 5, 2019).

[20] *Caterpillar Inc. v. United States*, 941 F. Supp. 1241 (1996).

[21] 19 U.S.C. section 1401a(b)(3)(B).

[22] HQ H304314 (Nov. 5, 2019).

strategy will only benefit a limited number of sellers, it is a good option to help manage costs.

V. Conclusion

Potential cost savings through the reduction of non-dutiable charges from the dutiable cost basis of imported goods are often overlooked or may not have been considered material in the past. However, in this high-tariff environment, these programs can help companies easily achieve cost savings. Also, many of these non-dutiable costs do not require much time to manage because, once established, there is typically little maintenance required. These opportunities can often be expanded globally, which will further enhance savings. Of course, as with any duty-savings program, strong controls must be implemented to preserve compliance. However, it is likely that steep tariffs will be in place for some time, so companies should evaluate which of these programs can help reduce costs and the potential return on investment, and then develop a plan to implement them. ■