

## US announces temporary pause on planned increase of List 3 tariffs on China origin goods; duties remain in force and key issues remain unresolved

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### Executive summary

On 1 December 2018, United States (US) President Trump announced that the US will temporarily leave the additional 10% ad valorem punitive tariffs in place on China-origin products beyond 1 January 2019. The announcement follows President Trump's meeting with China President Xi Jinping at the conclusion of the G20 summit in Buenos Aires, Argentina.

When first announced on 17 September 2018, President Trump stated that the 10% tariff, imposed on a wide range of products valued at US\$200b,<sup>1</sup> would increase to 25% at the beginning of the year. Duties of 25% previously imposed on \$50b of China-origin goods remain in force at this time. China has imposed retaliatory duties on \$110b of US-origin goods in response to the previous US actions.

During the meeting between the two leaders and senior officials on trade matters, China committed to purchasing agricultural, energy, industrial and other products from the US. The US and China further agreed to immediately begin negotiations to address US-stated concerns on China's policies with respect to forced technology transfers, intellectual property protection, non-tariff barriers, cyber intrusions and cyber theft, services and agriculture. The US has stated that it anticipates satisfactory completion of these negotiations within 90 days, noting however that should the parties not reach an agreement, the 10% tariffs will then be raised to 25% as originally planned.

## Detailed discussion

On 22 March 2018, President Trump executed a Presidential Memorandum directing the Administration to take a full range of action responding to China's acts, policies and practices involving unfair and harmful acquisition of US technology.<sup>2</sup> That action was based on a report released the same day by the US Trade Representative (USTR) providing findings of an investigation conducted under Section 301 of the *Trade Act of 1974*.<sup>3</sup> The investigation concluded that China's forced or coerced transfers of US technology burden or restrict US commerce, and an interagency team of subject matter experts and economists have estimated resultant harm to the US economy.

The President directed the USTR to propose 25% additional duties on imports of Chinese products "commensurate with the harm caused the US economy." The USTR subsequently proposed, and President Trump so ordered, punitive duties of 25% to be imposed and collected on 818 tariff lines covering \$34b worth of imports from China per year as of 6 July 2018 (US List 1).<sup>4</sup> The US then began collecting additional tariffs on another 279 tariff lines covering \$16b worth of imports from China per year on 23 August 2018 (US List 2).<sup>5</sup>

On 17 September 2018, the USTR announced a third list of China-origin products valued at \$200b which became subject to additional 10% ad valorem punitive tariffs beginning on 24 September 2018 (US List 3).<sup>6</sup> President Trump's statement<sup>7</sup> on imposing the duties stated that the ad valorem duty rate for the covered products on US List 3 will increase to 25% on 1 January 2019.<sup>8</sup> China has responded to US actions by collecting additional duties on up to \$110b of US-origin imports, including key agricultural products.

Separately, the USTR announced a product exclusion process for items covered by US Lists 1 and 2. The submission process for List 1 closed on 9 October 2018, with over 10,700 requests received. The USTR is continuing to process the requests, but to date, 9,200 requests remain pending and over 1,400 have been denied. The deadline for importers seeking an exclusion for items covered under List 2 is 18 December 2018 to submit a completed application. At this time, the USTR has not provided any further guidance or instruction on exclusion request procedures for items covered under List 3.

On 20 November 2018, the USTR released a report updating information on its Section 301 investigation of China's acts, policies and practices related to technology transfers,

intellectual property and innovation. The report states that "China has not fundamentally altered its unfair, unreasonable, and market-distorting practices that were the subject of the March 2018 report on our Section 301 investigation."<sup>9</sup>

On 28 November 2018, the USTR issued a statement on China's Auto Tariffs imposed on US-produced automobiles. The statement notes:

*China's aggressive, State-directed industrial policies are causing severe harm to U.S. workers and manufacturers. We are continuing to raise these issues with China. As of yet, China has not come to the table with proposals for meaningful reform. China's policies are especially egregious with respect to automobile tariffs. Currently, China imposes a tariff of 40 percent on U.S. automobiles. This is more than double the rate of 15 percent that China imposes on its other trading partners, and approximately one and a half times higher than the 27.5 percent tariff that the United States currently applies to Chinese-produced automobiles. At the President's direction, I will examine all available tools to equalize the tariffs applied to automobiles.*

### What to expect next?

Ahead of the G20 summit, China presented the US with a list of proposed items to address the trade concerns noted in the Section 301 study and as raised by the Trump Administration. With President Trump's recent statement providing temporary reprieve from the increase in List 3 duties to 25%, China is expected to take immediate action to purchase significant amounts of US agricultural products followed by plans to increase purchases of other critical goods.

The commitments are intended to help reduce the US-China trade deficit while both sides work through the other structural changes sought from China; namely, opening its markets and preventing forced technology transfers and intellectual property theft from US-based companies. Importantly, China appears to have agreed to not increase or add further retaliatory duties during the negotiation period, which provides US exporters a degree of certainty, for now.

Although the US previously signaled its intent to announce tariffs on additional items valued at \$267b following the 1 January 2019 increase date, which would account for roughly the remainder of China-origin imports beyond the \$250b of goods currently under punitive tariffs, it appears that the US will delay such an announcement at this time.

It is important to note that there is no relief for the 25% additional duties previously imposed on \$50b of China-origin goods and the corresponding Chinese retaliatory tariffs. These tariffs will remain in force until further actions are taken.

On 3 December 2018, President Trump announced his expectation that as part of the agreement reached, China will soon lower its 40% tariff on US-produced automobiles to 15%, similar to the tariff rate applied to other countries. While further details of timing and removal or reduction of retaliatory duties by China on other key commodities subject to the statement have not been announced, it is expected that similar actions will occur during the 90-day negotiation period.

### Actions for businesses

Any company involved in US-China trade is encouraged to identify the potential impact of additional duties and develop duty avoidance or mitigation strategies. Close monitoring of developments is warranted; however, while the present duties

remain in place and as the potential for further restrictions or increased or new duties remain a threat should negotiations not conclude favorably, company executives should continue to evaluate alternatives and plan accordingly. Immediate actions for such companies could include:

- ▶ Mapping their complete, end-to-end supply chain to fully understand the extent of products impacted, potential costs, alternative sourcing options, and to assess any opportunities to mitigate impact such as tariff engineering.
- ▶ Identifying strategies to defer, eliminate, or recover the excess duties such as bonded warehouses, Free Trade Zones, substitution drawback, Chapter 98 and equivalent programs under China customs regulations.
- ▶ Exploring strategies to minimize the customs value of imported products subject to the additional duties, re-evaluating current transfer pricing approaches, and for US imports, considering US customs strategies, such as First Sale for Export.

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## Endnotes

1. Currency references in this Alert are to US\$.
2. See EY Global Tax Alert, [Trump Administration announces imposition of \\$50B in tariffs on wide range of Chinese origin goods - specific product list to be announced](#), dated 22 March 2018.
3. Section 301 of the *Trade Act of 1974* (Section 301) allows them to impose duties or import restrictions upon a determination that an act, policy or practice of a foreign country violates, or is inconsistent with, a trade agreement such as the World Trade Organization (WTO), or is "unjustifiable and burdens or restricts United States Commerce." 19 USC § 2411 et seq.
4. ["USTR Issues Tariffs on Chinese Products in Response to Unfair Trade Practices,"](#) 15 June 2018.
5. ["USTR Finalizes Second Tranche of Tariffs on Chinese Products in Response to Unfair Trade Practices,"](#) 7 August 2018.
6. <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/september/ustr-finalizes-tariffs-200>.
7. <https://www.whitehouse.gov/briefings-statements/statement-from-the-president-4/>.
8. <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/september/ustr-finalizes-tariffs-200>.
9. <https://ustr.gov/sites/default/files/enforcement/301Investigations/301%20Report%20Update.pdf>.

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EYG no. 012057-18Gbl

1508-1600216 NY  
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