

US grants limited exemptions from Section 301 duties and announces annual special review of Section 301; continued uncertainty ahead

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Executive summary

On 21 December 2018, the Office of the United States (US) Trade Representative (USTR) announced its first round of decisions for exemption requests on certain imported Chinese-origin goods from Section 301 of the *Trade Act of 1974* (Section 301) punitive tariffs.¹ The product exclusions were subsequently published in a Federal Register Notice (FRN) on 28 December 2018 and cover approximately 1,000 separate requests by US importers covering a disparate range of products (details listed further below) that the USTR has determined meet specified criteria for exclusion. As of 30 December 2018, the USTR has approved 9%, denied 11.7% and continues to review 79% of the more than 10,800 submissions. Notably, the exclusions only span 21 unique tariff codes.²

Also on 28 December, the USTR announced its annual "special review" to identify countries that deny adequate and effective protection of intellectual property (IP) rights or deny fair and equitable market access to US persons who rely on IP protection under Section 301.³ The review assists the USTR with determining countries for which the USTR can implement an investigation pursuant to Section 301 to determine whether certain trade measures are appropriate to address a country's restrictions on trade and IP rights. The most recent investigation under Section 301 occurred in 2017 and 2018 and ultimately resulted in the USTR implementing the punitive tariffs now in place on approximately \$250 billion of imports from China.

Detailed discussion

Section 301 punitive duties background

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. That action was based on a report released the same day by the USTR providing findings of an investigation conducted under Section 301 of the *Trade Act of 1974*. 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 ordered, punitive duties of 25% to be imposed and collected on 818 tariff lines covering US\$34 billion⁴ worth of imports from China per year as of 6 July 2018 (US List 1).

Since that time, the US has imposed a 25% tariff on an additional \$16 billion of imports (US List 2) and a 10% tariff on \$200 billion of imports (US List 3). The US had said it would increase the 10% tariff to 25%, but recently announced it would delay that action until 2 March 2019 pending new negotiations with China.⁵

Following imposition of the punitive duties last year, the USTR subsequently 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 nearly 10,800 requests publicly posted. The deadline for importers seeking an exclusion for items covered under US List 2 recently passed on 18 December 2018. Over 1,640 requests have been publicly posted for consideration, totaling more than 12,440 separate requests for the \$50 billion of goods covered under the first two lists. At this time, the USTR has not provided any further guidance or instruction on exclusion request procedures for items covered under US List 3.

Exclusions granted

The USTR's recent 28 December 2018 FRN reaffirms that product exclusion decisions will be made based on the criteria stated in the notices establishing the exclusion process. Specifically, the criteria requires applicants to provide the following detailed information for consideration

of a determination to grant an exclusion: (1) availability of the product outside of China; (2) harm to US interests due to additional tariffs; (3) significance of the product to Chinese industrial policy; and (4) whether an exclusion would undermine the objective of the Section 301 investigation. The FRN also explains that exclusion decisions reflect advice from the Interagency Section 301 Committee as well as the USTR's consideration of public comments submitted during the exclusion request period.

The initial product exclusions granted by the USTR are set forth in the Annex of the agency's 28 December 2018 FRN and take two different forms. Seven product exclusions address 918 separate requests and consist of existing 10-digit subheadings that fall within one of the 8-digit subheadings covered by US List 1 (three 10-digit subheadings are found within the same 8-digit heading). The remaining 24 specific product exclusions address 66 separate requests and are limited to specially prepared product descriptions that fall within 10-digit subheadings. Importantly, the latter exclusions only apply to the product descriptions listed in the 28 December 2018 FRN Annex – not the entire 10-digit subheading.

Product exclusions apply to any product that meets the description contained in the FRN Annex which are entered for consumption or withdrawn from warehouse on or after 12:01 EST on 6 July 2018 and are not limited to the particular requestor. Exclusions apply retroactively to when the tariffs were implemented, 6 July 2018, and extend for one year after publication of the exclusion notice. US Customs and Border Protection is expected to publish specific guidelines for importers on procedures to seek refunds of punitive duties and for filing procedures on exemption-granted items.

Products excluded based on existing Harmonized Tariff Schedule of the US (HTSUS) 10-digit descriptions:

- (i) **8412.21.0075**: certain types of linear acting (cylinders)
- (ii) **8418.69.0120**: self-contained drinking water coolers
- (iii) **8480.71.8045**: certain kinds of injection type molds for rubber or plastics
- (iv) **8482.10.5044**: certain kinds of single row bearings with an outside diameter of 9 mm and over but not over 30 mm
- (v) **8482.10.5048**: certain kinds of single row bearings with an outside diameter of over 30 mm but not over 52 mm

(vi) **8482.10.5052:** certain kinds of single row bearings with an outside diameter of over 52 mm but not over 100 mm

(vii) **8525.60.1010:** Citizens Band (CB) transceivers

Products excluded based on specially prepared product descriptions:

(viii) **8407.21.0080:** Spark-ignition engines for marine propulsion, outboard, each rated at not less than 29.83 kW but not more than 44.74 kW (described in statistical reporting number)

(ix) **8412.21.0030:** Welded hydraulic linear acting (cylinders) engines and motors, each with piston bore of 12.7 mm or more but not over 34.6 mm, with stroke not over 11.43 m, overall length not over 15.24 m and rod diameter not over 1.219 m

(x) **8419.90.2000:** Stretchers of stainless steel, designed to move rollers to adjust tension of paper fabric to be dried, each with a pivoting arm with an actuator, linear rail movement with an actuator, and front and back units with mounting holes for tube roll bearing housings

(xi) **8420.10.9080:** Roller machines with dies for embossing paper, manually powered (described in statistical reporting number)

(xii) **8421.19.0000:** Salad spinners of plastics, with capacity of at least 2.4 liters but not more than 3.8 liters

(xiii) **8421.21.0000:** Nonelectric water filtration apparatus consisting of three cylinder-shaped filter cartridges, each measuring 6.35 cm by 26.67 cm, having water storage tank and plastic tubing measuring 0.63 cm or more but not over 0.95 cm, presented with installation kit

(xiv) **8425.39.0100:** Winches, each having a winch frame with a corrosion resistant coating and stainless steel mandrel with nylon bushings, operated manually by a worm gear mechanism

(xv) **8428.32.0000:** Elevators, comprising L-shaped steel buckets bolted to a steel chain, with guide rollers and a drive system

(xvi) **8428.33.0000:**

- ▶ Belt conveyors, each comprising a frame with leveling feet, electric motor and food grade plastic conveyor belt

- ▶ Belt conveyors, each comprising a welded frame with leveling feet and casters, electric motor and food grade plastic modular conveyor belt

(xvii) **8439.99.1000:**

- ▶ Guards of stainless steel, designed to shield operators of papermaking machines from moving or rotating equipment, each with dimensions ranging from 30 cm by 30 cm by 50 cm to 50 cm by 50 cm by 4 m, weighing 30 kg or more but not over 100 kg
- ▶ Scrapers (“doctors”) of stainless steel, designed to scrape impurities from the rotating roll surface of the forming and press sections of papermaking machines, each comprising a beam with a blade of non-symmetrical cross section, long aspect ratio, and mounting journals and turning devices on either end, with dimensions ranging from 50 cm by 50 cm by 8 m to 60 cm by 6 m by 11 m, weighing 1 metric ton or more but not over 3 metric tons
- ▶ Frameworks of the forming and press Section of papermaking machines, of stainless steel or clad mild steel with stainless or acid proof steel, each with dimensions ranging from 1 m by 1 m by 1 m to 2.3 m by 2.3 m by 12 m, weighing 500 kg or more but not over 40 metric tons
- ▶ Guides of stainless steel, designed for locating conveyer belts on papermaking machines, each with a moving arm with an actuator and front and back units with mounting holes for tube roll bearing houses, each with dimensions ranging from 40 cm by 50 cm by 30 cm to 1 m by 1 m by 50 cm, weighing 300 kg or more but not over 500 kg
- ▶ Rollers of steel and cast iron (nip rollers) with bearing journals on either end, designed for use in paper manufacturing to mechanically compress paper web to remove water or impart desired mechanical properties in paper web, each with a polymer cover, the foregoing with length of 7 m or more but not over 12 m, with diameter of 1 m or more but not over 1.5 m, weighing 15 metric tons or more but not over 30 metric tons
- ▶ Open containers (savealls) of stainless steel, designed to catch water run off generated in the papermaking process, constructed of large square shaped plates and flat constructions with mounting holes on ends, each with dimensions ranging from 50 cm by 50 cm by 50 cm to 1.5 m by 1 m by 10 m, weighing 50 kg or more but not over 2 metric tons

- ▶ Stretchers of stainless steel, designed to move rollers of papermaking machines to adjust tension of fabric, each with a pivoting arm with an actuator, linear rail movement with an actuator and front and back units with mounting holes for tube roll bearing housings
- ▶ Suction boxes of stainless steel, which remove water from paper web or papermaking fabrics during papermaking, each with dimensions ranging from 50 cm by 50 cm by 8 m to 1 m by 1 m by 10 m, weighing 1.5 metric tons or more but not over 2 metric tons
- ▶ Rollers of stainless steel or cast iron, designed for use in paper manufacturing to support and convey papermaking cloth (i.e., fabric) or the paper web, each weighing 7 metric tons or more but not over 20 metric tons, measuring 7 m or more but not over 12 m in length, with diameter of 40 cm or more but not over 1.5 m, presented with bearing journals on either end and a polymer cover

(xviii) **8466.92.5010:**

- ▶ Workstands designed to use with miter saws, each with metal tube frame, 4 metal legs and 2 metal extension arms
- ▶ Workstands designed for use with miter saws, each with wheels to make workstand mobile and with sides that fold up to extend the work area

(xix) **8481.90.9040:** Angle cock handle assemblies, of iron and steel, each measuring 11.43 cm by 21.59 cm by 5.08 cm and weighing 0.748 kg

(xx) **9022.14.0000:** Radiation therapy systems, each encased by steel-based structural shell with gantry cover comprising three pairs of plastics-based panels

(xxi) **9032.10.0030:** Thermostats designed for air conditioning or heating systems, not designed to connect to the internet, the foregoing designed for wall mounting

Annual Special 301 Review background

The annual Special 301 Review announced on 28 December 2018 requires the USTR, pursuant to Section 301 of the *Trade Act of 1974*, to identify countries that deny adequate and effective IP protections, or fair and equitable market access to US persons who rely on IP protection. The review procedures may result in the USTR designating a country as a Priority Foreign Country (PFC) if the country engages in the

most onerous and egregious acts, policies, and procedures that deny adequate IP protection, has the greatest adverse impact on US products, and is not entering into good faith bilateral or multilateral negotiations to protect IP rights. PFCs may then be placed on an agency created "Priority Watch List" or "Watch List," with the former determined to have serious IP rights deficiencies that will be closely monitored and potentially subject to additional actions including imposition of punitive duties.

To reach these determinations, the USTR's Special 301 Subcommittee will rely on information from multiple sources, including written comments and public testimony regarding IP issues in foreign countries. The USTR requested that interested parties provide written comments to identify "countries whose acts, policies, or practices deny adequate and effective protection for intellectual property rights or deny fair and equitable market access to U.S. persons who rely on intellectual property protection" by 7 February 2019 and those wishing to testify file notice of intent to appear at the public hearing by 21 February 2019. The public hearing will be held on 27 February 2019. The 2019 Special 301 Report will be published on or around 26 April 2019 per the USTR statement.

What to expect next?

Trade negotiations between the US and China remain complex and uncertain, although both nations have recently granted temporary concessions to avoid immediate escalation of tensions while continuing negotiations on US demands for trade reform of China's practices as defined in the Section 301 report.

On 1 December 2018, 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, for an additional 90 days, officially set as 2 March, instead of increasing the rate to 25% as originally planned. In response, Chinese leadership submitted a plan that would lower tariffs on imported US-origin automobiles to 15%, beginning in March so as to be commensurate with the US 90-day deferral, which would reflect the rate assessed on US produced vehicles to match that assessed on all other countries. It also committed to purchasing agricultural, energy, industrial and other products from the US.

The USTR will continue to review product exclusion requests for US Lists 1 and 2. Presently, 7,670 requests remain under "Stage 2" review with the USTR to determine whether the

exclusion request should be granted, based on the substantive criteria set out in the Product Exclusion Notice. For those requests determined by the USTR to meet the criteria, the next stage prior to granting of exclusion is submission of the conclusion to US Customs and Border Protection (CBP) in which the request is further reviewed to determine whether an exclusion would be administrable by CBP should the exclusion be granted. There are currently 886 requests at "Stage 3" and neither the USTR nor CBP have provided any details regarding processing times or criteria for determining "administrability." While additional exclusions are expected to be granted, the procedure is time-intensive and will be based upon both the USTR and CBP's available resources to process the requests.

Actions for businesses

Any company involved in US-China trade is encouraged to identify the potential impact of additional duties and identify which products they import could receive, or may already have received an exclusion. Companies who have paid punitive duties on imports now excluded from the tariffs since implementation in July 2018 should consider developing a comprehensive process for filing for a refund from Customs, upon publication and implementation of approved procedures.

Close monitoring of the exclusion process is warranted, as companies will want to immediately identify products exempt from the duties on the initial list of products announced, as well as any subsequent approvals for products covered under Lists 1 and 2. Additionally, for companies impacted by products included in List 3, monitoring of the USTR's procedures for exclusion requests, which have yet to be

announced, is recommended as submission timelines have been short and based on the denials and approvals to date, a well-articulated and substantiated argument meeting the exemption criteria will be necessary for success.

For companies that have experienced IP issues in foreign countries, consideration should be given to participating in the Special 301 review process as published by the USTR. With comments due in early February, preparation of comments should be undertaken now and should provide the requisite information for the USTR to identify the effect of a particular country's acts, policies, and practices.

Immediate actions for such companies could include:

- ▶ Isolating imports with approved or pending exclusions to maximize benefits under the current Customs regimes.
- ▶ Identifying imports of products subject to the punitive duties through import and export data analytics for developing refund strategies on eligible products.
- ▶ 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.

Endnotes

1. USTR Notice of Product Exclusions. See https://ustr.gov/sites/default/files/enforcement/301Investigations/12.21.18_Notice_of_Product_Exclusions.pdf.
2. 83 Federal Register 67463-67468. See <https://www.govinfo.gov/content/pkg/FR-2018-12-28/pdf/2018-28277.pdf>.
3. <https://www.govinfo.gov/content/pkg/FR-2018-12-28/pdf/2018-28319.pdf>.
4. Currency references in this Alert are to US\$.
5. See EY Global Tax Alert, [US announces temporary pause on planned increase of List 3 tariffs on China origin goods; duties remain in force and key issues remain unresolved](#), dated 3 December 2018.

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