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Indirect Tax Alert

US pauses implementation of sweeping tariffs on Mexico, approves new exclusions for certain products from Section 301 tariffs on imports from China

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Executive summary

On 7 June 2019, the United States (US) President Donald Trump announced that the US would indefinitely suspend the previously announced punitive tariffs on all goods imported from Mexico. The tariffs were set to be implemented today, 10 June, at a 5% rate and would have escalated to 25% over a four-month period.[1] The US State Department issued a formal announcement[2] stating Mexico and the US reached a deal to address concerns over migrants entering the US in violation of US law. The indefinite suspension will be followed up by a review and may be revisited in 90 days.[3]

Also, on 4 June 2019, the Office of the US Trade Representative announced[4] it was granting a new set of exclusions to one 10-digit Harmonized Tariff Schedule (HTS) code and 88 products subject to a 25% punitive tariff as part of the 818 tariff lines covering US$34 billion[5] worth of imports from China annually (US List 1).[6] The announcement continues the agency's process of reviewing claims by companies that their imports are not available outside of China and that the tariffs otherwise harm US interests.

This is the fifth action approving exemptions from the tariffs since late 2018.[7] As of 7 June 2019, the agency has received a total of 10,829 requests. It has denied 58% of those requested and granted 22% while 21 requests are still under consideration. As of the same date, the agency has received 2,920 requests for

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products to be excluded from 279 tariffs lines covering $16 billion worth of annual imports from China (US list 2).[8] The agency has denied 43% of those requests and the remainder of 82 are still under consideration.

Detailed discussion

Tariffs on Mexico

President Trump announced he would use the *International Emergency Economic Powers Act (IEEPA)*, a law from 1977 which provides the President the authority to respond to "any unusually and extraordinary threat" to national or economic security.[9] The President to date has used the law to declare a state of emergency citing border security and the humanitarian crisis on the US' southern border as a threat to national security.

The President's announcement[10] of the tariffs on Mexico stated that while a rate of 5% would be applied on imports beginning on 10 June 2019, the rate would be increased at the President's discretion to 10% on 1 July, 15% on 1 August, 20% on 1 September and lastly to 25% on 1 October.

The joint-statement made on Friday with Mexican officials, and in conjunction with the President's tweet that the tariffs would not go into effect on 10 June, did not specifically mention any trade measures or specific trade commitments by either country. The statement detailed programs to be undertaken by Mexico, intended to process migrant asylum claims more quickly and expand humanitarian protections for those at the border, noting that the migrants would remain in Mexico while their status is evaluated. Mexico also committed to deploying the National Guard to its border with Guatemala. The parties also agreed that, "in the event the measures adopted do not have the expected results, they will take further actions."

On 9 June, the President said that "we can always go back to our previous, very profitable, position of tariffs," adding, "but I don't believe that will be necessary."

USTR exclusions

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.[11] The USTR subsequently proposed, and President Trump ordered, punitive duties of 25% to be imposed on List 1.

The USTR's 4 June 2019 Federal Register Notice (FRN) reaffirms that product exclusion decisions will be made based on the criteria stated in the notices establishing the exclusion process. Specifically, the criteria require 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.

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.

The FRN added a new specific 10-digit HTS code, 9903.88.10, for reporting the products now covered by the latest exclusions. The exclusions include any products imported under one 10 digit code and 88 other products by specific descriptions. These products include:

- Any product imported under 8537.10.8000, touch-sensitive data input devices (so-called "touch screens") without display capabilities, for incorporation into apparatus having a display, which function by detecting the presence and location of a touch within the display area (such sensing may be obtained by means of resistance, electrostatic capability, acoustic pulse recognition, infra-red lights, or other touch-sensitive technology.)
- Non-aircraft gas turbines, imported under 8411.99.9085
- Oil well and oil field crank balanced, long-stroke, and beam pumps, imported under 8414.50.0010
- Certain pumps, imported under 8413.70 and 8413.91
- Certain conveyor belt and line assemblies imported under 8431.39
- Certain circuit assemblies imported under 8504.40 and 8504.90
- And others

Actions for businesses

For companies importing products from Mexico, close monitoring of the recent developments is warranted. While the threat of tariffs has been relieved based on the latest US actions, President Trump has stated that he retains the authority to implement the tariffs in the future should the US become dissatisfied with Mexico's actions regarding the migration process. This is significant as any proposed tariffs in the future would have a material impact on US industry and consumers. Companies involved in cross-border trade between the US and Mexico are encouraged to continue to identify the impact from any future additional duties and to develop potential mitigation strategies. Temporary and permanent actions to consider include but are not limited to:

Immediate:

- Assess tariff impact and prepare for stronger enforcement actions at the border.
- Consider using Bonded facilities and/or Foreign Trade Zones (FTZs) to defer duty payments.
- Use virtual transactions in Mexico, for maquilas, where possible.

Intermediate:

- Evaluate use of special customs provisions such as:
  - 9802.00.50/60/80 provisions as applicable to reduce value subject to tariff of goods reimported into the US.
  - First sale valuation as applicable to reduce value subject to tariff if applicable.
- Based on the nature of the punitive tariffs, revisit the NAFTA marking rules to determine the possibility of considering the goods coming from Mexico as non-Mexican origin.
- Organize manufacturing information to seek exclusion process requests (if such become available should tariffs be imposed).

Long-term:

- Consider moving final assembly to a third-country location (if substantial transformation can be achieved in the third country).
- Consider changing sourcing locations.
- Consider changing manufacturing footprint.

For companies importing products from China, trade negotiations between the US and China continue to remain uncertain. With the tariffs expected to remain in place and with the potential for additional tariffs,[12] any company involved in US-China trade is encouraged to continue to identify the potential impact of additional duties and explore mitigation strategies. Close monitoring of the negotiations and any political developments is warranted, as companies will want to assess any liability under a changing tariff regime. Terms of any deal reached are likely to contain specific conditions that may impact certainty, and possibly duration, of outcome and will need to be closely analyzed once made available.

Immediate actions for such companies to consider include:

- Reviewing contracts with suppliers and with customers to understand who has liability for increased duties and if there are opportunities for negotiation.
- 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 to address potential increases in 301 tariffs.
- Identifying strategies to defer, eliminate, or recover the excess duties paid under Section 301 such as bonded warehouses, FTZs, 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 under either 301 tariffs, re-evaluating current transfer pricing approaches, and for US imports, considering US customs strategies, such as First Sale for Export.

Endnotes

1. See EY Global Tax Alert, *US announces new import tariffs on Mexico, delays tariff increase on certain China goods and formalizes removal of India from GSP*, dated 3 June 2019.
2. US Mexico Joint Declaration, 7 June 2019.
3. Ibid.
4. 84 FR 25895, Notice of Product Exclusions: China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation.
5. Currency references in this Alert are in US$.
6. 83, FR 28711.
7. See EY Global Tax Alerts, *US grants limited exemptions from Section 301 duties and announces annual special review of 301; continued uncertainty ahead*, dated 2 January 2019 and *US grants additional tariff exclusion status to limited set of imports from China*, 25 March 2019.
8. USTR Finalizes Second Tranche of Tariffs on Chinese Products in Response to Unfair Trade Practices, 7 August 2018.
9. 50 U.S.C. § 1701.
10. Statement from the President Regarding Emergency Measures to Address the Border Crisis, 30 May 2019.
11. https://www.whitehouse.gov/presidential-actions/presidential-memorandum-actions-united-states-related-section-301-investigation/.
12. See EY Global Tax Alert, *USTR initiates actions to implement up to 25% tariffs on remaining products from China under Section 301; China retaliates with its own tariffs against most recent actions*, 15 May 2019.

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