

Options for Avoiding Section 301 Duties on Chinese-Origin Goods

In Short

The Situation: The U.S. government has imposed additional 25 percent duties on two sets of Chinese-origin goods, will shortly impose additional 10 to 25 percent duties on another set of Chinese-origin goods, and is considering imposing additional duties on more Chinese-origin products under Section 301.

The Developments: There are a number of options that companies can employ to avoid paying the Section 301 duties, including product exclusion requests, changing the tariff classification and country of origin of Chinese-origin products imported into the United States, and duty deferral or elimination programs.

The Impact: Companies should explore how they might avoid paying the Section 301 duties.

The U.S. government imposed additional 25 percent duties on imports of Chinese-origin products classified under Harmonized Tariff Schedule of the United States ("HTSUS") subheadings included on two lists ("List 1" and "List 2") [published](#) by the U.S. Trade Representative ("USTR") on [July 6](#) and [August 23](#). These additional duties, which were imposed pursuant to Section 301 of the Trade Act of 1974 ("Section 301"), target approximately \$50 billion worth of Chinese-origin products imported into the United States.

In addition to List 1 and List 2, the administration is considering imposing additional 10 to 25 percent duties on a third list ("List 3") of HTSUS subheadings covering approximately \$200 billion worth of Chinese-origin products. The notice and comment period associated with List 3 (which resulted in over 5,000 comments and submissions received on the docket from over 350 companies) ended on September 6. We expect a final announcement from the administration in the coming weeks with duties becoming effective shortly thereafter. Further, President Trump has signaled that he is ready to impose additional duties on the remaining approximately \$267 billion worth of Chinese-origin products imported into the United States annually pursuant to Section 301.

While it is unclear whether Section 301 duties will be imposed on all imports of Chinese-origin products or how long these duties will remain in place, companies should explore how they might avoid paying the duties, as discussed below. Companies must ensure that they understand and comply with the noted requirements and restrictions for each option.

1. Product Exclusion Request

On a company-specific, product-specific basis, companies may [request](#) that Chinese-origin products be excluded from the additional duties. While the administration has only announced an exclusion process for products classified under the HTSUS subheadings included on List 1, we expect that similar exclusion processes will be used for the other HTSUS subheadings on which Section 301 duties have been or will be imposed, including those covered by List 2 and List 3. Under the current process, the exclusions, if granted, are valid for one year and are retroactive to the date on which the duties were imposed. The deadline for product exclusion requests likely will depend on the list on which the HTSUS subheading is included. For example, product exclusion requests for products listed on List 1 must be submitted by October 9, 2018.

Under the current process, each product exclusion request must: (i) contain certain product-specific information, including the physical characteristics that distinguish the product from other products within the covered tariff classification; (ii) provide the quantity and value of the Chinese-origin product that the requester purchased in each of the last three years; and (iii) address the following factors, in addition to any other relevant information:

- Whether the particular product is available only from China;
- Whether the imposition of additional duties on the particular product would cause severe economic harm to the requester or other U.S. interests; and
- Whether the particular product is strategically important or related to "Made in China 2025" or other Chinese industrial programs.

Responses in support of or in opposition to an exclusion request must be submitted within 14 days after the request is posted for public comment, and any replies to such responses must be submitted within seven days after the close of the 14-day response period.

2. Bonded Warehouse

A bonded warehouse is a building or other secured area in which imported dutiable merchandise may be stored, manipulated, or undergo manufacturing operations without payment of duty for up to five years from the date of importation. Liability for duties on that merchandise generally is cancelled when the merchandise is exported, destroyed under the supervision of U.S. Customs and Border Protection ("CBP"), or withdrawn for consumption within the United States after payment of duty. Bonded warehouses may be a good option for companies seeking a product exclusion request that do not want to pay duties on the products and later need to seek a refund from CBP if the request is granted. Instead, those companies could store the merchandise in a bonded warehouse pending the outcome of their product exclusion request. They could then import the merchandise without paying the additional duties if the request is granted. They could decide to export the merchandise to avoid paying the additional duties if the request is denied.

3. Confirm Proper Tariff Classification

Companies may consider reevaluating whether they are using the correct HTSUS subheading for Chinese-origin products they import into the United States. Such an evaluation can be completed by reviewing the HTSUS, prior rulings issued by CBP, and, if that exercise does not provide the level of certainty desired, requesting a formal tariff classification ruling from CBP. If companies discover that they have been using an incorrect HTSUS subheading and the correct HTSUS subheading is not on any of the three lists, they would not have to pay the additional 25 percent duties.

Changing the tariff classification of merchandise imported into the United States can trigger historical liability for prior imports using an incorrect tariff classification. As such, companies changing the tariff classification of imported merchandise also need to evaluate whether and how to deal with any such liability, such as by submitting a voluntary disclosure to CBP.

4. Change Country of Origin

Companies may consider changing their supply chain and location of their manufacturing operations to change the country of origin of Chinese-origin products subject to the additional duties. Doing so requires evaluating whether the changes result in a new country of origin of the products. The relevant rule depends on whether a trade preference

agreement applies. For example, if manufacturing operations are moved to a country such as Malaysia (with which the United States does not have a free trade agreement), companies must evaluate whether operations in Malaysia substantially transform any Chinese-origin components, such that that country of origin of the final product becomes Malaysia. Substantial transformation analyses are very fact specific and must be undertaken on a case-by-case basis. Alternatively, if manufacturing operations are moved to, for example, Mexico, companies would apply a tariff shift rule to determine final country of origin. The tariff shift analysis is less subjective than the substantial transformation analysis.

5. Duty Drawback

Drawback means the refund or remission of a customs duty, fee, or internal revenue tax previously imposed on merchandise imported into the United States. There are several types of drawback. The most frequently used include: (i) manufacturing drawback, of which there are two types, direct identification manufacturing and substitution manufacturing; (ii) unused merchandise drawback; and (iii) rejected merchandise drawback. As an example, direct identification manufacturing drawback allows for drawback not exceeding 99 percent of the duties paid on imported merchandise when articles manufactured or produced in the United States using such merchandise are exported from the United States or destroyed. While the additional duties imposed under Section 301 are [eligible](#) for drawback, drawback is recognized as the most complex commercial program CBP administers because it involves both imports and exports.

6. Foreign Trade Zone

Foreign Trade Zones ("FTZs") are secure areas located in or near CBP ports of entry that are under CBP supervision and generally are considered outside CBP territory. Foreign and domestic merchandise may be moved into zones for operations, including storage, exhibition, assembly, manufacturing, and processing. According to USTR, any Chinese-origin products classified under the HTSUS subheadings included on List 1 and List 2 that are admitted into an FTZ on or after the date duties were imposed on those products may only be admitted as "privileged foreign status." We expect the "privileged foreign status" designation, with regard to products admitted to FTZs, will apply for the other HTSUS subheadings on which Section 301 duties will be imposed, including those covered by List 3. As a result, such products will be subject upon entry for consumption to any ad valorem rates of duty or quantitative limitations related to the classification under the applicable HTSUS subheading. For these reasons, the only way to likely avoid paying the Section 301 duties on Chinese-origin products imported into an FTZ is to export the products from the FTZ or manufacture a product in the FTZ that subsequently is exported from the United States. Companies wishing to use an FTZ may either establish a new FTZ or use an existing FTZ.

7 . Temporary Importation Under Bond

Temporary Importation Under Bond ("TIB") is a program administered by CBP pursuant to which, under certain conditions, merchandise may be temporarily entered into the United States free of duties, taxes, and fees. Instead of paying duties, taxes, and fees, the importer posts a bond for twice the amount of duty, taxes, and fees that otherwise would be owed in connection with the imported merchandise. Under the TIB program, the importer must export or destroy the imported merchandise within a specified period of time or pay liquidated damages. Only certain articles are eligible for importation under the TIB program.

Those articles include articles to be repaired, altered, or processed (including processes which result in articles being manufactured or produced in the United States).

Three Key Takeaways

1. The U.S. government has imposed additional 25 percent duties on two sets of Chinese-origin goods, will shortly impose additional 10 to 25 percent duties on another set of Chinese-origin goods, and is considering imposing additional duties on more Chinese-origin products under Section 301.
2. Companies importing products subject to the additional duties should evaluate their supply chain and explore how to potentially take advantage of the various options available to avoid paying the Section 301 duties.
3. For example, on a company-specific, product-specific basis, companies may file requests to exclude Chinese-origin products classified under HTSUS subheadings subject to the additional duties. Product exclusion requests for products on List 1 must be submitted by October 9, 2018.

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