



Insights on Trade & Customs

July 2018



Welcome to the KPMG Trade & Customs newsletter. Each month, our firm's trade compliance professionals share recent developments of interest to our clients and industry peers in this newsletter. Inquiries about the topics presented herein may be directed to any member of our practice's leadership team.

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On May 16, the European Commission released an implementing regulation to impose 25 percent tariffs on approximately \$3.34 billion worth of U.S. goods across a range of products including apparel, rice, cranberries, bourbon, corn, peanut butter, and steel products. The proposed tariffs were presented to the World Trade Organization (WTO) Council for Trade in Goods, which did not express disapproval. The tariffs went into effect on June 22.

Similarly, the Japanese government is considering imposing retaliatory tariffs of \$409 million on U.S. goods in response to the Section 232 tariffs on steel and aluminum. The proposed tariffs are the equivalent value of the U.S. tariffs. The Japanese government is preparing to present the proposed tariffs to the WTO, which is a requirement under the global trade rules. However, the Japanese government has not yet decided whether to move forward with implementing the tariffs.

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Section 301 – Tariff Updates

On June 15, the United States Trade Representative (USTR) released a list of products imported from China that will be subject to an additional duty of 25 percent under Section 301. There are approximately 818 Harmonized Tariff Schedule (HTS) classifications that will be subject to the additional duties as of July 6. The list focuses on products from the industrial sectors that contribute to or benefit from the “Made in China 2025” industrial policy, including aerospace, information and communications technology, robotics, industrial machinery, and automobiles. However, it does not include consumer products such as cell phones or televisions.

Additionally, the USTR identified a second list of 284 tariff lines that were not on the original proposed list. These are products that are benefitting from the “Made in China 2025” industrial policy. This list will undergo a public notice and comment process, including a public hearing.

The General Administration of Customs (China customs) and the China Certification and Inspection Corporation North America (CCIC)

In the wake of recent tariffs the United States has imposed on China, there has been increased scrutiny by Chinese customs authorities at the border and increased delays in certifications of imports for sale into China. To date, these nontariff trade barriers have impacted scrap metal, cars, fruit, pork, and raw log imports into China from the United States.

Scrap Metal: Chinese customs officials accused the CCIC¹ of not upholding China’s high purity standards when investigating scrap metal exports. As a result, China Customs has revoked CCIC’s ability to issue certificates for the next month, leaving thousands of shipments bound for China stuck in American ports. Without this clearance, shipments are likely to be rejected by China Customs. This can lead to very costly diversions or resale for the producers.

Automobiles: Vehicles produced in the United States have experienced increased scrutiny from China Customs, predominantly at the port of Tianjin. China Customs is examining integral parts of the car’s emissions systems, effectively requiring the disassembly of the car. During this process, cars remain at the port, causing significant storage costs.

Fruit: Shipments of oranges, lemons, cherries, and apples from the United States are now exposed to increased scrutiny upon arrival into China. Fruit is an easy target according to industry leaders since shipments can be flagged on the grounds of health and safety concerns. Further to the increased rate of inspections, Chinese Customs’ examinations have gone from clearing imports in a matter of hours to taking days to resolve issues, thus delaying the release of cargo. Many shipments of fruit are now rotting due to the length of the inspections, a tactic that China has utilized before when imposing nontariff barriers on Filipino bananas during territory disputes in the South China Sea.

Raw Tree Logs: The U.S. Animal and Plant Health Inspection Service (APHIS) has been called to look into cases of delayed clearance surrounding raw log exports to China. Raw logs have been historically imported into China and been fumigated upon arrival. However, now it appears that there are a large numbers of log shipments being rejected by China Customs before they are fumigated. Although a final response has not yet been determined, APHIS is working with affected parties, such as the International Wood Products Association, to compile reports regarding the situation.

Trade Rhetoric between the United States and China Continues in the Latest WTO Meeting

The war of words between the United States and China regarding trade has occurred in many forums over the past year including the World Trade Organization (WTO). At the WTO’s general council meeting in Geneva, Switzerland, trade representatives from the U.S. and Chinese governments continued to accuse each other of being protectionist and threatening the fundamentals of the global trading system that has opened access to international markets.

Deputy U.S. Trade Representative Dennis Shea challenged China’s position: “It is amazing to watch a country that is the world’s most protectionist mercantilist economy position itself as the self-proclaimed defender of free trade.”² The Chinese delegation countered by criticizing the White House’s decision to propose tariffs on \$150 billion USD of Chinese goods.

¹ CCIC is a third-party organization that provides a number of services including but not limited to inspection, surveying, certification, and testing for goods, including goods destined for China. CCIC employs an electronic management system that enables customers to apply for inspections worldwide, including clearing Customs in the ports of China. China Customs officials are able to view such electronic certifications via the electronic management system.

The Trump administration has made efforts to diminish the tension between it and China regarding the proposed tariffs. U.S. Treasury Secretary Steven Mnuchin led a U.S. delegation to China in an effort to negotiate a better trade relationship and Trump stated that he was going to talk to Chinese President Xi Jinping regarding trade. President Trump has consistently threatened allied and adversarial countries with tariffs as a way to enhance U.S. national security and its economy. However, these threats have been derided by trade representatives across the world. European Union Ambassador Marc Vanheukelen said that national security can't justify the U.S. Sections 232 (19 U.S.C. § 1862), and the steel and aluminum tariffs, and that the tariffs could "trigger systemic risks undermining the multilateral trading system." *Id.* He further claimed that the EU is concerned about the tariffs' potential impacts on global markets. *Id.*

CBP Ruling "Buy American" Substantial Transformation

On April 24, 2018, U.S. Customs and Border Protection (CBP) issued a final determination regarding whether certain gyrocompasses assembled in the United States—in part from foreign components—are considered products of the United States for the purpose of U.S. Government procurement (HQ H287851).

Because some of the components of the gyrocompasses came from outside the United States, CBP applied a "substantial transformation" analysis to determine the appropriate country of origin of the finished products. In the decision, CBP considered several factors in their determination of whether a substantial transformation occurred in the United States:

- The extent of the operations and processing performed in the United States
- Whether the foreign parts lost their identity and became an integral part of the new article
- The country of origin of the item's components
- Whether the processing in the U.S. rendered the product with a new name, character, and use
- The importance of the U.S. components to the functioning of the final product
- Whether the assembly operations are minimal/simple, or are complex and time-consuming.

CBP continued to uphold its position that a change in a product's name is the weakest evidence of a substantial transformation (see *Uniroyal, Inc. vs. United States*, 3 CIT 220, *aff'd* 703 F.2d 1022 (Fed. Cir. 1983)). In addition, CBP found that the significant post-assembly testing procedures undertaken for the finished products were evidence that the gyrocompasses were substantially transformed in the United States.

CBP and International E-Commerce Standards

CBP aims to shape global standards for e-commerce transactions. CBP published a response to the WCO draft framework for cross-border e-commerce practices. One of CBP's primary goals is to promote economic prosperity while also responding to threats to enforcement created by increasing volumes of international transactions on an e-commerce platform. Accordingly, CBP's strategy involves creating stronger partnerships with partner government agencies and foreign governments and educating importers on their compliance responsibilities. Further, CBP's comments to the WCO's proposed standards reflect CBP's focus on the future of e-commerce and commitment to the Presidential Executive Order 13785, "Establishing Enhanced Collection and Enforcement of Antidumping and Countervailing Duties and Violations of Trade and Customs Laws." CBP Trade Policy and Programs Executive Director John Leonard expressed at the National Customs Brokers & Forwarders Association of America (NCBFAA) Annual Conference in Rancho Mirage, CA in May, that he hopes CBP's response will postpone the release of a final framework from WCO for another year.

Blockchain Technology Program for the North American Free Trade Agreement (NAFTA)

CBP plans to launch a two-to-four-week pilot blockchain technology program for NAFTA and Central America Free Trade Agreement (CAFTA) certificates of origin. A blockchain is a distributed public ledger that records transactions between two users in a transparent and secure manner. The data related to the transactions is saved in connected cryptographic blocks, creating an endless chain of data blocks and allowing parties to keep track of all transactions conducted. Through the pilot, CBP will be investigating how blockchain technology can minimize data duplication and whether multiple block chain programs can communicate at the same time. To prepare for the launch of the pilot, CBP will be conducting user story refinement sessions and creating a time line and goals for delivery. The pilot will include imports across

² Bryce Baschuk, "Up Is Down" in the Crazy World of the China-U.S. WTO Clash, Bloomberg, 2018.

all ports. Blockchain is one of the first technologies the Emerging Technologies Working Group³ is assessing for how it can be used to benefit trade.

Australia Trusted Trader Program 2020 Goal

The Australian Trusted Trader (ATT) Program is a voluntary trade facilitation program that offers certain benefits to 'trusted traders' provided the business is trade compliant and has sufficient supply chain security controls in place. There has been significant interest in the program, particularly given that trusted traders will be offered duty deferral and streamlined reporting arrangements (slated for introduction later this year). Streamlined reporting is expected to result in significant savings to traders through a reduction in processing costs. Other key benefits include, but are not limited to, quicker access to international trade markets, priority trade services, access to Mutual Recognition Arrangements, a light touch at the border, etc.

Companies which do have an Australian Business Number would be eligible to apply for ATT, as far as the business has been active in the international supply chain for at least two years and is financially solvent. The process consists of completing an online application form followed by an onsite visit to the business premises to review the supply chain controls (which may also help identify improvements to enhance supply chain security). Following an assessment of the application and the on-site validation, the business may be offered ATT Accreditation to access its benefits.

Currently, the ABF has accredited 111 traders and 53 service providers with numerous others awaiting qualification. The ABF is aiming to accredit 250 businesses by July 1, 2018 and a maximum of 1,000 businesses by June 2020 to ensure the program is adequately resourced. With the ABF contemplating an eventual cutoff of trusted traders based on its finite resources to manage the initiative, now is the time for clients' companies to give serious consideration to joining this program.

U.S. Ceasing Participation in the JCPOA (Iran Nuclear Deal)

In early May, the United States announced its intent to abandon participation in the Joint Comprehensive Plan of Action (JCPOA), which is an agreement on the nuclear program in Iran, reached in 2015 between Iran, the five permanent members of the United Nations Security Council (China, France, Russia, United Kingdom, United States), Germany and the European Union, committing both sides to obligations related to limitations on Iran's nuclear development. The U.S. withdrawal will trigger changes in U.S. trade policy and reactivate certain sanctions against Iranian goods, services, and people.

As part of the JCPOA, the U.S. committed to ease certain sanctions imposed on non-U.S. parties (e.g., European manufacturers and banks) pursuant to secondary sanctions, thus opening up the Iranian economy for non-U.S. persons. The goal of secondary sanctions is to penalize non-U.S. companies and persons who commercially transact with Iran by

³ The group was founded in 2017 by the Global Supply Chain Subcommittee of the Commercial Customs Operations Advisory Committee (COAC). The COAC is tasked with advising the Secretaries of the Department of the Treasury (Treasury) and the Department of Homeland Security (DHS) on the commercial operations of CBP and related Treasury and DHS functions.



limiting their access to the American financial network and economy. Certain sanctions were reduced when JCPOA went into effect in January 2016 when the International Atomic Energy Agency (IAEA) determined that Iran was compliant with the initial nuclear components outlined in the Action.

The limited relief meant that U.S. persons, including financial institutions and companies, remained prohibited from engaging with Iran even after the JCPOA was implemented in 2016. This means, non-U.S. persons are still unable to leverage U.S. banks, insurance, and other institutions for cross-border finance and trade with Iran (e.g., non-U.S. persons could deal with Iran only in nondollar currencies).

Shortly after the announcement to withdraw, the President issued a National Security Presidential Memorandum (NSPM) directing the Secretary of State and the Secretary of the Treasury to immediately prepare for the reimposition of all of the U.S. sanctions lifted or waived in connection with the JCPOA, to be accomplished as expeditiously as possible and in no case later than 180 days from the date of the NSPM.

After the 180-day wind-down period, the U.S. Department of the Treasury's Office of Foreign Assets Control (OFAC) will also revoke General License H, which authorizes foreign entities of U.S. companies to do business with Iran, and the U.S. government will reimpose sanctions against individuals and entities removed from OFAC's list of Specially Designated Nationals and Blocked Persons (SDN List).

The United States could also potentially require the reintroduction of United Nation sanctions on Iran that were repealed with the passage of UN Security Council Resolution 2231 (2015) under a "snapback" provision included in the resolution, which endorsed the JCPOA. New reports indicate that Iran and the other JCPOA parties remain committed to the JCPOA and plan to negotiate a continuation of the deal, with or without the United States.

Treasury Response to Russian Affiliate Activity

On April 6, 2018, OFAC announced sanctions against seven Russian oligarchs, 12 companies owned or controlled by these oligarchs, 17 senior Russian government officials, a state-owned Russian weapons trading company, and its Russian bank subsidiary. The April 6 sanctions had widespread effects on many parties as U.S. persons are generally prohibited from transacting with blocked persons, unless otherwise authorized by OFAC. The presence of a sanctioned officer or director at a nonsanctioned company may, however, create issues for both U.S. and foreign persons dealing with those entities. U.S. persons

remain prohibited from dealing with a blocked person, even if that person is acting on behalf of a nonsanctioned entity.

OFAC designated United Company RUSAL PLC (RUSAL) for being owned or controlled by, directly or indirectly, EN+ Group. In that same action, OFAC designated EN+ Group for being owned or controlled by, directly or indirectly, Oleg Deripaska and other entities he owns or controls. Oleg Deripaska was designated for having acted or purported to act for or on behalf of, directly or indirectly, a senior official of the Government of the Russian Federation, as well as for operating in the energy sector of the Russian Federation economy. Deripaska has been investigated for money laundering, and has been accused of threatening the lives of business rivals, illegally wiretapping a government official, and taking part in extortion and racketeering. There are also allegations that Deripaska bribed a government official, ordered the murder of a businessman, and had links to a Russian organized crime group. These actions and allegations brought RUSAL under fire, as Deripaska is its majority shareholder.

The April 6 sanctions program was revised on May 1, 2018 by the Trump Administration providing RUSAL a means for relief from sanctions. Relief could be granted to RUSAL if it severs ties with Kremlin-linked billionaire Oleg Deripaska. In response, RUSAL has pledged that Deripaska, its majority stakeholder, would relinquish control. The U.S. Treasury also extended the deadline for companies to wind down dealings with the Russian aluminum producer by almost five months, to October 23, 2018, helping those who work with RUSAL and its subsidiaries.



ZTE Corporation Violation of the Export Administration Regulations (EAR) and Iranian Transactions and Sanctions Regulations (ITSR)

In March 2017, the United States Department of Commerce (Commerce Department) announced a \$1.19 billion penalty against ZTE Corporation for violating Export Administration Regulations (EAR) and the ITSR. As part of this penalty, the Commerce Department mandated that ZTE take disciplinary action against its senior employees involved in these EAR and ITSR violations. However, in April 2018, the Department of Commerce announced that ZTE had not taken the appropriate disciplinary actions against senior personnel responsible for the violations, and made false statements to this effect. As a result of these false statements and inaction, U.S. Secretary of Commerce Wilbur Ross announced a denial of export privileges for ZTE Corporation.

However, on June 7, the Commerce Department announced that it would be replacing its previously issued denial order with nearly approximately \$1.4 billion in penalties instead. Furthermore, BIS is requiring that ZTE contract a group of compliance coordinators that will report directly to BIS, and is also mandating that the board of directors and senior leadership be replaced in its entirety.

Additional pressure is being exerted on ZTE in Congress, where the Senate passed its annual defense reauthorization bill that includes an amendment on ZTE. Specifically, government agencies would be prevented from purchasing ZTE products. The amendment goes even further, and would re-impose any penalties on ZTE that were nullified by the Trump Administration.

As of this publication, the House had not yet finalized their version of the defense reauthorization bill. The ZTE amendment, therefore, could further change.

Conferences and Events in Trade Come see the KPMG T&C Team

— WIT-NC Presents – Artificial Intelligence & How Regulation of AI Affects Silicon Valley, A Conversation with Roz Thomsen (Thomsen and Burke LLP) – The Conference will be held on July 18, in Sunnyvale, California. Jessica Latham will be attending the conference.

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