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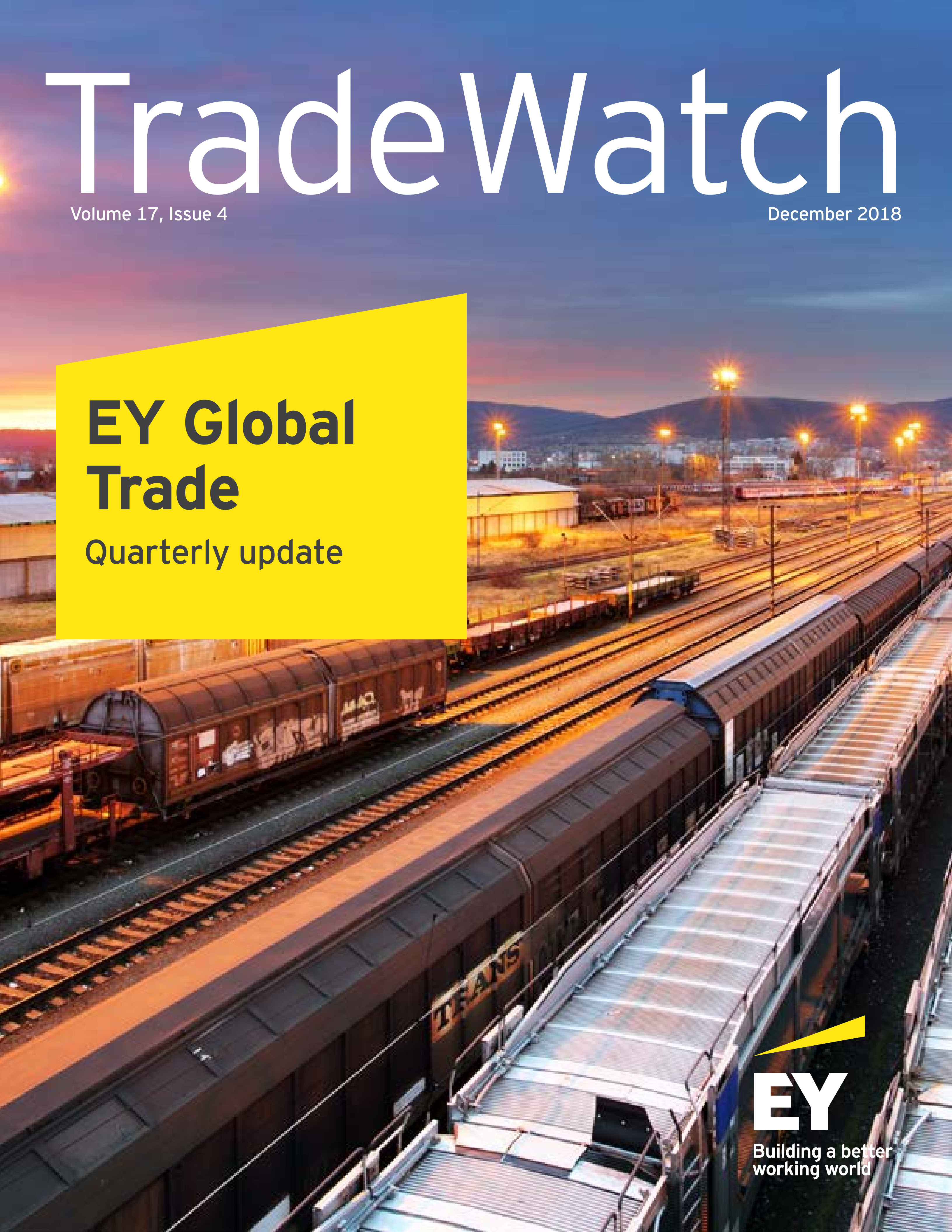

EY Global Trade

Quarterly update

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Spotlight on trade deals reached in principle: USMCA and Brexit

United States-Mexico-Canada Agreement to replace NAFTA

On 1 October 2018, US President Donald Trump announced a preliminary agreement with Canada to revise the terms of the existing North American Free Trade Agreement (NAFTA) between the US, Mexico and Canada.[1] The proposed agreement with Canada follows seven rounds of NAFTA renegotiations among the three nations that took place over the course of 13 months and comes roughly 30 days after the US and Mexico announced a similar "preliminary agreement in principle" to modernize the rules of NAFTA.[2]

The United States Trade Representative (USTR) published the full text of the proposed agreement on 1 October 2018,[3] which is named the United States–Mexico–Canada Agreement (USMCA). The USTR also released details on how the USMCA will achieve stated objectives to modernize previous commitments made under the NAFTA, including major changes to trade in agricultural products, automobiles, and automotive parts and textiles; increased thresholds for low-value (de minimis) shipments subject to informal entry procedures; enhanced data protection for biologic drugs; and other provisions, as discussed below.[4]

The proposed USMCA consists of 34 chapters, which exceeds the 22 chapters contained in the NAFTA, and covers new areas, such as labor, the environment, anti-corruption and regulatory policy, among others. Notably, it also includes 11 annexes and 12 side letters. Four of those side letters specifically grant Canada and Mexico important concessions pertaining to the ongoing US investigation into imported automobiles and automotive parts.[5] A similar agreement, however, was not reached on the additional duties presently being imposed on imported Mexican and Canadian steel and aluminum.

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1 "President Donald J. Trump Secures A Modern, Rebalanced Trade Agreement with Canada and Mexico," White House Fact Sheet, 1 October 2018. See https://www.whitehouse.gov/briefings-statements/president-donald-j-trump-secures-modern-rebalanced-trade-agreement-canada-mexico/.

2 See United States Trade Representative (USTR) Press Releases, 27 August 2018, "Strengthening NAFTA for Agriculture," "Modernizing NAFTA to be a 21st Century Trade Agreement," and "Rebalancing NAFTA to Support Manufacturing." Available at: https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018.

3 Text of the USMCA is available at: https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/united-states-mexico.

4 See USTR's US-Mexico-Canada Trade Fact Sheets, 1 October 2018. Available at https://ustr.gov/about-us/policy-offices/press-office/fact-sheets.

5 See United States-Mexico-Canada Agreement Text: Canada 232 Side Letter, US-Mexico 232 Side Letter, US-Canada 232 Process Side Letter and US-Mexico 232 Process Side Letter.

As discussed below, the preliminary agreement requires ratification by all three countries. Ratification is likely, and publication of the text provides businesses with a critical opportunity to now analyze the proposed provisions in advance, assess the impact on their operations and evaluate necessary business changes to take advantage of the new rules.

Key provisions of the USMCA

Rules of origin (Chapter 4)

The USMCA proposes major changes to the way that automobiles and automotive parts qualify for preferential treatment. The USMCA raises the regional value content (RVC) threshold for automobiles from 62.5% to 75.0%.[6] Particular RVC requirements vary based on the type of vehicle or parts under consideration. For example, while light vehicles would require 75% RVC, heavy vehicles would require 70%. The RVC for auto parts, on the other hand, would range from 65% to 75% depending on whether these are considered "core," "principal" or "complementary." While tariff shift rules (where applicable) remain in the proposed USMCA, the tracing list, which required that only certain auto parts be tracked to determine NAFTA content, is eliminated. The USMCA also adds a new labor value content rule requiring that 40% to 45% of auto content be produced by workers earning at least USD16 per hour.[7] Lastly, finished vehicle producers will be required to purchase 70% North American steel and aluminum.[8]

The USMCA also includes stricter rules of origin for other industrial products, such as chemicals, steel-intensive products, glass and optical fiber. For textiles and apparel, the USMCA limits rules contained in the NAFTA that permitted the use of certain non-NAFTA inputs. To qualify for preferential treatment under the USMCA, certain inputs incorporated into finished textile or apparel, such as sewing thread, pocketing fabric, narrow elastic bands and coated fabric, must be made in the same region as the finished product. For example, if a finished blouse is manufactured in Mexico, its inputs must originate in Canada, Mexico and/or the US.

Trade in agriculture — market access (Chapter 3)

Under the proposed USMCA, Canada has agreed to provide limited market access to US exports of dairy, poultry (turkey and chicken) and eggs. Likewise, the US has agreed to provide limited market access to Canada exports of dairy, peanuts and peanut products, and sugar and sugar products. Both nations will introduce new tariff rate quotas to facilitate these concessions. Canada also agreed to eliminate milk price classes 6 and 7 and adopt measures to limit the impact of its surplus skim milk production on external markets, such as the introduction of export surcharges.

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[6] USMCA Chapter 4.

[7] The specific calculation of the labor value content considers manufacturing costs, technology and assembly expenditures.

[8] Seventy percent of an original equipment manufacturer's annual purchases of aluminum and steel would have to be from the US, Mexico or Canada.

New provisions

Digital commerce (Chapter 19)

The USMCA contains provisions on digital trade that were not previously discussed in NAFTA. It bans data localization requirements, or laws that regulate the collection, storage and international transmission of data collected within the country. Additionally, internet companies will not be held liable for content posted from third parties, and companies wanting to do e-business do not require a physical presence in a jurisdiction to operate there.

Macroeconomic policies and exchange rate matters — addressing China's trade practices and policies (Chapter 33)

The USMCA includes the first-ever chapter on currency manipulation and monetary policy. It requires public disclosure of monthly data on currency reserves data and interventions in foreign exchange markets, quarterly balance of payments data, including exports and imports, and other public reporting via the International Monetary Fund (IMF). The USMCA also contains a clause relevant to future free trade agreement negotiations with nonmarket economies, most notably China. Specifically, it requires notice of intent to negotiate a free trade agreement with a nonmarket economy, disclosure of the objective of negotiations and text of the agreement at least 30 days before signing.

Other significant provisions

The USMCA includes the following key provisions:

- Establishes procedures that streamline certification and verification of rules of origin:
  - Certification of origin is now allowed to be made by the exporter, producer or importer of the goods.
- Maintains duty-free treatment for originating goods, prohibition on export duties and other charges, as well as waiver of customs processing fees
- Adds transparency to import and export licensing procedures
- Increases de minimis shipment values for Canada and Mexico (Chapter 7):
  - Mexico will provide duty-free entry for shipments valued at or below USD100, while maintaining duty- and tax-free treatment for shipments at or below USD50. Shipments at or below USD100 will be subject to minimal formal entry procedures.
  - Canada will provide duty-free entry for shipments up to CAD150 (approximately USD113) and raise its threshold from CAD20 to CAD40 (approximately USD15 to USD30) for shipments eligible for non-taxable importation under federal taxation regimes (e.g., imported free of import goods and services tax, GST). However, provincial taxes, which may apply in the case of business-to-consumer import transactions, are not covered by the negotiated outcomes. Shipments at or below CAD150 will be subject to minimal formal entry procedures, assuming they otherwise qualify for informal line clearance options.
- Incorporates NAFTA's Article 303 restrictions on duty deferral and duty drawback into Chapter 2
- Includes 10 years of data protection for biologic drugs and a robust scope of products eligible for protection (Chapter 20)
- Incorporates NAFTA's Chapter 19 dispute settlement provisions into the USMCA
- Establishes new government procurement rules between the US and Mexico, but procurement rules between the US and Canada will remain unchanged and will continue to operate according to the rules established under the World Trade Organization (WTO) Agreement on Government Procurement (Chapter 13)

- Contains the following Section 232 relief provisions for Mexico and Canada:
  - Two side letters provide Mexico and Canada with relief in the event that the US imposes punitive tariffs on imports of automobiles and automotive parts under Section 232 of the Trade Expansion Act of 1962 (Section 232):
    - Provides exclusion from Section 232 duties for the first 2.6 million passenger vehicles imported from Canada and for the first 2.6 million passenger vehicles imported from Mexico
    - Provides exclusion from Section 232 duties for light trucks imported from Canada and Mexico
    - Provides exclusion from Section 232 duties for the first USD32 billion worth of auto parts imported from Canada and the first USD108 billion worth of parts imported from Mexico
  - Two side letters establish a mandatory consultation process in the event that the US imposes Section 232 measures:
    - The US must provide a 60-day grace period from the date of imposition of any Section 232 duties before they take effect to allow for consultations.
    - Mexico and Canada have the right to take measures of equivalent commercial effect, including WTO rights to challenge a Section 232 measure.
  - Importantly, nothing in the USMCA addresses the existing punitive tariffs imposed by the US under Section 232 on Canadian- and Mexican-origin steel and aluminum products.
- Preserves cultural institution exemptions currently in the NAFTA

Entry into force, renewal and withdrawal (Chapter 34)

USMCA provisions also address entry into force, expiration, renewal and withdrawal:

- The agreement will enter into force on the first day of the third month following the notification of the last country to complete its domestic processes required for implementation of the agreement.
- The agreement will automatically terminate after 16 years of entry into force unless each country agrees to extend for another 16 years.
- The agreement will be reviewed by the countries every six years to determine whether changes are needed.
- Countries may withdraw from the agreement with a six-month written notice. In the event that one country withdraws, the agreement remains in effect for the other countries.

What to expect next?

Once signed by the Presidents of the United States and Mexico and by the Prime Minister of Canada, the legislatures of all three countries must subsequently ratify the USMCA before it will enter into force. In the US, under Trade Promotion Authority (TPA) legislation, the US President must provide Congress with 90 days' notice before signing a trade agreement and the legal text of the agreement 60 days before signing. The US President provided Congress with the requisite notice on 1 September, and the release of the text meets the second requirement.

In the US, while the US President is authorized to negotiate trade agreements, only Congress has the authority to implement them. Accordingly, once the president signs the agreement, an implementing bill must be submitted for congressional approval. Prior to a vote in Congress, the TPA legislation requires a series of actions, including an assessment of the agreement by the International Trade Commission, a description of the legal changes that would be required to comply with the provisions of the agreement and submission of the final text of the agreement to Congress. Once the implementing bill is introduced, Congress has a maximum of 90 days in session to enact it. Under TPA rules, the bill is subject to a simple yes or no majority vote, which means that amendments are not allowed to the text of the agreement. Until the US Congress passes implementing legislation for the USMCA, the NAFTA will remain in effect.

In Mexico, the USMCA must be submitted to the Senate and for revision by the Foreign Relations Ordinary Commission to be considered and ratified. A two-thirds majority of the Mexican Senate must vote in favor of the agreement to ratify the agreement (the Mexican Senate is composed of 128 senators). Notice of an agreement to terms between the US and Mexico was provided on 27 August 2018, which is significant because it gave former Mexican President Enrique Peña Nieto's administration enough time to sign the USMCA — a priority of his administration — before he left office on 1 December 2018. Mexico's President Andrés Manuel López Obrador supports the revised agreement, but had indicated that he might have sought to renegotiate its terms had it not been signed before he took office.

In Canada, the government must introduce the USMCA in the form of an implementing bill. The USMCA must first be put to a vote in the House of Commons and Senate after a full review by Parliament pursuant to Parliamentary Subcommittees' reports and debate. This process will likely take several months. Supplemental legislation would then need to be drafted and passed where required, although much of this would already be in existence under the existing NAFTA or CUSFTA (Canada-United States Free Trade Agreement) legislation. One issue to watch is the upcoming reactions of the provincial government that was elected in the province of Quebec on 1 October 2018. Canada has made concessions on access to its dairy market that are controversial in Quebec due to the size of its dairy industry, which could impact implementation of the USMCA's negotiated outcomes on dairy in Quebec.

Once the agreement is signed by the presidents of all three nations and then ratified by the legislatures of the US, Mexico and Canada, the USMCA will enter into force no sooner than three months from the date of the last country's notice. The ratification process is therefore likely to continue into 2019 before the USMCA becomes effective.

Actions for businesses

With publication of the text of the new USMCA, businesses can begin to model the impact of the proposed changes on their operations. For those in the automotive, textile and other industries, changes announced to the existing rules of origin will make qualification for benefits under the agreement more difficult. On the other hand, e-commerce retailers and consumers, intellectual property rights holders, such as drug manufacturers, among others, likely stand to benefit under the new terms of the preliminary agreement.

Based on the above, companies should further evaluate their current NAFTA footprint to quantify benefits presently recognized under the existing agreement and assess qualification benefits anticipated under the USMCA. By leveraging their customs data, companies can determine whether they may be adversely impacted by the proposed changes. Specifically, companies should understand how their products satisfy existing RVC requirements and then explore potential changes or alternatives to sourcing that may be required to preserve originating status under the terms of the proposed USMCA. Also, with regard to those products subject to an increase of RVC, changes to the applicability of qualification by tariff shift and, for the auto industry, the elimination of the tracing requirement, a closer look on origin qualification options and special methodologies is merited. For example, the use of the self-produced (intermediate) materials rules to aid NAFTA qualification has been quite effective in other industries that have been subject to similar rules under the NAFTA.

Businesses should consider the following key actions:

- Assemble relevant data from Canada, Mexico and the US
- Identify the company's most significant products manufactured in North America, considering:
  - Customs data — to determine categories, amounts and highest duty savings
  - Sales data — to determine highest volumes, values and sales forecasts
  - Products that don't currently qualify
  - Bills of material (e.g., product-specific data necessary for determining eligibility for trade benefits)
- Identify applicable rules of origin,[9] how the existing rule is currently met and how it will change under the proposed USMCA[10]
- Model the impact of proposed changes (per product) and explore solutions — ask:
  - Would your company need to replace non-originating components to comply with a stricter tariff shift rule or an increased RVC requirement?
  - How close are you in reaching the current RVC rule?
  - Would you need to use a special provision, such as the self-produced (intermediate) materials rule, to assist in meeting qualification requirements?
- Be prepared for increased enforcement, such as free trade agreement audits by local customs authorities
- Review the company's import transactions into Canada to reevaluate taxable importation status with respect to both federal and provincial regimes and to further determine any contingent requirements with respect to registration of the business in Canada, including any obsolescence of currently held registrations under the new de minimis value rules
- Continue to monitor the impact of the Section 232 US tariffs and Canadian and Mexican retaliatory tariffs and surtaxes and take advantage of drawbacks or remissions of such tariffs or surtaxes where applicable

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[9] Set forth in NAFTA Annex 401.

[10] USMCA Chapter 4.

Look for more insight into the USMCA developments in future issues of *TradeWatch*.

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Brexit: no change to trade fundamentals . . . yet

There has been progress of sorts on Brexit with the issuance of the draft Withdrawal Agreement[11] on 14 November 2018. While it reads positively for traders, it faces a rocky ratification road, which means that Brexit plans and actions aimed at mitigating a hard Brexit in March 2019 will remain unchanged until as late as February 2019.

The draft agreement provides detail on the relationship between the UK and rest of the EU (the EU27) during the proposed transition period to manage the UK's exit from the EU for the period from 29 March 2019 to 31 December 2020. In addition, there is a specific protocol on Ireland-Northern Ireland, the so-called "back-stop," which comes into effect if the EU27 and the UK have not resolved the Irish border issue in meeting the objective of there being no hard border within the transition period. However, it is materially lacking in information on the bigger issue of the end destination for the relationship between the EU and the UK.

The transition period aims to maintain the status quo relationship between the EU27 and the UK. From a trade perspective, it means the continuance of no customs borders and no tariffs or clearance-related costs. There is still potential change for businesses with regard to EU free trade agreements (FTAs), where the honoring of those agreements and accepting UK content as qualifying will require the agreement of the other parties to those agreements; albeit with the EU27's and the UK's trade deficit with these parties, there is an expectation that the preferential treatment will continue.

The back-stop comes into force if there is a failure to find a solution to the Ireland-Northern Ireland border within the transition period, noting there is also a potential provision to simply extend the transition period itself with six months' notice, i.e., before July 2020. The back-stop seeks to establish "a" customs union between the EU27 and the UK, but the UK, with the exception of Northern Ireland, will be in a separate regulatory regime. This means a "regulatory border" between mainland UK and both the EU27 and Northern Ireland, with the relevant enforcement and inspection requirements. The customs union will be managed by a movement certificate issued to evidence the free circulation status of goods and that is validated at export only, i.e. on movement out of the UK into the EU27 or vice versa. This arrangement has echoes of the EU relationship with Turkey, which traders can look to as a planning proxy, and there is a growing view that this is the target final customs relationship.

[11] European Union (Withdrawal) Act 2018.

Businesses have received the draft agreement positively. However, there is concern with its ratification to the extent that Brexit plans are essentially remaining unchanged.

25 Nov	EU summit to get formal agreement among EU leaders
Mid-Dec	Possible date for the "meaningful vote" in the UK Parliament 13–14 Dec: EU summit – possible agreement on any outstanding issues
Mid-Jan	Deadline for UK Government to come up with a new plan in the event of no majority in meaningful vote Possible date for ratification vote in European Parliament
Feb–Mar	Legal ratification of the agreement in both houses of the UK Parliament
29 Mar	Brexit

Unlike the overall deal itself, it does not need to be ratified in individual EU27 parliaments; rather, it requires a simple majority (greater than 50%) in the EU Parliament and a qualified majority (65%) in the European Council. The major challenge though is the UK Parliament with the so-called "meaningful vote" in December and formal ratification in February or March, all simple majority votes. The deal could fall at any of these hurdles, with the UK political environment particularly volatile as evidenced by the Cabinet resignations that accompanied the release of the draft agreement.

If this is unsuccessful, several options will then open up, which are not mutually exclusive:

- Renegotiation of the deal
- Extension of Article 50
- A second referendum
- A UK general election in the event of complete deadlock

Or

- The UK leaving on WTO terms

Given this spread of potential outcomes, the probabilities of which fluctuate daily, businesses are not yet viewing the Withdrawal Agreement as sufficiently reliable to change direction away from the core planning scenario of a no-deal Brexit in March 2019.

Planning for no deal

There is a wide span of views on the potential for a no-deal Brexit, assumed to mean WTO terms between the EU27 and the UK in March 2019. No matter the view on likelihood, the vast majority of businesses have set their planning focus on this outcome given the downside risks and lead times required to mitigate against it.

While potential tariff costs are unwelcome, the leading concern remains supply chain continuity in the face of a formal customs border at both export and import. From a trade perspective, this means ensuring the systems, data and resources (internal and external, e.g., brokers) are in place to meet customs declaration requirements. There is then additional activity on facilitation measures, such as Authorised Economic Operator (AEO) status and simplified clearance procedures, in the UK Customs Freight Simplified Procedures (CFSP).

To assist businesses to prepare for a potential hard Brexit, in July and August of this year, Her Majesty's Government (HMG) began publishing a series of Information Notices. HMG announced that there would be approximately 70 notices issued in total. In the June 2018 issue of TradeWatch, we described the most relevant notices published at that time. Since then, four additional notices have been published. Two of these have specific references to customs and international trade.

Notice 1: "Structuring your business if there's no Brexit deal"

This notice considers the cross-border business operations of both EU and UK businesses in the event that the UK leaves the EU with no deal. Currently, the UK follows EU rules and regulations covering company law. These regulations set out how companies and other legal entities operate within the Single Market, how they register and how they operate across country borders in the EU. Post-Brexit, the UK Government states its intention to ensure that the UK will continue to have a functioning regulatory framework for companies, so that as long as possible, current laws and rules will continue to apply.

That said, companies will need to consider their legal status post-Brexit and determine any changes that may need to be implemented to allow them to continue doing cross-border business post-Brexit.

Key changes identified by HMG include the following:

- EU companies that operate branches in the UK will become subject to the same information and filing requirements as any other third-country company branch.
- UK citizens may face restrictions on their ability to own, manage or direct a company registered in the EU, depending on the sector and EU member state in which the company is operating. This could involve meeting additional requirements on the nationality or residency of individuals allowed to act as senior managers or directors and/or limits on the amount of equity that can be held by non-nationals.
- UK businesses that own or run business operations in EU member states will likely face changes to the law under which they operate, depending on the sector and EU member state.
- UK companies and limited liability partnerships that have their central administration or principal place of business in certain EU member states may no longer have their limited liability recognized.
- UK investors in EU businesses may face restrictions on the amount of equity that they can hold in certain sectors in some EU member states.

In terms of implications for customs purposes, the notice discusses the issue of branches of UK companies located in the EU and branches of EU entities located in the UK. Both of these could prove problematic post-Brexit. In the event of a hard Brexit, export and import declarations will be required for all movements of goods between the UK and the EU. This will require a customs value to be determined for each item declared. The vast majority of UK and EU importers use, as the basis of their customs value, the transaction value, i.e., the price paid or payable for the goods between two legal entities (the seller and the buyer). However, branches are not considered to be separate legal entities from their parent company, therefore; a sale between a parent company and a branch is not considered as an acceptable transaction for customs valuation purposes. This issue could cause many companies and groups to have to consider restructuring their supply chain and/or transaction chain, or even consider using an alternative method of customs valuation. Any of these changes will inevitably cause additional work and compliance requirements for many companies.

Furthermore, many businesses are already facing the dilemma of how to deal with customs authorizations or accreditations, e.g., AEO, in respect of EU branches in the UK and UK branches in the EU. For example, the question has been asked of customs authorities in the EU as to whether an EU-located branch of a UK company can apply for AEO in its own right. There is a strong opinion among experts that the Union Customs Code (UCC) does offer some flexibility in this respect, and there are good arguments that the EU branch could apply for AEO itself if it fulfills the requirements of being considered established in the EU customs territory (having sufficient substance), as per the UCC, Art. 5. 31b. and 32., which state:

(31) "Person established in the customs territory of the Union" means:

(a) In the case of a natural person, any person who has his or her habitual residence in the customs territory of the Union

(b) In the case of a legal person or an association of persons, any person having his or her registered office, central headquarters or a permanent business establishment in the customs territory of the Union

(32) "Permanent business establishment" means a fixed place of business where both the necessary human and technical resources are permanently present and through which a person's customs-related operations are wholly or partly carried out.

This indicates that the requirement of a permanent establishment for customs purposes could be met by having a branch that has a registered office and/or that carries out its customs operations. This would appear to be a relatively easy requirement for many businesses to meet. However, the response from the EU customs authorities has been that they are unable to give an opinion on this point, or consider AEO applications in this respect, until the final post-Brexit agreement with the UK has been reached.

This lack of clarity adds further incentive for companies to consider restructuring their groups, supply chains or transactions to Brexit-proof their cross-border goods flows, rather than suffer the uncertainty of waiting for a final Brexit solution and risk being unable to operate effectively from day one post-Brexit.

Notice 2: "Existing free trade agreements if there's no Brexit deal"

This notice purports "to inform businesses and other interested parties about the government's plans to ensure continuity for the UK's existing trade agreements with partners outside the EU if the UK does not reach agreement with the EU on the terms of its withdrawal prior to 29 March 2019."

As a member of the EU, the UK currently participates in around 40 FTAs with over 70 countries. These FTAs cover a wide variety of relationships, including:

- Economic Partnership Agreements with developing nations
- Association agreements, which cover broader economic and political cooperation
- Trade agreements with countries that are closely aligned with the EU, such as Turkey and Switzerland
- Other FTAs

Many UK businesses make use of FTAs, association agreements and other trade-related agreements and obtain reduced or zero rates of import duties under these agreements' preferential duty arrangements. In 2017, the Office for National Statistics (ONS) data showed that trade with third countries that had FTAs with the EU accounted for around 12% of the UK's total trade. Currently, these duty benefits may apply to goods imported into the UK from trade agreement partner countries or to imports of goods into the partner countries from the UK. The UK is a member of these agreements by virtue of being an EU member state.

Therefore, post-Brexit, the UK will fall out of these preferential trade agreements and lose the duty reduction benefits both on imports into the UK and exports to partner countries. For many businesses, this could represent a large additional duty cost on their imports into the UK and on the goods they export (often to customers) in the beneficiary countries, as the full rate of duty will be payable in the beneficiary country.

In the notice, the HMG has declared its intent to maintain existing preferential trade benefits and states that it is working with partner countries to cover solutions for a range of different Brexit outcomes. It does acknowledge, however, that if there is no deal, there will be no implementation period and the UK will fall out of existing EU agreements on 29 March 2019. In this scenario, the government will seek to bring into force bilateral UK-third country agreements from exit day or as soon as possible thereafter. However, this will require significant resources to negotiate, which the UK doesn't have, and there is doubt whether the UK could negotiate comparable terms. The notice also confirms, "Should arrangements to maintain particular preferences in a no deal scenario not be in place on exit day, trade would then take place on a Most-Favored Nation (MFN) basis, which is sometimes referred to as 'WTO terms'"; in effect, full WTO duties would become payable.

For those currently utilizing existing EU FTAs, it presents a number of challenges around origin. Will products meet the rules if only UK and FTA party content qualifies? Even transactions with the EU, where there is UK content, does that cause the need for a reassessment? Even more detailed, would the validity of long-term supplier declarations issued before the UK's exit and where the Brexit impact question has not been posed be recognized?

What next?

Given the very uncertain landscape, companies should continue to mitigate the impacts of a March 2019 Brexit until the deal has at least been through the first vote in the UK Parliament and ratification in the European Parliament.

All impacted companies should by now have a Brexit plan in place for critical impacts and should have triggered mitigating actions where dictated by lead times or business-critical impacts.

As full legal ratification may not be completed until March, even in a best-case scenario, companies will have to decide whether to continue to mitigate until close to the exit date or whether to pull back on contingency plans based on partial ratification.

Under the Withdrawal Agreement, the UK's post-transition fallback position would no longer be WTO but a customs union with the EU, increasing the likelihood of that option if the agreement is ratified.

The Withdrawal Agreement comes with a seven-page political declaration setting out the shape of the future EU-UK relationship, but the details will be a matter for future EU-UK negotiations. Therefore, clarity on the end state may still not be available for businesses until late 2019 or 2020. That seems to be tomorrow's question, not today's.

Look for further insight and updates on the Brexit process in future issues of *TradeWatch*.

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The Comprehensive and Progressive Agreement for Trans-Pacific Partnership comes into effect on 30 December 2018

On 30 December 2018, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) will come into force.[12] This comes after New Zealand, Mexico, Japan, Singapore, Canada, Australia and, most recently, Vietnam ratified the agreement. Peru, Chile, Brunei and Malaysia are also part of the 11-member CPTPP but have not completed their ratification processes. It is expected that slower ratification of the agreement for these latter countries will result in later entry into force for their commitments. Companies interested in using the CPTPP may thus need to monitor and plan carefully due to the staggering of different country tariff elimination schedules and other commitments.

The CPTPP has large market access potential, accounting for nearly 13.5% of global gross domestic product (GDP), 6.7% of world population and 14.4% of world trade. Signed on 8 March 2018, the 30 chapter CPTPP is a revised version of the Trans-Pacific Partnership following the withdrawal of the United States under President Donald Trump.

It is regarded as a progressive agreement, as it not only benefits businesses in terms of trade in goods and services but also includes, among others, commitments on environment and labor. This article looks at some of these benefits and impacts to companies.

Trade in goods

The CPTPP aims to eliminate more than 98% of tariffs in the free trade area.[13] This covers areas including, but not limited to, industrial goods, seafood, horticulture and wine. New market access opportunities are present for trade between countries that did not have free trade agreements (FTAs) previously.

For example:

- Singapore is expected to enjoy tariff elimination on its exports of pharmaceutical products and organic chemicals into Mexico currently subjected to duty rates between 6.5% and 15%, respectively.[14]

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[12] "The Comprehensive and Progressive agreement for Trans-Pacific Partnership enters into force in December," *Ministry of Trade and Industry Singapore website*, https://www.mti.gov.sg/en/Newsroom/Press-Releases/2018/11/The-CPTPP-enters-into-force-in-December, accessed 21 November 2018.

[13] "TPP-11 outcomes at a glance," *Australian Government Department of Foreign Affairs and Trade website*, https://dfat.gov.au/trade/agreements/not-yet-in-force/tpp-11/outcomes-documents/Pages/tpp-11-outcomes-at-a-glance.aspx, accessed 21 November 2018.

[14] "The Comprehensive and Progressive agreement for Trans-Pacific Partnership enters into force in December," *Ministry of Trade and Industry Singapore website,* https://www.mti.gov.sg/-/media/MTI/Newsroom/Press-Releases/2018/11/Press-release---The-CPTPP-Enters-Into-Force-in-December.pdf.

- Tariffs on New Zealand wines imported into Canada (its fourth largest market), as well as apples and kiwifruit into Japan (its largest market) will also be eliminated. Tariffs on beef exports from New Zealand to Japan will be reduced from 38.5% to 9.0% over 16 years, which would eliminate Australian beef exporters' current tariff advantage over New Zealand in the Japanese market.[15]
- Canada has pledged to eliminate its 6.1% tariff on passenger vehicle imports over four years, as well as auto part tariffs of up to 8.5%, upon entry into force of the CPTPP.[16]

New market access opportunities are also created through the CPTPP above and beyond previous FTAs.

For example:

- Australia will enjoy additional market access into Vietnam, including tariff elimination on butane, propane, liquefied natural gas, refined petroleum products, iron and steel products, and automotive parts.
- Australia will also enjoy new market access into Japan for sugar exports and new quota access for rice and rice flour exports.
- Malaysia has also committed under the CPTPP to provide guaranteed access for Australian providers to engage in the wholesale distribution of automotive parts and components and to stop providing excise tax credits for locally produced automotive parts.[17]

Rules of origin

All market access opportunities under the Trade in Goods chapter are subject to rules of origin and other terms and conditions within the CPTPP. While most rules of origin are similar across countries, some bilateral rules of origin exist through bilateral side letters. For example, Canadian-made motor vehicles sold in Australia and Malaysia enjoy a more liberal rule of origin.[18]

The CPTPP also allows for regional cumulation. This is one of the unique benefits of a regional agreement versus a bilateral agreement. Regional cumulation allows the CPTPP to recognize input from all CPTPP countries as originating content. In this way, companies with cross-border supply chains could become more cost-effective and efficient.[19]

Trade in services

The CPTPP trade in services commitments go beyond those under the General Agreements on Trade in Services. This is due to the adoption of the "negative list" approach. There is new market access in sectors such as professional services, computer-related services, research and development services, construction services, education services, environmental services, mining-related services and services incidental to energy distribution.[20]

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[15] "Comprehensive and Progressive agreement for Trans-Pacific Partnership," *New Zealand Foreign Affairs & Trade website*, https://www.mfat.govt.nz/en/trade/free-trade-agreements/free-trade-agreements-concluded-but-not-in-force/cptpp/cptpp-overview/, accessed 21 November 2018.

[16] "Overview and benefits of the CPTPP," *Government of Canada website*, https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/overview-apercu.aspx?lang=eng, accessed 21 November 2018.

[17] "TPP-11 outcomes: Goods market access," Australian Government Department of Foreign Affairs and Trade website, https://dfat.gov.au/trade/agreements/not-yet-in-force/tpp-11/outcomes-documents/Pages/tpp-11-outcomes-goods-market-access.aspx, accessed 21 November 2018.

[18] "Overview and benefits of the CPTPP," Government of Canada website, https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/overview-apercu.aspx?lang=eng, accessed 21 November 2018.

[19] "The Comprehensive and Progressive agreement for Trans-Pacific Partnership enters into force in December," Ministry of Trade and Industry Singapore website, https://www.mti.gov.sg/-/media/MTI/Newsroom/Press-Releases/2018/11/Press-release---The-CPTPP-Enters-Into-Force-in-December.pdf.

[20] "What does the CPTPP mean for services," Government of Canada website, http://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/sectors-secteurs/services.aspx?lang=eng, accessed 21 November 2018.

CPTPP countries have also committed to allowing the supply of electronic payment services for payment card transactions into their countries on a cross-border basis. The CPTPP countries have agreed to guarantee not to prevent service suppliers and investors from transferring data across borders where it is part of business activity. Businesses will also not be forced to build data storage centers or use local computing services in CPTPP countries where they wish to conduct business.

Beyond the general commitments, bilateral cooperation initiatives also exist. One example is that Vietnam and Australia will launch a pilot program in the education sector to enable Australian universities to provide online courses to Vietnamese students.[21]

Government procurement

The Government Procurement chapter provides for new market access opportunities in terms of government procurement, especially in CPTPP countries that are not parties to the World Trade Organization Agreement on Government Procurement. For example, IT, construction, consultancy and government procurement projects in countries such as Malaysia, Mexico and Vietnam are no longer closed to foreign bidders but fall within the auspice of the CPTPP.[22]

Impact of the CPTPP

The impact of the CPTPP is expected to be extensive. The Canadian Government estimates tariff savings of CAD428 million (approximately USD322 million) to Canadian exports per year, with the bulk from exports to Japan (CAD338 million, approximately USD254 million), Australia (CAD47 million, approximately USD35 million) and Vietnam (CAD25 million, approximately USD19 million).[23] The New Zealand Government's estimates of tariff savings were NZD222 million (approximately USD151 million) annually, with NZD92 million (approximately USD63 million) starting as soon as the CPTPP enters into force.[24] The Singapore economy is expected to grow 0.2% by 2035 as a result of the CPTPP. The CPTPP as a whole, is expected to generate an additional SGD147 billion[25] (approximately USD107 billion) in global income.[26] Further, being an open-access FTA, the CPTPP has already invited queries from markets, such as Taiwan, Thailand, the UK and mainland China, that are studying the CPTPP for the purpose of accession. The scope and impact of the CPTPP may well expand in the future.

Considering the complex and uncertain trade situation in the world, investing in a CPTPP-relevant supply chain could provide not only new opportunities for growth in Asia-Pacific markets but also greater certainty and better risk-managed business value chains.

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21 "TPP-11 outcomes: Services," *Australian Government Department of Foreign Affairs and Trade website*, https://dfat.gov.au/trade/agreements/not-yet-in-force/tpp-11/outcomes-documents/Pages/tpp-11-outcomes-services.aspx, accessed 21 November 2018.

22 "The Comprehensive and Progressive agreement for Trans-Pacific Partnership enters into force in December," *Ministry of Trade and Industry Singapore website*, https://www.mti.gov.sg/en/Newsroom/Press-Releases/2018/11/The-CPTPP-enters-into-force-in-December, accessed 21 November 2018.

23 "Economic impact of Canada's participation in the Comprehensive and Progressive Agreement for *Trans-Pacific Partnership," Government of Canada website,* https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/impact-repercussions.aspx?lang=eng, accessed 21 November 2018.

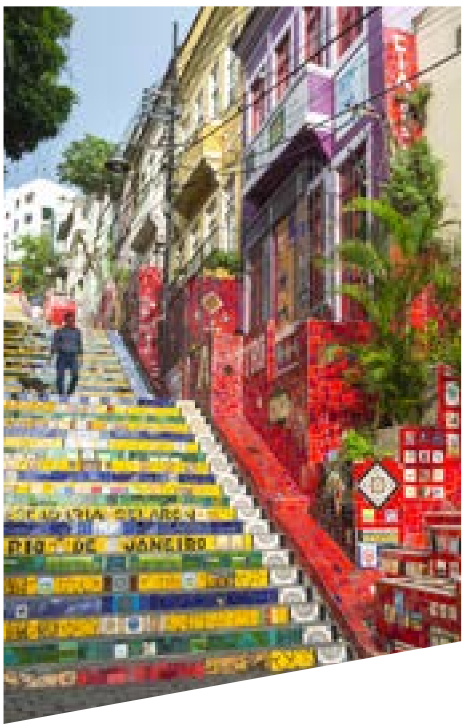
24 "Comprehensive and Progressive Agreement for Trans-Pacific Partnership," *New Zealand Foreign Affairs & Trade website*, https://www.mfat.govt.nz/en/trade/free-trade-agreements/free-trade-agreements-concluded-but-not-in-force/cptpp/cptpp-overview/, accessed 21 November 2018.

25 One billion is defined as one thousand million.

26 "Parliament: Singapore economy, exports expected to grow with CPTPP trade deal, says Chan Chun Sing," *The Straits Times,* 6 August 2018.

Brazil

Brazil to reduce bureaucracy in the customs clearance process



Brazil has recently introduced new import and export processes that are expected to make Brazilian companies more competitive abroad and to generally benefit companies doing business in Brazil by introducing a single window system and streamlining customs clearance processes.

New export process

The Brazilian Secretary of Foreign Trade introduced a new export process using the Single Portal of Foreign Trade under Ordinance SECEX No. 14/17 of 22 March 2017, as amended (the Ordinance). The purpose of the Ordinance is to bring Brazil into compliance with the guidelines of the World Trade Organization (WTO) Agreement on Trade Facilitation, to which Brazil is a signatory.

This new process aims to reduce clearance times and costs and to increase the competitiveness of Brazilian products abroad by streamlining government requirements. The government has been allowing companies to test the new system and give suggestions to be incorporated into the process since December 2016.

As of 1 October 2018, all new export operations must be registered through the Single Export Declaration (*Declaração Única de Exportação*, DU-E) in the Single Foreign Trade Portal, replacing, for all purposes, the Register of Export (*Registro de Exportação,* RE), the Export Declaration (*Declaração de Exportação*, DE) and the Simplified Export Declaration (*Declaração Simplificada de Exportação,* DSE) previously registered in the Foreign Trade System (*Sistema Integrado de Comércio Exterior,* SISCOMEX).

What's new for exporters?

The process brought new features, such as integration with the electronic invoice whereby all information from the electronic invoice will be automatically transported to the DU-E, a 60% reduction in data needed for completion in comparison with the old process and automation of information conferencing. The single window between exporters and the government will centralize access to services and systems, concentrating on one-point information that was previously dispersed among different systems.

The elimination of certain procedural steps means the end of duplicate authorizations in separate documents. In the future, it will be possible to use one authorization for more than one transaction, unlike in the past, when one authorization was valid for a single export transaction only.

In addition, procedural flows, such as customs clearance, cargo handling, and licensing and certification, are no longer sequential and are conducted in parallel, which is expected to reduce the average time to complete an export transaction by 40%.

New import process

The proposal for the new import process[27] was developed in close partnership with the private sector. Its purpose is to establish procedures that will make the import process more efficient and expedient, while enabling the authorities to provide effective control of import operations.

The pilot project was delivered on 2 October 2018, and only companies certified in the Brazilian Authorized Economic Operator (AEO) program, conformity level 2,[28] or importers that operate on behalf of these companies, were invited to participate and test the new system.

The import operations in the pilot project will be limited to the waterway mode. Customs will have exclusive control over the payment of federal taxes without the need for approval by other agencies.

What's new for importers?

The main benefit of the new process is the replacement of the current Import Declaration (*Declaração de Importação,* DI) and the Simplified Import Declaration (*Declaração Simplificada de Importação,* DSI) with the Single Import Declaration (*Declaração Única de Importação,* DUIMP), which makes it possible to include all the required information in a single document. The DUIMP can be registered even before the goods arrive in the country and, as a rule, parallel to the issuance of import licenses.

The process for granting import licenses has been simplified, which is another positive development. Previously, it was necessary to have a separate license for each import transaction. Under the new system, the request to obtain a license will be centralized, unlike the previous system where the request was routed through different government agencies, depending on the type of goods that are imported. These agencies included the National Institute of Metrology, Standardization and Industrial Quality (*Instituto Nacional de Metrologia, Qualidade e Tecnologia,* INMETRO), the Brazilian Institute of the Environment and Renewable Natural Resources (*Instituto Brasileiro do Meio Ambiente e dos Recursos Naturais Renováveis,* IBAMA), the Ministry of Agriculture, Livestock, and Supply (*Ministério da Agricultura, Pecuária e Abastecimento,* MAPA), among others.

Goods will remain in the primary zone[29] for a shorter period, which is likely to reduce importation costs. The harmonization of procedures adopted by the various public administration agencies responsible for the control of imports is also likely to save time and reduce bureaucracy.

Closing thoughts

The Brazilian authorities and politicians appear to be committed to improve and refine customs procedures to help companies be more competitive abroad and to develop Brazil's economy.

The new export and import processes are expected to make Brazilian companies more efficient by reducing bureaucracy, saving time, and eliminating unnecessary steps and duplication of effort. By integrating public administrative procedures, the new process eliminates the need to obtain duplicate authorizations and streamlines operations, which is expected to reduce the costs associated with import and export operations.

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[27] "Normative Instruction BFR nº 1,833" and "Ordinance of the Co-ordination-General of Customs Administration (Coana) nº. 77 of 2018."

[28] For a discussion of Brazil's Authorized Economic Operator program, see "Authorized Economic Operator in Brazil: Full Scope Launched," in the March 2016 issue of *TradeWatch*. See also "Brazil issues complementary module to the AEO-integrated program," in this issue of *TradeWatch*.

[29] The primary zone includes ports, airports and border area where the goods are first imported into Brazil's territory.

Brazil issues complementary module to the AEO-integrated program

Brazil's Ministry of Agriculture, Livestock, and Supply (*Ministério da Agricultura, Pecuária e Abastecimento,* MAPA) published, on 31 October 2018, the Normative Instruction SDA/MAPA No. 45 (the Ordinance) dated 30 October 2018 in the Official Gazette. The Ordinance amends Normative Instruction No. 39/2017 and introduces a complementary module to the Authorized Economic Operator (AEO) integrated program[30] called the AEO-Agro Program. The Ordinance also sets forth the certification rules, as well as the technical, administrative and operational controls, that interested AEO-certified companies must meet to obtain additional certification under the AEO-Agro Program.

The AEO-Agro certification is voluntary and is intended for importers and exporters of agricultural products. It will be granted according to the type of operations carried out by the importer or exporter so long as the compliance and reliability levels required by the AEO Program have been met.

The AEO-Agro certification grants, among others, the following benefits:

- Designation of an agro-authority responsible for the company for a direct channel of communication
- Priority issuance of sanitary and phytosanitary certificates
- Priority analysis and approval of goods in transit from a port/airport to a bonded warehouse

Approved AEO-Agro certifications are valid for three to five years as of the date of approval.

The AEO-Agro certification is an important enhancement to the AEO program. Companies that meet the certification requirements may realize supply chain benefits, greater business certainty and competitive advantages.

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[30] For a discussion of Brazil's Authorized Economic Operator program, see "Authorized Economic Operator in Brazil: Full Scope Launched," in the March 2016 issue of *TradeWatch*.

Costa Rica

Costa Rica modifies Free Trade Zone regime regulations to regulate logistic service companies

Costa Rica has modified the Free Trade Zone (FTZ) regime regulations to establish a new legal and operative framework for FTZ regime beneficiaries that provide logistic services (servicios logísticos or SEL companies). Executive Decree No. 41263-COMEX-H (the Decree) went into effect on 10 September 2018.

An amendment to Section 5 of the FTZ regulations issued in July 2018 initially regulated SEL companies. However, that amendment only set out the authorized activities and operations that SEL companies may conduct.

The Decree, on the other hand, establishes a comprehensive framework, providing legal certainty to these companies. The regulations include provisions for the operations SEL companies may conduct, facility requirements, obligations, customs valuation, reexport of merchandise and commercial invoice equivalents. SEL companies also may sell up to 50% of their services in Costa Rica.

Under the Decree, logistic centers could facilitate trade for the merchandise owners by moving goods to different customs territories safely and efficiently, which is expected to allow Costa Rica to consolidate logistic centers in the Central America region.

This is an important development for companies that wish to offer logistic services because unlike past legislation, the Decree provides much needed guidance.

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United States

US Customs clarifies how it will levy tariffs on USD250 billion of China-origin goods in Sino-US trade dispute

The US and China continue to be locked in an escalating trade dispute that is now affecting over USD360 billion[31] of trade between the two nations. Since imposing a third round of tariffs against one another on 24 September 2018, the US continues to threaten to levy punitive tariffs on all China-origin imports. China has promised "tit for tat" countermeasures in response to US threats. With no signs of either side backing down, businesses should expect prolonged trade disruption into next year and beyond.

Country	Product list	Affected tariff lines	Additional duties applicable to listed tariff lines	Scope	Effective date of tariffs	Product exclusion deadline
US	List 1	818	25%	USD34b	6/7/18	9/10/2018
US	List 2	279	25%	USD16b	23/8/18	18/12/2018
US	List 3	5,745	10% to 31/12/18; 25% afterward	USD200b	24/9/18	Not announced
China	List 1	545	25%	USD34b	6/7/18	Not announced
China	List 2	333	25%	USD16b	23/8/18	Not announced
China	List 3	5,207	5%, 10%, 20%, 25%	USD60b	24/9/18	Not announced

[31] One billion is defined as one thousand million.

While the outcome of the Sino-US trade dispute remains unclear, US Customs and Border Protection's (CBP) approach to assess Section 301 duties on importers of China-origin goods is beginning to take shape. CBP recently issued two important ruling letters that discuss how it will apply Section 301 duties to products imported from the North American Free Trade Agreement (NAFTA) countries[32] and goods imported in "sets."[33] The US also implemented important changes to the Harmonized Tariff Schedule of the US (HTSUS) that affect the classification and application of Section 301 duties to imported networking equipment, Bluetooth devices and chemicals.

Detailed analysis

CBP clarifies origin rules for purposes of applying Section 301 tariffs to goods from NAFTA countries

On 13 September 2018, CBP issued an important headquarters ruling letter, HQ300226, discussing the interplay between Section 301 tariffs, country of origin and the NAFTA marking rules. The facts and holding in HQ300226 are quite narrow: CBP determined that an electric motor assembled in Mexico from three China-origin components was a product of Mexico for country of origin marking purposes, but of China-origin for Section 301 duty purposes. Notably, the ruling *did not* address a scenario in which the electric motor was NAFTA-originating (eligible for normal duty-free entry) under HTSUS General Note 12. CBP's rationale did, however, include a clear articulation of the standard for determining origin for purposes of Section 301 that warrants further consideration in the context of NAFTA-originating goods, goods eligible for preferential treatment under other free trade agreements (FTAs) and goods with special origin rules, such as textile and apparel articles:

> *"[When] considering a product that may be subject to antidumping, countervailing, or other safeguard measures [including Section 301], the substantial transformation analysis is applied to determine the country of origin."*

CBP went on to explain:

> *"[I]n accordance with 19 C.F.R. § 102.0, the 102 marking rules are applicable for the limited purposes of: "country of origin marking; determining the rate of duty and staging category applicable to originating textile and apparel products as set out in Section 2 (Tariff Elimination) of Annex 300–B (Textile and Apparel Goods); and determining the rate of duty and staging category applicable to an originating good as set out in Annex 302.2 (Tariff Elimination)."*

This ruling serves as a good reminder that the criteria for determining origin for purposes of Section 301 is the non-preferential "substantial transformation" standard. Qualification as originating for purposes of a preferential trade agreement such as NAFTA, while often helpful in evaluating the subjective substantial transformation standard, is not determinative of origin determination under Section 301.

[32] Mexico, Canada and the United States recently reached an agreement in principle to revise the terms of the North American Free Trade Agreement. A detailed discussion of the agreement, which has been named the United States-Mexico-Canada Agreement (USMCA), is featured in this edition of *TradeWatch*.

[33] From a US Customs perspective, a "set" generally consists of at least two articles classifiable in different headings that are put up together to meet a particular need in a manner that is suitable for direct sale without repackaging.

It is also important to consider any special criteria for origin applicable to specific categories of goods, such as textiles and apparel.[34] Firsthand discussions with CBP regarding the textile/apparel origin rules confirmed that the agency will, at a minimum, rely on the principles contained in those rules when determining origin for purposes of administering Section 301 duties.

In light of the subjective nature of the substantial transformation standard and the financial impact at stake, importers that have traditionally evaluated only preferential origin criteria for a product should exercise enhanced diligence of country of origin determination when Section 301 duties can be in play. In analyzing country of origin, importers may discover that their origin conclusions vary under the different sets of rules (e.g., substantial transformation vs. preferential origin rules). For products potentially subject to Section 301 tariffs, importers should consider obtaining an advance ruling from CBP or, at a minimum, develop documentation that demonstrates that they have exercised reasonable care in determining their product's country of origin.

CBP clarifies applicability of Section 301 tariffs to imports of "sets"

On 6 September 2018, CBP issued HQ H299857 affirming its ruling in NY N298532 (26 July 2018), which addressed whether Section 301 tariffs were owed on an imported toolset partially consisting of China-origin tools. The importer did not dispute classification of the 129-piece mechanic's toolset under HTSUS 8206.00.00, which provides for "[t]ools of two or more headings 8202 to 8205, put up in sets for retail sale." Nor did the importer dispute that the general rate of duty applicable to products of subheading 8206.00.00 is "[t]he rate of duty applicable to the article in the set subject to the highest rate of duty." Accordingly, CBP considered the duty rate of each article in the set and identified five items classified under subheading 8466.10.0175 as the items with the highest applicable rate of duty. These items were subject to normal duties of 3.9% plus additional Section 301 duties of 25.0% for a total duty rate of 28.9% ad valorem. Consequently, CBP concluded that the rate of duty applicable to the entire set was 28.9%.

The importer argued that previous guidance issued by CBP in a Section 301 frequently asked questions (FAQ) document stated that punitive duties apply to an entire set only if the HTSUS of the item that provides the set's essential character is subject to the Section 301 duties. In other words, additional duties are not owed on a set when its essential character is derived under an HTSUS subheading that is not otherwise subject to Section 301 duties.

CBP concluded that duties were owed on the entire set after clarifying that its Section 301 FAQ document only applies to situations where the imported goods are classified in accordance with General Rule of Interpretation (GRI) 3. It further explained that certain areas of the HTSUS mention sets specifically by name, whether at the heading or subheading level. Where sets specifically mentioned in the subheading of the HTSUS describe the imported goods, classification can be determined according to GRI 1 and GRI 6. The toolset under consideration fell under 8206.00.00, which provides for "[t]ools of two or more headings 8202 to 8205, put up in sets for retail sale." Importantly, the HTSUS subheading specifically describes the imported goods, it is an eo nominee provision, and since the toolset is classified under GRI 1, the rules governing GRI 3(b) sets do not apply to the imported goods.

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[34] Section 334 of the Uruguay Round Agreements Act (Pub L 103-465, codified as 19 USC §3592 and implemented as 19 CFR §102.21) establishes rules of origin for textile and apparel products that are imported into the US. Except as otherwise provided by statute, these rules apply for purposes of the customs laws and the administration of quantitative restrictions (quotas).

Since the goods were classified pursuant to GRI 1, CBP concluded that the agency's guidance pertaining to the applicability of Section 301 duties to sets does not apply to the imported toolset because its guidance is limited to situations where goods are classified under the principles of GRI 3(b).

In light of CBP's decision in H299857, goods classified pursuant to GRI 3(b) principles are subject to punitive duties to the extent that the essential character of the set (i.e., the HTSUS provision under which the entire set is classified) is derived from a China-origin product that is described on one of the Section 301 lists. If the HTSUS provision, under which the entire set is classified according to GRI 3(b), is not covered by the Section 301 tariffs, but the set contains components that are classified in a subheading covered by the 301 list, the 301 duties will not be assessed on the individual components.

A similar result should occur when an unassembled or incomplete item, often referred to as a kit, is imported. According to GRI 2(a):

> *"Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as entered, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also include a reference to that article complete or finished (or falling [sic] to be classified as complete or finished by virtue of this rule), entered unassembled or disassembled."*

Any importer contemplating importation of a kit or a set should review the consequences of the essential character assessment, and if a Section 301 duty would be imposed on the entire import value, the importer also should consider whether separate importations of the component items would achieve a better result.

US excludes certain electronic consumer devices from punitive tariffs

On 13 September 2018, the Committee for the Statistical Annotation of the Tariff Schedule received a request from the United States Trade Representative (USTR) to create a new statistical suffix (e.g., 10-digit level) within HTSUS 8517.62.00 that effectively excludes imported China-origin smart watches and other Bluetooth-enabled consumer devices from punitive tariffs.

HTSUS subheading 8517.62.00 covers:

> *"Telephone sets, including telephones for cellular networks or for other wireless networks; other apparatus for the transmission or reception of voice, images or other data, including apparatus for communication in a wired or wireless network (such as a local or wide area network), other than transmission or reception apparatus of heading 8443, 8525, 8527 or 8528; parts thereof: Other apparatus for transmission or reception of voice, images or other data, including apparatus for communication in a wired or wireless network (such as a local or wide area network): Machines for the reception, conversion and transmission or regeneration of voice, images or other data, including switching and routing apparatus"*

HTSUS subheading 8517.62.00 previously covered modems, switches, routers and other Bluetooth-enabled devices, including consumer devices, within two statistical suffixes: 8517.62.0010, which covered "Modems, of a kind used with data processing machines of heading 8471," and 8517.62.0050, which covered "Other." Effective as of 21 September 2018, the new statistical breakout for HTSUS subheading 8517.62.00 is now:

- 8517.62.0010: Modems, of a kind used with data processing machines of heading 8471
- 8517.62.0020: Switching and routing apparatus
- 8517.62.0090: Other

Importantly, US Section 301 List 3 punitive tariffs apply to the first two subheadings of 8517.62 (8517.62.0010 and 8517.62.0020) that cover modems, switching apparatus and routing apparatus, but not to the newly created subheading 8517.62.0090 that likely covers smart watches and other Bluetooth-enabled consumer devices. US List 3 punitive duties also apply to similar equipment that is not specified in subheading 8517.62 but that is covered under the residual basket provision of 8517.69.0000 ("Other apparatus for transmission or reception of voice, images or other data, including apparatus for communication in a wired or wireless network (such as a local or wide area network): Other").

Importers of China-origin devices classified under 8517.62.00 should immediately assess the impact of the HTSUS changes. As of 19 November 2018, CBP has issued seven rulings classifying merchandise under subheading 8517.62.0090 and two classifying products under subheading 8517.62.0090. Very little elaboration on the standard of review is given; although, in one ruling, N300976 (30 October 2018), CBP appears to be using a very broad definition of "switching and routing apparatus":

- CBP does not view the terms "switching and routing apparatus" to be specific to any one technology or system. All types of transmission systems may require that their signals be routed and/or switched to effect the desired result.

Importers with importations of items previously classified in HTS 8562.17.0050 should proceed cautiously with the proper determination of the new classifications. As the Section 301 duties will increase to 25% on 1 January 2019, the consequences can be quite material.

US temporarily suspends/reduces normal duties on imports of certain chemicals and other items

On 13 October 2018, HTSUS amendments contained in the Miscellaneous Tariff Bill Act of 2018 became effective. These amendments temporarily reduce normal duties on some products while eliminating normal duties on others through 31 December 2020. The duty suspensions/reductions are contained within Subchapter II to Chapter 99 of the HTSUS and cover approximately 1,660 separate tariff lines. The changes largely impact importers of raw material and intermediate chemicals classified under HTSUS Chapters 28 (inorganic chemicals), 29 (organic chemicals) and 38 (miscellaneous chemical products), which account for over 50% of the tariff lines, while the remaining changes are spread across 50 other HTSUS chapters.

Importantly, roughly half of the goods classified under HTSUS codes impacted by the changes are currently imported from China. To the extent that those HTSUS codes are also described on a Section 301 list, such goods remain subject to punitive duties per CBP's guidance in Cargo Systems Messaging Service (CSMS) announcement 18-000493 (21 August 2018). Businesses in the industrial chemicals, life sciences and related sectors should review the HTSUS changes to determine the impact on their operations and ensure that their customs brokers are paying the correct amount of duties.

Update on Section 301 exclusion requests

US List 1

The deadline for submitting product exclusion requests to the USTR for items subject to punitive duties under US List 1 expired on 9 October 2018. As of 1 November 2018, 7,818 requests for exclusion were filed, and the USTR has not posted any decisions granting a requested exclusion. Of these requests, 816 were denied and a letter to the requestor was published. The remaining 7,002 requests have moved on to further review by the USTR and CBP.

Stage 1 of the review process consists of the public notice and comment period where interested parties have 14 days from the date that the request is posted to comment on the request. If a response is submitted within that time frame, the requester then has seven days to reply. As of 1 November 2018, there are 5,008 requests in this stage. During Stage 2 of the review process, the USTR determines whether the request meets the substantive criteria as set out in its Product Exclusion Notice. As of 1 November 2018, there are 1,756 requests in this stage. During Stage 3 of the review process, the USTR consults with CBP to determine whether the requested exclusion is administrable. As of 1 November 2018, only 238 requests have moved to this stage. The USTR has stated that it will publish exclusion requests that are granted on a rolling basis; although, as of 1 November 2018, no exclusions have been granted.

US List 2

Notably, the procedures for submitting an exclusion request for items covered on US List 2 were updated to include the following requirements:

> *"For imports sold as final products, requesters must provide the percentage of their total gross sales in 2017 that sales of the Chinese-origin product accounted for. For imports used in the production of final products, requesters must provide the percentage of the total cost of producing the final product(s) the Chinese-origin input accounts for and the percentage of their total gross sales in 2017 that sales of the final product(s) accounted for."*

The deadline for submitting product exclusion requests for items on US List 2 is 18 December 2018. As of 1 November 2018, 3,384 requests were filed, and, of these requests, 3,192 are currently in Stage 1 and 192 are in Stage 2.

US List 3

White House and USTR statements announcing the previous two rounds of Section 301 tariffs (US Lists 1 and 2) notably contained a promise to establish a product exclusion process, stating "USTR will publish a separate notice describing the product exclusion process, including the procedures for submitting exclusion requests, and an opportunity for interested persons to submit oppositions to a request." Similar language was conspicuously absent from announcements of US List 3, and neither the White House nor the USTR have communicated that a similar process will be established for items subject to US List 3.[35]

What to expect next?

The future of Sino-US trade relations remains unclear as President Donald Trump continues to threaten China with more tariffs. President Trump and China President Xi Jinping are scheduled to meet at the G20 summit in December. China has reportedly sent a written response to US demands in advance of the meeting, but President Trump commented on 16 November that the offer is "just not acceptable to me yet."

Actions for businesses

With a fourth wave of punitive US tariffs imminent, which is threatened to cover all remaining imports of China-origin goods not subject to Section 301 tariffs, and China countermeasures likely, importers should immediately analyze their existing US and China supply chains and evaluate proactive mitigation strategies.

[35] US List 3 FR Notice: https://www.gpo.gov/fdsys/pkg/FR-2018-09-21/pdf/2018-20610.pdf. White House announcement of US List 3: https://www.whitehouse.gov/briefings-statements/statement-from-the-president-4/.

In addition to mapping the company's end-to-end supply chain and determining plausible mitigation strategies as discussed in the September 2018 issue of TradeWatch, importers should consider how the recent HTSUS changes and CBP rulings on sets and NAFTA rules impact their options for relief from Section 301 duties.[36] In light of CBP's enhanced scrutiny of origin declarations, companies should carefully document their country of origin rationale, especially where importers plan to declare non-China country of origin for products partially manufactured in China or made from China-origin inputs. In certain circumstances, a CBP advance ruling on country of origin is recommended.

As the deadline for US List 1 product exclusion requests has expired, companies should continue to monitor USTR exclusion decisions, as they will be published on a rolling basis. Importers with products covered by US List 2 should also consider submitting product exclusion requests before the 18 December deadline.

Look for more insight into Section 301 developments in future issues of *TradeWatch*.

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[36] *TradeWatch* Volume 17, Issue 3 (September 2018), at https://www.ey.com/Publication/vwLUAssets/EY-tax-alert-2018-1974/$File/EY-tax-alert-2018-1974.pdf). Also, EY Indirect Tax Alert, "US announces tariffs on $200b China-origin goods; trade pressures to continue" (18 September 2018), at https://www.ey.com/gl/en/services/tax/international-tax/alert--us-announces-tariffs-on-200b-china-origin-goods---trade-pressures-to-continue.

Indonesia

Indonesia releases new regulations on import taxes

In September 2018, the Indonesian Government issued two new regulations on import taxes that increased the withholding tax rates on a range of goods and updated the regulations on importing goods through the postal service. The new regulations are intended to control the imports of consumer goods in an effort to reduce Indonesia's current account deficit, as the deficit has been considered a factor in the Indonesian rupiah's recent depreciation.

Further, the new regulations are aimed at protecting the national interest and encouraging domestic industrial growth.

This article summarizes key aspects of new regulations on import taxes.

Changes to Article 22 withholding tax for certain imported goods

On 5 September 2018, Indonesia's Minister of Finance (MoF) issued MoF Regulation No. 110/PMK.010/2018 (PMK-110) to increase the rate of the Article 22 withholding tax on the importation of certain goods or delivery of goods for other business activities. PMK-110 is effective for transactions occurring on or after 13 September 2018.

The Article 22 withholding tax is in the nature of a prepayment that can be credited against an importer's annual corporate income tax liability.

PMK-110 amends MoF Regulation No. 34/PMK.010/2017 (PMK-34), under which the Directorate General of Customs and Excise is responsible to collect Article 22 withholding tax upon the importation or exportation of the following goods:

Category	Importation of:	Tax rate
1	Certain consumer goods, including but not limited to: perfume, clothing, carpet, garments, shoes, statues, ceramic goods, glass products, gold and silver products, and consigned goods up to a certain amount, which are subject to a single import duty tariff according to the customs law, whether or not such goods are imported by using an Importer Identification Number (*Angka Pengenal Impor,* API)	10.0%
2	Other goods, such as electric household items, telephone equipment, monitors and projectors, motor cars and other motor vehicles, whether or not such goods are imported by using API	7.5%
3	Soybeans, wheat and wheat flour, if imported by using API	0.5%
4	Goods, other than goods stated under Categories 1, 2 and 3, if imported by using API	2.5%
5	Goods stated in Categories 3 and 4, if imported without using API	7.5%
6	Unclaimed goods that are auctioned	7.5%
	Exportation of:	
7	Certain coal, metal minerals and nonmetal minerals mining commodities	1.5%

PMK-110 reclassifies certain goods from Category 2 (7.5%) to Category 1 (10.0%). This reclassification affects more than 1,100 items of goods, ranging from consumer goods, personal care products and cosmetics, to luxury cars. Details are provided in the appendix of PMK-110.

Changes on the import provisions for consigned goods

On 6 September 2018, the MoF issued MoF Regulation No. 112/PMK.04/2018 (PMK-112), effective on 10 October 2018. PMK-112 amends MoF Regulation No. 182/PMK.04/2016 (PMK-182) that governs the import provisions on goods that are imported into Indonesia through a postal service in accordance with the postal laws and regulations.

PMK-112 is aimed at protecting the national interest, given the increase in the volume of imported goods through the postal service, as well as improving domestic industrial growth.

Under PMK-182, imported goods for consumption with a maximum customs value of free-on-board (FOB) USD100 for each shipment were exempt from import duty. PMK-112 decreases the maximum customs value for the exemption to FOB USD75 for each shipment per day or more than one shipment per day, provided that the total customs value of all shipments does not exceed FOB USD75. If the value exceeds the threshold, the shipment is subject to import duty and import taxes on the total customs value.

Where the threshold is exceeded, the customs and excise officer will officially assess the import duty and the customs value as follows:

1. The imported goods are subject to a 7.5% import duty.
2. The customs value is determined in accordance with the customs law and regulations.

PMK-112 also revises some definitions and limits concerning the importation of tobacco and alcohol products. PMK-182 is still applicable to provisions other than those specified in PMK-112.

Companies doing business in the Indonesian market need to assess the implications of these new regulations on their operations given the wide range of products and industry sectors that are affected.

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Taiwan

Taiwan issues draft amendment to FTZ exemption law

On 4 October 2018, Taiwan's Executive Yuan passed draft amendments (the amendments) to the Act for the Establishment and Management of Free Trade Zones (FTZs) (the Act). The action was taken in an attempt to comply with certain requirements made by the European Union (EU) during the peer review, improve international economic cooperation and reduce the tax burden for foreign companies operating in Taiwan. The Draft will be submitted to the Legislative Yuan for further review.

The Draft includes the following key measures:

- **Changing the taxation threshold in line with international tax practices:** Under the Act, foreign companies and their Taiwan branches are entitled to a corporate income tax (CIT) exemption on their sales from an FTZ if they only conduct "storage and simple processing" activities in the FTZ. Under the Draft, foreign companies performing "preparatory or auxiliary activities" are also eligible for the CIT exemption. The term "preparatory or auxiliary activities" refers to the Organisation for Economic Co-operation and Development's guidance provided in Base Erosion and Profit Shifting Action 7, determined on a case-by-case basis. For instance, if a foreign company in the manufacturing sector stores, displays and delivers its products from the FTZ to customers inside and outside Taiwan, its income deriving from the sales would be exempt. However, simple processing that is classified as tax-exempt activities under current law would be a taxable activity under the Draft. Labeling, packaging and classification activities are still treated as tax-exempt activities.
- **Expansion of the tax-exemption basis:** Currently, qualified foreign companies are partially CIT exempt for sales made to local customers and fully exempt from CIT for sales made to foreign customers. The Draft grants full exemption to qualified foreign companies for both domestic sales and export sales.
- **Transition rule:** The Act still applies to CIT-exempt applications submitted by the end of 2018, as the amendments become effective for CIT-exempt applications submitted on or after 1 January 2019.

The tax treatment for foreign companies engaged in taxable activities (e.g., simple processing) in the FTZ is governed by tax ruling No. 10600664060 issued in April 2018, which uses a formula method to determine the profits attributable to the taxable nexus.

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Thailand

Changes to BOI's procedures on raw materials imported under duty exemption privileges

On 3 September 2018, the Board of Investment (BOI) released BOI Notification No. Por.8/2561 related to procedures for utilizing duty exemption privileges under Section 36(1) of the BOI Act B.E.2520 (1977) for imported raw materials and essential materials that are used for manufacture for export. This new notification replaces BOI Notification No. Por.3/2556, dated 19 June B.E.2556 (2013), and BOI Notification No. Por.1/2557, dated 26 June B.E.2557 (2014).

Key changes

1) With immediate effect, a BOI-approved company is allowed to proceed with the stock cut process for raw materials and essential materials imported under the BOI duty exemption privileges through the Investor Club (IC) using past export declarations for finished goods that were exported at any time in the past. Previously, the stock cut process through the IC was permitted only for exports that had occurred during the past 12 months.

2) Effective from 1 March 2019, the following additional changes will apply:

   a) The approved "maximum stock" threshold of imported materials eligible for duty exemption privileges that is granted to a BOI-approved project will be reduced from six-months' volume to four-months' volume. This threshold is generally calculated based on each BOI-approved project's production volume of finished products, provided that this does not exceed the approved production capacity and is in accordance with the proportion of finished products specified as being for export.

   b) Application for an extension of the BOI duty exemption privilege for imported raw materials for a BOI-approved project is made annually. The applicant must complete the stock cut process through the IC for past export declarations made more than one year in advance (counting from the date of the application for the extension) within six months from the expiration date of the privilege.

Upon completion of the stock cut process with the IC, the BOI will consider the application for an extension. If the applicant is unable to complete its BOI stock cut for exports made more than 12 months before a date that is within six months from the expiration of the privileges, the BOI will not approve the application.

c) If no annual extension application is made for the duty exemption privileges of a BOI project after its expiration date, the privileges will be discontinued.

If the BOI-approved company wishes to subsequently apply for the duty exemption privileges, it must make a separate application for additional duty exemption privileges for imported raw materials to be used in the production of finished goods for export. If making such an application, the applicant must complete the stock cut process through the IC for export declarations made more than one year in advance of a date that is within six months from the date of the application. If the applicant fails to do so, the BOI will not approve the application.

Who does this impact?

Companies affected by these changes include:

- BOI-approved companies that export finished goods directly overseas and/or to Free Zones (FZs), I-EA-T Free Zones or Export Processing Zones (EPZs)
- BOI-approved companies that supply or deliver finished goods to other BOI-approved companies for subsequent indirect export overseas and/or to FZs, I-EA-T FZs or EPZs

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Bahrain

Bahrain releases VAT Law

On 9 October 2019, the Kingdom of Bahrain (Bahrain) released its Value Added Tax (VAT) Law under Royal Decree No. (48) of 2018 (the VAT Law). The VAT implementation date will be 1 January 2019.

Bahrain's VAT Law differs in key areas from corresponding legislation introduced in Saudi Arabia and the United Arab Emirates (UAE) in that it provides for more and broader zero rates and exemptions, with a view to balance a range of relatively unique socioeconomic objectives.

Background

In November 2016, the member states of the Gulf Cooperation Council (GCC) executed the Common VAT Agreement of the States of the GCC (the GCC VAT Agreement), outlining the framework that member states should follow when implementing their domestic VAT rules. Saudi Arabia and the UAE implemented their VAT systems on 1 January 2018.

Bahrain released the VAT Law on 9 October 2018 via the Official Gazette website. The Royal Decree states that VAT will be implemented on 1 January 2019. The Implementing Regulations (the Regulations) are expected to be published shortly.

Highlights of the VAT Law

Effective date of implementation – Article 4 of the Royal Decree states that the VAT Law will come into force on 1 January 2019.

Scope of VAT – In accordance with the GCC VAT Agreement, Article 2 of the VAT Law provides that the supply of all goods and services made in Bahrain, as well as imports, shall be subject to VAT.

Rates of VAT – Article 3 of the VAT Law provides for a standard rate of 5%, while certain goods and services may be subject to a zero rate or exempt from VAT.

Zero-rated supplies – Article 53 of the VAT Law sets out provisions where certain supplies and sectors are subject to the zero rate of VAT (subject to satisfying conditions and procedures that will be outlined in the Regulations). These include:

- Oil, oil derivatives and gas sector
- Supply and importation of foodstuffs (based on a list approved by the Financial and Economic Cooperation Committee)
- Local transport sector
- International transportation services and the supply of related means of transport
- Construction of new buildings
- Supply of educational services, as well as the related goods and services to nursery, preschool, primary, secondary and higher education

- Preventive and basic health care services, as well as related goods and services
- Supplies or imports of certain medicines and medical equipment
- Export of goods to outside of the implementing states
- Export of services to a customer residing outside of the implementing states
- Supply of goods under a customs duty suspension scheme
- The supply or importation of investment gold, silver and platinum with a purity level not less than 99%, which is tradeable on the Global Bullion Market (and subject to obtaining a certificate)
- The first supply of gold, silver and platinum after extraction for commercial purposes
- Supply and import of pearls and precious stones (subject to obtaining a certificate)

Exemptions — Articles 54 to 56 set out the scope of exemptions, which include:

- The supply of financial services, unless the payment is made by way of an explicit fee, commission or commercial discount (the rules and conditions with respect to these services will be outlined in the Regulations)
- Supply of vacant land and buildings by way of lease or sale (subject to further rules and conditions to be outlined in the Regulations)
- The importation of:
  - Goods where the supply of such goods in the final country of destination is exempt or zero rated
  - Goods that are exempt from customs duty in accordance with the terms and conditions set forth in the Common Customs Law, and that are as follows:
    - Diplomatic exemptions
    - Military exemptions
    - Used personal effects and household items transported by nationals living abroad on return and expatriates moving to live in Bahrain for the first time
  - Personal luggage and gifts carried by travelers
  - Necessities for people with special needs

Exemptions will be subject to satisfying conditions and procedures to be outlined in the Regulations.

Import VAT — Article 51 provides that import VAT should be paid to the customs authority, where Bahrain is the first point of entry. Tax authorities may allow the taxable person to defer the payment of VAT until the submission of the VAT returns.

Registration — Article 29 provides an overview of the persons required to be registered for VAT purposes.

The thresholds for registration are in line with the GCC VAT Agreement, which are as follows:

- Mandatory registration threshold – SAR375,000 (approximately BHD37,700) (approximately USD100,031).
- Voluntary registration threshold – SAR187,500 (approximately BHD18,850) (approximately USD50,016).
- Nonresident persons shall be required to register in Bahrain, regardless of the value of supplies, as long as they are obliged to pay the tax in Bahrain. Registration can be done directly or through a tax representative.
- Exception from registration – Article 32 outlines that a taxable person who has a mandatory registration requirement where all taxable supplies are zero rated may request an exception from having to register.

According to a recent announcement from the Ministry of Finance, a phased VAT implementation process will apply. The first phase for VAT implementation from 1 January 2019, will only apply to companies/persons that have annual turnover exceeding BHD5 million (approximately USD13.27 million).

Group registration – Article 30 allows two or more taxable legal persons, resident in Bahrain, to register as a VAT group upon application and approval (as per the Regulations).

Tax period – Article 35 provides that the Regulations will specify the duration of the tax period, which should not be less than one month.

Filing of the tax return – Article 36 provides that the deadline for filing the VAT return is the last day of the month following the month in which the tax period ends.

Tax invoices – Article 38 provides that the Regulations will determine the content and conditions relating to tax invoices.

Issuance of a tax invoice – Article 39 states that tax invoices should be issued within 15 days of the month following the date of the supply.

Penalties – The law outlines the penalties that may be imposed for noncompliance. These include penalties for failing to register for VAT (up to BHD10,000) (approximately USD26,533) and failing to provide the tax authority with information it requests (up to BHD5,000) (approximately USD13,267). Under Article 63, the following violations may be regarded as tax evasion and may result in imprisonment:

- Failure to register for VAT within 60 days of the registration deadline
- Failure to pay VAT within 60 days of the payment deadline
- Failure to provide a tax invoice
- Charging VAT on nontaxable items
- Unrightfully recovering input VAT

Transitional rules – Articles 75 to 79 set out the transitional provisions relating to supplies that span the implementation date. These include:

- Special time of supply (Article 75) – Should the supply take place after 1 January 2019, but the invoice is issued or payment is received before 1 January 2019, the time of supply will be the date when the supply is made and VAT should be due.
- Contracts silent on VAT (Article 76 (a)) – Where a contract has been signed prior to 1 January 2019 that relates to supplies provided partially or fully after 1 January 2019, the consideration for the supply would be treated as VAT inclusive (in case VAT is applicable). The Regulations will provide special provisions for such contracts.
- Government contracts silent on VAT (Article 76 (b)) – Under special conditions, supplies after 1 January 2019 under contracts signed with the government before 1 January 2019 should be zero rated until the earlier of the contract renewal date, contract expiration date or 31 December 2023.

- Intra-GCC supplies (Article 78) — Until the implementation of the Electronic Services System, supplies of goods that are transported from Bahrain to other GCC implementing states will be treated as an export of goods.
- Treatment of non-implementing states (Article 79) — Bahrain will not treat a GCC member state that has already implemented VAT as an implementing state where that member state does not treat Bahrain as an implementing state and does not fully comply with the GCC VAT Agreement.

The original law is published in Arabic. In case of a conflict between the original version (Arabic) and any translation, the Arabic version prevails.

Implications

The introduction of VAT in Bahrain will affect all economic sectors. Businesses may require considerable effort and action to update their people, processes, systems, contracts and stakeholders for VAT. For businesses accustomed to operating in a tax-free environment in Bahrain, VAT compliance requirements will require a fundamental change in many business practices.

An implementation date of 1 January 2019 for VAT does not leave much time for businesses to prepare. Some businesses may benefit from lessons learned during the recent implementation exercises in Saudi Arabia and the UAE. However, it is important for businesses to initiate their VAT preparations quickly to reduce the risk of noncompliance and penalties when the new rules are implemented.

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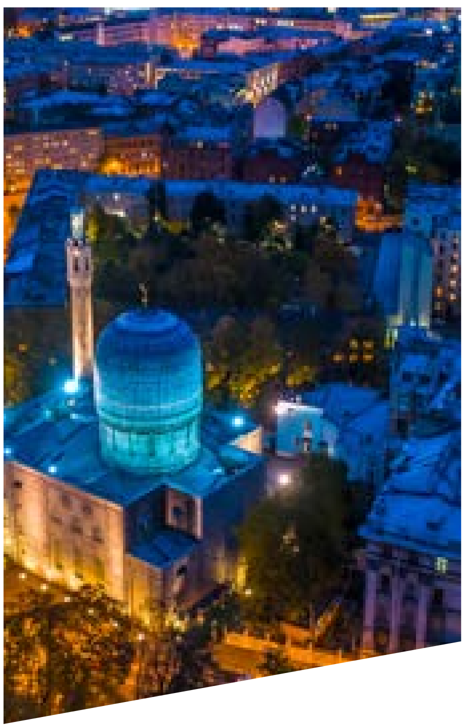
Saudi Arabia

Saudi Customs publishes information on its Authorized Economic Operator program



Saudi Arabia has developed an Authorized Economic Operator (AEO) program and published the requirements to join. Businesses achieving AEO status obtain various customs benefits, including dedicated fast lanes and priority treatment.

The accreditation process can be lengthy. Interested businesses should perform a thorough assessment of their customs and supply chain controls to ensure they meet AEO criteria before submitting an application.

Background

In June 2005, the World Customs Organization adopted the SAFE[37] Framework of Standards to Secure and Facilitate Global Trade to act as a deterrent to international terrorism, secure revenue collections and promote trade facilitation worldwide. One of the building blocks of this international framework is the AEO concept, where customs authorities can accredit businesses that have high-quality internal processes that prevent tampering with goods in international transport. AEO is aimed at various stakeholders involved in the international trade of goods, including importers, exporters, warehouse owners, clearing agents and logistic carriers.

AEO accreditation gives businesses an internationally recognized quality mark that indicates that their international supply chain is secure.

Saudi Arabia has developed its own AEO program, and Saudi Customs has published information on the requirements to join the program and the benefits that it can bring for businesses. Saudi Customs piloted the program with a limited number of large organizations in the country and has now opened up applications to the wider business community.

Requirements to become an AEO

Before granting a business with AEO status, Saudi Customs will carry out an in-depth analysis of the existing processes and controls relating to the international supply chain. As a minimum, the applicant should meet the following requirements:

- Three years of strong customs compliance and lack of criminal offenses
- The existence of a robust electronic record-keeping system
- Financial solvency for the parent company and subsidiaries
- The appointment of a responsible contact person with extensive corporate knowledge of customs-related matters

[37] SAFE stands for Security and Facilitation in a global Environment.

- A policy for security-focused training and awareness for staff
- Satisfactory procedures for verifying the accuracy of customs declarations and confidentiality
- The ability to demonstrate safety measures in regards to containers, transport, company premises, warehouses, facilities, and the security of staff and workers
- A process to check the adherence of business partners to security standards
- An efficient system of crisis management and incident recovery
- The ability to track key performance indicators to reduce risks and enhance security

Given the global profile of AEO status and the benefits it can bring, the criteria are set at a very high level. Even businesses experienced in customs practices should review the robustness of their processes and controls.

Advantages of AEO status

Achieving AEO status brings a host of benefits to businesses, including:

- A dedicated fast lane at all points of entry in Saudi Arabia
- Priority over non-AEO shipments in all customs procedures
- The possibility to clear goods prior to arrival/departure
- The possibility to have goods released before payment by using bank guarantees
- Reduced physical inspection of goods
- The possibility of physical inspections to be carried out at the warehouse or storage facilities of the AEO
- The potential to benefit from similar programs in countries with Mutual Recognition Agreements
- Use of the AEO logo in marketing materials
- A dedicated Saudi Customs account manager

Joining the program

The process to join the AEO program is as follows:

1. The business submits an application.
2. Saudi Customs assesses the application against the AEO criteria.
3. The business performs a self-assessment using a questionnaire.
4. Saudi Customs will assign a team to review the application and carry out necessary on-site checks.
5. AEO status is granted to an applicant that satisfies all program criteria.
6. Saudi Customs assigns to the AEO a dedicated account manager.

During the application process, Saudi Customs is likely to request process documents for review and carry out on-site audits to make sure the applicant's facilities meet the AEO criteria.

Implications

AEO accreditation can offer significant benefits to businesses in Saudi Arabia, including enhanced movement of goods and lower costs for international trade.

Interested businesses should perform a thorough assessment of their customs and supply chain controls to ensure they meet AEO criteria before submitting an application. Submitting an application before carrying out a current state assessment could lead to rejection by Saudi Customs and having to restart the process.

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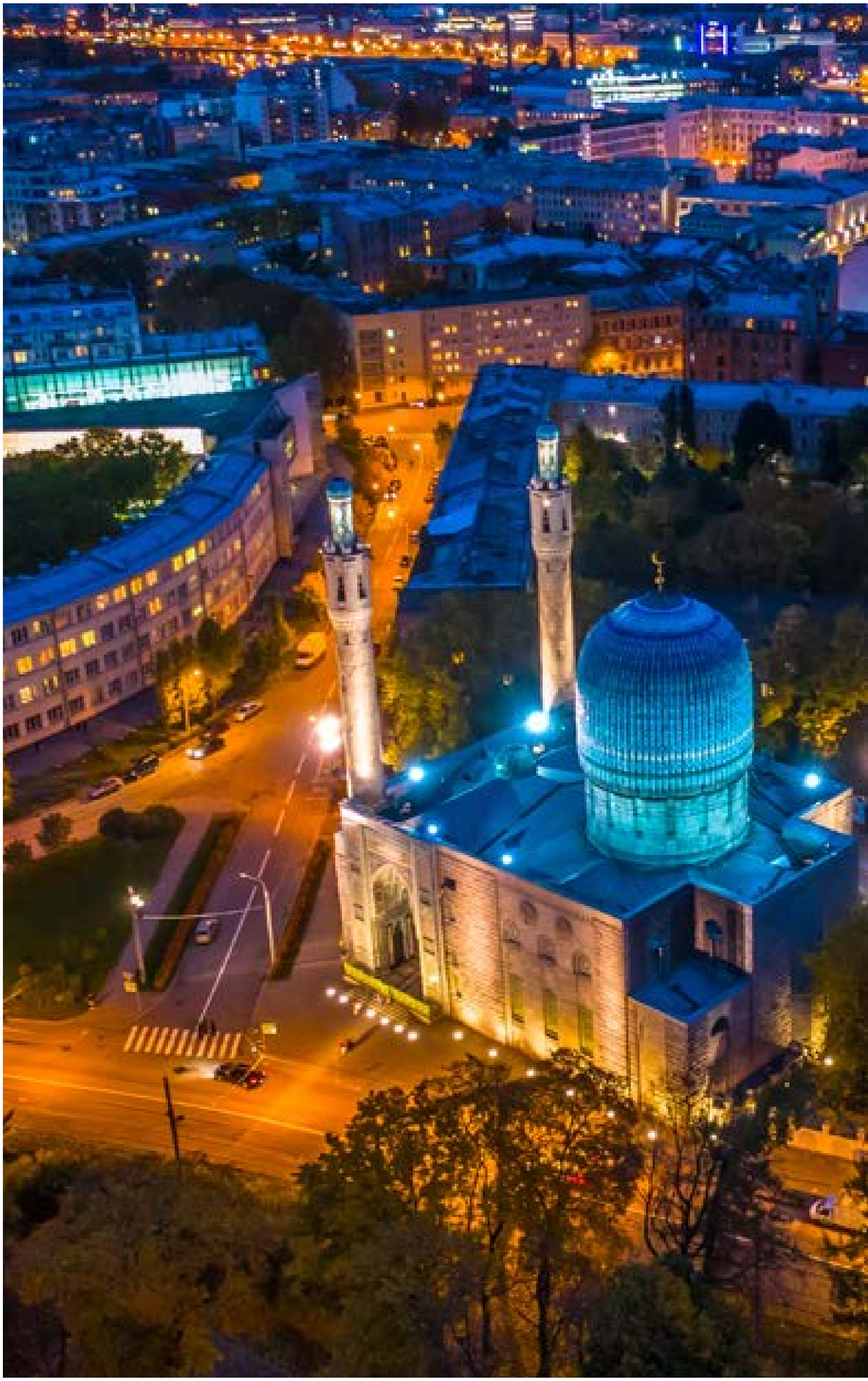
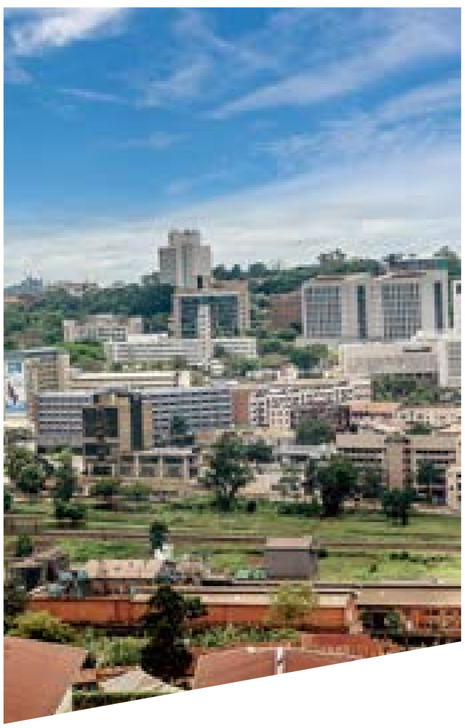


Uganda

Uganda implements new regulations on the importation of used motor vehicles



In a bid to improve compliance with existing international, regional and national commitments on environmental protection, as well as compliance with anti-dumping safeguards, the Government of Uganda has moved to implement stricter regulations on the importation of used motor vehicles that are 15 or more years old from the date of manufacture. These regulations allow only a few exceptions.

In addition, the government has instituted several rates of environmental levies for certain used motor vehicles. The environmental levy rates applicable to imported used motor vehicles that are at least five years old from the date of manufacture have been increased, ranging from 20% to 50% of the Cost, Insurance and Freight (CIF) value.

The registration fees for all motor vehicles imported into Uganda have been increased to either UGX1.5 million (approximately USD400) or UGX1.7 million (approximately USD455), depending on the type of motor vehicle.

The ban on most imported used motor vehicles

Before the Traffic and Road Safety (Amendment) Act 2018 introduced these changes, no restrictions existed on the importation of motor vehicles into Uganda. The law took effect on 1 July 2018; however, motor vehicles 15 years old or older that were in transit before the law's effective date and had arrived in Uganda by 30 September 2018 were excluded from the ban and allowed into the country.

The ban does not apply to certain other imported used motor vehicles. These include road tractors for semitrailers, motor vehicles for the transport of goods with a gross vehicle weight of at least six metric tons, agricultural or forestry tractors, earth-moving motor vehicles, tamping machines and road rollers.

Additionally, the ban on imported used motor vehicles does not apply to imported special-purpose motor vehicles, including breakdown lorries, crane lorries, firefighting vehicles, concrete mixer lorries, road sweeper lorries, spraying lorries, mobile workshops, forklifts, mobile drilling rigs, mobile radiological units, work trucks, tanks and other armored fighting vehicles, cesspool emptiers, water bowsers, bullion spreaders, bitumen spreaders, bucket trucks, aircraft refuelers, spraying trucks, workshop vans and mobile banks.

Revision of environment levy rates for imported used motor vehicles

The environmental levy imposed on imported used motor vehicles that are nine or more years old has been increased.

Imported motor vehicle	Environment levy
A motor vehicle that is five to eight years old from the date of manufacture, excluding goods vehicles	35% of the CIF value
A motor vehicle that is nine or more years old from the date of manufacture, imported or in transit before the commencement of the law, and that arrives in Uganda by 30 September 2018	50% of the CIF value
A motor vehicle that is nine or more years old and is principally designed to carry goods	20% of the CIF value

Previously, motor vehicles (excluding goods vehicles) that were between five to ten years old were subject to an environment levy of 35% of the CIF value. Motor vehicles (excluding goods vehicles) 10 or more years old were also subject to an environmental levy at different rates.

In the past, there was no environmental levy imposed on goods vehicles. Now, goods vehicles that are nine or more years old are subject to an environmental levy of 20% of the CIF value.

Registration fees

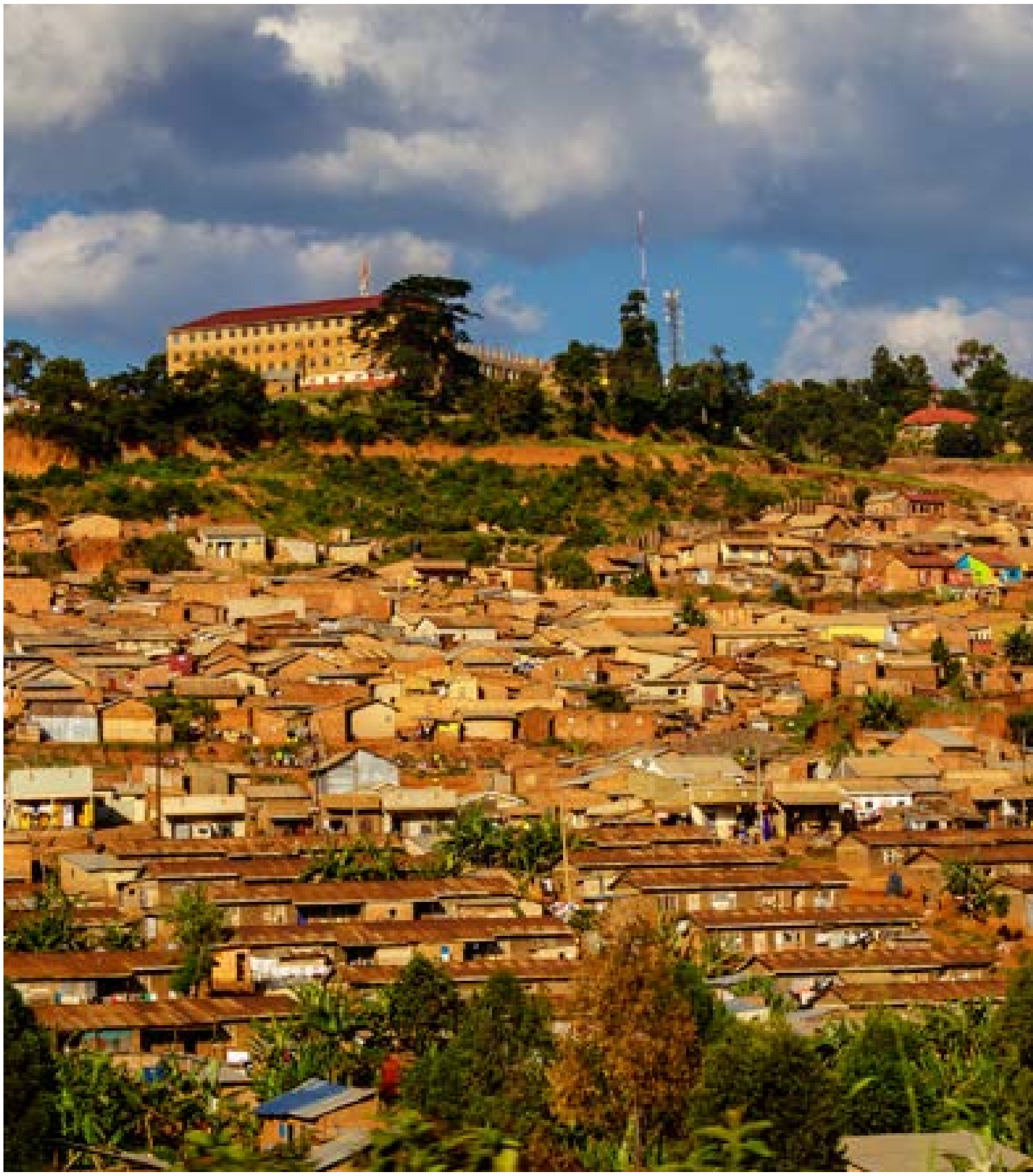
The revised registration fees for all imported motor vehicles have been increased, as reflected in the table below.

Imported motor vehicle	Old fees (UGX)	New fees (UGX)
Sedan cars, saloon cars, estate cars (excluding dual-purpose goods passenger vehicles)	1,200,000	1,500,000
Passenger vehicles, including light omnibuses with a seating capacity not exceeding 28 passengers	1,200,000	1,500,000
Estate and station wagon vehicles with an engine capacity of 3,500 cc or above	1,700,000	1,700,000
Medium omnibuses and heavy omnibuses with a seating capacity of more than 28 passengers	1,200,000	1,500,000

What to expect

Going forward, any person intending to import a secondhand motor vehicle into Uganda needs to be aware of the changes described above. Before negotiating and buying used vehicles from overseas, the buyer in Uganda should ascertain that the age of the motor vehicle is within the acceptable range (new to 15 years) unless exceptions from the ban apply. It is also important that any buyer or importer of any motor vehicles into Uganda is knowledgeable about the amounts of an environmental levy (if any) and the registration fees that will need to be paid upon importation together with the other applicable customs duties. Generally, the cost of acquiring an imported used vehicle in Uganda has increased, and most of the motor vehicles that are older than 15 years may no longer be imported into Uganda.

The customs authorities will rely on the mandatory Pre-Export Verification of Conformity (PVoC) to Standards Programme and other measures for exports to Uganda to ascertain that imported used cars conform to the new regulations.



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Ukraine

Recent amendments to single window and non-tariff regulations

Amendments to Ukraine's Customs Code[38] (the amendments) and other laws regarding state control on goods that cross the border came into force on 4 October 2018. These amendments are summarized below.

Single window portal

- The State Fiscal Service is responsible for implementing the single window web portal, which serves for obtaining permits and for the exchange of data between companies and state authorities. This web portal is expected to replace the existing single window system to which some state authorities are connected.
- The new single window will liaise businesses, customs and other state authorities that issue permits for goods moved across the border. The number of authorities connected to the single window system is expected to increase.
- The single window may be used to remit customs payments and other levies related to movement of goods control.
- Information will be exchanged solely electronically.

Amendments to non-tariff regulations

- The number of controls upon import of goods has been reduced to three: 1) phytosanitary control, 2) veterinary control and 3) control of food, feed, animal origin by-products and animal health.
- Radiological, environmental, and health and environmental controls that were previously enforced upon importation are no longer in effect.
- Official control measures under the amended regulations do not apply to the export of goods.
- The Border Guard controls radiation safety measures at checkpoints (in case of a natural radiation level increase).
- Health and environmental control is subject to legislation regulating market control and control over non-food items.
- Customs officials check whether importers have permits for pesticides, agro chemicals, waste, genetically modified organisms (GMOs), biological resources, and wild plants and animals.

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[38] The Law of Ukraine "On Amendments to Customs Code of Ukraine and Certain Laws of Ukraine regarding Implementation of "Single Window" System and Optimisation of Controlling Procedures during Movement of Goods Across Customs Border of Ukraine" No. 2530-VIII dated 6 September 2018.

Transitional provisions

The non-tariff regulation amendments establish the following transitional periods (from the date of entry into force):

- Three months — for updating the regulations in line with the amendments. During this time, the environmental inspection officials continue to perform radiation safety control of goods at checkpoints that are not equipped with automatic systems for radiation level measurement.
- Six months — for setup and launch of the single window web portal.

Other changes

The amendments have improved the inward processing customs procedure, including the use of this procedure during the importation of raw materials purchased by Ukrainian businesses for processing into finished goods.

Overall, the amendments should significantly facilitate cross-border trade and streamline state controls over goods moved across borders. Changes to inward processing create new opportunities for duty-free importation of goods into Ukraine for processing to be subsequently reexported as finished goods. Ukrainian companies need to assess the implications that these recent amendments may have on their operations.

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