TORRES LAW
INTERNATIONAL TRADE & NATIONAL SECURITY

Customs Guide for General Counsel, C-Executives, and Accounting Firms

Under U.S. law, the importer of record (IOR) is the person or company for whose account the importation is made. The IOR is responsible for Customs compliance, payment of duties, and compliance with all applicable laws and regulations. In cases where Customs violations are discovered, the IOR will be the party liable for additional duties and potential penalties. The agency that administers the Customs laws in the United States is U.S. Customs and Border Protection (CBP). This is the U.S. Government's second largest revenue generator (IRS being the largest one).

Why Care About Customs?

A proactive approach to compliance tends to provide significant duty savings as you will have aligned business strategy and Customs compliance to take advantage of duty preferential treatments available as well as other programs that can lead to increased efficiencies. And it also saves you potential costs associated with Customs audits and penalties.

Customs Penalties

When assessing penalties for Customs violations, CBP charges the violator with one of three levels of culpability (*i.e.*, negligence, gross negligence, or fraud). The amount of penalties assessed depends on what level of culpability is assigned to the violator. For a violation with loss of duty, fraud charges may result in a penalty five to eight times the duty loss; for gross negligence, the maximum statutory level is the lesser of the domestic value or four times the duty loss; and negligence, the maximum statutory level is the lesser of the domestic value or two times the duty loss.

For more details on Customs penalties, please visit Torres Law Insights-Import Violations: What You Need to Know about 19 USC 1592.

Routine Inquiries

Customs routinely issues CBP Form 28 (CF 28) Requests for Information to importers when there is insufficient information in the entry summary package to determine admissibility, appraised value, or classification of the imported merchandise. A CF 28 is not a voluntary request, an importer will have 30 days to provide a response.

For more information on CF 28s, please visit Torres Law Insights-Give CF28s the Proper Respect.

With or without first issuing a CF 28, Customs can also issue a CBP Form 29 (CF 29) Notice of Action, which can take the form of a Proposed Action or Notice of Action Taken, making a final determination as to the issue in question. Pursuant to Customs guidance, a CF 29 can constitute the notice of the commencement of an investigation, which would bar the filing of a prior disclosure.

Audits and Investigations

Conducted by Customs Regulatory Audit and Agency Advisory Services (RAAS), in recent years Customs has added more types of audits to its more traditional roster of audits. One of the best known and

entailed type of audit is known as a Focused Assessment which reviews procedures and controls at the company and proceeds to full audit-like reviews if controls are found to be inadequate. Recently Customs has introduced Quick Response Audits (which are more streamlined audits focusing to a single or a couple of areas (*e.g.*, classification and/or valuation). Another mechanism being utilized by Customs and which Customs indicates is not an audit (but depending on the findings could lead to an audit) is a Customs survey. An audit survey permits Customs to quickly assess import activities compliance levels without committing substantial time and resources required by a full audit. For more details on Customs audits, please visit our article *Customs Audits 101* at Torres Law Insights-Customs Audits 101.

Customs investigations are conducted by Special Agents of the Bureau of Immigration and Customs Enforcement, Homeland security Investigations, or CBP officials with appropriate authority. Typically, companies will receive a formal notice of investigation and depending on the results of the investigation civil or criminal penalties are possible.

What areas should you be mindful of?

Classification

All products imported into the United States must be classified under the Harmonized Tariff Schedule of the United States (HTSUS). The HTS is an internationally recognized standardized system of classifications up to the 6-digit level and individual countries and add further specifications up to 8 or 10 digits. The HTS review is complex and technical and extremely important as each tariff classification provides for applicable duty rates, special program eligibility, review by other government agencies, and collection of trade statistics.

Valuation

The appraisement of imported goods is important for the proposer assessment of Customs duties and fees and maintaining accurate trade statistics. Importantly, the appraised value for customs purposes can be, and often is, different from the actual amount paid for merchandise. There are various methods that Customs allows when determining the value of the imported merchandise and Transaction Value is the preferred method (e.g., invoice price) but it requires a bona-fide arm's length sale for export. If Transaction Value is not permitted for the particular transaction, then there are other methods that can be evaluated in order of preference such as Deductive Value starting with U.S. wholesale price, with deductions taken; Computed Value, computed by compiling costs of materials, labor, overhead, and profit; and Fallback Method, obtained by making a reasonable modification or combination of the above described methods.

If using Transaction Value, there are certain additions to the price paid or payable (which in our experience are often overlooked) such as packing costs, selling commissions, assists (*e.g.*, tooling, dies, molds, etc. provided free of charge to the seller), royalties or license fees, and proceeds of any subsequent resale or disposition of the item that accrue to the seller. On the other hand, international freight and insurance and costs for technical assistance or transport after importation are not required to be added to the price paid or payable.

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Valuation is one of the most challenging areas and if your company has not had a recent audit reviewing your valuation practices, for Customs law purposes, it would be imperative that you review your current practices as most companies fall short of compliance in this area.

Other common valuation risk areas include importation of items that were not sold such as samples, repairs, and intra-company transfers of materials and equipment, or related parties and IRS Transfer Pricing Agreements.

Origin and Marking

With some of the recent developments on tariffs assessed on certain countries, it has become ever more important for companies to revisit the country of origin of their products to ensure that they meet adequate Customs laws and standards. Ascertaining the correct country of origin of your goods is important because it will affect the product's admissibility into the United States (*e.g.*, tariffs, embargoes, quotas) and it can also have an impact on duties and fees applicable to the imported article (*e.g.*, preferential trade programs, ADD/CVD). The country of origin determination will also inform customers in the United States where the product is from. Because of globalization, determining the country of origin of goods for which certain assemblies and components are manufactured in multiple countries and incorporating components from multiple countries of origin is not an easy task.

If an article has material or processing from more than one country, the country of origin is where the article last underwent a Substantial Transformation. Although in some ways subjective, Substantial Transformation is understood to be a manufacturing process that results in the article have a new name, character, or use. To determine whether Substantial Transformation applies to the manufacture of a particular product requires an in-depth analysis of your supply chain, components and parts, and the complexity of the manufacture and operations undertaken.

Best Practices

Depending on the nature and size of your organization, you must ensure you allocate adequate resources to the Customs compliance function. Note that relying on the Company's customs broker is not enough. The IOR is legally responsible for Customs violations.

The first step to ensuring compliance is developing, implementing, and maintain a strong import compliance program inclusive of written import manual with desktop level instructions, personnel training, broker oversight, HTSUS classification database, valuation reviews and audits.

Compliance and Enforcement

As discussed, TFTEA has led to increased CBP enforcement efforts on a variety of fronts, including more aggressive enforcement of antidumping and countervailing duty (AD/CVD) orders; forced labor import prohibitions; and intellectual property rights of rightful owners.

Enforcement Trends

Per CBP's trade and travel report, for the fiscal year (FY) 2019, the agency collected about approximately $80.7 billion in duties, taxes, and other fees, including $71.9 billion in duties, an increase of nearly 73% over the FY2018's duty collections. The agency states that much of the increase in duty collections is attributed to the ongoing assessment and collection of duties on steel, aluminum, washing

machines, washing machine parts, solar panels, and goods from China. These duties as well as certain quotas on steel and aluminum imports were ordered by the President during FY2018, pursuant to Sections 201 and 301 of the Trade Act of 1974 and Section 232 of the Trade Expansion Act of 1962. Furthermore, CBP assessed nearly $716 million in Section 201 duties, more than $1.1 billion in Section 232 aluminum duties, nearly $4 billion in Section 232 steel duties, and more than $29 billion in Section 301 tariffs on goods from China.

AD/CVD Enforcement

For the FY 2019, CBP began enforcing 33 new AD/CVD orders, resulting in 503 AC/CVD orders in effect and $19 billion of the imported goods were subject to those orders. Overall, the agency collected approximately $1.9 billion in AD/CVD deposits. The AD/CVD enforcement actions included CBP: 1) levied over $80.5 million in monetary penalties on importers for fraud, gross negligence, and negligence for AD/CVD violations; 2) conducted entry summary reviews that resulted in recovery of over $121.8 million in AD/CVD duties owed (nearly an 86% increase over the revenue recovered in FY2018); 3) audits identified approximately $20.4 million in AD/CVD duties owed (with $4.8 million collected to date); and 4) seized shipments with a domestic value of more than $131,000 for AD/CVD violations.

Lastly, CBP reported an increase in activity under the Enforce and Protect Act (EAPA) to combat duty evasion. CBP received 38 new allegations under EAPA from interested parties (slight increase from the 33 allegations in FY2018), and took interim measures in 31 EAPA investigations, a significant increase from the six EAPA investigations in FY2018. Additionally, the agency issued final determinations for seven investigations in FY2019. CBP's activities under the EAPA have also increased, such that CBP: initiated 36 EAPA investigations; and conducted 21 foreign onsite visits or verifications in Thailand, Vietnam, Malaysia, and the Philippines.

Trade Enforcement Activities

Based on CBP's trade enforcement activities published on its website, there was a rise in FY2019, compared to the previous year. CBP completed 391 audits and collected $43.1 million from importer audits, very similar numbers as in FY2018 (435 audits and $42.2 million). Additionally, CBP collected $30.1 million in trade-related penalties and liquidated damages, approximately double the amount collected in FY2018, a total of $15.5 million. For FY2019, there were a total of 65,509 trade seizures, including intellectual property rights, import safety, and other trade violation seizures. The trade seizures in FY2019, increased by over 12,000 seizures from FY2018's 50,952 total trade seizures.

Prior Disclosures

If an importer discovers Customs violations, it has the option to preparing and filing a prior disclosure seeking mitigation of penalties for the disclosed issues. A valid prior disclosure discloses errors (e.g., undervaluation, classification, etc.) prior to the commencement of a formal investigation by Customs. A valid prior disclosure also includes the tender of any loss duty to Customs. Prior disclosures are voluntary (not required by law) and an importer should carefully assess its particular facts and circumstances in deciding whether to disclose. The biggest benefit is avoidance of Customs fines and penalties and peace of mind. For more details regarding the complex process of a prior disclosure, please visit Torres Law Insights-Should I File a Customs Prior Disclosure?.

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Recent Developments

Section 301 Tariffs on China

On June 15, 2018, the United States Trade Representative announced the imposition of an additional 25% tariffs on imports of $50 million of certain Chinese-origin goods pursuant to Section 301 of the Trade Act of 1974, which authorizes the President to take action to obtain the removal of any act, policy, or practice of a foreign government that violates an international trade agreement or is unjustified, unreasonable, or discriminatory, and that burdens or restricts U.S. commerce. Since then, the USTR has imposed tariffs of various levels on $370 million in Chinese goods, in four different tariff lists:

- 25% Tariff on $34 Billion in Chinese Goods ("List 1");
- 25% Tariff on $16 Billion in Chinese Goods ("List 2");
- 25% Tariff on $200 Billion in Chinese Goods ("List 3"); and
- 7.5% Tariff on $120 Billion in Chinese Goods ("List 4A")

Impacted parties were able to request exclusions from the Section 301 tariffs for particular products after imposition, but the deadline to request these exclusions has closed for all four lists.

Section 232 Tariffs on Steel and Aluminum

On March 23, 2018, the Trump Administration implemented tariffs of 25% on imports of certain steel products and 10% on imports of certain aluminum products, as well as quotas on some countries for imports of steel and aluminum products. These Safeguard duties and Safeguard quotas were recommended pursuant to an investigation by the Department of Commerce (DOC) and are authorized by Section 232 of the Trade Expansion Act of 1962, which allows for such measures against products that threaten to impair the national security of the United States.

The 25% tariff on steel products applies to all countries of origin except Argentina, Australia, Brazil, Canada, Mexico, and South Korea. However, Argentina, Brazil, and South Korea are subject to absolute quotas. The 10% tariff on aluminum products applies to all countries of origin except Argentina, Australia, Canada, and Mexico. However, Argentina is subject to an absolute quota.

Individuals or organizations operating in the United States that use the steel or aluminum products subject to the Section 232 tariffs are eligible to apply for an exclusion from the tariffs. These exclusion requests are accepted and reviewed by DOC on a rolling basis. DOC is authorized to grant exclusions in cases where a steel or aluminum article is not produced in the United States in a sufficient quantity or of satisfactory quality, or if the steel or aluminum article should be excluded from the duties based on national security considerations.

USMCA

The United States, Mexico, and Canada ratified the new USMCA trade agreement in 2020. Notable changes include strict country of origin rules in various sectors or industries such as the automotive and textile industries. Other important chapters include IP rights, labor rights, digital trade, and environment to name a few. The agreement will be effective starting July 1, 2020. Companies must ensure compliance with the new agreement provisions to enjoy duty-free treatment for their products.