2023 YEAR–END TAX PLANNING GUIDE FOR BUSINESSES

Customs & International Trade

FustCharles

INTRODUCTION

FustCharles has had a very eventful 2023. We moved our headquarters from Widewaters Parkway to Merchants Commons in downtown Syracuse, embarked on a major rebranding, and opened a second location in Rochester. It's been an exceptional year and we're excited to continue our commitment to talent development, innovation and teamwork to provide our clients with a best-in-class service experience.

As of the date of this publication, 2023 has been a relatively quiet year in tax legislation. The IRS has been busy issuing guidance for both the 2022 tax legislative changes and pieces of the Tax Cuts & Jobs Act (TCJA). Given the upcoming US presidential election, there may be continued stalemate in Congress or the potential for more robust legislative changes – only time will tell.

FustCharles Tax professionals grasp the intricate connections between evolving laws, economic dynamics, and the tax implications of various business decisions and are well-positioned to serve as strategic advisors, steering companies toward success. Tax planning remains a vital aspect for businesses seeking to optimize cash flow by managing their long-term tax obligations. Our 2023 Year-End Tax Guide delves into effective tax strategies, taking into account recent administrative guidance and potential legislative changes that are currently under review. For further information and assistance, please reach out to a member of our expert tax team.

Unless explicitly stated otherwise, the information provided in this guide is based on existing tax laws and policies as of the publication date, and it may be subject to adjustments in response to future legislative or tax policy changes.

Customs & International Trade

As 2023 comes to a close, companies that import tangible merchandise into the U.S. should consider three topics: the Section 301 China tariffs, the Uyghur Forced Labor Prevention Act (UFLPA) and the country of origin rules. These measures can have a significant financial impact on businesses' profitability given that customs duties are "above the line," i.e., they are always cash. In addition, supply chain disruption and even closure can result from failure to comply with UFLPA. [1]

Section 301: Product Exclusions and Sunset Review

In 2018, the U.S. government implemented additional tariffs on Chinese goods under Section 301 of the Tariff Act of 1930 in four separate "tranches" (lists) of products. The tariffs are triggered by the tariff classification code and are imposed in addition to the general *ad valorem* duty rates (and other U.S. trade remedies, e.g., Section 232 tariffs, antidumping and countervailing duties). Goods of Chinese origin are subject to an additional 25% or 7.5% duty, depending on the product list they fall under.

In addition, the United States Trade Representative (USTR) is obligated to conduct a "sunset review" every four years to evaluate whether the Section 301 tariffs (1) are effective in accomplishing their intended purpose and (2) have any adverse effect on the U.S. economy. Earlier this year, USTR allowed importers to submit comments on the effect of the tariffs on their businesses and whether Section 301 should continue at current rates, be modified or be eliminated. USTR is expected to announce the results of its review in the near future but there is no statutory deadline for USTR to submit its recommendations to the President.

While these tariffs continue to remain in effect, the USTR has granted ongoing exclusions from Section 301 for 352 products. Merchandise may qualify for a product exclusion if its applied tariff code and specifications match one of the 352 descriptions. These exclusions had been previously set to expire several times, but have been extended by USTR, most recently until December 31, 2023. Importers of Chinese-origin goods should review the list of extended product exclusions and assess the applicability to their merchandise.

Pending future actions, importers should be taking steps to address ways to legally lower the customs value of merchandise imported from China to correspondingly lower their duty spend – or to "tariff engineer" their products into a new tariff code that does not attract the Section 301 duties.

Uyghur Forced Labor Prevention Act

ESG has become an issue for executives in the C-suite. Of all the proposed laws in the ESG world, only one has become federal law in the U.S.: the UFLPA, which became effective on June 21, 2022, and prohibits the importation of any merchandise made in whole or in part with forced labor, specifically targeting the Xinjiang Uyghur Autonomous Region (XUAR) of China. Importers are now required to "prove the negative." Thus, if goods are withheld, importers must document that the goods were not

[1] FustCharles partners with BDO to provide Customs & Trade Services.

made with forced labor for the withheld merchandise to be released and imported into the U.S. If the importers are unsuccessful, the goods must be re-exported or may be seized by Customs and Border Protection (CBP). Accordingly, potentially affected importers should consider taking steps to avoid the potentially devastating impacts of noncompliance with the UFLPA, e.g., loss of merchandise value, reputational harm and supply chain disruption.

This law continues to remain relevant as the U.S. government has pushed for even stronger measures against China and the use of forced labor in 2023 via legislation and sanctions against complicit companies. As of October 5, 2023, CBP has examined over 5,300 entries (shipments) valued at roughly $1.81 billion for compliance with UFLPA and held hundreds of meetings with importers to clarify the adjudication process. The electronics industry was by far subject to the most detentions, likely because electronics contain microchips made with polysilicon and the XUAR is the world's largest source of this substance. The electronics industry was followed by the industrial/manufacturing materials and apparel/clothing industries. While China is the main focus of the UFLPA, it is also notable that the majority of denied shipments in terms of value comes from Malaysia ($1.1 billion), followed by Vietnam ($429 million), indicating that importations from other countries are also at risk because finished goods produced there use XUAR-originating inputs.

Companies should be proactively taking steps to map their supply chains to verify that:

- No party on the UFLPA Entity List is a party to their transactions;
- None of their direct suppliers or their suppliers' suppliers, etc. use forced labor anywhere in the supply chain in producing any raw material or finished good; and
- Evidence is available of on-site factory visits to substantiate the absence of forced labor conditions and the existence of documentation confirming the origin of all raw materials and the finished good.

Additionally, mapping and documenting the supply chain may help uncover overlooked efficiencies in current sourcing arrangements and provide additional duty-saving opportunities through country of origin/free trade agreement qualification.

Country of Origin

Country of origin typically is relevant for ascertaining whether goods are eligible to claim preferential treatment under a free trade agreement or otherwise are subject to the Normal Trade Relations duty rate and other special tariffs, such as the Section 301 tariffs. Since the advent of the Section 301 China tariffs, country of origin has vexed importers because CBP's application of the traditional "substantial transformation" rule has not been consistent, in part due to CBP's reliance on a troublesome 2016 decision by the U.S. Court of International Trade (CIT), which has now been modified in part.

Substantial transformation refers to a manufacturing process that results in a product with a new name, character and use and renders the country of origin for the good. However, in 2016, the CIT issued a decision in the Energizer Battery v. United States case in which it rejected the traditional substantial transformation standard in favor of a "predetermined-end use" of foreign components standard, under which there is no change in use if the end use of imported merchandise was pre-determined at the time of import. CBP has used that standard since 2016.

In February 2023, the CIT issued another decision interpreting the substantial transformation analysis. At issue in Cyber Power Systems was whether the importer could demonstrate that parts originally manufactured in China underwent sufficient changes in its Philippines factory so that they would be considered "substantially transformed" for country of origin purposes to avoid the application of the Section 301 China tariffs. The CIT rejected the methods of analysis used in Energizer Battery, concluding that the approach adopted in 2016 was unworkable and instead focused on a comparison of all the parts and the finished product, not just the parts before and after assembly. The CIT reemphasized that application of the country of origin rule is based on the facts and circumstances of each case and concluded that CBP should focus on whether the *finished product* has a new name, character and use rather than the *parts* from which the finished good was made.

In light of the CIT's decision on the substantial transformation analysis for determining the country of origin, importers may wish to consider requesting a ruling from CBP or reconsideration of prior CBP rulings that were based on now-challenged methods of analysis. This may be particularly relevant for importers that purchase goods from suppliers that source components from China but conduct additional processing in a third country to avoid the Section 301 China tariffs.

Proactive tax planning and seamless tax compliance are essential components of financial success. At FustCharles, we are dedicated to providing year-round support, ensuring you stay informed about emerging opportunities, evolving tax laws, and optimal strategies. Our commitment is to guide you towards the most advantageous course of action aligned with your objectives, ultimately contributing to your business's financial well-being.

For more information, please reach out to our Tax Team Leaders:

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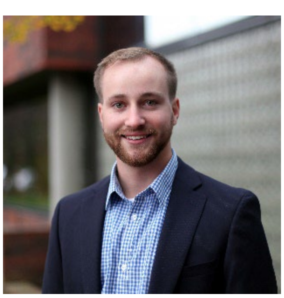

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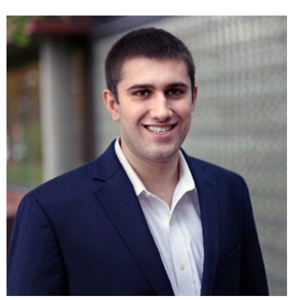

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