TradeWatch

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EY Global Trade

Quarterly update

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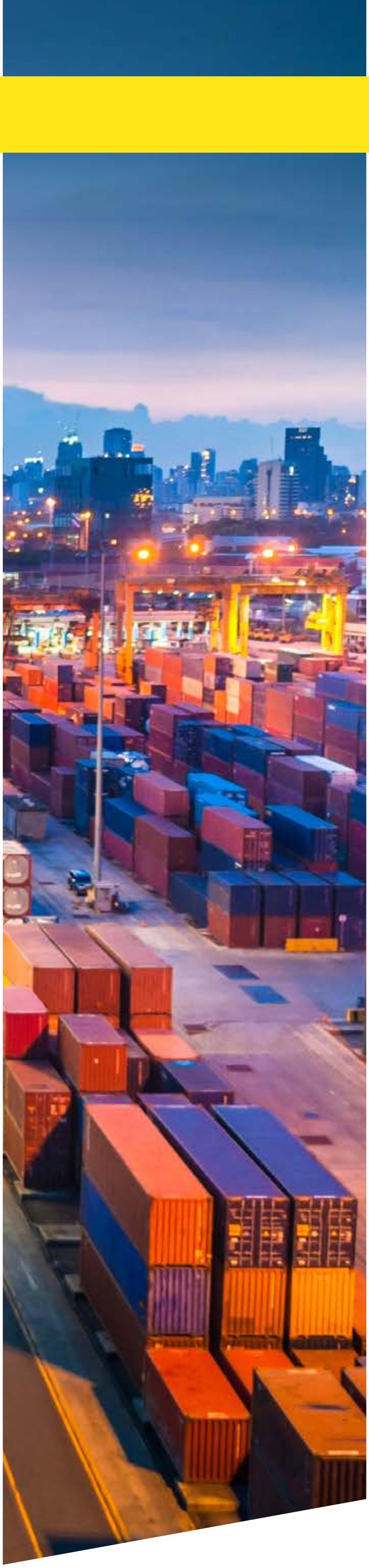

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The UK vote to leave the European Union: implications for multinational companies

The decision by the voters of the United Kingdom to leave the European Union (commonly referred to as Brexit) marks a significant change for both the UK and the EU and will impact other trading partners. However, as the European Council President has confirmed, all EU directives and regulations, as well as the treaties themselves, remain in force in respect of the UK until it formally leaves the EU. Therefore, on a regulatory level, nothing has changed and no changes are expected for the foreseeable future.

Following the Brexit vote, British Prime Minister David Cameron resigned on 13 July 2016. He was replaced by Teresa May, under whose leadership negotiations for the UK's exit from the EU will commence through the activation of Article 50 of the Lisbon treaty.

Under Article 50, a country has two years from the date of activation to negotiate and agree on its exit arrangements before it formally leaves the EU. At this time, no date has been set to activate Article 50, with recent indications that this is not likely to take place until 2017 at the earliest. It is anticipated that the UK will wish to ensure tariff-free trading arrangements as far as possible, but that discussions with the EU may be complicated by the principle of free movement of people.

Current customs benefits of membership of the EU

As a member of the EU, the UK is part of a single market, giving it tariff-free access to markets in other EU countries and EU Free Trade Agreements (FTAs). As a member of the EU Single Market, the UK also applies the Common Customs Tariff. Therefore, in leaving the EU the UK will not only have to renegotiate access to both European and international markets, but it will also have to introduce new legislation for a domestic tariff system.

Possible future UK trade relations with EU

At this stage, it is not known what form the UK's relationship with the EU will take post-Brexit. It is almost certain, however, that shipments between the UK and EU countries would be subject to customs declarations and possibly tariffs. Various potential post-Brexit trade models have been identified. These range from an EU Special Status model that would aim to mirror as closely as possible the current UK membership of the EU, to a World Trade Organization (WTO) most favored nation (MFN) model.

In between these two ends of the spectrum, the UK's future relationship with the EU could be similar to Norway's and Switzerland's current relationship with the EU, whereby those two countries, while not benefiting from full membership of the EU, do have tariff-free access for the majority of their goods.

Possible future UK trade relations with the rest of the world

As is the case with the UK's future relationship with the EU, its trade relationship with the rest of the world is also unclear at this stage. It is, however, almost certain that the UK will no longer be a party to the current EU FTAs. As such, it will need to renegotiate these within the framework of the WTO rules on bilateral trade agreements. While this is certain to be a lengthy process, it will also allow the UK a previously unknown degree of freedom in its negotiations. Where as a member of the EU, all trade negotiations were handled centrally, post-Brexit the UK would be free to choose its own trading partners and make its own agreements.

Value-added tax

It is likely that the UK will largely retain the current system of value-added tax (VAT) on leaving. However, taxpayers would no longer have a right of appeal to the European Court, and the UK Government would have additional flexibility on setting the rates and scope of VAT as the VAT system moves away from the EU directives on which it is based.

This will provide the opportunity for lobbying for existing VAT treatments to continue or change, but also gives the UK Government the opportunity to change VAT legislation it no longer wishes to follow, whereas European Court rulings relating to VAT refunds and interest may be reversed. Any changes, however, would be prospective rather than retrospective.

For VAT purposes, trade between the UK and non-EU jurisdictions is unlikely to change. In fact, trade between the UK and current EU Member States is likely to take a similar VAT model to that for current UK-US transactions. However, businesses with UK or EU operations will need to review the VAT implications and pay close attention to the Brexit developments to ensure they can adapt to any changes, in particular:

- Review current supply chains against potential Brexit trade options
- Maximize current reliefs
- Understand potential systems changes
- Model cash flow and cash funding requirements
- Factor in indirect taxes into any business transformation

What can companies do now?

It is apparent that the UK's exit from the EU will not be occurring in the immediate future and, at the moment, there is a degree of uncertainty as to what a post-Brexit trade landscape will look like. Nevertheless, companies should be using this intervening period to assess the implications and ensure they can effectively manage the transition.

In particular, as companies prepare for the UK's departure from the EU, it is important that they consider the various tax and trade implications, including the following:

- Immediate foreign currency, liquidity and trade impacts that have already and/or will occur
- Dividend and interest flows and associated withholding tax costs that would result from the UK being outside the EU and the related impact on group structure
- Supply chains and how EU trade flows and tariffs may affect costs
- Tax impact of any restructuring and relocation
- Issues relating to the cross-border movement of staff

Look for further insight into the forthcoming Brexit developments in future issues of *TradeWatch*.

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The UK vote to leave the European Union: implications for the GCC

There is little doubt over the influence of the UK's impending exit from the EU (Brexit) on the global market. The plummeting value of the pound sterling as well as the downgrading of the UK's credit ratings are telltale signs of the adverse impact Brexit has had on the British and the global economy. However, from the Gulf Cooperation Council (GCC: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates) countries' perspective, Brexit may present itself as an opportunity.

The UK has historically been a major foreign presence in the region since the early 1800s, when the British imposed the General Treaty of 1820 on local rulers to protect British trade that had started with the presence of the British East India Company in the Gulf in the 1770s. Since then, the British influence continued for a period of about 150 years, during which a number of tie-strengthening treaties were signed, oil was discovered, and British oil companies were set up in the region.

After the UK joined the EU in 1973, however, its influence over the Gulf gradually waned. Currently, no free trade agreements (FTAs) exist between the EU and the GCC despite ongoing talks since 1988. Additionally, the UK's trade, investments and military initiatives with the region (Gulf Initiative and Gulf Strategy, introduced in 2010 and 2015, respectively) that were intended to strengthen the UK's relationship with the region have been neither actively carried out nor discussed.

However, Brexit may be able to put the UK's Gulf initiatives back onto its main agenda as the UK will have to come up with an action plan to address its trade needs post-Brexit. Combined with the uncertainty over what its trading structure or arrangement with the EU will be, as well as the freedom to enter into FTAs with countries that were unable to reach one with the EU, the UK is likely to be propelled to seek out trade agreement negotiations. The GCC could potentially be on the top of the list given the historical ties.

Aside from the apparent trade deal benefits, Brexit could also be an important opportunity for GCC-based sovereign wealth funds to acquire British assets considering that the value of the pound sterling has decreased by almost 30% since the announcement of the referendum result and the likelihood of some volatility for the foreseeable future.

In addition, the UK may introduce a lower corporation tax rate to attract foreign investment and to minimize the outflow of businesses wishing to relocate to an EU alternative to the UK. As such, with these elements working together, GCC-based entities and sovereign wealth funds may be able to tap into the British market for an unprecedentedly low price.

Although there are some concerns over the UK's political roles in the Middle East, Brexit can potentially open up interesting trade and investment opportunities that can reconnect the broken links between the UK and the GCC.

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WTO Information Technology Agreement expansion: tariff reductions begin

The long-awaited first-round tariff reductions from the expanded World Trade Organization (WTO) Information Technology Agreement (ITA) are now in effect. Despite rapid innovation in information technology products and worldwide growth of the industry, the ITA's list of covered products had not been updated since 1997. Finally, in July 2015, WTO members agreed to expand the ITA, which provides for the elimination or reduction of duties on certain information technology products to cover an additional 201 products. Products in the expansion include, among other items, certain touch screens, new-generation semiconductors, global positioning system (GPS) navigation systems, tools used in the manufacturing of printed circuits, telecommunication satellites and medical equipment.

ITA signatories have each negotiated their own tariff reduction schedules for the additional covered products. All customs duties on these products will be eliminated by 1 July 2019 with interim reduction deadlines of 1 July 2016, 1 July 2017 and 1 July 2018. With the implementation of the ITA duty reduction schedules, customs duties on approximately 65% of the additional covered products are eliminated as of 1 July 2016. The rest of the duties will be variably reduced and eliminated over the next three years according to each signatory's schedule.

The ITA expansion provides apparent benefits to companies in the information technology sector in the form of eliminated duties. The duty elimination, however, also provides benefits in the form of reduced compliance costs and burdens to companies currently claiming preferential treatment of information technology products covered under various free trade agreements. As these products will eventually be unconditionally duty-free based on the Harmonized Tariff Schedule (HTS) alone, companies importing these goods will no longer need to claim preferential treatment to receive duty benefits.

Look for updates in future issues of *TradeWatch*.

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Highlights of the Canada–Ukraine Free Trade Agreement

On 11 July 2016, Canada and Ukraine signed the Canada-Ukraine Free Trade Agreement (CUFTA), Ukraine's first bilateral agreement with a North American trade partner.[1] Although no target date has been published, a smooth and swift ratification process can be expected.

Negotiated outcomes and commitments

As befits any free trade agreement, Canada and Ukraine have agreed to virtually eliminate all import duties on goods originating in these countries. Duties will be eliminated or reduced either immediately, or according to the agreed-upon staging lists, over a period of up to seven years. Ukraine and Canada may, however, continue to apply export duties, agricultural tariff-rate-quota duties, and special trade measures such as anti-dumping and countervailing duties, in accordance with their respective WTO commitments.

The CUFTA is a trade in goods agreement, and its scope does not cover international trade in services or international investment flows. The CUFTA does, however, contain commitments related to trade facilitation to reduce red tape and to facilitate trade in the digital economy. The CUFTA chapter on electric commerce obliges Canada and Ukraine to not levy customs duties or other charges on electronically transmitted digital products.

Lastly, Canada and Ukraine have engaged to undertake customs cooperation initiatives to promote automated border procedures to expedite the release of goods, and to establish a fair bilateral system for addressing complaints regarding customs rulings and decisions. These provisions aim to make business in the Canadian and Ukrainian markets fair and predictable for foreign-based companies seeking to benefit from the agreement.

[1] Ukraine currently has free trade agreements with the European Free Trade Association (EFTA: Iceland, Liechtenstein, Norway and Switzerland) states, EU countries, the Commonwealth of Independent States (CIS) countries except for Russia (suspended), Georgia, and with Montenegro and Macedonia. Canada currently has only one multilateral agreement (in force) with nations in Europe, namely with the EFTA states, making the CUFTA Canada's second such agreement with a European nation. Canada has also negotiated the Comprehensive Economic and Trade Agreement (CETA) with the European Union; it is yet to be ratified.

Import of Ukrainian goods into Canada

For Ukrainian imports into Canada, key CUFTA duty concessions include:

- Canada will immediately eliminate tariffs on all industrial products, fish, seafood and 99.9% of Ukrainian agricultural imports upon entry into force of the CUFTA.
- Other Ukrainian products that will benefit from duty-free access under the CUFTA include sunflower oil, sugar and chocolate confectionary, baked goods, vodka, iron and steel, apparel, ceramics and minerals.

Some economically sensitive tariffs, such as those for certain motor vehicles of heading 8703, will be reduced gradually over the transitional period of up to seven years.

Import of Canadian goods into Ukraine

Depending on the tariff code of the imports, Ukrainian duties for goods originating in Canada will be eliminated or reduced, as follows:

- Ukraine will immediately eliminate tariffs on 86% of Canadian imports upon CUFTA's entry into force. The balance of tariff concessions will be implemented over periods of up to seven years.
- Canadian products benefiting from immediate or eventual duty-free access include beef, certain pulses, grains, canola oil, processed foods, animal feed, frozen fish, caviar, certain articles of iron and steel, industrial machinery, articles of plastics, and cosmetics. Tariffs will also be eliminated on fresh and chilled pork.
- There will be a gradual elimination of duties with a transitional period of one, three or seven years for certain economically sensitive agricultural and industrial goods. In particular, significant reductions of high-duty tariff lines by as much as 20%, 30% or 50% will occur over a transitional period of five years (e.g., vegetable oils) or seven years (e.g., poultry).

Tariff quotas and exemptions from the free trade regime

Ukraine has introduced a preferential tariff rate quota for duty-free Canadian pork imports under tariff headings 0203, 0206, 0209. Quotas will be distributed on a first-come, first-served basis. The quota is expected to exceed current volumes of imported Canadian frozen pork and pork offal by a large margin.

Canada has introduced preferential tariff rate quotas for certain Ukrainian imports of poultry, dairy products and eggs, in line with Canada's long-standing agricultural supply management policies. Canada will distribute these quotas according to its national legislation. Import of the goods over quota would attract Canadian customs duty, which may exceed 200% of the goods' value for certain types of merchandise.

Sugar and artificial honey (tariff heading 1702) are excluded from the free trade agreement and, therefore, continue to be subject to the general rate of duty.

Rules of origin

Both trade partners have agreed to provide access to advance rulings on the origin or tariff classification of products. The CUFTA provides comprehensive rules for the determination of the goods' origin, with specific rules of origin for determining whether non-originating materials in specified products meet sufficient transformation requirements. These specific rules are based on tariff shift and regional value content criteria. The general rules essentially provide that originating Ukrainian or Canadian goods must meet one of the following criteria:

- Be wholly obtained in the territory of the relevant country — the goods do not contain foreign raw materials (foreign materials from the other party to the agreement are considered originating by virtue of the cumulation rule)
- Be sufficiently produced in the territory of either party from both domestic and foreign raw materials, provided that the foreign materials are deemed originating by virtue of meeting any required tariff shift and regional value content criteria specific to the product in question

Notwithstanding the above, originating Ukrainian or Canadian goods:

- May contain foreign non-originating materials provided that the total value of those non-originating materials does not exceed 10% of the value of the product
- Must be shipped directly to the importing country from the other country, with allowances for transshipment through third countries only where goods remain under documented customs control

Proof of origin

To certify the goods' origin, the exporter must issue a written declaration of origin on the invoice or other commercial document. This declaration is valid for 12 months. Moreover, under the provisions of the agreement, a single declaration of origin may be used for several consignments of identical goods. The CUFTA does not provide for the issuing of origin certificates by customs or any other government authorities.

Entry into force

The Parliaments of Ukraine and Canada must ratify the CUFTA before it may enter into force. The CUFTA becomes effective on the first day of the second month following receipt of the latter party's notification on the completion of the legislative ratification process.

At the time of writing, the relevant draft law has not yet been registered in either the *Verkhovna Rada* (Parliament) of Ukraine or the Canadian Parliament.

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The Eurasian Economic Union-Vietnam Free Trade Agreement now in force

The free trade agreement (FTA) between the Eurasian Economic Union (EEU: Russia, Belarus, Kazakhstan, Armenia and Kyrgyzstan) and Vietnam was signed on 29 May 2015.[2] However, the EEU countries completed the FTA's ratification process only in mid-June 2016. Since the FTA enters into force 60 days after the receipt of the last completion of ratification procedures notification, the FTA will take effect on 5 October 2016.

The FTA covers such key topics as trade in goods and preferential treatment, trade protection measures, customs administration and trade simplification, sanitary and phytosanitary measures, trade in services, capital investments, movement of people, intellectual property, government procurement, electronic technologies in trade, and others.

The major advantage for importers resulting from the FTA is the reduction of import customs duty rates on goods. The reduction will affect 88% of the EEU Unified Customs Tariff commodity lines, and for 59% of such commodity lines the duty will be reduced to zero immediately after the FTA comes into effect. For example, the current rate of import customs duty for footwear with soles of natural leather is EUR1.63 per pair. After the FTA enters into force, the rate for that item will be 0% of the customs value.

The FTA also provides for exemptions from customs duty for a range of goods. However, if the volume of imports of such goods exceeds a specified (trigger) level during any calendar year, duties will be levied in the normal manner the following year (so-called trigger measures). For example, the trigger level for shirts and blouses classified under headings 6105, 6106, 6205 and 6206 will be 973,976 kilograms in 2016, but will rise to 1,193,163 kilograms by 2019. Trigger measures will apply for six months with the option of extension for an additional three months. The conditions for the application of a trigger measure will be reviewed every three years.

Rice exported to the EEU as well as eggs, processed tobacco and tobacco refuse exported to Vietnam will be subject to quotas.

Other goods will be subject to most-favored-nation treatment, i.e., general duty rates.

2 The signing of the EEU-Vietnam FTA was discussed in the September 2015 issue of *TradeWatch*.

Preferential treatment may be granted only when the following three conditions are met:

- **Direct transhipment rule** — under this rule, a commodity must be shipped directly from the territory of the exporting party to the FTA and may be transported via third countries because of geographical considerations, so long as this is done under customs supervision. The goods in transit must not be traded, used or subject to any handling other than handling required to preserve the goods.
- **Direct purchase rule** — this rule will be observed whether the invoice for goods is issued by a resident of one of the FTA countries or by a resident of a third country. However, the FTA establishes a list of ineligible offshore countries, and goods imported by persons registered in those countries will not be granted preferential treatment.
- **Confirmation of originating goods** — to be recognized as originating in a country that is a party to the FTA, the goods must meet one of the following conditions:
  - The goods must have been wholly obtained or produced in the country.
  - The goods must have been wholly produced in one or both parties to the FTA exclusively from originating materials.
  - The goods may have been produced using materials originating in third countries, but must meet special origin criteria. There are different origin criteria for different goods. An example of a special origin criterion is a change in the tariff classification code of materials at the six-digit level. Other criteria include added value. Even when the goods do not fully meet the requirements of tariff shift, they still may be regarded as originating in a country that is a party to the FTA. This is the case if the value of non-originating materials that have not undergone tariff shift remains below a certain percentage of the finished product value and all other conditions are met.

To confirm the country of origin, an importer must provide a Certificate of Origin (on the EAV[3] form) that is valid for 12 months for each consignment of goods. A certificate does not have to be provided for a consignment with a value not exceeding USD200.

When the FTA becomes effective, importers may encounter a number of risks. For example, the EEU customs authorities may request verification of origin (certificates, criteria) and carry out on-site audits in Vietnam. In addition, importers run the risk of being subjected to trigger and other protective measures and the possibility of a temporary or complete suspension of preferential treatment.

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[3] EAV stands for EurAsia Vietnam.

Brazil

Brazil adopts ATA Carnet regime in time for the Olympics

Brazil is now the 75th country to implement and utilize the ATA[4] Carnet regime for temporary importation of goods. Normative Instruction 1639 published on 10 May 2016 also made Brazil the first country within the Mercosur region to adopt the ATA Carnet regime.

The Istanbul Convention, adopted by the World Customs Organization (WCO) in 1990 (the successor of the 1961 Customs Convention on the ATA Carnet for the Temporary Admission of Goods), is the result of a partnership between the WCO and the International Chamber of Commerce (ICC), which provides the procedural system of the ATA Carnet regime.

The ATA Carnet — occasionally referred to as a "passport" for goods — is a customs document that may be used for importing duty-free certain goods temporarily. Eligible goods include commercial samples, professional equipment, and goods for use in fairs, shows, exhibitions, sporting events and others. Imported goods may circulate within one or more countries with the same Carnet for up to 12 months.

The adoption of this globally recognized regime in Brazil triggers various possible benefits to importers, including:

- Pre-clearance of goods at a determined cost
- Transit with the goods through more than one country
- Use of the same document for various shipments during its period of validity
- Return of goods to country of origin without delays
- Suspension of import duties

While the regime is likely to bring benefits to users, the Brazilian customs authorities will also benefit as the temporary importation process is simpler (especially as it relates to financial guarantees) and requires less time and fewer resources.

This new regime had special relevance for the Rio 2016 Olympic and Paralympic Games, for which large volumes of equipment related to the athletes, events, global media and various committees entered Brazil temporarily. As of July 2016, Brazilian Customs also recognizes the ATA Carnets of other countries, thus greatly facilitating and expediting the entry of sports equipment and other related goods.

[4] ATA is derived from "Admission Temporaire/Temporary Admission," a combination of the English and French terms.

The 27 industry federations in Brazil plan to start issuing Brazilian ATA Carnets in September 2016.

This introduction of the ATA Carnet regime represents a significant step in the development and globalization of Brazilian international trade and commerce, and it may have relevance for all businesses with temporary importation in Brazil. Companies need to assess the potential benefits that may apply to them and accordingly, initiate procedures to implement the regime.

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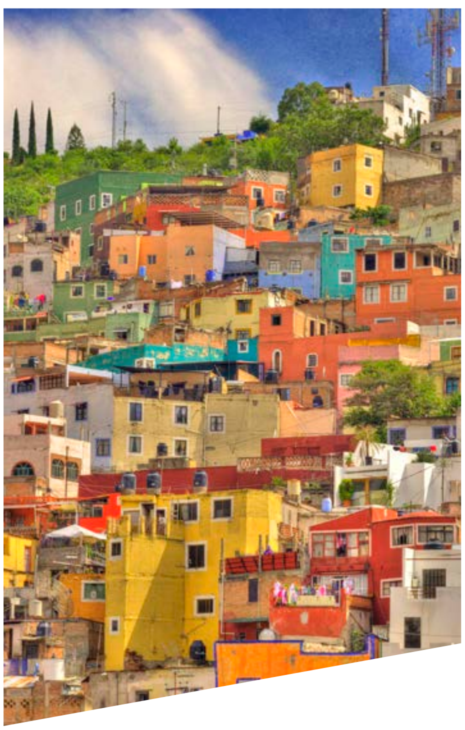
Mexico

Special Economic Zones in Mexico



In an effort to promote economic activity in regions with high poverty rates, the Mexican Government published the Federal Law on Special Economic Zones (the Law) on 1 June 2016. The Law creates the framework for the operation of Special Economic Zones that will be introduced in Mexico.

In line with the Law's main objectives, Special Economic Zones will initially be established in the 10 Mexican states with the highest poverty rates. These include Yucatán, Quintana Roo, Campeche and Tabasco in southern Mexico; Veracruz on the Gulf of Mexico; and the Pacific states of Oaxaca, Guerrero and Michoacán and others. The states in Mexico's central and northern regions are not included because poverty rates are lower and there is a higher number of manufacturing operations through the IMMEX (*Industria Manufacturera, Maquiladora y de Servicios de Exportación*), or maquila, program.

Individuals and entities carrying out operations in the zones will be eligible to receive various tax, customs and economic benefits. The Mexican government will issue a specific decree establishing the benefits that will be exclusive to each authorized zone. These benefits will be temporary and will be reduced over a specified period, although they must be in place for a minimum of eight years.

While the benefits will be zone-specific according to the decree to be issued by the Mexican Government, the Law provides that customs duties will be waived upon entry into a zone and a specific customs regime will be drafted to regulate the admission and withdrawal of domestic and foreign goods.

Goods that are admitted into the Zone will be subject to a 0% value-added tax (VAT) rate. In addition, all services provided in the Zone as well as the sale of goods that are in the Zone, will be subject to a 0% VAT rate. The Law does not state whether operators will need to comply with mechanisms similar to the Annex 31 of the General Foreign Trade Rules, which monitors VAT compliance for IMMEX companies.

An Integral Administrator who has responsibility for developing and operating the zone will manage each zone. The permits obtained by the Integral Administrator will be granted for up to 40 years and may be extended for another 40-year period. The investors are the foreign or domestic companies who obtain authorization to perform productive economic activities in the zone.

As the framework for the zones continues to be developed, it will be important to get a better understanding of the requirements and controls that apply to zone operators and their manufacturing operations to identify potential business opportunities. Moreover, companies should stay informed on how the zones will interact with manufacturers that are already established and operating under the IMMEX program or the Strategic Bonded Warehouse customs regime[5] throughout Mexico.

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[5] The Strategic Bonded Warehouse regime was discussed in the June 2016 issue of TradeWatch.

United States

Upcoming changes to the reconciliation program

On 1 November 2015, the Automated Commercial Environment (ACE) became the US Customs and Border Protection's (CBP) official system of record for all electronically transmitted entry and corresponding entry summary data. CBP has adopted a phased approach towards mandatory filing of electronic entries and entry summaries in ACE. As part of the final phase of transition to ACE, the ability to submit reconciliation entries (type 09) on ACE is scheduled to be available as of 29 October 2016.

The reconciliation program allows importers to file entry summaries with best available information at the time of import to be reconciled or corrected within 21 months of date of importation. Reconciliation is used regularly for valuation issues (e.g. assists, royalties, goods subject to transfer pricing adjustments, valuation of US goods returned). It is also used with regard to Free Trade Agreement (FTA) eligibility (although with a timeframe for reconciliation generally limited to 12 months), and in some limited situations for classification.

CBP has published an updated reconciliation guide — "Automated Commercial Environment Reconciliation (Prototype), A Guide to Compliance, Version 1.0, September 2016." The guide describes the following updates to the reconciliation program that will be effective upon CBP's transition to ACE Reconciliation Prototype:

- Reconciliation application eliminated: Importers will no longer be required to submit an application to participate in reconciliation. All importer account profiles on ACE will be defaulted to "yes" to indicate eligibility for participation in the reconciliation prototype. Importers can start flagging entry summaries after establishing a reconciliation bond rider to their continuous customs bond. Upon obtaining the reconciliation bond CBP will be notified of the importer's intent to flag entries for reconciliation.
- Reconciliation flag changes: CBP will no longer blanket flag entry summaries for Reconciliation. Importers will be required to rely on their brokers to either flag entry-by-entry or blanket flag using automated functionality in the Automated Broker Interface (ABI) software, if available.

- Reconciliation submissions through EDI: Changes are also expected to the process of reconciliation submissions. All reconciliation submissions will be made electronically through an Electronic Data Interchange (EDI) transmission. This includes association files, line item data summary file and required declaration statements for FTA reconciliations. Hard copy submissions of reconciliation packages will no longer be required. A soft copy of the line data summary file on a CD will also no longer be required.
- Reconciliation processing locations expanded: Reconciliation submissions will no longer be restricted to the thirteen reconciliation ports. Reconciliation entries may be filed at any port of entry. Personnel from the Center of Excellence and Expertise (CEE) will process the reconciliation entries.

Implications

The changes are welcome news for importers that set prices using profits-based transfer pricing methodologies, which can result in the need to use the reconciliation program to report post-importation adjustments to transfer price. These importers will automatically be eligible for reconciliation, rather than having to file an application and be approved into the program.

While the anticipated changes promise simplified application and submission processes, it will be important to update existing reconciliation processes to align with the changes to ensure smooth transition. Importers that operate under the blanket flag option will need to instruct each of their customs broker to develop a methodology to automatically flag entry summaries to ensure that there are no gaps in flagging of entry summaries. As the anticipated changes are just around the corner, importers should address the changes to their reconciliation processes immediately.

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US Customs releases new Valuation Encyclopedia

In June 2016 US Customs and Border Protection (CBP) issued the latest version of the Valuation Encyclopedia, a compilation of cases, CBP Headquarters rulings, Treasury Decisions, and Notices dealing with customs valuation. The June release updates the December 2010 release and contains decisions from 1980 through 2015. More than 50 topics are covered in 580 pages.

Always a very useful resource, this version of the Valuation Encyclopedia is especially welcome given the many new and important decisions in several key areas, including related party pricing, since 2010. As the summaries are prepared by CBP, the commentaries themselves can be quite useful. One good example is the Valuation Encyclopedia summary of CBP ruling H208055 (Oct.12, 2012), which deals with providing satisfactory evidence to meet the CBP criteria for obtaining refunds due to transfer pricing adjustments, generally referenced as the "5-factor test." The Encyclopedia summary states: "This decision serves as example of the types of documentation CBP is looking for in order for the 5-factor test to be met." With this comment, CBP is clearly pointing to this as the example to be followed, which can be immensely helpful for importers.

Commentary can also focus the reader on critical decision factors, often in cases with seemingly similar facts decided in close proximity. For example, two 2015 CBP Headquarters rulings profiled on pages 340-342 of the Valuation Encyclopedia deal with importers who determined prices using the Comparable Profits Method (CPM) for transfer pricing, with the US importer the tested party. In both cases, products sold by the comparable companies in the transfer pricing analyses were not in the same class or kind as goods imported. In H238027 (Feb. 19, 2015), CBP rules that transaction value was the appropriate method of appraisement, and that transfer pricing adjustments would be respected. In comparison, H254700 (November 25, 2015) rules that the same transfer pricing approach is ineligible for transaction value and that the importer must use deductive value. The difference in the rulings is that in the first the importer submitted a study of the importer's industry prepared by Ernst & Young LLP, including both a qualitative and quantitative verification, as well as information regarding its own profitability vs. that of its competitors. In the second ruling, CBP's summary states that, "Apart from identifying the parent company's competitors in the crop protection industry, there was no quantitative or qualitative information provided with respect to the U.S. importer/buyer's direct competitors in the U.S."

The Valuation Encyclopedia can be found under "Informed Compliance Publications" in the "Trade" tab at www.cbp.gov.

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New Miscellaneous Tariff Bills process for temporary duty suspension and reduction

In February 2016, the President of the United States signed into law the Trade Facilitation and Trade Enforcement Act of 2015, a bill that altered several laws affecting international trade.[6] Tucked near the end was a nonbinding "Sense of Congress" provision calling for development of a regular, predictable legislative process for crafting temporary duty suspension and reduction bills.[7] These bills, known commonly as Miscellaneous Tariff Bills (MTBs), are targeted at imported goods with little to no domestic production. Previously, members of Congress submitted individual tariff suspension bills that were vetted by the International Trade Commission (ITC) and consolidated into a single bill.

The last MTB was passed in 2010 and expired at the end of 2012.[8] At the time of its expiration, Members of Congress were seeking to eliminate "earmark spending," which is the process of appropriating federal funds to specific projects, often to the political benefit of the legislator whose congressional district received the funds.

An unofficial moratorium on earmark spending was instituted. Several legislators in Congress believed tariff suspension under an MTB amounts to a "limited tariff benefit," which under the Rules of the House of Representatives is treated the same as an earmark. While there was disagreement on whether an MTB meets the definition of "limited tariff benefit," earmark moratorium led enough legislators to oppose renewal of the MTB when it expired.[9]

To remedy the appearance of earmarking, the new MTB process is initiated yearly through the ITC rather than by individual legislators.[10] Any individual or company who would be a beneficiary of tariff suspension or reduction may petition the ITC to include specific tariff provisions in the MTB. The petition must show that the petitioner will benefit from the suspension and include a description of the industry that uses the article, the total amount of the article imported and other information.

6 Trade Facilitation and Trade Enforcement Act of 2015, Pub. L. No. 114-125, 130 Stat. 122 (2016).

7 Id. at § 919, 130 Stat. at 280.

8 Manufacturing Enhancement Act of 2010, Pub. L. 111-227, 124 Stat. 2409 (11 August 2010).

9 Colby Itkowitz, "How Congress hopes to de-earmark trade earmarks," *The Washington Post*, 19 May 2015.

10 American Manufacturing and Competitiveness Act of 2016, Pub. L. No. 114-159, 130 Stat. 396 (2016).

The ITC then posts each petition on its website and requests public comment prior to submitting a preliminary report of recommended tariff suspensions to Congress. The House Ways and Means Committee and Senate Finance Committee review the preliminary report and may submit additional information to the ITC. After reviewing the petitions in light of the public comments and congressional recommendations received, the ITC prepares a final report making recommendations for tariff suspension and submits that report to the two committees. The committees may remove or adjust any individual tariff suspensions, but may not add any tariff suspension not recommended in the ITC final report.

The deadline for submitting petitions to the ITC for inclusion in next year's MTB is 15 October 2016.[11] This new MTB process may provide opportunities for businesses as it allows a more streamlined, data-driven approach to obtaining tariff suspension for domestic manufacturers. Industry analysis, along with revenue effects on the federal purse, will determine which tariffs are suspended, rather than the advocacy of any individual legislator. Companies that wish to obtain possible MTB benefits are advised to perform this analysis, formulate the necessary arguments and submit petitions to the ITC before the published deadline.

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[11] The proposed forms for submission of petitions can be found on the ITC's website: https://pubapps2.usitc.gov/comments_mtbps/ (last visited 15 June 2016).

CBP publishes new ADD/CVD anti-evasion regulations

US Customs and Border Protection (CBP) released interim regulations on 22 August 2016 to enable new investigation procedures regarding the evasion of antidumping duties (ADD) and countervailing duties (CVD) pursuant to the Enforce and Protect Act enacted earlier this year. These new trade remedy enforcement regulations, which can be found in 19 CFR Part 165, outline CBP's procedures for the investigation of evasion claims of ADD/CVD orders and the rights and duties of interested parties.

The regulations were issued just one week after the Government Accountability Office (GAO) released an audit report of CBP, which estimates that $2.3 billion in ADD and CVD has gone uncollected between 2001 and 2014.[12]

The Enforce and Protect Act, part of the Trade Facilitation and Trade Enforcement of 2015 (see *TradeWatch*, Volume 15, Issue 1, March 2016), establishes the Trade Remedy Law Enforcement Directorate within CBP's Office of Trade. The regulations establish the procedures for interested parties or governmental agencies to file allegations of evasion and requests for investigation by the Directorate, the investigation procedures and the administrative reviews. Notably, the definition of interested party is quite broad and includes any manufacturer, producer, importer or exporter of a product covered by an ADD or CVD order; a manufacturer, producer or wholesaler of a like kind domestic product; or trade associations or unions majority composed of interested parties. Along with timelines imposed on CBP investigative actions, there are specific provisions for the notification of interested parties and provisions that allow CBP to reach conclusions more swiftly. As an example, 19 CFR §165.6 allows CBP to apply an "adverse inference" if a party, exporter or importer of target product "fails to cooperate and comply to the best of its ability with a request for information."

With new enforcement procedures and heightened concern over revenue loss from ADD and CVD evasion, importers of products that are covered by ADD or CVD orders should expect more scrutiny.

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12 The GAO report is available at http://www.gao.gov/products/GAO-16-542.

China

The State Council makes significant revisions to the regulations on customs audits

The original *Regulations of the People's Republic of China on Customs Audits* (the original Regulations), established China's customs audit system in 1997. Nearly 20 years after their release, on 1 July 2016, the State Council issued *Decision of the State Council on Revising the Regulations of the People's Republic of China on Customs Audits* (the new Regulations). The new Regulations become effective on 1 October 2016.

Although the overall framework and most of the content from the original Regulations remain unchanged, the new Regulations include notable revisions to the original Regulations aiming to facilitate Customs' adaptation to the new trends of foreign trade development and to meet the ever-growing demand for port clearance facilitation.

The new Regulations have incorporated revisions in a number of areas (e.g., definition of customs audit, the audit procedures and others) and included clarification on certain specific matters. As a highlight, the new Regulations formally introduce a voluntary disclosure mechanism and allow the involvement of third-party professional firms to assist in the audit process.

The table below outlines some of the main changes:

Changes	Content
Additions	▸ Inter-government sharing of company information: "Customs may collect information related to import and export of certain specific commodities and certain industries from related industry associations, government sectors and enterprises as required for a customs audit. Customs shall not disclose any information collected in relation to commercial secrets."
	▸ Involvement of third-party firms to assist with audits: "When conducting an audit, Customs may engage third party accounting or tax firms for a professional conclusion on related issues. Where the parties being audited have engaged any third party accounting or tax firms, their professional conclusions may be used as reference for a customs audit."
	▸ Requiring Customs to substantiate its decisions: "Customs should explain the reasons for their decision in the audit conclusion and inform the parties under audit of their rights."
	▸ Voluntary disclosure: "Where the enterprises who are directly related to import/export goods voluntarily report their non-compliance to Customs and accept the corresponding penalty, a more lenient treatment shall be granted or a reduced administrative penalty shall be imposed."
	▸ Penalties: "If a party being audited fails to set up or compile the relevant records as appropriate, or transfers, conceals, alters or destroys the relevant records, legal liabilities shall be investigated and prosecuted in accordance with the Accounting Law."
Revisions	▸ The audit period of bonded goods or goods imported under exemption or other relief programs has been changed from "within the Customs supervision period" to "within the customs supervision period and the following three years."
	▸ Record-keeping requirements: companies are no longer required to keep hard-copy records if their computerized accounting system is sound and records can be printed at any time. Companies may now keep records in electronic form.
	▸ Customs may take into consideration a company's "credit rating and risk profile relevant to import/export operations" when deciding which companies to audit.
	▸ "Director of Customs" is defined as the director of the Customs office that is directly affiliated with Central Customs or its authorized director of the subordinate Customs office.
	▸ A seizure provision to specify that Customs may seal or seize relevant data-storage media has been added.
	▸ Customs fines for noncompliance in the original Article 29 (now Article 30) have been increased as follows: ▸ RMB10,000 to RMB30,000 (approximately USD1,496 to USD4,487) has been changed to RMB20,000 to RMB100,000 (approximately USD2,991 to USD14,957). ▸ RMB1,000 to RMB5,000 (approximately USD150 to USD748) has been changed to RMB5,000 to RMB 50,000 (approximately USD748 to USD7478). ▸ A provision that a company "shall be subject to criminal liabilities if a crime is constituted" has been added.
	▸ The kinds of violations that would result in penalties as prescribed in the original Article 30 (now Article 31) have been revised.
Removals	The provision that requires companies to submit to Customs certain materials concerning the purchase, marketing, processing, utilizing, loss and inventory of import and export goods has been removed.

Observations

The new Regulations represent further improvement of China's customs audit system. They are in line with a series of rules that Customs has published during the past two years to streamline administration, delegate powers and transform functions. The new Regulations have addressed specific issues with the customs audit process through notable revisions to the original Regulations.

For Customs authorities, the revisions to the original Regulations are expected to promote the sharing of information among different government authorities and to enhance unity, transparency and flexibility during the customs audit process.

For importers and exporters, the revisions present both opportunities and challenges. For example, companies will be permitted to engage third-party professional firms for assistance in managing their customs function and in the customs audit process. At the same time, the revisions also institute more stringent requirements on businesses and their customs staff concerning day-to-day customs operations management.

Additional details regarding the opportunities and challenges

Information sharing among different government authorities

- The new Regulations allow Customs to exchange with other government agencies information of common concern (e.g., royalty payments and related party transactions). The new Regulations are in line with the information sharing process that was started with the issuance and implementation of the *Provisional Measures of the Customs of the People's Republic of China for the Administration of Enterprise Credit,* General Administration of Customs Order No. 225 in force since 2014.
- When disclosing information to appropriate government authorities, companies should ensure that such information is authentic and consistent. Any violation of the laws or regulations with one government department will affect a company's dealings with other government authorities with whom the information has been shared.
- Article 8 of the new Regulations now allows companies to keep electronic records (instead of hard-copy) so long as the accounting system directly related to import and export activities is sound and bookkeeping and business accounting can be carried out by computers.
- This will be an important area for both Customs audit and Authorized Economic Operator (AEO) certification. Therefore, companies should improve their record management according to the new regulatory requirements.

Involvement of third-party professional firms in Customs audits

- The new Regulations allow Customs to engage accounting and tax firms for their professional opinion on related issues during an audit. At the same time, businesses may also engage accounting and tax professional firms, and their opinions will also be used as references for customs audit purposes.
- Before the publication of the new Regulations, Customs rolled out a program on the involvement of third-party professional firms in audit on a pilot basis in certain locations. The new Regulations now formally incorporate and implement this program throughout China.
- As a result, third-party firms can help "bridge" the communication between companies and Customs during an audit. The ability of third-party firms to communicate with Customs and their professional knowledge is critical for properly assessing potential customs risks and providing effective solutions to address such risks.

Self-discipline management/ voluntary disclosure program

Starting in 2015, Customs authorities in many districts successively introduced a self-discipline management/voluntary disclosure pilot program for businesses. Pursuant to this pilot program, companies were encouraged to engage third-party firms to perform an independent self-audit and voluntarily report possible violations of customs regulations. The new Regulations formally incorporate and implement this program throughout China. The formal establishment of the voluntary disclosure system promises to be a win-win outcome for both Customs and businesses.

Companies are advised to conduct the necessary self-assessment for managing customs issues, identify any potential gaps, and promptly remedy and correct such gaps.

Certain matters may need further clarification

The new Regulations clarify and standardize certain provisions in the original Regulations. However, questions may arise during the implementation of the new Regulations that may require further clarification and guidance. These may include:

- How should "certain specific goods" be defined in information sharing?
- What procedures should companies follow during voluntary disclosure? After voluntary disclosure, will the case still be handed over to an anti-smuggling department? Are there specific criteria for reduced or mitigated administrative penalties?
- Are there any identification and selection criteria for a third-party "professional firm"? What are the specific procedural requirements for a third-party professional firm's participation in a customs audit? To what extent may Customs deem as "reference" a professional report issued by a third-party firm?

Conclusion

With the incorporation of notable revisions in a number of areas and the clarification on a number of specific provisions, the new Regulations have introduced significant changes into the original Regulations. Businesses are advised to assess their operations to determine whether these changes apply to them and to revise their procedures accordingly. As to issues awaiting further clarification, businesses need to pay close attention to new developments.

Look for updates in future issues of *TradeWatch*.

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New Zealand

The new Customs & Excise Act: bill to be introduced soon

New Zealand's Customs & Excise Act 1996 has been subject to an overhaul that is long overdue, as the legislation has become outdated. Recently, the proposed changes received Cabinet approval and a new Act could be in place by early 2017.

Unfortunately, it is apparent that businesses are left with a smorgasbord of changes that are hard to navigate and difficult to assess.

In this article, we look at the highs and lows of the changes that the Cabinet has approved.

Information sharing will continue to protect confidentiality

Customs handles a lot of information about cross-border travelers and cross-border trade. Approximately a third of all the decisions made by the Cabinet as part of this review are in respect of information sharing.

What is reassuring for business is Customs' commitment to ensuring confidentiality of commercially sensitive information. Customs is also looking to access and share information to boost the use of preferential rates of duty under free trade agreements.

The disadvantage for businesses is the requirement to share information with Inland Revenue as well as with overseas customs authorities.

Greater powers to intercept illicit goods

The changes are principally designed to help Customs intercept illicit goods and dangerous persons. Business travelers should be aware of Customs' broad powers to inspect accompanying luggage and digital devices.

Interest and late payment penalties to replace additional duty

Customs is looking to scrap the onerous additional duty regime whereby additional duty compounds for excise taxpayers who short pay. Instead, Customs is exploring a system similar to that of Inland Revenue whereby penalties apply to late payments and interest is charged for underpayments of all forms of duty. It will be controversial if Customs decides to impose interest on Goods and Services Tax (GST) errors for importers that are registered for GST and can claim back GST from Inland Revenue (i.e., where there is no loss of revenue to the government).

Customs brokers face a raft of changes to the administrative penalties regime, including the extension of administrative penalties to export entries. Businesses should be aware of their contractual responsibilities with their customs brokers in relation to administrative penalties.

Excise tax fails to deliver bonded warehouse regime

Wineries will be breathing a sigh of relief that they have not lost their offsite storage concessions. Brewers will be raising a glass, as the concession will be extended to all domestic alcohol manufacturers.

Unfortunately, Customs has rejected the introduction of a bonded warehouse regime for imports and domestic manufacture of excise goods. Customs claims this could be a reversion to a pre-GST sales tax regime but ignores the economic benefits. Many countries with a GST system operate a bonded warehouse regime.

New domestic producers are also likely to be disappointed with the requirement to file and pay on a monthly basis regardless of their excise liability. They can earn the right to a deferral period (6 or 12 months according to their annual excise liability) until Customs is satisfied that this compliance burden can be lifted.

No GST simplification

Much to the frustration of GST-registered importers, GST will still be treated as a duty, and Customs will continue to collect GST as such. Practically, this means that there will be no simplification in the short and possibly medium term. Customs will continue audit activity where only GST is at stake and the GST is recoverable from Inland Revenue.

Additional work in this area is expected.

Progress on valuation and transfer pricing problems

The good news is the introduction of a binding ruling system on valuation and a formal mechanism for dealing with transfer pricing adjustments and other adjustments to the customs value of imported goods.

However, extreme caution is required when approaching Customs on valuation matters. Recent case law highlights the difficulties (such as disregard for the nature of the transaction between seller and importer and years-long delays) that can be encountered when seeking clearance from Customs on valuation matters.[13]

Retailers to miss out

Brick and mortar retailers are out of luck. The low value threshold for imported goods is out of scope for the proposed changes.

Separate consideration of the low value threshold appears to be continually delayed as Customs tries to grapple with possible solutions, and no doubt technology, for this thorny issue.

Approach to the new Act

Fortunately, Customs is taking a purposive approach to the new Act. This should help provide greater certainty for businesses. Other positive developments are that the Comptroller of Customs will have statutory discretion concerning the collection of revenue and that a new dispute resolution process is being put in place.

This should bode well for future administration of revenue collection by Customs, particularly given that a significant portion of GST revenue collected by Customs is simply refunded by Inland Revenue.

In closing, the success of the new Act will ultimately depend on how well Customs embraces the changes at an operational level.

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[13] See, e.g., Q v. Chief Executive of the New Zealand Customs Service [2016] NZCAA 1 (11 April 2016), www.nzlii.org/nz/cases/NZCAA/2016/1.html.

Common Market of East and South Africa

Fewer COMESA goods eligible for import duty exemption in Uganda after June 2016 budget

Uganda is a member of the Common Market for Eastern and Southern Africa (COMESA) regional trading bloc, which comprises 19 member states[14] in Africa. Prior to July 2014, Uganda offered preferential import duty rates of 6% instead of 25% and 4% instead of 6% to imports coming from COMESA member states.

Since 1 July 2014, goods originating from member states of COMESA have entered Uganda duty-free except for a specific few that include organic surface active agents preparations, fruits and ready-to-drink juices, soap and organic surface active products, as well as all items on the sensitive list.[15]

The duty exemption provided by the Finance Act, 2014 applies to goods from COMESA countries that offer reciprocal benefits (i.e., duty-free treatment for Uganda-originating goods) and does not apply to specified exceptions of imported goods, even when they originate from COMESA member states.

Effective 1 July 2016, the Finance Act, 2016 has expanded the list of non-qualifying COMESA imports into Uganda that will now be subject to duty. These imports include:

- Lubricants
- Un-denatured alcohol
- Steel and steel products
- Electronics including refrigerators, washing machines, radios, DVD players and television sets
- Paper and paper products
- Diapers

As a result, the earlier applicable preferential rates of 4% and 6% will be applicable on the specified COMESA imports that have been excluded from the duty exemption benefit.

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[14] Burundi, Comoros, Democratic Republic of Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia and Zimbabwe.

[15] Sensitive items include goods subject to higher than 25% Common External Tariff (CET) rates ranging from 35% to 100% including milk, maize, sugar, rice, cigarettes, primary cells and batteries, among others.

It is apparent that this protectionist measure is intended to protect the nascent manufacturing industry in Uganda from competition with established manufacturers and traders from other COMESA countries. The budding producers, manufacturers and assemblers in these sectors have been earmarked to produce for the local market, but mostly to improve Uganda's unfavorable balance of payments deficit by promoting trade.

Impact on importers of affected items

Importers of excluded items are likely to incur an extra cost when importing these items. This cost will either be passed on to subsequent consumers through price increases or will be absorbed by the affected businesses without increase in prices, but with reduced profits.

Affected importers will need to look into additional supply chain planning for their sourcing as well as consider restructuring of their operations, where necessary, to manage these changes.

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East Africa Community

What the 2016-17 EAC budgets mean to importers and exporters

The East African Community (EAC) budgets were read 8 June 2016. Changes affecting customs and some excise duties went into effect on 1 July 2016, while value-added tax (VAT) and certain other changes affecting excise duties went into effect on 9 June 2016.

In general, there were no surprises as the countries had already shared the budget expenditure frameworks and some of the finance bills a few months earlier. As in previous years, many of the revenue raising measures to fund the budget focused on import duties. At the same time, the budgets include a number of measures intended to reduce import costs for some industry sectors and to promote local development and economic growth.

The following paragraphs highlight the implications of some of the trade-related budget proposals to importers and exporters across Kenya, Uganda, Tanzania and Rwanda.

Kenya

Kenya's budget for the coming financial year is projected at KES2.26 trillion (approximately USD22.3 billion) , almost three times that of Uganda and two times that of Tanzania.[16]

Stay of CET application

Countries that may have a compelling reason not to apply the agreed-upon Common External Tariff (CET) rates may request a stay of application. Kenya has been granted a stay of application for the following goods:

- Rice will be subject to 35% of the customs value or USD200 per metric ton (whichever is higher) instead of 75% or USD345 per metric ton. The stay of application is expected to help alleviate Kenya's rice shortage.
- Duty on paper and paperboard (heading 4805) will be 25% instead of 10%. This measure is to protect Kenya's domestic paper industry and to help make it more competitive.
- Duty on gas cylinders will be 25% instead of 0%. This stay of application was proposed during the previous financial year and has been extended to 2016-17.
- Ready-made garments and leather footwear procured from the Export Processing Zone (EPZ) may be sold on the domestic market at 0% duty so long as sales of these goods do not exceed 20% of a company's total sales. This measure has been introduced to support the textile and leather industry and to discourage trade in used clothing and shoes.

[16] One billion (10^9) is defined as one thousand million; one trillion (10^{12}) is defined as one million million.

- Duty on iron and steel structures (tariff item 7308.90.99) will be 25% or USD250 per metric ton for FY 2016-17. This is yet another measure aiming to protect local manufacturers from unfair competition.

Increase and decrease in CET rates

Manufacturing sectors in Kenya have been facing stiff completion from imports of similar products as those produced locally, and duty rates may be increased for goods from these sectors. On the other hand, CET rates will be reduced for some goods that are considered essential, but are in short supply. Listed below are some examples of both rate increases and decreases:

- The duty rate for made-up fishing nets will increase from 10% to 25%.
- The specific duty rate on used clothing and other used articles will increase from USD0.20/kg to USD0.40/kg so that the applicable rate is 35% or USD0.40/kg, whichever is higher.
- Import duty rates for oil or gas filters for engines will increase from 10% to 25% to encourage purchases from local manufacturers.
- To encourage use of environmentally friendly energy efficient stoves and appliances for solid fuel, the duty rate has been reduced from 25% to 10%.
- Import duty for aluminum/milk cans will increase from 10% to 25%. This year all EAC countries, except Rwanda, will apply 25%.
- The duty rate for selected iron and steel products will increase from 10% to 25% to protect local producers.

Duty remission scheme

Section 140 of the EAC Customs Management Act mandates that member states remit duty on goods imported for use as raw materials in the manufacture of goods for subsequent export or domestic consumption. These include the following:

- Inputs for the manufacture of matches and matchboxes at 0%
- Nylon yarn — mostly for hosiery manufacturers: 0% instead of 25%
- Trigger sprays and lotion pumps (containers for cosmetics, surface cleaners and other products): 10% instead of 25%
- Inputs for the manufacture of solar equipment: 0% duty, a welcome move for local manufacturers since solar equipment imports are already exempt from duty
- Bars and rods for the manufacture of automobile bolts, nuts and leaf springs: 0%
- Aluminum plates and sheets for the manufacturing of aluminum cans: 0%
- Motorcycle completely knocked down (CKD) kits: 10% for one year
- Raw sugar for refining into industrial sugar: 0% for one year
- Sugar for industrial use: effective 2017-18 the duty rate will increase to 15% and then increase by 5% every year until 2019-20, when it will be 25% upon application for remission (Unless there is local supply of sugar for industrial use, this measure will increase the cost and eventually the prices of the respective finished products.)

Other changes affecting importers and exporters in Kenya

Excise duty amendments

- Kerosene: excise duty was introduced at KES7,205 (approximately USD72) per 1,000 liters. This measure was adopted to help eliminate the practice of using cheap kerosene (which is not subject to excise tax) for adulteration of other products.
- Motor vehicles: the ad valorem rate of 20% on imported motor vehicles has been reintroduced. According to the Excise Duty Act 2015, the duty rate had been set at KES200,000 (approximately USD1,970) for motor vehicles that are more than three years old and KES150,000 (approximately USD1,478) for motor vehicles that are less than three years old. The new 20% ad valorem rate appears more fair because it is progressive (i.e., the tax is higher for more expensive cars and lower for less expensive cars).
- Ordinary water: ordinary water/natural/tap water is not subject to excise duty. However mineral/bottled and flavored water will continue to be taxed at KES5 (approximately USD0.05) per liter.
- Cosmetics, personal care and beauty products are subject to 10% excise tax. These products were excluded from excise tax in December 2015. Before December 2015 the excise tax rate was 5%. Affected products include fragrances, makeup, deodorants and antiperspirants, preparations for the hair, bath, shaving, manicure/pedicure and others.
- Plastic sacks and bags: the scope of excise duty was extended to include plastic sacks and bags (except vacuum bags for fruit juices, tea and coffee). These products are now subject to excise tax of KES120/kg (approximately USD1.18/kg). Previously, only plastic shopping bags were subject to excise tax.

Uganda

The Common Market for Eastern and Southern Africa (COMESA)[17] preferential duty rates for certain goods imported from COMESA countries have been discontinued. In general, goods with proper certificates of origin from a COMESA country that are imported into Uganda are subject to 4% or 6% duty where the CET rates are 10% or 25%, respectively. As discussed in the prior article in this issue (starting on page 29) recently, these preferential rates were reviewed and certain goods are now subject to the general CET rates even when imported from a COMESA country to protect local manufacturers of similar products. The affected products include:

- Lubricants
- Un-denatured alcohol
- Steel and steel products
- Electronics and electrical appliances including refrigerators, washing machines, radios and others
- DVD players and television sets
- Paper and paper products
- Diapers

[17] Burundi, Comoros, Democratic Republic of Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia and Zimbabwe.

Motor vehicles for transportation of goods and buses for transportation of more than 25 passengers are subject to 10% duty rate instead of 25%. Rwanda has also announced similar duty rate reductions on imports of similar vehicles. This is a welcome measure for importers in Uganda and Rwanda, but it could have a ripple effect on the future growth of assembly and manufacturing plants in the region, as imports will be cheaper than similar locally manufactured goods. Kenya, being the assembling hub for the region, is likely to be affected the most.

Because of an internal shortage of barley, Uganda will stay application of the 25% CET rate and impose a duty rate of 10%.

Excise duties have been increased on:

- Diesel and gasoline (petrol) by UGX100/liter (approximately USD0.03/liter)
- Sweets and confectionaries at 20%, up from 10% last year
- Certain brands of cigarettes to UGX50,000 (approximately USD14.84) or UGX80,000 (approximately USD23.74) per 1,000 cigarettes.

Tanzania

- Crude edible oil: a stay of application to apply 10% instead of 0% for one year has been granted. This is to protect local industries producing similar oil in Tanzania.
- Specific paper grades: duty rate of 25% instead of 10% will be imposed.
- Cement: to support local industry, imports of cement will attract a CET rate of 35% instead of the current rate of 25% applied by the rest of the EAC member states.

Rwanda

Increase and decrease in CET rates

- Rwanda will stay application of the 25% rate for made-up fishing nets and apply a rate of 10%.
- Rwanda will stay application of the CET rate (35% or USD0.40/kg, whichever is higher) on used clothing and shoes and apply a duty rate of USD2.50/kg for used clothing and USD5/kg for used shoes. This is to discourage trade in "mitumbas"[18] and to help support local apparel and footwear manufacturers.
- Rwanda will stay the application of the increased duty rate (from 10% to 25%) and will apply a rate of 10%.
- The CET duty rate for selected iron and steel products has been increased from 10% to 25% to protect local producers. Rwanda has been granted stays of applications for some of these products.
- Rwanda will decrease the duty rate for motor vehicles for transportation of goods and buses for transportation of more than 25 passengers to 10% duty rate instead of 25%.

Closing thoughts

Each of the EAC member states, just like any other economy, is challenged every year to widen the tax base. Whereas higher tax rates are introduced to protect local industries and other new taxes are introduced to cast the net farther, it is likely that the need to widen the tax base will continue in the foreseeable future until countries become less reliant on borrowed funds to finance their budgets.

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[18] Mitumba (literally "bundle") refers to secondhand clothes and shoes.

Gabon

Recent regulation modifies customs audits

Gabon's Ministry of Sustainable Development and Investment Promotion recently issued Order 0015 dated 11 March 2016 (the Order), which replaces Memorandum No. 00003801 dated 7 December 2011. The Order regulates all aspects of customs audits in Gabon.

The Order defines customs audits as a set of investigations led by the customs administration to verify importers or their representatives' compliance with customs regulations.

This article outlines the different types of customs audits, the authority granted to customs agents with regard to audits, and importers' rights and responsibilities.

Types of audits

The Order provides for three types of audits: immediate (or frontline), post-clearance and surveillance.

1. Immediate audits

Immediate or frontline audits consist of a complete review of customs declarations as well as their attachments and, where necessary, a physical examination of the imported goods.

Customs agents attached to central services (Bureaux Centraux) are the only agents allowed to perform such investigations; however, surveillance agents may assist them.

Agents have 48 hours from submission of the declaration to complete the audit. They may have an additional 24 hours, based on the difficulty of the investigations.

2. Post-clearance audits

Post-clearance audits consist of review of customs declarations, documents related to the management of the company, or any other relevant documents following clearance of the imported goods.

There are two types of post-clearance audits:

- A differed audit (an audit that is different from an immediate audit)
- An audit carried out on the premises of the company

Differed audits consist of a review of customs declarations by teams from the Regional Departments of the Customs administration carried out at Customs' premises.

Customs agents record their findings in a written report that is later sent to the importer. The importer has 15 business days to accept or contest the findings. Failure to respond within this deadline may trigger a second investigation by the Customs administration.

Any declarations not reviewed by a customs agent within six months of clearance will fall outside the scope of the audit.

However, if any infractions are discovered during the six-month period, Customs may go back and audit past transactions from the previous three years.

Audits held on the company's premises consist of in-depth investigations of importers' operations during a specified period as well as investigation of transactions carried out under special customs regimes, if applicable.

Customs Direction of Investigation and Litigation leads the audit, which is limited to three months (but is renewable once), according to the following procedure:

- The Director of Customs, on proposal by the Director of the Customs Investigations, provides a mission letter.
- The importer is notified of the audit 10 business days before the starting date.

The importer may request a postponement of the starting date for not more than 15 business days.

During the investigation, customs agents have the authority to access any documents necessary for their review. Customs provides a written report once the audit on the premises of the company is completed.

3. Surveillance audits

Surveillance audits are led by at least two customs agents and consist of physical examination of the imported goods.

In cases of infraction, customs agents have the authority to seize the goods and record their findings in a written report.

Customs authority

During audits, customs agents have the authority to:

- Require document submissions
- Use scanned images stored in a scan system
- Conduct physical examinations

At the same time, customs agents have the duty to:

- Follow the rules and regulations as well as the ethical duties and responsibilities of the customs profession
- Protect confidentiality

ustoms agents may not interfere with the audited company's management. Additionally, they have the obligation to identify themselves before starting an investigation.

Customs agents may be subject to disciplinary or legal action for failure to comply with the legal requirements.

Importers' rights and guarantees

Importers may hire qualified counsel (e.g., lawyer or customs broker) for assistance. They also have the right to appeal any decisions to the department in charge of customs litigation.

On the other hand, importers have the duty to:

- Provide to customs agents all necessary safety equipment depending on the nature of the goods subject to physical examination
- Facilitate the physical inspection of goods, installations and premises
- Provide requested samples
- Make available all documents required during the audit

Importers are subject to penalties under Section 397 of the Customs Code for failure to comply with these obligations.

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Kenya

Kenya's PVOC program: implications for importers

Background

Standards and technical regulations ensure that conformity assessment systems are implemented to improve production efficiency and quality of exports, to protect the environment, and to facilitate trade. In enhancing production efficiency, standards encourage technology transfer and adoption by prescribing the minimum threshold for products or processes to conform to existing requirements. Furthermore, adequate implementation of national, regional and international standards helps countries deter deceptive trade practices such as counterfeiting.

However, the same standards and technical regulations can also constitute barriers to trade, especially if introduced in a discretionary manner. World Trade Organization (WTO) member countries drafted the Agreement on Technical Barriers to Trade to limit the conditions under which member countries may introduce standards without a transparent rationale that is based on scientific principles, and impose conditions on product performance as opposed to product description. Similarly, the most-favored-nation principle as embodied in General Agreement on Tariffs and Trade (GATT) 1994 rules was enshrined in the agreement.

The PVOC program

Kenya's pre-export verification on conformity (PVOC) program was established under Legal Notice No.78 of 15 July 2005 to implement a conformity assessment regime in Kenya based on Kenyan and East African Community (EAC) standards. The PVOC program was designed to replace the pre-shipment inspection (PSI) program. The PSI covered advance determination of the origin, value and classification of the goods to safeguard revenue collection by the Kenya Revenue Authority, which had inadequate capacity at the time. The Authority has since transformed into an autonomous body corporate capable of discharging its mandate.

Under PVOC, products to be imported into Kenya must be inspected at the point of export by any one of the four appointed certification bodies (Messrs Bureau Veritas, China Certification, Société Générale de Surveillance (SGS) and Inspection Group, and Intertek International).

The appointed certification bodies signed identical contracts with the Kenya Bureau of Standards (KEBS) on 18 January 2015. The certification firms apply a standard rate based on the nature of the goods and risk-based selection criteria for importers as follows:

- A (unregistered products)
- B (registered suppliers or manufacturers of products)
- C (licensed products)

Each designation depends on the product's type, its homogeneity, its frequency of shipments and the manufacturer's quality management system.

The applied standard fee for rate A, B and C is 0.5%, 0.45% and 0.25%, respectively, of the FOB value of the goods subject to a minimum of USD250 and a maximum of USD2,675. Upon inspection, the certification body issues a certificate of conformity (COC), which is used to clear the goods.

Program scope revision

The inspection regime was adjusted to cover all products imported into Kenya beginning 1 September 2015, after the previous PVOC list, which itemized covered products by tariff code, was eliminated. A new exemption framework was developed that covers:

- Raw materials, machinery and replacement spares used in production by registered manufacturers
- Goods imported by registered "diamond mark" importers
- Goods originating from EAC partner states provided they have another mark or are imported by Export Processing Zone (EPZ) companies

The new exemption framework maximizes coverage of products subject to conformity assessment and is expected to result in increased revenue.

Following complaints from new vehicle importers, by public notice dated 6 July 2016, KEBS withdrew the adjusted PVOC requirements on new road vehicles imported directly from the brand owner or his agent. KEBS also allowed new trailers, bulldozers, agricultural tractors, excavators, graders and other off-road vehicles to be imported without a certificate of conformity. To avoid introducing a loophole, KEBS appointed Quality Inspection Services Japan (QISJ) to inspect new vehicles that were sourced from third parties and that used spare parts from selected countries. KEBS will conduct destination inspection on used vehicles and spare parts originating in countries not covered by QISJ.

PVOC or PSI model inspections by appointed certification agencies plug into the capacity gaps in most African economies. In Kenya, for example, laboratory results must originate from a government laboratory to be accepted, yet there is inadequate capacity to test some technologically advanced products. Most high import volume African countries' inspection regimes are no different from Kenya's. Zimbabwe recently introduced a scheme to control the influx of substandard goods and boost revenue collection by the Zimbabwe Revenue Authority. Tanzania, Zambia, Ghana, Nigeria, Niger and Ethiopia, among others, all have PVOC programs in place.

While the PVOC program provides for product inspection, an adequate traceability mechanism to enhance market surveillance at the shelf is necessary. For this purpose, a mandatory import standardization mark (ISM) sticker applicable on all imported finished products at a cost of KES0.49 (approximately USD0.005) per sticker (inclusive of taxes) is required, while an equivalent mandatory standards mark (SM) sticker is applicable for all locally manufactured goods. Motor vehicles and motorcycles are issued a number plate in place of the ISM or SM stickers. Similarly, Diamond Mark (DM) products do not require ISM or SM marks. Payment for the certified mark is based on retail units, meaning that a manufacturer will have to secure different registrations for the SM mark for different brands of the same product. Due to counterfeiting of the ISM stickers by importers, a new secure ISM sticker with quick reference code verifiable through phone short code has been implemented in Kenya from 1July 2016. Old stock keeping units (SKUs) had to be disposed of before this date.

Penalties for noncompliance

Importers in Kenya are subject to a penalty equal to 15% of the value of the goods at the point of clearance if the exporter to Kenya failed to conduct quality certification. This penalty is in addition to the mandatory destination inspection fees. Further, should the destination inspection yield unfavorable results, the importer may have to ship the goods back to the exporter at his or her own expense.

Conclusion

The expanded scope of PVOC is expected to enable importers to clear their cargo faster. Under the newly established pre-clearance program, goods are likely to be cleared within 24 hours after lodging an import declaration provided all requirements are met. Importers wishing to benefit from this program should notify the revenue authority by email and submit their name, agent's name and tax pins. Importers should ensure the goods have been inspected unless such goods are exempted from the requirement. To enroll a shipment, importers need to submit a declaration and a copy of the applicable certificate of conformity at least seven days before vessel arrival.

Businesses that can effectively make the most of the PVOC program can often secure a competitive advantage.

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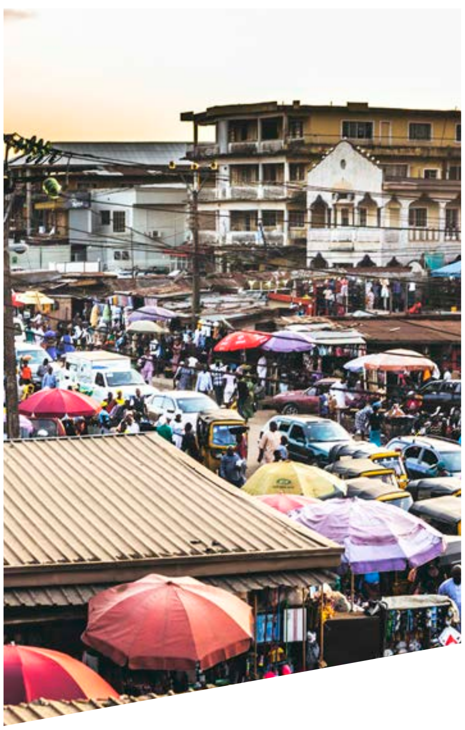
Nigeria

New exchange rate policy for importation of goods into Nigeria



The Central Bank of Nigeria (CBN) introduced a flexible exchange rate system in June 2016, whereby the exchange rate for the Nigerian naira (NGN) will be determined by the interbank foreign currency exchange (forex) market. Under the new exchange rate system, the applicable exchange rate for the purpose of import duty payments will be the daily interbank forex closing rate as published on the CBN website.

The Nigerian Customs Service (NCS), through a Circular issued on 1 July 2016, disclosed that customs duties assessed on goods would be impacted by the new foreign exchange regime after the CBN introduces the flexible exchange rate system.

The NCS Circular clarifies that the calculation of customs duties based on the previous exchange rate of NGN197 per USD will no longer apply. The Circular directs all customs commands to begin to charge duties based on the new foreign exchange regime. According to the Circular, the applicable rate will be the exchange rate at the time of making customs entry.

Implications for importers

Based on the new flexible exchange rate system, the determination of customs duties will vary depending on the interbank forex market, i.e., the prevailing market exchange rate on the date of the transaction. To this end, at the inception of the new policy, the CBN adjusted the benchmark exchange rate from NGN197 to NGN282 per USD, which, in accordance with the Circular, results in about a 40% increase in customs duties that importers are now struggling to meet.

However, because market forces will determine the value of the NGN from now on, adjustments are likely to be made regularly, as the exchange rate will vary depending on the daily market value of the NGN.

Importers may need to evaluate their operations and consider possible arrangements to mitigate foreign currency exchange risks.

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