Managing Tariff Volatility for Supply Chain

August 2019

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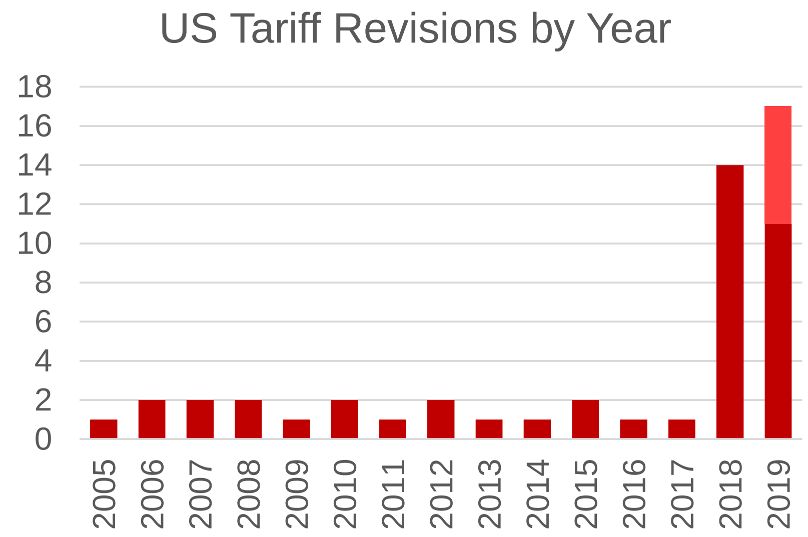
Executive Summary

- ***Tariff Management –*** Companies must understand their contracts, value chain and existing laws to determine if and to what magnitude tariffs apply for them and their suppliers.
- ***INCOTERMS –*** Setting original contract intent aside, the importer typically pays for tariffs unless the terms are DDP.
- ***First Sale Rule –*** Tariffs only apply to the cost of a good, so brokers should not apply tariffs to their markups.
- ***9802 Exemption –*** Tariffs are not added to items manufactured in the US and shipped abroad where it is assembled without modification and returned to the US in a final assembly.
- ***Duty Drawbacks –*** Items that are imported to the US as components and then exported in the form of a final assembly may be eligible for drawbacks.
- ***Value Chain –*** Tariff impact can be mitigated by changing the value chain.

Tariff Revisions

The pace of tariff revisions accelerated in the past two years creating timing and accuracy challenges for supply chain.

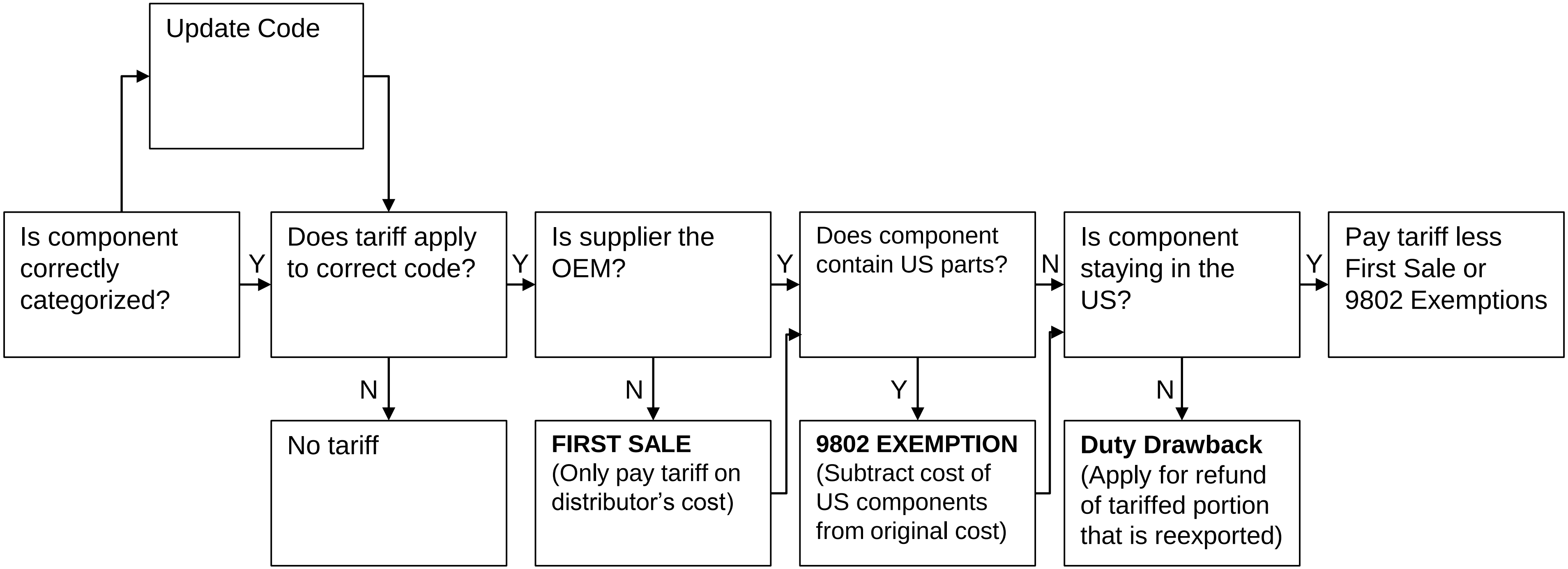
- Each round of tariff revisions requires contract maintenance, value chain reassessment and administrative support
- Revisions have unique effective dates depending on the day product leaves the affected country and when the goods arrive in the US.
- Maintaining accurate and timely tariff data is challenging for buyers trying to manage tariff related price increases from suppliers



Source: United States International Trade Commission

Tariff Exemptions and Drawbacks

Buyers may be able to apply for exemptions depending upon a component's value chain.



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Less Visibility → More Visibility

Condition	Pay Tariff?	First Sale?	9802 Exemption?	Duty Drawback?
HTS code is correct and has a tariff	YES			
Supplier is OEM	YES	NO		
Component from OEM contains US parts and will stay in the US	YES	NO	YES	NO
Component from OEM contains US parts and will be shipped overseas after value add	YES	NO	YES	YES
Component from OEM does not contain US parts	YES	NO	NO	
Component from OEM does not contain US parts and will be shipped overseas after value add	YES	NO	NO	YES
Supplier is distributor	YES	YES		
Component from distributor contains US parts and will stay in the US	YES	NO	YES	NO
Component from distributor contains US parts and will be shipped overseas after value add	YES	NO	YES	YES
Component from distributor does not contain US parts	YES	NO	NO	
Component from distributor does not contain US parts and will be shipped overseas after value add	YES	NO	NO	YES

INCOTERMS

Setting original contract intent aside, the importer typically pays for tariffs unless the terms are DDP.

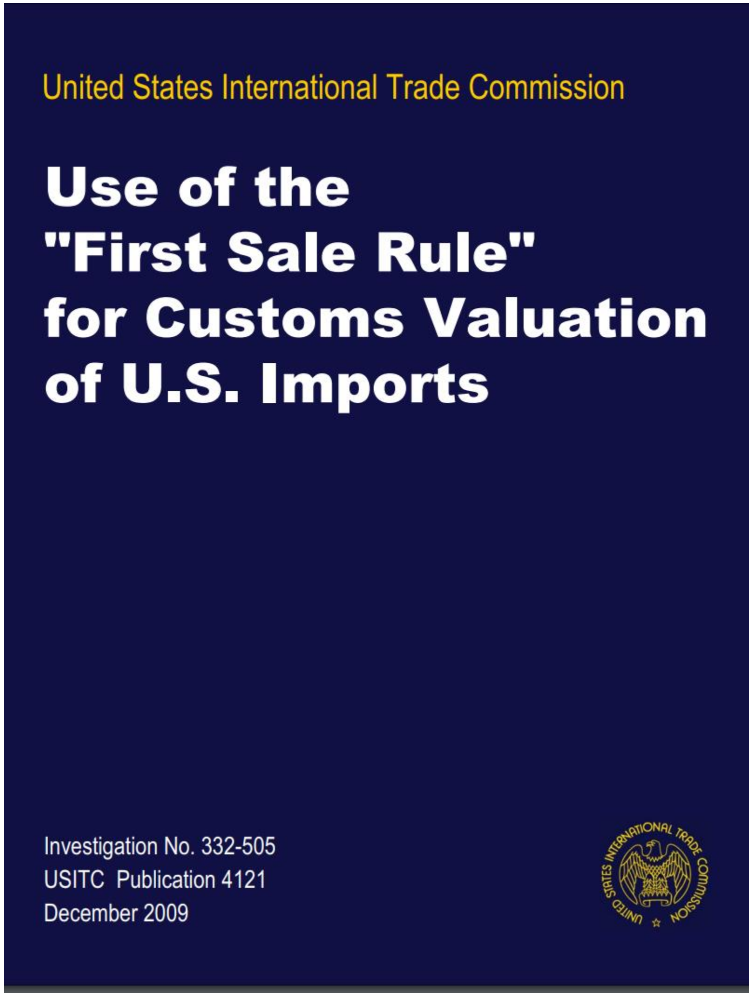
Incoterm	Detail	Tariff Payer
EXW	Ex Works	Buyer
FCA	Free Carrier	Buyer
FAS	Free Alongside Ship	Buyer
FOB	Free On Board	Buyer
CFR	Cost & Freight	Buyer
CIF	Cost, Insurance & Freight	Buyer
CPT	Carriage Paid To	Buyer
CIP	Carriage & Insurance Paid To	Buyer
DAT	Delivered At Terminal	Buyer
DAP	Delivered At Place	Buyer
DDP	Delivered Duty Paid	SELLER

Source: United States Department of Commerce

First Sale Rule

Tariffs only apply to the cost of a good, so brokers should not apply tariffs to their markups.

- Supply chain transparency can enable the use of the First Sale rule to lower the duties paid by importers.
- First Sale rule allows importers, in certain circumstances, to use the price paid in the “first or earlier sale” as the basis for the customs value of the goods rather than the price the importer ultimately paid for the goods (i.e. pay on distributor’s original cost, not final price).
- First Sale rule allows an earlier sale to be used in declaring customs value as long as that sale can be documented as a sale for exportation to the United States and the importer meets all other Customs requirements.


United States International Trade Commission

Use of the "First Sale Rule" for Customs Valuation of U.S. Imports

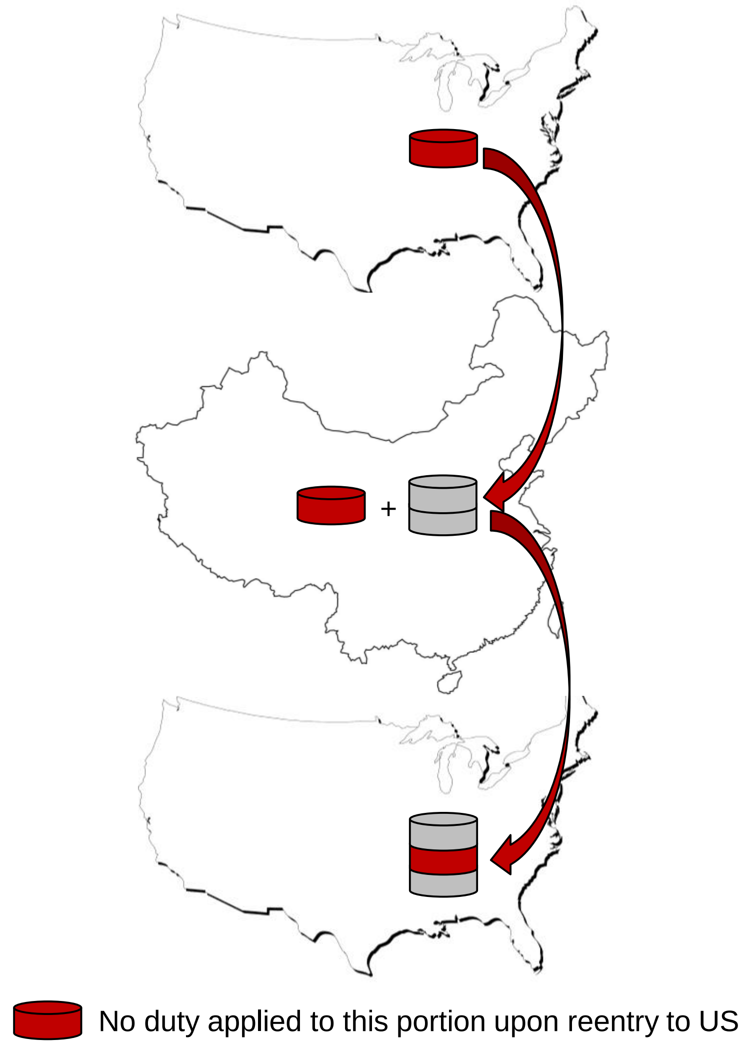
Investigation No. 332-505
USITC Publication 4121
December 2009

Source: United States International Trade Commission

9802 Exemption

Tariffs are not added to items manufactured in the US and shipped abroad where it is assembled without modification.

- The cost of the item from the US should be subtracted from the value payable to customs
- Approved assembly methods include welding, soldering, riveting, gluing, fastening, and laminating

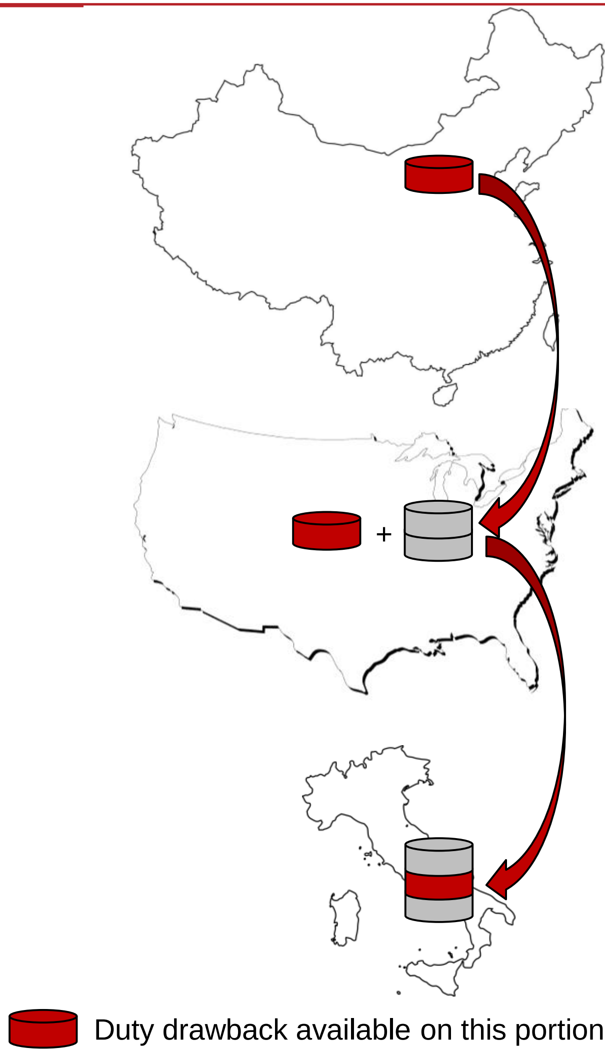


Source: United States International Trade Commission, Journal of Commerce

Duty Drawback

Items that are imported to the US as components and then exported to another country in the form of a final assembly may be eligible.

- Duty drawbacks typically apply to reexports
- Items used for the manufacture of products in the US that will later be shipped abroad may be eligible for a refund, or duty drawback
- An example is if parts are imported from China to go into equipment which is manufactured in the US, then exported to Italy
- Cost of administration and data management needs to be weighed against the potential benefits

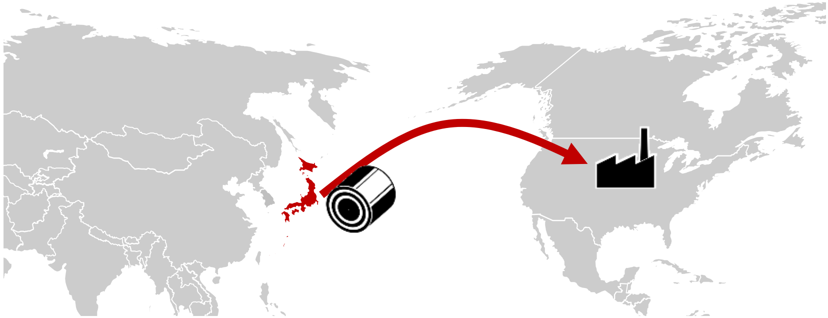


Source: United States International Trade Commission, Journal of Commerce

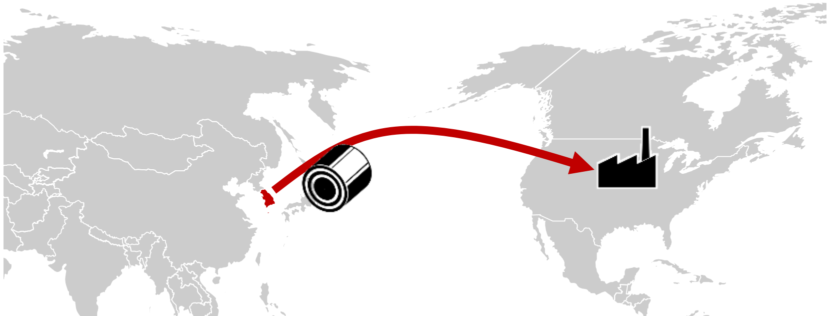
Value Chain Optimization

Several options exist to provide cost savings and footprint alternatives to mitigate the impact of various tariffs.

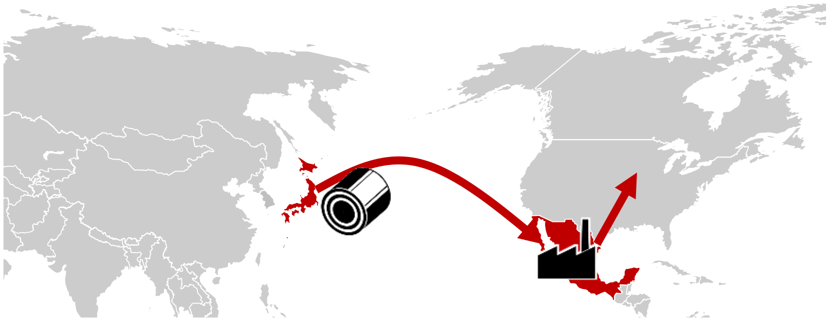
- Material imported and assessed a tariff will have to be paid based on effective dates and changes to trade agreements



- Sourcing from countries of origin not covered by the tariff



- If alternative origins are not feasible, import material into Mexico, fabricate the component and ship into the US without duties.



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Source: United States International Trade Commission, Journal of Commerce

Approach

Managing tariff impact requires data analysis, up to date tariff detail and assessment of the value chain.

Current State Review	Opportunity Quantification	Opportunity Prioritization	Opportunity Execution
▪ Gather impact of tariffs from suppliers and customs brokers ▪ Evaluate current structure of value chain ▪ Audit tariff codes, country of origin and effective dates ▪ Identify historical pricing and tariff impact	▪ Combine tariff impact with other changes cost drivers to set target prices ▪ Identify applicability of drawbacks, 9802 exemptions and First Sale Rule ▪ Audit historical payment of tariffs to identify potential over-payments or missed clawbacks	▪ Rank opportunities ▪ Review with steering group ▪ Develop action plan and assign owners ▪ Define follow-up process before kick-off	▪ Prepare fact-based negotiation agendas ▪ Set target pricing for suppliers ▪ Develop value chain footprint alternatives