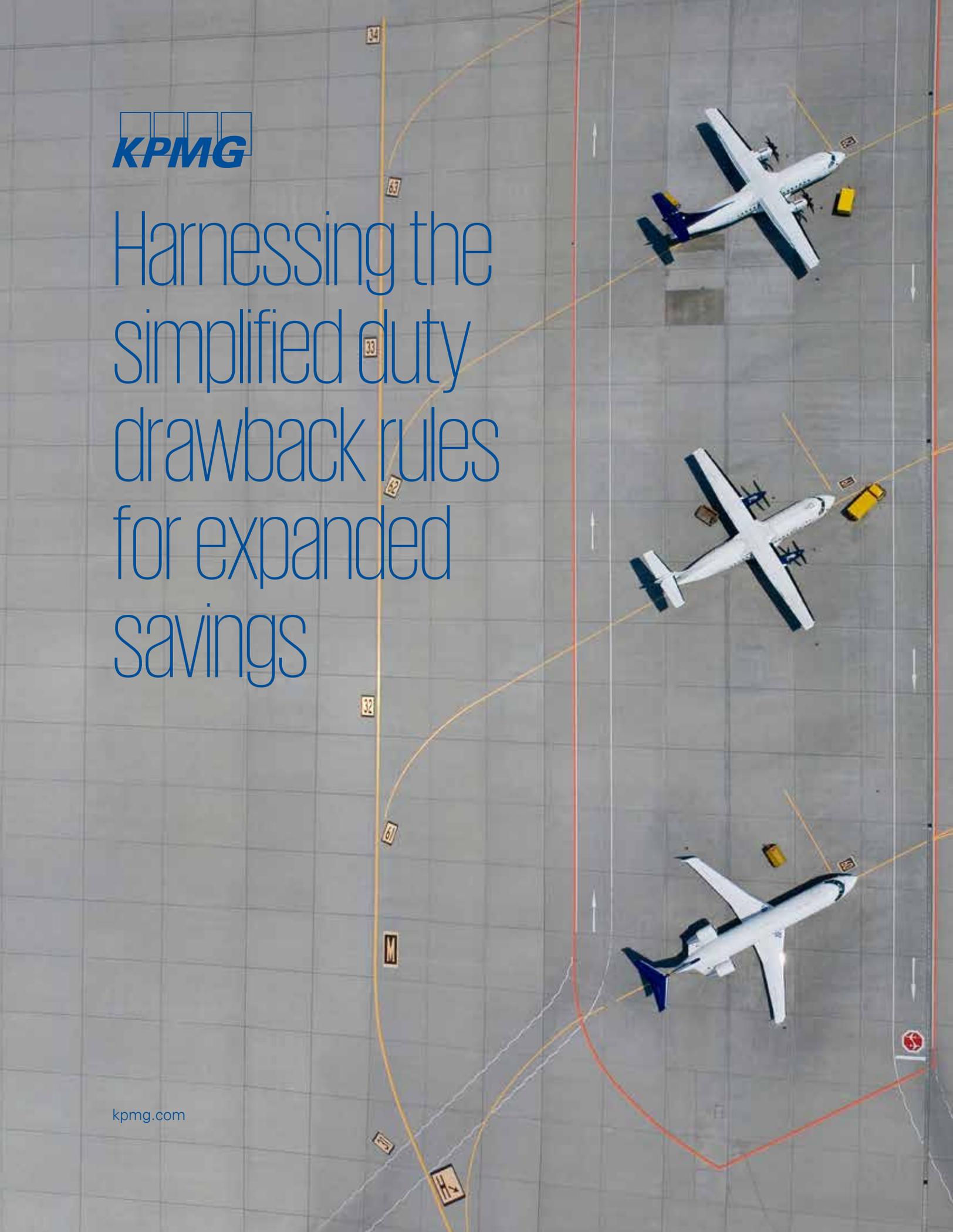




Harnessing the simplified duty drawback rules for expanded savings



As new U.S. duty drawback regulations will go into effect on February 24, 2018, what can you do to prepare? Now is the time for strategic and transactional planning that can result in significant benefits to importers and exporters, and can reduce risk through processes not captured in current controls.



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A photograph of two men in business attire (suits and ties) sitting at a desk. The man on the right is wearing glasses and has a beard. They are both looking at a document on the desk. The man on the left is holding a pen. The background is a bright, out-of-focus office setting with a window.

Background

On February 24, 2016, the Trade Facilitation and Trade Enforcement Act of 2015 (TFTEA) was signed into law. The primary goal of the TFTEA is to encourage international trade through the simplification of U.S. trade regulations. In particular, duty drawback (drawback), a long-standing yet complex trade mechanism allowing for duty refunds on goods imported to the U.S. and subsequently exported, will create opportunities for broader qualification through the easing of product substitution rules, a simplified filing time frame, and modernized record-keeping requirements. These new changes come at a time of further automation of the drawback process for United States Customs and Border Protection (CBP) through the Automated Commercial Environment (ACE), and will transform the way claimants manage their duty drawback programs in the future.

TFTEA and Duty Drawback

Duty Drawback is a program that allows for a refund of 99 percent of duties, fees, and taxes for merchandise imported with duties or fees paid and subsequently exported (or destroyed); this includes finished goods, products used in manufacturing, defective merchandise, and substituted goods.¹

Duty drawback may be claimed, provided the goods qualify as any of the following:

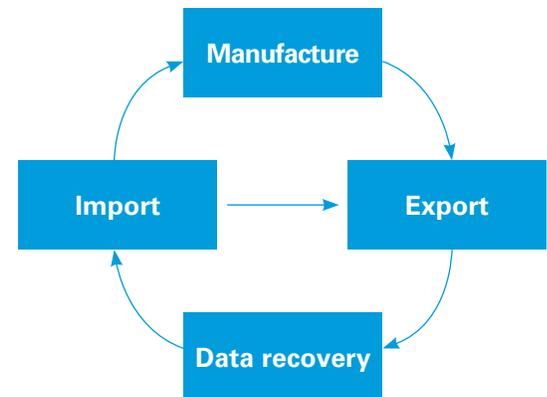
- Manufacturing – Direct Identification
- Manufacturing – Substitution
- Rejected Merchandise
- Unused Merchandise – Substitution
- Unused Merchandise – Direct Identification

In most cases, the exporter may claim drawback...

- Within 3 years after the date of export; and within 5 years after the date of import.

Claimants can request expedited refunds...

- Accelerated payment applications allow for accurate and compliant drawback submissions to be refunded within three weeks of electronic filing.



Types of Drawback

Manufacturing

- This applies when imported goods are used to manufacture an item in the United States that is subsequently exported.
- CBP must approve a claimant's manufacturing scenario prior to filing a refund claim.
- While there are several general rulings that may apply, there are instances where a specific manufacturing ruling is required.

Unused

- This applies when goods are imported into the United States and exported without material changes.
- The exporter of unused goods can facilitate claims through requesting approval from CBP for "Waiver of prior notice of intent to export," a privilege that if not obtained would require notification to CBP prior to each export shipment.
- When substituting one good for another as the basis of a drawback claim, CBP's guidelines for "commercially interchangeable" must be approved by CBP.
- Unlike manufacturing drawback, no rulings are required prior to submission. However, the exporter must provide an application (or waiver) of prior notice to Customs of its intent to export.

The revised TFTEA drawback rules will still generally allow claimants to receive a refund of 99 percent of duty paid on imports subsequently exported under each of the types of duty drawback²; however, the qualification requirements for a drawback refund on an imported product that is "commercially interchangeable" and substituted with that product which is actually exported will be eased, allowing claimants to potentially realize increased opportunities for duty refunds. Simultaneously, a simplified time frame and the modernized record-keeping requirements may provide queues on when to file your next drawback claim, and how companies can expand beyond their current drawback programs.

¹ Drawback opportunities do not apply to shipments to NAFTA countries and Chile per 19 U.S.C. § 1313 (j) (4) and 19 U.S.C. § 1313 (n-o).

² According to 19 U.S.C. § 1313 (l) (2) (B-D) updated with the TFTEA guidelines, refunds for both unused and manufacturing drawback will equal 99% of duties, taxes and fees paid on imported merchandise and for substituted and destroyed goods, the refund will equal 99% the lesser-of the amount of the duties, taxes, and fees attributed to the imported article or the exported/destroyed article.

Trade and Customs impacts

Eased substitution drawback rules

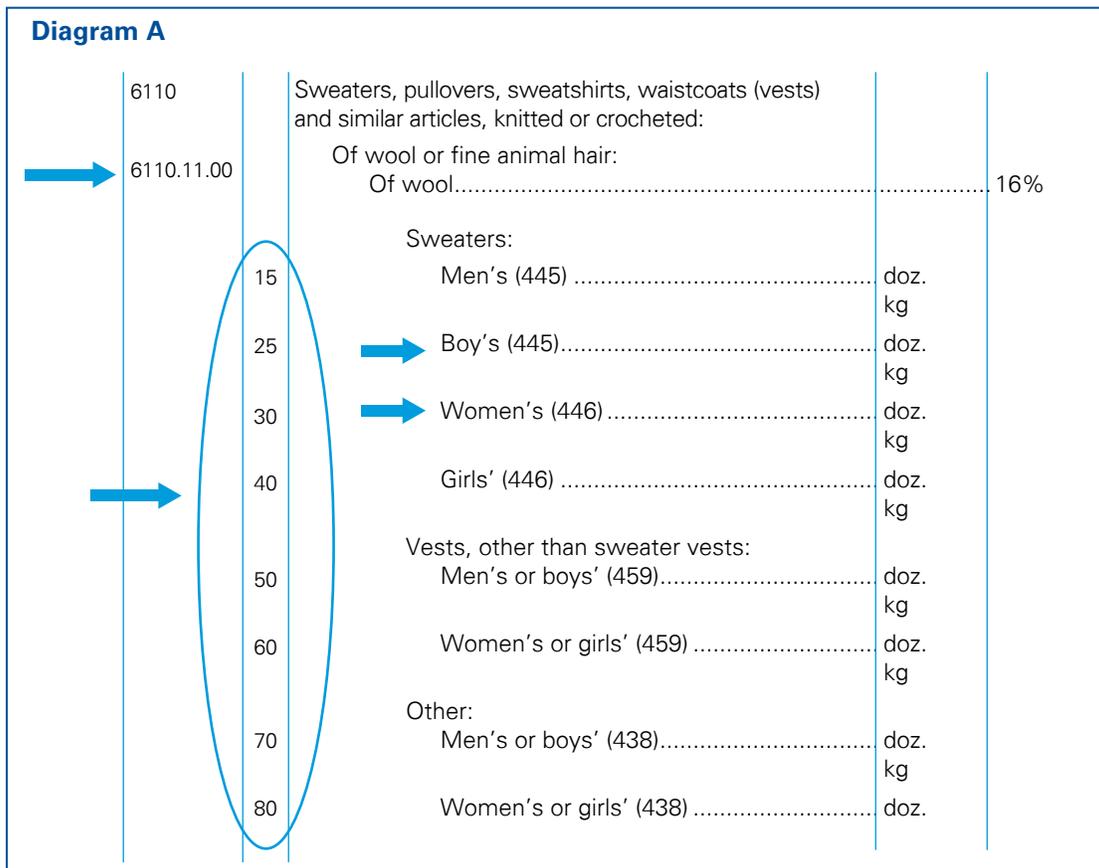
Under the current rules, drawback may be claimed on exported merchandise that is “commercially interchangeable” with imported merchandise. In determining commercial interchangeability, CBP evaluates the “critical properties” of the substituted merchandise. Among others, CBP considers:

- Governmental and recognized industrial standards
- Part numbers
- Tariff classification
- Value³

Currently, prospective substitution drawback claimants may obtain a formal ruling from CBP, or they may submit all required documents to CBP for a commercial interchangeability determination with each individual drawback claim. Both options are fact specific, sometimes subjective, often time-consuming, and may result in a narrow determination of commercial interchangeability.

The new rules ease the commercial interchangeability requirement for substitution drawback by allowing a match to the 8-digit tariff classification (out of the 10-digit classification) to the imported article. As a result, significantly more products will be eligible for substitution drawback. For illustration purposes, consider women’s red wool knit sweaters classified as 6110.11.0030, with a duty rate of 16 percent (per 2017 HTS). Under the current drawback rules, a claimant must match the exported part numbers representing women’s red wool knit sweaters with identical characteristics (size, color, etc.) of the imported, duty-paid item.

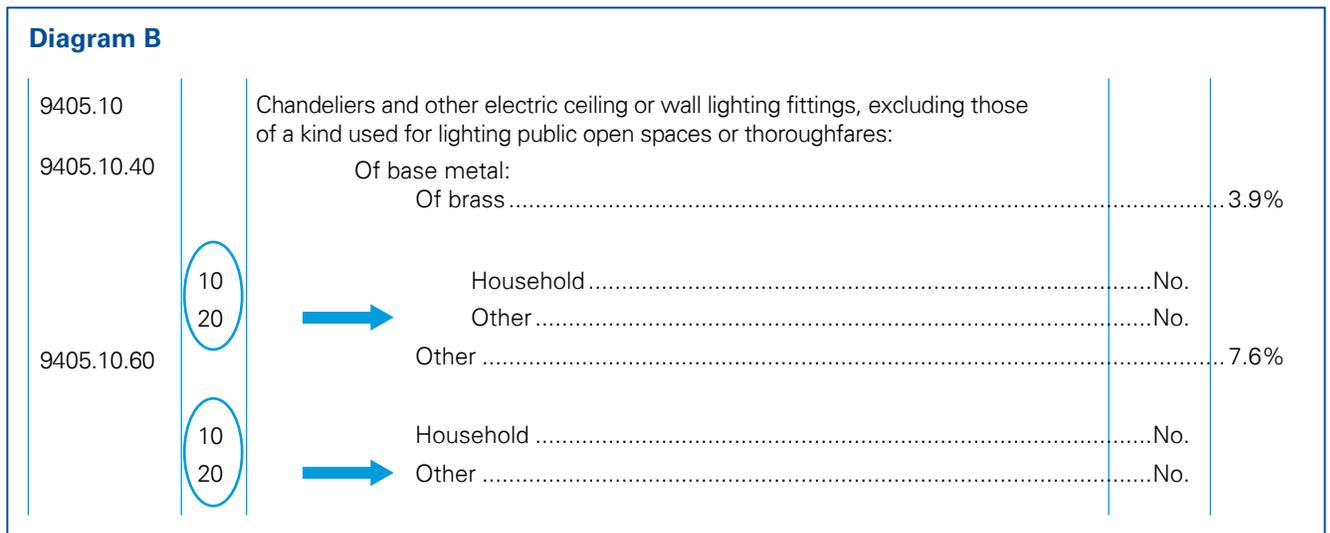
Under the new substitution rules, a claimant may file a substitution drawback claim for exported women’s red wool knit sweaters based on the import of boys’ green knit wool sweaters (as shown in Diagram A).



³ 19 C.F.R. § 191.32(c).

In summary, the change from claiming drawback based on specific part numbers or a subjective “commercially interchangeable” determination by CBP, to a match on the 8-digit tariff classification means that more products can potentially be included in substitution drawback claims, expanding savings opportunities.

However, note that under the new 8-digit classification requirement there is an “Other” clause. If products are classified under a tariff classification beginning with “Other,” (as shown in Diagram B) then a 10-digit classification match is required. This significantly reduces subjectivity while ensuring that goods are commercially interchangeable based on the same principles as the new 8-digit tariff match.



Relevant to the simplified substitution drawback rules, many multinational companies involved in cross-border transactions have been involved in mergers and acquisitions over the past decade. The result is an increase in the number of importing and exporting entities that may be under a corporate umbrella, with each entity often importing and exporting similar products.⁴ An examination of the benefits of the new 8-digit substitution drawback rules may drive companies to take another look at the number of importing and exporting entities under a single corporate umbrella, for both the sake of expanded drawback refunds and efficiencies with trade compliance management. Since CBP rules require that claimants must have possessed the substituted merchandise that was exported or destroyed,⁵ conducting a top-down legal entity analysis of the impact of the new 8-digit substitution drawback rules may help companies identify instances where they may create a larger drawback pool while meeting CBP entry and drawback requirements.

Insights – Eased substitution drawback rules

- Have you conducted a classification review lately? Now more than ever, verifying the accuracy of import and export classifications can mean the difference between obtaining a refund and owing CBP duty. Leveraging systems to maintain and sync import and export classifications can be a key to success.
- Does your company have multiple importers and exporters of record? Consider how managing your importer of record entities can help create a stronger platform for the new substitution drawback rules.

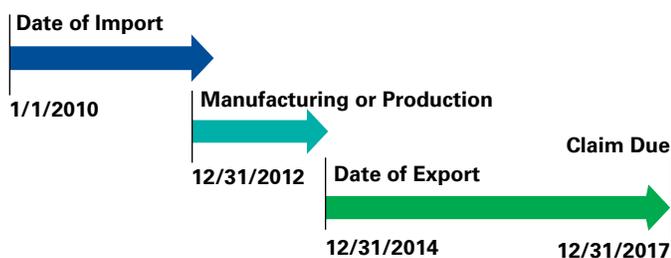
⁴ The party claiming drawback must be either the importer of the imported merchandise or must have received from the party that imported and paid duties on the imported merchandise, a certificate of delivery transferring to that party the imported merchandise, commercially interchangeable merchandise, or any combination thereof. See 19 U.S.C. § 1313(j) (2) (C) (ii) (I)-(II).

⁵ 19 C.F.R. § 191.32 (b) (1) requires that claimant must have possessed the substituted merchandise that was exported or destroyed.

Simplified filing time frame

The time frame for filing drawback claims has been significantly simplified. Previously, manufacturing drawback and unused drawback claims had different and complex, multiyear time lines that were difficult to follow. In an effort to streamline drawback, a new blanket time frame for filing of claims five years from the date of import will be implemented and goods will qualify for duty drawback as long as the export occurs within the five-year time frame after the import (shown in Exhibit 1).

Current State: Manufacturing Drawback



Future State: Manufacturing Drawback



Current State: Unused Drawback



Future State: Unused Drawback



Beginning February 24, 2018, drawback claimants will be able to apply the new rules, including the filing time frame changes. The new rules will allow claimants to file drawback on exports made after they are imported as far back as February 24, 2013. The new filing time frame makes now an ideal time for companies who have never filed drawback to begin identifying their potential drawback opportunities.

Insights – Simplified filing time frame

- **Already benefitting from substitution drawback?**
Consider whether waiting until the eased substitution drawback rules go into effect to file your next claim may help increase your company's overall duty refunds.
- **Have you missed out on drawback for exports in 2013?**
The requirement to file a drawback claim within three years from the date of export would have exports in 2013 fall out of scope. With the new rules, most exports in 2013 will once again be available to companies as the basis for potential drawback claims.

Modernized documentation requirements

Certificates of Delivery

A number of supply chain scenarios can provide an opportunity for drawback, even when you are not the importer of the goods. For example, Company A imports passenger tires into the United States and pays 4 percent duty upon entry. Company A then sells the tires to Company B, also located in the United States. Company B then exports the tires from the United States. Company B has the right to claim drawback on the exported tires; but in order to do so, they must obtain a Certificate of Delivery (COD), a specific form from Company A, indicating that the tires were transferred from Company A to Company B.

The TFTEA modernizes the documentation requirements by removing the need for CODs, and will allow the use of Company A's and Company B's business records to prove transfer of merchandise. This change greatly reduces the administrative burden involved in claiming drawback for Company A. As a result, exporters who currently receive CODs from importers should consider the business documents available to them that can help support the transfer of merchandise from Company A to Company B.

Export records

Claimants realize a constant struggle to provide sufficient proof of export to support drawback claims. While the modernization of documentation requirements associated with exports may sound trivial to some, trade professionals familiar with CBP's drawback desk reviews know that there are challenges associated with obtaining original or even certified bills of lading with the proper export shipment details listed on them to establish sufficient support for export. The exercise oftentimes requires constant and direct communication with freight forwarders, consolidators, airlines, and steamship lines, creating a challenge for an effective drawback program. As a result, claimants may even see their savings reduced or full refunds returned to CBP due to lack of export documentation in support of their claims.

The modernized drawback documentation rules will allow claimants to support exports "through the use of records kept in the normal course of business or through an electronic export system of the United States Government, as determined by the Commissioner of U.S. Customs and Border Protection."⁶ What does this mean for claimants? Export support may be established using Electronic Export Information (EEI) filings submitted via ACE. Not only can these new export documentation rules increase the efficiency of managing existing drawback programs, they can help expand drawback for exports by the U.S. Principal Parties in Interest (USPPIs) that were previously missed.

Insights – Modernized documentation requirements

- **No export records for routed export transactions?** With business documents and EEI filings as support, consider working with your foreign customers to establish support for future exports.

Updated saving calculation requirements

There is an anti-abuse stipulation that imposes a "lesser-of" calculation. The drawback claim will be limited to the lesser of the value of 99 percent of the duties, fees, and taxes paid on imported goods, or the duties, fees, and taxes that would apply to the exported goods if the exported goods were imported. This is aimed to prevent importers from importing low-value goods and exporting high-value goods in order to seek larger refunds. For example, you cannot import an average four-door sedan and export a one-million-dollar sports car with the intent of claiming the duty refund on the sports car. Per the lesser-of rule, the refund would be applied using the lesser of those two calculations; thus, the refund would only include 99 percent of duties, taxes, and fees on the average four-door sedan.

⁶ TFTEA, Section 906 (d) Proof of Exportation.

Insights – Increase your refunds

- By modeling your lesser-of calculation you can perform a value analysis to determine the best inventory methods and claim filing strategies for highest potential savings through the duty drawback program.
- **For example:** Company Z imports two luxury cars and three sedans, but subsequently exports only one luxury car and two sedans. In order to increase savings with the new lesser-of calculation for those vehicles, the trade data and drawback claim should be analyzed in order to pair similarly valued products for filing a drawback claim.
 - **Scenario 1:** One of the two imported luxury cars and two of the three imported sedans are declared with the exported luxury car and two sedans in Company Z's drawback claim.
 - **Scenario 2:** All three imported sedans are declared with the exported luxury car and two sedans in Company Z's drawback claim.

Scenario 1 demonstrates increased savings under the new drawback regulations. All imported goods were paired with similarly valued goods. If Company Z had used scenario 2 for a drawback refund, the lesser-of calculation would have prevented it from obtaining all its potential savings due to the method in which it used to submit its drawback claim.

Obviously, different importers/exporters have varying scenarios and needs; however, proper planning can help discover new and expanded savings opportunities, commonly overlooked.

New filing drawback in ACE

- New ACE filing capabilities will be rolled out in winter/spring of 2017.
- Filing drawback claims will include successful claim acceptance in ACE and the Digital Image System (DIS) submission of all required documents. This should occur within 24 hours of claim acceptance in ACE.
- CBP Form 7551 will be automated; therefore, ACE transmission replaces this step and allows you to process the final claim in ACE. However, the drawback claim cannot be directly submitted to the ACE portal. The claim will still require submission through ABI.
- All ACE drawback claims will be submitted as entry type "47."
- The four current drawback offices and specialists will remain in San Francisco CA, Newark NJ, Houston TX, and Chicago IL.
- There are no changes to the application or desk review processes; all will occur manually and via mail.
- For a list of required documentation for the new duty drawback ACE filing please visit: <https://www.cbp.gov/trade/automated/news/drawback>

⁷ Claimants can request a one-time waiver from the requirement of prior notice of intent to export unused drawback merchandise for past and future exports under 19 C.F.R. § 191.91. Claimants may request Accelerated payment of drawback under 19 C.F.R. § 191.92. Accelerated payment of drawback consists of the payment of estimated drawback before liquidation of the drawback entry.



Managing the drawback program of the future

As discussed, the TFTEA rules will have a big impact on existing and future drawback claims. The new rules will enable companies and their trade professionals to manage duty drawback more efficiently while expanding savings. Companies that are currently filing drawback claims are encouraged to rethink their current program based on the eased substitution rules, simplified time line, and modernized documentation requirements. Companies that have not filed drawback in the past should consider a feasibility analysis to claim drawback under the extended filing time frame of five years from import. However, whether you are an existing claimant or just now considering drawback as a savings opportunity, expanded benefits via the new drawback rules may be missed without proper preparation, diligence, and a review of the drawback options available for each of your supply chains.

Here are seven steps you can take to prepare your drawback program of the future:

Step 1 – Gather records of your existing drawback approvals by CBP for privileges (one time-waiver of prior notice to export and accelerated payment)⁷ and update the information therein with CBP to reflect the company's latest drawback program information.

Step 2 – Conduct an analysis of each supply chain stream that can benefit from drawback. These may include instances where your company is:

- a. Importer of record
- b. Exporter (in a nonrouted export or USPPI in a routed export)
- c. All of the above.

Step 3 – Consider the business partners, customs brokers, and freight forwarders involved in supply chain, the documents they maintain, and their reporting capabilities.

Step 4 – Analyze the impact of the eased substitution drawback rules, the simplified time frame for filing, and the modernized documentation requirements.

Step 5 – Collect and test your reports against your manufacturing, import, and export documents.

Step 6 – Develop a robust drawback compliance program that includes prefiling reviews, a record-keeping protocol, and an approach to drawback documentation auditing.

Step 7 – Evaluate and engage drawback filers to assist with claim submissions with an emphasis on data and documentation quality review and established communication protocol with your team and CBP.

It is important to keep in mind that the steps outlined above take time, and so with one year left before the new rules take effect, there is no time like the present to prepare.



Key takeaways

- The new TFTEA rules will enable companies and their trade professionals to manage duty drawback more efficiently while expanding savings.
- Leveraging systems to maintain and sync import and export classifications can be a key to success.
- Consider how managing your importer of record entities can help create a stronger platform for the new substitution drawback rules.
- Also, consider whether preparing but waiting to submit your next claim at the time the eased substitution drawback rules go into effect may help increase your company's overall duty refunds.
- With business documents and EEI filings as support, consider also working with your foreign customers, in order to establish support for future exports.
- Proper planning can help discover new and expanded savings opportunities, commonly overlooked.



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