Association of Corporate Counsel San Diego

Tariffs and Taxes: Trade Policy Insights

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DLA PIPER

Tariff Landscape

Trump's America First/Reciprocal Trade Policies

President Trump instructed his administration to:

- Investigate the causes of the United States' large/persistent annual **trade deficits** and recommend measures such as **across-the-board reciprocal tariffs** to address
- Assess threats on key domestic industries and propose **industry-specific tariffs** to address (including steel, aluminum, autos, copper, semiconductors, pharmaceuticals)
- Assess the loss of revenues/risks of illegal imports that result from the $800 or less, **duty-free *de minimis* exemption under Section 321** (already phased out for China, and globally on 8/29)
- Consider **China's Permanent Normal Trade Relations** (PNTR) status
- Begin public consultation process for **July 2026 review of the USMCA**

***Agency reports on these issues were due on April 1; various tariff regimes followed**

Legal Authorities and Tariff Actions

International Emergency Economic Powers Act (“IEEPA”)

- Authorizes the president to regulate imports (including impose tariffs) during a national emergency declared under the National Emergencies Act
- Traditionally used to implement US sanctions programs against Iran and other countries
- Precursor to IEEPA used by Nixon to impose tariffs and survived legal challenge
- Can declare national emergency and impose tariffs with immediate effect
- **ACTION: Canada/Mexico Tariffs and China Tariffs pursuant to border/fentanyl emergencies; Reciprocal Tariffs**

The Court of International Trade (CIT) has blocked President Trump from imposing IEEPA-based tariffs, but the U.S. Court of Appeals for the Federal Circuit (CAFC) stayed the CIT’s decision pending appeal

Legal Authorities and Tariff Actions

Section 301 of the Trade Act of 1974

- Can impose tariffs to address any **“unfair” act, policy, or practice** of a foreign government burdening US commerce

- Used during Trump’s first term for **China Lists 1-4A (7.5%-25%)** that were expanded by President Biden

- Following an **investigation** by the Office of the United States Trade Representative (“USTR”)

- **New investigation/implementation could take up to a year (but pending Section 301 cases offer opportunity for faster action)**

- **ACTION: China Maritime/Shipbuilding investigation will result in service fees on China vessel owners/operators at US ports; wide-ranging investigation on Brazil initiated July 15**

Legal Authorities and Tariff Actions

Section 232 of the Trade Expansion Act of 1962

- Can impose tariffs to address imports that **threaten national security**
- Used to impose tariffs on **steel and aluminum** imports during Trump's first term
- Following an **investigation** by the Department of Commerce
- **New investigation/implementation could take up to a year (but pending Section 232 cases offer opportunity for faster action and administration moving fast)**
- **ACTION: Steel/Aluminum reimposed; tariffs on Copper began Aug. 1**
- **Pending Investigations: Processed Critical Minerals, Trucks, Pharmaceuticals and Ingredients, Semiconductors and Equipment, Timber and Lumber; Commercial Aircraft and Jet Engines; Polysilicon; Unmanned Aircraft Systems (UAS)**

Trump 2.0 - Tariffs

President Trump and his administration have announced/imposed the following tariffs:

- **China** 10% reciprocal tariffs; 20% fentanyl tariffs; existing tariffs (301 and general)

- **Mexico and Canada**
  - 25%, 10% on energy resources from Canada, effective March 4, with products entered under USMCA preferential treatment exempted – border emergency **(35% for Canada beginning Aug. 1)**

- **All countries**
  - 10% - reciprocal tariffs (higher country-specific rates beginning August 9); **now 15% on Europe and 50% on Brazil**
  - 50% on all steel/aluminum products
  - 25% on autos and certain parts, or 15% in the cases of Japan and the EU; USMCA autos only tariffed on non-US content; USMCA parts exempted; refunds for US manufacturers/their suppliers; UK negotiated lower rate with quota
  - **50% on copper products began August 1**

- **Default Rule:** tariffs are **stackable unless otherwise indicated** (shifting economic/foreign policy priorities, ongoing negotiations, and new tariff regimes have led to shifts in which tariff regimes apply over others)

- **Trade Deals: UK and preliminary announcements re: Vietnam, Indonesia, China, EU**

Tariff Mitigation Strategies

U.S. Customs and Border Protection (CBP) Requirements

Every "Importer of Record" is required to exercise "reasonable care" to determine and accurately report the following data to CBP (CBP may flag shipments and audit importers to confirm compliance):

- **Classification** for their merchandise according to the Harmonized Tariff Schedule of the United States (HTSUS)

- **Country of Origin (COO)** for their merchandise according to CBP "substantial transformation" rules and precedent

- **Valuation** for their merchandise (usually transaction value unless parties are related)

***These three factors are used to calculate total duties owed to CBP**

***Expanded audits, penalties, and increased scrutiny at the border can results from inaccurate reporting of import data or inaccurate duty payments (5 year SOL)**

Tariff Mitigation – classification

To be ready to address tariff increases and minimize duty liability importers should:

- Review Harmonized Tariff Schedule of the United States (“HTSUS”) product classifications.

  - Assess potential gray areas in HTSUS rules/precedent and tweaks to product characteristics for opportunities to **reclassify** merchandise (i.e., **tariff engineering**)

  - Classification determinations depend on product characteristics/use and:
    - HTSUS **General Rules of Interpretation** and **Explanatory Notes**
    - Existing precedent in the form of **Customs rulings** and **Court of International Trade decisions** regarding similar items

***Applying for a product-specific classification ruling is an option depending on situation and risk tolerance**

Tariff Mitigation – country of origin

To be ready to address tariff increases and minimize duty liability importers should:

- Review the country of origin ("COO") determination for product/supply chain.

  - Assess application of relevant "substantial transformation" rules for opportunities to **shift COO** based on applicable precedent or sourcing/production tweaks (i.e., **tariff engineering or supply chain planning**)

  - COO determinations depend on product characteristics/use and:
    - Applicable "substantial transformation" rules (e.g., name/character/use, essential character, tariff shift)
    - Existing precedent in the form of **Customs rulings** and **Court of International Trade decisions** regarding similar items/supply chains

***Applying for a product-specific classification ruling is an option depending on situation and risk tolerance**

Tariff Mitigation - valuation

Methods of Determining Customs Value

- **Transaction Value (preferred/most common):** price paid or payable; defensible in related-party transactions

- **Transaction Value of Identical/Similar Merchandise:** must be a previously accepted customs value

- **Deductive Value:** the resale price in the US after importation of the merchandise, with deductions for certain items, including profit and general expenses

- **Computed Value (Deductive/Computed Value order can be reversed):** materials, fabrication, and other processing used in production, profit and general expenses, any assists, and packing costs

- **Values if Other Values Cannot be Determined (fallback/hybrid approach):** based on a value derived from one of the previous methods, reasonably adjusted as necessary

Tariff Mitigation Techniques

1. **Classification analysis:** reviewing existing classification determinations may reveal alternative classification or secondary classifications with more favorable duty rate
2. **Changes in product characteristics:** to change classification; tariff engineering; classic example is adding pockets to shirts to shift classification to more favorable HTS code
3. **Country of origin:** analysis to determine potential alternatives; reviewing existing country of origin determinations may reveal reasonable argument for shifting country of origin and lay the groundwork for potential supply chain planning
4. **Supply chain/sourcing shift to change country of origin:** supply chain planning; often CBP precedent reveals key component that are determinative with respect to country of origin – said to grant the product its "essential character"; can shift source of key component to country with more favorable tariff rate to effect change in country of origin to country with lower rate, while keeping the rest of the supply chain intact
5. **Duty Drawback:** if importing then exporting, can recoup 99% of duties upon export; availability depends on tariff regime involved; FTZ operations offer similar benefits
6. **Exclusions/Exemptions:** if/when windows to apply are announced
7. **Customs value assessment:** potential unbundling of costs/services from dutiable value; freight and insurance are excluded from transaction value and other costs/services may potentially be excluded depending on how they relate to the manufacturing processes and the imported finished product
8. **First Sale:** CBP allows importers to use the price paid in an earlier transaction in the supply chain as the customs value if the importer satisfies requirements and submits supporting documentation at the time of entry

International Tax Trends

A Brief History: International Tax Cooperation

- **Starting in 2013, the OECD and G20 began its Base Erosion and Profit Shifting ("BEPS") project to combat tax avoidance by standardizing aspects of global taxation regimes:**
  - Proposed conformity of rules regarding controlled foreign corporation (“CFC”) regimes, anti-hybrid rules, permanent establishments (“PE”), tax treaties and other perceived abuses.

- **In 2016, an Inclusive Framework initiative was spun out of the BEPS project to include developing countries. Currently, 140+ countries have joined the Inclusive Framework.**
  - Two proposals to address tax challenges arising from digitalization:
    - Pillar 1 —Taxing right for market jurisdictions.
    - Pillar 2 — 15% global minimum tax.

A Quick Look Back: International Tax Developments

OECD Base Erosion and Profit Shifting	European Union / Anti-Tax Avoidance Directives	United States Tax Reform
• **Digital Economy** • **Hybrid Mismatches** • Controlled Foreign Company (CFC) • Limitation on Interest Deductions • Harmful Tax Practices • Tax Treaty Abuse • Transfer Pricing • Country-by-Country Reporting • **DEMPE substance**	• Interest limitation rules • **Exit taxation rules** • General anti-abuse rules • Controlled Foreign Company (CFC) rules • **Anti-hybrid mismatch rules** • Shell companies and **minimum substance** • Debt v. equity funding • DAC 6	• **Headline rate reduction to 21%** • Elimination of foreign income deferral system: **Global Intangible Low-Taxed Income** (now Net CFC Tested Income) • Foreign-Derived Intangible Income (now Foreign-Derived Deduction Eligible Income) • **Base Erosion Anti-Abuse Tax**

The “Revenge Tax”

- Section 899 was proposed to target foreign countries that impose the following “unfair foreign taxes” on US companies:
  - Undertaxed profits rules (UTPR) under Pillar 2;
  - Digital service taxes (DSTs); and
  - Diverted profits taxes (DPTs).
- Delegated authority to the US Treasury to identify jurisdictions that impose unfair foreign taxes.
- Increased the tax burden on investors from those countries:
  - (1) Increased rates applicable to:
    - Withholding taxes on dividends, interest, royalties and similar income;
    - Income received by non-US persons that is effectively connected to a US trade or business; and
    - Dispositions of US real property interests.
  - (2) “Super” BEAT: Amendments to increase the rate, eliminate the threshold, etc.

G7 Framework Agreement and Outlook Going Forward

- In June 2025, the US Treasury Department announced a deal with G7 allies to work cooperatively to exclude US companies from certain OECD Pillar 2 taxes imposed by other countries (preliminarily UTPRs and IIRs).
  - Advertised as a “joint understanding to preserve US tax sovereignty.”
- Simultaneously, Section 899 was removed from the US Senate’s bill, which later became law.
- Negotiations still ongoing; no final agreement has been reached.
- Future of Section 899 is still uncertain and it may resurface if international negotiations are not successful.
- Other ways in which the US could respond to UTPRs, DSTs or DPTs:
  - Tariffs
  - Executive Orders
  - Section 891: Doubling of rates of tax on citizens and corporations of designated foreign countries

US Tax Developments

The One Big Beautiful Bill

- “An Act to provide for reconciliation pursuant to title II of H. Con. Res. 14” passed 4 July 2025.
  - Colloquially referred to as the One Big Beautiful Bill (OBBB).
- Introduced broad range of changes impacting both corporate and individual taxpayers.
- Most changes impacting international tax provisions are effective for taxable years beginning in 2026.
- Key provisions:
  - Changes to timing for deducting research and experimental expenditures.
  - Revisions to limitations on deducting interest expense.
  - Refreshers to bonus depreciation.
  - Modifications to GILTI minimum tax on certain foreign earnings.
  - Enhancements to FDII export incentive.
  - Stabilizes the Base Erosion and Anti-Abuse Tax.

Research and Experimental Expenditures

- **Prior Rule:**
  - US-based research and experimental (R&E) expenditures required to be capitalized and amortized over a 5-year period.
  - Foreign-based R&D required to be capitalized and amortized over a 15-year period.

- **New Section 174A**
  - Full expensing of US-based R&E expenditures allowed starting in 2025.
  - Taxpayers may elect to amortize such R&E expenditures over a period of not less than 5 years.
  - Clarified that software development is treated as an R&E expenditure.
  - Non-US R&E still required to be capitalized and amortized over 15 years.
  - Generally favorable, but full R&D expensing may have collateral adverse implications in light of interplay with other provisions.

Interest Expense

- Section 163(j) provides a thin capitalization limit on deductions for net business interest expense with reference to 30% of adjusted taxable income.
- Adjusted taxable income (ATI):
  - For taxable years beginning before January 1, 2022, ATI was generally computed as an EBITDA proxy: earnings before interest, tax, depreciation and amortization.
  - For taxable years beginning after December 31, 2021, ATI was generally computed as an EBIT proxy: earnings before interest and tax.
    - Reduced ATI and therefore the limit on business interest expense deduction.
- OBBB Changes:
  - Beginning in 2025, ATI is calculated with reference to the more favorable EBITDA proxy standard.
    - However, beginning in 2026 taxpayers calculate ATI without regard to CFC inclusions.
  - Generally favorable, but increased interest expense can also have collateral adverse implications under other provisions.

Bonus Depreciation for Business Assets

Asset Expensing Provision	Pre-OBBB	Post-OBBB	Effective Dates
Section 168(k)	20% bonus depreciation as of 2025	Permanently reinstates 100% bonus depreciation, with election to lower percentages	Property acquired after January 19, 2025
Section 168(n)	Not applicable	Bonus depreciation for newly constructed production facilities	Qualifying production property (used to manufacture tangible goods) constructed after January 19, 2025
Section 179	Set the maximum amount of section 179 property that a taxpayer can expense at $1M, reduced by the amount by which the cost of section 179 property exceeds $2.5M	Increases the maximum amount of section 179 property that a taxpayer can expense to $2.5M, reduced by the amount by which the cost of qualifying property exceeds $4M	Property acquired for use in a trade or business and put into service after December 31, 2024

Global Intangible Low-Taxed Income

- The Tax Cuts and Jobs Act was enacted in 2017 and converted US international taxation from a worldwide system with deferral to a current inclusion system with a participation exemption.
    - Exceptions for certain tainted income taxed currently under the Subpart F regime (e.g., portable passive income, income arising from certain related party transactions, etc.).
- Section 951A introduced Global Intangible Low-Taxed Income (GILTI) as a US “minimum tax” on foreign earnings of a CFC.
    - Imposed on CFC’s US Shareholders for CFC tax years beginning after December 31, 2017.
    - Advertised as taxing a CFC’s income from intangible assets, achieved by taxing income above a 10% deemed return on a CFC’s tangible assets.
    - Some relief was provided to corporate shareholders in the way of a 50% deduction on GILTI, which resulted in a GILTI effective rate of 10.5% (21% rate x 50% deduction).
    - Under the TCJA, GILTI deduction was scheduled to decrease to 37.5% (which would have increased the effective tax rate to 13.125%).
    - GILTI foreign tax credits (FTCs) were subject to an 80% allowance.

Global Intangible Low-Taxed Income (cont'd)

- OBBB changes effective after December 31, 2025:
  - Renamed Net CFC Tested Income.
  - GILTI no longer calculated by reducing Net CFC Tested Income by a deemed tangible income return.
  - GILTI deduction reduced to 40%, resulting in an effective tax rate of 12.6% (21% x 60%).
  - FTCs are now subject to an allowance of 90%.
  - Deductions allocated to Net CFC Tested Income are now limited.
    - Interest expense, R&E expenditures and certain other expenses now allocated only to US source income.

Foreign-Derived Intangible Income

- Foreign-derived intangible income ("FDII") provides a deduction (similar to patent boxes) for US corporations to the extent they sell property to foreign persons for foreign use and/or provide services to foreign persons.
  - Benefit reduced by a 10% deemed return to tangible property.
- OBBB changes generally effective beginning in 2026:
  - Renamed foreign-derived deduction eligible income (FDDEI).
  - Deduction reduced from 37.5% to 33.34%, resulting in an effective tax rate increase from ~13.125% to ~14%.
  - As with GILTI, FDDEI will not be reduced by a deemed tangible income return.
  - Interest and R&E expenses are no longer allocated to FDDEI, which should generally increase FDDEI amounts.
  - Calculation of FDDEI now generally excludes gains from sales or dispositions of intangible property and certain other property (effective June 16, 2025).

Base Erosion and Anti-Abuse Tax

- Section 59A was enacted as part of the Tax Cuts and Jobs Act in 2017 and introduced the Base Erosion and Anti-Abuse Tax (BEAT).
  - Imposes an additional tax on certain large corporate US taxpayers that make excess “base erosion payments” to non-US related persons.
- Applies to taxpayers with: (1) average annual gross receipts of at least USD 500 million for the three preceding tax years and (2) deductible “base erosion payments” totaling 3% or more of total deductions (e.g., related-party payments such as interest, royalties, services).
- Imposes a tax equal to 10% of “modified taxable income” in excess of the taxpayer’s regular tax liability reduced by certain tax credits (known as the “modified tax liability”).
  - In computing “modified taxable income” taxpayer cannot deduct otherwise deductible “base erosion payments” from its gross income
- Rate was set to increase to 12.5% in 2026.

Base Erosion and Anti-Abuse Tax (cont'd)

- OBBB changes generally effective beginning in 2026:
  - BEAT rate is 10.5% (for most taxpayers).
  - Section 38 research and other business credits will be permanently considered in the BEAT calculation to generally reduce the BEAT liability.
    - Generally favorable, but may have collateral adverse implications in light of interplay with other provisions.
- Importantly, many of the unfavorable changes to BEAT that were considered during the OBBB legislative process were not included in the final bill (e.g., increase rate to 14% or the "Super" BEAT).

Thank you