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BPE Global Hot Topic – July 2023

Foreign Manufacturing –Truly Outside U.S. Jurisdiction?

This month's topic addresses a common misconception and area of enforcement: foreign manufacturing. Before jumping at the opportunity to save production costs and lower tariff impact, it is important to remember that manufacturing overseas does not necessarily absolve a company from having product subject to U.S. jurisdiction. Read on for a reminder of the considerations prior to ruling foreign-produced items "not subject to U.S. jurisdiction."

There are evident scenarios when an item overseas could be subject to U.S. jurisdiction: it could be a U.S. origin item located outside of the U.S., it could be a foreign national involved in development of an export-controlled U.S.- origin software or hardware. A less-evident scenario would be evaluating a foreign-made item that incorporate U.S. origin commodities at certain value thresholds (or foreign-made commodities that are bundled with controlled U.S. origin software). Another scenario would be to vet foreign-produced items that are either the direct product of specified U.S.-origin software and technology, or foreign-produced direct products of a complete plant or major component of a plant as described in the Export Administration Regulations (EAR). The first scenario vets the Foreign Direct Product Rules ("FDPR") as described under Part 734.9 of the EAR The second scenario evaluates foreign-produced items against de minimis requirements as described under Part 734.4 of the EAR. Though not a comprehensive review of these regulations, this article broadly summarizes these two considerations, and provides operational insight as to how to address and vet within your organization.

Foreign Direct Product Rule

The FDPR are provisions of the EAR that extend extraterritorial coverage of U.S. export controls to certain items produced abroad. If subject under the rules, these foreign products would be considered subject to the EAR, and therefore within the scope of U.S. export controls. There are eight FDPRs. You must always evaluate the FDPR National Security Rule and then any other FDPR that might apply based on various combinations of a product, destination, or end-user scope. The FDPRs are shown in the table below:

Foreign Direct Product Rule	Product (Item or Major Component)	Country/ Destination	End-User
National Security - §734.9(b)	X	X	-
9X515 - §734.9(c)	X	X	-
600-series - §734.9(d)	X	X	
Entity List - §734.9(e)	X	-	X
Russia/Belarus - §734.9(f)	X	X	-
Russia/Belarus - Military - §734.9(g)	X	X	X
Advanced Computing - §734.9(h)	X	X	-
Supercomputing - §734.9(i)	X	X	X

De Minimis

Foreign-produced items with U.S. controlled components exceeding the de minimis levels as described in Part 734.4 of the EAR are subject to U.S. jurisdiction. This regulation is specific and clearly defines items

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for which there is no de minimis level. The overarching reminder with the de minimis rule is to evaluate any foreign-produced item (including bundled software, encryption, etc.) against this sub-part to ensure an item is not captured by its criteria.

Operational Implementation

The simplest method is often the most effective, and as a starting point, we recommend a spreadsheet. Bonus points if you use a product classification chart which may have already vetted a foreign produced item's Harmonized Tariff Code and its export controls. Turn the spreadsheet into a workbook as follows:

- FDPR
  Add a few columns to address FDPR considerations. Identify (using our chart above!), what specific FDPR may apply. For example, if the items produced overseas are destined to Russia/Belarus, your columns will address Part 734.9(f) of the EAR. Flush out columns to address the product scope, others for the destination scope. In the case of a Russian destination, the product scope consists of several parts, one of which is whether an item is listed on Supplement no 6 or 7 of Part 746. Therefore, one column would be: "Is the item described on Supplement 6 or 7?" and then the workbook would be sent to a knowledgeable party to confirm.
- De Minimis
  Following the FDPR vetting, add a few columns to address de minimis rules. A tactic for a scenario where country of origin, classification, and value of the bill of materials (BOM) is unknown at the time of analysis would be to have the knowledgeable overseas party provide total cost of the item and a sum total of all U.S. origin sub-components. Should the percentage of the U.S. subcomponents be close to or exceed the de minimis threshold, focus on assessing those items for whether they would truly be described in the regulation.
- Tariff Engineering
  Consider any foreign-produced items now flagged as U.S. jurisdiction by virtue of FDPR or de minimis in a tariff-engineering mindset. Often deliberated amongst trade professionals as a "dirty word," tariff engineering describes how companies can make small changes in their processes in order to reclassify their final product under a more favorable duty category. Rather than a tariff reduction end-game, it is possible that small changes to processes, such as kitting or sub-assembly strategy could result in a foreign-produced item's jurisdiction as truly foreign.

Our call to action is for you to pressure-test the foreign manufacturing within your organizations. Partner with the overseas technical experts to conduct this vetting. It is essential that you maintain a comprehensive audit trail of your analysis which means that you must exercise the diligence, maintain the workbooks to support the process, reference if and when the regulations will continue to evolve in these areas.

BPE Global is a 19-year-old global trade compliance consulting and training firm. BPE Global is a global trade consulting and training firm. We are committed to changing the way that companies approach global trade compliance. Rather than look at global trade as a means to an end, we strongly believe that it is critical to a company's overall strategy and is a competitive advantage.

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