



MAYER | BROWN

Geographic Risk: Re-Shoring and Diversifying Your Supply Chain



Alex Dell

Partner

+44 20 3130 3121

adell@mayerbrown.com

Steven Tran

Partner

+852 2843 2209

steven.tran@mayerbrown.com

Sydney H. Mintzer

Partner

+1 202 263 3866

smintzer@mayerbrown.com

Yu-Jin Tay

Partner

+65 6327 0252

yujin.tay@mayerbrown.com

Michael Lebovitz

Partner

+1 213 229 5149

mlebovitz@mayerbrown.com

September 23, 2020

Our Presenters



Alex Dell

Partner - London
[Bio](#)



Steven Tran

Partner – Hong Kong
[Bio](#)



Yu-Jin Tay

Partner - Singapore
[Bio](#)



Sydney Mintzer

Partner- Washington DC
[Bio](#)



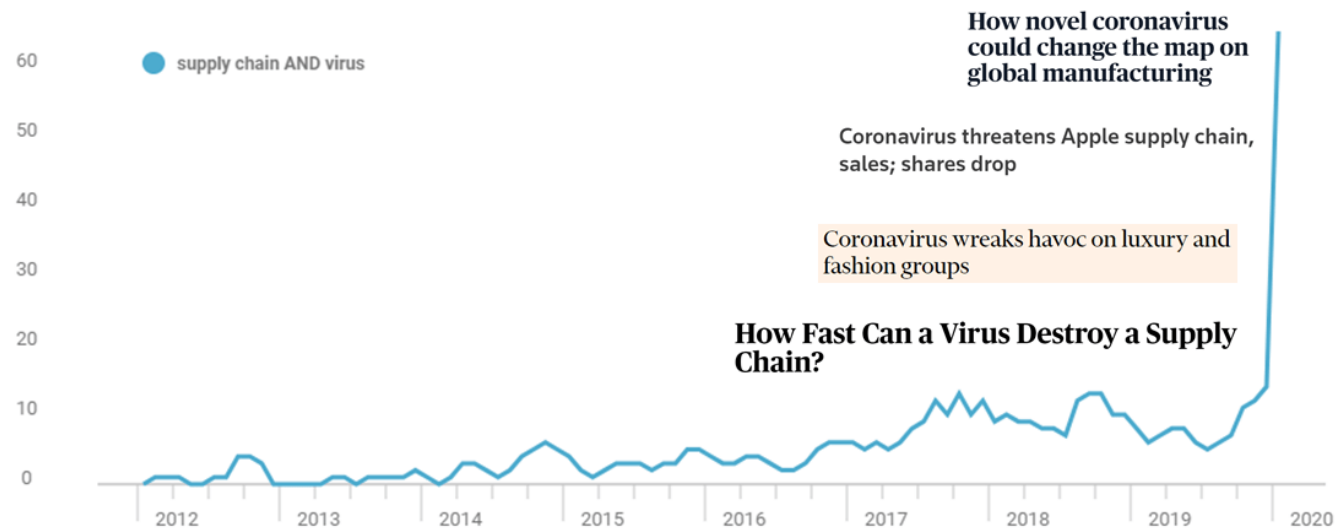
Michael Lebovitz

Partner – Los Angeles
[Bio](#)

In 2020, Supply Chains Made News

Media discussion of **supply chain** and **virus** skyrockets

News Coverage





Expect Further Supply Chain Disruptions

“Since 2000, the value of intermediate goods traded globally has tripled to more than \$10 trillion annually. Businesses that successfully implemented a lean, global model of manufacturing achieved improvements in indicators such as inventory levels, on-time-in-full deliveries, and shorter lead times.

“However, these operating model choices sometimes led to unintended consequences Intricate production networks were designed for efficiency, cost, and proximity to markets but not necessarily for transparency or resilience. Now they are operating in a world where disruptions are regular occurrences.

Averaging across industries, companies can now expect supply chain disruptions lasting a month or longer to occur every 3.7 years, and the most severe events take a major financial toll.”

- *Risk, resilience, and rebalancing in global value chains*, McKinsey Global Institute, August 6, 2020



Supply Chain & Distribution Lawyers Help Clients to:

1. Strengthen supplier and distributor relationships.
2. Manage risk of financially challenged suppliers and distributors.
3. Address potential and actual disputes.
4. Prepare for business continuity and disaster recovery.
5. Anticipate and address customs, tariffs, and other trade regulations.
6. Address compliance risks and advance CSR/ESG goals.
7. Optimize tax efficiency.
8. Protect IP rights.
9. Comply with antitrust and competition laws.
10. Leverage AI, platforms and other technology to innovate and adapt.



Re-Shoring and Supply Chain Diversification Landscape in Asia

- International companies with global supply chains have been seeking lower-cost alternatives to China for years.
- Trend continues of international companies seeking to shift China-based manufacturing operations elsewhere, and global buyers pivoting supplier base away from China – driven by trade war tariffs, disruption caused by pandemic, and anxiety about deteriorating US-China relationship.
- Governments are also talking about re-shoring to reduce dependence on China and other countries as primary source of critical goods.
- Greatest beneficiary of re-shoring activities and supply chain pivot: Southeast Asia.
- Challenges to making the shift away from China – not at all like “flipping a switch.”

Potential Disputes Arising From Supply Chain Diversification

- **Are we seeing disputes arising from supply chain diversification?**
 - Two types of disputes/risks: (1) disputes arising from decoupling former supply chain in original country; (2) disputes associated with forging new supply chain in new country
 - *Disputes from terminating old supply chains (supply-cutting)*
 - Disputes with JV partners or suppliers – such as unilateral termination by invoking fault or non-fault based (e.g., FM) grounds for termination
 - Local exit or downsizing-related disputes with employees (e.g. early dismissal compensation); local disputes with governmental bodies (removing tools/moulds/equipment), IP issues (leaving know-how behind)
 - *Disputes linked to new supply chains (supply-shifting)*
 - Risks associated with any new investment in new jurisdiction – e.g., relationship with new partner, new cultural environment, unfamiliarity with local laws/government, construction and production quality, standards accreditation, IP protection
 - Careful due diligence to mitigate risks
 - Takes time to build capacity outside China in 2nd choice countries
- **Southeast Asia as a potential beneficiary of supply chain diversification away from China?**
 - Trade war (short term) and pandemic (need for resilience) have accelerated trends that were already there
 - Not a zero sum game; China remains competitive and important – we are unlikely to see massive factory moves



US-China Trade War – Avoiding Relocation Pitfalls

- Political risk importing into the United States from China
 - 301 duties
 - Sanctions on designated parties/export controls
 - Forced labor enforcement
- November 2020 presidential election – will it matter?
 - Biden vs Trump on China
 - What policies may change
 - What policies may continue



Country of Origin under U.S. Law

- U.S. law determines country of origin by utilizing the *substantial transformation test*
 - Qualitative test balancing several factors – Where is merchandise substantially transformed?
 - Manufacturing activities in exporting country
 - Costs incurred
 - Source of major inputs
 - Straightforward application – chemical producers
- *Substantial transformation test* is unique among major trading countries, which tend to rely on official government agencies or designees to determine origin



Tax Considerations in Re-Shoring

Three basic questions

- Where do you re-shore?
- Can you leave without material tax costs?
- Is the United States a tax efficient option?



Where Do You Re-Shore?

General considerations

- Low corporate income tax rate
- Tax incentives for manufacturing or other activities
- No or minimal tax costs to repatriate profit
- Stable tax regime
- Can you retain any tax efficiencies in your home country
 - Application of controlled foreign corporation rules
 - Potential global minimum tax regime



Can You Leave?

- Potentially significant tax consequences in changing a supply chain structure
- Most countries will seek to impose some sort of “exit tax” on deemed transfer of goodwill
 - Well developed concept in Europe
 - Expect China to impose similar tax on transfers of supply chains to other countries
 - Potential double taxation if home country does not allow a credit for the exit tax
- Analysis required to determine what “value” is leaving the country



The US as a Re-Shoring Option

- The 2017 US Tax Reform created a number of incentives to bring manufacturing and supply chains back to the US
 - 21% corporate tax rate
 - 50% deduction for “foreign derived intangible income”
- At the same time, disincentives were built into the system to discourage offshoring
 - Immediate taxation of accumulated offshore profits
 - Minimum tax on future offshore profits
 - Minimum tax on payments to foreign related parties



The US as a Re-Shoring Option

- US Tax Reform combined with tax reform on a global level has encouraged some re-shoring back to the United States
- Biden-Harris Tax Plan would further encourage re-shoring and disincentivize offshoring
 - 10% surcharge on “roundtripping”
 - 10% credit for new investment in US manufacturing and jobs
- Global tax landscape is in flux
- Decision making will be increasingly challenging in this unstable environment



Supply Chain & Distribution Practice

- We help clients on supply chain and distribution contracting, compliance and disputes across the globe
- We have 70+ partners with deep experience in supply chains across 15 domestic and international offices
- For more information, visit www.mayerbrown.com and search “Supply Chain”



Americas | Asia | Europe | Middle East

mayerbrown.com

Mayer Brown is a global services provider comprising associated legal practices that are separate entities, including Mayer Brown LLP (Illinois, USA), Mayer Brown International LLP (England), Mayer Brown (a Hong Kong partnership) and Tauil & Chequer Advogados (a Brazilian law partnership) (collectively the "Mayer Brown Practices") and non-legal service providers, which provide consultancy services (the "Mayer Brown Consultancies"). The Mayer Brown Practices and Mayer Brown Consultancies are established in various jurisdictions and may be a legal person or a partnership. Details of the individual Mayer Brown Practices and Mayer Brown Consultancies can be found in the Legal Notices section of our website. "Mayer Brown" and the Mayer Brown logo are the trademarks of Mayer Brown. © Mayer Brown. All rights reserved.