

UNDERSTANDING THE US-CHINA TRANSSHIPMENT ISSUES FROM A MALAYSIAN PERSPECTIVE

It is a known fact that Malaysia is famous for its ports and strategic location which undeniably attracts investors through import and export activities. It was reported back in 2021 that Port Klang operated efficiently by dealing with an average of 131 ships weekly and taking just 1.7 days to service each vessel which was considered a quick handling rate during the pandemic.[1]

It would in turn not be a surprise why Malaysia has been an ideal location for transshipping activities which has been a growingly interesting concern entangled in trade wars, tariff and legal issues.

Under the **Customs Act 1967**, transshipment is defined as (a) transferring of goods from one vessel or aircraft to another vessel or aircraft; or (b) unloading of goods from a vessel or aircraft and depositing such goods in a customs or licensed warehouse or in a warehouse or other place approved by the Director General, for the purpose of shipment out of Malaysia on that other vessel or aircraft within the jurisdictional area of the same customs office relating to the importation and exportation.

In other words, the goods which arrive from its origin country, regardless of its mode of transportation, will make a stop in Malaysia's customs or licensed warehouse only for it to be shipped out of Malaysia to another destination.

The guidelines of the transit and transshipment procedures are governed under **s.35 Customs Act 1967**. During transshipment, the goods are imported into the country on board a vessel, aircraft, vehicle or a railway carriage to be transported through Malaysia from the place of import in Malaysia to a place of exit in Malaysia for the purpose of export.[2]

The goods are cleared for transit and completed when such goods are cleared and released for another customs procedure approved by the proper customs officer.[3]

Goods moved under transshipment shall reach the destination point as indicated in the declaration and be exported within the period as determined by the Director General upon completion.[4] Transshipment ends before its completion if it is interrupted by certain circumstances such as the goods having been abandoned, destroyed or lost.[5]

Trade War between the USA and China

Quite interestingly, the trade war between the United States of America (“**USA**”) and China has shifted the paradigm of transshipping on this side of the globe. The USA experienced an economic imbalance in 2018, which often happens when, inter alia, a nation's imports exceed its exports.

President of the United States at the time, Donald Trump, imposed high tariffs on commodities coming from China, and in response, China levied a 25% tax on every 100 products coming from the USA. Both nations published a list of planned tariffs on a range of goods during that year and agreed to halt the implementation of any additional trade taxes in December 2018.

The arrangement was extended through 2019, however, the tax rate was raised from 10% to 25% in May 2019 for each \$200 billion worth of imported products from China. In turn, China responded by restricting imports of American agricultural items[6]. The trade war with China has persisted to this day.[7]

Impact of the Trade War

Companies in the USA have been impacted by the increase in import costs and naturally, they have reacted to increase the price of the products they sell. Alternatively, some businesses resort to finding different suppliers outside of China, but this could be more difficult than it appears. With the USA struggling to match its own demand it is forced to import goods from abroad[8].

In recent years, Malaysia, amongst other neighboring Southeast Asian countries, is often targeted as a country used for circumventing the US's tariffs against China. Companies are reportedly using transshipment as a method to avoid high tariffs being imposed.

Chinese goods that are intended to be exported to the US are purportedly not exported to the US directly. Instead, the products would be delivered to Malaysia first before being transshipped to the US.[9]

For instance, one Chinese supplier of steel nails, repackages the products and transships them through Malaysia to hide their Chinese origin[10]. Often to solicitate the process, companies have a partner company incorporated in Malaysia. The Malaysian company receives the goods and immediately ships them to the US. The goods are then regarded as Malaysian goods and are not taxed.[11]

In most circumstances, transshipments are legal. Only when the country of origin has been concealed from the receiving country, would it be considered illegal.[12]

In the steel and aluminium industry, some companies send basic metal to other countries like Malaysia in order to undergo minimal processing before it is exported to the US.[13] Though the goods do not transship from port to port, this very minimal processing still does not amount to the product being categorised as “Made in Malaysia”.

What is the Criteria for the Goods to be Categorised as Made in Malaysia?

One reason why some Chinese companies prefer to employ Malaysia as an intermediary before delivering their goods to the US is because of the country's free trade agreement.

The Regional Comprehensive Economic Partnership (RCEP), which enables the enforcement of free trade agreements between members of the alliance, has been signed by 15 nations. Malaysia and China are also a party to this agreement. As a result, these companies would be able to save costs by first exporting their products to Malaysia without being heavily taxed before delivering them to the US[14].

It is important to note that Malaysia has regulations against document fraud relating to certificates of origin and business that wrongfully declares their goods are produced locally. [15] For instance, when the goods reach Malaysia and the shipping containers are replaced however, the certificate of origin states that it was made in Malaysia even though the products were made in another country entirely.[16]

This is illegal under Section 133 of the Customs Act of 1967 because it involves fraudulent behavior. Under this provision, violators are subject to a maximum fine of RM500,000, a maximum sentence of seven years in jail, or both.[17]

In order to understand the illegality behind transshipping, it is important to understand what is defined as “Manufactured in Malaysia”, “Made in Malaysia” and the certificate of origin that qualifies the goods.

a) Manufactured in Malaysia

Section 3 of the Sales Tax Act 2018

Manufacturing is defined as:

“Manufacturing is the process of changing the organic or inorganic materials manually or mechanically, into a new product by changing the size, shape, composition, properties or quality of the material”.[18]

Section 2 of the Industrial Coordination Act 1975

Manufacturing activity is defined as:

“Manufacturing activity” with means the making, altering, blending, ornamenting, finishing or otherwise treating or adapting any article or substance with a view to its use, sale, transport, delivery or disposal and includes the assembly of parts and ship repairing but shall not include any activity normally associated with retail or wholesale trade.”[19]

b) Made in Malaysia

Made in Malaysia Logo is the recognition given when it is determined that the products are made in Malaysia (country of origin).

The requirements that a company will have to comply with in order to receive the “Made in Malaysia” logo on their product are as follows:

- (i) The said company has to be registered under Companies Commission of Malaysia or other registered bodies;
- (ii) The company must hold a current PBT (local authority) operating license;
- (iii) The company must also possess a license of manufacturing (only if applicable);
- (iv) The goods produced by the company must be involved in some sort of manufacturing process (for manufacturing activity);
- (v) The goods or product must be made or manufactured in Malaysia and have at least 51% local or substance content; and
- (vi) The said company (applicant) is urged to apply to the Malaysian Intellectual Property Corporation for registration of its intellectual property (IP).[20]

c) Certificate of Origin

Certificate of Origin is a document that attests to where products were developed, produced, or manufactured. It is necessary when exporting to nations, when it is requested by the consignee for customs clearance, or when a letter of credit specifies it.

The Certificate of Origin lists the products and includes a declaration from a government agency or other appropriately qualified organization attesting to the products' country of origin.

Manufacturers, exporters, and merchants must be registered with the Companies Commission of Malaysia in order to determine the origin of goods. Products that are:

- (i) 100% locally produced or manufactured in Malaysia;

- (ii) Produced or manufactured in Malaysia using a transformation method that modifies the tariff code categorization at the six-digit level; or
- (iii) Produced or manufactured in Malaysia with at least 25% locally produced components[21]

• **Custom Amendment Act 2019**

s.99D (1) A producer or an exporter may apply for a preferential and non-preferential certificate of origin to the issuing authority.

s.99F (1) - In any declaration of goods imported or to be exported, the importer, producer or the exporter shall give the true and correct origin of the goods declared.

• **Custom Act 1967**

“origin of goods”–

(a) in relation to preferential tariff treatment, means the country in which the goods were wholly obtained, produced or regarded as having been produced according to the applicable rules of origin adopted within the framework of international or regional agreements in force; and[22]

(b) in relation to non-preferential tariff treatment, means Malaysia in which the goods were wholly obtained, produced or regarded as having been produced according to the rules adopted in Malaysia.

• **Custom Act 1967**

Section 35I until Section 35N of the Customs Act 1967 provides for the laws or regulations relating to transshipment that has to be complied with by any individual that wishes to transship goods.

In conclusion, the intricate landscape of transshipment issues between the United States and China, viewed from a Malaysian perspective, underscores the complexities that arise at the intersection of trade wars, tariffs, and legal regulations. Malaysia's strategic location and robust port operations have made it a favoured stopover for transshipment activities, offering potential means for businesses to navigate the challenges posed by trade disputes. In navigating the intricate transshipment landscape, adherence to legal procedures becomes crucial. This is especially important when the US government places the burden on the US company itself to ascertain that the country of origin of the goods it is importing into the United States is in fact from the country stated on the entry forms. It is advisable for US companies to conduct proper due diligence on the Malaysian company before importing products to determine whether the Malaysian company is manufacturing the goods or does it act as a shadow company for transshipment purposes.

It is often good practice to conduct a physical visit of the manufacturing plant before contracting to import. Alternatively, it is advisable to hire local law firms to verify the existence of the company through physical visits, perusing manufacturing related documents and providing written statements to corroborate the information provided by the company itself.

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