HEEDING THE CALL FOR A PREDICTABLE RULE OF ORIGIN

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1. INTRODUCTION

Rules of origin are those laws and regulations that determine the country of origin of goods in international trade. These rules are primarily applied to imported articles that are not wholly grown, mined or produced in a single country. Origin problems have surfaced in the last thirty years with the growth of multiple-party manufacturing and the implementation of country-specific preferential agreements and trade restrictions. Traditionally, origin rules were concerned with determining the country of origin for purposes of tariff classification and fulfilling the marking requirements set out in the Tariff Act of 1930. Currently the rules are used to identify eligibility for special tariff treatment under the Generalized System of Preferences, the Caribbean Basin Initiative, and the United States-Israel Free Trade Area Agreement. Rules of origin also establish United States status for purposes

2 See infra notes 60-66, 71-77 and accompanying text.
of drawback,7 government procurement,8 and United States goods exported and returned.9

Despite the importance of rules of origin, little guidance exists concerning the operation of such rules.10 The most commonly used standard in the United States is the "substantial transformation test."11 Under this test, an article processed in more than one country is considered a product of that country in which it last underwent a substantial transformation. A substantial transformation occurs when a product emerges from a processing operation with a name, character, or use different from that of the product before processing.12 Many statutes and regulations require a substantial transformation for a change in country of origin, but none provides a description of "transformation" or a method of measuring what is "substantial." Court decisions and administrative rulings of the Treasury Department and the Customs Service have given the phrase meaning.13

The substantial transformation test currently in use presents serious problems. It is fraught with inconsistency and unpredictability. Because the test is applied on a case-by-case basis, precedential determinations are made in a variety of fora, based on unique facts, amidst differing political and economic forces. There exist statutory guidelines setting out criteria for identifying a transformation. Court decisions enumerate several criteria under the rubric of substantial transformation, yet assign no consistent weight to them. A court may deem a single criterion sufficient in one case, yet require three or four in another. Similarly, Customs has justified an origin determination in one legal area by reference to principles used in a different area, while dismissing attempts by others to do the same.14

7 See infra notes 67-70 and accompanying text.
8 See infra notes 57-59 and accompanying text.
9 See infra notes 60-66 and accompanying text.
13 Simpson Transcript, supra note 11, 112 F.R.D. at 525. See infra notes 85-164 and accompanying text.
14 Palmeter, supra note 1, at 30-31. Palmeter notes that Congress did not intend for Customs to apply different origin rules for purposes of country of origin marking
Recent court cases highlight the deficiencies of the substantial transformation test and illustrate the need for a standard United States rule of origin to provide definitive and predictable determinations. A report by the International Trade Commission states that a single reliable standard will simplify customs considerations in business planning and reduce chances of trade deflection. Adopting an international origin standard would extend clarity and predictability to governments and businesses worldwide. It would facilitate understanding of country-specific trade information and provide a frame of reference for identifying discriminatory practices.

This Comment explores the need for a uniform rule of origin to replace the currently deficient state of origin rules in the United States. Part 2 focuses on the applications of the principal United States rule of origin, the substantial transformation standard. Part 3 discusses the evolution of the substantial transformation test to its current state of confusion. Finally, Part 4 proposes a standard rule based on the Harmonized System of tariff classification.

2. Applications of the "Substantial Transformation" Test

In the 1908 case Anheuser-Busch Brewing Association v. United States, a unanimous Supreme Court articulated the basic test for determining origin. In its definitive opinion on country of origin, the Court stated that "manufacture implies a change, but every change is not manufacture . . . . [S]omething more is necessary as set forth and illustrated in Hartranft v. Weidman, 121 U.S. 609 (1887). There must be a transformation; a new and different article must emerge, 'having a distinctive name, character, or use.'" This concept of a transformation has become the key element in determining origin. A processing operation must result in a new arti-
cle before a transformation will be deemed substantial.\textsuperscript{22} This requirement of a substantial transformation is incorporated in many contexts where a country of origin must be determined.

2.1. \textit{Country of Origin Marking}

Marking an article imported into the United States with its country of origin was first required by a provision included in the Tariff Act of 1890.\textsuperscript{23} It has been part of every tariff act since that time, including the Tariff Act of 1930 (Tariff Act), which serves as the foundation for current marking laws.\textsuperscript{24} Section 304 of the Tariff Act requires the marking of every imported good in a manner that informs the “ultimate purchaser” in the United States of its country of origin.\textsuperscript{25} The final person in the United States to receive the product in its imported form is usually considered the “ultimate purchaser.”\textsuperscript{26} Customs regulations provide that where an imported article is not the product of a single country, the substantial transformation test determines the country of origin for marking purposes.\textsuperscript{27} A United States manufacturer is considered the “ultimate purchaser” and exempted from the marking requirements, provided the manufacturer substantially transforms the imported product.\textsuperscript{28} Despite the critical role of the substantial transformation standard in origin marking, however, no statutory or regulatory provisions detail the components of a substantial transformation.

\textsuperscript{22} United States v. Gibson-Thomsen Co., 27 C.C.P.A. 267 (1940).


\textsuperscript{25} 19 U.S.C. § 1304(a). The main purpose of the marking statute is to alert the ultimate purchaser to the place of production so that the purchaser may seek out or avoid products of particular countries. Palmeter, \textit{supra} note 1, at 4-5 n.2.

\textsuperscript{26} 19 C.F.R. § 134.1(d) (1988). “The ‘ultimate purchaser’ is generally the last person in the United States who will receive the article in the form in which it was imported.” \textit{Id.} “If an article is to be sold at retail in its imported form, the purchaser at retail is the ‘ultimate purchaser.’” \textit{Id.} § 134.1(d)(3). “If the imported article is distributed as a gift the recipient is the ‘ultimate purchaser.’” \textit{Id.} § 134.1(d)(4).

\textsuperscript{27} 19 C.F.R. § 134.1(b) (1988).

\textit{Country of origin.} ‘Country of origin’ means the country of manufacture, production, or growth of any article of foreign origin entering the United States. Further work or material added to an article in another country must effect a substantial transformation in order to render such other country the ‘country of origin’ within the meaning of this part.

\textit{Id.}

\textsuperscript{28} 19 C.F.R. § 134.1(d)(1) (1988). “If an imported article will be used in manufacture, the manufacturer may be the ‘ultimate purchaser’ if he subjects the imported article to a process which results in a substantial transformation of the article, even though the process may not result in a new or different article.” \textit{Id.}
2.2. Generalized System of Preferences

The Generalized System of Preferences (GSP), established by the Trade Act of 1974, authorizes duty-free treatment of eligible products of designated beneficiary countries. An article must be imported directly to the United States from a beneficiary developing country (BDC) to be eligible for GSP benefits. In addition, the sum of the cost of materials produced in the BDC plus the direct costs of processing must equal at least 35 percent of the appraised value of the article at the time of its entry into the United States. The relevant Customs regulations provide that products of the BDC are those composed of materials: (1) wholly grown, produced, or manufactured in the BDC; or (2) substantially transformed in the BDC into a new and different article of commerce. Because a substantial transformation may occur with less than 35 percent added value, the 35 percent minimum is required to ensure that benefits are conferred on developing countries without stimulating the growth of "pass-through" operations. When the BDC contribution does not reach the 35 percent threshold, Customs provides for a "dual substantial transformation" standard where non-BDC components can be counted towards meeting eligibility requirements.

A dual substantial transformation finding is based on an examination of intermediate processing operations in the BDC. Raw materials or components imported into the BDC must first be substantially tran-
formed into new and different items destined for subsequent manufacturing processes. Subsequent processes must then substantially transform these items into the final product ultimately exported to the United States. Because the raw materials are initially transformed into products of the BDC, their value may be counted toward the thirty-five percent threshold. The Court of Appeals for the Federal Circuit in Torrington Co. v. United States used the dual substantial transformation test. In Torrington, Portugal, a BDC, exported sewing machine needles to the United States. Portugal produced the needles from imported steel wire; the wire's value, therefore, did not apply to the thirty-five percent minimum. The processing of the wire in Portugal added less than thirty-five percent to the needles' value. However, the court conferred GSP benefits when it found a dual substantial transformation. The initial transformation resulted when wire was drawn into needle blanks, while the second occurred when the needle blanks were hardened, holed and sharpened. This finding allowed the full value of the needle blanks to be included in the thirty-five percent total. Torrington illustrates the importance of the substantial transformation test in the GSP context.

2.3. Caribbean Basin Initiative

The recently implemented Caribbean Basin Initiative (CBI) includes a trade measure that designates qualified Caribbean nations to receive duty-free treatment for eligible exports to the United States. Because the CBI's goal of fostering economic growth in underdeveloped countries parallels that of the GSP, the similarity between their respective rules of origin is understandable. As with the GSP, the CBI

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36 764 F.2d 1563 (Fed. Cir. 1985).
37 Id. at 1571-72.
38 Id. at 1568-72.
40 See supra notes 38-37 and accompanying text.
41 See supra note 38 and accompanying text.
42 The origin rules developed for the CBERA are based upon the origin rules for the GSP program. The rules for the CBERA are liberalized for specified beneficiary
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The CBI rules also require direct importation and 35 percent value added. Raw materials imported into a beneficiary country qualify as materials of that country provided they are substantially transformed into a new and different article. The CBI allows for a dual substantial transformation whereby non-beneficiary country goods may count toward the 35 percent threshold. The substantial transformation test has equivalent significance for CBI purposes and for GSP purposes.

countries. ITC 1976, supra note 1, at 7.

43 Compare 19 U.S.C. § 2703(a)(1) (Supp. V 1987) (CBI: “Unless otherwise excluded from eligibility by this chapter, the duty-free treatment provided under this chapter shall apply to any article which is the growth, product, or manufacture of a beneficiary country . . .” with 19 U.S.C. § 2463(b)(2) (1982) (GSP: Duty-free treatment is accorded if the cost of materials and operations is not less than 35%; if all materials are indigenous, then this is easily met.).

44 19 U.S.C. § 2703(a)(1). This requirement, however, is not as strict as that for the GSP. Compare 19 U.S.C. § 2463(b)(1)-(2) (GSP: In order to qualify for the GSP treatment, the eligible product must be imported directly from the beneficiary developing country for which the preference is provided.) with 19 U.S.C. § 2703(a)(1) (CBI: Eligible products need not be imported from the country for which the benefit is provided, but may be imported from any of the designated beneficiary countries.).

45 19 U.S.C. § 2703(a)(1). This requirement, however, is not as strict as that for the GSP. Compare 19 U.S.C. § 2463(b)(1)-(2) (GSP: In order to qualify for the GSP treatment, the eligible product must be imported directly from the beneficiary developing country for which the preference is provided.) with 19 U.S.C. § 2703(a)(1) (CBI: Eligible products need not be imported from the country for which the benefit is provided, but may be imported from any of the designated beneficiary countries.).

46 19 U.S.C. § 2703(a)(1). Customs regulations further mandate that an article will not be deemed to have been substantially transformed “by virtue of having merely undergone simple (as opposed to complex or meaningful) combining or packaging operations, or mere dilution with water or mere dilution with another substance that does not materially alter the characteristics of the article.” 19 C.F.R. § 10.195(a)(1) (1988).

47 19 C.F.R. § 10.196(a)(2) (1988). Whereas Torrington, supra notes 35-37, was a court-manufactured example of a dual substantial transformation for GSP purposes, Customs furnishes its own example for CBI purposes. Example 3 notes:

A raw, perishable skin of an animal grown in a non-beneficiary country is sent to a beneficiary country where it is tanned to create nonperishable ‘crust leather’. The tanned material is then cut, sewn and assembled with a metal buckle imported from a non-beneficiary country to create a finished belt which is imported directly into the United States. Because the operations performed in the beneficiary country involved both the substantial transformation of the raw skin into a new or different article and the use of that intermediate article in the production or manufacture of a new or different article imported into the U.S., the cost or value of the tanned material used to make the imported article may be counted towards the 35 percent requirement. The cost or value of the metal buckle imported into the beneficiary country may not be counted towards the 35 percent value requirement because the buckle was not substantially transformed in the beneficiary country into a new or different article prior to its incorporation in the finished belt.

2.4. United States-Israel Free-Trade Area Agreement

In 1985, Israel and the United States entered into a Free-Trade Area (FTA) Agreement that by 1995 will eliminate tariff and nontariff barriers to trade between the countries. In order to qualify for FTA treatment under the United States-Israel agreement, products must be of Israeli or United States origin. As Congress set out, the United States-Israel agreement includes rules of origin similar to those in the Caribbean Basin Initiative, and requires direct importation and 35 percent value added. Issues of origin are likely to arise with the use of components imported from countries not party to the agreement. Consequently, imported materials are required by the United States-Israel agreement to undergo a "substantial transformation" resulting in "a new and different article of commerce, having a new name, character or use" compared with the material from which it was transformed.

2.5. Government Procurement

Government procurement is the purchase of products by the United States government for its own use. The Buy American Act requires the federal government to give preference to domestically produced goods in its purchases. The Buy American Act propounds two

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49 Agreement, supra note 48, annexes 1, 2. A free trade area is a group of two or more customs territories in which duties and other restrictive barriers to trade are eliminated on all or substantially all trade between the territories on products originating in those territories. See General Agreement on Tariffs and Trade, Oct. 30, 1947, art. XXIV, 61 Stat. A3, T.I.A.S. No. 1700, 55 U.N.T.S. 187.

50 Agreement, supra note 48, annex 3.


52 See supra notes 38-47 and accompanying text for a discussion of the Caribbean Basin Initiative rules of origin.

53 Agreement, supra note 48, annex 3, para. 1(b).

54 Id. at annex 3, para. 1(c).

55 GUIDE, supra note 48, at 23.

56 Agreement, supra note 48, at annex 3, para. 4.

situations where origin determinations must be made. Initially, a determination must be made as to whether or not an article is an "American" product. In order to reduce the discriminatory effect of "buy-domestic" arrangements, the International Agreement on Government Procurement was adopted to allow a waiver of such restrictions for signatory countries. This agreement also requires an origin determination to establish whether an article is a product of a signatory country. The substantial transformation test is used in both instances.

2.6. United States Products Exported and Returned

Specific tariff provisions apply to United States goods exported and subsequently re-imported. If an exported product is returned without being advanced in value or improved in condition abroad, the product enters the United States duty-free. The substantial transformation test figures prominently in three aspects of these goods that are exported and returned. First, United States articles exported for repair or alteration are subject to duty only on the value of the repairs or alterations performed abroad. If foreign processing exceeds the scope of repair and alteration, however, then there is considered to have been a substantial transformation and a duty is assessed upon the full value of the article. Secondly, articles assembled abroad with United States components and returned to the United States are exempt from duty to the extent of the value of the components. Finally, foreign articles or materials may become United States components if they undergo a processing operation in the United States that results in a substantial

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59 An article is a product of a country or instrumentality only if (i) it is wholly the growth, product, or manufacture of that country or instrumentality, or (ii) in the case of an article which consists in whole or in part of materials from another country or instrumentality, it has been substantially transformed into a new and different article of commerce with a name, character, or use distinct from that of the article or articles from which it was so transformed.
62 ITC 1695, supra note 1, at 34.
63 HTS, supra note 60, Heading 9802.00.40.
64 19 C.F.R. § 10.8 (1988).
65 Burstrom v. United States, 44 C.C.P.A. 27 (1956) (the conversion of steel ingots into steel slabs held to be a manufacture beyond the scope of mere alteration), noted in Finance Hearing, supra note 10, at 142.
66 HTS, supra note 60, Heading 9802.00.80 (1988).
2.7. Drawback

A drawback statute provides that when articles manufactured in the United States using imported components are exported, the duties paid on those components shall be refunded as drawback (less one percent). There exist no statutes or regulations defining when an article is manufactured in the United States. However, two prominent court decisions suggest an examination for substantial transformation as the proper standard to apply in such cases. The Supreme Court, in Anheuser-Busch Brewing Association v. United States, held that there must be a transformation into a new and different article. United States v. International Paint Co. subsequently held that a change in either name, character or use as a result of processing can be sufficient to indicate a transformation.

2.8. Tariff Treatment

General headnote 3 of the Tariff Schedules of the United States (TSUS) provides for different rates of duty on imported articles as determined by the country of origin of each article. If a product is not entered on a claim of preference, and is not the product of a Communist country, it is assessed the "most-favored-nation" (MFN) rate of duty. Products of Communist countries are subject to the highest rate.

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66 19 C.F.R. § 10.14(b) (1988). Example 1 of the regulation provides:
A cast metal housing for a valve is made in the United States from imported copper ingots, the product of a foreign country. The housing is a product of the United States because the manufacturing operations performed in the United States to produce the housing resulted in a substantial transformation of the foreign copper ingots.

Id.

68 207 U.S. 556 (1908).
69 Id. at 562.
70 35 C.C.P.A. 87, 93 (1948).
72 See, e.g., Generalized System of Preferences, Caribbean Basin Initiative, insular possessions treatment, United States-Israel Free Trade Area, supra notes 29-56 and accompanying text.
Origin determinations are critical in this context because country of origin affects the rate of duty. A 1984 Court of Appeals for the Federal Circuit case, *Belcrest Linens v. United States*, held that the substantial transformation test applies in determining origin for purposes of tariff assessment.

2.9. Textile Regulations

In March 1985, permanent regulations propounding rules of origin for textiles and textile products were issued pursuant to President Reagan’s request. The Customs Commissioner explained that this regulation was designed “to prevent circumvention or frustration of visa or export license requirements contained in multilateral and bilateral agreements to which the United States is a party in order to facilitate the efficient and equitable administration of the U.S. Textile Import Program.” The regulations employ the substantial transformation standard and provide that a “textile or textile product will be considered to have undergone a substantial transformation if it has been transformed by means of substantial manufacturing or processing operations into a new and different article of commerce.” A definition of substantial manufacturing or processing for textiles is included, but it is not exclusive. Customs has asserted that the criteria for determining

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76 741 F.2d 1368 (Fed. Cir. 1984).
77 Id. at 1371.
82 The regulations further provide:

(2) In determining whether merchandise has been subjected to substantial manufacturing or processing operations, the following will be considered:

(i) The physical change in the material or article as a result of the manufacturing or processing operations in each foreign territory or country, or insular possession of the U.S.

(ii) The time involved in the manufacturing or processing operations in each foreign territory or country, or insular possession of the U.S.

(iii) The complexity of the manufacturing or processing operations

(iv) The level or degree of skill and/or technology required in the manufacturing or processing operations

(v) The value added to the article in each foreign territory or country, or insular possession of the U.S., compared to its value when imported
substantial transformation of imported textiles also apply to such determinations of non-textile products.\textsuperscript{83} Customs claims that the recent textile regulations apply because of their genesis in Customs interpretations of judicial decisions.\textsuperscript{84}

3. Evolution of the Substantial Transformation Test

Despite its application in many contexts, no statute or regulation specifically defines the substantial transformation standard.\textsuperscript{85} Determining substantial transformation is a confusing task for the courts due to the volume of goods in international trade and the variety of processes to which each good may be subjected. It is difficult to discern the point at which a processing operation causes a product to become a new and different article.\textsuperscript{86} Several criteria have emerged through judicial precedent as indicia of a substantial transformation.

3.1. Substantial Transformation Criteria

3.1.1. Lost Identity

United States v. Gibson-Thomsen Co.\textsuperscript{87} held that a substantial transformation occurs when imported articles “are so processed in the United States that each loses its identity in a tariff sense and becomes an integral part of a new article having a new name, character, and use.”\textsuperscript{88} The issue in this case was whether toothbrushes and hairbrushes, comprised of United States bristles and Japanese handles, should be marked as products of Japan.\textsuperscript{89} In the court’s view, the bristles were the product’s essence and the wooden handles’ once-independent identity was subordinated in the final product.\textsuperscript{90}

Chemo Pure Manufacturing Corp. v. United States\textsuperscript{91} considered the origin of tannic acid produced in the United Kingdom from nutgalls grown in China. The court found that the “identity of the nutgalls

\begin{footnotes}
\item[85] 19 Cust. B. & Dec. at 596.
\item[86] Finance Hearing, supra note 10, at 134.
\item[87] Anheuser-Busch Brewing Ass’n v. United States, 207 U.S. 556, 562 (1908), held that for a transformation to result, a new and different article having a distinctive name, character, or use must emerge.
\item[88] 27 C.C.P.A. 267 (1940).
\item[89] Id. at 273.
\item[90] Id.
\item[91] Id. at 273. See Simpson Transcript, supra note 11, at 112 F.R.D. 526.
\end{footnotes}
produced in China has been lost, and a new product with a new name, a new use, and a distinct tariff status has been produced. If an article has lost its identity in merging with another article, a new name, character or use has resulted.93

3.1.2. Producer Good-Consumer Good Distinction

*Midwood Industries, Inc. v. United States*94 held that a substantial transformation results when processing alters an article from one usable solely by the producer, to a consumer-ready product. In *Midwood*, the court held that rough steel forgings, the approximate size of the finished product, were substantially transformed after being trimmed or tapered, beveled, bored, and subjected to other finishing processes to create flanges and fittings for pipes.95 According to the court, the steel forgings could not be used by consumers without processing and such a step was, necessarily, a substantial one.96

*Uniroyal, Inc. v. United States*97 departed from the producer good-consumer good distinction demonstrated in *Midwood*,98 finding that such a shift is not determinative.99 *Uniroyal*, a 1982 case involving attachment in the United States of domestic outersoles to imported shoe uppers, relied primarily on the lost-identity criterion.100

The producer good-consumer good distinction, however, was restored three years later. In *Torrington Co. v. United States*,101 steel wire was imported into Portugal, a GSP country,102 and processed into sewing needles. The need for a dual substantial transformation103 required the wire to be transformed into a product of Portugal, and then for that product to be transformed into needles.104 An initial process converting the wire into needle blanks constituted one transformation,105 while a second operation of sharpening and holing the needle

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92 Id. at 11.
95 Id.
96 Id. at 957.
98 *See supra* notes 93-95 and accompanying text.
100 Id. at 1029. *See supra* notes 87-92 and accompanying text.
101 764 F.2d 1563 (Fed. Cir. 1985).
102 *See supra* note 29 and accompanying text.
105 The initial stage is where wire is straightened, cut to the desired shape, beveled, and drawn to form a needle blank. *Torrington*, 764 F.2d at 1568.
blanks constituted a second transformation. The court found that the needle blanks were fit only for use by a producer, whereas a second stage was required to create a consumer usable item. The importance assigned to this criterion varies with each case, indicating the unpredictability with which the substantial transformation test is applied.

3.1.3. Value Added Standard

The addition of significant value to a product or the incurring of significant processing costs is another standard for gauging substantial transformation. United States v. Murray, held:

[T]he sub-term “substantial transformation” means a fundamental change in the form, appearance, nature, or character of an article which adds to the value of the article an amount or percentage which is significant in comparison with the value which the article had when exported from the country in which it was first manufactured, produced, or grown.

The court noted further that “[t]he adjective ‘substantial’ informs us that the degree of change is to be measured with reference to economic value, and the degree must be very great.” However, suggestions of substantiality were not offered.

The court in Uniroyal, while examining whether an imported article retained its essence or lost its independent identity, also focused on added value. In Uniroyal, Indonesian footwear uppers were imported into the United States for attachment of rubber soles. Because the cost of creating the uppers was significantly higher than the cost of soling them, the court failed to find a substantial transformation. According to the court, a certain percentage of value added is necessary to effect a transformation. No specific percentage, however, was suggested.

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106 Id. at 1571-72.
107 Id. at 1571.
108 621 F.2d 1163 (1st Cir. 1980).
109 Id. at 1169.
110 Id. In this case, the mixing and bagging of Chinese glue in Holland was deemed merely a fraudulent guise to avoid higher duties. No significant value was added to the product in Holland. Id. at 1166-67.
111 See text accompanying notes 87-92.
113 Id.
114 Id.
3.1.4. Comparison of Processing Operations

The concept of a value added standard closely relates to whether the operation claimed to effect a substantial transformation involves minor or major processing. Processing may be differentiated by the amount of labor and level of capital investment required by the process. Uniroyal held that "the attachment of the outsole to the upper is a minor manufacturing or combining process." The court compared the Indonesian manufacturing of shoe uppers with the attachment of soles to those uppers in the United States and found that soling took less skill, time and money. As an assembly operation, this compared with the finishing operation of attaching buttons to a shirt. The court in Murray v. United States similarly found only minor processing in an operation in which Chinese glue imported into Holland was screened for impurities, remixed and bagged.

Texas Instruments, Inc. v. United States held that an assembly process could result in a substantial transformation if the process was a complicated one. The court found that the processing of photodiodes and integrated circuits in Taiwan resulted in conversion into new articles.

3.1.5. Change in Tariff Classification

A change in the tariff classification of an article is also a criterion courts use to determine whether a processing operation results in a substantial transformation of the article. If processing operations in a country result in a change in the tariff classification of the article, then that country will be considered the country of origin. Belcrest Linens v. United States held that a change in a product's tariff classification under the Tariff Schedules of the United States may be considered as a factor in the substantial transformation determination analysis.
Belcrest Linens, bolts of Chinese cloth were cut, decoratively stitched and sewn on the sides after importation into Hong Kong.\textsuperscript{126} The origin determination for the final product, pillow cases, was important because the duty on Chinese products was over two and one half times that for Hong Kong manufactures.\textsuperscript{127} The court found that the pillow cases were substantial transformations of the original Chinese cloth.

3.2. Inconsistent Application of the Substantial Transformation Criteria

The courts have used various criteria in making their substantial transformation determinations, and no single criterion has emerged as the single, uniform test. As a result, international traders must analyze all the factors in arranging business ventures or in deciding whether to bring suit against Customs for an adverse origin ruling. The effects of processing may be determinative in one case, yet ignored in another despite similar factual circumstances.

A Court of International Trade decision, National Juice Products Association \textit{v.} United States,\textsuperscript{128} reversed a prior Customs decision.\textsuperscript{129} Customs had held in 1980 that a substantial transformation would result from blending imported orange juice concentrate with domestic juice, orange oils, flavoring ingredients, concentrates or a combination thereof.\textsuperscript{130} The \textit{National Juice} court agreed with Customs' position\textsuperscript{131} that the process of converting imported concentrated orange juice for manufacturing (COJM) into frozen concentrated orange juice or reconstituted orange juice does not result in a substantial transformation.

The court examined the transition from COJM to frozen concentrated juice and reconstituted orange juice, yet explicitly rejected the producer good to consumer good shift as no longer determinative in light of recent precedent.\textsuperscript{132} The court stated that a party "must demonstrate that the processing done in the United States substantially increases the value of the product or transforms the import so that it is

\begin{itemize}
  \item \textsuperscript{126} \textit{Id.} at 1374.
  \item \textsuperscript{127} \textit{Id.} at 1369.
  \item \textsuperscript{128} 628 F. Supp. 978 (Ct. Int'l Trade 1986).
  \item \textsuperscript{130} C.S.D. 80-162, 14 Cust. B. & Dec. 1002, 1004 (1980). Specifically, a manufacture would result from blending with (a) fresh orange juice, (b) pasteurized orange juice, (c) essential oils and flavoring components, (d) essential oils, flavoring components and water, (e) essential oils, flavoring components and other orange concentrates, and (f) a combination of any of the above. \textit{Id.}
  \item \textsuperscript{132} \textit{National Juice}, 628 F. Supp. at 989-90. For an explanation of the producer good-consumer good distinction, see \textit{supra} notes 93-106 and accompanying text.
\end{itemize}
no longer the essence of the final product.”\textsuperscript{133}

The court found that the Food and Drug Administration’s usage of different names for the products before and after processing carried little weight\textsuperscript{134} and held that the different names referred to the identical substance (orange juice) at different stages of its production.\textsuperscript{135} The Court of International Trade manipulated the tests for substantial transformation to support Customs’ reversal of its prior position.

The \textit{National Juice} case also illustrates another aspect of the unpredictability surrounding this area of international trade. The court noted that “the policies underlying the different statutes [e.g., marking, GSP, drawback] are similar but not identical . . . . Thus, although the language of the test applied under the three statutes is similar, the results may differ where differences in statutory language and purpose are pertinent.”\textsuperscript{136} In making this argument for differing rules of origin, \textit{National Juice} contradicted a Treasury Department view, expressed a year earlier, that “Congress did not intend for Customs to apply one rule of origin for duty and marking purposes and a different rule of origin for the purposes [of textile quotas].”\textsuperscript{137} Another Court of International Trade decision consistent with \textit{National Juice, Yuri Fashions Co. v. United States},\textsuperscript{138} held that sweaters were a product of Korea for quota purposes, but a product of the Northern Marianas Islands for tariff and marking purposes.\textsuperscript{139} Despite these judicial pronouncements, Customs maintained in 1987 that the textile regulations derive from recent caselaw and represent the law applicable in all country of origin decisions.\textsuperscript{140} That same year, however, in \textit{Ferrostaal Metals Corp. v. United States},\textsuperscript{141} a case involving Japanese steel processed in New Zea-
land, Customs argued that the substantial transformation standard must be applied to further the intent of the voluntary steel restraint agreement between the United States and Japan.\textsuperscript{142} \textit{Ferrostaal} ruled against Customs and abandoned the stance taken in \textit{Yuri Fashions} and \textit{National Juice}:

No legitimate purpose is served by employing some other test in order to bring within the terms of the Arrangement steel which the United States has not attempted to restrict. As a practical matter, multiple standards in these cases would confuse importers and provide grounds for distinguishing useful precedents. Thus, using the name, character and use criteria, the Court applies the substantial transformation test in accordance with longstanding precedents and rules.\textsuperscript{143}

The court explicitly found,\textsuperscript{144} contrary to Customs' assertion, that an "essence" test\textsuperscript{145} has not displaced the traditional name, character or use test.\textsuperscript{146}

Despite this language, \textit{Ferrostaal} did not apply a traditional test. If the court did not directly consider the purpose behind the restraint agreement in this case, then its heightened scrutiny of processing operations suggests the decision was written with an eye to the future. Many criteria were compounded, as if to justify a decision adverse to administrative policy. These included: (1) added value,\textsuperscript{147} (2) tariff classification change,\textsuperscript{148} (3) loss of original identity,\textsuperscript{149} (4) capital investment;\textsuperscript{150} process that results in a substantial transformation. \textit{Id.} at 536.

\textsuperscript{142} \textit{Id.} at 538.

Defendant says that 'decisions of the courts hold that the various criteria applied in substantial transformation cases must be considered in light of the objectives of the statute in question . . . . Thus, in this case, where the purposes of the VRA [voluntary restraint agreement] and its statutory foundations is to limit imports of Japanese steel products and to foster the growth of the American steel industry, the nature of the overall changes which occur in New Zealand must be more substantial than when a statute fostering operations in a foreign country are being construed.'

\textit{Id.} (quoting Post-trial Brief of Customs Service at 33).

\textsuperscript{143} \textit{Id.} at 538-39.

\textsuperscript{144} \textit{Id.} at 538.

\textsuperscript{145} Customs argued that a product should be deemed transformed if its essence has changed. This suggestion was based on the court's use of the word "essence" to describe the character of merchandise in \textit{National Juice Products Ass'n v. United States}, 628 F. Supp. 978, 991 (Ct. Int'l Trade 1986).

\textsuperscript{146} See supra notes 19-20 and accompanying text.

\textsuperscript{147} \textit{Ferrostaal}, 664 F. Supp. at 540. The evidence showed a change in value from $350 per ton of steel before processing to $550 per ton after processing. \textit{Id.}

\textsuperscript{148} \textit{Id.} at 541. Full, hard, cold-rolled steel is classified under item 607.83, Tariff Schedules of the United States, while the galvanized steel sheet is classified under item 608.13, Tariff Schedules of the United States. \textit{Id.}.
(5) chemical and mechanical change;\textsuperscript{151} (6) producer good-consumer good distinction;\textsuperscript{152} and (7) evidence of a change in name.\textsuperscript{153} The many qualifications and criteria only serve to decrease predictability and make inconsistency, unintended or otherwise, more likely.

\textit{Superior Wire v. United States}\textsuperscript{154} was decided two months after \textit{Ferrostaal} and held that the Canadian operation of drawing Spanish wire rod into wire was not a substantial transformation.\textsuperscript{155} The court focused specifically on disparities between the Spanish conversion of steel into rod and the Canadian conversion of rod into wire in the areas of labor, capital investment and physical change.\textsuperscript{156} Several traditional criteria and important factors, however, were accorded little weight. \textit{Superior Wire} held that while the criteria of tariff classification, change of name and value added were successfully met, they were not determinative.\textsuperscript{157}

\textit{Superior Wire} presented another apparent departure from accepted standards. In 1977, \textit{United States v. Kanthal Corp.} determined

\begin{itemize}
\item \textsuperscript{149} See id. at 540-41.
\item \textsuperscript{150} Id. at 539. A special furnace is required for the processing. It must heat and cool the steel in a controlled fashion, using twenty zones correlating to time and temperature patterns. Id.
\item \textsuperscript{151} Id. at 540. The steel is transformed from a brittle product into a ductile one with permanent chemical changes resulting in corrosion-resistance. Id.
\item \textsuperscript{152} Id. at 541. The court noted that heat treatment is necessary to increase the utility of cold-rolled steel and cited Midwood Industries, Inc. v. United States, 313 F. Supp. 951 (C.C.P.A. 1970). Id. See also supra notes 93-95 and accompanying text.
\item \textsuperscript{153} \textit{Ferrostaal}, 664 F. Supp. at 541. "[T]he satisfaction of the name criterion in this case lends support to plaintiffs' claim. The witnesses for both parties testified that the processing . . . results in a product which has a different name . . . ." Id.
\item \textsuperscript{154} 669 F. Supp. 472 (Ct. Int'l Trade 1987), aff'd, 867 F.2d 1409 (Fed. Cir. 1989). In \textit{Superior Wire}, 2,700-pound coils of wire rod from Spain were uncoiled and cleaned during passage through a mechanical de-scaling machine. The machine removed a hard oxide crust through reverse bending of the rod. The rod was then coated with lubricant and rust preventative before the rod coils were joined by butt-welding to make feeding the drawing dies easier. Butt-welding generally involves annealing across the joint to ensure uniform composition. Two die passes were usually used to create a 2,000-pound coil of wire. Cross-sectional area was reduced by 30%, the wire became less ductile, and tensile strength rose 30-40% after the drawing. \textit{Id.} at 474.
\item \textsuperscript{155} Id. at 480.
\item \textsuperscript{156} Id. at 478.
\end{itemize}

The fifteen percent added value figure for the wire standing alone does not pull in either direction, but related concepts, including the amount of labor required to accomplish the change and the capital investment required relative to that required to produce the entire article, are also relevant to a determination of whether the change involves minor processing. Id.

\textsuperscript{157} This holding was issued despite a name change and different treatment by people in the steel and wire industries, different tariff classification, and a finding of at least 15% value added. The court noted that such standards can be supportive of a transformation determination, but are not dispositive. Though these three standards were met here, they were neither dispositive, nor supportive. \textit{Id.} at 478-79.
that wire rod and drawn wire were not the same product.\textsuperscript{168} Relying almost exclusively on the processing comparison criterion of Uniroyal,\textsuperscript{159} however, the court in \textit{Superior Wire} found the transformation described in \textit{Kanthal} to be a minor one.\textsuperscript{160}

Finally, the \textit{Superior Wire} court had to address the precedential value of \textit{Torrington},\textsuperscript{161} which also involved processing of metal articles without combination or further assembly. In attempting to distinguish \textit{Torrington}, the \textit{Superior Wire} court found that "[a]lthough some of the processes involved here are the same as those involved in the second phase of \textit{Torrington}, there is no clear change from producers’ to consumers’ goods."\textsuperscript{162} However, the processes involved in drawing rod into wire are far more similar to the first stage of \textit{Torrington} where wire was drawn into needle blanks.\textsuperscript{163} In that stage there was no question of a producer good/consumer good distinction. The court noted that after the wire was drawn in the first stage of \textit{Torrington} it really could only be used for making needles.\textsuperscript{164} Similarly, the court found that wire rod has little use except for making wire.\textsuperscript{165} The court's failure to resolve or explain its different treatment of parallel situations reinforces the uncertainty facing those in international trade.

These cases stand for the proposition that courts have inconsistently applied the various criteria in making the standard of substantial transformation determinations. Criteria may be mixed, their respective weights may be reapportioned, and they may sometimes be disregarded entirely.

4. Toward a Uniform Rule of Origin

Any proposed uniform rule of origin must comport with the purposes of such rules in general and eliminate the deficiencies of those presently used. Because origin rules must be applied in such a range of contexts,\textsuperscript{166} consistency and ease of application are of primary con-

\textsuperscript{158} 554 F.2d 456 (C.C.P.A. 1977). While this case did not require a substantial transformation determination, the court's discussion of the processing noted that the manufacturer had taken all the steps necessary to warrant the product being imported as wire. \textit{Id.} at 461. The relevance to \textit{Superior Wire} is striking, particularly in light of the fact that the rod in \textit{Kanthal} was drawn once, while that in \textit{Superior Wire} was drawn twice. \textit{Superior Wire}, 669 F. Supp. at 474.

\textsuperscript{159} See supra notes 115-18 and accompanying text.

\textsuperscript{160} \textit{Superior Wire}, 669 F. Supp. at 480.

\textsuperscript{161} See supra notes 35-37 and accompanying text.

\textsuperscript{162} \textit{Superior Wire}, 669 F. Supp. at 479.

\textsuperscript{163} See supra note 37 and accompanying text.

\textsuperscript{164} \textit{Superior Wire}, 669 F. Supp. at 479.

\textsuperscript{165} \textit{Id.} at 474.

\textsuperscript{166} See supra notes 19-84 and accompanying text.
cern. The need for a uniform rule is underscored at the domestic level by the difficult task our courts face when making substantial transformation determinations. The variety of manufacturing processes, the volume of case-by-case determinations and the flexibility of criteria for making such determinations have rendered predictability impossible. Traders are as uncertain of business planning as Customs is of administering the rules. From an international perspective, the divergence of substantial transformation criteria distorts the accuracy of statistical collection. There are problems with calculating value added because exchange rates fluctuate. Processing expenses may differ significantly from disparity of labor costs among nations. Countries may easily differ as to what is an important manufacturing operation and what is not.

In the quest for uniformity and predictability, primary consideration must be given to a rule of origin that eliminates subjectivity. It must not be susceptible to the wide interpretation of the substantial transformation standard. This Comment has discussed changes in tariff classification under the Tariff Schedules of the United States as a criterion indicating a substantial transformation. Some cases have suggested that the existence of such reclassification is not dispositive. A classification-based origin rule must be adaptable, however, to be viable as a uniform rule of origin. Because a system geared to one country's tariff schedules would likely confer benefits on the nation able to change the schedules, a more equitable approach would be one based on an internationally accepted system of classification.

4.1. The Harmonized System

The idea of an internationally accepted tariff basis is over fifty years old. The Harmonized System is an international standard of

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167 The ITC reported that the four critical elements of a standard origin rule are uniformity, simplicity, predictability and administrability. ITC 1976, supra note 1, at 12-13.
168 Id. at 13.
169 See supra notes 123-26 and accompanying text.
171 The notion of a common basis for customs tariffs was initiated by the 1927 World Economic Conference. The Geneva nomenclature resulting from that conference was completed in 1931, revised in 1937, and used as a basis for the Brussels Tariff Nomenclature (BTN). In 1950, the Customs Co-operation Council (CCC) was established by a convention of various trading nations. The BTN was approved by the CCC in 1950, revised in 1955, and renamed the Customs Co-operation Council Nomenclature (CCCN) in 1959. A CCC report, released in 1973, concluded that the development of a uniform commodity classification system had become essential for the long-term interests of international trade. This report culminated in 1983 with completion of the harmonized system and an international convention for its implementation. The
six-digit numerical classification codes designed to make tariff nomenclature uniform worldwide.\textsuperscript{172} The Harmonized System attempts to organize tariff items into a hierarchical framework reflecting increasing technical sophistication and economic effort.\textsuperscript{173} This aim closely parallels that of substantial transformation determinations, where products are examined in light of character changes and economic factors. The Harmonized System covers nearly ten thousand different items in its twenty-one sections. These sections are divided into ninety-nine chapters which are, in turn, subdivided into headings.\textsuperscript{174} As one recent article explains:

"By its nature, a subdivision cannot provide for an item outside the scope of the entry being subdivided. Furthermore, if an entry is subdivided, the subdivisions must exhaust the entry. And finally, each subdivision at the same level must be mutually exclusive. Thus, the hierarchical structure of the nomenclature assists in drawing the reader to the most specific tariff item.\textsuperscript{175}"

In addition to its logical framework, the Harmonized System will be more modern than the current TSUS, will utilize the same system as the current TSUS for imports and exports, and will provide a greater degree of certainty.\textsuperscript{176} At present, Customs is prepared to implement the Harmonized System\textsuperscript{177} as soon as Congress authorizes it do so.\textsuperscript{178} A universally accepted and uniform nomenclature, like the Harmonized System, would provide an excellent base upon which to build a new definition of national origin.


The United States has participated in the development of the Harmonized System since its inception. Participation was based on the expectation that the Harmonized System would replace the Tariff Schedules of the United States. Id. at 21 (statement of Francis W. Foote, Esq.) [hereinafter Foote Statement].

\textsuperscript{175} Morgan & Wilson, supra note 171, at 710.

\textsuperscript{176} Id.

\textsuperscript{177} Id.


\textsuperscript{177} HS Hearing, supra note 170, at 3 (statement of Christopher Marsich, Director of Tariff Affairs, Office of the United States Trade Representative).

4.2. Harmonized System "Plus"

The Harmonized System's logical and definitive framework is well-suited to form the basis for an origin guide. Its status as an international nomenclature and its codified nature would translate into wide acceptance and predictable administration. While the Harmonized System alone might not be a complete solution, incorporating product or sector-specific amendments could provide for a successful and objective rule of origin.

One disadvantage associated with using a change of tariff heading as an indication of a new country of origin is the difficulty of finding a nomenclature commonly applied at the international level.\(^\text{179}\) Though the Harmonized System is unequivocally international, some argue that it was not drafted with rules of origin in mind.\(^\text{180}\) If the system were put into such use, however, modifications would surely be forthcoming. It would evolve and develop its particular character as nations learned to utilize its classifications most efficiently.\(^\text{181}\) According to the International Trade Commission (ITC), the shortcoming of such a classification-based rule is that it does not function effectively with regard to assembly-oriented products.\(^\text{182}\) For example, components imported from one or more countries could be assembled in a simple operation in the country of export and would be considered products of that country if a change in classification results.\(^\text{183}\) It is precisely for this reason that the Harmonized System alone would not be a panacea. Rather, specific rules would be drafted to flesh out the gaps that remain. If an assembly operation is at issue, two or more tariff heading shifts might be required. Perhaps the components alone would have to undergo a classification shift; or, the article composed of the parts might have to undergo a shift.

Because a rule based on the Harmonized System plus specific amendments would focus on tariff provisions, the rule would rarely need to examine particular manufacturing operations or processes.\(^\text{184}\) This rule would remedy one of the problems presented by the uniform

\(^{179}\) ITC 1976, supra note 1, at 18-19.

\(^{180}\) Id.

\(^{181}\) In the ITC report on standardization of rules of origin, the solution offered for a uniform rule is one based on a list of processes for an enumerated product. Specifically, origin would be conferred on the last country where one of the enumerated processes took place. The Commission noted that such a system would be subject to updating, while also evolving its own discipline. ITC 1976, supra note 1, at 22. It is obvious that no system will operate flawlessly until there has been a “break-in” period.

\(^{182}\) ITC 1976, supra note 1, at 19.

\(^{183}\) Id.

\(^{184}\) Id.
rule suggested by the ITC.

The Commission recommends a standard based on processing requirements where origin would be conferred on the last country in which an enumerated process was applied to the particular product involved. However, the Commission admits the validity of concerns that, under this rule, separate shipments of a specific article made by different processes might be given different origins. This problem would not arise under the Harmonized System Plus standard, which is concerned with product, not process.

The codified nature of the underlying nomenclature and its nearly universal acceptance among trading nations permit a greater degree of flexibility. Whereas flexibility in the substantial transformation criteria equates to unguided formlessness, the objective and mechanically precise character of the Harmonized System renders it capable of sustaining exceptions and special rules without losing its identity.

5. Conclusion

The ITC has suggested four critical elements of rules of origin: uniformity, simplicity, predictability, and administrability. Each of these elements is lacking in the present substantial transformation test for determining country of origin. The Courts and the Customs Service apply it inconsistently. The judicial review process that is often necessary consumes considerable time and money. The deficiencies of the substantial transformation test as a viable standard have resulted in the emergence of several secondary criteria. These have only heightened the confusion by providing factors that can be either relied upon or ignored, depending on the desired outcome of the case.

The Harmonized System of tariff classification is an international tariff nomenclature already used by most major trading nations. Its codified structure is the solution to the search for a uniform rule of origin. Adopting a rule that an article is a product of the nation where it last underwent a change in Harmonized System classification would eliminate subjectivity from origin determinations. Because all ports of entry into the United States would follow the same nomenclature, administrative rulings would be more uniform. Other nations would be able to predict Customs determinations because they would already have a working understanding of the same international system. Any problems associated with the nomenclature could be worked out at in-

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185 Id. at 20.
186 Id.
international conventions. While it would take time for the system to work its way into all the various trade sectors, that time would be amply compensated by a generous return of clarity and consistency in the realm of country of origin determinations.