

Proposed Rules of Origin Changes to the Rules of the Game

Presentation to the ICPA

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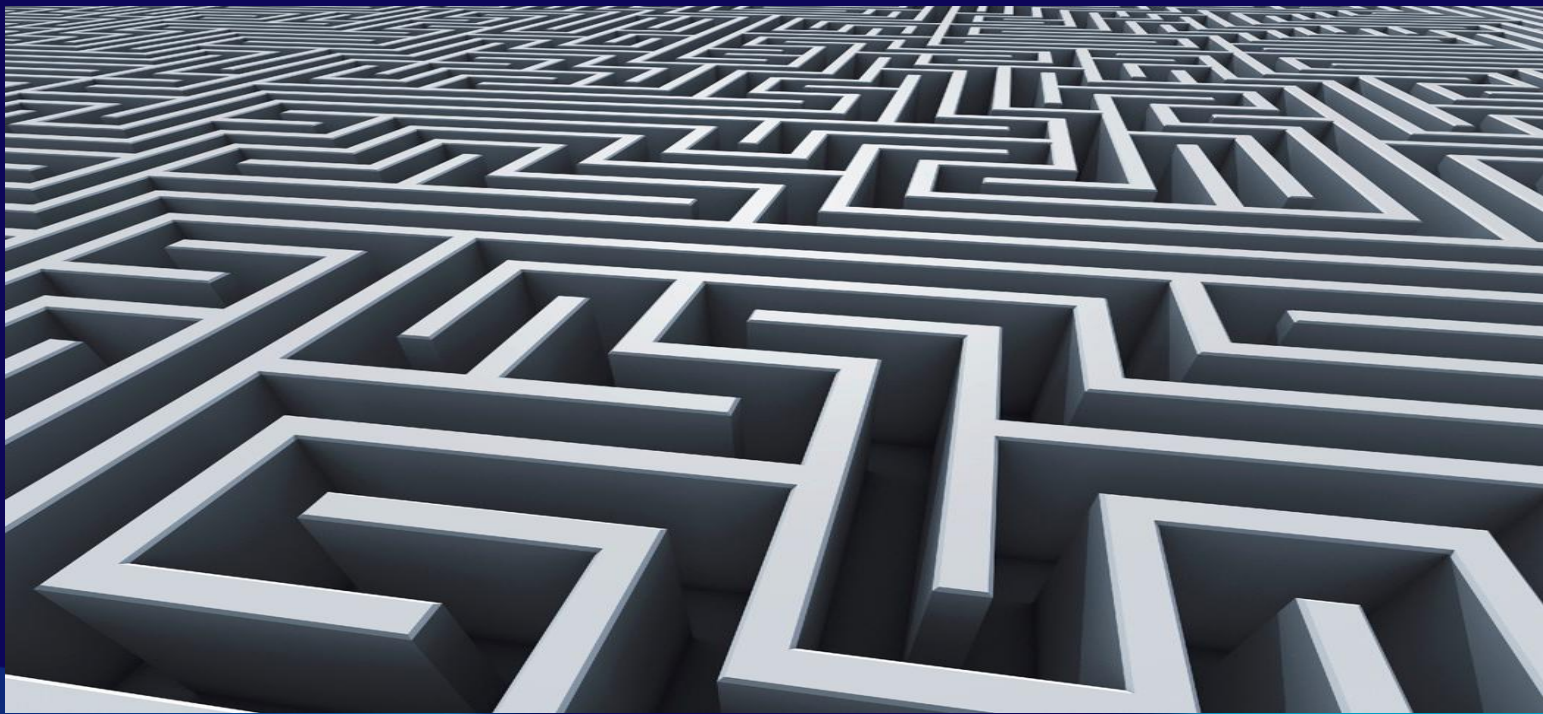
The Fine Print (Disclaimer)



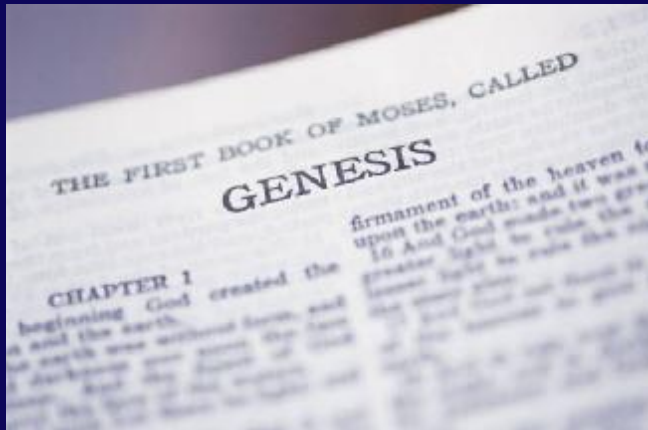
- *The opinions expressed in this Presentation are my own. They are not necessarily the positions of Tyco International, its affiliates or subsidiaries.*

Discussion Roadmap

- Current Status of the Proposal
- Industry Views
- Practical Advice for Companies



History of the Game



- Substantial Transformation since the beginning
- 25 July 2008
 - q CBP proposes (3rd time in ~17 years) to move from the concept of Substantial Transformation to a tariff-shift method for making all country of origin determinations
- First time around was 1991
 - q Last time around was 1994
 - Comments (with extension) were due 23 October 2008
 - CBP published update to Part 102 Rules and asked for specific example comments by 1 December 2008

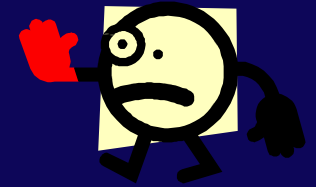
History of the Game

- Nearly 100 Years of Substantial Transformation to be overturned



q *Anheuser Busch Brewing Association v. The United States*, 207 US 556 (1908), as well as other cases that have all held that “for tariff purposes, a substantial transformation occurs if a new and different article emerges having a distinctive name, character or use.”

Industry Initial Reactions



- Why?

- Why again after this was defeated twice before?
- Why now when the WTO/WCO is working on this issue still for some global uniformity?

- What?

- What will the real impact be?
- What, and how many different areas will really be impacted?
- What will the real costs to importers be?
- What perceived problem is this solving?



The Proposal

- Extend 19 CFR Part 102 (the NAFTA Marking Rules) to be universally applicable in country of origin determinations
- Affected areas of the regulations (collateral damage)
 - q Part 4 – Vessels
 - q Part 10 – Free or Conditionally Free Goods
 - q Part 102 – Applicability of the Marking Rules
 - q Part 134 - Marking



CBP's Perceived Problems Solved

Perceived Problem

- Substantial Transformation is:
 - Too subjective
 - Too much “case by case” basis
 - Too confusing
 - Too hard to administer
 - Not simple
 - Not Standard



Proposed Solution

- Tariff Shift Rules offer:
 - Simplicity
 - Standardization
 - Rules CBP is familiar with



Trade's Perceptions

Many pieces missing to understand the true impact of the proposal.

Perceived problems remain unsolved by a Tariff-Shift system



...Or could be made worse



Tariff Classification is Not Always Objective

- Classification

- Reasonable people can disagree
- Customs regimes often disagree
- May require more interpretation than substantial transformation (Why else have GRI's?):
 - Many factual determinations need to be made to classify
 - Essential character?
 - Common, commercial, or technical name?
 - Does it fit a basket provision?

- Substantial Transformation

- Manufacturing is what it is
- New/different article of commerce, distinct name, character or use is a relatively simple standard
- People have fewer origin questions than classification questions:
 - 2008
 - 4,512 classification rulings
 - 72 origin rulings



Other Tariff-Shift Troubles



- Tariff Classification is not always Available to the Importer at the Component Level
- Preference Program Rules of Origin are not necessarily uniformly Adaptable
- Tariff Classification and Tariff-Shift Have Unintended Consequences
- Tariff-Shift does not promote the spirit of the marking statute
- Tariff-Shift Does Not Solve the Case-by-Case Problem
- Tariff-Shift does not make it easier to demonstrate reasonable care

Economic Impacts Uncertain

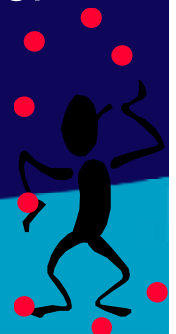
- CBP did not perform an economic impact analysis
 - Based on position that the NPRM is interpreting a court decision
 - General disbelief that the court case cited alleviates the need for an economic impact analysis
- Expected additional costs
 - Additional extensive component classifications for products produced outside of the NAFTA countries
 - Added bill of material analysis where not done before
 - More ruling requests to confirm origin



Reasonable Care Risks



- Inconsistency in tariff classification determination of component parts and finished goods between various countries leads to inaccurate or contested origin determinations.
- Heavy reliance on unrelated parties to correctly apply the uniform rules of origin to imported products when no BOM visibility exists to an importer's compliance professionals could result in CBP's allegations of a lack of reasonable care.
- Reluctance of foreign suppliers to perform the uniform rules of origin tariff-shift analysis when the substantial transformation method is adequate in their country and the countries of other customers.
- Reluctance of suppliers to provide the necessary BOM information, which may be proprietary, to allow the importer to conduct the uniform rules of origin tariff-shift analysis.



Rulings & Court Decisions

- Removes country of origin as a viable issue to bring before a court
 - Everything hinges on classification of the finished good
- Potential to overturn court decisions and CBP rulings on origin and interpretations of substantial transformation
 - Example: Longstanding Rules on Battery Packs (HQ 563045)
 - q Old Rule: Assembly of battery cells into packs does not result in a substantial transformation of the cells because the essential character of the cells does not change by placing them together in a plastic case. Origin is the country where the battery cells are made.
 - q Proposed Rule: Tariff-shift rules apply depending upon the classification of the battery pack in Heading 8507. For battery packs classifiable in HTS subheading 8507.80 (battery packs), the tariff-shift rule would be satisfied by a shift from any other subheading. Therefore, it appears that origin would not be conferred based on the origin of the cells, in contrast to the current substantial transformation rule.



Rulings & Court Decisions

- Unrecorded magnetic media / Software
 - Old Rule: Stamping or recording software onto previously unrecorded media effects a substantial transformation.
 - Proposed Rule: the country of origin of recorded media will no longer be the country in which the recording occurs.



Slow Churned Ice Cream Costs More

Dieters to suffer!

- In HQ 230942 (June 6, 2005) CBP considered whether the process of slow-churning ice cream in the US resulted in a product of the US.
 - The ruling went to great lengths to establish that the process did constitute manufacture and resulted in a substantial transformation of liquid ice cream into the finished product and conferred origin.
 - Proposed rule: Ice cream in liquid form & finished slow-churned ice cream are both classified in 2105. No tariff-shift occurs.



Ripple Effects on Enforcement Not Covered

- 19 USC 1304 –Origin Mark required on imports
 - Issue: CBP challenges classification post entry
 - q Marking was correct at time of entry based on importer's classification and use of tariff-shift rule.
 - q CBP's decision changes the classification and associated tariff-shift rule.
 - q Country of origin result is now different.
 - Now what?
 - q Does CBP go after importer for a marking violation?
 - q 2 compliance dings? Classification and Origin?



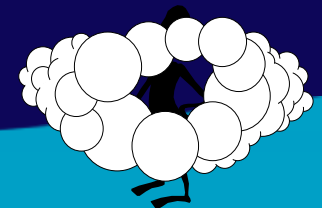
Ripple Effects on Other Agency Regulations

- Many OGA Regulations rely on Substantial Transformation
 - Government Contracting / Buy Americaca / Buy Americancan Act
 - BIS EAR regulations tend to rely on CBP interpretation of origin
 - OFAC, relies on “substantial transformation” when examining exports to third countries and transshipments
 - Jones Act
- CBP needs to provide specificity on all these issues before industry can just relax and accept the imposition of the new rules



Position Summary on CBP's Proposal

- ∅ Exaggerates subjectivity and case-by-case nature of substantial transformation.
- ∅ Shifts the undue and unnecessary responsibility, cost, and risk of classification and tariff-shift analysis to importers while failing to reduce either the number or the impact of country of origin disputes.
- ∅ Undermines or negates well-established judicial and CBP precedent.
- ∅ Takes premature action in light of the existing two-year delay in the reconciliation of 19 CFR 102 rules of origin with the 2007 Harmonized Tariff System (“HTS”) changes.
- ∅ Incompatible with the WTO country of origin harmonization effort.
- ∅ Imposes significant financial burdens on US business in a time of economic distress.
- ∅ Creates new litigation hazards.



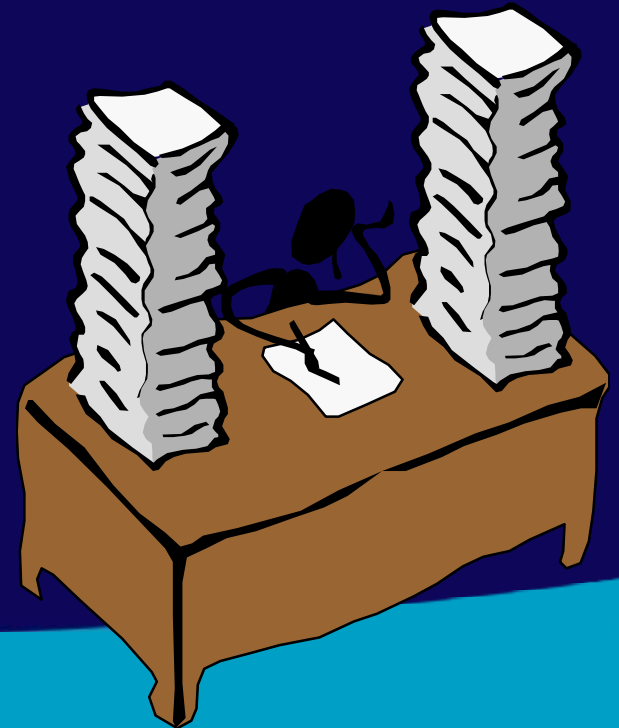
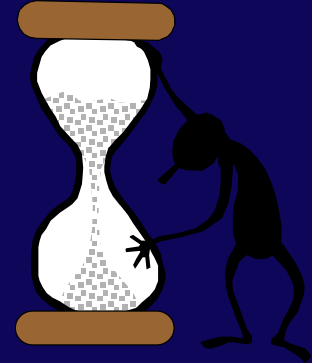
Advice – if this comes to pass



- Prepare to spend money
 - All importers need to review their parts databases
 - ◻ Verify that tariff shift rules do or do not apply
 - ◻ Compare current country of origin with tariff shift rule and see if they match – and comment!
 - Apply trade preference program verification/analysis process to all imported goods for origin determination
 - Prepare for collateral damage (enforcement unknowns)

Please Comment Before Time Runs Out!

- Review products and bills of materials and submit comments!
 - How long did the process take?
 - Do you reach different conclusions under the new system?



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Q&A