

Title : Inclusion of defective materials and scrap or waste as assists; Modification of HRL 544758; Section 402(h)(1)(A) of the TAA; 19 CFR 152.103(d)(1) and (e)(1)

HQ 545910
November 30, 1995
VAL RR:IT:VA 545910 LPF
CATEGORY: Valuation
Ms. Julie White Nordstrom, Inc.

A/P Import Office P.O. Box 870 Seattle, WA 98111
RE: Inclusion of defective materials and scrap or waste as assists; Modification of HRL 544758; Section 402(h)(1)(A) of the TAA; 19 CFR 152.103(d)(1) and (e)(1)
Dear Ms. White:

This decision concerns Headquarters Ruling Letter (HRL) 544758, issued February 21, 1992, wherein it was determined, in pertinent part, that the value of defective fabric not physically incorporated into the imported merchandise was not to be included in the transaction value of the merchandise. We have reviewed this portion of the decision and the proper appraisal is as follows. Pursuant to section 625, Tariff Act of 1930 (19 U.S.C. 1625), as amended by section 623 of Title VI (Customs Modernization) of the North American Free Trade Agreement Implementation Act, Pub. L. 103-182, 107 Stat. 2057, 2186 (1993) (hereinafter section 625), notice of the proposed modification of HRL 544758 was published on May 17, 1995, in the Customs Bulletin, Volume 29, Number 20.

FACTS:

Nordstrom, Inc., the importer, purchases fabric from a foreign vendor and subsequently gives it to a foreign CMT vendor to be used in the assembly of apparel. Nordstrom receives a cut scale along with the commercial invoice from the CMT vendor. The cut scale indicates the quality and value of the fabric used and also indicates the number of pieces cut as compared to the number of pieces ultimately sent to Nordstrom. It is our understanding that the discrepancy between pieces cut and pieces sent is due to defective fabric that is stained, torn, or incorrectly cut.

ISSUE:

Whether materials which are defective or scrapped may constitute assists and, if so, in what manner they are to be valued and apportioned to the imported merchandise.

LAW AND ANALYSIS:

The preferred method of appraising merchandise imported into the United States is transaction value pursuant to section 402(b) of the Tariff Act of 1930, as amended by the Trade Agreements Act of 1979 (TAA), codified at 19 U.S.C. 1401a. Section 402(b)(1) of the TAA provides, in pertinent part, that the transaction value of imported merchandise is the "price actually paid or payable for the merchandise when sold for exportation to the United States" plus enumerated statutory additions, including the value apportioned as appropriate of any assist. 19 U.S.C. 1401a(b)(1).

The "price actually paid or payable" is defined in section 402(b)(4)(A) of the TAA as the "total payment (whether direct or indirect, and exclusive of any costs, charges, or expenses incurred for transportation, insurance, and related services incident to the international shipment of the merchandise...) made, or to be made, for the imported merchandise by the buyer to, or for the benefit of, the seller."

Section 402(h)(1)(A) of the TAA provides, in pertinent part, as follows:

The term 'assist' means any of the following if supplied directly or indirectly, and free of charge or at reduced cost, by the buyer of imported merchandise for use in connection with the production or the sale for export to the United States of the merchandise:

- (i) Materials, components, parts, and similar items incorporated in the imported merchandise.
- (ii) Tools, dies, molds, and similar items used in the production of the imported merchandise.
- (iii) Merchandise consumed in the production of the imported merchandise.
- (iv) Engineering, development, artwork, design work, and plans and sketches that are undertaken elsewhere than in the United States and are necessary for the production of the imported merchandise.

Furthermore, the TAA Statement of Administrative Action (SAA) and section 152.103(d)(1), Customs Regulations (19 CFR 152.103(d)(1)), set forth the manner in which assists are to be valued. In particular,

section 152.103(d)(1) states that:

If the assist consists of materials, components, parts, or similar items incorporated in the imported merchandise, or items consumed in the production of the imported merchandise, acquired by the buyer from an unrelated seller, the value of the assist is the cost of its acquisition. If the assist were produced by the buyer or a person related to the buyer, its value would be the cost of its production. In either case, the value of the assist would include transportation costs to the place of production.

Finally, the SAA and section 152.103(e)(1), Customs Regulations (19 CFR 152.103(e)(1)), provide the manner in which the value of an assist is to be apportioned to the imported merchandise:

The apportionment of the value of assists to imported merchandise will be made in a reasonable manner appropriate to the circumstances and in accordance with generally accepted accounting principles. The method of apportionment actually accepted by Customs will depend upon the documentation submitted by the importer. If the entire anticipated production using the assist is for exportation to the United States, the total value may be apportioned over (i) the first shipment, if the importer wishes to pay duty on the entire value at once, (ii) the number of units produced up to the time of the first shipment, or (iii) the entire anticipated production. In addition to these three methods, the importer may request some other method of apportionment in accordance with generally accepted accounting principles. If the anticipated production is only partially for exportation to the United States, or if the assist is used in several countries, the method of appraisal will depend upon the documentation submitted by the importer.

Based on the statutory and regulatory language cited above, it remains Customs position that in regard to material or components which may constitute assists, a three part analysis must be employed. First, the material or components must fit the definition of an assist; second, it must appropriately be valued as an assist; and third, the value of the assist must be apportioned to the imported merchandise.

Upon review, it is our position that in situations where scrap or waste results from, or during, the production process, limiting the analysis only to consider whether the material or components were physically incorporated into the completed imported merchandise is inconsistent with the language provided in the TAA. Rather, we stress that the TAA provides that material or components "use[d] in connection with the production or the sale for export to the United States of the merchandise" constitutes an assist not only when "incorporated in the imported merchandise," but also when "consumed in the production of the imported merchandise (emphasis added)." The fact that waste or scrap (of a material such as a bolt of fabric) which results from, or during, the production of the imported merchandise is not physically incorporated in that merchandise does not negate the fact that such material or components still may be consumed in the production of the merchandise and constitute assists.

The definition of an assist is not inextricably tied to the value or apportionment of an assist. Once it is determined that material or components meet the definition of an assist, the inquiry then concerns the cost of acquisition or production of that assist. Apportionment of the value of the assist subsequently comes into consideration.

Accordingly, once it is determined that material or components meet the definition of an assist in accordance with the above, then Customs will consider, among other things, the accounting records of the supplier of the assists to determine the value of the assist. Customs would consider such information in cases including those where scrap or waste results from, or during, the production of the imported merchandise.

In the instant situation, Customs now considers material to have been consumed in the production of the imported apparel in accordance with section 402(h)(1)(A)(iii) of the TAA and, hence, to constitute an assist if such material:

- a. during the manufacture of the imported merchandise;
- b. either falls to the factory floor (or otherwise is accumulated when the fabric is cut or worked), is found to be defective or not up to quality, or is mishandled and rendered dysfunctional; and
- c. subsequently is discarded, scrapped or otherwise destroyed.

On the other hand, material would not be deemed incorporated in, nor consumed in the production of, the imported apparel and, therefore, would not constitute an assist if such material either is found to be defective or not up to quality, or is mishandled and rendered dysfunctional, and does not enter the manufacturing process of the imported merchandise.

Valuation of the assist (including the material consumed in the production of the apparel) and apportionment of that value to the imported merchandise subsequently are considered. See 19 CFR 152.103(d)(1) and (e)(1). These latter determinations are to be based on objective and quantifiable data including, among other things, the accounting records of the supplier of the assists made in conformity with generally accepted accounting

principles.

HOLDING:

The defective or scrapped material at issue constitutes an assist when, in accordance with the foregoing, it is consumed in the production of the imported apparel pursuant to section 402(h)(1)(A)(iii) of the TAA. Valuation of the assist and apportionment of that value to the imported merchandise is to be based on objective and quantifiable data, including, among other things, the accounting records of the supplier of the assists made in conformity with generally accepted accounting principles.

HRL 544758 is modified accordingly. In accordance with section 625, this ruling will become effective 60 days from its publication in the Customs Bulletin. Interested parties who import merchandise consistent with the facts set forth in this decision are encouraged to contact the appropriate Customs field personnel to discuss the processing of their specific entries and may submit requests for new binding valuation rulings to the Value Branch, Office of Regulations and Rulings.

Sincerely,
Acting Director, International Trade Compliance Division

Copyright 2009 CUSTOMS Info LLC. All Rights Reserved.