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Customs Provisions and Rules of Origin Under the NAFTA

This article discusses the principal customs provisions and rules of origin provisions of the North American Free Trade Agreement (NAFTA).¹ The authors base the article on the NAFTA text dated December 17, 1992. While this NAFTA text is substantially more detailed than the United States-Canada Free Trade Agreement (CFTA),² the signatories must still supplement it with further details, including the implementing legislation in all three countries and the Uniform Regulations and Marking Regulations anticipated by the NAFTA itself. Accordingly, specific details of procedures and implementation are not yet available.

The NAFTA drafters designed the customs administration provisions of the NAFTA to ensure that only goods satisfying the NAFTA rules of origin are accorded preferential tariff treatment and to encourage certainty and streamlined

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1. North American Free Trade Agreement [hereinafter NAFTA]. All references to the NAFTA are to the December 17, 1992, draft. The Parties have not legally adopted the NAFTA as of the date of this publication.

2. United States-Canada Free Trade Agreement, Jan. 2, 1988, U.S.-Can., 27 I.L.M. 281 [hereinafter CFTA].

procedures for importers, exporters, and producers of the three countries.³ The NAFTA also contains related customs provisions that in many respects follow present U.S. law and practice.

I. General Customs Issues—Chapter 3

Chapter 3 of the NAFTA covers general customs matters. The body of chapter 3 contains generic rules, with country-specific references and exceptions set out in the annexes. The annexes also provide special transitional rules for market access in the automotive⁴ and textile and apparel sectors.⁵ Special rules in other chapters (for example, the energy and petrochemical sector in chapter 6 and the agricultural sector in chapter 7) sometimes supersede the rules in chapter 3.

The rules in chapter 3 apply to different categories of merchandise. For example, tariff elimination (article 302) applies only to "originating goods" as defined in chapter 4;⁶ national treatment (article 301) applies to goods of a Party;⁷ temporary admission rules (article 305) apply to goods imported into the territory of one NAFTA Party regardless of origin;⁸ and most-favored-nation treatment (article 308) applies to a number of goods, including automatic data processing goods and certain color television tubes.⁹

A. NATIONAL TREATMENT—ARTICLE 301

The NAFTA incorporates the fundamental national treatment obligation of the General Agreement on Tariffs and Trade (GATT).¹⁰ Once one NAFTA country has imported goods from another NAFTA country, the goods must not be the object of discrimination. This commitment extends to provincial and state measures and the Parties agree to ensure that the state and provincial governments take all necessary measures¹¹ to give effect to this commitment.¹² In this respect the NAFTA goes farther than the GATT.¹³ However, how this application to states and provinces will work remains unclear.

3. See Description of the Proposed North American Free Trade Agreement Prepared by the Governments of Canada, the United Mexican States, and the United States of America (Aug. 12, 1992) [hereinafter Description].

4. NAFTA, *supra* note 1, annex 300(A).

5. *Id.* annex 300(B).

6. *Id.* art. 302(1), (2).

7. *Id.* art. 301(1).

8. *Id.* art. 305(1).

9. *Id.* art. 308(1)(2).

10. The General Agreement on Tariffs and Trade, Oct. 30, 1947, 55 U.N.T.S. 194, part II, art. III [hereinafter GATT].

11. NAFTA, *supra* note 1, art. 105.

12. *Id.* arts. 105, 301(2). These provisions are substantially similar to art. 103 and arts. 501 and 502 of the CFTA, *supra* note 2.

13. Both the NAFTA and the CFTA contain stronger language than the GATT, which provides that the Parties "shall take such reasonable measures as may be available to it" to ensure observance of the provisions of GATT, including the national treatment provision, by states and provinces.

B. TARIFF ELIMINATION—ARTICLE 302¹⁴

Like article 401 of the CFTA, the NAFTA prohibits the Parties from increasing existing tariffs or adopting any tariff on an originating good except as provided by the NAFTA.¹⁵ The NAFTA also eliminates customs duties on originating goods over certain time periods (staging) in accordance with a Party's schedule to Annex 302.2 or as indicated in Annex 300-B.¹⁶ For example, some goods receive duty free treatment upon the NAFTA's entry into force on January 1, 1994 (Category A).¹⁷ Other goods, however, become duty free in five years on January 1, 1998 (Category B),¹⁸ others in ten years on January 1, 2003 (Category C),¹⁹ and still others in fifteen years on January 1, 2008 (Category C+).²⁰ Some goods, however, continue to receive duty free treatment (Category D).²¹ While Annex 302.2 mentions only five types of staging categories, the NAFTA tariff schedules provide for numerous variations on staged elimination, including delaying the start of tariff elimination for several years.²² Base rates are those tariffs generally in effect on July 1, 1991, including rates of the U.S. Generalized System of Preferences and the General Preferential Tariff of Canada.²³ For staging purposes, the NAFTA requires interim stage rates to be rounded down to the

See GATT, *supra* note 10, art. XXIV:12; see also SHAWNA K. VOGEL, *PROVINCIAL AND STATE PERSPECTIVES ON THE NAFTA* 9 (1992). While a recent panel decision evidences an effort to strengthen the GATT language, the standard in the GATT remains a "best efforts" standard while the NAFTA requires the Parties to take all necessary measures. See *Canada—Measures Affecting Alcoholic and Malt Beverages* 68–70 (Oct. 19, 1991) (for discriminatory practices that had been identified in an earlier panel report; Canada was required to demonstrate that it had made "a serious, persistent and convincing effort to secure compliance by the provincial liquor boards" in order to meet its obligations under article XXIV:12; however, for discriminatory practices that had not been previously identified, the "serious persistent and convincing effort" standard was not initially applied to determine whether Canada had met its obligations under article XXIV:12; rather, the panel found that Canada should be given a reasonable time to take measures to bring the practices in question into line with the GATT).

14. When the staged elimination of a tariff causes or threatens to cause harm to an industry of a NAFTA Party, chapter 8 provides for the increase in the NAFTA tariffs on a short-term emergency basis. NAFTA, *supra* note 1, art. 801(1)(b). Conversely, chapter 8 also provides for the exemption of the goods of Parties from the application of global emergency action. *Id.* art. 802(1).

15. *Id.* art. 302(1).

16. *Id.* art. 302(2).

17. *Id.* annex 302.2(1)(a).

18. *Id.* annex 302.2(1)(b).

19. *Id.* annex 302.2(1)(c).

20. *Id.* annex 302.2(1)(d).

21. *Id.* annex 302.2(1)(e).

22. For example, for goods imported into the United States with a "1B8" staging category, duties will be eliminated in two stages, beginning in 1998, four years after the NAFTA is to take effect. Similarly, for goods imported into the United States with a "BP" staging category, the NAFTA will eliminate duties in three stages as follows: (1) on January 1, 1997, a 20 percent tariff cut will take effect; (2) on January 1, 1998, a 10 percent tariff cut will take effect; and (3) on January 1, 1999, the NAFTA will eliminate all duties. See Tariff Schedules of the United States, NAFTA, *supra* note 1, annex 302.2.

23. *Id.* annex 302.2(2).

nearest tenth of a percentage point.²⁴ The rounding rules are basically the same as those rules provided in article 402 of the CFTA.

Determining duty rates during the staging period can be extremely confusing and require more than a determination that a good is an originating good under the NAFTA. This complexity arises because the United States and Mexico established bilateral tariff elimination schedules as did Canada and Mexico, and the signatories incorporated the CFTA tariff elimination schedule into the NAFTA.²⁵ Accordingly, during the transition to zero duty rates importers and exporters will need to determine whether a good is of Mexican, U.S., Canadian, or NAFTA origin for duty purposes.

C. DRAWBACK AND DUTY DEFERRAL PROGRAMS—ARTICLE 303²⁶

Duty drawback is the repayment of duties upon the exportation of goods that contain duty paid components. Duty deferral is the delayed payment of duties that may never be paid if the country exports either the good or a good manufactured using the good. The NAFTA, unlike the CFTA, does not entirely eliminate duty drawback and duty deferral. Instead, the NAFTA eliminates the double payment of duties to two Parties on goods that are not the NAFTA originating goods. The NAFTA basically allows drawback and duty deferral in an amount equal to the lesser of (1) the total amount of customs duties on the good on importation into the country from which the good is subsequently exported, or (2) the total amount of customs duties paid to the Party to which the good is exported.²⁷ In the case of duty deferral, the NAFTA provides a grace period of sixty days to allow an importer/exporter to demonstrate that duties have been paid in the importing NAFTA country.²⁸ Otherwise the customs administration of the Party must assess customs duties as if the good had been withdrawn for domestic consumption, but may also refund the amount later upon presentation of certain evidence.²⁹

In determining the amount of customs duties that may be refunded, waived, or reduced as provided above, each Party must require presentation of satisfactory evidence.³⁰ This evidence should include the amount of customs duties paid to

24. *Id.* annex 302.2(3).

25. *Id.* annex 302.2(4).

26. The effective date of these provisions is Jan. 1, 1996, for U.S.–Canada trade. *Id.* annex 303.7(A)(a). The effective date is Jan. 1, 2001, for U.S.–Mexico and Mexico–Canada trade. *Id.* annex 303.7(A)(b), (c).

27. *Id.* art. 303(1).

28. *Id.* art. 303(5).

29. *Id.* art. 303(5)(a), (b).

30. Satisfactory evidence means a receipt or a copy of a receipt evidencing payment of customs duties on a particular entry; a copy of the entry document with evidence that it was received by customs administration; a copy of a final customs duty determination by a customs administration respecting the relevant entry; or any other evidence of payment of customs duties acceptable under the uniform regulations developed in accordance with ch. 5 of the NAFTA. *Id.* art. 318(a)–(d).

another Party on the good that has been subsequently exported to the territory of that other Party.³¹

The NAFTA prohibits the refund, waiver, or reduction of certain duty payments based on drawback.³² For example, the NAFTA prohibits the refund of duty payments for antidumping duties. Additionally, the NAFTA rules prohibiting drawback do not apply in certain cases, such as same condition drawback, transportation, and exportation entries.³³ The NAFTA also provides special rules for duty deferral and drawback on certain products, including color picture tubes, sugar, and certain textiles.³⁴

D. TEMPORARY ADMISSION OF GOODS—ARTICLE 305

Unlike the CFTA, the NAFTA contains a specific provision on the temporary admission of goods.³⁵ Article 305 of the NAFTA is similar to the temporary importation under bond provisions that already exist in U.S. law.³⁶ Under this provision each Party grants duty free admission (on which it may place certain restrictions and requirements, for example, bonds³⁷) on the following classes of articles should another Party import them, regardless of their origin and regardless of whether like, directly competitive, or substitutable goods are available in the territory of the Party:

- (a) professional equipment necessary for carrying out the business activity, trade, or profession of a business person who qualifies for temporary entry pursuant to chapter 16 (Temporary Entry for Business Persons);³⁸
- (b) equipment for the press or for sound or television broadcasting and cinematographic equipment;³⁹
- (c) goods imported for sports purposes⁴⁰ and goods intended for display or demonstration;⁴¹ and
- (d) commercial samples⁴² and advertising films.⁴³

31. *Id.* art. 303(4).

32. *Id.* art. 303(2)(a). Currently, antidumping duties and countervailing duties are not subject to drawback in the United States.

33. *Id.* art. 303(6)(a).

34. *Id.* annexes 303(6), 303(8).

35. *Id.* art. 305.

36. *See* 19 C.F.R. § 10.31 (1992).

37. *See* NAFTA, *supra* note 1, art. 305(2), which sets forth permissible conditions.

38. *Id.* art. 305(1)(a). This provision is similar to current U.S. law. *See* Harmonized Tariff Schedule (HTS), 19 U.S.C. § 1202 (1988).

39. NAFTA, *supra* note 1, art. 305(1)(b); *see also* 19 U.S.C. § 1202, item 9813.00.50.

40. NAFTA, *supra* note 1, art. 305(1)(c); *see also* 19 U.S.C. § 1202, item 9813.00.35.

41. NAFTA, *supra* note 1, art. 305(1)(c); *see also* 19 U.S.C. § 1202, items 9813.00.70, 9813.00.65, 9813.00.75.

42. NAFTA, *supra* note 1, art. 305(1)(d); *see also* 19 U.S.C. § 1202, item 9813.00.20. Article 306 provides duty free entry for certain commercial supplies of negligible value and printed advertising materials.

43. NAFTA, *supra* note 1, art. 305(1)(d); *see also* 19 U.S.C. § 1202, item 9813.00.25.

These provisions will allow individuals in one Party to work temporarily in another Party using their own equipment.

E. GOODS REENTERED AFTER REPAIR OR ALTERATION—ARTICLE 307

The NAFTA provides for the free flow of goods between the Parties (that is, no import duties in either country) for repair or alteration regardless of the origin of the goods.⁴⁴ Article 307 of the NAFTA supersedes the duty deferral and drawback provisions.⁴⁵ For Canada and Mexico, article 307 does not apply to repairs or alterations of certain ships and vessels.⁴⁶ For the United States, this provision applies except in the case of repairs or alterations to certain ships and vessels, and in the case of U.S.–Canada trade, the provision does not apply to any repairs or alterations except warranty repairs.⁴⁷ Article 307 represents a significant change from current U.S. law and supersedes Harmonized Tariff Schedule (HTS) subheadings 9800.02.40/.50, which impose a duty on the value of the repairs or alterations. The NAFTA rates will generally apply to dutiable repairs or alterations regardless of the origin of the goods.

F. CUSTOMS USER FEES—ARTICLE 310

The NAFTA prohibits adoption of any customs user fee of the type specified in Annex 310.1 for originating goods.⁴⁸ However, the Parties may maintain existing fees in accordance with the annex.⁴⁹ Under Annex 310.1, Mexico cannot increase its customs processing fee on originating goods and should eliminate the fee on originating goods by June 30, 1999.⁵⁰ The United States cannot increase its merchandise processing fee.⁵¹ Additionally, the United States should eliminate this fee according to the schedule set out in article 403 of the CFTA on originating goods when those goods qualify to be marked as goods of Canada pursuant to Annex 311⁵² (that is, by January 1, 1994) and on originating goods qualified to be marked as goods of Mexico by June 30, 1999.⁵³

44. NAFTA, *supra* note 1, art. 307(1)(2). “[R]epair or alteration does not include an operation or process that either destroys the essential characteristics of a good or creates a new or commercially different good.” *Id.* art. 318.

45. *Id.* arts. 303, 307(2).

46. *Id.* art. 307(3), annex 307.3.

47. *Id.* annex 307.1(A)–(C).

48. *Id.* art. 310(1).

49. *Id.* art. 310(2).

50. *Id.* annex 310.1(A).

51. *Id.* annex 310.1(B)(1). The NAFTA prohibits the United States from increasing its “merchandise processing fee,” but the CFTA, *supra* note 2, art. 403 related to U.S. “customs user fees.” Also, the CFTA allowed for a changing of the level of the fees. *Id.*

52. NAFTA, *supra* note 1, annex 310.1(B)(1).

53. *Id.* annex 310.1(B)(2).

G. COUNTRY OF ORIGIN MARKING—ARTICLE 311

The NAFTA provides a framework for the creation of rules for country of origin marking.⁵⁴ These rules must be established by January 1, 1994.⁵⁵ Under these rules each Party may require that the good of another Party bear a conspicuous, legible, and sufficiently permanent country of origin marking to indicate to the ultimate purchaser of that good the name of its country of origin.⁵⁶ Thus, the rules generally preserve the U.S. country of origin marking law.⁵⁷ The rules also enumerate certain exemptions from country of origin marking.⁵⁸ Additionally, when the rules exempt a good from marking, except with respect to certain circumstances, the outermost container must be marked.⁵⁹

In determining the country of origin for marking and the ultimate purchaser, the manner in which substantial transformation is presently determined in U.S. customs law will not apply. Instead, a Party will use a change in tariff classification test.⁶⁰ The requisite changes in tariff classification will be set forth in the marking rules and thus may differ from the rules used to determine originating goods.

H. CONSULTATIONS—ARTICLE 316

The NAFTA establishes a committee on trade in goods that will comprise representatives of each Party⁶¹ and will meet at the request of any Party or the Commission to consider any matter arising out of chapter 3.⁶² At least once each year the Parties must convene a meeting of their officials responsible for customs, immigration, inspection of food and agricultural products, border inspection facilities, and regulation of transportation to address issues related to the movement of goods through the Parties' ports of entry.⁶³

II. Country of Origin Determinations—Chapter 4

Chapter 4 contains the basic NAFTA Rules of Origin. These origin rules—or, more strictly speaking, standards of preference⁶⁴—raised some of the more

54. *Id.* art. 311.

55. *Id.* annex 311(1).

56. *Id.* annex 311(5)(a).

57. *See* 19 C.F.R. § 134.11 (1992). One distinction may be the provision in annex 311(3) permitting the marking to be in English, French, or Spanish, except where as part of its general consumer information measures it may require imported goods to be marked the same as its goods. NAFTA, *supra* note 1, annex 311(3).

58. NAFTA, *supra* note 1, annex 311(5)(b). These are similar to those under U.S. law. *See* 19 C.F.R. § 134.32 (1992).

59. NAFTA, *supra* note 1, annex 311(6).

60. Description of the Proposed North American Free Trade Agreement (Aug. 12, 1992), 9 Int'l Trade Rep. (BNA) 1454, 1457.

61. NAFTA, *supra* note 1, art. 316(1).

62. *Id.* art. 316(2).

63. *Id.* art. 316(3).

64. A useful distinction exists between "rules of origin" and "standards of preference." Rules of origin traditionally involve a neutral determination of where particular goods are considered to have been made for purposes of statistical record-keeping, country of origin marking, and other

controversial and difficult issues in the NAFTA negotiations. The governments involved, as well as many of the important economic and political interests in the three countries, were very concerned that the reduced duties available under the NAFTA only benefit products that involve significant manufacturing and other economic activity in the three countries. For example, the governments and other interests did not want Mexico, with its lower wage rates and other costs, to be used as an "export platform" for entry into the United States of goods that consisted largely of third-country materials. Controversies involved in the United States Customs Service's administration of the CFTA's origin rules also increased interest in the NAFTA origin rules.⁶⁵

One significant difference between the origin rules in the NAFTA and those in the CFTA is that the NAFTA rules are much more detailed, complex, and comprehensive. Some measure of this difference can be seen in the length of the origin provisions in the two agreements. The origin rules in chapter 3 of Part Two of the CFTA consisted essentially of only seven pages, including a five-page Rules section, with definitions of five terms, and a two-page Interpretations section, plus a twenty-seven-page listing of the rules for individual provisions of the HTS. By contrast, the NAFTA origin rules include a twenty-six-page Rules of Origin section in chapter 4, including express definitions of thirty terms, a seventeen-page Customs Procedures section in chapter 5, two pages of a Notes section following chapter 22 (providing further clarification of some origin rules), and a 168-page annex 401 with specific rules of origin for individual HTS chapters. Needless to say, this brief summary of the NAFTA origin rules provides only an overview of an enormously complicated area.

A. ORIGINATING GOODS—ARTICLE 401

Article 401 of the NAFTA provides the basic tests for determining whether a good will be considered to originate in the territory of a Party to the NAFTA. The basic standard, which is similar to that in the CFTA, involves a change in tariff classification approach.⁶⁶ Specifically, article 401 provides that a good will qualify as an originating good when each of the nonoriginating materials used to

purposes. Standards of preference concern the analytically different issue of whether particular goods should receive special, preferential treatment, typically a reduced or eliminated duty rate. Although the NAFTA characterizes the rules as "origin" rules (and those rules are so described in this article), they are plainly "standards of preference," since they determine whether the goods involved will be eligible for the preferential NAFTA duty rates. Accordingly, it is possible for goods to be treated as Canadian goods for country of origin marking purposes, but not to qualify as "originating in" Canada for purposes of the CFTA or the NAFTA. However, the United States Customs Service has proposed to adopt general origin rules based on the "change in tariff classification" approach of the NAFTA, as discussed below. See 56 Fed. Reg. 48,448 (1991).

65. See, e.g., UNITED STATES INTERNATIONAL TRADE COMMISSION, PUB. NO. 2460, RULES OF ORIGIN ISSUES RELATED TO THE NAFTA AND THE NORTH AMERICAN AUTOMOBILE INDUSTRY 31-44 (1991) [hereinafter ITC ORIGIN REPORT].

66. NAFTA, *supra* note 1, art. 401(b).

produce the good undergoes an applicable change in tariff classification, as set forth in Annex 401, as a result of production occurring entirely in the territory of one or more of the Parties.⁶⁷ As noted above, Annex 401 is a 168-page annex providing specific rules for each chapter of the HTS.⁶⁸ Additionally, in many cases the good must also satisfy a minimum regional value content requirement.⁶⁹ Article 401 also permits a good to qualify where nonoriginating materials provided for as “parts” under the HTS do not undergo a change in tariff classification because of two types of circumstances, with the further proviso of a minimum regional value content.⁷⁰

B. REGIONAL VALUE CONTENT—ARTICLE 402

1. *Basic Definitions*

Article 402 explains the calculation of the regional value content of a good where the specific origin rules in Annex 401 require such a calculation. Article 402 generally provides that this regional value content (RVC) may be calculated on the basis of either the transaction-value method or the net-cost method.⁷¹

Under the transaction-value method, the NAFTA expresses the RVC as a percentage equal to the transaction value of the goods⁷² (adjusted to an F.O.B. basis) (TV), less the value of nonoriginating materials (VNM) used by the producer in the production of the good, divided by the TV, multiplied by 100, that is:

$$\text{RVC} = \frac{\text{TV} - \text{VNM}}{\text{TV}} \times 100^{73}$$

Under the net-cost method, the NAFTA calculates the RVC as a percentage equal to the net cost of the good (NC), less the value of nonoriginating materials (VNM) used by the producer in the production of the good, divided by the NC, multiplied by 100, that is:

67. *Id.* art. 401(b). The NAFTA will also consider goods to originate in the territory of a Party where the good is “wholly obtained or produced entirely” in the territory of one or more of the Parties, or where the good is produced in such territories “exclusively from originating materials.” See *id.* arts. 401(a), (c).

68. The specific rules vary, generally requiring either a change in HTS heading or a change in HTS subheading.

69. *Id.* art. 402(1).

70. *Id.* art. 401(d).

71. *Id.* art. 402(1).

72. *Id.* art. 402(2). The NAFTA defines the “transaction value” as “the price actually paid or payable for a good or material,” with the qualification that this price is to be “adjusted in accordance with the principles of paragraphs 1, 3, and 4 of Article 8 of the GATT Customs Valuation Code.” *Id.* art. 415.

73. *Id.* art. 402(2).

$$\text{RVC} = \frac{\text{NC} - \text{VNM}}{\text{NC}} \times 100^{74}$$

The NAFTA defines the net cost in turn, as the “total cost” less the following specific costs: “sales promotion, marketing and after-sales service costs, royalties, shipping and packing costs, and non-allowable interest costs that are included in the total cost.”⁷⁵ Article 402 further provides that in calculating the net cost, the producer may use several allocation methods, provided the chosen method is consistent with Uniform Regulations to be established under article 511.⁷⁶ The producer may, for example, reasonably allocate each cost that forms part of the total cost incurred with respect to the good so that the aggregate of these costs does not include any of the items excluded from the net cost definition.⁷⁷

2. *Basic Differences with the CFTA*

Both the transaction-value method and the net-cost method are fundamentally different from the comparable value content methodology employed in the CFTA. The CFTA value content methodology essentially involves a “bottom-up” calculation that requires a determination of the “value of materials originating in the territory of either Party or both Parties,” plus a calculation of the “direct cost of processing [or the direct cost of assembling] performed in the territory of either Party or both Parties.”⁷⁸ This CFTA approach, coupled with ambiguities in the CFTA definitions of “originating” materials and the “direct cost of processing or direct cost of assembling” led to much uncertainty and controversy.⁷⁹ By

74. *Id.* art. 402(3).

75. *Id.* art. 415. Article 415 further defines each of these categories of excluded costs.

76. *Id.* art. 402(8).

77. *Id.* art. 402(8)(c).

78. CFTA, *supra* note 2, at 305.

79. For example, although the CFTA definition of the term “direct cost of processing” refers both to costs that are “directly incurred in” the production of the goods *and* to costs that “can reasonably be allocated to” such production, *id.* at 296, the United States Customs Service regulations issued on January 22, 1992—more than three years after the January 1, 1989, effective date of the CFTA—provide that to be included in the “direct cost of processing” the costs “*must be directly incurred in the production of the exported goods. . . .*” See 19 C.F.R. § 10.305(a)(3)(ii) (1992) (emphasis added); see also United States Customs Service Ruling HQ 089427 (Dec. 9, 1991) (holding, without citation to any authority, that “[t]he phrase ‘or can reasonably be allocated to . . . the production of goods . . .’ did not expand the nature of the costs that can be included to those costs which are not direct.”)

This position by the United States Customs Service is, however, contrary both to the position taken by the Canadian Government in its implementation of the CFTA and to language in a decision of a binational panel established under CFTA art. 1807 to resolve a dispute concerning the treatment of interest expenses. Thus, in its June 8, 1992, Final Report, the panel held that the definition of “direct cost of processing” had “two branches,” with the “second branch”—a reference to “the costs . . . that can reasonably be allocated to the production of goods”—intended to “broaden the meaning that would otherwise flow from the first branch of the definition” that refers to “directly incurred costs.” See Final Report of the Panel in the Matter of Article 304 and the Definition of Direct Cost of

contrast, the NAFTA regional value content rules involve essentially "top-down" methods. For example, the NAFTA rules provide for calculations based on the total price or the total cost, with deductions for certain cost items and/or the value of nonoriginating materials. The hope, no doubt, is that this approach will be more certain and less controversial.

3. *Transaction-Value Method versus Net-Cost Method*

One basic difference between the two RVC methods in the NAFTA is that the transaction-value method includes some costs that are excluded in the net-cost method. Thus, the net-cost method excludes such costs as "sales promotion, marketing and after-sales service costs," and does not include profit.⁸⁰ The NAFTA bases transaction-value method on "the price actually paid or payable for a good or material," and may thus include all costs plus profit.⁸¹ To compensate for this difference the transaction-value method requires a higher percentage of RVC.⁸² Additionally, article 402 provides for certain circumstances where the exporter or producer of the good *must* calculate the RVC using the net-cost method.⁸³ Finally, the exporter/producer of a good may also calculate using the net-cost method where it initially used the transaction-value method. But this method is determined to be "unacceptable" during a verification.⁸⁴

4. *The Value of Nonoriginating Materials*

As noted, both the transaction-value method and the net-cost method require the calculation of the value of nonoriginating materials.⁸⁵ NAFTA bases this value generally on the transaction value of such materials determined in accordance with article 1 of the Customs Valuation Code,⁸⁶ that is, the price actually paid or

Processing or Direct Cost of Assembling, Secretariat Case No. USA-92-1807-01, at 13-15 (June 8, 1992). The panel also expressly rejected the limitation on interest in the United States Customs Service's CFTA regulations. *Id.* at 35-36.

80. NAFTA, *supra* note 1, arts. 402(3), 415.

81. *Id.* arts. 402(2), 415.

82. For most tariff provisions the difference is between a 60 percent requirement under the transaction-value method and a 50 percent requirement under the net-cost method, although other differences exist. *See, e.g.*, HTS subheading 3402.20 (requiring 65 percent under the transaction-value method and 50 percent under the net-cost method).

83. NAFTA, *supra* note 1, art. 402(5). These circumstances include (a) where the good has no transaction value; (b) where the transaction value is "unacceptable" under article 1 of the Customs Valuation Code; (c) where the good is sold to a related person (as defined in article 415) and 85 percent of the producer's sales of the good (by units of quantity) were to related persons during the six-month period prior to the month the good involved is sold; (d) where the good falls within certain tariff classifications, including those for motor vehicles and word processing machines; (e) where the exporter/producer chooses to accumulate the RVC pursuant to article 404, as discussed below; and (f) where the exporter producer designated the good as an "intermediate material," as discussed below, and is subject to an RVC requirement. *Id.* art. 402(5).

84. *Id.* art. 402(6).

85. *Id.* art. 402(9)(3).

86. *Id.* art. 402(9)(a).

payable for the material.⁸⁷ Also included in this value are the costs to transport the material to the location of the producer, such as freight, insurance, and packing.⁸⁸ Additionally, the value includes duties taxes and customs brokerage fees, as well as the cost of waste and spoilage, less the value of renewable scrap or by-product.⁸⁹

In most cases, the decision of whether materials used by a producer are originating or nonoriginating is made on an all-or-nothing basis. That is, if the material qualifies as originating under the NAFTA origin rules, then no portion of its value is treated as nonoriginating, even if the material is comprised in part of nonoriginating submaterials. This result may be referred to as the "roll-up" of the value of the nonoriginating submaterials. Similarly, if the material does not qualify as originating—for example, because it does not satisfy the change in tariff classification requirement or the minimum RVC requirement—the full value is treated as nonoriginating, including any originating submaterials and regional value added. This result may be referred to as the "roll-down" of the originating material and regional value added. A similar roll-up/roll-down applies in the CFTA and became quite controversial, particularly in the automotive area.⁹⁰ Accordingly, as discussed below, a new "tracing" approach was added for motor vehicle products.

5. *Intermediate Materials*

The term "intermediate material" refers to material that a producer creates and then uses in the production of another good.⁹¹ Both the CFTA and the NAFTA implicitly or explicitly recognize that such seller-produced materials can qualify as originating materials.⁹² In an effort to deal with a concern about roll-up,

87. *Id.* art. 415. One difference with the CFTA is that under the NAFTA the transaction value of the material may be found to be unacceptable under article 1 of the Customs Valuation Code. *Id.* art. 402(9)(b). By contrast, the CFTA defines the "value of materials" as "the price paid by the producer of an exported good for materials," with no provision for finding this price unacceptable. See CFTA, *supra* note 2, at 296. See also 19 C.F.R. § 10.305(b)(3)(i) (1992) ("The actual price paid for such materials will determine the value of those materials for purposes of the value content requirement, even though a relationship between the producer and the seller of the materials may have influenced the price . . .").

88. NAFTA, *supra* note 1, art. 402(9)(c).

89. *Id.*

90. See, e.g., ITC ORIGIN REPORT, *supra* note 65, at 33–39.

91. NAFTA, *supra* note 1, art. 415.

92. Under the CFTA, the provisions implicitly provide for "intermediate materials," since the definition of the term "value of materials originating in the territory of either party or both parties" includes "the price paid by the producer of an exported good . . . for materials imported from a third country used or consumed in the production of . . . originating materials." CFTA, *supra* note 2, at 296. See also 19 C.F.R. § 10.305(b)(3)(ii)(1992) (permitting a "vertically integrated producer" to claim "materials which that producer has also made" as originating materials for purposes of qualifying the finished good made with those materials). The NAFTA treats intermediate materials more expressly. NAFTA, *supra* note 1, art. 402(4) (providing that generally the value of nonoriginating materials shall not include "the value of nonoriginating materials used to produce originating materials that are subsequently used in the production of the good"); *id.* art. 402(10) (providing generally that

however, the NAFTA provides that where the intermediate material is subject to an RVC requirement, the producer may not designate as an intermediate material any other self-produced material also subject to an RVC requirement that was used to produce that intermediate material.⁹³ This restriction deals with so-called "cascading roll-up," which was also the subject of CFTA concern.⁹⁴

In an effort to deal with another very controversial issue under the CFTA, the NAFTA provides that the value of an intermediate material includes the "total cost . . . that can be reasonably allocated to that intermediate material."⁹⁵ By contrast, the United States Customs Service had construed the CFTA to limit the material value of an intermediate material to the value of only the *nonoriginating* submaterials used to produce the material.⁹⁶

C. AUTOMOTIVE GOODS—ARTICLE 403

Consistent with the enormous importance of automotive manufacturing and trade in and among the three countries involved, article 403 includes separate origin rules for automotive goods.⁹⁷ One significant aspect of these rules concerns the provision for tracing the value of nonoriginating materials. As noted above, most materials are subject to an all-or-nothing approach based on whether the material does or does not qualify as "originating" under the NAFTA rules. For most motor vehicles, however, article 403 requires the tracing of the actual value of most if not all nonoriginating materials, even if those materials are imported by a supplier that uses them to produce a qualifying originating material. Specifically, for most motor vehicles, including passenger automobiles and light trucks, the value of nonoriginating materials includes the delivered value of all nonoriginating materials that are (1) imported from outside the territory of the three NAFTA Parties, (2) classified under certain tariff provisions listed in Annex 403.1, and (3) used in the production of either the good or any material used in

a producer may "designate any self-produced material used in the production of the good as an intermediate material," with exceptions and a proviso); *id.* art. 415 (defining "intermediate material").

93. *Id.* art. 402(10).

94. The concern was, for example, that a company could qualify "intermediate submaterial A" with, for example, 51 percent North American value content, and then treat this submaterial A as 100 percent North American value for purposes of qualifying "intermediate material B" in order ultimately to qualify the good involved. See ITC ORIGIN REPORT, *supra* note 65, at 38-39.

95. NAFTA, *supra* note 1, art. 402(11).

96. See 19 C.F.R. § 10.305(b)(ii)(1992) (declaring that the value of an originating material produced by a vertically integrated producer "is limited to the price paid for those materials imported from the third country [used to produce the material]," *not* including the value of any United States or Canadian materials used to produce the originating material). See also United States Customs Service Ruling HQ 000131 (Dec. 12, 1991).

97. Some provisions in other articles of chapter 4 also apply to automotive goods. For example, as noted above, producers of certain motor vehicles and parts must use the net cost method for the RVC calculation. See NAFTA, *supra* note 1, art. 403(5).

the production of the good.⁹⁸ This provision means that producers of these goods will have to develop procedures to calculate the value of these nonoriginating materials, even if a supplier or subsupplier imports the materials.

Article 403 also provides a means for averaging the RVC calculations over the motor vehicle producer's fiscal year using one of various categories, such as "the same model line of motor vehicles in the same class of vehicles produced in the same plant of the territory of a Party."⁹⁹ Additionally, article 403 permits averaging the RVC calculations for automotive goods provided for in the tariff provisions listed in Annex 403.2, which should simplify the calculations for suppliers of automotive goods to motor vehicle manufacturers.¹⁰⁰

Article 403 also includes specific increased RVC requirements for the covered motor vehicles and motor vehicle goods. Thus, for passenger motor vehicles and related goods, the RVC percentage increases to 56 percent for the producer's fiscal year beginning closest to January 1, 1998, and to 62.5 percent for the producer's fiscal year closest to January 1, 2002.¹⁰¹

D. ACCUMULATION—ARTICLE 404

Article 404 provides that in determining whether a good qualifies as originating, the exporter/producer of the good can "accumulate" production of the good by other producers, provided that on this accumulated basis all nonoriginating materials undergo the required tariff classification change and the good satisfies any applicable RVC requirement.¹⁰² This article would apparently permit, for example, a good that producer *A* processed initially in Mexico and that Producer *B* imported and further processed in the United States to qualify as an originating good on the basis of the overall production by producers *A* and *B* when the good is exported to Canada.¹⁰³

E. DE MINIMIS RULE—ARTICLE 405

As indicated above, for a good to qualify as originating under the NAFTA, each nonoriginating material used to produce the good must generally undergo

98. NAFTA, *supra* note 1, art. 403(1)(a). This same tracing rule also applies to goods provided for in the tariff provisions listed in annex 403.1 that are for use as original equipment for the production of certain motor vehicles and are subject to an RVC requirement. *Id.* art. 403(1)(b). A similar rule involving less tracing applies to other motor vehicles such as heavy trucks. *Id.* art. 403(2).

99. *Id.* art. 403(3)(a).

100. *Id.* art. 403(4).

101. *Id.* art. 403(5)(1). Article 403, however, permits a 50 percent RVC rate for a period of five years after certain new motor vehicle production in "the territory of any of the Parties." *Id.* art. 403(6). Annex 403.3 also contains a separate RVC method for motor vehicles produced by one company—CAMI Automotive, Inc.—in Canada and imported into the United States.

102. *Id.* art. 404(a)(b).

103. However, article 402(10)'s "cascading roll-up" limitation restricts this accumulation alternative. In addition, during the transition period of duty reduction, special rules in annex 302.2 offset the accumulation. *See id.* annex 302.2(4), 302.2(5).

a required change in tariff classification. The United States Customs Service had interpreted a comparable provision in the CFTA to provide not even a *de minimis* exception, requiring literally 100 percent of nonoriginating materials to meet this test.¹⁰⁴ Article 405 of the NAFTA provides, however, a 7 percent *de minimis* exception. That is, the NAFTA shall generally consider a good as originating if the value of nonoriginating materials that do not undergo the required tariff classification change is (a) "not more than seven percent of the transaction value of the good, adjusted to a F.O.B. basis," or, (b) if the transaction value is "unacceptable," not more than "seven percent of the total cost of the good."¹⁰⁵ Similarly, a good subject to an RVC requirement will qualify if the value of all nonoriginating materials used to produce the good is not more than 7 percent of the adjusted transaction value (or not more than 7 percent of the total cost of the good if the transaction value is unacceptable).¹⁰⁶

However, exceptions to these *de minimis* rules for certain products do exist, for example, originating materials used to produce a gas stove or range.¹⁰⁷

F. FUNGIBLE GOODS AND MATERIALS—ARTICLE 406

The CFTA provides for a value content requirement based on the value of originating materials. The CFTA definitions, however, do not specify how this value should be calculated when the producer uses both originating and non-originating materials that are fungible.¹⁰⁸ The NAFTA expressly provides that in this case the determination of whether materials are originating need not be made through "identification of any specific fungible material," but may be based on "any of the inventory management methods set out in the Uniform Regulations."¹⁰⁹ A similar rule applies where the producer/exporter commingles both originating and nonoriginating fungible goods.¹¹⁰

G. NONQUALIFYING OPERATIONS—ARTICLE 412

Article 412 provides that a good shall not be considered to be an originating good "merely by reason of . . . any production or pricing practice in respect of which it may be demonstrated, on the basis of a preponderance of evidence, that

104. See United States Customs Service Ruling HQ 000117 (Nov. 14, 1991) ("[T]here exists no '*de minimis*' standard or principle in the CFTA's rules of origin for third country materials or components.")

105. NAFTA, *supra* note 1, art. 405(1).

106. *Id.* art. 405(2).

107. *Id.* art. 405(3)(i).

108. CFTA, *supra* note 2, at 296-97.

109. NAFTA, *supra* note 1, art. 406(a).

110. *Id.* art. 406(b). The NAFTA defines "fungible goods" and "fungible materials" as "goods or materials that are interchangeable for commercial purposes and whose properties are essentially identical." *Id.* art. 415.

the object was to circumvent this Chapter."¹¹¹ This article significantly expands the comparable CFTA provision, both in terms of the type of "circumvention" that will justify treating the good as nonoriginating and the showing required to establish such circumvention.¹¹²

III. Customs Procedures—Chapter 5

Presumably as a result of the difficulties that arose under the CFTA, the NAFTA has an entire chapter concerning customs procedures, compared to the limited provisions for these matters in article 406 and Annex 406 of the CFTA. The drafters of the NAFTA divided chapter 5 of the NAFTA into provisions on Certificates of Origin, Administration and Enforcement including Advance Rulings, Review and Appeals of Decisions, Uniform Regulations, and Cooperation.

A. CERTIFICATES OF ORIGIN—ARTICLES 501, 502, AND 503

Unlike the CFTA, the NAFTA article 501 requires the Parties to establish a Certificate of Origin (Certificate) to certify that a good being exported from a Party into another Party qualifies as an originating good.¹¹³ Each Party may require that the Certificate for a good imported into its territory be completed in a language required under its laws.¹¹⁴ In limited instances the NAFTA does not require a Certificate, and the importing Party can waive the certificate requirement in these instances.¹¹⁵

An exporter must complete and sign a Certificate for any exportation of a good for which an importer may claim preferential tariff treatment.¹¹⁶ Where the exporter is not the producer of the good, the exporter may complete and sign the Certificate on the basis of (a) the exporter's knowledge of whether the good qualifies as an originating good; (b) the exporter's reasonable reliance on the producer's written representation that the good qualifies as an originating good; or (c) the exporter's reliance on a completed and signed Certificate for the good that the producer voluntarily provided to the exporter.¹¹⁷ The NAFTA does not require a producer to provide a Certificate to an exporter.¹¹⁸

111. *Id.* art. 412(b).

112. Thus, in terms of the types of circumvention, the comparable CFTA provision is limited to "any process or work," *see* CFTA, *supra* note 2, at 295, compared to the NAFTA reference to "any production or pricing practice," NAFTA, *supra* note 1, art. 412(b). In terms of the showing required, the CFTA requires a showing that the "sole object was to circumvent the provisions of this Chapter," CFTA, *supra* note 2, at 295, in contrast to the demonstration in the NAFTA art. 412 that "the object" was such circumvention.

113. NAFTA, *supra* note 1, art. 501(1). Under the CFTA, a certificate requirement was established by U.S. Customs Service Regulations. *See* 19 C.F.R. § 10.307(c) (1992).

114. NAFTA, *supra* note 1, art. 501(2).

115. *Id.* art. 503(c).

116. *Id.* art. 501(3)(a).

117. *Id.* art. 501(3)(b).

118. *Id.* art. 501(4).

A Party's customs administration must accept a completed and signed Certificate for four years after the date on which an exporter signed it.¹¹⁹ The Certificate may be for a single importation or for multiple importations of identical goods into the Party's territory that occur within a specified time period, not exceeding twelve months, set out therein by the exporter or producer.¹²⁰

An importer that claims the NAFTA tariff treatment must (a) make a written declaration, based on a valid Certificate, that the good qualifies as an originating good;¹²¹ (b) have the Certificate in its possession at the time the importer makes the declaration;¹²² (c) provide, upon request of that Party's customs administration, a copy of the Certificate;¹²³ and (d) promptly make a corrected declaration and pay any duties owed where the importer has reason to believe that a Certificate contains incorrect information.¹²⁴ The failure of an importer to comply with any requirement of chapter 5 may result in denial of the NAFTA tariff treatment.¹²⁵ While NAFTA article 501 provides that an importer will not be subject to penalties for making an incorrect declaration if the importer voluntarily makes a corrected declaration,¹²⁶ NAFTA article 508 allows the imposition of penalties in such a case.¹²⁷ Basically, the U.S. prior voluntary disclosure requirements still apply.¹²⁸

If a good would have qualified as an originating good when it was imported, but an importer did not claim the NAFTA tariff treatment at that time, the importer has one year after the import date to apply for a refund of excess duties paid.¹²⁹ To make such a claim the importer must present a written declaration that the good qualified as an originating good at the time of importation, a copy of the Certificate, and such other documentation relating to the importation of the good as that Party may require.¹³⁰ This provision differs from the current U.S. customs law that limits most changes to entries to ninety days after liquidation,¹³¹ which occurs within one year unless extended¹³² and in practice generally occurs ninety days after entry. Accordingly, this NAFTA provision can both broaden and limit current U.S. law on the finality of liquidation.¹³³

119. *Id.* art. 501(5).

120. *Id.*

121. These provisions are similar to current U.S. law under the NAFTA. *See* 19 C.F.R. § 10.307.

122. *Id.* § 10.307(c).

123. *Id.*

124. NAFTA, *supra* note 1, art. 502(1).

125. *Id.* art. 502(2)(a).

126. *Id.* art. 502(2)(b).

127. *See id.* art 508(1)

128. *See* 19 C.F.R. § 162.74 (1992).

129. NAFTA, *supra* note 1, art. 502(3).

130. *Id.* art. 502(3)(a)–(c).

131. 19 U.S.C. § 1501 (1988).

132. *Id.* § 1504(a).

133. United States law requires that a claim for CFTA preferential treatment be made at the time of filing of the entry summary. 19 C.F.R. § 10.307(a) (1992). Failure to make a timely claim for preference results in liquidation at the rate of duty that would otherwise be applicable. *Id.* § 10.307(b).

An exporter, or a producer that has provided an exporter with a copy of a Certificate, must provide a copy of the Certificate to its customs administration upon request.¹³⁴ If the exporter or producer has reason to believe that the Certificate contains incorrect information, it must promptly notify in writing all persons to whom the Certificate was given of any change that could affect the accuracy or validity of the Certificate.¹³⁵ A false certification by an exporter or a producer that a good is an originating good has the same legal consequences, with appropriate modifications, as apply to an importer in the Party's territory for a contravention of customs laws and regulations regarding a false statement or representation.¹³⁶ Moreover, each Party may apply "such measures as the circumstances may warrant" when an exporter or producer in its territory fails to comply with any requirement in chapter 5.¹³⁷ Finally, article 504 provides that each Party shall not impose penalties on an exporter or a producer in its territory that voluntarily provides written notification of an incorrect Certificate promptly; but, article 508 allows for the imposition of penalties.¹³⁸

B. ADMINISTRATION AND ENFORCEMENT—RECORDKEEPING AND VERIFICATIONS—ARTICLES 505, 506, 509

The NAFTA imposes recordkeeping requirements on exporters or producers who sign the Certificate and on importers. These exporters and producers must maintain for five years after the date of signing (or for longer if specified by the Party from which the good was exported) all records relating to the origin of a good for which they claimed preferential tariff treatment.¹³⁹ The recordkeeping requirement that the NAFTA imposes on the importer includes keeping a copy of the Certificate and all other documentation required by the Party relating to the importation of the good for five years after the date of importation (or longer if specified by the Party into which the good was imported).¹⁴⁰ Thus, a U.S. importer's requirements are basically the same as exist today.¹⁴¹

Under the NAFTA, a Party may conduct a verification to determine whether

134. NAFTA, *supra* note 1, art. 504(1)(a).

135. *Id.* art. 504(1)(b).

136. *Id.* art. 504(2)(a). See United States–Canada Free-Trade Agreement Implementation Act of 1988, Pub. L. No. 100-449, § 205(a)(3), 102 Stat. 1851, 1864 (1988) (codified as amended at 19 U.S.C. § 2112 note (1988 & Supp. III 1991)). Basically, civil Customs penalties apply. See 19 U.S.C. § 1592 (1988).

137. NAFTA, *supra* note 1, art. 504(2)(b).

138. See *id.* art. 508.

139. Such records include (but presumably are not limited to): the purchase of, cost of, value of, and payment for: (1) the good that is exported from a Party's territory; (2) all materials, including indirect materials, used in the production of the good that is exported from a Party's territory; and (3) the production of the good in the form in which the good was exported from the Party's territory. *Id.* art. 505(a).

140. *Id.* art. 505(b).

141. See 19 C.F.R. § 162.16 (1992) for U.S. recordkeeping requirements.

a good imported into its territory is an originating good.¹⁴² Unless the Parties agree to another procedure,¹⁴³ verification must be by (1) written questions to an exporter or a producer in the territory of another Party;¹⁴⁴ or (2) visits to the premises of an exporter or a producer in the territory of another Party to review the records that must be kept according to article 505(a) and to observe the facilities used in production.¹⁴⁵ Prior to such a visit the Party, through its customs administration, must deliver a written notification¹⁴⁶ of its intention to conduct the visit to (1) the exporter or producer in question; (2) the customs administration of the Party in whose territory the exporter or producer is located;¹⁴⁷ and (3) if requested by the other Party, the embassy of the other Party in the territory of the Party proposing to conduct the visit.¹⁴⁸ Before the visit the Party must also obtain the written consent of the exporter or producer whose premises are to be visited.¹⁴⁹ If the exporter or producer does not give its written consent within thirty days of receipt of the notification, the Party may deny preferential tariff treatment to the good.¹⁵⁰

During the visit the exporter or producer may have two observers present provided that (1) the observers do not participate other than as observers, and (2) the failure of the exporter or producer to designate observers shall not result in postponement of the visit.¹⁵¹

The Party must conduct the verification of the RVC requirement in accordance with the Generally Accepted Accounting Principles (GAAP) applied in the territory of the Party from which the goods were exported.¹⁵²

The Party conducting the visit will provide the exporter or producer with a written determination of whether the good in question qualifies as an originating

142. NAFTA, *supra* note 1, art. 506(1).

143. *Id.* art. 506(1)(c).

144. *Id.* art. 506(1)(a). Whether this provision is limited to producers who sign a certificate is unclear. But the verification requirement will likely apply to all producers of exported goods.

145. *Id.* art. 506(1)(b). Again, whether all producers are covered by this provision is unclear.

146. The notification must contain the following: (1) the identity of the customs administration issuing the notification; (2) the name of the exporter or producer to be visited; (3) the date and place of the visit; (4) the object and scope of the visit, including specific reference to the good in question; (5) the names and titles of the officials performing the visit; and (6) the legal authority for the visit. *Id.* art. 506(3).

147. When the customs administration in a territory receives notification that another Party proposes a verification visit, it may, within 15 days of receipt, postpone the proposed visit for up to 60 days or for a longer period if the Parties agree. *Id.* art. 506(5). A Party is not to deny preferential treatment to a good "solely" on the postponement of a verification visit. *Id.* art. 506(6). Nonetheless, penalties may be imposed. *See id.* art. 508.

148. *Id.* art. 506(2)(a)(iii).

149. *Id.* art. 506(2)(b).

150. *Id.* art. 506(4). It is unclear if this denial is permanent or temporary and can be retroactively applied later under art. 502.

151. *Id.* art. 506(7). We understand that the NAFTA drafters intended these limitations to apply to officials of the government of the exporter or producer, not outside accountants and attorneys for the exporter or producer.

152. *Id.* art. 506(8).

good.¹⁵³ Findings of fact and conclusions of law must be a part of this determination.¹⁵⁴

If the verification visit indicates a pattern of conduct by an exporter or a producer of false or unsupported representations that a good imported into its territory qualifies as an originating good, the Party may withhold preferential tariff treatment to identical goods exported or produced by the exporter or producer until it establishes compliance with the NAFTA rules of origin.¹⁵⁵ When an importing Party denies preferential treatment as a result of differing tariff classifications or customs values by the Parties from whose territory the good was exported and imported,¹⁵⁶ the importing Party's negative determination does not take effect until the Party notifies in writing both the importer of the good and the person who completed and signed the Certificate.¹⁵⁷ Further, a Party may not apply such a determination to importations made before the effective date of the determination when (a) the customs administration of the Party from whose territory the good was exported has issued an advance ruling on the tariff classification or on the customs value of such materials, or has given consistent treatment to the entry of the materials under the tariff classification or customs value at issue, on which a person can rely;¹⁵⁸ and (b) the advance ruling or consistent treatment was given prior to notification of the determination.¹⁵⁹ Moreover, the customs administration of a Party must postpone the effective date of such a determination for a period not exceeding ninety days if the importer or person who completed and signed the Certificate demonstrates that it relied in good faith to its detriment on the tariff classification or customs value applied to such materials by the customs administration of the exporting Party.¹⁶⁰

In an attempt to increase certainty, the NAFTA requires each Party to issue advance rulings on certain issues to importers in its territory or to exporters or producers in the territory of another Party.¹⁶¹ Each Party must have procedures for the issuance of advance rulings, including a detailed description of the information that must be provided to process the application for the ruling.¹⁶² Each Party's

153. *Id.* art. 506(9).

154. *Id.*

155. *Id.* art. 506(10).

156. *Id.* art. 506(11).

157. *Id.* art. 506(11).

158. *Id.* art. 506(12)(a). See 19 C.F.R. § 177.10(b)-(e) (1992) for U.S. laws and regulations specifying practices (i.e., letter rulings and a uniform and established practice) on which a person can rely.

159. NAFTA, *supra* note 1, art. 506(12)(b).

160. *Id.* art. 506(13); see also 19 C.F.R. § 177.10(e).

161. NAFTA, *supra* note 1, art. 509(1). These issues include whether a good meets the value content requirement, whether there has been a requisite change in tariff heading; the appropriate customs value; whether a good qualifies as originating; qualification for duty free treatment after repair or alteration; country of origin marking; and such other matters as the Parties may agree. See also 19 C.F.R. § 177.0-9 (1992) (U.S. Customs Service's regulations on rulings). The CFTA regulations do not refer to rulings. *Id.* § 10.300.

162. NAFTA, *supra* note 1, art. 509(2).

customs administration may request supplemental information from the person requesting the ruling and, after obtaining all necessary information, must issue a ruling within time periods to be specified in the Uniform Regulations.¹⁶³ When an advance ruling is unfavorable to the person requesting it, the customs administration that issued the ruling must provide a full explanation of the reasons for the ruling.¹⁶⁴

The NAFTA also requires consistency in issuing rulings. If the facts and circumstances surrounding a request for a ruling are identical in all material respects to the facts and circumstances surrounding another request, the Party must provide the same treatment, including the same interpretation and application of the provisions of chapter 4 regarding a determination of origin, to each request.¹⁶⁵ As a practical matter, the United States already has a broad advance rulings program.¹⁶⁶

In general, an advance ruling applies to importations beginning on the date of its issuance or any later date specified in the ruling.¹⁶⁷ A Party may modify or revoke a ruling¹⁶⁸ and any such modification or revocation takes effect on the date issued or on a specified later date.¹⁶⁹ If a person can show detrimental reliance, however, a Party shall postpone the effective date of a modification or revocation for up to ninety days.¹⁷⁰ A Party can apply a modification or revocation to earlier importations if the person who requested the ruling did not act in accordance with its terms and conditions. If a Party modifies or revokes a ruling because the ruling was based on incorrect information, the person requesting the ruling will not be subject to penalties if that person demonstrates that it used reasonable care and acted in good faith in presenting the facts and circumstances in question.¹⁷¹ If a person has misrepresented or omitted material facts or circumstances, however, a Party may apply such measures as warranted by the circumstances.¹⁷²

C. UNIFORM REGULATIONS—ARTICLE 511

While the NAFTA is much more specific than the CFTA, further specificity will result from the Uniform Regulations, which will interpret, apply, and administer chapters 4 and 5 and "other matters as may be agreed to by the Parties."¹⁷³ The Parties must establish and implement Uniform Regulations

163. *Id.* art. 509(3)(a), (b).

164. *Id.* art. 509(3)(c).

165. *Id.* art. 509(5).

166. *See* 19 C.F.R. § 177.0-.9.

167. NAFTA, *supra* note 1, art. 509(4).

168. *Id.* art. 509(5).

169. *Id.* art. 509(7).

170. *Id.* art. 509(8). This provision is similar to U.S. regulations. 19 C.F.R. § 177.9(d)(2) (1992).

171. NAFTA, *supra* note 1, art. 509(11).

172. *Id.* art. 509(12).

173. *Id.* art. 511(1).

through their respective laws or regulations. The Parties also must implement any modifications to the Uniform Regulations within 180 days after the Parties agree to them.

D. REVIEW AND APPEAL

Each Party must grant substantially the same rights of review and appeal of determinations of origin and advance rulings by its customs administration as it provides to importers in its territory to any person who completes and signs a Certificate; to any person whose good has been the subject of a country of origin marking determination pursuant to article 311; or to any person who has received an advance ruling pursuant to article 509(1).¹⁷⁴ The rights of review and appeal must include access to "(a) at least one level of administrative review independent of the official or office responsible for the determination under review; and (b) in accordance with [the Party's] domestic law, judicial or quasi-judicial review of the determination or decision taken at the final level of administrative review."¹⁷⁵

E. COOPERATION WORKING GROUP AND CUSTOMS SUBGROUP—ARTICLES 512, 513

The NAFTA provides for cooperation among the Parties by notification of actions, cooperation in enforcement, and establishment of working groups and subgroups with at least quarterly meetings.

IV. Conclusion

As should be apparent from the above discussion, the NAFTA drafters made a considerable effort to provide detailed origin rules and customs procedures in the NAFTA, a result that presumably stemmed in significant part from difficulties and uncertainties that arose in connection with the much more summary comparable provisions in the CFTA. Further, in an effort to encourage consistency in application among the Parties, the NAFTA drafters also provided for Uniform Regulations to be jointly developed and implemented by each of the three Parties. Indeed, it is an indication of how complex and important these origin rules and customs procedures are that the development of such Uniform Regulations was thought essential notwithstanding the detail that exists in the NAFTA provisions themselves.

As a substantive matter, the NAFTA origin rules appear to be a considerable improvement over the comparable rules in the CFTA. And these NAFTA rules

174. *Id.* art. 510(1).

175. *Id.* art. 510(2)(b). The United States may not currently meet this standard, since the U.S. regulations do not specifically provide for administrative review, at least of Customs' Headquarters decisions. See 19 C.F.R. § 177.2 (1992).

should be considerably easier to implement both for the producers, exporters, and importers who must deal with the origin judgments in the first place and for the Parties reviewing these judgments in verification proceedings. If the past is any guide, however, notwithstanding the efforts of the NAFTA drafters, there will inevitably be uncertainties and controversies in the actual implementation of the NAFTA origin and customs provisions.

