

Primer: Substantial Transformation

General Rules

In the United States, non-preferential rules of origin employ the “wholly obtained” criterion for goods that are wholly the growth, product, or manufacture of a country. For goods that consist of materials from more than one country, the rules employ the “substantial transformation” criterion. “Substantial transformation” is typically based on a change in name, character, and use—meaning that an article is a product of the country in which it has been substantially transformed into a new and different article with a name, character, and use distinct from that of the article(s) from which it was so transformed.

The determinative factor is the extent of operations performed and whether the parts lose their identity and become an integral part of the new article. *Belcrest Linens v. United States*, 573 F. Supp. 1149, 1152 (Ct. Int'l Trade 1983), *aff'd* 741 F.2d 1368 (Fed. Cir. 1984). Assembly operations that are simple and minimal as opposed to complex or meaningful generally do not result in a substantial transformation. Further, if the manufacturing or combining process is merely a minor one that leaves the identity of the imported article intact, a substantial transformation has not occurred. *Uniroyal, Inc. v. United States*, 542 F. Supp. 1026, 1029 (Ct. Int'l Trade 1982), *aff'd* 702 F.2d 1022 (Fed. Cir. 1983).

To determine whether a substantial transformation occurs when components of various origin are combined into a finished good, Customs and Border Protection (CBP) evaluates the totality of the circumstances on a case-by-case basis. Primary factors for consideration include the country of origin of the components, extent of processing within a country, and whether processing results in a product with a new name, character, and use. Additional factors, such as the resources expended on product design and development, the extent and nature of post-assembly inspection and testing procedures, worker skill required during manufacturing, and software programming that confers a new use or function are also considered. No one factor is determinative.

NAFTA Rules

Goods that are imported into the U.S. from Mexico or Canada are subject to different rules of origin under NAFTA. The “wholly obtained” criterion still applies, but for goods that consist of materials from more than one country, the origin is determined by a “tariff-shift” method based on changes to the classification of goods. For example, “a change to subheading 9003.90 from any other heading” in the HTSUS would constitute a change in the origin of goods subject to these rules.

Goods Subject to Section 301 Tariffs

In HQ H300226 (Sept. 13, 2018), CBP reconsidered an earlier ruling (NY N299096 (July 25, 2018)) regarding the origin of an electric motor assembled in Mexico using three Chinese-origin parts subject to Section 301 duties. In NY N299096, CBP applied the NAFTA Rules to determine the country of origin of the final product for both duty and marking purposes. Those rules generally required that any non-originating components undergo a requisite tariff shift as set forth in the rule applicable to the final product's tariff classification.

CBP explained in HQ H300226 that, for purposes of assessing Section 301 duties, CBP now will apply the substantial transformation standard to determine the country of origin of merchandise produced in Canada or Mexico using components subject to Section 301, rather than the NAFTA Marking Rules. CBP wrote that if operations in Mexico involve Chinese-origin components subject to Section 301 duties, the NAFTA Marking Rules apply only for purposes of determining the country of origin for *marking* purposes and that the substantial transformation standard applies for purposes of determining country of origin for *duty liability* purposes. This approach, which previously had been applied only in the context of antidumping and countervailing duties and safeguard measures, resulted in a final product that will be marked as Mexican-origin but will be treated as Chinese-origin for duty purposes.