PEANUT BUTTER – SANDWICHED BETWEEN COMPETING COUNTRY OF ORIGIN MARKING REQUIREMENTS:

AN ANALYSIS OF *BESTFOODS V. UNITED STATES*

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The full extent of the role of peanut butter in shaping international trade and customs laws has never been fully appreciated! All joking aside, the confusion over how to properly mark Canadian peanut slurry for U.S. country of marking purposes has led to one of the most important recent developments in international trade and customs law, a development so important that it changes nearly one hundred years of existing U.S. practice.

On December 17, 1992, the U.S., Canada, and Mexico signed the North American Free Trade Agreement (the "NAFTA")[1] and, in doing so, created the largest free trade area in the world. Implementation of the NAFTA in the U.S. gave rise to new country of origin marking requirements that dramatically altered the traditional approach used in the U.S. for nearly one hundred years. The new NAFTA country of origin marking requirements created much confusion among U.S. based importers and even befuddled U.S. Customs and the U.S. Court of International Trade. Nowhere is this confusion more apparent than in *Bestfoods v. United States,*[2] a recent decision of the U.S. Court of Appeals for the Federal Circuit, where the issue was how to properly mark "Skippy" brand peanut butter.

The Federal Circuit's decision in *Bestfoods* resolved this confusion by holding that the NAFTA's tariff-shift test rather than the traditional substantial transformation test applies for country of origin marking requirements for goods imported from Canada or Mexico. After *Bestfoods*, it is clear that two separate and distinct regimes exist for determining country of origin marking requirements under U.S. law. One for goods imported from a NAFTA country and another for goods imported from a non-NAFTA country. As a result, U.S. companies conducting business with Mexico and Canada need to ensure that their products meet the applicable NAFTA tariff-shift requirements in order to receive benefits under the NAFTA.

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1 North American Free Trade Agreement, Dec. 17, 1992, 32 I.L.M. 289 (1993).

2 165 F.3d. 1371 (Fed. Cir. 1999).

Before addressing the sticky issue of the proper country of origin marking requirements of peanut butter in *Bestfoods,* this comment first examines the development of country of origin marking requirements under the traditional substantial transformation test. Next, this comment focuses on the development of a competing test, the tariff shift test, as a means to determine country of origin for marking purposes. Third, this comment discusses the NAFTA's tariff-shift test for determining country of origin marking requirements. Fourth, this comment returns to the *Bestfoods* decision and analyzes judicial interpretation of the NAFTA's country of origin marking requirements. Finally, this comment looks at the impact the *Bestfoods* decision will have on the global trading community.

I. THE ORIGIN AND DEVELOPMENT OF COUNTRY OF ORIGIN MARKING REQUIREMENTS UNDER THE SUBSTANTIAL TRANSFORMATION REGIME

Every day U.S. consumers, cognizant of it or not, come face to face with U.S. country of origin marking requirements. As we shop for products we learn that the car we want was "Made in South Korea," the stereo system "Made in Japan," the clothes "Made in Mexico," the toy "Made in China" and in the *Bestfoods* case the peanut butter "Made in Canada."

A. THE FEDERAL MARKING STATUTE: 19 U.S.C. 1304

Country of origin marking requirements first appeared in the U. S. with the passage of the Tariff Act of 1890[3] and have been a part of every tariff act subsequently passed by the U.S. Congress including section 304 of the Tariff Act of 1930, as amended (19 U.S.C. 1304) (the "Marking Statute"). The Marking Statute reads in pertinent part:

> Every article of foreign origin ... imported into the United States shall be marked in a conspicuous place as legibly, indelibly, and permanently as the nature of the article will permit in such a manner as to indicate to an ultimate purchaser in the United States the English name of the country of origin of the article.

The purpose of the Marking Statute is to facilitate consumer purchasing decisions by indicating to the consumer where a product was

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[3] Tariff Act of 1890, ch. 1244, 2504, 26 Stat. 567, 613 (1891) (codified at 19 U.S.C. § 1304).

manufactured. As explained by the U.S. Court of Customs and Patent Appeals, the predecessor to the current U.S. Court of International Trade ("CIT"), in *United States v. Friedlaender & Co.*, the purpose of the Marking Statute is "to mark goods so that at the time of purchase the ultimate purchaser, may by knowing where the goods are produced, be able to buy or refuse to buy them, if such marking will influence his will."[4] Providing consumers with the information required by the Marking Statute allows markets to operate more efficiently and facilitates free trade by allowing more informed purchasing decisions.[5] The Marking Statute further allows U.S. consumers who prefer domestic goods to easily detect and purchase them, thus benefiting domestic producers vis a vis global competitors.[6] For this reason, country of origin marking requirements can function as a non-tariff barrier to trade by imposing requirements that make it commercially difficult, if not impossible, to mark, and therefore to import, a particular item.

The Marking Statute is implemented under U.S. law by regulations issued by the U.S. Customs Service ("Customs"). The regulations require an importer to determine a single country of origin for an imported article. During the early years of the Marking Statute designating one country of origin was a relatively easy task since goods were usually made in one country with no foreign inputs. Under such a circumstance the country of origin of the good was the country of production. However, with the rise in multi-national corporations a good may pass through several countries and processes of manufacture before importation into the U.S. In such a circumstance, determination of the good's country of origin becomes extremely difficult and complex.

Country of origin marking rules are of more than just mere academic interest. The Marking Statute has become a pitfall for those involved in the import-export business because failure to follow the rules can have very real world consequences that can substantially affect the bottom line of such companies. Failure to comply with the Marking Statute and accompanying

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[4] 27 C.C.P.A. 297, 302 (1940). In *Friedlaender*, the issue involved the proper country of origin marking of imported merchandise which was wholly manufactured in Czechoslovakia, except at the time the goods were exported, the territory in which the goods were manufactured was under German occupation. Customs held that marking the goods as products of Czechoslovakia was not acceptable. The court agreed with Customs and held that as the goods were exported at a time when that part of Czechoslovakia in which the goods were manufactured was under German occupation, the marking "Czechoslovakia" was not in compliance with the requirements of the marking statute, and the goods should be marked to indicate "Germany" as the country of origin.

[5] Nadine S. Samter, *National Juice Products Association v. United States: A Narrower Approach to Substantial Transformation Determinations for Country of Origin Marking*, 18 LAW & POLICY IN INT'L. BUS. 671 (1986).

[6] *Id.*

regulations can result in harsh penalties. For example, customs can seize or require supplemental marking duties on products marked with the incorrect country of origin.[7] Importers also face monetary or criminal penalties if the country of origin mark is intentionally obscured, removed, or altered.[8]

B. THE SUBSTANTIAL TRANSFORMATION TEST

An analysis of country of origin marking requirements requires an understanding of the interplay between the terms "ultimate purchaser" and "substantial transformation." The term "ultimate purchaser" is not defined in the Marking Statute nor has Congress ever attempted to provide a definition of the term. Nevertheless, broadly stated, an "ultimate purchaser" may be defined as the last person in the U.S. who receives an article in the form in which it was imported. Therefore, if the imported article will be used for manufacturing in the U.S., then the manufacturer is the "ultimate purchaser;" if the article is to be sold at retail in its imported form, then the purchaser at retail is the "ultimate purchaser."

"Substantial transformation" is significant for country of origin marking requirements because it determines who will be the "ultimate purchaser" of the product. A U.S. manufacturer will be the "ultimate purchaser" if it "substantially transforms" the imported product. On the other hand, the U.S. consumer will be the "ultimate purchaser" if the U.S. manufacturer does not "substantially transform" the imported product. Determining whether a "substantial transformation" has taken place is of extreme importance under the Marking Statute because if a "substantial transformation" takes place the product will be considered a product of the U.S. and the importer will not be required to mark the product under the Marking Statute. As a result, a U.S. manufacturer will do everything in its power to "substantially transform" an imported product so they can mark the product "Made in the U.S.A."

While no statutes or regulations specifically define the term "substantial transformation," various court decisions have given meaning to the phrase. The first definitive statement on substantial transformation came from the U.S. Supreme Court in 1908 in *Anheuser-Busch Brewing Ass'n v.*

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[7] Michael P. Maxwell, *Formulating Rules of Origin for imported Merchandise: Transforming the Substantial Transformation Test*, 23 GEO. WASH. J. INT'L L. & ECON. 669, 670 (1990).

[8] *Id.* Maxwell continues, "The Trademark Act of 1946, 15 U.S.C. §§1051-1127, prohibits the importation of articles of foreign origin which display a name or mark intended to persuade the public to believe that an imported product was manufactured in the U.S. or in any foreign country other than the country in which it was actually manufactured." *Id.*

United States.[9] In this decision, the Supreme Court stated that a product is substantially transformed when it is transformed into a "new and different article ... having a distinctive name, character or use."[10]

The seminal case interpreting substantial transformation under the Marking Statute is *United States v. Gibson-Thomsen Co., Inc.*[11] In *Gibson-Thomsen,* a U.S. company imported wood brush blocks and toothbrush handles into the port of New York from Japan.[12] After importation, the U.S. manufacturer inserted bristles into both the wood brush blocks and toothbrush handles thereby converting them into hairbrushes and toothbrushes. The U.S. Court of Customs and Patent Appeals found that the Japanese parts, after processing in the U.S., lost their identity and became new articles having a new name, character and use.[13] Therefore, the court found that the U.S. manufacturer and not the U.S. consumer was the ultimate purchaser of the imported products from Japan thereby exempting the finished products from the marking requirements of the Marking Statute.

The *Gibson-Thomsen* test has gained wide acceptance and is incorporated into section 134.35(a) of the Code of Federal Regulations.[14] In addition, the *Gibson-Thomsen* new "name, character and use" substantial transformation test has been cited in virtually every case applying the Marking Statute and has consistently been followed by courts in determining whether imported goods must be marked in accordance with the Marking Statute.[15] Despite the long history the *Gibson-Thomsen* substantial

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9 207 U.S. 556, 562 (1908). In *Anheuser-Busch,* the U.S. Supreme Court held that corks imported from Spain did not qualify for duty drawback, because the corks were not manufactured in the U.S. from imported materials, but were chemically and physically treated in the U.S. to make them fit for use in bottling beer for export. The drawback statute at issue in *Anheuser-Busch* allowed a U.S. importer to collect a refund of U.S. duties paid on imported materials if the imported materials were used in the manufacture of a product that was subsequently exported from the U.S. In *Anheuser-Busch,* the Supreme Court found that the exported product was beer, not cork, so the duties paid on the imported cork were not subject to the duty drawback.

10 *Id.* at 556.

11 27 C.C.P.A. 267 (1940).

12 *Id.* at 268.

13 *Id.* at 270.

14 134.35 C.F.R. Articles Substantially Changed by Manufacture. (a) *Articles other than goods of a NAFTA country.* An article used in the U.S. in manufacture which results in an article having a name, character or use differing from that of the imported article, will be within the principle of the decision in the case of *United States v. Gibson-Thomsen Co., Inc.* Under this principle, the manufacturer or processor in the U.S. who converts or combines the imported article into the different article will be considered the "ultimate purchaser" of the imported article within the contemplation of ... the Marking Statute ... and the article shall be excepted from marking. The outermost containers of the imported articles shall be marked in accord with this part.

15 *See e.g.* Uniroyal, Inc. v. U. S., 702 F.2d 1022 (Fed. Cir. 1983); Nat'l Hand Tool Corp. v. U. S., 16 CIT 308, 1992, WL 101006 (1992); Koru North America v. U. S., 12 CIT 1120, 701 F.Supp. 229 (1988); Superior Wire v. U. S., 11 CIT 608, 669 F.Supp. 472 (1987); Ferrostaal Metals Corp. v. U. S., 11 CIT 470, 664 F.Supp. 535 (1987); Nat'l Juice Products Ass'n v. U.S.,

transformation test has enjoyed under U.S. trade and customs law, its administration has not been without problems. Most of these problems stem from the fact that the test is applied on a case-by-case basis and requires courts to make subjective judgments as to what constitutes a new and different article.[16] The fact that application of the substantial transformation test has been the subject of a plethora of judicial and administrative determinations is proof that the test fails to provide those involved in the import-export business the necessary degree of predictability to make important business decisions. Because of the perceived inadequacies of the substantial transformation test, a competing test has recently evolved to provide a greater degree of certainty and predictability to those involved in the import-export business.

II. THE TARIFF-SHIFT TEST

A. HOW A TARIFF-SHIFT TEST WORKS

Unlike a substantial transformation test which looks to see if processing or manufacturing of an imported good results in a new good with a different name, character and use, a tariff-shift test looks to see if operations performed in the importing country are sufficient to change the tariff classification of a good. Essentially a tariff-shift test requires classification of the good in question twice: once on arrival into a country and again on departure from the country or if the good stays in the domestic marketplace upon exit from a U.S. manufacturing facility. If the exported good or good released to the market has a different tariff classification than the imported good, then a tariff-shift has taken place and the U.S. manufacturer whose processing resulted in the tariff-shift is able to mark the good as "Made in the U.S.A." The advantage of a tariff-shift test, as opposed to a substantial transformation test, is that it is transparent and is based upon objective, specific criterion, thereby providing a degree of certainty and objectivity to both those in the international trading community and Customs officials who must apply the Marking Statute to a variety of goods in a variety of circumstances.

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10 CIT 48, 628 F. Supp. 978 (1986); Carlson Furniture Indus. v. U. S., 65 Cust.Ct. 474, C.D. 4126 (1970); Midwood Indus., Inc. v. U.S., 64 Cust.Ct. 499, C.D. 2046, 313 F.Supp. 951 (1970), and Grafton Spools, Ltd. V. United States, 45 Cust.Ct. 16, C.D. 2190 (1960).

[16] Mark R. Sandstrom, *Rules of Origin: Consideration for Investment and Trade in North America*, 16 ARIZ. J. INT'L. & COMP. L. 217, 221 (1999).

B. EVOLUTION OF THE TARIFF-SHIFT TEST

In addition to the disadvantages of the substantial transformation test referenced above, several factors have enhanced the desirability of the tariff-shift test. Most prominent are the signing of the U.S. – Canada Free Trade Agreement and implementation of the Harmonized Commodity Description and Coding System (the "Harmonized System").

In 1988, the U.S. and Canada signed the U.S.-Canada Free Trade Agreement ("CFTA")[17] which eliminated tariffs and other barriers to trade between the two countries.[18] In the CFTA negotiations, Canada rejected the traditional substantial transformation test used in the U.S. for determining the country of origin of an imported product.[19] Canada's rejection of the substantial transformation test led to the establishment of a tariff-shift regime for determining the country of origin of a product under the CFTA. Article 301 and Annex 301.2 of the CFTA requires that for marking purposes materials imported into the U.S. or Canada from a third country must undergo specific types of processing in the U.S. or Canada that produce a change in the material's tariff heading.

The tariff-shift test also received a boost in 1988 when most trading countries in the world adopted the Harmonized System.[20] The theory behind a world-wide Harmonized System is that a good should carry the same tariff number and description in any country, even though the tariff rate may well differ from country to country. The U.S. implemented the Harmonized System on January 1, 1989, as the Harmonized Tariff Schedule of the U.S.[21]

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[17] United States – Canada Free Trade Agreement, Jan. 2, 1988, United States – Canada, 27 I.L.M. 293 (1988).

[18] At the time, the CFTA was the first all sector free trade agreement entered into by the U.S. 16 ARIZ. J. INT'L & COMP. L. 217, 222 (1999).

[19] Allan S. Galper, *Restructuring Rules of Origin in the U.S. – Israel Free Trade Agreement: Does the EC – Israel Agreement Offer an Effective Model,* 19 FORDHAM INT'L. L. J. 2028, 2062 (1996).

[20] The Harmonized System has twenty-two sections divided into ninety-seven chapters and contains over 5,000 article descriptions using a six-digit description for all products. The HTS headings are designed to progress from crude products to those based on increasingly sophisticated processing. The first two digits are the "Chapter" in which the product is contained. There are ninety-seven Chapters in the Harmonized System, reflecting the diversity of possible product categories. The first four digits taken together are called the "Heading" and provide a more specific description of the product. The last two digits of the six digits provide a still more specific level of description. Some individual countries, including the U.S., have added two to four more digits for a total of ten digits. These additional digits are for tariff rate distinctions and for statistical purposes. For example sweet cherries would fall under the classification number 0809.20. This would indicate Chapter 8 (edible fruits and nuts), Heading 0809 (apricots, cherries, peaches and nectarines, plums and sloes), and subheading 0809.20 (cherries). Robert J. Leo & Ralph H. Sheppard, *NAFTA Rules of Origin – Improvements on Past Rules?,* 6 AUT. INT'L L. PRACTICUM 24, 25 (1993).

[21] *Id.*

Prior to the development of the Harmonized System it would have been very difficult and indeed impractical for the U.S. to adopt a tariff-shift system since U.S. tariff schedules were based on different nomenclatures than the tariff schedules of its trading partners.[22]

No doubt, the NAFTA negotiators were cognizant of these developments during the NAFTA negotiations; in fact, the CFTA was the starting point for the NAFTA negotiations.[23] As a result, it should come as no surprise that the NAFTA's country of origin marking requirements are based on a tariff-shift test and not the traditional *Gibson-Thomsen* substantial transformation test.

III. COUNTRY OF ORIGIN MARKING UNDER THE NAFTA

A. ARTICLE 311 AND ANNEX 311 OF THE NAFTA

The issue of country of origin marking was discussed at great length during the NAFTA negotiations. Prior to the NAFTA, the marking requirements in the U.S., Mexico and Canada were widely divergent. In the U.S., Customs used the substantial transformation approach, as interpreted in a series of judicial decisions, to determine the country of origin of goods. In contrast, Mexico had not administered marking rules of origin and Canada had done so only in limited circumstances.[24] As a result, some at the NAFTA negotiating table suggested that marking requirements be eliminated entirely for NAFTA goods traded within North America since marking requirements were inconsistent with the notion and creation of a free trade zone. Disputes between the parties soon narrowed and centered on the issue of whether country of origin markings should be uniform or merely based on uniform principals.[25] Ultimately, the parties agreed to establish Marking Rules uniform in principal for purposes of determining country of origin marking requirements under the NAFTA.[26]

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[22] United States – Canada Free Trade Agreement, *supra* note 17 at 222. In fact, dissimilarity between U.S. and non – U.S. tariff schedules created all sorts of difficulties in the negotiation of tariff reductions under the Kennedy and Tokyo Round conducted under the GATT. *Id.* at 222-23.

[23] Leo, *supra* note 20.

[24] Andrew W. Shoyer, *Market Access and the North American Free Trade Agreement*, 4 TRANSNAT'L LAW AND CONTEMP. PROBS. 133, 155 (1994).

[25] Scott Otteman, *U.S. Balks at Call for Identical Marking Rules in First NAFTA Meeting*, INSIDE NAFTA, Jan. 26, 1994 at 1, 8.

[26] Marking Rules are defined simply as "rules for determining whether a good is a good of a Party" under Annex 311(1).

The NAFTA Marking Rules, not unlike the federal Marking Statute, require products imported from a NAFTA country to bear a conspicuous, legible, and sufficiently permanent country of origin mark that indicates to the ultimate purchaser of the product the name of its country of origin. The definitional provisions of Annex 311 make it clear that the Marking Rules that each NAFTA party was obligated to adopt must employ a tariff-shift method for determining whether a good is a good of the exporting country or whether it has been sufficiently altered after importation to qualify as a good of the importing country.[27] Just as the Marking Statute has traditionally exempted from the marking requirements goods that were substantially transformed in the U.S., the NAFTA Marking Rules exempt from country of origin marking requirements any good of another NAFTA country that undergoes production in the territory of the importing party, by the importer, in a manner that results in the good becoming a good of the importing party under the Marking Rules.[28] The effect of this provision is to exempt a good from the NAFTA Marking Rules if it undergoes processing in the importing country that results in a change in the tariff classification of the good.

B. U.S IMPLEMENTATION OF THE NAFTA MARKING RULES

U.S. obligations under the NAFTA were implemented into national law by the NAFTA Implementation Act of 1993 (the "Implementation Act").[29] The Implementation Act authorized the promulgation of such regulations as necessary or appropriate to immediately implement applicable U.S. obligations under the NAFTA. Pursuant to U.S. obligations under Annex 11 of the NAFTA, U.S. Marking Rules were promulgated by the Secretary of the Treasury of the U.S. (the "Secretary") in 19 C.F.R. Part 102 and 19 C.F.R. Part 134, section 134.35.[30]

These regulations treat NAFTA and non-NAFTA goods differently for purposes of country of origin marking requirements. For non-NAFTA goods, 19 C.F.R. section 134.35(a) directs the use of the familiar *Gibson-*

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[27] Specifically, the term "ultimate purchaser" is defined to mean "the last person in the territory of an importing Party that purchases the good in the form in which it was imported," and the phrase "the form in which it was imported" is defined to mean "the condition of the good before it has undergone one of the changes in tariff classification described in the Marking Rules." *See* Annex 311(11).

[28] *Id.* at ¶ 5(b)(viii).

[29] North American Free Trade Agreement Implementation Act of 1993, Pub.L. 103-182, 107 Stat. 2057-2225 (1993).

[30] 19 C.F.R. § 102 set forth rules for determining the country of origin of imported goods for the purposes specified in paragraph 1 of Annex 311 of the NAFTA. 19 C.F.R. § 134 sets forth regulations implementing the country of origin marking requirements and exceptions to the Marking Statute.

Thomsen new "name, character or use" test to determine whether a good has been substantially transformed following its importation into the U.S. and therefore exempt from the Marking Statute. For NAFTA goods, 19 C.F.R. section 134.35(b) directs the use of the tariff-shift method and exempts from the Marking Statute those goods that are to be processed in the U.S. in a manner that would result in the good becoming a good of the U.S. under the NAFTA Marking Rules.[31] Confusion over these similar yet distinct regimes soon developed after the Secretary promulgated the regulations.

IV. JUDICIAL INTERPRETATION OF THE NAFTA'S COUNTRY OF ORIGIN MARKING REQUIREMENTS: *BESTFOODS V. UNITED STATES*

Bestfoods was the first judicial challenge to the new NAFTA country of origin Marking Rules and concerned the issue of whether "Skippy" brand peanut butter should be marked as "Made in the U.S.A." or "Made in Canada." Before reaching the federal circuit this sticky issue had been the subject of two Customs' ruling and two decisions by the CIT. While *Bestfoods* did not definitively settle the issue of how "Skippy" brand peanut butter should be marked, it did eliminate the cloud that previously hung over the issue of the proper country of origin marking of NAFTA goods.

A. THE FACTS OF *BESTFOODS*

Bestfoods,[32] a major multi-national food producer, produces "Skippy" brand peanut butter at its Little Rock, Arkansas plant. An essential ingredient of "Skippy" brand peanut butter is peanut slurry.[33] Bestfoods needed to use both domestic and foreign peanut slurry in making "Skippy" brand peanut butter. The foreign peanut slurry Bestfoods proposed to use was processed in Canada from shelled peanuts from various countries. Prior to importing the Canadian peanut slurry, Bestfoods sought an administrative ruling from Customs on whether its "Skippy" brand peanut butter containing

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[31] 19 C.F.R. § 102.20 which contains very detailed sets of charts containing the various HTSUS numbers and indicate the requirements for whether the required "tariff shift" has taken place.

[32] Bestfoods is formerly known as CPC International, Inc. To avoid confusion, throughout this article we have chosen to call the plaintiff Bestfoods even though the real party of interest in the first two cases was CPC International, Inc.

[33] Peanut slurry is a gritty paste made from shelled peanuts that have been roasted, blanched, split and ground. 21 C.I.T. at 786. Peanut slurry lacks the smooth and creamy character and flavor which consumers typically associate with peanut butter, however peanut slurry can be sold commercially as old fashioned or natural peanut butter. *Id.*

a small amount of Canadian origin peanut slurry must be marked to show Canada as the country of origin as required by federal the Marking Statute.

Accompanying Bestfoods request for an administrative ruling was the following proposed manufacturing process of "Skippy" brand peanut butter. Following importation of the Canadian origin peanut slurry to the Arkansas facility, the peanut slurry would be placed in a holding kettle and heated to a temperature of approximately 120–150 degrees Fahrenheit.[34] Next, the Canadian origin peanut slurry would be mixed with peanut slurry prepared from shelled U.S. origin peanuts[35] and sent to an ingredient station where additives such as salt, sweeteners (dextrose and sucrose), peanut oil, and stabilizers (rapseed, cottonseed, and soybean oils) were to be injected into the combined peanut slurry.[36] According to Bestfoods, the resulting product was then to be pumped through a heat exchanger to a size reduction mill which would break up the peanut particles and create a product which was no longer gritty but of smooth consistency.[37] The smooth product was then to be pumped into a vacuum kettle for de-gassing and was to be cooled to 92 degrees Fahrenheit at which time fat crystal structures were to form giving the product a smooth consistency.[38] The soft product was then to be pumped into retail jars, sealed and stored in a warehouse for at least 24 hours to permit further cooling and to allow the product's texture to solidify.[39] Finally, the product was to be transported to stores across the U.S. for consumer consumption.

B. CUSTOMS' FIRST PRE-IMPORTATION RULING

Customs pre-importation ruling held that Bestfoods' "Skippy" brand peanut butter must be marked as a product of Canada and not the U.S.[40] Since the Canadian origin peanut slurry was a NAFTA good, Customs applied the newly promulgated tariff-shift country of origin marking requirements as required by 19 C.F.R. § 134.35(b).[41] Customs found that the processing of

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[34] CPC Internat'l, Inc. v. U.S., 971 F.Supp. 574, 577 (Ct. Int'l Trade 1997).

[35] According to Bestfoods, the ratio of Canadian origin slurry at this point would be between 10 to 40% of the entire peanut slurry mix. *Id.* at 577.

[36] *Id.* at 577-78.

[37] *Id.* at 578.

[38] *Id.*

[39] *Id.*

[40] Customs Headquarters Ruling Letter 557994 of October 25, 1994. Customs' rulings are *available at* http://www.customs.ustreas.gov/about/about.htm.

[41] 19 C.F.R. § 134.35(b) employs a "tariff shift" method for determining whether goods imported into the U.S. have undergone a substantial transformation following their importation and thus do not need to be marked to indicate their foreign origin. The regulation provides that an article imported into the U.S. from a NAFTA country will be considered to have undergone a

the Canadian origin peanut slurry into finished "Skippy" brand peanut butter did not result in the required change in classification or tariff-shift under the NAFTA Marking Rules to make the Canadian peanut slurry exempt for U.S. marking requirements.[42] Bestfoods challenged Customs' ruling on the basis of their failure to apply the substantial transformation test under the federal Marking Statute, as enunciated in *Gibson-Thomsen,* by filing an action in the CIT seeking pre-importation judicial review of Customs adverse ruling.[43]

C. THE CIT'S FIRST REVIEW OF CUSTOMS' RULING: *CPC INTERNATIONAL, INC. V. UNITED STATES*

Bestfoods argued before the CIT that Customs pre-importation ruling was arbitrarily and contrary to the law because it failed to address whether Bestfoods post-importation processing of the Canadian origin peanut slurry at its Arkansas facility resulted in a substantial transformation of the Canadian origin peanut slurry under the traditional *Gibson-Thomsen* "name, character and use" test.[44] Bestfoods insisted that the *Gibson-Thomsen* test remained "alive and well for NAFTA as well as non-NAFTA imports."[45] Under the *Gibson-Thomsen* substantial transformation test, Bestfoods argued that they were the ultimate purchaser of the Canadian origin peanut slurry and that the manufacturing process performed at its Arkansas facility substantially transformed the Canadian origin peanut slurry into U.S. origin peanut butter thus exempting finished "Skippy" brand peanut butter from the federal Marking Statute.

The CIT evaluated Customs' rationale for segregating NAFTA articles from non-NAFTA articles for purposes of determining country of origin marking requirements. The issue before the CIT, therefore, was whether congressional approval of the NAFTA allowed Customs to abolish, for NAFTA goods imported into the U.S., the long-standing *Gibson-Thomsen* substantial transformation test for determining who is the ultimate purchaser of goods under the Marking Statute. The court held that Customs exceeded its authority by abolishing the long standing *Gibson-Thomsen* substantial

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substantial transformation only if the processing or manufacturing steps in the U.S. are sufficient to change the article's tariff classification.

42 19 C.F.R. § 134.35(b), *supra* note 41. Customs ruled that Canadian peanut slurry is classifiable under subheading 2008.11.90 of the Harmonized Tariff Schedules of the U.S. ("HTSUS"), and the finished peanut butter is classifiable under subheading 2008.11.10, HTSUS. Thus according to the specific "tariff shift" requirements for subheading 2008.11 the required "tariff shift" was not met. 19 C.F.R. § 102.20.

43 Bestfoods invoked the Court of International Trade's jurisdiction to grant declaratory relief from Customs' ruling prior to importation. 28 U.S.C. § 1581(h).

44 CPC Internat'l, Inc. v. U.S., 933 F.Supp. 1093, 1095-96 (Ct. Int'l Trade 1996).

45 *Id.* at 1096.

transformation test for NAFTA articles and held that Congress did not intend to abolish the traditional *Gibson-Thomsen* substantial transformation test for NAFTA goods. Thus, the CIT found that the *Gibson-Thomsen* test remained valid for NAFTA goods as well as the tariff-shift test specified under the NAFTA.[46] In addition, the CIT ruled that the NAFTA regulations were invalid to the extent they contradicted the *Gibson-Thomsen* test.[47] Having found Customs' ruling arbitrary and not in accordance with the law, the court remanded to Customs the question of whether the Canadian origin peanut slurry was substantially transformed by Bestfoods at its Arkansas facility resulting in Bestfoods becoming the ultimate purchaser of the Canadian origin peanut slurry under the Marking Statute.

D. CUSTOMS' SECOND PRE-IMPORTATION RULING

On remand, Customs determined that Bestfoods would not be the ultimate purchaser of the Canadian origin peanut slurry because the Canadian origin peanut slurry would not become a new and different article having a new name, character or use when mixed with U.S. origin peanut slurry and other ingredients to produce "Skippy" brand peanut butter.[48] Customs relied heavily on an analogous case, *National Juice Products Ass'n v. United States*,[49] in concluding that processing of the Canadian origin peanut slurry in the U.S. would not result in a substantial transformation of the Canadian origin peanut slurry.[50] Since no substantial transformation would take place, Customs concluded that the retail consumer in the U.S. would be the ultimate purchaser of the Canadian origin peanut slurry under the Marking Statute and as a result the retail container of "Skippy" brand peanut butter must be marked to show Canada as the country of origin.[51] Unsatisfied with Customs' ruling, Bestfoods once again appealed to the CIT.

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[46] *Id.* at 1098.

[47] Implementation Act § 102(a), 19 U.S.C. § 3312(a). The Implementation Act expresses an intent to avoid conflicting application of the NAFTA with existing U.S. law. 19 U.S.C. § 3312(a)(1).

[48] Customs Headquarters Ruling Letter 559965 of January 24, 1997.

[49] 628 F.Supp. 978 (1986). In *National Juice*, foreign and domestic batches of frozen orange juice concentrate were blended into a manufacturing concentrate to which water, orange essences, orange oil, and in some cases, fresh juice were added to produce the finished retail product: frozen concentrate orange juice. Customs ruled, and the court upheld the finding that no substantial transformation of the foreign concentrate had resulted from the domestic processing. Following the *Gibson-Thomsen* substantial transformation criteria of change of name, character or use, the court held that a party claiming that processing results in a substantial transformation must demonstrate that the processing done in the U.S. substantially increases the value of the product or transforms the import so that it is no longer the essence of the final product. *Id.* at 990.

[50] National Juice Products Ass'n, *supra* note 49.

[51] *Id.*

E. THE CIT'S SECOND REVIEW OF CUSTOMS' RULING: *CPC INTERNATIONAL, INC. V. UNITED STATES*

On second appeal to the CIT, Bestfoods argued Customs' remand ruling, finding that Canadian peanut slurry was not substantially transformed, was arbitrary, capricious, an abuse of discretion and not in accordance with the law. Once again, the CIT rejected Bestfoods challenge finding that Customs did not act arbitrary, capricious, abuse its discretion or act contrary to the law in determining that the Canadian origin peanut slurry was not substantially transformed by the addition of U.S. origin peanut slurry and other ingredients.[52] As a result, the CIT concluded that Bestfoods would not be the ultimate purchaser of the Canadian origin peanut slurry and that "Skippy" brand peanut butter would not fall within the country of origin marking exemptions of the Marking Statute.[53] Like Customs' previous remand ruling, the CIT found *National Juice* compellingly analogous and noted that the addition of various ingredients into the Canadian origin peanut slurry did not change the fundamental character of the Canadian origin peanut slurry or change the fact that the essential character of "Skippy" brand peanut butter was imparted by the peanut slurry.[54] The CIT also found support for its findings by noting that peanut slurry and finished peanut butter have the same tariff classification.[55] In the end, the CIT upheld Customs' remand ruling that Bestfoods was required to mark its "Skippy" brand peanut butter in a manner indicating that it had originated in Canada.

Following the CIT's second decision, both the U.S. and Bestfoods appealed to the U.S. Court of Appeals for the Federal Circuit. The U.S. government appealed the first decision of the CIT holding the NAFTA regulations invalid and Bestfoods appealed the second decision of the CIT holding Bestfoods was required to mark "Skippy" brand peanut butter as a product of Canada under the *Gibson-Thomsen* test.

F. *BESTFOODS V. UNITED STATES*

The Federal Circuit reversed the first decision of the CIT holding the NAFTA Marking Rules invalid to the extent they imposed marking requirements based on the tariff-shift test.[56] As a result of this ruling the

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52 CPC Internat'l, Inc. v. U.S., 971 F.Supp. 574, 585 (Ct. Int'l. Trade 1997).

53 *Id.* at 586.

54 *Id.* at 580.

55 *Id.* at 583-84. Whether the court intended or not, such a finding would also suggest that Bestfoods' argument would fail even under the tariff-shift test of the NAFTA Marking Rules.

56 Bestfoods v. U.S., 165 F.3d 1371, 1376 (Fed. Cir. 1999).

correct method for determining the country of origin of a NAFTA product for marking purposes is the tariff-shift test *not* the *Gibson-Thomsen* substantial transformation test. The Federal Circuit's ruling does not affect country of origin marking requirements for non-NAFTA goods.

The Federal Circuit rejected Bestfoods argument that the new NAFTA Marking Rules conflict with the Marking Statute. The court noted that the Marking Statute does not specify which methodology, tariff-shift test or the *Gibson-Thomsen* substantial transformation test, must be used to determine when an article is an "article of foreign commerce" or who is the "ultimate purchaser" of the imported good.[57] The Federal Circuit did acknowledge that in this absence the court in *Gibson-Thomsen* adopted the case-by-case "name, character, and use" approach.[58] However, as the court found, nothing in the Marking Statute required this approach. Therefore, when the NAFTA Marking Rules displaced the traditional *Gibson-Thomsen* test for NAFTA goods, it did not conflict with the Marking Statute because the Marking Statue never required use of the *Gibson-Thomsen* test in the first place.[59] Because, the court found the NAFTA tariff-shift regulations to be valid, it did not address the second issue on appeal, whether Bestfoods was required to mark its "Skippy" brand peanut butter under the substantial transformation test.

V. IMPACT OF THE *BESTFOODS* DECISION AND RECENT DEVELOPMENTS

The decision in *Bestfoods* will have a significant impact on trade between the U.S., Mexico and Canada. After *Bestfoods*, it is clear that the country of origin for goods imported from Canada and Mexico for marking purposes will be determined by applying the NAFTA tariff-shift rules, rather than the traditional *Gibson-Thomsen* substantial transformation test. As a result, importers seeking to qualify their goods as Canadian or Mexican must ensure that the goods meet the applicable tariff-shift requirements of the NAFTA.

The country of origin determination as highlighted by *Bestfoods* will continue to have an effect on the trade arising out of the NAFTA and the proposed Free Trade Area of the Americas ("FTAA").[60] Article 303 of the

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[57] *Id.* at 1375.

[58] *Id.*

[59] *Id.* at 1375-76.

[60] Thirty-four democratic nations of the Western Hemisphere have been engaged in negotiations toward establishing an FTAA Agreement which would eliminate tariffs and create common trade and investment rules beginning on January 1, 2005. Co-author, Ulice Payne, Jr., participated

NAFTA effectively changes the duties assigned to goods imported into Mexico, which are then processed (manufacture or assembly) and exported.[61] This provision of the NAFTA stated that until January 1, 2001, nonoriginating component parts imported into Mexico by a *maquiladora* that are subsequently exported in the form of finished goods to the U.S., Asia or Europe can be imported into Mexico duty free. Machinery, equipment and tools temporarily imported into Mexico by a *maquiladora* in 2000 enter duty free for five years or the period of depreciation, whichever is greater.

The Mexico Commerce Secretariat published a new Decree on October 30, 2000 regarding the implementation of the Article 303 regulations in Mexico. This Decree states that the provisions of Article 303 will apply to all *maquiladora* imports beginning on November 20, 2000 which are part of the finished products exported out of Mexico beginning on January 1, 2001. In most instances, customs duties will have to be paid for temporary importation into Mexico of: (1) nonoriginating component parts; or (2) machinery, equipment and tools *regardless* of the country where the finished goods will be exported. Under certain circumstances, there may be no duties payable if the component parts are of NAFTA origin and the finished product is exported to Canada or the U.S.

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as a U.S. delegate in the VI Americas Business Forum held in Buenos Aires, Argentina on April 5-6, 2001 for the purpose of making recommendations to the trade ministers of the FTAA countries who will meet in the Third Summit of the Americas in Quebec City, Canada on April 20-22, 2001. One of the principal topics of the proposed FTAA Agreement is Rules of Origin addressing tariff shift, regional content value and related requirements.

[61] The Free Trade Agreement between Mexico and the European Union includes a similar provision to Article 303 of the NAFTA. This provision, Annex 3 of the Decision 2/2000, becomes effective on January 1, 2003.