



**PACER Plus**

# **THE TARIFF AND RULES OF ORIGIN**

Understanding rules of origin based on  
the tariff classification of the goods







## FOREWORD

In negotiating rules of origin and interacting with business to assess their needs, I have always found that a basic knowledge of the structure of the national tariff provides a very strong foundation for understanding the design of rules of origin.

If you understand how the tariff is built, the concept of rules based on a change in tariff classification for the composite parts of a product, falls into place.

In this paper I have attempted to provide a simple explanation of the structure of the tariff, its relationship to international conventions, and how more recently, it has been used to design the Product Specific Rules of Origin based on a change in tariff classification - commonly referred to as CTC rules.

The primary audience for this paper is customs brokers, and customs officials engaged in implementation, including training, and enforcement.

Christine Mullinder



# THE TARIFF AND RULES OF ORIGIN

## Classification of goods

When goods are traded between countries, they have to be cleared for entry into the importing country by the customs administration.

The importer must make an import entry to the customs administration. This import entry provides important information about the goods, such as their description, their value and where they have come from.

This information is needed by the importing country for various purposes such as:

**Revenue collection;** identifying what customs duties are payable and calculating the amount payable;

**Trade data;** collecting trade data to assist economic planning and to assist in responding to domestic threat. For example, a domestic producer could be exposed to a sudden influx of goods that threatens the viability of that industry. The trade data collected from imports can be used to identify the source of the risk (global over-supply, unfair trade practices etc.) and help develop tools to safeguard the domestic industry;

**Monitoring goods;** identifying goods that may require special handling (e.g. hazardous goods) or which pose a bio-security risk, or which need to meet other requirements (e.g. safety standards);

The government and traders need **certainty** about the customs duties and other charges that are imposed. These revenues on the part of the government and costs on the part of traders, play a significant role in decision-making for both government and business. Equally, if data is to be useful it must have a high level of accuracy and uniformity.

### Example

If you are monitoring fish, you need data about the species and what level of processing it has undergone. A simple entry stating “fish” will not provide useful data and will not identify the correct customs duty.

To achieve this certainty and to ensure that the data collected has an appropriate level of uniformity, the international community has adopted a standard method of classifying goods known as the Harmonised Commodity Description and Coding System (HS Code). More than 200 countries representing more than 98% of world trade use the HS Code as the basis for their national tariffs.



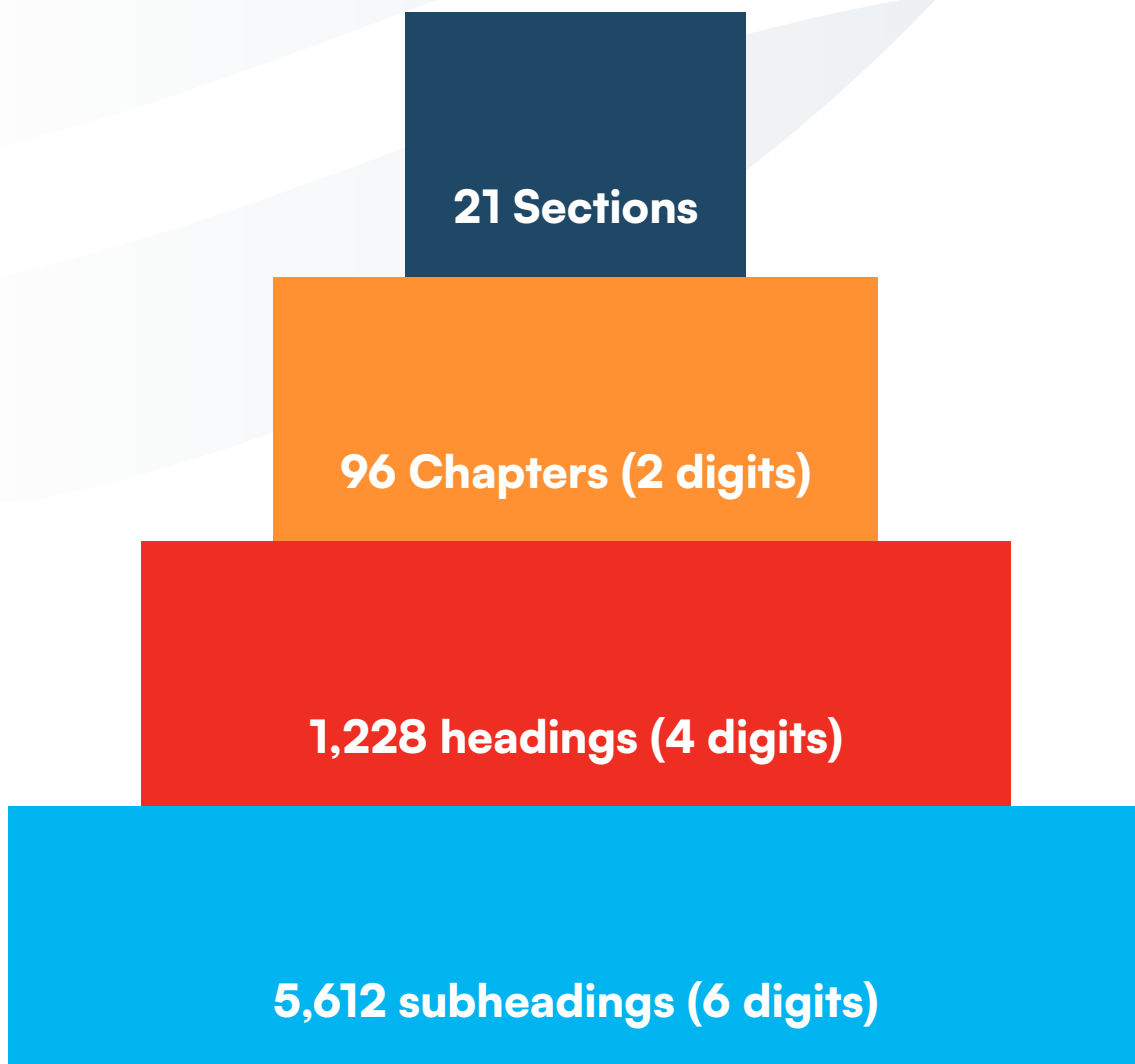


# AT THE INTERNATIONAL LEVEL

## The Harmonised System (HS Code)

The HS Code is a classification system based on the essential character of the goods - what the goods are made of and how much processing has been undertaken, rather than what the goods are used for.

The HS Code is a numerical system. It is divided into sections, chapters, headings and subheadings





## Sections

The Sections classify the goods at the broadest level, beginning from the natural or unprocessed state of the good and moving through to the highly processed products made from the basic material.

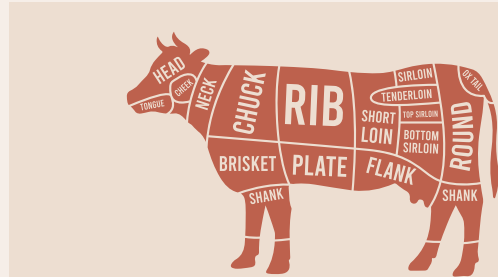
Example: relating to the processing of an animal

### SECTION I

#### Live Animals: Animal Products

Basic materials are live cattle, beef cut into carcasses and fillets and edible offal

Chapters 01 through 05



### SECTION III

#### Animal or Vegetable Fats and Oils

etc.  
Further processing results in unrefined and refined animal fats and oils and fats made from bones or waste.

Chapter 15



### SECTION IV

#### Prepared foodstuffs etc.

Included here are preparations of meat such as sausages, crumbed wiener schnitzel, corned beef, and other canned meats, sauces and soups based on meat. Extracts and juices of meat used as an ingredient in further preparation and dietary supplements. Residues and waste from processing are also in this section.

Chapters 16; 19; 21 and 23





## SECTION VI

**Products of the chemical and allied industries**

More sophisticated processing allows blood and glands and amino acids to be recovered for pharmaceutical purposes. Soap made from tallow is also included here.

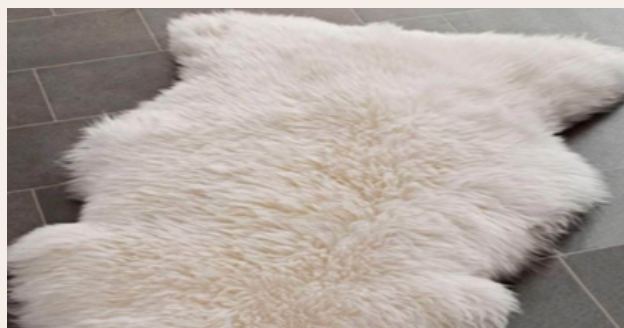
Chapters 29; 30; 32; 34 and 35



## SECTION VIII

**Raw hides and skins, leather etc.** Non-meat parts of the animal are also processed. This section includes raw hides and skins and prepared leather and articles made from leather such as clothing, handbags and suitcases.

Chapters 41 and 42



## SECTION XII

**Footwear**

The leather or skins are highly processed before being made into shoes

Chapter 64



## SECTION XX

**Miscellaneous manufactured articles**

Furniture, mattresses, specialist medical furniture — dentist chairs. These products are made of many different materials and parts.

Chapter 94





## Chapters

The Sections are then divided into **Chapters**. The classification numbering starts at the chapter level (at 2 digits).

Example **Section I Live animals, animal products**

<b>Chapter 01</b>	Live animals
<b>Chapter 02</b>	Meat and edible meat offals
<b>Chapter 03</b>	Fish and crustaceans, molluscs and other aquatic invertebrates
<b>Chapter 04</b>	Dairy produce, birds' eggs, natural honey, edible products of animal origin, not elsewhere specified
<b>Chapter 05</b>	Products of animal origin, not elsewhere specified or included

The classification at this level is still very broad. The chapters in Section 1 group animals by their essential character: live animals; carcasses and cuts of meat; fish and products obtained from live animals (e.g. milk and honey).

In the table above, the Chapter 05 description “Products of animal origin, not elsewhere specified or included” means any other product of animal origin that does not fit within the description of any of the preceding chapters. The use of terms “not elsewhere specified or included” and “other” are often used to provide a default classification for goods that are not traded in sufficient volume to warrant detailed classification, but nonetheless need to be accounted for.

Example

Horsehair, guts bladders and stomachs of animals, ivory are all classified in Chapter 05 because they do not fit the descriptions of the other chapters but are not traded in sufficient volume globally to be identified separately.





## Headings

Chapters are then divided into **headings** to provide more detail about the product. Headings are numbered at four digits.

### Example 1: Chapter 01 Live animals

<b>0101</b>	Live horses, asses, mules and hinnies
<b>0102</b>	Live bovine animals
<b>0103</b>	Live swine
<b>0104</b>	Live sheep and goats
<b>0105</b>	Live poultry, that is to say fowls of the species <i>Gallus domesticus</i> , ducks, geese, turkeys and guinea fowls
<b>0106</b>	Other live animals

In this chapter the headings are used to separately identify the types of live animals that are commonly traded. In heading 0106 above we see the use of “other live animals” which means that if the animal is not separately classified in the list of headings in Chapter 01, then it will be classified in heading 0106 (e.g. primates, whales and dolphins, camels, rabbits and hares).

### Example 2: Chapter 02 meat and edible offal

<b>0201</b>	Meat of bovine animals, fresh or chilled
<b>0202</b>	Meat of bovine animals, frozen

In this chapter the headings adopt the same separation into types of animal meats as for Chapter 01 but expand the detail of this by separately identifying the state in which the meat is traded; fresh or chilled, or frozen.

This is because fresh or chilled meat and frozen meat are traded in substantial volumes globally. There may be different customs duties applied to the fresh or frozen product and there will certainly be differences in the clearance procedures for fresh product compared to frozen product.

Having the state of the products clearly identified in the coding system helps process these goods appropriately and efficiently at the border.



## Subheadings

The headings are then further divided into **subheadings**. Numbered at six digits. The six-digit level provides the greatest detail about the product under the HS Code.

Example: **Heading 0201**

<b>02</b>	<b>Meat and edible meat offal</b>
<b>0201</b>	<b>Meat of bovine animals, fresh or chilled</b>
<b>0201.10</b>	- Carcasses and half-carcasses
<b>0201.20</b>	- Other cuts with bone in
<b>0201.30</b>	- Boneless

In this heading the classification of the fresh or chilled beef is further broken down into three subheadings to identify the level of processing that has been undertaken.

There are substantial differences in value between a carcass and a fine boneless cut of meat and customs duties and other taxes on these products will vary.

By creating separate subheadings for these products, the importer knows what customs duty to expect, the customs officer knows what duty to charge, and import or export data can be collected to inform important decision making.



## AT THE NATIONAL LEVEL

### The National Tariff

Each country develops its own national tariff based on the structure of the HS Code. Keeping the numbering system, all national tariffs use the same first six digits. National tariffs generally extend the number of digits to allow for different customs duties depending on the level of processing, and gathering more detailed information for reporting or monitoring trade of particular interest to their economy.

If greater detail is not required, countries simply add “.00” to the HS Code structure to maintain at least eight digits in the national tariff. The number of digits can range from 8-12 and some countries also use statistical keys. The tariff classification generally applies to both imports and exports under the country’s tariff so the need for more detailed information about certain products may be related to exports as well as imports.

Example 1

Country	National tariff	Goods description
Samoa	0402.99.10	-Evaporated or condensed milk nes
	0402.99.90	-Other milk and cream other than evaporated or condensed milk nes
Cook Islands	0402.99.00	Other
Australia	0402.99.00	Other
New Zealand		Other — concentrated
	0402.99.00.10D	- - Condensed
	0402.99.00.15E	- - Evaporated
	0402.99.00.17A	- - Other
		Other — other
	0402.99.00.21K	- - UHT milk, sweetened
	0402.99.00.29E	- - Other



In the above example, Samoa and New Zealand are both seeking more detailed information about these products.

- Samoa has implemented two tariff items (0402.99.10 and 0402.99.90) to gather separate information about trade in evaporated or condensed milk from the other products classified in 0402.99 but allows data on these two products to be grouped together.
- New Zealand has not implemented additional tariff items (0402.99.00) but has used 5 statistical keys to gather more detailed data about condensed milk, evaporated milk, and unconcentrated sweetened milk such as UHT milk (.10D, .15E, .17A, .21K, and .29E). The tariff rates are the same for all products.
- Australia and the Cook Islands do not seek any differentiation between the products classified in 0402.99 and have simply added the “.00” to maintain an 8-digit tariff item (0402.99.00).

Example 2

### 0714.40 Taro (*Colocasia spp.*)

Country	National tariff	Goods description
Cook Islands		Taro ( <i>Colocasia spp.</i> )
	0714.40.10A	-Cooked and preserved by freezing, not containing added sugar (1 Dec -31 Aug)
	0714.40.10B	-Cooked and preserved by freezing, not containing added sugar (1 Sept - 30 Nov)
	0714.40.90A	-Other (1 Dec -31 Aug)
	0714.40.90B	-Other (1 Sept - 30 Nov)
New Zealand		Taro ( <i>Colocasia spp.</i> )
	0714.40.10.OOF	-Cooked and preserved by freezing, not containing added sugar
	0714.40.90.OOK	-Other
Kiribati	0714.40.00	Taro ( <i>Colocasia spp.</i> )
Samoa	0714.40.00	Taro ( <i>Colocasia spp.</i> )



In this example the Cook Islands and New Zealand are seeking more detailed information about taro that has been cooked and preserved by freezing and does not contain added sugar.

- The Cook Islands have implemented two tariff items to separate the frozen cooked product from other forms of taro, (0714.40.10 and 0714.40.90) and then split these tariff items with the use of a statistical key (...A...B). This allows the Cook Islands to impose a seasonal tariff, removed in the off season, but imposed in season.
- New Zealand has similarly implemented two tariff items to separate the frozen cooked taro from other forms of taro (0714.40.10 and 0714.40.90). The New Zealand tariff attaches a statistical key to all tariff items so the statistical key in the above example has no specific significance.
- Kiribati and Samoa have simply added the “.00” to maintain an 8-digit tariff item (0714.40.00). They do not seek information other than that the product is taro (fresh, chilled, dried or cooked and preserved by freezing).

NOTE: it is only at the **8-digit** level that the classification differs from the international standard (the HS Code). The first **6 digits** will always be the same; the subsequent numbers are used at the national level to make a more detailed distinction if required.



# THE TARIFF AND RULES OF ORIGIN

## What are rules of origin?

Rules of origin are the rules that determine the “**economic nationality**” of a good. Many countries may participate in the manufacturing of a good, providing specialised ingredients or parts, but when the finished good crosses the border into the importing country there can be only one country of origin. A set of rules is needed to determine that country.

Rules of origin are particularly important in trade agreements.

Agreements can be

- **unilateral** — the country offering the benefits does not require reciprocal treatment, such as SPARTECA
- **bilateral** — these are reciprocal agreements negotiated between two countries with agreed benefits offered by each side, such as ANZCERTA between Australia and New Zealand, or
- **plurilateral** — these are reciprocal agreements negotiated between several countries, frequently but not always on a regional basis, such as PACER Plus.

A **rule of origin** is needed regardless of whether the agreement is reciprocal or non-reciprocal.

- In a non-reciprocal agreement, the benefit provider wants to ensure that only the nominated recipients receive the special treatment.
- In a negotiated reciprocal agreement, the trading partners want to keep the benefits of the agreement to the participating countries. They have paid for these benefits by offering reciprocal benefits and do not want free-riders.

## Rules of origin have three specific purposes

- defining originating status
- setting out rules for how the goods are treated when they cross other borders on their way to the importing country, and
- setting out the documentary requirements, at the point of importation and post clearance to support a claim of preference, if requested.



NOTE: this paper explores only the rules governing originating status, with a particular emphasis on how the Tariff is used to construct rules of origin based on a change in tariff classification.

Transit and transportation requirements, documentary evidence requirements, and the actual product specific rules of the PACER Plus Agreement are explored in detail in the paper Supplementary Guidelines to PACER Plus Rules of Origin.

## Defining originating status

An “**originating material**” means a material that is either wholly obtained in one or more of the PP Parties, or a material that has undergone sufficient processing in one or more of the PP Parties, to meet the PSR criteria in the PSR schedule in the ROO Chapter of PACER Plus.

A “**non-originating material**” means a material or component that has been imported from a country that is not a Party to PACER Plus, and has not undergone sufficient processing to meet the PSR criteria, or is a material of undetermined origin. That is, the material’s origin is not known or cannot be proven.

There are three pathways to achieving originating status.

### 1. The goods are wholly obtained (WO)

This means that the goods do not contain any raw materials, ingredients or parts that have been produced outside of the parties to the agreement. Essentially this means primary products such as plants, live animals and fish, minerals, and natural resources and products that have been made from primary products without the addition of any imported materials.

Wholly obtained goods are generally classified in the Tariff as follows:

Live animals and products obtained from live animals (including fish)	Chapters 1 through 5
Plants and plant products	Chapters 6 through 14
Minerals	Chapters 25 through 27
Plastics, rubber, wood, raw fibres	Early headings of Chapters 39 through 52
Unprocessed natural stones, precious metals and base metals	Early headings of Chapters 71 through 80



## 2. The goods are produced entirely from originating materials (PE)

This means goods that are made from originating materials produced by the trading partners. Most of the trade under this umbrella will be similar to the above (wholly obtained goods) because materials will be sourced from within the region.

However, non-originating raw materials may be used provided those materials have been sufficiently transformed before being used in further production.

Example 1: Production using only PACER Plus materials

Bauxite from Australia 2606 2606	New Zealand produces aluminium sheets 7606	Vanuatu produces corrugated aluminium roofing sheets 7606	Samoa imports the roofing sheets
WO	WO or PE	WO or PE	
All of the materials used have originated in one or more of the PP Parties.			

Example 2: Production using a non-originating material which is further processed into an originating material

Aluminium rod from China 7604	Vanuatu produces aluminium sheets 7606	Samoa produces corrugated aluminium roofing sheets 7606	Samoa exports to other PP Parties
Non-originating	PSR (meets CTH rule)	PE	PE
Even though the aluminium rod originated from China, sufficient working has been undertaken in Vanuatu to achieve originating status for the aluminium sheets. Further work on the sheets is therefore being carried out on an originating product.			



### 3. The goods are produced using non-originating materials - Product Specific Rule

These rules are designed for goods that use non-originating materials in the later stages of production. They are generally presented in an Annex to the Chapter on Rules of Origin as a Schedule of Product Specific Rules of Origin (PSRs).

- a rule based on a specified change in tariff classification (CTC) rule, or
- a regional value content (RVC) rule, or
- a specified process rule, or
- a rule which combines one or more of the above.

Some PSRs will offer optional rules RVC (40) or CTC rule or process rule. Some PSRs will offer only one option.

Goods using the PSR pathway will be classified throughout the Tariff.

The critical factor in using the PSR is that the non-originating material that has been incorporated into the product in a later stage of production has been sufficiently transformed to result in a new product or has had sufficient value added to meet the value threshold.



# PRODUCT SPECIFIC RULES (PSRS)

## Change in Tariff Classification (CTC) Rule

**Concept:** a material that has been sufficiently transformed (that is, the processing undertaken on the material has resulted in the creation of a different product), should have the “economic nationality” of the country where that transformation took place.

The HS Code provides a useful tool for designing rules of origin because

- it classifies goods according to their base material and the processing undertaken on that base material,
- it is a classification system used for 98% of world trade
- trade in goods world-wide is harmonised to a six-digit numbering system so a rule set at the six-digit level will mean the same thing in the exporting and importing country, and
- a rule based on a change in tariff classification (tariff shift) provides certainty. It is not vulnerable to price movements or exchange rate fluctuations.

It is not a perfect tool.

The HS Code was designed to classify products and identify customs duties payable. Goods that are traded in high volumes or value are identified in separate headings or subheadings while other goods are grouped together.

Example: Impact of trade volumes -

<b>0910.11</b>	Ginger (whole)
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<b>0910.12</b>	Ginger crushed or ground
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<b>0910.20</b>	Saffron (both whole and crushed or ground)
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Ginger is traded in sufficient volume in both the whole state and the ground state to warrant separate classification.

Unprocessed saffron and ground saffron are grouped together. A CTC rule may need to be different for these products to achieve the same outcome.



The descriptions at heading level for food products and preparations based on primary goods are more general in scope than the headings for more manufactured products classified in the later part of the HS Code.

Example: More detailed classification (narrower scope)

**2001**

Vegetables, fruit, nuts and other edible parts of plants, prepared or preserved by vinegar or acetic acid.

**5405**

Artificial monofilament of 67 decitex or more and of which no cross-sectional dimension exceeds 1mm; strip and the like (for example, artificial straw) of artificial textile materials of an apparent width not exceeding 5mm.

Some products may be classified separately at either heading level or subheading simply because they are traded in sufficient volume in bulk form or in retail packaging to warrant separate identification or different customs duties.

Example: packaging separately classified at heading level

**5107**

Yarn of combed wool, not put up for retail sale

**5109**

Yarn of wool or of fine animal hair, put up for retail sale

Example: packaging separately classified at subheading level

**5204**

Cotton sewing thread, whether or not put up for retail sale

**5204.11**

-Not put up for retail sale

**5204.20**

-Put up for retail sale

Simply repackaging a bulk product into retail packages is generally not considered sufficient transformation to achieve originating status, but the rule to achieve this will be different depending on what level these goods are classified in the HS Code (heading or subheading level).

For the above reasons, a generic tariff shift - e.g. change in classification of the good at the tariff heading level — is not appropriate to decide origin.



Products that are highly specialised but which fall into a default “other” category may not qualify as originating because they may be classified in the same heading or subheading as other highly processed ingredients, while products that are simply repackaged from bulk to smaller retail packaging could be originating simply because they are traded in sufficient volume to be classified separately at subheading or heading level.

To ensure that processing is treated equally for all products, and origin is not conferred through simple repackaging operations, rules that are based on a change in tariff classification, are designed at a level to suit the specific product.

## The CTC rules are presented as CC, CTH or CTSH.

“**CC**” is short hand for “a change to a good of chapter XX from any other chapter”. It means that any material used in the production of the good that is classified in the same chapter must have been produced in a PACER Plus Party. In other words, if the rule is “CC” you cannot use non-originating materials (i.e. materials from a non-Party) that are classified in the same chapter as the good.

CC Change of Chapter

Goods classified in the same chapter (first 2 digits are the same) must be originating in the region

“**CTH**” is short hand for “a change to a good of heading XXXX from any other heading” and means that any material used in the production of the good that is classified in the same heading must have been produced in a PACER Plus Party. In other words, materials that are classified in the same heading cannot be non-originating, i.e. cannot come from a non-PACER Plus Party.

CTH Change of Heading

Goods classified in the same heading (first 4 digits are the same) must be originating in the region

“**CTSH**” is short hand for “a change to a good of subheading XXXX.XX from any other subheading” and means that any material used in the production of the good that is classified in the same subheading must have been produced in a PACER Plus Party. In other words, materials that are classified in the same subheading cannot be non-originating, i.e. cannot come from a non-PACER Plus Party.

CTSH Change of Subheading

Goods classified in the same subheading (first 6 digits are the same) must be originating in the region



### Important things to know about CTC rules:

- the required tariff shift applies only to non-originating goods or materials. Any amount of goods from the PP Parties can be used, regardless of where they are classified.
- the level the rule is set at (CC, CTH, CTSH) depends on the structure of the HS Code. That is, whether it is CC, CTH or CTSH will depend on where the contributing ingredients or components are classified, not because CC, CTH or CTSH represent a stricter or more liberal rule.

### Example 1 Heading 0201

0201	Meat of bovine animals, fresh or chilled
0201.10	- Carcasses and half-carcasses
0201.20	- Other cuts with bone in
0201.30	- Boneless
Relevant inputs	
Chapter 01 0102	Live animals and products obtained from live animals (including fish) - live bovine animals
Chapter 02	Meat and edible offal
0201	- meat of bovine animals, fresh or chilled
0202	- meat of bovine animals, frozen
PACER Plus rule for 0201 CC	
<p>This means that non-originating materials classified in Chapter 02 cannot be used. In processing terms this means that PACER Plus does not allow a non-originating carcass (classified also in Chapter 02) to be imported and cut into finer cuts of meat for export to other PACER Plus Parties.</p> <p>However, it does allow the slaughtering of a live animal that has been imported from a non-PP Party. This is because live animals are not classified in the same chapter as the meat. They are classified in another chapter (Chapter 01).</p> <p>So non-originating meat can be processed for export to other PACER Plus Parties provided the slaughtering of the animal has been undertaken in a PACER Plus Party.</p> <p><b>There is no restriction on any use of PACER Plus Party livestock or meat.</b></p>	



## What would other CTC rules allow?

A CTH rule would allow importing non-originating frozen meat and simply thawing it, because the HS Code separates fresh or chilled meat (**0201**) from frozen meat (**0202**) at the heading level.

It would not allow the preparation of boneless cuts from a non-originating carcass because carcasses, cuts with the bone in, and boneless cuts are all classified in the same heading.

A CTSB rule would allow the same simple thawing process as under the CTH rule. It would also allow a non-originating carcass to be imported and processed into a finer cut, either with bone in or boneless.

CTSB + RVC 40 would allow the same as above with a condition attached that at least 40% of regional value was created in the processing.

CC except from Chapter 1 would mean that the livestock would have to be born and raised in the PACER Plus Parties. Slaughtering an animal from a non-PACER Plus Party would not be allowed.

### De Minimis (tolerance rule)

Because the HS Code was not specifically designed to construct rules of origin, there is a tolerance rule (de minimis) that allows up to 10% of the FOB value of the final product to include non-originating materials that do not meet the PSR rule to be included.

For example: Mixed frozen vegetables. Vegetables are classified in Chapter 07 so under a “CC” rule for mixed frozen vegetables, all the vegetables need to be originating. The de minimis rule nonetheless allows you to use some non-originating materials (for example baby bamboo shoots) provided their value does not exceed 10% of the FOB price of your mixed vegetables.

### Packaging

If the product is normally presented in some sort of packaging, other than that used for transportation purposes (i.e. packing crates) those materials are classified together with the good and you do not have to separately identify the origin of the packaging materials.



## Regional Value Content Rule

**Concept:** A certain percentage of the value of the good has been added by the exporting Party. The assumption is that this added value is sufficient to transform the good into a different product that can then be claimed as an originating good of the exporting country. In the case of PACER Plus, the added value of all PACER Plus Parties can be added together. The focus of the RVC rule is on the value that has been added in the domestic (or regional) production of the product.

### Calculating the value added:

The two most commonly used methods for calculating the added value are the “build-down” and the “build-up” method. Both methods are based on the value of originating and non-originating materials.

PACER Plus uses the build-down method for calculating regional value content.

#### Build-down Method: Based on Value of Non-Originating Materials

This method simply takes the final value of the good and subtracts the combined value of all the non-originating materials. If the combined value of the non-originating materials is more than 60 percent of the value of the exported good then the good has not achieved originating status. That is, the PP Parties must have contributed 40% to the value of the product.

The roll-up principle for intermediate goods: if a non-originating material (product A e.g. aluminium rod) has been transformed into another product (product B e.g. aluminium sheet) and then product B has been further processed into Product C (corrugated roofing sheet), all of the value of product B (aluminium sheet) - commonly known as an intermediate good - can be considered as originating value. The value of product A (e.g. aluminium rod) does not need to be counted as a non-originating material because it has been sufficiently transformed earlier the production process to make it originating.

Packaging: The costs of packaging materials is taken into account in the calculation of the value of the product. It is classed as originating or non-originating, depending on where the packaging was produced.

#### Minimal operations:

There is an article defining certain minimal operations that are insufficient to be counted towards the local value contribution when they are the only processes undertaken on a non-originating material. For example, affixing a brand name or logo to an article of clothing. While this can add significant value to the product, it does not result in a new product being made (i.e. no transformation has occurred).



## Process rule

**Concept:** A specified process has been undertaken. The process rule is generally used when an added value rule or a CTC (tariff shift) rule are not considered appropriate.

Example 1:

Crushing, grinding and mixing of spices may not achieve the 40% value threshold, but the production process certainly transforms the original product into an entirely new one.

A CTC rule is not appropriate where the spices in the crushed or ground state are not separately classified in the HS Code, so an optional process rule “crushing or grinding” is necessary.

PACER Plus e.g. 0910.20 Saffron CC or RVC (40) or “Crushing or grinding”

Example 2

The chemical industry:

In the chemical industry the price of input materials, particularly petroleum products, are subject to significant fluctuations. A value-add rule may be met one day and not be achieved the next because of these price fluctuations.

Similarly, there are chemical processes that inform the fundamental nature of a product, but that product remains classified in the same subheading or heading under the HS Code. For example, a “standards material” will be classified in the same heading or subheading as the product for which it provides the standard.

There are several commonly used chemical process rules that are offered as optional process rules to accommodate the processes involved in chemical manufacturing.

PACER Plus e.g. Chapter Notes to Chapter 27 and Chapters 28 to 40.



### Example 3:

Another example of where a CTC rule may not achieve the outcome required is in Chapter 15, the chapter classifying fats and oils.

While many of the subheadings do identify crude oil separately from refined oil, the reality is that most fats or oils that are exported are partially refined to prevent despoliation during transport.

This means that a partially refined oil will be classified in the same subheading as the fully refined product.

A process rule is needed to recognize that the full refining process which is undertaken on a partially refined good is sufficient to achieve originating status.

PACER Plus e.g. 1511 Palm oil CC or “Change through refining”

A Chapter Note for Chapter 15 states “For the purposes of this Chapter, the refining process (chemical or physical) entails removing the odour, taste, colour and acidity of a crude or partially refined fat or oil”.

This process rule is applied to headings 1501, 1502 and 1504 through 1515 as an optional process rule.





## KEEPING THE HS RELEVANT

The HS Code is reviewed regularly (generally on a 5-year basis) to ensure that it remains relevant to changes in global trade and is able to collect appropriate data on trade in goods of particular international interest. This regular review is essential because:

### *Products become obsolete*

Example:

In the past typewriters were the commonly traded office tool and had their own heading/subheadings. With the introduction of first, word processors and then subsequently personal computers, the classification of these goods needed to be revised. Typewriters, now obsolete, were relegated to a default “other” category’.

### *New technologies and new products emerge*

New headings and subheadings are created to take account of the new electronic products.

Example:

New subheading for “smartphones” (HS 2022: 8517.13) and a new separate heading (HS 2022: 8485) for machines for additive manufacturing (3-D printers).

### *Trade volumes increase*

An increase in trade volumes could be simply that certain products have become more popular. Or it could signal global over supply or the possibility of unfair trade practices.

Examples 1 and 2

New subheadings for truffles and other varieties of mushroom because of the increasing volume of trade in these products. (HS 2022: 0802.91, 0802.92 and 0802.99)

Pine nuts in the shell and shelled pine nuts now have separate subheadings because of the increasing volume of trade in the shelled product. (HS 2022: 0802.91 and 0802.92)



## Closer monitoring of trade

Many international organisations are seeking more detailed information (data) on trade in goods that may pose some sort of threat to public health and safety, to the environment or to the sustainability of natural resources.

### Example 1

New subheading to provide separately for the bark of African cherry (*Prunus africana*), in order to monitor the potential impact of the over-exploitation of this tree in the wild because of the increasing use of its bark, especially by the international pharmaceutical industry. (HS 2022: 1211.60)

### Example 2

The appropriate disposition of waste materials has become an international concern. Many new subheadings were created to more accurately identify waste product and track its movement and a new heading was created for electrical and electronical waste and scrap (HS: 2022 85.49).

## Identifying products that contribute to sustainability

Governments also want to monitor trade in goods that promote positive environmental or health outcomes.

### Example 1

Creation of new subheading was created for placebos and blinded (or double-blinded) clinical trial kits for a recognized clinical trial, put up in measured doses in response to the COVID 19 pandemic (HS 2022: 3006.93).

### Example 2

New subheadings to provide for solar energy products (HS 2022: 8501 and 8541.41 through 8541.49).



## TRANSPOSING THESE CHANGES

When the HS Code is revised and new headings and subheadings are created, or products that are no longer traded in volume, are moved to an “-Other” default classification, the national tariffs have to be revised as well to accommodate these changes.

This process is commonly called “transposition”.

Because rules of origin depend on where a product is classified the Product Specific Rules of Origin in a free trade agreement also have to be reviewed to ensure that the rules of origin negotiated between the Parties are appropriately carried over to the national nomenclature, and that obligations and commitments agreed to, are maintained.









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