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New “Country of Origin” Textile Regulations Violate the Multifiber Arrangement

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Thomas T. Janover

Abstract

This Note argues that the implementation of the new regulations violate both the spirit and the letter of bilateral and multilateral trade agreements to which the United States is a party. This Note will also examine the new textile regulations in light of judicial and administrative rulings. An examination of the conflict between the new regulations and the MFA follows. Finally, an analysis of the effects of the new regulations on the domestic economy and on international relations will be discussed.

NEW "COUNTRY OF ORIGIN" TEXTILE REGULATIONS VIOLATE THE MULTIFIBER ARRANGEMENT

INTRODUCTION

On March 5, 1985, the United States Customs Service¹ published regulations affecting the importation of textiles and textile products into the United States.² They dramatically alter current commercial practices by establishing new criteria

1. The United States Customs Service (formerly the Bureau of Customs) is a bureau in the Department of the Treasury. 19 U.S.C. § 2071 (1982).

2. Customs Regulations Relating to Country of Origin for Textiles and Textile Products, 50 Fed. Reg. 8710 (1985). These regulations are issued pursuant to the Agriculture Act of 1956, § 204, 7 U.S.C. § 1854 (1982), which provides authority for the President to issue regulations governing the entry of textiles and textile products into the United States. *Id.*; see *infra* notes 93-110 and accompanying text.

The regulations change rules and documentation requirements by which the United States Customs Service regulates the importation of textiles and textile products into the United States. They provide amendments to the Air commerce regulations, 19 C.F.R. § 6.18; Special classes of merchandise, 19 C.F.R. §§ 12.130-131; Transportation in bond and merchandise in transit, 19 C.F.R. § 18.11; Customs warehouses, container stations and control of merchandise, 19 C.F.R. § 19.11; Entry of merchandise, 19 C.F.R. § 141.52; Consumption, appraisalment and informal entries, 19 C.F.R. §§ 143.21-22; Warehouse and re-warehouse entries and withdrawals, 19 C.F.R. § 144.38; Foreign trade zones, 19 C.F.R. § 146.49. See 50 Fed. Reg. at 8723. The regulations became effective on April 4, 1985. *Id.* at 8711; see *infra* note 99.

The recent United States-Hong Kong bilateral textile agreement, contained the following categories: The major divisions are Yarn, Fabric, Apparel, and Made-ups and Miscellaneous; each division had subcategories of cotton, wool and manmade fiber; and each subcategory set forth specific types of products, e.g., gingham, corduroy, sheeting, broadcloth, printcloth, shirtings, duck, and other fabrics. Apparels was similarly divided into categories of cotton, wool, and manmade fibers. Further divisions included limits for specific items, e.g., handkerchiefs, gloves, suit-type coats, dresses, knit shirts, blouses, skirts. Agreement Relating to Trade in Cotton, Wool and Man-Made Fiber Textiles and Textile Products, June 23, 1982, United States-Hong Kong, — U.S.T. —, T.I.A.S. No. 10,420 [hereinafter cited as Hong Kong Treaty].

The Hong Kong treaty is similar to all of the bilateral agreements negotiated by the United States. The United States-China bilateral textile agreement of September 17, 1980 included a similar list of categories for textiles and textile products. Agreement Relating to Trade in Cotton, Wool, and Man-Made Fiber Textiles and Textile Products, Sept. 17, 1980, United States-People's Republic of China, 32 U.S.T. 2071, T.I.A.S. No. 9820 [hereinafter cited as China Treaty].

Textiles and textile products are defined in the country of origin regulations. 50 Fed. Reg. at 8723-24 (to be codified at 19 C.F.R. § 12.130(a)). The term includes merchandise subject to any of the tariff item numbers specifically listed in the Tariff Schedules of the United States, 19 U.S.C. § 1202. 50 Fed. Reg. at 8723. In addition, textiles and textile products include merchandise:

- (1) In chief value of cotton, wool, man-made fibers, or blends thereof in

for the determination of the "country of origin."³ Such a determination is important in the interpretation of quota requirements in the case of textiles manufactured in a multicountry operation.⁴ Under prior court decisions and administrative rulings, goods manufactured in more than one country were classified by reference to the "country of exportation" stan-

which those fibers, in the aggregate, exceed in value each other single component fiber thereof, or

(2) In which either the cotton content [sic] or the man-made fiber content equals or exceeds 50 percent by weight of all component fibers thereof, or

(3) In which the wool content exceeds 17 percent by weight of all component fibers thereof, or

(4) Containing blends of cotton, wool, or man-made fibers, which fibers, in the aggregate, amount to 50 percent or more by weight of all component fibers thereof

Id. at 8723-24.

3. *See infra* notes 58-124 and accompanying text. Under the new regulations, the Customs Service will enforce visa and export procedures, documentation, and other requirements for the importation of textiles and textile products. 50 Fed. Reg. at 8724 (to be codified at 19 C.F.R. § 12.130(f)). The regulations require visa or export licenses for textiles or textile products to enter the United States, to be issued by the government authorities of the "country of origin" irrespective of whether the goods are directly imported to the United States. *Id.* If Customs determines that the information in the declaration is incomplete or insufficient, Customs will detain the goods. *Id.* at 8725 (to be codified at 19 C.F.R. § 12.130(g)). The regulations define the "country of origin" for articles which consist, in whole or in part, of materials which originated or were processed in another foreign territory or country. *Id.* at 8724 (to be codified at 19 C.F.R. § 12.130(b)). The "country of origin" is the country of original production, or the country in which the goods are subjected to "substantial manufacturing or processing operations" that substantially transforms them into "new and different article[s] of commerce." *Id.*

The regulations provide that Customs will determine whether textiles or textile products have been substantially transformed by applying several criteria including changes in identity, changes in character, or changes in commercial use. *Id.* (to be codified at 19 C.F.R. § 12.130(d)(1)(2)). However, the regulations specifically preclude several manufacturing or processing operations from being considered as resulting in substantial transformation, e.g., finishing and assembling of components. *Id.* (to be codified at 19 C.F.R. § 12.130(e)(2)).

4. *See infra* notes 58-79 and accompanying text. The regulations define the term multicountry operation by requiring a declaration for all merchandise that undergoes a multiple country operation. 50 Fed. Reg. at 8725 (to be codified at 19 C.F.R. § 12.130(f)(2)).

Textiles and textiles [sic] products which were subjected to manufacturing or processing operations in, and/or incorporate materials originating in more than one foreign territory or country, or an insular possession of the U.S. or were assembled in, and/or incorporate fabricated components which are the product of the U.S. and more than one foreign territory, country or insular possession of the U.S., shall be identified in a declaration

Id.

dard.⁵ The new regulations, however, impose a complex "substantial transformation" test under which that classification is made.⁶

This Note argues that the implementation of the new regulations violates both the spirit and the letter of bilateral and multilateral trade agreements to which the United States is a party.⁷ In particular, the regulations contradict the Arrange-

5. See *Cardinal Glove Co. v. United States*, 4 Ct. Int'l Trade 41, 44 (1982). Generally, the country of exportation standard held the country from which the goods are immediately exported to the United States accountable for the goods under its bilateral agreement. *Id.*; see *infra* notes 76-79 and accompanying text. In *Cardinal Glove*, the court determined that for textiles and textile products manufactured in a multicountry operation, the country of exportation is a material term in any bilateral restraint agreement, and "[i]n the absence of specific statutory or regulatory authority to the contrary, therefore, the court shall adhere to the rationale and the standards adopted by prior court and customs decisions in ascertaining the country of exportation." *Cardinal Glove*, 4 Ct. Int'l Trade at 44; see *infra* notes 65-73 and accompanying text.

6. 50 Fed. Reg. at 8723 (to be codified at 19 C.F.R. § 12.130). The Customs Service described the new regulations as follows:

[I]n order to change the country of origin of merchandise produced in one country and sent to a second country for processing, the merchandise must be substantially transformed in the second country into a new and different article of commerce by a substantial manufacturing or processing operation. Criteria to be used in determining if a new and different article has emerged and if there has been a substantial manufacturing or processing operation are included in the regulations.

U.S. Customs Service, Questions and Answers 2 (Aug. 22, 1984), *reprinted in* Daily News Rec., Aug. 23, 1984, at 11, col. 2.

7. See *infra* notes 126-46 and accompanying text. United States importers and retailers of textile products filed for a preliminary injunction on the promulgation of the new regulations. *Mast Industries, Inc. v. United States*, No. 84-111, slip op. (Ct. Int'l Trade Oct. 4, 1984) (defendant's motion for summary judgment granted). Plaintiffs contended that the regulations exceed the Customs Service's delegated authority under the Agriculture Act of 1956, § 204, 7 U.S.C. § 1854 (1982), and that the regulations are arbitrary, capricious, and contrary to binding precedent. *Mast Industries*, No. 84-111, slip op. at 12. Plaintiffs also contended that the regulations were promulgated in violation of the prior notice and comment procedures of the Administrative Procedure Act, 5 U.S.C. § 553 (1982). *Mast Industries*, No. 84-111, slip op. at 11.

The court held that the congressional delegation to the President to issue regulations to limit textile imports is valid and the new regulations are within his authority. *Id.* at 19. The court also held that the regulations involve a foreign affairs exception under 5 U.S.C. § 553(a)(1) and therefore are exempt from the rulemaking procedures of the Administrative Procedure Act. *Mast Industries*, No. 84-111, slip op. at 38.

The court, in an opinion written by Justice DiCarlo, discussed the issues of the delegation and the Administrative Procedures Act notice at length. *Id.* at 16-39. The court, however, dismissed plaintiffs contention that the regulations violate the MFA

ment Regarding International Trade in Textiles⁸ (Multifiber Arrangement or MFA), an international agreement established to provide for orderly and nondiscriminatory trade in textiles and textile products.⁹ After an overview of the textile and apparel industry,¹⁰ the United States' enabling statute,¹¹ and the MFA,¹² this Note will examine the new textile regulations in light of judicial and administrative rulings.¹³ An examination of the conflict between the new regulations and the MFA follows.¹⁴ Finally, an analysis of the effects of the new regulations on the domestic economy and on international relations will be discussed.¹⁵

and the bilateral trade agreements. *Id.* at 22. The court stated that neither the language of the MFA nor that of any bilateral agreements "would show an intent to create private rights, *i.e.*, to make the agreements self-executing. Plaintiffs do not have a protected interest to argue that the country of origin regulations violate the terms of the MFA or the bilaterals, or are promulgated outside their framework." *Id.* This Note focuses on the contention of the plaintiffs in *Mast Industries*, that the regulations violate the terms of the MFA and the bilateral agreements. The Customs Service stated that the *Mast Industries* court addressed the issue that the country of origin regulations violate the MFA and the various bilateral agreements negotiated by the United States to limit imports. 50 Fed. Reg. at 8722. However, the *Mast Industries* court did not review the issue.

8. Dec. 20, 1973, 25 U.S.T. 1001, T.I.A.S. No. 7840, 930 U.N.T.S. 166 [hereinafter cited as MFA].

9. *Id.* art. 1(2). In December 1973, under the auspices of the General Agreement on Tariffs and Trade, opened for signature Oct. 30, 1947, 61 Stat. A5, T.I.A.S. No. 1700, 55 U.N.T.S. 194 [hereinafter cited as GATT], representatives of 50 nations negotiated the MFA. The MFA covers textiles and textile products which have chief weight or chief value in cotton, wool, or manmade fibers, or which contain over 17%, by weight, of wool. MFA, *supra* note 8, art. 12(1). For a comprehensive outline of the MFA, see Das, *The GATT Multifiber Arrangement*, 17 J. WORLD TRADE L. 95 (1983).

The MFA provides for textile importing nations, like the United States to negotiate bilateral agreements to establish restraints, or quotas, with exporting nations. MFA, *supra* note 8, art. 4(2)(3); see, *e.g.*, Agreement Relating to Trade in Cotton, Wool, and Man-Made Fiber Textiles and Textile Products, Dec. 1, 1982, United States-Korea, — U.S.T. —, T.I.A.S. No. 10,611; Hong Kong Treaty, *supra* note 2; Agreement Relating to Trade in Cotton, Wool and Man-Made Fiber Textiles and Textile Products, Dec. 5, 1980, United States-Malaysia, — U.S.T. —, T.I.A.S. No. 10,101. The United States has entered into bilateral agreements with 28 nations. 49 Fed. Reg. 31,248 (1984). The United States also has bilateral agreements with eight MFA nonsignatory nations. *Id.*

10. See *infra* notes 16-32 and accompanying text.

11. See *infra* notes 33-35 and accompanying text.

12. See *infra* notes 36-58 and accompanying text.

13. See *infra* notes 59-124 and accompanying text.

14. See *infra* notes 125-46 and accompanying text.

15. See *infra* notes 147-75 and accompanying text.

I. *BACKGROUND*A. *The Textile and Apparel Industry*

International trade in textiles and textile products accounts for nearly five percent of total world trade.¹⁶ In the United States, the textile and apparel industry employs approximately 1.9 million workers and provides at least 2 million jobs in other related industries.¹⁷ These industries generate a gross national product of U.S.\$45 billion.¹⁸ The textile and apparel industry in the United States,¹⁹ like that of other developed industrialized nations²⁰ has been challenged by the textile industries of newly industrialized states.²¹ These states have been able to combine inexpensive labor and standardized production to undersell textile producers in developed nations.²² For many of these newly industrialized countries, textile production serves as an appropriate "take off" industry for sustained economic growth.²³ The significant export perform-

16. Das, *supra* note 9, at 95.

17. BUREAU OF LABOR STATISTICS, U.S. DEP'T OF LABOR, EMPLOYMENT AND EARNINGS, 48-49 (Dec. 1984).

18. U.S. DEP'T OF COM., SURVEY OF CURRENT BUSINESS VOL. 65, NO. 1, S30-S32 (1985).

19. For an excellent history of protectionism and the United States textile and apparel industry, see Aggarwal & Haggard, *The Politics of Protection in the U.S. Textile and Apparel Industries*, in AMERICAN INDUSTRY IN INTERNATIONAL COMPETITION 249, 263-307 (1983).

20. The identity of the developed countries is not subject to wide debate. R. SUNDRUM, DEVELOPMENT ECONOMICS 21 (1983). The classification includes all the countries of Europe (except Turkey) and North America, three countries of South America (Argentina, Chile and Uruguay), Israel, Japan, South Africa, Australia, and New Zealand. *Id.* The Soviet Union and the countries of the East European bloc are also considered developed countries. *Id.*

21. Aggarwal & Haggard, *supra* note 19, at 250. The distinction between newly industrialized states and less developed countries is essentially arbitrary. Haberler, *The Liberal International Economic Order in Historical Perspective*, in CHALLENGES TO A LIBERAL INTERNATIONAL ECONOMIC ORDER 43, 51 (1979). However, countries such as South Korea, Taiwan, Malaysia, Brazil, Hong Kong, and Singapore have pursued market-oriented policies in foreign trade and have achieved high growth rates. *Id.*; see Little, *The Developing Countries and the International Order*, in CHALLENGES TO A LIBERAL INTERNATIONAL ECONOMIC ORDER 259, 270-71 (1979); *infra* notes 23-26 and accompanying text.

22. Aggarwal & Haggard, *supra* note 19, at 249.

23. See Perlow, *The Multilateral Supervision of International Trade: Has the Textiles Experiment Worked?*, 75 AM. J. INT'L L. 93, 94 (1981). Textile manufacturing is an important "take off" industry for underdeveloped countries that wish to establish initial stages of industrialization. For labor-abundant, less developed countries, textile manufacturing is competitive with markets in developed nations, and these states are

ances of Hong Kong, Taiwan, the Republic of Korea, and Singapore, since the 1960's,²⁴ and the People's Republic of China since the 1970's,²⁵ is a direct result of export-promotion economic planning.²⁶

This global shift in textile production has resulted in long-term losses of production and employment in the United States.²⁷ Since the 1950's, a number of factors, including changes in consumption patterns and fashion, competition from manmade fibers, and rising wages in the northern United States, have forced textile firms to merge and relocate in the southern United States.²⁸ Despite a recessionary period in the mid-1970's, total imports of textiles and textile products into the United States have increased dramatically. In 1984, the textile and apparel trade deficit reached a record high of U.S.\$16.2 billion, a fifty-three percent increase over the previ-

able to build their export potential and improve their balance of payments. *Id.*; see W. ROSTOW, *THE STAGES OF ECONOMIC GROWTH* 4-12 (1960). *But see* R. SUNDRUM, *supra* note 20, at 132. Rostow's analysis of the five stages of growth, including the "take off" stage, is derived from the past experience of the developed nations. *See* W. ROSTOW, *supra*, at 1. However, there is little evidence that many of the less developed nations will be able to follow the same pattern of growth. R. SUNDRUM, *supra* note 20, at 132.

24. *See* R. SUNDRUM, *supra* note 20, at 42-44; M. TODARO, *ECONOMIC DEVELOPMENT IN THE THIRD WORLD* 373 (2d ed. 1981).

25. *See* A. HO, *DEVELOPING THE ECONOMY OF THE PEOPLE'S REPUBLIC OF CHINA* 33-37 (1982); Eckstein, *China's Trade Policy & Sino-American Relations*, 54 *FOREIGN AFF.* 134, 144 (1975).

26. *See* R. SUNDRUM, *supra* note 20, at 42-44; M. TODARO, *supra* note 24, at 373. These newly industrialized states have not retained the characteristics of the low income countries. Myint, *Comment on International Inequality and Foreign Aid in Retrospect*, in *PIONEERS IN DEVELOPMENT* 166, 171 (1984). Development economists have cited the deliberate pursuit of export expansion policies by Hong Kong, Taiwan, Singapore, and South Korea. *Id.* These countries have succeeded in expanding labor-intensive manufactured exports by encouraging small scale industry in close proximity to a dynamic and labor-intensive agricultural sector. *Id.* at 170. However, other development economists have debated the policy of export promotion as the key to sustained economic growth. Streeten, *Development Dichotomies*, in *PIONEERS IN DEVELOPMENT* 337, 346 (1984). It is argued that the reasons for the successes of these newly industrialized states are more complex. *Id.* "[T]he singling out of export promotion through liberal trade policies is a false account of the success stories." *Id.*

27. Aggarwal & Haggard, *supra* note 19, at 256-57.

28. *Id.* at 255. In 1950, 40.5% of textile employment in the United States was in six Northeastern states. *Id.* at 256. By 1970, these states accounted for only 21.7%. *Id.* at 256-57. With modern equipment and nonunionized workers, firms in the South were able to sell textile products at a lower cost than the Northeastern firms. *Id.* at 257.

ous year.²⁹ Figures released by the United States Department of Commerce show that, in 1984, imports of textiles and apparel increased by forty-one percent to U.S.\$18 billion, while exports remained constant at U.S.\$2.9 billion.³⁰

United States firms have increasingly sought greater protection in textile trade through the negotiation of bilateral agreements and the establishment of quotas.³¹ Furthermore, the textile and apparel industries in the United States have placed political pressure on the Reagan Administration to further regulate the infiltration of the domestic market by low-wage imports.³² Against this background of economic and political pressures, new trade regulations were promulgated.

B. *The Multifiber Arrangement*

The Constitution of the United States vests in Congress the power to regulate commerce between the United States and foreign nations.³³ Congress has delegated to the Executive branch the power to regulate the importation of foreign-made textiles into the United States under section 204 of the Agriculture Act of 1956.³⁴ Section 204 gives the President broad

29. U.S. BUREAU OF THE CENSUS, U.S. DEP'T OF COM., MAJOR SHIPPERS OF COTTON, WOOL, AND MAN-MADE FIBER TEXTILES AND APPAREL, category O, total (Dec. 1984). In 1983, the deficit for textiles and apparel was U.S.\$10.6 billion. *Id.*

30. *Id.*

31. Aggarwal & Haggard, *supra* note 19, at 252. Since the early 1960's, industry and labor "groups in the textile and apparel industries have responded to global market changes by attempting to insulate the domestic market from international competition. Arguing that low profits, unemployment, and plant closings are due to imports, they have insisted that the government impose quotas. Their efforts have been successful." *Id.* "By 1982, the United States was severely restricting imports of cotton, wool, and man-made fiber textiles and apparel under the global Multifiber Arrangement, which controlled virtually all world trade in textiles and apparel." *Id.*

32. See Pine, *How President Came to Favor Concessions for U.S. Textile Makers—Concerns of an Election Year Played Part in Instituting a Plan to Tighten Trade*, *Wall Street J.*, Jan. 6, 1984, at 1, col. 6.

33. U.S. CONST. art. I, § 8, cls. 1, 3. "The Congress shall have the power [t]o lay and collect Taxes, Duties, Imposts and Excises . . ." *Id.* cl. 1. "[The Congress shall have the power] [t]o regulate Commerce with foreign Nations, and among the several States . . ." *Id.* cl. 3.

34. 7 U.S.C. § 1854 (1982). That section provides:

The President may, whenever he determines such action appropriate, negotiate with representatives of foreign governments in an effort to obtain agreements limiting the export from such countries and the importation into the United States of any agricultural commodity or product manufactured therefrom or textiles or textile products, and the President is author-

authority to negotiate agreements with foreign governments for the purposes of limiting textile imports and to issue regulations governing the entry of any textile subject to these agreements.³⁵

Pursuant to section 204,³⁶ the United States entered into the MFA.³⁷ The purpose of the MFA is

to achieve the expansion of trade, the reduction of barriers to such trade and the progressive liberalization of world trade in textile products, while at the same time ensuring

ized to issue regulations governing the entry or withdrawal from warehouse of any such commodity, product, textiles, or textile products to carry out any such agreement. In addition, if a multilateral agreement has been or shall be concluded under the authority of this section among countries accounting for a significant part of world trade in the articles with respect to which the agreement was concluded, the President may also issue, in order to carry out such an agreement, regulations governing the entry or withdrawal from warehouse of the same articles which are the products of countries not parties to the agreement. Nothing herein shall affect the authority provided under section 624 of this title.

Id. As originally enacted, this section gave the President the authority to issue regulations to implement negotiated textile agreements. However, Congress failed to give the President the authority to control imports from countries not a party to a specific textile agreement. Consequently, Congress amended section 204 to grant the President authority to control imports from countries not party to multilateral or bilateral agreements. See Pub. L. No. 87-488, 76 Stat. 104 (codified as amended at 7 U.S.C. § 1854 (1982)).

35. 7 U.S.C. § 1854 (1982). The scope of the President's authority under § 204 was recently determined by the United States Court of Appeals for the Federal Circuit. *Am. Ass'n of Exporters & Importers-Textile & Apparel Group v. United States*, 751 F.2d 1239 (Fed. Cir. 1985). The court affirmed a Court of International Trade decision that had refused to overturn the imposition of quotas on Chinese textile imports. *Id.* at 1240; see 48 Fed. Reg. 2164 (1983) (textile and textile products from China are restrained in absence of a bilateral agreement). Plaintiff, a group of apparel importers, claimed that the United States Department of Commerce did not have the authority to impose the restrictions without a finding of a market disruption or consultations under the MFA. *Am. Ass'n of Exporters & Importers*, 751 F.2d at 1242. The court ruled that § 204 "is a broad grant of authority to the President in the international field in which congressional delegations are normally given a broad construction." *Id.* at 1247 (citing *South Puerto Rico Sugar Co. Trading Corp. v. United States*, 334 F.2d 622, 632 (Ct. Cl. 1964)). In addition, the court held that § 204 "imposes no restrictions on the President's administration of the textile trade program. There are no procedural requirements nor limitations All that is needed is that the President's action be relevant to the enforcement of some existing textile agreement." *Am. Ass'n of Exporters & Importers*, 751 F.2d at 1247; see *Federal Appeals Court Affirms CIT Ruling on Chinese Textile Complaint by Importers*, [Jan.-June] 2 INT'L TRADE REP. (BNA) No. 2, at 68 (Jan. 9, 1985).

36. 7 U.S.C. § 1854 (1982).

37. MFA, *supra* note 8.

the orderly and equitable development of this trade and avoidance of disruptive effects in individual markets and on individual lines of production in both importing and exporting countries.³⁸

The MFA strikes a balance between the interests of exporting countries and those of importing countries.³⁹ It attempts to reconcile the needs of developing countries to sustain growth in exports with the desire of more developed countries to limit low-wage imports.⁴⁰

While the MFA does not establish any quantitative restraints on trade in textiles, it does outline procedures to achieve its goals.⁴¹ If an importing country determines that it is suffering a market disruption,⁴² and that quantitative restraints on the influx of foreign-produced textiles are necessary to protect its markets, article 3 of the MFA requires that it consult the country whose exports it believes to be disruptive.⁴³ If no agreement on restraint is reached between the im-

38. *Id.* art. 1(2).

39. See Perlow, *supra* note 23, at 100. This balance had been articulated by earlier multilateral agreements to manage international trade in textiles. *Id.* Under the auspices of GATT, *supra* note 9, the principle framework governing international trade, the Long Term Arrangement Regarding International Trade in Cotton Textiles and Apparel, Feb. 9, 1962, 13 U.S.T. 2673, T.I.A.S. No. 5240, 471 U.N.T.S. 296 [hereinafter cited as LTA], regulated trade in textiles and apparel from 1962 until its expiration in 1973.

40. MFA, *supra* note 8, art. 1(2).

41. See *id.* For an outline of the procedures of the MFA, see Perlow, *supra* note 23, at 100-03.

42. The MFA defines the concept of market disruption generally as follows: The determination of a situation of "market disruption" . . . shall be based on the existence of a serious damage to domestic producers or actual threat thereof. Such damage must demonstrably be caused by [two factors, generally in combination: 1) a sharp and substantial increase or imminent increase of imports of particular products from particular sources, and 2) prices which are substantially below those for similar goods of comparable quality in the market of the importing country] The existence of damage shall be determined on the basis of an examination of the appropriate factors having a bearing on the evolution of the state of the industry in question such as: turnover, market share, profits, export performance, employment, volume of disruptive and other imports, production, utilization of capacity, productivity and investments. No one or several of these factors can necessarily give decisive guidance.

MFA, *supra* note 8, annex A. The ambiguity of the market disruption concept is examined by K. DAM, *THE GATT LAW AND INTERNATIONAL ORGANIZATION* 313-14 (1970).

43. MFA, *supra* note 8, art. 3(3).

porting country and the exporting country within sixty days of the request for consultation, the importing country may impose restraints unilaterally.⁴⁴ That country is given authority under article 3 to restrain trade prior to consultation in "highly unusual and critical circumstances,"⁴⁵ where continued importation during the consultation period would result in serious damage.⁴⁶

Article 4 of the MFA allows participating countries to enter into bilateral agreements to restrain trade, if such agreements are consistent with the goals of the MFA.⁴⁷ Most of these agreements establish aggregate limits for textiles or textile products entering a country.⁴⁸ Specific import levels may be established in a given bilateral agreement for sensitive items where import penetration is high.⁴⁹ Bilateral agreements may also provide for consultation levels for products not subject to negotiated ceilings.⁵⁰ Such a provision would allow an exporting country to request higher ceilings at any time during the term of the agreement.⁵¹

In order to assure compliance with the terms of the MFA and those of any bilateral agreements made pursuant to article 4, the MFA establishes a Textile Committee.⁵² The Committee consists of parties to the MFA,⁵³ who then select a nine mem-

44. *Id.* art. 3(5)(i). The restraints, or quotas, must be pursuant to either the appropriate provisions of GATT, *supra* note 9, or the MFA's definition of market disruption, MFA, *supra* note 8, annex A; *see supra* note 42.

45. MFA, *supra* note 8, art. 3(6).

46. *Id.* Measures taken under article 3 of the MFA are to be introduced for a period not exceeding one year, subject to renewal or extension, if agreement is reached between the countries concerned with the renewal or extension. *Id.* art. 3(8). These extensions are easily obtained. Perlow, *supra* note 23, at 101.

47. MFA, *supra* note 8, art. 4(2). For a statement of the principal goals of the MFA, *see id.* art. 1(2).

48. *See* SUBCOMM. ON TRADE OF THE H.R. COMM. ON WAYS AND MEANS, 95TH CONG., 2D SESS., BACKGROUND MATERIAL ON THE MULTIFIBER ARRANGEMENT 4 (Comm. Print 1978) [hereinafter cited as BACKGROUND MATERIAL]. The various groups of products include yarn, apparel, and wool products. *Id.*; *see supra* note 2. For examples of such bilateral agreements, *see supra* note 9.

49. BACKGROUND MATERIALS, *supra* note 48, at 4. Sensitive items are specifically listed as subcategories in the bilateral agreement, examples of which are cotton knit sweaters or manmade fiber gloves. *Id.* at 4-5.

50. *Id.* at 4.

51. *Id.* The House Committee report sets forth a sample of the structure of a bilateral agreement. *Id.* at 5-7.

52. MFA, *supra* note 8, art. 10(1).

53. *Id.* The Textile Committee is responsible for the production of periodic re-

ber Textile Surveillance Body (TSB) to oversee the implementation of the MFA.⁵⁴ The TSB is an independent body established to review particular disputes between member states.⁵⁵ It does not, however, have authority to issue binding opinions.⁵⁶

Article 8 of the MFA addresses in general terms the problem of circumvention of the bilateral textile agreements due to rerouting and transshipment.⁵⁷ It provides that "[a] country should consult with the exporting country of origin and with other countries involved in the circumvention with a view to seeking promptly a mutually satisfactory solution."⁵⁸

ports and studies of world production and trade in textiles in order to further the goals of trade liberalization. *Id.* art. 10(3); *see* Perlow, *supra* note 23, at 103.

54. MFA, *supra* note 8, art. 11(1). The Textile Surveillance Body (TSB) reviews particular disputes between states at the request of a party to the dispute. *Id.* arts. 11(4)-(5). Although the TSB has no enforcement powers, the MFA requires that all members "shall endeavor to accept [the TSB's] recommendation in full." *Id.* art. 11(8).

For a comprehensive study of the Textile Committee and the TSB as supervisory organs of international textile trade, *see* Perlow, *supra* note 23, at 103-18. It is concluded that the overall contributions of these supervisory groups have been satisfactory, having a "tangible and positive impact" on the course of international trade. *Id.* at 131. It is suggested that the TSB-type supervisory body represents an improvement over ad hoc panels and the GATT system. *Id.*

55. MFA, *supra* note 8, art. 11(1).

56. *See id.* arts. 11(5)-(6); Perlow, *supra* note 23, at 103.

57. MFA, *supra* note 8, art. 8(1). Rerouting and transshipment are trade actions by which textiles and textile products legally or illegally avoid quotas of an importing country. SUBCOMM. ON OVERSIGHT AND INVESTIGATIONS OF THE H.R. COMM. ON ENERGY AND COMMERCE, 98TH CONG. 2D SESS., *THE ILLEGAL AND UNFAIR IMPORTATION OF TEXTILES, APPAREL GOODS, ELECTRONICS, AND STEEL 78* (Comm. Print 1984) (statement of Wilbur Daniels, Executive Vice President, International Ladies' Garment Workers Union) [hereinafter cited as *OVERSIGHT HEARINGS*]. If quotas from one exporting country are filled, it is not contrary to the MFA for exporters to arrange for production of textiles from a country with an unfilled quota or a country that is not a member of a bilateral agreement. *Id.* In addition, goods are often modified to avoid quota restrictions. *Id.* The practice of blending fabrics that are not covered by the MFA or the bilateral agreements, such as silk, linen, and ramie, with controlled fibers removes the items from quota restrictions. *Id.* at 79; *see* Ehrlich, *Asia Quota Bushfire Has US Facing an Importer's Nightmare*, *Women's Wear Daily*, Feb. 23, 1984, at 10, col. 1. False labeling or false documentation are obvious fraudulent violations. *OVERSIGHT HEARINGS*, *supra*, at 78.

58. MFA, *supra* note 8, art. 8(2).

II. THE NEW REGULATIONS: A DEFINITION OF "COUNTRY OF ORIGIN"

A. Cardinal Glove Co. v. United States: *The Country of Exportation Standard*

Under the terms of the MFA, textiles and apparel products are subject to import restrictions based upon their country of exportation as well as their country of origin.⁵⁹ However, the MFA does not define these terms.⁶⁰ Article 3 of the MFA recognizes that importing nations may seek to negotiate restrictions on textiles and textile products of "countries whose exports . . . are causing market disruption" in the importing nation.⁶¹ Article 4 also refers to the "exporting countries" of textile products.⁶² However, where there has been circumvention of a trade agreement, article 8 provides for consultations "with the exporting country of origin."⁶³

While the meaning under the MFA of "country of exportation" and "country of origin" is unclear, the terms of a bilateral agreement between the United States and Hong Kong⁶⁴ incorporating those of the MFA were reviewed by the United States Court of International Trade in *Cardinal Glove Co. v. United States*.⁶⁵ The issue before the court was whether glove panels produced in Hong Kong, but assembled in Haiti, constituted exports from Hong Kong so as to require an export license and visa from Hong Kong upon shipment.⁶⁶ The United States Government contended that the merchandise,

59. See *infra* notes 60-63 and accompanying text (discussing the terminology used in the MFA and the lack of any clear standards in the agreement itself).

60. According to the Customs Service, GATT has not been willing to define specific rules for country of origin issues. 50 Fed. Reg. 8722 (1985). "Consequently, there is no GATT, MFA, or bilateral agreement provision defining country of origin or restricting such definition." *Id.*

61. MFA, *supra* note 8, art. 3(2).

62. *Id.* art. 4(2).

63. *Id.* art. 8(2).

64. Hong Kong Treaty, *supra* note 2.

65. 4 Ct. Int'l Trade 41, 42 (1982). The court reviewed the bilateral textile agreement between the United States and Hong Kong and stated that "[d]uring the term of the Agreement, the Government of Hong Kong shall limit annual exports from Hong Kong of cotton, wool, and man-made fiber textiles and textile products of Hong Kong origin to the United States of America" *Id.*

66. *Id.* at 43. The present United States-Hong Kong bilateral trade agreement states that the agreement applies to exports to the United States. See Hong Kong Treaty, *supra* note 2, para. 2. Paragraph 4 of the agreement provides for the setting

which was cut into components in Hong Kong from cotton fabric produced in Hong Kong and shipped after processing to Haiti, prior to shipment to the United States, was subject to the United States-Hong Kong bilateral agreement.⁶⁷ Plaintiff argued that the gloves were products of Haiti because they had been assembled in Haiti and could not be denied entry into the United States for lack of a Hong Kong export license.⁶⁸ The sole issue presented was a determination of the country from which the merchandise was exported.⁶⁹

The court found that the United States Government's argument would place "a grossly unfair burden"⁷⁰ on Hong Kong and would challenge the practice of multicountry manufacturing.⁷¹ The "country of exportation" was held to be the country from which the goods are immediately imported into the United States.⁷² However, the court also noted that a country from which textiles or textile products were directly shipped to the United States might not be considered the country of exportation if the merchandise was intended to enter the commerce of the intermediate country.⁷³

of quota limits for "annual exports from Hong Kong . . . to the United States." *Id.* para. 4.

67. *Cardinal Glove*, 4 Ct. Int'l Trade at 42.

68. *Id.* at 43.

69. *Id.*

70. *Id.*

71. *Id.* at 43-44. The court stated that:

[T]he exportation of merchandise from a country producing a product to an intermediate country for the purpose of processing, manipulating or assembling that product, is a common practice in our present day industrial and technological economy. Accordingly, in ascertaining the intent of the agreement the language therein referring to "exports from Hong Kong" must be given a construction consistent with the interpretation given to similar language in the ascertainment of the "country of exportation" in the administration of our tariff laws.

Id. (emphasis added).

72. *Id.* at 44; (citing *United States v. G.W. Sheldon & Co.*, T.D. 42,541, 53 *Treas. Dec.* 34, 36 (1928)).

73. *Cardinal Glove*, 4 Ct. Int'l Trade at 44. The court in *Cardinal Glove* held that the country prior to importation to the United States would not be the country of exportation if: 1) no part of the merchandise was intended for diversion into the commerce of the intermediate country; 2) none of the goods were, in fact, diverted into the commerce of the intermediate country; 3) a contingency of diversion did not exist; and 4) none of the merchandise was in any way treated, processed, altered, manipulated or changed in character in the intermediate country. *Id.* The terms of the exception are not defined.

Although the United States Government did not appeal the *Cardinal Glove* decision, the United States Customs Service expressed dissatisfaction with the holding.⁷⁴ The Customs Service stated that the interpretation of all United States bilateral textile restraint agreements currently in force should be read with reference to a "country of origin" standard and not a "country of exportation" standard as defined by the *Cardinal Glove* court.⁷⁵ For goods manufactured in more than one country, the Customs Service argued that in order to change the country of origin from the country of initial production, a manufacturing operation must have taken place in a subsequent country from which "a new and different article emerge[s], having a distinctive name, character, or use."⁷⁶ According to the Customs Service, this "substantial transformation" test must be met in order to change the country of origin of textiles or textile products for quota purposes.⁷⁷ The Customs Service explained that it would consider a number of factors, including the results of processing operations in the country prior to export to the United States.⁷⁸ However, the Customs Service did not disagree with the court's conclusion in *Cardinal Glove* be-

74. T.D. 82-169, 16 Cust. B. & Dec. 471 (1982). The Customs Service wrote that they had been "advised by the Departments of State and Commerce that the application of the 'country of exportation' concept to entries of merchandise under bilateral textile trade agreements would seriously undermine the operation of the [United States] textile program." *Id.* at 471.

75. *Id.* at 472.

76. *Id.* (citing *Anheuser-Busch Brewing Ass'n v. United States*, 207 U.S. 556, 562 (1907) (corks processed in Spain before import to the United States were deemed not to have been substantially transformed for drawback duty requirements).

77. C.S.D. 80-10, 14 Cust. B. & Dec. 740 (1981). The Customs Service relied on the "substantial transformation" for merchandise which has been processed in two or more countries. *Id.* In Customs Service Decision 80-10, the assembly and finishing of sweaters in Hong Kong from knit panels made in Taiwan was held to be "substantial transformation" and Hong Kong was the "country of origin" for tariff purposes. *Id.*

78. *Id.* at 741. According to the Customs Service:

[The merchandise] is considered for tariff purposes to be a product of the last country in which the processing created a new and different article.

.....
A number of factors may be considered in determining whether a particular process results in the creation of a new and different article. A major consideration is whether a new use results from the processing and the degree of change from any former use. Another consideration is the amount of processing performed in each country and whether the processing results in an article having a new identity.

Id. (citations omitted).

cause the assembly and finishing of the glove panels in Haiti constituted a substantial transformation sufficient to change the country of origin.⁷⁹

B. *The United States Textile Import Program*

The authority granted by Congress to the President to administer bilateral textile agreements has been exercised by the Executive through a network of high-level executive committees.⁸⁰ Chief among the advisory groups is the Committee for the Implementation of Textile Agreements⁸¹ (CITA), consisting of representatives of the Departments of State, Commerce, Labor, and the Treasury, and the United States Trade Representative.⁸² CITA's function is to supervise all textile trade agreements and to take appropriate action concerning textiles and textile products under section 204.⁸³

In response to concerns expressed by the domestic textile industry,⁸⁴ the Reagan administration established a task force⁸⁵ to analyze the import situation and the effects of rising imports on the domestic market.⁸⁶ That task force concluded that reg-

79. T.D. 82-169, 16 Cust. B. & Dec. at 472.

80. *Am. Ass'n of Exporters & Importers-Textiles & Apparel Group v. United States*, 583 F. Supp. 591, 593 (Ct. Int'l Trade 1984), *aff'd*, 751 F.2d 1239 (Fed. Cir. 1985); see *infra* notes 81-84 and accompanying text.

81. Exec. Order No. 11,651, 3 C.F.R. 676 (1976) *amended by* Exec. Order No. 11,951, 42 Fed. Reg. 1453 (1977) *reprinted in* 7 U.S.C. § 1854 (1982) [hereinafter cited as Exec. Order No. 11,651], established the Committee for the Implementation of Textile Agreements (CITA). The amendment simply deleted the reference to the LTA, *supra* note 39, and substituted reference to the MFA, *supra* note 8.

82. Exec. Order No. 11,651, *supra* note 81, § 1(a). The United States Trade Representative or his designee serves on CITA as a nonvoting member. *Id.*

83. *Id.* § 1. CITA's authority is to "the extent authorized by the President and by such officials as the President may from time to time designate." *Id.* § 1(c).

84. See OVERSIGHT HEARINGS, *supra* note 57, at 78-79. Recent hearings before the United States House of Representatives Subcommittee on Oversight and Investigations have reported that United States quotas and tariffs of textiles and apparel imports are easily and frequently circumvented. *Id.* According to government and industry witnesses, mislabeled country of origin markings, illegal transshipments, and counterfeit products are costing United States industry—already under tough trade competition from legitimate imports—millions of dollars in lost sales. *Id.*; see *House Investigation Panel Looks at Textile Fraud, Inadequacies in U.S. Customs Service*, [Oct.-Mar.] U.S. IMPORT WEEKLY (BNA) No. 22, at 724 (Mar. 7, 1984).

85. See *White House Releases Treasury Directive on Textile, Apparel Program Implementation*, [Apr.-Nov.] U.S. IMPORT WEEKLY (BNA) No. 32, at 996 (May 16, 1984).

86. See Affidavit of Walter C. Lenehan, Chairman of CITA at 5, *Mast Industries, Inc. v. United States*, No. 84-111, slip op. (Ct. Int'l Trade Oct. 4, 1984).

ulations should be promulgated to tighten the program.⁸⁷

On May 9, 1984, President Reagan issued Executive Order 12,475⁸⁸ in response to the task force's recommendations "to prevent circumvention or frustration of multilateral and bilateral agreements to which the United States is a party," and to increase the effectiveness of the textile import program.⁸⁹ The President directed the Secretary of the Treasury to consult with CITA and to issue interim regulations.⁹⁰ The regulations were to clarify or revise the country of origin rules as used by the Customs Service for textiles and textile products subject to section 204 and other appropriate administrative provisions.⁹¹ Final regulations were issued on March 5, 1985.⁹²

C. *The New Regulations*

The August 3, 1984 notice of the interim regulations,⁹³ explained that "in recent months the U.S. Customs Service has been faced with an ever increasing number and variety of instances where attempts have been made, either intentionally or otherwise, to circumvent the textile import program."⁹⁴ The final regulations are designed to prevent a situation where, Country A ships its recently completed textile products to Country B, where the product undergoes an insubstantial manufacturing process, e.g., sewing or repackaging. From there, the product is exported to the United States under Country B's quota for that product. In this way, if Country A's quota had been filled, the products would enter the United States in circumvention of the negotiated bilateral agreement.⁹⁵ The Customs Service contends that such circumven-

87. *Id.*

88. Exec. Order No. 12,475, 49 Fed. Reg. 19,955 (1984).

89. *Id.*

90. *Id.*

91. *Id.* CITA's policy guidelines were sent to the Treasury Department on July 17, 1984 and on August 3, 1984, the Commissioner of Customs, in his capacity as delegatee of the Secretary of the Treasury, issued the interim "country of origin" regulations. 49 Fed. Reg. 31,248 (1984).

92. 50 Fed. Reg. 8710 (1985). Over 650 comments on the interim regulations were received by the Customs Service. *Id.* at 8711.

93. 49 Fed. Reg. 31,248 (1984).

94. *Id.*; see *supra* note 84 and accompanying text.

95. See *Mast Industries*, No. 84-111, slip op. at 8; OVERSIGHT HEARINGS, *supra* note 57, at 53 (statement of James T. Broyhill, Congressman, North Carolina). Mr.

tion, made possible under the *Cardinal Glove* country of exportation standard,⁹⁶ severely jeopardizes the success of the United States Textile Program.⁹⁷

The new regulations apply to all imports of textiles and textile products subject to the MFA.⁹⁸ They amend several

Wilbur Daniels, of the International Ladies' Garment Workers Union, testified on the circumvention of quotas by transshipment and rerouting:

One of the most obvious ways of getting around filled quotas is transshipment through a country from which such shipments are not controlled. Generally, such transshipments involve false invoices and sewing labels into garments showing the false country of origin. . . . There is yet another more elusive type of transshipment—partially finished garments transferred to a country with open quota and then completed and marked to show the completing country as the country of origin. Since relatively little work is done in the second country, the garments should more properly be charged against the account of the initiating country, the one that has done most of the work.

Id. at 78. Mr. Daniels noted the effect of the growing import penetration on employment of United States workers. *Id.* at 77. Between 1973 and 1983, employment in the apparel industry dropped 23.7%, a loss in that period of nearly 300 thousand jobs. *Id.*

96. 4 Ct. Int'l Trade 41 (1982); see *supra* notes 67-91 and accompanying text.

97. 50 Fed. Reg. at 8711. In the supplementary information to the new regulations, the Customs Service wrote:

The future administration of these [bilateral restraint] agreements was severely jeopardized by the decision of the United States Court of International Trade in *Cardinal Glove Co. v. United States*, 4 C.I.T. 41, which concluded that, absent specific regulatory authority to the contrary, the bilateral textile agreement at issue therein was applicable only to textile products in which the agreement country was the "country of exportation."

50 Fed. Reg. at 8711.

98. 50 Fed. Reg. at 8716. In general, this covers most products which have chief weight or chief value in cotton, wool, or manmade fibers or which contain over 17%, by weight, of wool. MFA, *supra* note 8, art. 12(1). In addition, the regulations are applicable to merchandise which is produced by countries with which the United States has no textile agreements, under the authority delegated to the Executive by the Agriculture Act of 1956, § 204, 7 U.S.C. § 1854 (1982); see *supra* note 40 and accompanying text. Regulation 12.130(a) sets forth the scope of the regulations. 50 Fed. Reg. at 8723-24 (to be codified at 19 C.F.R. § 12.130(a)). In sum, any article that is subject to the MFA may be covered by the regulations. *Id.* The Customs Service explains that:

Customs does not believe the suggestion that the regulations cover non-MFA products has merit. Section 204 authorizes the President to issue regulations to carry out bilateral and multinational agreements that have been entered into pursuant to that section. There are no such agreements which cover non-MFA products. Therefore, there is no authority to include non-MFA products within the scope of these regulations, except insofar as information is required to distinguish those products from MFA products.

50 Fed. Reg. at 8717. This statement represents a change in opinion on this scope of the regulations. In September 1984, the Customs Service wrote, "since the princi-

provisions of the existing Customs Service regulations.⁹⁹ Regulation 12.130(b) defines the term country of origin as follows:

[A] textile or textile product . . . shall be a product of a particular foreign territory or country, or insular possession of the U.S., if it is wholly the growth, product, or manufacture of that foreign territory or country, or insular possession. However, except as provided in paragraph (c) [Applicability to United States articles sent abroad], a textile or textile product, subject to section 204, which consists of materials produced or derived from, or processed in, more than one foreign territory or country, or insular possession of the U.S., shall be a product of that foreign territory or country, or insular possession where it last underwent a substantial transformation. *A textile or textile product will be considered to have undergone a substantial transformation if it has been transformed by means of substantial manufacturing or processing operations into a new and different article of commerce.*¹⁰⁰

In effect, two tests are applied to products that have been sent to an intermediate country prior to shipment to the United States.¹⁰¹ First, in order to change the country of ori-

ples in the regulations used to determine the origin of merchandise were taken from court decisions, those principles will be applied to *all* textiles and textile products." U.S. Customs Service, Questions and Answers at 2, (Sept. 7, 1984), *reprinted in* Daily News Rec., Sept. 10, 1984, at 12, col. 3 (emphasis added).

99. The interim amendments to 19 C.F.R. §§ 6.18, 19.11, 141.52, 143.21, 143.22, 144.38 and 146.49 and the addition of 19 C.F.R. § 12.131 as published at 49 Fed. Reg. 31,248 (1984) are adopted with changes. 50 Fed. Reg. at 8723. The interim amendments to 19 C.F.R. §§ 18.5, 18.11, and 146.49 as published in 49 Fed. Reg. 38,245 (1984) are adopted without change. 50 Fed. Reg. at 8723.

100. 50 Fed. Reg. 8724 (to be codified at 19 C.F.R. § 12.130(b)) (emphasis added).

101. *See infra* notes 102-07 and accompanying text. The Customs Service described the new regulations as follows:

[I]n order to change the country of origin of merchandise produced in one country and sent to a second country for processing, the merchandise must be substantially transformed in the second country into a new and different article of commerce by a substantial manufacturing or processing operation. Criteria to be used in determining if a new and different article has emerged and if there has been a substantial manufacturing or processing operation are included in the regulations.

U.S. Customs Service, Questions and Answers 2 (Aug. 22, 1984), *reprinted in* Daily News Rec., Aug. 23, 1984, at 11, col. 2. The Customs Service has subsequently preferred to interpret the concept of a new and different article and a substantial manufacturing or processing operation as "particular aspects of substantial transformation." 50 Fed. Reg. at 8715-16. The Customs Service feels that prior court decisions have combined the two aspects of the present test. *Id.* at 8715; *see* *Belcrest Linens v.*

gin, a "substantial manufacturing or processing operation" must have been applied to the products in the intermediate country.¹⁰² Paragraph (d)(2) of regulation 12.130 establishes a standard for determining whether there has been a substantial operation.¹⁰³ A comparison is made before and after the manufacturing or processing operation performed in a subsequent country. In determining whether a textile or textile product has undergone a substantial manufacturing or processing operation, the Customs Service will consider the following criteria: 1) the physical change in the material or article; 2) the time involved in the operations; 3) the complexity of the operations; 4) the level or degree of skill or technology required; and 5) the value added to the articles.¹⁰⁴ Some manufacturing or processing operations are deemed to be insufficient for substantial transformation.¹⁰⁵

Second, the manufacturing or processing operation must also result in a new and different article.¹⁰⁶ Criteria used to determine if in fact a new and different article has resulted from the manufacturing or processing operation include changes in: 1) commercial designation or identity; 2) funda-

United States, 741 F.2d 1368 (Fed. Cir. 1984); *Uniroyal, Inc. v. United States*, 542 F. Supp. 1026, 1029-30 (Ct. Int'l Trade 1982) *aff'd per curiam*, 702 F.2d 1022 (Fed. Cir. 1983).

102. 50 Fed. Reg. 8724 (to be codified at 19 C.F.R. § 12.130(b)).

103. *Id.* (to be codified at 19 C.F.R. § 12.130(d)(2)).

104. *Id.*

105. *Id.* (to be codified at 19 C.F.R. § 12.130(e)(2)). The regulations set forth specific manufacturing operations which usually will not be deemed "substantial" operations by the Customs Service. These operations include:

(i) Simple combining operations, labeling, pressing cleaning or dry cleaning, or packaging operations, or any combination thereof;

(ii) Cutting to length or width and hemming or overlocking fabrics which are readily identifiable as being intended for a particular commercial use;

(iii) Trimming and/or joining together by sewing, looping, linking, or other means of attaching otherwise completed knit-to-shape component parts produced in a single country, even when accompanied by other processes (*e.g.* washing, drying, mending, etc.) normally incident to the assembly process;

(iv) One or more finishing operations on yarns, fabrics, or other textile articles, such as showerproofing, superwashing, bleaching, decatizing, fulling, shrinking, mercerizing, or similar operations; or

(v) Dyeing and/or printing of fabrics or yarns.

Id.

106. *Id.* (to be codified at 19 C.F.R. § 12.130(d)(1)).

mental character; or 3) commercial use.¹⁰⁷

Visas or export licenses¹⁰⁸ are necessary for textiles imported into the United States regardless of whether the products were shipped directly from that country to the United States or were transshipped.¹⁰⁹ This documentation¹¹⁰ makes it more difficult to alter the designation of the country of origin of merchandise produced in one country and sent to another before final shipment to the United States.¹¹¹

The country of origin rules set out in the regulations are a departure from the long standing principles articulated by the Customs Service and the courts.¹¹² Under *Cardinal Glove*, textile products were usually subject to the import quota of the country of assembly and finishing.¹¹³ The new regulations establish that the country of origin is the country where the components are produced, unless the goods are "substantially transformed."¹¹⁴

The regulations differ from the "substantial transforma-

107. *Id.*

108. The visa or export license is issued by the government of the country of origin. The Customs Service explained the additional documentation under the new regulations:

In order for the Customs Service to determine the proper country of origin of imported textiles and textile products, the regulations require that a declaration containing pertinent information must be filed with each importation. The format to be used and information required are expressly set out in the regulations. These declarations may be signed by the manufacturer, exporter, or importer. If all the information called for by the declaration cannot be supplied, the importer will submit a certification attesting to the fact that after the exercise of due diligence the importer is unable to provide further information. In that event, Customs will utilize the best information available, including the experience of domestic industry, to determine the country of origin of the imported merchandise.

U.S. Customs Service, Questions and Answers at 2 (Aug. 22, 1984), *reprinted in* Daily News Rec., Aug. 23, 1984, at 11, col. 1.

109. *See* 50 Fed. Reg. 8724-25 (to be codified at 19 C.F.R. § 12.130(f)).

110. The form of the appropriate documentation is set forth at 50 Fed. Reg. 8725.

111. *Compare Cardinal Glove*, 4 Ct. Int'l Trade at 44 with 50 Fed. Reg. 8724 (to be codified at 19 C.F.R. § 12.130(b)).

112. *See infra* notes 113-24 and accompanying text.

113. *Cardinal Glove*, 4 Ct. Int'l Trade at 43-44; *see supra* notes 72-73 and accompanying text.

114. 50 Fed. Reg. 8724 (to be codified at 19 C.F.R. 12.130(b)); *see supra* notes 77-78 and accompanying text.

tion" test suggested in Custom Service Decision 80-10.¹¹⁵ Under that "substantial transformation" test, to change the country of origin of merchandise, there must simply be a substantial manufacturing operation which results in a new and different article.¹¹⁶ Now, in determining whether a substantial manufacturing operation has occurred, the Customs Service will compare the article before and after manufacturing.¹¹⁷ The focus has shifted from the nature of the product to the nature of production. This type of fact-specific comparison may not, however, lend itself to uniform application.¹¹⁸ For example, labor costs and processing methods differ from country to country,¹¹⁹ and therefore, the same processing may be "substantial" in a high cost country, but insubstantial in another country where costs are low. Although the Customs Service and the courts have generally examined the time,¹²⁰ skill,¹²¹ and cost¹²² involved in a manufacturing operation in the context of a tariff issue, their analysis has depended upon whether the transformation could be considered to have resulted in an article with a different name, character, or use.¹²³

115. C.S.D. 80-10, 14 Cust. B. & Dec. 740 (1981); see *supra* notes 77-78 and accompanying text.

116. C.S.D. 80-10, 14 Cust. B. & Dec. at 742. In the August 3, 1984 notice of the interim regulations, the Customs Service distinguished its administrative decision, Custom Service Decision 80-10, which sets forth a prior "substantial transformation" standard. 49 Fed. Reg. at 31,249. Customs argues that its decision was based upon an inadequate record and "poorly developed evidentiary facts." *Id.*

117. See *supra* notes 103-07 and accompanying text.

118. See *Belcrest Linens v. United States*, 741 F.2d 1368 (Fed. Cir. 1984). In that case, the process of cutting fabric which had been previously marked with cutting lines, sewing, and hemming was held to significantly cause a change in character and identity so as to meet a substantial transformation test. *Id.* at 1374. The Customs Service felt that "[i]n determining the country of origin of pre-marked fabric that is further processed in one or more countries, Customs will be guided by the facts in each particular case" 50 Fed. Reg. at 8714.

119. See generally INTERNATIONAL MARKETING DATA AND STATISTICS 1984 (1984) (compiling comparative international statistics of employment and economic costs).

120. See, e.g., *Lee Enterprises, Inc. v. United States*, 84 Cust. Ct. 208, 211 (1980).

121. See, e.g., *Uniroyal, Inc. v. United States*, 542 F. Supp. 1026, 1029-30 (Ct. Int'l Trade 1982) *aff'd per curiam*, 702 F.2d 1022 (Fed. Cir. 1983); *Amity Fabrics Co. v. United States*, 43 Cust. Ct. 64, 68 (1954); *Rolland Freres, Inc. v. United States*, 23 C.C.P.A. 81, 88-89 (1935).

122. See, e.g., *Texas Instruments, Inc. v. United States*, 681 F.2d 778, 784 (Ct. Cust. Pat. App. 1982).

123. See, e.g., *Uniroyal*, 542 F. Supp. at 1029; *Rolland Freres*, 23 C.C.P.A. at 87.

The regulations represent a departure from precedent¹²⁴ and could not, therefore, have been contemplated or foreseen by the parties to the MFA and the various bilateral trade agreements.

III. THE CONFLICT BETWEEN THE REGULATIONS AND THE MULTIFIBER ARRANGEMENT

An international agreement is essentially a contract between nations. Each party agrees to be bound by the terms of the agreement.¹²⁵ The principal goal of the MFA is to foster greater international cooperation and to reduce restrictions in textile trade.¹²⁶ However, the implementation of the new textile trade regulations by the United States violates both the spirit and the letter of the MFA.¹²⁷ In particular, the violations of articles 3, 5, and 8 of the MFA upset the balance of rights and obligations due all participating nations.¹²⁸

Article 3 provides that no new restrictions on trade in textiles shall be introduced by a participating country, unless such action is justified by a finding of market disruption prior to the imposition of the restrictions.¹²⁹ Generally, the MFA defines market disruption as an imminent or substantial increase in the number of particular products imported from particular sources.¹³⁰ The new regulations place restrictions on the importation of textiles and textile products not warranted by such imminent market disruptions.¹³¹ The regulations, therefore,

124. See *supra* notes 113-24 and accompanying text. The Customs Service cannot disregard judicial precedent. See *FTC v. Colgate-Palmolive, Co.*, 380 U.S. 374, 385 (1965). The Supreme Court held that while an administrative agency's interpretive judgment is to be given great weight, final review remains with the court. *Id.*

125. See Vienna Convention on the Law of Treaties, U.N. Doc. A/CONF. 39/27, art. 26 (1969). "Every treaty in force is binding upon the parties to it and must be performed by them in good faith." *Id.*

126. MFA, *supra* note 8, art. 1(2).

127. See *supra* notes 64-65 and accompanying text. Consequently, the implementation of the new country of origin rules contradicts the bilateral trade agreements to which the United States is a party that incorporate the MFA as the basic framework for international trade in textiles. *Id.*

128. See *supra* notes 38-39 and accompanying text.

129. MFA, *supra* note 8, arts. 3(1), 3(3).

130. *Id.* annex A, para. II(i); see *supra* note 42 and accompanying text.

131. MFA, *supra* note 8, annex A; see *supra* notes 42-46 and accompanying text. Unilateral action by an importing country is allowed under the MFA after a finding of a market disruption. MFA, *supra* note 8, art. 3. However, the definition of a market disruption is limited to actual damage or threat of an immediate increase in imported

constitute a nontariff barrier to trade, in violation of article 3.¹³²

The MFA attempts to reduce barriers to trade and to limit unilateral protectionist actions that might have a disruptive effect on individual markets in both importing and exporting countries.¹³³ Under article 5 of the MFA, therefore, participating countries agree to restrict imports of textiles and textile products in a "flexible and equitable manner."¹³⁴ Participating countries also agree to establish quotas and tariff classifications consistent with "normal commercial practices."¹³⁵ The new textile regulations constitute a dramatic change¹³⁶ from the *Cardinal Glove* country of exportation standard.¹³⁷ This change frustrates the implementation of negotiated textile agreements by denying entry of textiles into the United States which would have been allowed under the old quota rules.¹³⁸ This action further frustrates the aims of article 5 and contravenes the intent of international agreements.¹³⁹

The United States as a party to the MFA reiterated its understanding that any serious problems of international trade should be resolved through consultation and negotiation with other signatory nations.¹⁴⁰ The United States also agreed in article 8 to refrain from taking any unilateral measures and to avoid circumvention of the MFA without exhausting all the re-

products or the import of substantially lower priced goods, comparable to the domestic economy. *Id.* annex A. Compare *id.* with *supra* note 84.

132. MFA, *supra* note 8, art. 3. Nontariff barriers to trade are defined as "barriers to *free trade* that take forms other than *tariffs*, such as *quotas*," or import regulations. M. TODARO, *supra* note 24, at 541.

133. MFA, *supra* note 8, art. 1(4). This article provides that "actions taken under this Arrangement should be accompanied by the pursuit of appropriate economic and social policies, in a manner consistent with national laws and systems . . ." *Id.*; see *supra* notes 39-41 and accompanying text.

134. MFA, *supra* note 8, art. 5.

135. *Id.*

136. See *supra* notes 112-24 and accompanying text.

137. See *supra* notes 72-73 and accompanying text.

138. See *supra* notes 108-24 and accompanying text.

139. Statement by Sergio Delgado of Mexico on Behalf of Developing Countries Exporters of Textile and Clothing, to the GATT Textile Committee, para. 11 (Sept. 4, 1984).

140. See Protocol Extending the Arrangement Regarding International Trade in Textiles, Dec. 22, 1982, — U.S.T. —, T.I.A.S. No. 10,323, reprinted in [Oct.-Mar.] U.S. IMPORT WEEKLY (BNA) No. 109, at 323 (Jan. 6, 1982) [hereinafter cited as 1981 Protocol].

lief measures provided therein.¹⁴¹ If a participating nation believes that the MFA is being circumvented or frustrated, and no appropriate action is being taken by other nations, that nation is obligated to seek a prompt and mutually satisfactory solution through the MFA's supervisory organs or diplomatic channels.¹⁴² If no solution is thereby reached, unilateral action is still precluded, and the matter must be referred to the Textile Surveillance Body.¹⁴³

The unilateral imposition by the United States of the new regulations, even in light of legitimate concerns about the circumvention of its bilateral agreements,¹⁴⁴ is contrary to the MFA's international consultation requirements.¹⁴⁵ The United States has not consulted with the Textile Surveillance Body regarding its allegations of circumvention and frustration.¹⁴⁶ In addition, the United States has ignored the most basic objectives of the MFA and has acted unilaterally in imposing nontariff import restrictions.

IV. ANALYSIS AND EFFECTS

The major impact of the new regulations is on the wide-

141. See MFA, *supra* note 8, arts. 8(1)-(2); 1981 Protocol, *supra* note 140, para. 5.

142. See MFA, *supra* note 8, arts. 8(1)-(2). Article 8(3) of the MFA allows a participating nation to take unilateral action in response to "frustration" of the agreement. However, "frustration" refers specifically to "exports of similar goods [to goods from countries covered by the MFA] of any country not party to this Arrangement which are causing, or actually threatening, market disruption." *Id.* art. 8(3). The new regulations do not address such activity and are not within this unilateral action exception. The 1981 Protocol allows parties to the MFA to negotiate "mutually acceptable solutions" to trade disputes. 1981 Protocol, *supra* note 140, paras. 6, 9-11, 14; see *supra* notes 52-55 and accompanying text.

143. MFA, *supra* note 8, art. 8(2). The language of the MFA is clear:

The participating countries agree to collaborate with a view to taking appropriate administrative action to avoid such circumvention. Should any participating country believe that the Arrangement is being circumvented and that no appropriate administrative measures are being applied to avoid such circumvention, that country should consult with the exporting country of origin and with other countries involved in the circumvention with a view to seeking promptly a mutually satisfactory solution. If such a solution is not reached the matter shall be referred to the Textile Surveillance Body.

Id.

144. See *supra* note 84 and accompanying text.

145. MFA, *supra* note 8, art. 8(2).

146. See *GATT Textiles Board Rules Against U.S. in Hong Kong Complaint about New Rules*, [July-Dec.] INT'L TRADE REP. (BNA) No. 24, at 754 (Dec. 19, 1984). The TSB criticized the United States for introducing the regulations without proper notice. *Id.*

spread practice of multicountry production of textiles and textile products.¹⁴⁷ Retail firms and importers in the United States have regularly procured textile and apparel articles that are assembled and finished in one country from components produced in another.¹⁴⁸ The disruption caused by the new regulations on the conduct of international trade may be dramatic.¹⁴⁹

The new regulations have had an immediate impact on domestic retailers.¹⁵⁰ The retail industry suffered a severe loss of many textile and apparel orders for the holiday 1984 selling season, as previously eligible import orders were subject to quota restrictions.¹⁵¹ The adverse effect on retail merchandise could be as high as U.S.\$1.6 billion in permanently lost sales.¹⁵²

Protectionism also has international effects.¹⁵³ Developing countries have a limited ability to shift their resources or to diversify their investments into other competitive markets.¹⁵⁴ Political conflicts between the United States and its trading partners have arisen over the implementation of the country of origin regulations.¹⁵⁵ For example, the Government of Hong Kong has protested that more than fifteen percent of its total annual apparel trade with the United States, valued at U.S.\$280 million, will be affected by the regulations.¹⁵⁶ Textile experts note that the colony's sweater industry will suffer

147. NAT'L RETAIL MERCHANTS ASS'N, *EFFECT OF COUNTRY OF ORIGIN REGULATIONS 1-4* (Aug. 17, 1984) [hereinafter cited as *EFFECT OF REGULATIONS*].

148. See *Big Stores, Importers File Suit*, *Daily News Rec.*, Aug. 30, 1984, at 23, col. 5.

149. *EFFECT OF REGULATIONS*, *supra* note 147, at 2.

150. *Id.*

151. *Id.*

152. *Id.*; see *Mast Industries*, No. 84-111, slip op. at 9.

153. For a discussion on the effects of protectionism on international trade, see generally *TARIFFS, QUOTAS & TRADE: THE POLITICS OF PROTECTIONISM* (Inst. for Contemp. Stud. ed. 1979). For an economic analysis of the role of tariffs, quotas, and other forms of protectionism, see B. SÖDERSTEN, *INTERNATIONAL ECONOMICS* 169-213 (2d ed. 1980).

154. See M. TODARO, *supra* note 24, at 353. The implication is that "the internal processes of adjustment and resource reallocation necessary to capitalize on changing world economic conditions are much more difficult for the less diversified economies of the Third World" than for developed countries. *Id.*

155. Ehrlich, *Hong Kong Group to Protest U.S. Origin Regs*, *Daily News Rec.*, Aug. 10, 1984, at 8, col. 1.

156. *Id.*

the most.¹⁵⁷ At least eighty percent of Hong Kong's sweater exports to the United States are assembled from components made in China.¹⁵⁸ In 1983, Hong Kong shipped nearly 55 million sweaters (about half of its total production) to the United States.¹⁵⁹

Correlative losses in producing countries will be equally significant. The People's Republic of China, for example, has estimated that U.S.\$100 million in semifinished Chinese textile products shipped to Hong Kong for finishing and reexported to the United States will now be counted against China's export quota.¹⁶⁰ Chinese officials were particularly incensed that the Reagan administration gave Beijing no advance notice of the new regulations prior to publication.¹⁶¹ This omission is contrary to Sino-American textile agreements, which call for "consultation" if provisions are to be altered.¹⁶² Also, it is likely that importers to the United States will not be able to secure appropriate documentation from some countries that manufacture component parts. China has formally notified the United States that it will not issue export licenses for materials and components sent to other countries for further operations.¹⁶³

The new regulations portend a dramatic shift in United States policy toward international trade. Since 1945, the

157. *Id.*

158. *Id.*

159. *Id.*

160. Ehrlich, *Hong Kong Knitwear Executive: US Delaying Origin Regs to '85*, Daily News Rec., Aug. 29, 1984, at 1, col. 3.

161. Wightman, *China Files Official US Reg Protest*, Daily News Rec. Aug. 16, 1984, at 9, col. 1.

162. *See* China Treaty, *supra* note 2, para. 12. "The Government of the United States of America and the Government of the People's Republic of China agree to consult on any question arising in the implementation of the Agreement." *Id.*

163. Letter from Zhang Wenjin, Ambassador of the People's Republic of China, to the Honorable William E. Brock, United States Trade Representative (Aug. 15, 1984). The Ambassador wrote that:

[The new regulations] completely change the rules and the basis for quotas in existence and relied upon by the People's Republic of China at the time it entered into its bilateral agreement on textile products with the United States. As such, adoption of these proposals would constitute a clear violation of the bilateral agreement. Hence, we cannot agree to charge materials and components sent to third countries or areas for further manufacture to our quotas in the way it is proposed in the regulations and we will not issue export licenses under our quotas for the same.

Id.

United States has been the leader in the establishment of a liberal international economic order.¹⁶⁴ The postwar efforts of United States decision makers to lower trade barriers, to eliminate trade discrimination, and to establish currency convertability, resulted in the creation of such instruments as the World Bank,¹⁶⁵ the International Monetary Fund,¹⁶⁶ and the General Agreement on Tariffs and Trade.¹⁶⁷ The United States' decentralized political system has been characterized by a relatively protectionist Congress and a free trade oriented Executive.¹⁶⁸ American foreign economic policy throughout the 1950's promoted a liberal economic system.¹⁶⁹ As liberal trade exposed domestic producers to international competition, increasing domestic protectionist sentiment¹⁷⁰ began to erode the successes that had culminated in the Kennedy Round of multilateral trade negotiations and the Trade Expansion Act of 1962.¹⁷¹ In recent years, the United States textile

164. Krasner, *United States Commercial and Monetary Policy: Unravelling the Paradox of External Strength and Internal Weakness*, in *BETWEEN POWER AND PLENTY: FOREIGN ECONOMIC POLICIES OF ADVANCED INDUSTRIAL STATES* 51, 52 (P. Katzenstein ed. 1978). The fundamental object of post-war United States decision makers was to create a liberal economic regime. *Id.* "This meant that barriers to the [international] movement of goods, services, capital, and technology would be minimized." *Id.*

165. The International Bank for Reconstruction and Development, as the World Bank is officially known, is an international financial institution, affiliated with the United Nations. Its main objective is to promote development funds to less developed nations in the form of loans and technical assistance. For a comprehensive study of the World Bank, see generally E. MASON & R. ASHER, *THE WORLD BANK SINCE BRETTON WOODS* (1973); C. PAYER, *THE WORLD BANK: A CRITICAL ANALYSIS* 15-52 (1982).

166. The International Monetary Fund is an autonomous financial institution that originated from the Bretton Woods Conference of 1944. Its main purpose is to regulate the international monetary exchange system and to control fluctuations in exchange rates in world currencies. See *INTERNATIONAL MONETARY FUND, ANNUAL REPORT 1984*, 1-32 (1984); *THE IMF AND STABILIZATION: DEVELOPING COUNTRY EXPERIENCES* 1-18 (T. Killick ed. 1984).

167. GATT *supra* note 9; see Krasner, *supra* note 164, at 72-73. For a comprehensive study of GATT, see J. JACKSON, *WORLD TRADE AND THE LAW OF GATT* (1969).

168. Katzenstein, *Conclusion: Domestic Structures and Strategies of Foreign Economic Policy*, in *BETWEEN POWER AND PLENTY: FOREIGN ECONOMIC POLICIES OF ADVANCED INDUSTRIAL STATES* 295, 311-12 (P. Katzenstein ed. 1978).

169. Krasner, *supra* note 164, at 77.

170. *Id.* at 79.

171. 19 U.S.C. § 1801 (1976). The Kennedy Administration introduced and passed the Trade Expansion Act of 1962, which was aimed at vast reciprocal trade barrier reductions. Subsequently, negotiations with the European Economic Community resulted in large tariff reductions by developed countries. B. SÖDERSTEN,

and apparel industries have coalesced into a formidable and influential lobby.¹⁷² It was widely believed in Washington that the Reagan administration announced the new country of origin rules in an attempt to win election year support from textile and apparel industry leaders and southern textile state voters.¹⁷³ Since the early 1960's, textile manufacturing interest groups have argued for increased protection against low-cost imports.¹⁷⁴ While protectionist policy has preserved domestic jobs, avoided plant closings, and maintained a competitive industry, consumers are forced to pay higher prices for textiles and apparel, and the economy is allocating labor and capital into an industry in which the United States may no longer have a comparative advantage.¹⁷⁵

CONCLUSION

New United States Customs Service regulations determine the country of origin of textiles and textile products for quota purposes. In particular, they define the country of origin for goods that undergo a manufacturing or processing operation in more than one country.¹⁷⁶ The new regulations, however, differ from the prior country of exportation standard articulated in *Cardinal Glove Co. v. United States*.¹⁷⁷ Generally, textile and textile products will be the product of the country of initial production or manufacture, unless the product undergoes substantial transformation. Substantial transformation occurs if a textile or textile product is transformed by means of a substantial manufacturing or processing operation into a new and different article of commerce.¹⁷⁸

The country of origin regulations violate various provisions of the Multifiber Arrangement.¹⁷⁹ The United States'

supra note 153, at 240. The reciprocal reductions concentrated on manufactured goods that were of interest to developed countries and on raw materials. *Id.*

172. Aggarwal & Haggard, *supra* note 19, at 249-50; *see supra* notes 31-32 and accompanying text.

173. Hosenball, *AAMA Asks Delay in Rules of Origin*, Daily News Rec., Aug. 23, 1984, at 1, col. 4.

174. Aggarwal & Haggard, *supra* note 19, at 250.

175. *Id.* at 308; *see* B. SÖDERSTERN, *supra* note 153, at 184-85.

176. *See supra* notes 98-109 and accompanying text.

177. 4 Ct. Int'l Trade 41 (1982); *see supra* notes 112-24 and accompanying text.

178. *See supra* notes 100-07 and accompanying text.

179. MFA, *supra* note 8; *see supra* notes 125-46 and accompanying text.

unilateral imposition of the regulations is contrary to provisions that provide for international consultation and cooperation in world textile trade.¹⁸⁰ This action is not consistent with the United States' history as a leader of liberal world trade. This inconsistency may be explained by domestic political pressure on the Reagan Administration, in an election year, from textile and apparel groups.¹⁸¹ Nonetheless, the violation by the United States of the MFA and its bilateral textile treaty obligations is a serious obstruction to the orderly conduct of international trade.

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180. *See supra* notes 140-46, 161-62 and accompanying text.

181. *See supra* notes 173-75 and accompanying text.