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Nissho Iwai American Corp. v. United States: Customs Appraisement and Middleman Pricing Under Section 402 of the Tariff Act of 1930

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Nissho Iwai American Corp. v. United States: Customs Appraisal and Middleman Pricing Under Section 402 of the Tariff Act of 1930

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Abstract

This Comment argues that the Federal Circuit correctly rejected Customs' "most direct cause" test. Part I explains the transaction value of the imported merchandise valuation method and traces its legislative history. In addition, Part I reviews Customs and prior judicial treatment of middleman import transactions. Part II describes the Federal Circuit's decision in *Nissho Iwai*. Part III argues that Customs' "most direct cause" test is contrary to judicial precedent and unsupported by the legislative history of Section 402. Part III also discusses the implications and limitations of *Nissho Iwai* for American importers. This Comment concludes that *Nissho Iwai* represents a significant decision in customs valuation law and U.S. importers that purchase merchandise from non-U.S. middlemen will benefit by paying less duties.

NISSHO IWAI AMERICAN CORP. v. UNITED STATES:
CUSTOMS APPRAISEMENT AND MIDDLEMAN
PRICING UNDER SECTION 402 OF THE
TARIFF ACT OF 1930

INTRODUCTION

U.S. customs law¹ requires importers to pay customs duties on imported merchandise unless an exception exists for duty-free entry.² Since most customs duties are calculated as a percentage of the appraised value of the imported merchandise,³ appraisal plays an important role in determining the amount of duty an importer pays.⁴ U.S. customs law delegates the responsi-

1. RUTH F. STURM, CUSTOMS LAW & ADMINISTRATION at 41 (3d ed. 1993). Customs Law is the field of administrative law concerned with government procedures and regulations affecting the importation and exportation of merchandise into and from the United States. *Id.*

2. 19 U.S.C. § 1202 (1988) (general notes 1, 3, 4). The current version of 19 U.S.C. § 1202 is located in U.S. Int'l Trade Comm'n, Harmonized Tariff Schedule of the United States, USITC Pub. No. 2449 (1993) [hereinafter HTSUS]. The HTSUS lists those goods subject to duty and those goods entitled to duty-free entry. *Id.*

To determine whether the Customs law imposes duty on imported merchandise, or otherwise restricts its importation, the importer must consult the Harmonized Tariff Schedule of the United States to classify the merchandise. Peggy Chaplin, *An Introduction to the Harmonized System*, 12 N.C. J. INT'L L. & COM. REG. 417 (1987) [hereinafter *Harmonized System*]. Classifying imported merchandise involves selecting the item numbers with accompanying language descriptions which are most appropriate and specific to the imported merchandise. *Id.* Importers and Customs often disagree on the proper classification of imported merchandise. *Id.* Once the proper classification is determined, however, the selected item number provides the amount of duty imposed on the entry. *Id.*

An entry consists of filing the forms and documents required to permit customs officials to determine whether specific merchandise is admissible and whether it may be released from customs custody and an entry also includes the filing of such other documentation necessary to enable customs officers to assess duties, collect accurate statistics, and determine whether requirements of laws other than customs laws are met. 19 U.S.C. § 1484 (1988); 19 C.F.R. § 142.3 (1992). See 1 BRUCE E. CLUBB, UNITED STATES FOREIGN TRADE LAW 375-419 (1991) (providing example of standard import transaction and regulations that affect import transactions).

3. STURM, *supra* note 1, § 1.1, at 1; DAVID SERKO, IMPORT PRACTICE: CUSTOMS AND INTERNATIONAL TRADE LAW 107 (2d ed. 1991) [hereinafter SERKO]; SAUL L. SHERMAN AND HINRICH GLASHOFF, CUSTOMS VALUATION: COMMENTARY ON THE GATT CUSTOMS VALUATION CODE 51 (1988) [hereinafter COMMENTARY]. There are three types of customs duties: *ad valorem*, specific, and combination. STURM, *supra* note 1, § 1.1. *Ad valorem* duties are calculated as a percentage of the value of the dutiable merchandise. *Id.* Specific duties are calculated on the basis of quantity, *i.e.*, U.S.\$x per unit. *Id.* Combination duties are calculated using both *ad valorem* and specific rates, *i.e.*, U.S.\$x per unit plus a percent of the dutiable merchandise. *Id.*

4. SERKO, *supra* note 3, at 107.

bility of appraising the value of imported merchandise to the U.S. Customs Service ("Customs").⁵

Section 402 of the Tariff Act of 1930 ("Section 402"), as amended by the Trade Agreements Act of 1979, provides the statutory basis for appraising of imported merchandise.⁶ Under Section 402, the transaction value of the imported merchandise is the primary⁷ method of calculating appraised value.⁸ Section

5. 19 U.S.C. § 1500 (1988); STURM, *supra* note 1, §§ 4.2, 6.1, 6.2. The United States Customs Service is an agency of the Department of the Treasury charged with the responsibility of assessing and collecting duties on imported merchandise, and enforcing the customs laws and related statutes. *Id.* Customs utilizes a regional management system, where the United States customs territory is divided into seven regions. STURM, *supra* note 1, § 4.1, at 68. Each region is subdivided into districts, which, in turn, are subdivided into ports of entry and subports. *Id.* Each district is managed by a district director. *Id.*; see 19 C.F.R. § 101.3 (1992) (describing Customs regions, districts, and ports).

6. 19 U.S.C. § 1401a (1988). The Trade Agreements Act of 1979 ("TAA") implemented a number of changes to United States trade law which were necessary to implement the trade agreements negotiated by the United States in the Tokyo Round of Multilateral Trade Negotiations of the General Agreement on Tariffs and Trade ("GATT"), including adoption of the new customs valuation code. H.R. DOC. NO. 153, 96th Cong., 1st Sess., pt. 2, at 389 (1979) [hereinafter STATEMENT OF ADMINISTRATIVE ACTION]. The GATT is an international agreement subscribed to by almost all nations of the free world. General Agreement on Tariffs and Trade, opened for signature, Oct. 30, 1947, 61 Stat. (pts. 5 & 6) A3, 55 U.N.T.S. 187 (1947) [hereinafter GATT]; EUGENE T. ROSSIDES, U.S. IMPORT TRADE REGULATIONS 401, 416-17 (1986). The GATT establishes rules for the conduct of international trade. *Id.*; ALAN C. SWAN & JOHN F. MURPHY, CASES AND MATERIALS ON THE REGULATION OF INTERNATIONAL BUSINESS AND ECONOMIC RELATIONS (1991).

7. 19 U.S.C. § 1401a(a). Section 402 provides that Customs shall appraise imported merchandise using the transaction value of the imported merchandise, unless the transaction value of the imported merchandise cannot be determined. *Id.* § 1401a(a)(1)(A). In addition, Customs may use the transaction value of the imported merchandise only if certain conditions are met. *Id.* § 1401a(b)(2). First, there must be a sale for exportation to the United States. *Id.* § 1401a(b)(1); see *Orbisphere Corp. v. United States*, 726 F. Supp. 1344 (Ct. Int'l Trade 1989) (holding transaction value of imported merchandise unavailable where evidence demonstrated sales of products were concluded in United States by U.S. company for sale to U.S. customers). The situs of the sale is, however, irrelevant to determining whether the transaction is a sale for exportation to the United States. General Notice, 26 Cust. B. & Dec., No. 8, at 13 (Jan. 27, 1992). Second, there must be sufficient information to establish the accuracy of the invoice price. 19 U.S.C. § 1401a(b)(1). "Sufficient information" means information that establishes the accuracy of any adjustment. *Id.* § 1401a(h)(5). The term "adjustment" refers to the additions and deductions to the price paid or payable for the imported merchandise that are described in § 1401a(b)(1), (3). Third, the transaction value of the imported merchandise may be used to appraise merchandise imported in a transaction between "related parties" only if the parties' relationship does not influence the price, or if the price closely approximates certain test values of identical or similar merchandise. *Id.* § 1401a(b)(2)(B). Related parties are defined by statute as:

402 states that the transaction value of the imported merchandise is equivalent to the price actually paid or payable for the

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- (A) Members of the same family, including brothers and sisters (whether by whole or half blood), spouse, ancestors, and lineal descendants.
 - (B) Any officer or director of an organization and such organization.
 - (C) An officer or director of an organization and an officer or director of another organization, if each such individual is also an officer or director in the other organization.
 - (D) Partners.
 - (E) Employer and employee.
 - (F) Any person directly or indirectly owning, controlling, or holding with power to vote, 5 percent or more of the outstanding voting stock or shares of any organization and such organization.
 - (G) Two or more persons directly or indirectly controlling, controlled by, or under common control with, any person.

Id. § 1401a(g). Related parties should also note that the transaction value of the imported merchandise limits the related U.S. importer's tax deduction for costs of goods sold. 26 U.S.C. § 1059A.

If there are restrictions on the disposition or use of the merchandise, if the sale is subject to any condition for which a value cannot be determined, or if an adjustment for benefits that accrue to the seller cannot be made, then Customs must use an alternative valuation method. *Id.* § 1401a(b)(2)(A)(i)-(iii).

If the transaction value of the imported merchandise cannot be determined, other possible statutory bases of valuation are utilized in the following order of preference: the transaction value of identical merchandise, the transaction value of similar merchandise, the deductive value, and the computed value. *Id.* § 1401a(a)(1)(B)-(E). If computed value cannot be determined, appraised value may be determined from one of the other methods of valuation by making reasonable adjustments. *Id.* § 1401a(a)(1)(F).

Appraisal under the transaction value of identical or similar merchandise methods is similar to appraisement under the transaction value of the imported merchandise. *SERKO, supra* note 3, at 125. The principal difference is that the transaction value of identical or similar merchandise looks to the price paid or payable for identical or similar merchandise exported to the United States at about the same time that the merchandise being appraised is exported to the United States. 19 U.S.C. § 1401a(c)(1); *SERKO, supra* note 3, at 126; *See* 19 U.S.C. §§ 1401a(h)(2) and 1401a(h)(4) (defining terms "identical" and "similar").

Appraisal under the deductive value method is calculated by using the price at which the merchandise being appraised, or identical or similar merchandise is sold in the United States and making certain deductions. 19 U.S.C. § 1401a(d); *SERKO, supra* note 3, at 127-31.

Appraisal under the computed value method is calculated as the sum of (1) materials, fabrication, and other processing used in the production of the imported merchandise, (2) profits and general expenses, (3) assists not included in other items, and (4) packing costs. 19 U.S.C. § 1401a(e); *SERKO, supra* note 3, at 131-32.

Finally, if Customs cannot appraise the imported merchandise using any of the above methods, it may appraise the imported merchandise using a method derived from one of the above valuation methods. 19 U.S.C. § 1401a(f); *SERKO, supra* note 3, at 132-33.

8. 19 U.S.C. § 1401a.

merchandise when sold for exportation to the United States.⁹

Use of the transaction value of the imported merchandise to appraise imported merchandise is complicated by the fact that two separate transactions may qualify as sales for exportation to the United States.¹⁰ For example, a Japanese middleman¹¹ may contract with a Japanese manufacturer for the production of merchandise ordered by a U.S. importer. The transaction between the Japanese middleman and the Japanese manufacturer (the "first tier transaction") qualifies as a sale for exportation to the United States if the Japanese manufacturer sells merchandise to the Japanese middleman for ultimate export to the United States.¹² Additionally, the transaction between the Japanese middleman and the U.S. importer (the "second tier transaction") qualifies as a sale for exportation to the United States since the Japanese middleman sells and exports the merchandise to the U.S. importer.¹³ When two sales form

9. 19 U.S.C. § 1401a(b)(1). The precise definition of "transaction value of imported merchandise" is:

[T]he price actually paid or payable for the merchandise when sold for exportation to the United States, plus amounts equal to —

(A) the packing costs incurred by the buyer with respect to the imported merchandise;

(B) any selling commission incurred by the buyer with respect to the imported merchandise;

(C) the value, apportioned as appropriate, of any assist;

(D) any royalty or license fee related to the imported merchandise that the buyer is required to pay, directly or indirectly, as a condition of the sale of the imported merchandise for exportation to the United States; and

(E) the proceeds of any subsequent resale, disposal, or use of the imported merchandise that accrue, directly or indirectly, to the seller.

Id. The term "price paid or payable" is defined as:

(A) . . . the total payment (whether direct or indirect, and exclusive of any costs, charges, or expenses incurred for transportation, insurance, and related services incident to the international shipment of the merchandise from the country of exportation to the place of importation in the United States) made, or to be made, for imported merchandise by the buyer to, or for the benefit of, the seller.

Id. § 1401a(b)(4)(A).

10. STURM, *supra* note 1, § 47.2, at 12-14.

11. *Distribu-Dor, Inc. v. Karadanis*, 11 Cal. App. 3d 463, 90 Cal. Rptr. 231, 235 (1970) (defining middleman as one who buys at one price from manufacturer for resale at higher price); BLACK'S LAW DICTIONARY 992 (6th ed. 1990). As used in this Comment, the term "middleman" refers to one who buys at one price from a manufacturer for resale at a higher price. *Id.*

12. 19 U.S.C. § 1401a.

13. 19 U.S.C. § 1401a.

the basis of the transaction value of the imported merchandise, as in the case of transactions involving middlemen, Section 402 fails to provide guidance as to which sale sets the transaction value.¹⁴

Prior to the recent decision by the Court of Appeals for the Federal Circuit¹⁵ in *Nissho Iwai American Corp. v. United States*,¹⁶ importers and Customs disagreed on whether the first tier transaction may form the basis of the transaction value of imported merchandise.¹⁷ Customs ruled, based on the legislative history of Section 402, that the first tier transaction may form the basis

14. Saul L. Sherman, *Reflections on the New Customs Valuation Code*, 12 *LAW & POL'Y INT'L BUS.* 119, 144 (1980) [hereinafter *Reflections*].

15. STURM, *supra* note 1, § 34.2, at 3. The Federal Courts Improvement Act of 1982 created the Court of Appeals for the Federal Circuit, which replaced the Court of Customs and Patent Appeals and the Court of Claims. Federal Courts Improvement Act, Pub. L. 97-164, 96 Stat. 25 (codified as amended in scattered sections of 28 U.S.C.); STURM, *supra* note 1 § 34.2, at 3. Decisions rendered by the Court of Customs and Patent Appeals are precedents for cases before the Court of Appeals for the Federal Circuit. *South Corporation v. United States*, 690 F.2d 1368 (Fed. Cir. 1982). In *South Corporation* the Federal Circuit announced:

The adoption of precedents here announced continues the stability in those areas of law previously within the jurisdiction of our predecessor courts. That jurisdiction was established in great part by judges now members of this court. The public and the bar have presumably structured their legal affairs in accordance with that jurisprudence. To abandon it at this stage would be to cast the court, the public, and the bar adrift on a sea of uncertainty. . . .

As a court of nationwide geographic jurisdiction, created and chartered with the hope and intent that stability and uniformity would be achieved in all fields of law within its substantive jurisdiction, we begin by adopting as a basic foundation the jurisprudence of the two national courts which served not only as our predecessors, but as outstanding contributors to the administration of justice for a combined total of 199 years, the Court of Claims and the Court of Customs and Patent Appeals.

Id. at 1371.

The Court of Appeals for the Federal Circuit has exclusive jurisdiction of appeals from final decisions of the Court of International Trade. 28 U.S.C. § 1295(a)(5) (1988); STURM, *supra* note 1, § 34.4, at 7. In addition, the Court of Appeals for the Federal Circuit has jurisdiction over various interlocutory appeals from the Court of International Trade and appeals from decisions of the International Trade Commission relating to unfair trade practices in the import trade under 19 U.S.C. § 1337. 19 U.S.C. § 1337(c) (1988), 28 U.S.C. § 1292(c)(1), (d)(1)-(3) (1988); 28 U.S.C. § 1295(a)(5)-(6) (1988); STURM, *supra* note 1 § 34.4, at 9-14.

16. 982 F.2d 505 (Fed. Cir. 1992).

17. *E.C. McAfee Co. v. United States*, 842 F.2d 314 (Fed. Cir. 1988); *Brosterhous, Coleman & Co. A/C Lurgi Chemie und Hüttentechnik GmbH v. United States*, 737 F. Supp. 1197 (Ct. Int'l Trade 1990); C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); C.S.D. 81-52, 15 Cust. Bull. 880, *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

of the transaction value of the imported merchandise only if the first tier transaction "most directly causes" the merchandise to be exported to the United States.¹⁸ Customs rulings¹⁹ consistently held that the second tier transaction, rather than the first tier transaction, was the most direct cause of the exportation of the imported merchandise to the United States.²⁰ Appraising imports on the basis of the second tier transaction resulted in the U.S. importer paying higher duties because the second tier transaction included the higher middleman price.²¹ In *Nissho Iwai*, however, the Federal Circuit rejected Customs' use of a

18. C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); C.S.D. 81-52, 15 Cust. Bull. 880, *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

19. 19 C.F.R. § 177 (1992). A ruling is a written statement issued by Customs that interprets and applies Customs and related laws to a particular set of facts. 19 C.F.R. § 177.1(d) (1992). See *SERKO*, *supra* note 3, at 613-42 (discussing administrative rulings by Customs).

Customs promulgated Part 177 of the Customs Regulations to enable an importer to determine the impact of the customs and related laws on an import transaction before the importer engages in the transaction. 19 C.F.R. § 177.1(a)(1) (1992); *SERKO*, *supra* note 3, at 613-14. To request a ruling on a prospective transaction, an importer must have a direct and demonstrable interest in the question or questions presented in the ruling request. 19 C.F.R. § 177.1(c) (1992). A request for a ruling should be in the form of a letter. *Id.* § 177.2(a). Each request for a ruling should contain a complete statement of all relevant facts relating to the transaction and a description of the transaction. *Id.* § 177.2(b).

Rulings issued under Part 177 represent the official position of Customs with respect to the particular transaction or issue described in the ruling and are binding on Customs unless they are modified or revoked. *Id.* § 177.9(a) (1992). Customs may modify or revoke any ruling found to be in error or not in accordance with the current views of Customs by giving notice to the person to whom the ruling was addressed and, if necessary, by publishing notice of the modification or revocation in the official Customs publication, the Customs Bulletin. *Id.* § 177.9(d).

For example, prior to importing Ferrari automobiles, a U.S. importer may write a letter to Customs describing the details of the proposed import transaction (i.e., the nature of the imported merchandise, how much the importer will pay for the merchandise, etc.) and ask Customs to determine the appraised value of the Ferraris and the correct tariff rate. Customs' response is binding with regard to the transaction described in the importer's letter to Customs. *Id.* § 177.9(a). Thus, a ruling enables the importer to determine the amount of duties that will have to be paid before the importer engages in the transaction.

20. C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); C.S.D. 81-52, 15 Cust. Bull. 880, *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

21. See *supra* note 11 (defining middleman as one who buys at one price and resells at higher price).

"most direct cause" test.²² The Federal Circuit ruled that where both transactions meet the requirements of Section 402,²³ the first tier transaction forms the basis for the transaction value of the imported merchandise.²⁴

This Comment argues that the Federal Circuit correctly rejected Customs' "most direct cause" test. Part I explains the transaction value of the imported merchandise valuation method and traces its legislative history. In addition, Part I reviews Customs and prior judicial treatment of middleman import transactions. Part II describes the Federal Circuit's decision in *Nissho Iwai*. Part III argues that Customs' "most direct cause" test is contrary to judicial precedent and unsupported by the legislative history of Section 402. Part III also discusses the implications and limitations of *Nissho Iwai* for American importers. This Comment concludes that *Nissho Iwai* represents a significant decision in customs valuation law and U.S. importers that purchase merchandise from non-U.S. middlemen will benefit by paying less duties.

I. THE TRANSACTION VALUE OF IMPORTED MERCHANDISE AND TREATMENT OF TRANSACTIONS INVOLVING MIDDLEMEN

Under Section 402, Customs primarily²⁵ uses the transaction value of the imported merchandise to appraise imported merchandise.²⁶ The Court of Appeals for the Federal Circuit and its predecessor, the Court of Customs and Patent Appeals, have ruled consistently that Customs must appraise imported merchandise based on a first tier transaction if that transaction meets the statutory requirements of Section 402.²⁷ Nonetheless, Customs has interpreted the transaction value of the imported merchandise as requiring transaction value to be based on the

22. *Nissho Iwai American Corp. v. United States*, 982 F.2d 505, 511 (Fed. Cir. 1992).

23. See *supra* note 7 (discussing statutory requirements of Section 402).

24. 982 F.2d 505 (Fed. Cir. 1992).

25. See *supra* note 7 (discussing alternative Customs valuation methods).

26. See *supra* notes 6-9 and accompanying text (discussing statutory basis for appraisal of merchandise).

27. *E.C. McAfee Co. v. United States*, 842 F.2d 314 (Fed. Cir. 1988); *United States v. Getz Bros. & Co.*, 55 C.C.P.A. 11 (1967); *R.J. Saunders & Co., Inc. v. United States*, 42 C.C.P.A. 55 (1954); *United States v. S.S. Kresge Co.*, 26 C.C.P.A. 349 (1939); see *supra* note 7 (discussing statutory requirements of Section 402).

transaction that "most directly causes" the merchandise to be exported to the United States.²⁸ In determining which transaction of a two-tiered transaction constitutes the "most direct cause" of exportation, Customs has consistently found that the second tier transaction "most directly causes" the merchandise to be exported to the United States.²⁹

A. *The Transaction Value of Imported Merchandise*

Section 402 provides that the primary³⁰ method of calculating appraised value is the transaction value of the imported merchandise.³¹ Section 402 defines the transaction value of imported merchandise as the price actually paid or payable for merchandise when sold for exportation to the United States.³² While the transaction value of the imported merchandise is based on the price paid for the merchandise, the transaction value of the imported merchandise is not always equivalent to the price shown on the commercial invoice.³³ Often, certain deductions and additions to the invoiced price are required to determine the transaction value of the imported merchandise.³⁴

28. C.S.D. 89-30, 23 Cust. Bull. 587 (1988); C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); *contra* C.S.D. 81-72, 15 Cust. Bull. 876 (1980), *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

29. C.S.D. 89-30, 23 Cust. Bull. 587 (1988); C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); *contra* C.S.D. 81-72, 15 Cust. Bull. 876 (1980), *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

30. *See supra* note 7 (discussing methods of appraising imported merchandise).

31. 19 U.S.C. § 1401a(b)(1); *see supra* note 7 (defining preferential order of basis for appraisement).

32. *See supra* note 9 (noting precise definition of transaction value of imported merchandise).

33. 19 U.S.C. § 1401a; *see* SERKO, *supra* note 3 at 109-25 (discussing transaction value of imported merchandise); STURM, *supra* note 1, § 47.2, at 5-28 (discussing transaction value of imported merchandise).

34. 19 U.S.C. § 1401a(b)(1), (3). Transaction value does not include costs incurred for transportation, insurance and related services that are incidental to the international and post-importation shipment of merchandise, or United States duties and taxes levied on imported merchandise. *Id.* § 1401a(b)(3-4). In addition, transaction value does not include reasonable charges for post-importation assembly or maintenance. *Id.*

Transaction value includes certain additions to the invoice price if not already included, such as packing charges, selling commissions, royalties, license fees, and assists. *Id.* § 1401a(b)(1). Transaction value also adds to the invoiced price various benefits that accrue to the seller, such as proceeds from post-importation resale, disposal or use of the merchandise. *Id.* § 1401a(b)(1)(E).

The following examples illustrate calculation of the transaction value of imported merchandise.³⁵ If a U.S. importer pays a foreign manufacturer U.S.\$10,000 in an arms length transaction for a shipment of meat products, and the foreign manufacturer does not impose any conditions or limitations upon the buyer,³⁶ the transaction value of the meat products is U.S.\$10,000.³⁷ If the invoice between the foreign manufacturer and United States importer states that the total cost of the meat products is U.S.\$10,000, with U.S.\$9,000 representing the cost of the meat products and U.S.\$1,000 representing the cost of ocean freight and insurance, the transaction value of the imported meat is U.S.\$9,000 since transaction value does not include international freight and insurance.³⁸

1. Legislative History of Section 402

The General Agreement on Tariffs and Trade ("GATT") is an international agreement established in 1947 for the purpose of reducing trade barriers and ending discriminatory treatment in international commerce.³⁹ Contracting parties to the GATT meet regularly to negotiate reductions of trade barriers.⁴⁰ To date, the contracting parties to the GATT have concluded seven rounds of multilateral trade negotiations.⁴¹

Prior to the seventh round of trade negotiations, the Tokyo Round of Multilateral Trade Negotiations (1973-1979), the method by which countries' valued imports constituted a barrier

35. 19 C.F.R. § 152.103(a)(1), ex. 1,4 (1992).

36. See *supra* note 7 (discussing limits on use of transaction value of imported merchandise).

37. 19 C.F.R. § 152.103(a)(1), ex. 1 (1992).

38. 19 C.F.R. § 152.103(a)(1), ex. 4 (1992); see *supra* note 9 (defining price paid or payable); see also SERKO, *supra* note 3, at 109-25 (discussing computation of transaction value of imported merchandise); STURM, *supra* note 1, § 47.2, at 5-28 (discussing computation of transaction value of imported merchandise). See generally 19 C.F.R. § 152.103(a) (1992) (giving examples of transaction value of imported merchandise).

39. GATT, *supra* note 6. STURM, *supra* note 1, § 62, at 1; Will Martyn, *International Trade: The General Agreement on Tariffs and Trade*, 29 HARV. INT'L L.J. 199 (1988) [hereinafter *International Trade*].

40. *International Trade*, *supra* note 39, at 199. Currently, there are 105 contracting states. SWAN & MURPHY, *supra* note 6, at 219. In addition, at least 20 other nations apply the GATT to their trade relations. *Id.*

41. *International Trade*, *supra* note 39, at 199 n.1. An eighth round of negotiations, the Uruguay Round, is still in progress. Keith Bradsher, *The Trade Accord: Europeans Agree with U.S. on Cutting Farm Subsidies; French Withhold Support; 2 Sides Compromise*, N.Y. TIMES, Nov. 21, 1992, at A1.

to trade.⁴² Calculation of customs value often was used to increase duties collected and to protect domestic industries.⁴³ In addition, the method by which contracting states valued imported merchandise varied considerably.⁴⁴ The GATT originally required customs valuation to be calculated according to fair, non-discriminatory rules consistent with commercial practices.⁴⁵ The presence of a "grandfather clause," however, permitted contracting states to calculate the value of imported merchandise according to customs laws that did not meet the GATT's requirements.⁴⁶

In the Tokyo Round of Multilateral Trade Negotiations, the contracting parties to the GATT negotiated, *inter alia*, a compre-

42. COMMENTARY, *supra* note 3, at 52-54; S. REP. NO. 249, 96th Cong., 1st Sess., 494 (1979), reprinted in 1979 U.S.C.A.N. 381, 494 [hereinafter S. REP. NO. 249].

43. S. REP. NO. 249, *supra* note 42, at 494; *Trade Agreements Act of 1979: Hearings Before the Subcomm. on International Trade of the Senate Comm. on Finance*, 96th Cong., 1st Sess. 521 (1979) (Summary of Testimony, Joint Industry Group).

44. S. REP. NO. 249, *supra* note 42, at 494; STAFF OF SUBCOMM. ON INTERNATIONAL TRADE, COMM. ON FINANCE, 96TH CONG., 1ST SESS., AGREEMENTS BEING NEGOTIATED AT THE MULTILATERAL TRADE NEGOTIATIONS IN GENEVA —U.S. INTERNATIONAL TRADE COMMISSION INVESTIGATION NO. 332-101 12 (Comm. Print 1979) [hereinafter MTN STUDIES]; COMMENTARY, *supra* note 3, at 52. The customs laws of most of the world's major trading countries, except the United States and Canada, calculated appraised imported merchandise using the Brussels Definition of Value ("BDV") method. S. REP. NO. 249, *supra* note 42, at 494; MTN STUDIES, *supra*, at 12; COMMENTARY, *supra* note 3, at 52. The BDV was a "notional" method of determining the value of imported merchandise. The BDV based appraised value on the price at which a product would be sold if the actual transaction in question were a perfectly competitive transaction. S. REP. NO. 249, *supra* note 42, at 494; MTN STUDIES, *supra*, at 12. Adjustments were made to actual price to reach the competitive price, often resulting in increased tariff liability. S. REP. NO. 249, *supra* note 42, at 494; MTN STUDIES, *supra*, at 12. In addition, countries interpreted BDV provisions differently, resulting in inconsistent application of the BDV method. COMMENTARY, *supra* note 3, at 53; REPORT BY THE DIRECTOR-GENERAL OF GATT, THE TOKYO ROUND OF MULTILATERAL TRADE NEGOTIATIONS, 69 (1979).

Canadian customs law based appraised value on the "fair market value" of the imported goods. MTN STUDIES, *supra*, at 14. Canadian customs law defined the "fair market value" of the imported goods as the price of similar goods when sold for home consumption in the country of exportation. *Id.* Thus, Canadian customs law used the time of exportation and the place from which the goods were shipped directly to Canada in determining appraised value. *Id.*

U.S. customs law provided for nine alternative methods of valuing imported merchandise.

U.S. goals in the MTN with respect to customs valuation were to provide a "positive" standard of customs valuation, i.e., one that based appraised value on the transaction value and to provide a "transparent" standard, i.e., one that would be more predictable. S. REP. NO. 249, *supra* note 42, at 495; COMMENTARY, *supra* note 3, at 51.

45. COMMENTARY, *supra* note 3, at 52.

46. *Id.*

hensive customs valuation code (the "GATT Valuation Code").⁴⁷ The GATT Valuation Code established that the preferred method of calculating appraised value is the transaction value of the imported merchandise.⁴⁸ The GATT Valuation Code defined the transaction value of the imported merchandise as the price paid or payable for the merchandise when sold for exportation to the country of importation.⁴⁹ In 1979, Congress enacted the Trade Agreements Act (the "TAA") to implement the GATT Valuation Code.⁵⁰

Prior to U.S. adherence to the GATT Valuation Code, U.S. customs law required Customs to calculate appraised value according to the export value of the imported merchandise.⁵¹ Sec-

47. AGREEMENT ON IMPLEMENTATION OF ARTICLE VII OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE, Apr. 12, 1979, T.I.A.S. No. 10,402 [hereinafter GATT VALUATION CODE]; COMMENTARY, *supra* note 3, at 51; S. REP. NO. 96-249, *supra* note 42, at 494. See ROSSIDES, *supra* note 6, at 111-12 (discussing adoption of GATT Valuation Agreement); SERKO, *supra* note 3, at 107-108 (discussing adoption of GATT Valuation Agreement); *Reflections*, *supra* note 14, at 119-20 (examining goals in adopting GATT Valuation Agreement, highlighting intriguing provisions, and identifying questions and problems left unresolved by negotiators).

48. GATT, art. vii, *supra* note 6, 55 U.N.T.S. at 216-18.

49. *Id.* arts. i, viii, 55 U.N.T.S. at 196-200, 218-20.

50. Trade Agreements Act of 1979 § 201, Pub. L. No. 96-39, 93 Stat. 144 (1980); STATEMENT OF ADMINISTRATIVE ACTION, *supra* note 6, at 463; S. REP. NO. 249, *supra* note 42, at 108; H. REP. NO. 96-317, 96th Cong., 1st Sess., (1979) [hereinafter H. REP. NO. 96-317]. In enacting the Trade Agreements Act, Congress stated the general rule that appraised value under Section 402 will be determined on the basis of information readily available in the United States. STATEMENT OF ADMINISTRATIVE ACTION, *supra* note 6, at 456.

51. 19 U.S.C. §§ 1401a, 1402, *amended by* Trade Agreements Act of 1979, Pub. L. No. 96-39, 93 Stat. 144 (1980); ROSSIDES, *supra* note 6, at 132-38. More precisely, prior to adoption of the GATT Valuation Code, U.S. customs valuation law consisted of two statutes: 19 U.S.C. § 1401a and 19 U.S.C. § 1402. *Id.* Determining which Customs used in calculating appraised value depended upon the article being appraised. T.D. 54521, 93 Treas. Dec. 14 (1958). Approximately 86% of all customs entries were valued under 19 U.S.C. § 1401a. S. REP. NO. 249, *supra* note 42, at 498.

Under the pre-1979 version of 19 U.S.C. § 1401a, the primary method of appraising imported merchandise was export value. 19 U.S.C. § 1401a, *amended by* Trade Agreements Act of 1979, Pub. L. No. 96-39, 93 Stat. 144 (1980). If the export value could not be calculated, Customs used the U.S. value of the imported merchandise to calculate appraised value. *Id.* § 1401a(a)(2). The U.S. value was the price at the time of exportation at which such or similar merchandise was freely sold or offered for sale in the principal market of the United States for domestic consumption, packed ready for delivery, in the usual wholesale quantities, and in the ordinary course of trade. *Id.* § 1401a(c). In calculating U.S. value, Customs deducted commissions paid, any amount usually added for general expenses and profit, usual expenses from the place of shipment to the place of delivery, and ordinary customs duties and federal excise and other taxes. *Id.* § 1401a(c)(1)-(3). If neither the export value nor the U.S. value of the

tion 402 defined export value as the price in the country of exportation at which merchandise similar to the imported merchandise is sold or offered for sale for exportation to the United

imported merchandise could be found, Customs used the constructed value of the imported merchandise to calculate appraised value. *Id.* § 1401a(a)(3). The constructed value was the sum of the cost of materials and of the fabrication and or other processing employed in producing such or similar merchandise prior to exportation, plus an amount for general expenses and profit equal to that usually reflected in sales of the merchandise and for the cost of containers, coverings and packing for shipment to the United States. *Id.* § 1401a(d). In addition, under the pre-1979 version of 19 U.S.C. § 1401a, Congress selected certain merchandise to be appraised on the basis of the American Selling Price, rather than the above methods of valuation. *Id.* § 1401a(a)(4). The American Selling Price was the price, including the cost of containers, coverings and packing, at which an article manufactured or produced in the United States was freely sold or offered for sale for domestic consumption in the United States or the price that the owner would have been willing to receive for such merchandise at the time of exportation of the imported article. *Id.* § 1401a(e).

Under the pre-1979 version of 19 U.S.C. § 1402, the primary method of calculating appraised value was the foreign value or the export value, whichever is higher. 19 U.S.C. § 1402, *amended by* Trade Agreements Act of 1979, Pub. L. No. 96-39, 93 Stat. 144 (1980). The foreign value was the price at which merchandise was sold for home consumption at the time of exportation of the merchandise to the United States, plus amounts equal to the cost of readying the merchandise for shipment. *Id.* § 1402(c). The export value was the market value or the price at the time of exportation at which the merchandise was freely offered for sale to the United States. *Id.* § 1402(d). If neither the foreign value nor the export value could be found, Customs appraised the imported merchandise using the U.S. value of the imported merchandise. *Id.* § 1402(a)(2). The U.S. value was the price at which the imported merchandise is freely offered for sale for domestic consumption, with an allowance for duty, costs of transportation and insurance, other necessary expenses from the place of shipment to the place of delivery, and a commission not exceeding six percent of goods acquired other than by purchase, or, if purchased, profits not to exceed eight percent and a reasonable allowance for general expenses not to exceed eight percent. *Id.* § 1402(e). If none of the three above values could be found, Customs appraised imported merchandise according to the cost of production of the imported merchandise. *Id.* § 1402(a)(3). The cost of production was defined as the total cost of materials and the work done on those materials in manufacturing or producing such or similar merchandise prior to the date of exportation, plus the usual general expenses (not less than ten percent), the cost of containers, coverings, packing, and other costs for putting the merchandise into condition ready for shipment to the United States, and an addition for ordinary profit of not less than eight percent of the total amount for the cost of materials and of fabrication and the usual general expenses. *Id.* § 1402(f). Finally, under 19 U.S.C. § 1402, Congress selected certain merchandise to be appraised on the basis of the American Selling Price, rather than the above methods of valuation. *Id.* § 1402(a)(4). The American Selling Price was the price, including the cost of containers, coverings and packing, at which an article manufactured or produced in the United States was freely sold or offered for sale for domestic consumption in the United States or the price that the owner would have been willing to receive for such merchandise at the time of exportation of the imported article. *Id.* § 1402(g).

States.⁵² Thus, determining export value under Section 402 required Customs to determine what constitutes a sale for exportation to the United States.⁵³ In replacing the export value method with the transaction value of the imported merchandise method, however, Congress failed to indicate which sale sets the transaction value where more than one sale qualifies as one for exportation to the United States.⁵⁴

Export value differs from the transaction value of the imported merchandise in two significant aspects.⁵⁵ First, export value bases valuation on the price of the merchandise at the time of exportation.⁵⁶ Transaction value, by contrast, bases valuation on the price of the merchandise at the time of the transaction.⁵⁷ Second, export value bases valuation on the price associated with the usual wholesale quantities.⁵⁸ Transaction value, on the other hand, bases valuation on the price associated with the actual

52. 19 U.S.C. § 1401a, *amended by* Trade Agreements Act of 1979, Pub. L. No. 96-39, 93 Stat. 144 (1980); ROSSIDES, *supra* note 6, at 133. More precisely, export value under 19 U.S.C. § 1401a was defined as:

the price, at the time of exportation to the United States of the merchandise undergoing appraisement, at which such or similar merchandise is freely sold or, in the absence of sales, offered for sale in the principal markets of the country of exportation, in the usual wholesale quantities and in the ordinary course of trade, for exportation to the United States, plus, when not included in such price, the cost of all containers and coverings of whatever nature and all other expenses incidental to placing the merchandise in condition, packed ready for shipment to the United States.

19 U.S.C. § 1401a, *amended by* Trade Agreements Act of 1979, Pub. L. No. 96-39, 93 Stat. 144 (1980). Export value under 19 U.S.C. § 1402 was defined as:

the market value or the price, at the time of exportation of such merchandise to the United States, at which such or similar merchandise is freely offered for sale to all purchasers in the principal markets of the country from which exported, in the usual wholesale quantities and in the ordinary course of trade, for exportation to the United States, plus, when not included in such price, the cost of all containers and coverings of whatever nature, and all other costs, charges, and expenses incident to placing the merchandise in condition, packed ready for shipment to the United States.

19 U.S.C. § 1402, *amended by* Trade Agreement Act of 1979, *amended by*, Pub. L. No. 96-39, 93 Stat. 144 (1980).

53. *See supra* note 52 (quoting definition of export value).

54. *See Reflections, supra* note 14, at 144.

55. ADVISORY COMMITTEE FOR TRADE NEGOTIATIONS, REPORT TO THE PRESIDENT, THE CONGRESS AND THE SPECIAL REPRESENTATIVE FOR TRADE NEGOTIATIONS 22 (1979).

56. *Id.*

57. *See supra* note 7 (defining transaction value of imported merchandise).

58. 19 U.S.C. § 1401a, *amended by* Trade Agreements Act of 1979, Pub. L. No. 96-39, 93 Stat. 144 (1980); 19 U.S.C. § 1402, *amended by* Trade Agreement Act of 1979, Pub. L. No. 96-39, 93 Stat. 144 (1980); STURM, *supra* note 1, § 47.1, at 1.

quantity involved in the transaction.⁵⁹

B. Customs and Judicial Treatment of Transactions Involving Middlemen

In resolving Section 402's ambiguity, the Court of Appeals for the Federal Circuit and its predecessor court, the Court of Customs and Patent Appeals, ruled that Customs must base appraised value on a first tier transaction if that transaction meets the requirements of Section 402.⁶⁰ Nonetheless, Customs and the Court of International Trade⁶¹ interpreted Section 402 to allow appraised value to be based on the first tier transaction only if the first tier transaction was the "most direct cause" of the exportation of the merchandise to the United States.⁶²

1. Customs' Rulings

Prior to *Nissho Iwai*, Customs policy for determining the appraised value of an import transaction involving middlemen was clear.⁶³ Customs based transaction value on the transaction that "most directly caused" the merchandise to be exported to the

59. See *supra* note 7 (defining transaction value of imported merchandise).

60. *United States v. Getz Bros. & Co.*, 55 C.C.P.A. 11 (1967); *R.J. Saunders & Co., Inc. v. United States*, 42 C.C.P.A. 55 (1954); *United States v. S.S. Kresge Co.*, 26 C.C.P.A. 349 (1939); see *supra* note 7 (discussing statutory requirements of Section 402).

61. Hon. Edward D. Re, *Litigation Before the United States Court of International Trade*, 19 U.S.C.A. xi, xiv (West Supp. 1993). The Court of International Trade is a court of national jurisdiction established under Article III of the U.S. Constitution. *Id.* The Court of International Trade consists of nine judges appointed by the President with the advice and consent of the Senate. *Id.* at xiv; 28 U.S.C. § 251(a) (1988). Pursuant to the Customs Court Act of 1980, the Court of International Trade has jurisdiction over civil actions arising from adverse agency actions arising out of import transactions. 28 U.S.C. §§ 1581-1585 (1988); Re, *supra*, at xvi. The Court of International Trade has all powers in law and equity or as conferred by statute upon a federal district court, as well as power to render money judgments for and against the United States, to order retrials, rehearings, or remands for further administrative hearings, and to fashion whatever relief is appropriate in a particular case, including the power to issue injunctions, writs of mandamus, and declaratory judgments. 28 U.S.C. §§ 1585, 2643 (1988); Re, *supra*, at xviii. Private parties and Customs may appeal decisions of the Court of International Trade to the Court of Appeals for the Federal Circuit. See STURM, *supra* note 1, §§ 30-32 (discussing judicial review of Customs' action and United States Court of International Trade).

62. C.S.D. 89-30, 23 Cust. Bull. 587 (1988); C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); *contra* C.S.D. 81-72, 15 Cust. Bull. 876 (1980), *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

63. C.S.D. 89-30, 23 Cust. Bull. 587 (1988); C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); *contra*

United States.⁶⁴ In utilizing a "most direct cause" test, Customs consistently found that the transaction between the middleman and the United States importer (i.e., the second tier transaction) was the "most direct cause" of the importation.⁶⁵

In the seminal Customs ruling on middleman pricing, Customs Service Decision ("C.S.D.") 83-46,⁶⁶ Customs held that when two or more transactions qualify as sales for exportation to the United States, the transaction to which the phrase "when sold for exportation to the United States" refers is the transaction which "most directly causes" the merchandise to be exported to the United States.⁶⁷ C.S.D. 83-46 involved a British Virgin Islands corporation ("BVI Corporation") acting as a middleman in the sale of cooking apparatus from a Far East manufacturer to a U.S. customer.⁶⁸ BVI Corporation planned to contract for production of the cooking apparatus with an Asian manufacturer that would produce the cooking apparatus according to specifications provided by BVI Corporation.⁶⁹ The Asian manufacturer would then ship the goods to BVI Corporation's U.S. customer.⁷⁰ Customs ruled that the transaction that "most directly caused" the exportation of the cooking apparatus to the United States was the sale from BVI Corporation to the U.S. branch.⁷¹

C.S.D. 81-72, 15 Cust. Bull. 876 (1980), *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

64. C.S.D. 89-30, 23 Cust. Bull. 587 (1988); C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); *contra* C.S.D. 81-72, 15 Cust. Bull. 876 (1980), *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

65. C.S.D. 89-30, 23 Cust. Bull. 587 (1988); C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); *contra* C.S.D. 81-72, 15 Cust. Bull. 880 (1980), *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

66. T.D. 78-414, 12 Cust. Bull. 920 (1978). Customs Service Decisions are published Customs rulings. *Id.* Published Customs rulings are those rulings deemed to be of precedential value. 19 C.F.R. § 177.10 (1992). Precedential rulings are published in the Customs Bulletin within 120 days of their issuance. *Id.* Unlike regular rulings, which are binding only with regard to the specific transaction described in the ruling, Customs Service Decisions are binding on Customs as to all importers with similar transactions. *Id.*

67. C.S.D. 83-46, 17 Cust. Bull. 811 (1983).

68. *Id.*

69. *Id.*

70. *Id.* at 812.

71. *Id.* Customs stated:

In regard to the [Trade Agreements Act of 1979], it is the position of the

Similarly, in C.S.D. 83-95, Customs appraised imported goods based on a sale between a Hong Kong middleman and the U.S. importer.⁷² The U.S. importer ordered custom-made shirts from a Hong Kong middleman who, in turn, ordered and purchased the shirts from a manufacturer in the People's Republic of China.⁷³ The Hong Kong middleman then resold the shirts to the U.S. importer.⁷⁴ Citing C.S.D. 83-46, Customs held that the contract for sale between the Hong Kong middleman and the U.S. importer was the transaction that "most directly caused" the goods to be exported to the United States.⁷⁵

Finally, in C.S.D. 84-54, Customs again calculated transaction value based on a sale between the middleman and the U.S. importer.⁷⁶ In C.S.D. 84-54, an English middleman planned to enter into an agreement with a Salvadoran shoe manufacturer for the purchase of shoes that would be shipped directly from El

Customs Service that the transaction to which the phrase "when sold for exportation to the United States" refers when there are two or more transactions which might give rise to a transaction value, is the transaction which most directly causes the merchandise to be exported to the United States.

In the circumstances described above, the sale from the manufacturers to [BVI corporation] does not cause the goods to be exported to the United States. The goods are not shipped as a result of this sale. The transaction that most directly causes their actual exportation is the sale from [BVI corporation to the U.S. customer]. Therefore, it is this sale to which we must look for a transaction value.

Id. at 813.

Although Customs found that the sale between BVI and the United States branch is the sale relevant to transaction value, Customs held that the transaction value of the imported merchandise was not the proper basis of appraisement since insufficient information was available to determine proceeds due BVI from subsequent resale arrangements. *Id.*

72. C.S.D. 83-95, 17 Cust. Bull. 930 (1983).

73. *Id.*

74. *Id.*

75. *Id.* Customs reasoned:

We . . . disagree with the view that the sale from (middleman) to the importer did not occur until the merchandise reached Hong Kong. In our view, the importer's purchase order and its acceptance by (middleman) constituted a contract for the sale of future goods, title to which passed to the importer when the goods were placed on board the vessel in Hong Kong. The merchandise was *not* resold while in transit to the U.S. Rather, the transfer of title to the importer was in furtherance of the preexisting contract to sell. That contract and the transfer of title to the importer were the "transaction" which most directly caused the goods to be exported to the United States.

Id. at 932.

76. C.S.D. 84-54, 18 Cust. Bull. 979 (1983)

Salvador to a U.S. importer.⁷⁷ The U.S. importer argued that the contract between the English middleman and the Salvadoran shoe manufacturer was the "most direct cause" of the exportation of the shoes to the United States.⁷⁸ Citing C.S.D. 83-46, Customs rejected the U.S. importer's contention, holding that the sale between the English middleman and the U.S. customer would be the sale that "most directly caused" the shoes to be exported to the United States.⁷⁹ Customs explained that using the transaction between the English middleman and the U.S. importer conforms with the legislative history of Section 402, which supports basing appraised value on information readily available in the United States.⁸⁰ Customs reasoned that calculating appraised value based on the transaction between the middleman and the Salvadoran manufacturer would require use of information derived primarily from non-U.S. sources.⁸¹

2. The Court of International Trade Adopts the "Most Direct Cause" Test

In *Brosterhous Coleman & Co. A/C Lurgi Chemie und Hüt-
tenteknik GmbH v. United States*,⁸² the Court of International
Trade ruled that the transaction value of the imported merchan-
dise should be based on the transaction that "most directly

77. *Id.*

78. *Id.*

79. *Id.* Customs explained:

The Statement of Administrative Action relating to section 402 of the [Trade Agreements Act of 1979] provides that "As a general rule, the Customs value determined under proposed section 402 will be on the basis of information readily available in the United States." We believe that our interpretation of the words "when sold for exportation to the United States" set forth in [C.S.D. 83-46] conforms to the above-stated intention since it generally results in our basing transaction value on information available in the United States. In contrast to this result, a determination that the above-quoted phrase refers to the transaction between the foreign manufacturer and the second foreign company would require transaction value to be based on information derived primarily from foreign sources.

Therefore, applying our holding in [C.S.D. 83-46] to the facts in this case, it is clear that the transaction which most directly causes the shoes to be exported from El Salvador to the United States is the sale from the English company, A, to the purchaser in the United States, D.

Id. at 980.

80. *Id.*; see *supra* notes 39-59 and accompanying text (discussing legislative history of Section 402).

81. C.S.D. 84-54, 18 Cust. Bull. 979, 980 (1983).

82. 737 F. Supp. 1197 (Ct. Int'l Trade 1990).

causes" the exportation to the United States.⁸³ Crown Zellerbach Corp. ("Crown"), a U.S. producer of paper, contracted with Lurgi Chemie und Huttentechnik GmbH ("Lurgi"), a German corporation, for the design, fabrication, and supervision of the construction of a chlorine dioxide bleach plant at Crown's paper-making facility in Camas, Washington.⁸⁴ The contract between Crown and Lurgi did not specify which vendors would supply the necessary components or even where the components would be purchased.⁸⁵ Lurgi bought the components from a German manufacturer.⁸⁶ Brosterhous Coleman & Co., a U.S. corporation, imported the equipment into the United States on behalf of Lurgi.⁸⁷ Customs appraised the imported components based on the transaction between Crown and Lurgi, not the transaction between Lurgi and the non-U.S. manufacturer.⁸⁸

In determining which transaction represented the transaction value of the imported merchandise, the Court of International Trade adopted Customs' rule that when more than one transaction qualifies as a sale for exportation to the United States, the transaction value should be based on the transaction that "most directly causes" the merchandise to be exported to the United States.⁸⁹ The court found, however, that unlike prior customs service decisions in which the contracts at issue contemplated the importation of merchandise,⁹⁰ the contract between

83. *Id.* at 1199; *see supra* note 61 (discussing role of Court of International Trade).
84. 737 F. Supp. at 1198.

85. *Id.* The contract contained the following clause:

The compensation indicated above . . . is understood to be for delivery of equipment and the engineering package c.i.f. Camas, Washington, including adequate packing as necessary, unloading not included. Customs duties up to 3.5% applying customs tariff No. 661.67 covering pulp paper machinery is also included. All other taxes, fees or expenses payable in the U.S.A. shall be paid and borne by Buyer.

Id. at 1199.

The court rejected Customs' assertion that the above clause required that the merchandise be imported. *Id.* Instead, the court found that the clause meant that the seller would be responsible only for duties up to 3.5% of the contract price. *Id.*

86. *Id.* at 1198.

87. *Id.*

88. *Id.* at 1199.

89. *Id.* at 1200.

90. C.S.D. 84-54, 18 Cust. Bull. 979 (1983); C.S.D. 83-95, 17 Cust. Bull. 930 (1983); C.S.D. 83-46, 17 Cust. Bull. 811 (1983); C.S.D. 81-72, 15 Cust. Bull. 880 (1980), *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

Crown and Lurgi did not require importation of merchandise.⁹¹ The court concluded that the contract was not the "most direct cause" of the exportation to the United States and that Customs incorrectly appraised the imported merchandise based on the contract.⁹²

3. Federal Circuit and Court of Customs and Patent Appeals Decisions on Transactions Involving Middlemen

Prior to *Nissho Iwai*, the Court of Appeals for the Federal Circuit and its predecessor court, the Court of Customs and Patent Appeals, analyzed whether the non-U.S. manufacturer's price associated with the first tier transaction may constitute the basis of appraisal.⁹³ Court of Customs and Patent Appeals decisions rendered before the Trade Agreements Act of 1979

91. *Brosterhous*, 737 F. Supp. at 1200. Judge, now Chief Judge, DiCarlo, reasoned:

The determinations upon which the government relies to support its position that the contract between Crown and Lurgi is the sale which most directly caused the exportation are inapposite. In C.S.D. 84-54, a United States company entered into a contract to purchase shoes from an English company that, in turn, purchased the shoes from a manufacturer in El Salvador. The manufacturer in El Salvador was to ship the merchandise directly to the United States. C.S.D. 84-54, 18 Cust. Bull. at 979. In C.S.D. 83-95, a United States company ordered shirts from a supplier in Hong Kong who would deliver them to the buyer in Hong Kong. The distributor purchased the merchandise from a manufacturer in the People's Republic of China. C.S.D. 83-95, 17 Cust. Bull. at 931. See also CLA-2 CO:R:CV:V 542928 BLS, TAA #57 (Jan. 21, 1983) (sale by Virgin Island distributor of cooking equipment manufactured in Asia to United States buyer).

In each instance, Customs determined that the sale for exportation was the transaction between the United States customer and the foreign distributor. See C.S.D. 84-54, 18 Cust. Bull. at 980; C.S.D. 83-95, 17 Cust. Bull. at 932; TAA #57 at 3. In each case, however, the contract with the United States purchaser contemplated that the merchandise would be imported.

Id.; see *supra* notes 63-81 and accompanying text (discussing Customs rulings on middleman pricing).

92. *Id.* Judge DiCarlo, found:

... When there is more than one sale for exportation, Customs policy is that transaction value should be calculated according to the sale which most directly caused the merchandise to be exported to the United States

... [T]he Court finds that the transaction between Crown and Lurgi was not the sale for exportation that most directly caused the merchandise to be exported to the United States. The transactions between Lurgi and its vendors are, therefore, the sales for exportation for purposes of calculating transaction value under 19 U.S.C. § 1401a(b) (1988).

Id. at 1199-1200.

93. *E.C. McAfee Co. v. United States*, 842 F.2d 314 (Fed. Cir. 1988); *United States v. Getz Bros. & Co.*, 55 C.C.P.A. 11 (1967); *R.J. Saunders & Co., Inc. v. United States*, 42

("TAA") consistently held that there was no need to consider the second tier transaction in calculating appraised value if the price associated with the first tier transaction also satisfied the statutory requirements of Section 402.⁹⁴ The sole decision by the Court of Appeals for the Federal Circuit rendered subsequent to the enactment of the TAA concurred that there was no need to consider the second tier transaction in calculating appraised value if the first tier transaction meets the elements of Section 402.⁹⁵

a. Decisions Rendered Prior to Enactment of the TAA

In *United States v. S.S. Kresge Co.*,⁹⁶ the Court of Customs and Patent Appeals established that the price associated with a first tier transaction may serve as the basis for appraisement under Section 402 of the Tariff Act of 1930.⁹⁷ In *S.S. Kresge Co.*, a U.S. importer purchased Christmas tree ornaments from a German middleman who had purchased the ornaments from several German manufacturers.⁹⁸ Customs contended that the manufacturers' price was not the proper basis of appraisement since that price was not available to other purchasers.⁹⁹ Thus, Customs argued that the ornaments should be appraised on the higher middleman's price associated with the second tier transaction.¹⁰⁰ The Court of Customs and Patent Appeals rejected Customs' argument and found that the record contained substantial evidence that the price was available to other purchasers.¹⁰¹ Thus, the court held that the German manufacturers' price was the

C.C.P.A. 55 (1954); *United States v. S.S. Kresge Co.*, 26 C.C.P.A. 349 (1939); *see supra* note 15 (describing jurisdiction of Court of Appeals for the Federal Circuit).

94. *United States v. Getz Bros. & Co.*, 55 C.C.P.A. 11 (1967); *R.J. Saunders & Co., Inc. v. United States*, 42 C.C.P.A. 55 (1954); *United States v. S.S. Kresge Co.*, 26 C.C.P.A. 349 (1939); *see supra* note 7 (discussing statutory requirements of Section 402).

95. *E.C. McAfee Co. v. United States*, 842 F.2d 314 (Fed. Cir. 1988); *see supra* note 7 (discussing statutory requirements of Section 402).

96. 26 C.C.P.A. 349 (1939).

97. *Id.*

98. *Id.* at 350-51.

99. *Id.* at 351-52. Section 402(d) of the Tariff Act of 1930 required that the merchandise be sold or offered for sale in the ordinary course of trade in the principal markets of the exporting country for exportation to the United States. 19 U.S.C. §§ 1401a, 1402; *see supra* note 52 (discussing requirements of export value).

100. 26 C.C.P.A. at 351-52.

101. *Id.* at 352; *see supra* notes 52-53 and accompanying text (discussing requirements of export value).

proper basis of appraisal even though the price associated with the second tier transaction also satisfied the statutory requirements of Section 402.¹⁰²

In *R.J. Saunders & Co., Inc. v. United States*,¹⁰³ the Court of Customs and Patent Appeals again ruled that the middleman's price associated with the second tier transaction cannot be used as the basis of appraisal if the manufacturer's price qualifies under Section 402.¹⁰⁴ The court in *R.J. Saunders* considered whether a resale restriction requiring Canadian middlemen to export meat paste disqualified the first tier transaction from forming the basis of export value.¹⁰⁵ The resale restriction imposed in the first tier transaction prevented the Canadian middlemen from selling the canned meat paste in Canada, requiring the middlemen to export the canned meat paste.¹⁰⁶ The court ruled that the restriction requiring exportation included exportation to the United States.¹⁰⁷ Therefore, the manufacturer's price could be the basis of export value.¹⁰⁸ The court indicated that export value need not be determined solely on the basis of sales to U.S. importers.¹⁰⁹

Finally, in *United States v. Getz Bros. & Co.*,¹¹⁰ the Court of Customs and Patent Appeals adhered to the principle set forth in *S.S. Kresge* and held that if a manufacturer and a middleman's price each meet the statutory standards for export value, Customs must appraise the merchandise using the manufacturer's

102. 26 C.C.P.A. at 352.

103. 42 C.C.P.A. 55 (1954).

104. *Id.*; see *supra* notes 52-53 and accompanying text (discussing requirements of export value).

105. 42 C.C.P.A. at 56-57; see *supra* notes 52-53 and accompanying text (discussing requirements of export value).

106. 42 C.C.P.A. at 57.

107. *Id.* at 59. The court stated:

Under the . . . language of the statute, the transactions between the Canadian manufacturer and [Canadian middlemen] cannot be deemed to be controlled sales in the sense that the limitation imposed thereon should operate in derogation of the establishment of a freely offered price for export to the United States.

Id. at 59-60.

108. *Id.*; see *supra* notes 52-53 and accompanying text (discussing requirements of export value).

109. 42 C.C.P.A. at 60.

110. 55 C.C.P.A. 11 (1967).

price.¹¹¹ Customs contended that the prices charged by Japanese plywood manufacturers to Japanese middlemen did not meet the statutory requirements for export value because the Japanese middlemen were not required to export the plywood.¹¹² Rejecting Customs' position, the court held that substantial evidence existed that the sales between the manufacturers and middlemen were sales for exportation to the United States.¹¹³

b. Middleman Pricing After Enactment of the TAA—*E.C. McAfee Co. v. United States*

In *E.C. McAfee Co. v. United States*,¹¹⁴ the Court of Appeals for the Federal Circuit ruled that Customs incorrectly appraised imported made-to-measure clothing based on the price paid by the importer to a middleman in the second tier transaction.¹¹⁵ The importer of record in *McAfee* was American Air Parcel Forwarding Company, Ltd. ("AAP"), a freight forwarder for Hong Kong clothing distributors that sold clothing to U.S. customers.¹¹⁶ Sales representatives of the Hong Kong distributors solicited orders in the United States from U.S. customers.¹¹⁷ In addition, retail shops in Hong Kong solicited orders from U.S. tourists.¹¹⁸ Upon receiving an order, the sales representatives and retail stores forwarded the order to the Hong Kong distribu-

111. *Id.*; see *supra* notes 52-53 and accompanying text (discussing requirements of export value).

112. 55 C.C.P.A. at 19-20; see *supra* notes 52-53 and accompanying text (discussing requirements of export value).

113. 55 C.C.P.A. at 20. *Getz Bros. & Co.* arose as a result of Japanese export quota and licensing requirements, that limited the amount of plywood which could be exported to various countries. *Id.* at 13. In 1955, decline in the price of plywood, due primarily to excess production capacity, caused the Japanese government to impose a quota and export licensing system. *Id.* The Japanese government assigned quotas to Japanese manufacturers of plywood, as well as to middlemen dealing in Japanese plywood, that limited the amount of plywood that could be exported. *Id.* The government enforced the quota system by requiring exporters to obtain export licenses from the government. *Id.* at 14. Exporters could not obtain an export license unless they had quota. *Id.*

114. 842 F.2d 314 (Fed. Cir. 1988); see *supra* notes 39-59 and accompanying text (describing enactment of the Trade Agreements Act of 1979).

115. 842 F.2d at 315.

116. *Id.*

117. *Id.*

118. *Id.* at 315-16.

tors.¹¹⁹ The Hong Kong distributors, in turn, contracted with tailors in Hong Kong for production of the clothing.¹²⁰ The tailors performed a "cut, make, and trim" operation.¹²¹ After receiving the manufactured clothing from the tailors, the Hong Kong distributors delivered the clothing to AAP for transport to the United States.¹²²

The Federal Circuit determined that the transaction between the Hong Kong manufacturer and the Hong Kong middleman, the first tier transaction, was a sale for exportation to the United States because the goods made by the Hong Kong manufacturer were clearly destined for the United States.¹²³ As a result, the importer was entitled to the benefit of valuation based on the first tier transaction between the Hong Kong manufacturer and Hong Kong middleman even though Customs' valuation, based on the second tier transaction between the Hong Kong middleman and U.S. importer, also satisfied the statutory requirements of Section 402.¹²⁴ The court reasoned that cases decided prior to the 1979 enactment of the TAA¹²⁵ supported

119. *Id.* at 315.

120. *Id.* at 316.

121. *Id.* The tailors cut the fabric, sewed the cut parts together, and supplied the garments' trim. *Id.*

122. *Id.*

123. *Id.* at 319. The court stated:

We conclude that the tailors' actual knowledge that the particular suits are destined for the United States is irrelevant. Where clothing is made-to-measure for individual United States customers and ultimately sent to those customers, the reality of the transaction between the distributors and the tailors is that the goods, at the time of the transaction between the distributor and tailors, are "for exportation to the United States." Apart from this factor, there is no dispute that the merchandise was being made for export to the United States. Accordingly, we hold that the trial court's finding to the contrary is clearly erroneous

The merchandise at issue is unique in that, from the time of the initial contact until eventual importation, the goods in question were being made for a specific United States consumer, not the United States market generally. That should not be taken to mean that only goods tailor-made for a United States individual are goods clearly destined for the [sic] exportation to the United States, but rather that is, in this case, the factor which *compels a reversal* of the finding that the goods were not for exportation to the United States at the time of assembly.

Id.

124. *Id.* at 318-19; *see supra* note 7 (discussing statutory requirements of Section 402).

125. *United States v. Getz Bros. & Co.*, 55 C.C.P.A. 11 (1967); *R.J. Saunders & Co., Inc. v. United States*, 42 C.C.P.A. 55 (1954); *United States v. S.S. Kresge Co.*, 26 C.C.P.A.

the court's holding that the price charged by the Hong Kong manufacturers provided the proper basis for appraising the merchandise.¹²⁶

One month after the Federal Circuit's holding in *McAfee*, however, Customs issued a ruling that limited the availability of the benefits of *McAfee* to U.S. importers.¹²⁷ In Ruling No. 544,179, Customs indicated its position that the holding of *McAfee* is limited to factual situations identical to those of *McAfee*.¹²⁸ Thus, only importers of made-to-measure clothing, where the manufacturer of the clothing and middleman were located in the same country, could benefit by *McAfee*'s holding.¹²⁹

349 (1939); see *supra* notes 39-59 and accompanying text (describing enactment of the Trade Agreements Act of 1979).

126. *E.C. McAfee*, 842 F.2d at 318. The court reasoned:

[Section 402] provides that transaction value is based on the price for the merchandise "when sold for exportation to the United States." In *United States v. Getz Bros. & Co.*, 55 C.C.P.A. 11 (1967), a precedential decision of the Court of Customs and Patent Appeals, a similar, three-tiered, distribution situation was presented. While the *Getz* case was decided under 19 U.S.C. § 1401a(b) as it appeared before amendment by the Trade Agreements Act of 1979, the language of the earlier statute is not significantly different from the quoted provision of the current statute. The issue in *Getz* was whether valuation of certain plywood should be at the manufacturer's price to a foreign middleman or that middleman's price to the United States customer. Two holdings in that case are significant here. First, a sale need not be to purchasers located in the United States to provide the basis for valuation. Second, if the transaction between the manufacturer and the middleman falls within the statutory provision for valuation, the manufacturer's price, rather than the price from the middleman to his customer, is used for appraisal.

Id. (citing *United States v. Getz Bros. & Co.*, 55 C.C.P.A. 11, 18 (1967); *R.J. Saunders & Co. v. United States*, 42 C.C.P.A. 55, 59 (1954); *United States v. S.S. Kresge Co.*, 26 C.C.P.A. 349, 352 (1939); *Rodriguez v. United States*, 23 Cust. Ct. 296, 300 (1949)).

127. Customs Ruling Letter No. 544,179 (Apr. 1, 1988).

128. *Id.* at 2. Customs stated:

[I]t is Headquarter's position that the holding of [*McAfee*] is clearly limited by the language of the court to the facts which are peculiar [sic] to [*McAfee*]. This approach is required not only because of the commercial circumstances before the court but also by the difficulties implicit in determinations regarding the term "assembly" under these circumstances. Accordingly, insofar as Headquarters is concerned, the principles set forth within [*McAfee*] should only be applied with regard to the importation of made-to-measure clothing when the distributor and tailor are located in the same country. Further, all field offices should be satisfied that the clothing involved is in fact made-to-measure.

Id.

129. *Id.*

II. NISSHO IWAI AMERICAN CORP. v. UNITED STATES

In *Nissho Iwai American Corp. v. United States*,¹³⁰ the Court of Appeals for the Federal Circuit analyzed whether Customs should appraise imported merchandise based on a Japanese middleman's price associated with a second tier transaction, rather than a Japanese manufacturer's price associated with a first tier transaction.¹³¹ The Federal Circuit concluded that where both the Japanese manufacturer's price and the Japanese middleman's price are statutorily viable transaction values,¹³² the Japanese manufacturer's price provides the basis for determining transaction value.¹³³ Moreover, the Federal Circuit rejected using a "most direct cause" test to determine which of two viable transactions may be used to determine transaction value.¹³⁴

A. Facts and Procedural History

The importer in *Nissho Iwai*, the Metropolitan Transportation Authority of New York City ("MTA"), purchased 325 rapid transit passenger cars pursuant to a contract with Nissho Iwai American Corporation ("NIAC").¹³⁵ The MTA paid NIAC U.S.\$844,500 per passenger car.¹³⁶ The contract provided for the production of the passenger cars in Japan by a third party, Kawasaki Heavy Industries, Ltd. ("KHI").¹³⁷ The contract also obligated KHI to use U.S. propulsion and brake systems.¹³⁸ NIAC assigned its rights and obligations under the contract to its parent corporation, Nissho Iwai Corporation ("NIC"), on the same day NIAC executed the contract with the MTA.¹³⁹

NIC entered into a contract with KHI for production of the

130. 982 F.2d 505 (Fed. Cir. 1992).

131. *Id.* at 511.

132. See *supra* note 7 (discussing statutory requirements of Section 402).

133. 982 F.2d at 511; see *supra* note 7 (discussing statutory requirements of Section 402).

134. 982 F.2d at 511.

135. *Id.* at 506.

136. *Id.*

137. *Id.* KHI worked with NIAC's parent corporation, Nissho Iwai Corporation, in placing the bid for the contract. 15 Ct. Int'l Trade 644, 645, *rev'd*, 982 F.2d 505 (Fed. Cir. 1992). KHI signed a warranty of performance to MTA and to NIAC on the same day that NIAC signed the contract with MTA. *Id.*

138. 15 Ct. Int'l Trade at 645, *rev'd*, 982 F.2d 505 (Fed. Cir. 1992).

139. 982 F.2d at 506.

passenger cars.¹⁴⁰ NIC and KHI agreed to be jointly responsible for the quality of the cars.¹⁴¹ KHI agreed to provide technical assistance following delivery of the passenger cars.¹⁴² KHI also agreed to deliver the passenger cars to NIC, free on board, to Kobe, Japan.¹⁴³ NIC paid KHI approximately U.S.\$331,300 per passenger car.¹⁴⁴

NIAC imported the passenger cars into the United States in sixteen entries¹⁴⁵ from 1983 to 1985.¹⁴⁶ In the first eleven entries, Customs appraised the passenger cars on the basis of the lower price provided for in the KHI contract.¹⁴⁷ In the remaining five entries, however, Customs appraised the passenger cars based on the higher price provided for in the MTA contract.¹⁴⁸

NIAC protested¹⁴⁹ Customs' appraisal of the value of

140. *Id.* KHI manufactured the passenger cars specifically for sale to MTA; the passenger cars could not be used for any other purpose. *Id.* at 506-7.

141. 15 Ct. Int'l Trade at 646, *rev'd*, 982 F.2d 505 (Fed. Cir. 1992).

142. *Id.*

143. 982 F.2d at 507.

144. *Id.* ¥80,002,100 converted to U.S. currency at 241.50 yen per dollar. *Foreign Exchange*, N.Y. TIMES, Mar. 18, 1982, Business, at D12.

145. *See supra* note 2 (defining entry).

146. 982 F.2d at 507.

147. *Id.*

148. *Id.* Customs deducted a total of U.S.\$347,355.32 from the contract price of each passenger car for various nondutiable costs, charges, and payments associated with the price paid by MTA to NIC. *Id.* n.5. For vehicles entered in 1983, Customs appraised the vehicles at U.S.\$497,737.61. *Id.* at 507. For passenger cars entered in 1984, Customs appraised the passenger cars at U.S.\$500,495.16. *Id.* For vehicles entered in 1985, Customs appraised the vehicles at U.S.\$503,751.17. *Id.* Customs calculated the final dutiable value of each vehicle by deducting from U.S.\$542,036.45 duties of 8.9% for 1983 entries, 8.3% for 1984 entries, and 7.6% for 1985 entries. *Id.* n.6. Customs' appraised value is nearly U.S.\$200,000 greater than the value provided for in the contract between KHI and NIC.

149. *Id.* at 507. A protest is a written statement filed with a district director of Customs objecting to Customs decisions regarding the following issues:

- (1) the appraised value of the imported merchandise;
- (2) the classification and rate and amount of duties chargeable;
- (3) all charges or exactions of whatever character within the jurisdiction of the Secretary of the Treasury;
- (4) the exclusion of merchandise from entry or delivery or a demand for redelivery to customs custody under any provision of the customs laws, except a determination appealable under section 1337 of this title;
- (5) the liquidation or reliquidation of an entry, or any modification thereof;
- (6) the refusal to pay a claim for drawback; and
- (7) the refusal to reliquidate an entry under section 1520(c) of this title[.]

19 U.S.C. § 1514(a), (c) (1988); 19 C.F.R. § 174.11 (1992); *see supra* note 5 (describing organization of Customs).

the passenger cars imported in the last five entries.¹⁵⁰ NIAC re-

Protests must be filed within 90 days following (1) the date of notice of liquidation of the imported merchandise, (2) the date of the decision as to which the protest is made (e.g., the date of written notice excluding merchandise from entry), or (3) the date of mailing of notice of demand for payment against a bond in the case of a surety. 19 C.F.R. § 174.12(e). If a protest is not filed within the 90 day time period, Customs decisions regarding protestable issues are final and conclusive upon all persons, including Customs. 19 U.S.C. § 1514(a). The following parties may file protests:

- (1) [t]he importer or consignee shown on the entry papers, or their sureties;
- (2) [a]ny person paying any charge or exaction;
- (3) [a]ny person seeking entry or delivery;
- (4) [a]ny person filing a claim for drawback; or
- (5) [a]ny [duly] authorized agent of any of the persons described [above].

19 C.F.R. § 174.12(a) (1992).

After a protest is filed, the district director must act upon the protest within two years from the date of filing, unless the protest concerns the exclusion of merchandise, or if there is a request for an accelerated disposition, in which case Customs must act upon the protest within 30 days from the date of filing a request for accelerated disposition. *Id.* § 174.21(a), (b); *Id.* § 174.22(a), (c); *Id.* § 174.29. If Customs fails to act upon an accelerated protest within the 30 day time period, the protest is denied by operation of law. *Id.* § 174.22(d). Any person whose protest has been denied may contest the denial of the protest by filing an action in the United States Court of International Trade within 180 days after the date of mailing of notice of the denial or the date of the protest for which an accelerated disposition was requested. *Id.* § 174.31.

In addition, a protesting party may file an application for further review of a protest with a district director of Customs where the protesting party believes that a Customs' decision:

- (a) [i]s alleged to be inconsistent with a ruling of the Commissioner of Customs or his designee, or with a decision made in any district with respect to the same or substantially similar merchandise;
- (b) [i]s alleged to involve questions of law or fact which have not been ruled upon by the Commissioner of Customs or his designee or by the Customs courts;
- (c) [i]nvolves matters previously ruled upon by the Commissioner of Customs or his designee or by the Customs courts but facts are alleged or legal arguments presented which were not considered at the time of the original ruling; or
- (d) [i]s alleged to involve questions which the Headquarters Office, United States Customs Service, refused to consider in the form of a request for internal advice.

Id. § 174.24.

In the event the district director denies the protest, the protest is reviewed by the regional commissioner of Customs, or the Commissioner of Customs if the protest involved lack of uniform treatment of an issue by Customs, the existence of an established uniform practice, an interpretation of a court decision or ruling of the Commissioner of Customs, or a question that has not been the subject of a Headquarters, U.S. Customs Service ruling or court decision. *Id.* § 174.26(b). If the regional commissioner or Commissioner of Customs subsequently deny the protest, the protesting party may file seek judicial review in the United States Court of International Trade. *Id.* § 174.31.

¹⁵⁰. 982 F.2d at 507.

quested Customs to issue a ruling that the appraised value of the vehicles should be based on the lower price provided for in the KHI contract.¹⁵¹ Customs refused to issue such a ruling and adhered to its previous decision that the MTA contract price represented the transaction value of the imported passenger cars.¹⁵² Arguing that the holding in *E.C. McAfee Co. v. United States*¹⁵³ mandated appraisement of the passenger cars based upon the KHI contract price, NIAC commenced an action in the Court of International Trade.¹⁵⁴

B. *The Court of International Trade Decision*

The Court of International Trade rejected NIAC's assertion that *McAfee* was dispositive in determining the transaction value of the imported passenger cars.¹⁵⁵ The court distinguished *McAfee* on several grounds.¹⁵⁶ According to the court, *McAfee* involved two distinct agreements.¹⁵⁷ The court reasoned that *Nissho Iwai*, by contrast, essentially involved one agreement.¹⁵⁸

151. *Id.*

152. *Id.* at 507-08.

153. 842 F.2d 314 (Fed. Cir. 1988).

154. *Nissho Iwai American Corp. v. United States*, 15 Ct. Int'l Trade 644, 647-51, *rev'd*, 982 F.2d 505 (Fed. Cir. 1992); *see supra* notes 114-29 and accompanying text (discussing *E.C. McAfee Co. v. United States*, 842 F.2d 314 (Fed. Cir. 1992)).

155. 15 Ct. Int'l Trade 644, 650 *rev'd*, 982 F.2d 505 (Fed. Cir. 1992); *see supra* notes 27-35 and accompanying text (discussing transaction value of imported merchandise).

156. 15 Ct. Int'l Trade 644, 648, *rev'd*, 982 F.2d 505 (Fed. Cir. 1992). Judge Musgrave acknowledged, however, that *E.C. McAfee Co. v. United States* might require that the appraised value of the passenger cars be based on the KHI-NIC contract:

A clear understanding of the [MTA-NIAC contract] shows that the facts are decidedly different from *McAfee*, although a more doctrinaire reading of the contract in the context of the *McAfee* case might come to a different conclusion.

Id.

157. *Id.* at 650. The court reasoned:

The Court of Appeals for the Federal Circuit valued the *McAfee* transaction between the assembler and the middleman. It had a choice between two discrete transactions. Here the Court is presented with a manufacturer which has dealt extensively with the U.S. customer, and a secondary contract which seems more like an afterthought than a true arms-length transaction. The result is that the case differs greatly from *McAfee*.

Id. at 649-50.

158. *Id.* at 649. The court noted that in *McAfee* only the middleman had contact with both the foreign manufacturer and the United States importer, while KHI had extensive contact with MTA. *Id.* Judge Musgrave wrote:

Although Kawasaki was not a signatory to the [contract between the MTA and NIAC], the arrangements made show that it was excluded in only the for-

Thus, the court did not have the option of choosing between two independent transactions.¹⁵⁹ The court also noted that *McAfee* involved a one hundred percent imported suit, while in *Nissho Iwai* the imports were fifty-seven percent Japanese and forty-three percent American.¹⁶⁰ Finally, the court noted that *McAfee* involved an assembly operation, whereas the contract between MTA and NIAC involved manufacturing.¹⁶¹

The court held that NIAC did not overcome the presumption of correctness attaching to Customs' valuation of the imported passenger cars.¹⁶² Using the "most direct cause" test set

mal sense of the contract. Kawasaki was pre-selected by the MTA as manufacturer before the [contract] was signed. Its name appears several times in the contract, and it had rights and duties according to a major role in the contract. There were face-to-face meetings between KHI and the MTA. Kawasaki signed a warranty of performance to both the MTA and NIAC, and agreed to abide by the terms of the [MTA and NIAC contract]. It was, at the very least, a third-party beneficiary named explicitly in the [MTA-NIAC contract].

Id. at 649.

159. See *supra* note 157 (quoting court's language on why court could not choose between two independent transactions).

160. 15 Ct. Int'l Trade 644, 649, *rev'd*, 982 F.2d 505 (Fed. Cir. 1992). Judge Musgrave did not explain why the commingling of American-made parts was a material difference between *Nissho Iwai* and *McAfee*. *Id.* In fact, Judge Musgrave acknowledged that the commingling of American-made parts did not require a different result from *McAfee*. *Id.*

161. *Id.* at 650. Judge Musgrave reasoned:

The case at bar involves manufactured goods, not assembled merchandise, within the meaning of Customs Regulation 19 C.F.R. § 152.103, and to the extent that *McAfee* involved "assembled merchandise," it is inapplicable here. Kawasaki provided its own raw materials for the Japanese portion of the cars. As manufacturer rather than assembler, KHI had an interest in the merchandise other than as an assembler under § 152.103(a)(3). Kawasaki also provided significant technical support and warranty service after delivery.

The *McAfee* Court framed the questions before it as "whether the custom-made clothing is assembled merchandise within the meaning of the regulation and, if so, whether the transaction value of the merchandise should be determined on that basis, although it held that the transaction value should be based on the actual price paid rather than the assembly price. But the tailored suits were assembled from supplied components, and the fact that the [sic] KHI manufactured the subway cars in large part from scratch is a significant distinction between the *McAfee* export transaction and the [NIAC-MTA] contract.

Id. at 650-51 (footnotes omitted).

162. *Id.* at 644; 28 U.S.C. § 2639(a)(1)(1988); see *Federal Election Comm'n v. Democratic Senatorial Campaign Comm.*, 454 U.S. 27, 37 (1981) (stating agency's interpretation of statute is entitled to deference); *Jarvis Clark Co. v. United States*, 733 F.2d 873, 876 (Fed. Cir. 1984) (stating presumption of correctness attaches to Customs decision).

forth in *Brosterhous, Coleman & Co. A/C Lurgi Chemie und Hüttentechnik GmbH v. United States*,¹⁶³ the Court of International Trade concurred with Customs that the contract between the MTA and NIAC was the “most direct cause” of the exportation of the passenger cars to the United States because the contract between MTA and NIAC obligated NIAC to import the passenger cars.¹⁶⁴ The court also determined that NIC and KHI were not related parties pursuant to Section 402.¹⁶⁵

163. See *supra* notes 82-92 (discussing *Brosterhous, Coleman & Co. A/C Lurgi Chemie und Hüttentechnik GmbH v. United States*, 737 F. Supp. 1197 (Ct. Int'l Trade 1990)).

164. 15 Ct. Int'l Trade 644, 647, *rev'd*, 982 F.2d 505 (Fed. Cir. 1992). Judge Musgrave reasoned:

In *Brosterhous, Coleman & Co. v. United States*, an American manufacturer contracted with a West German firm to construct a chlorine dioxide bleach plant in the United States. The contract did not specify which subcontractors should be used and the foreign seller decided to use foreign components. *Brosterhous* held that “[w]hen there is more than one sale for exportation, Customs policy is that transaction value should be calculated according to the sale which most directly caused the merchandise to be exported to the United States.” The transaction value was the price the foreign seller paid for the components, rather than the contract amount, because the foreign seller was free to buy from any supplier, and *could* have fulfilled the contract by using only U.S. suppliers. Because the foreign seller was not obligated to buy from abroad, the contract with the U.S. customer did not primarily cause the goods to be exported to the United States.

The operative facts in this case are directly contrary to *Brosterhous*. The MTA negotiated with NIAC on the express understanding that Kawasaki would build the cars. The Master Contract specified Kawasaki as the “primary builder.” NIC/NIAC was *not* free to pick its supplier. It was obligated to buy from abroad. Following the *Brosterhous* analysis, the [NIAC-MTA] contract was the contract which most directly caused the goods to be exported to the United States.

Id. (emphasis in original) (citing *Brosterhous Coleman & Co. A/C Lurgi Chemie und Hüttentechnik GmbH v. United States*, 737 F. Supp. 1197 (Ct. Int'l Trade 1990)).

165. *Id.* at 651. The court found:

Nissho Japan and KHI agreed to allocate windfall profits and losses in the Side Agreement, but their interaction did not constitute a partnership or joint venture to produce the cars under 19 U.S.C. § 1401a(g)(1)(D) (1991). Kawasaki and NIC did not share overall profits or losses on the project, or pool their resources or expertise. Each handled its own area of responsibility as laid out in the [NIAC-MTA] contract: Kawasaki manufactured, and Nissho Japan administered.

Nissho Japan and Kawasaki each owned no more than one percent of the other, so they were not “related parties” within the meaning of the cross-ownership provisions of 19 U.S.C. § 1401a(g)(1)(F) (1991). Their involvement does tend to show that the agreements between NIC and KHI were of a different nature from the foreign-transactions in either *Getz* or *McAfee*.

Id.; see *supra* note 7 (defining term “related parties”).

C. *The Court of Appeals Decision*

The Court of Appeals for the Federal Circuit held that *McAfee*¹⁶⁶ was binding precedent for valuing import transactions involving middlemen.¹⁶⁷ In *McAfee*,¹⁶⁸ the court reasoned that where both the first and second tier transactions meet the elements of Section 402,¹⁶⁹ the first tier transaction, rather than the second tier transaction, was the basis of the transaction value of the imported merchandise.¹⁷⁰ As a result, the Federal Circuit

166. *McAfee*, 842 F.2d 314 (Fed. Cir. 1988).

167. *Nissho Iwai*, 982 F.2d at 510-11. Writing for the unanimous court, Judge Lourie reasoned:

Accepting that both the manufacturer's price and the middleman's price may serve as the basis of transaction value, the critical issue on appeal here centers upon which price is legally proper. In view of the controlling and binding authority of *McAfee*, we hold that the transaction value of the imported passenger cars at issue must be based on the KHI-NIC contract price.

The trial court, however, determined that *McAfee* was distinguishable from the instant case and thus did not consider it controlling authority in appraising the transaction value of the imported vehicles. Instead, the court employed the analysis set forth in *Brosterhous*, 737 F. Supp. 1197 (Ct. Int'l Trade 1990), in determining that the transaction value should be based on the price paid by the purchaser. We agree with NIAC that the trial court committed reversible error in failing to follow the controlling authority of *McAfee*.

Although the trial court cited differences in the material facts of *McAfee*, none supports its conclusion that those differences mandate a different result. The trial court determined that *McAfee* is inapplicable because it involved "assembled merchandise" within the meaning of 19 C.F.R. § 152.103 and did not involve the valuation of manufactured goods. The court found that KHI had an interest in the imported vehicles other than as an assembler because KHI was extensively involved in the negotiations with the MTA and that KHI possessed a significant stake in the ensuing contract between MTA and NIAC. That distinction, however, does not take this case out from under the rule of *McAfee*. In fact, it emphasizes KHI's role in the export of the vehicles to the United States, supporting the conclusion that its sale to NIC is the legally-controlling transaction.

The ultimate issue in *McAfee* was whether the assembly price of the imported merchandise, rather than the price paid by the purchaser, should serve as the basis for determining transaction value. Similarly, the critical issue here is whether the sales price paid by NIC to KHI should serve as the basis for appraising the transaction value of the imported vehicles. *McAfee* speaks directly to that question and answers it in the affirmative. That case is not only applicable here, it is dispositive.

Id. at 510-11 (footnote omitted) (citing *Generra Sportswear Co. v. United States*, 905 F.2d 377, n.7 (Fed. Cir. 1990)).

168. 842 F.2d 314 (Fed. Cir. 1988).

169. See *supra* note 7 (discussing statutory requirements of Section 402).

170. *McAfee*, 842 F.2d 314 (Fed. Cir. 1988); see *supra* notes 114-29 and accompanying text (discussing *E.C. McAfee Co. v. United States*, 842 F.2d 314 (Fed. Cir. 1988)).

held that the Court of International Trade erred in affirming Customs' determination that based transaction value on the second tier transaction between MTA and NIAC.¹⁷¹

In following *McAfee*, the Federal Circuit acknowledged that *Nissho Iwai* applies solely to situations in which there exists a legitimate choice between two statutorily viable transactions.¹⁷² The existence of a viable transaction for determining the transaction value of imported merchandise depends upon the presence of two fact-specific elements.¹⁷³ First, the goods must be "clearly destined" for export to the United States.¹⁷⁴ Second, the manufacturer and middleman must deal with each other at arms-length.¹⁷⁵

171. 982 F.2d 505 (Fed. Cir. 1992). Significantly, two Court of International Trade cases decided subsequent to *Nissho Iwai* have adhered to *Nissho Iwai*'s holding that U.S. importers are entitled to valuation based on the first tier transaction. *Synergy Sport International, Ltd. v. United States*, No. 91-11-00836, slip op. 93-5 (Ct. Int'l Trade Jan. 12, 1993); *Generra Sportswear, Inc. v. United States*, No. 88-07-00474S (Ct. Int'l Trade June 29, 1993) (order granting plaintiff's motion to remand entries to district directors for reliquidation). In addition, Customs has since established guidelines for applying *Nissho Iwai* to import transactions. DIRECTOR OF CUSTOMS OFFICE OF TRADE OPERATIONS, EFFECT OF NISSHO IWAI AND RELATED CASES ON FIELD OPERATIONS (Mar. 8, 1993). The guidelines provide:

1. Entered values based on a sale from a manufacturer to a middleman may be liquidated once the importer has demonstrated to the satisfaction of the import specialist that the sale from the manufacturer to the middleman was a bona fide sale for export to the U.S. and was at arm's length. Import specialists are referred to Customs notice on transfer pricing for guidance on what constitutes an arm's length transaction when parties to a sale are related (58 Fed. Reg. 5445 January 21, 1993).
2. Protests of entered values on liquidated entry summaries, based on the decisions in *Nissho Iwai*, *Synergy*, Court No. 91-11-00836 (Ct. Int'l Trade January 12, 1993), *McAfee*, 6 Fed.Cir. (T) 92, 842 F.2d 314 (Fed. Cir. 1988), and related court cases, may be allowed once the importer establishes that the sale from the manufacturer to the middleman was a bona fide sale for export to the U.S. and was at arm's length, as indicated above.

Id.

172. *Id.* The Federal Circuit cautioned that not every contract between a foreign manufacturer and foreign middleman may serve as the basis for calculating appraised value. *Id.* at 509. Such a rule would threaten tariff revenues if manufacturers conspire with importers to charge artificially low prices. *Id.*

173. *Id.*

174. *Id.*

175. *Id.* Judge Lourie stated:

[T]he rule only applies where there is a legitimate choice between two statutorily viable transaction values. The manufacturer's price constitutes a viable transaction value when the goods are clearly destined for export to the United States and when the manufacturer and the middleman deal with each other at

The Federal Circuit found that *Nissho Iwai* involved two viable transactions for determining the transaction value of the imported merchandise.¹⁷⁶ The Federal Circuit characterized the first tier transaction between KHI and NIC as a viable transaction for determining transaction value because the imported passenger cars were manufactured for a specific U.S. purchaser and had no possible alternative destination.¹⁷⁷ In addition, the KHI contract was the result of arms-length bargaining.¹⁷⁸

More significantly, the Federal Circuit also overruled the "most direct cause" test of *Brosterhous, Coleman & Co. v. United States*.¹⁷⁹ According to the Federal Circuit, nothing in the legis-

arm's length, in the absence of any non-market influences that affect the legitimacy of the sales price.

Id.

176. *Id.*

177. *Id.* Judge Lourie wrote:

In this case, the vehicles that were the subject of the KHI-NIC contract were manufactured for a specific United States purchaser, the MTA. They were unquestionably intended for "exportation to the United States" and had no possible alternative destination.

Id. at 509.

178. *Id.*

179. *Id.* at 511. The court proceeded:

In the interest of clarifying the law, we consider it necessary to examine the case of *Brosterhous, Coleman & Co. v. United States*, 737 F. Supp. 1197 (Ct. Int'l Trade 1990), upon which the trial court relied in reaching its decision. The court in *Brosterhous* held that where there are two transactions that can be considered to be sales for importation to the United States, "Customs policy is that transaction value should be calculated according to the sale which most directly caused the merchandise to be exported to the United States." *Id.* at 1199.

The U.S. Customs Service issued a seminal ruling in CLA-2 CO:R:CV:V, 5429238 BLS, TAA #57, C.S.D. 83-46, 17 Cust. Bull. 811 (January 21, 1983) in which it stated its position that "the transaction to which the phrase 'when sold for exportation to the United States' refers when there are two or more transactions which might give rise to a transaction value, is the transaction which most directly causes the merchandise to be exported to the United States." C.S.D. 83-46, 17 Cust. Bull. at 813. In so ruling, Customs acknowledged that under 19 U.S.C. § 1401a(b), as it existed before amendment by the Trade Agreements Act of 1979, "it was possible to use as the sale for exportation to the United States for purposes of determining statutory export value a sale from a foreign seller to a foreign buyer, who in turn sold the merchandise to a United States importer." However, Customs departed from that view because the Trade Agreements Act replaced "export value" with "transaction value" as the primary basis for valuation. Thus Customs concluded that "cases decided under the prior law are not, therefore, necessarily precedent under the [Trade Agreements Act]." C.S.D. 83-46, 17 Cust. Bull. at 813.

We reject the Customs Service's rationale as being legally unsound. A

lative history of Section 402 supported a rule requiring consideration of which transaction is the "most direct cause" of an exportation.¹⁸⁰ The Federal Circuit reasoned that judicial precedent prior to the 1979 amendment of Section 402 supported rejection of a "most direct cause" test since the current version of Section 402 and its predecessor both required a sale for exportation to the United States.¹⁸¹

III. THE FEDERAL CIRCUIT CORRECTLY REJECTED THE "MOST DIRECT CAUSE" TEST RESULTING IN SIGNIFICANT DUTY-SAVINGS FOR AMERICAN IMPORTERS

In *Nissho Iwai American Corp. v. United States*,¹⁸² the Court of Appeals for the Federal Circuit correctly rejected the "most direct cause" test used by Customs in applying Section 402 to transactions involving middleman pricing.¹⁸³ By holding that an importer is entitled to appraisement based on the first tier transaction, the Federal Circuit significantly clarified customs valuation law concerning import transactions involving middlemen.¹⁸⁴ Further, although there are limits to the availability of savings

similar argument was rejected by the court in *McAfee*, which recognized that "the language of the earlier statute is not significantly different from the . . . provision of the current statute." 842 F.2d at 318, 6 Fed. Cir. at 97. We agree with NIAC that the 1979 amendment did not change the operative language of the statutory provision for valuation which requires that the sale be "for exportation to the United States." Further, we can discern nothing in the legislative history of the 1979 amendment that suggests that Customs . . . should undertake an investigation focusing on which of two transactions most directly caused the exportation. The "Customs policy" followed by *Brosterhous* proceeds from an invalid premise. To the extent *Brosterhous* is inconsistent with this court's decision in *McAfee* by requiring a weighing of the relative importance of two viable transactions, it is overruled.

Id. at 511; see *Brosterhous, Coleman & Co. v. United States*, 737 F. Supp. 1197 (Ct. Int'l Trade 1990); see also *supra* notes 82-92 and accompanying text (discussing *Brosterhous, Coleman & Co. v. United States*, 737 F. Supp. 1197 (Ct. Int'l Trade 1990)).

180. 982 F.2d at 511; see *supra* notes 39-59 and accompanying text (discussing legislative history of Section 402).

181. 982 F.2d at 511; see *supra* notes 96-113 and accompanying text (discussing judicial precedent on middleman pricing prior to enactment of TAA); see also *supra* note 7 (discussing statutory requirements of Section 402).

182. 982 F.2d 505 (Fed. Cir. 1992).

183. See *supra* notes 10-14 and accompanying text (describing transactions involving middlemen).

184. See *supra* note 179 (quoting court's clarification of customs valuation law concerning import transactions involving middlemen).

under the Federal Circuit's decision, *Nissho Iwai* should result in duty-savings for U.S. importers since first tier transactions between non-U.S. manufacturers and middlemen should be of less value than second tier transactions between non-U.S. middlemen and U.S. importers.¹⁸⁵

A. *The Federal Circuit Correctly Rejected the "Most Direct Cause" Test*

Subsequent to the enactment of the TAA, Customs used a "most direct cause" test to determine which of two viable transactions should form the basis of transaction value.¹⁸⁶ Customs' rationale for employing a "most direct cause" test was that the TAA had replaced export value with transaction value as the primary basis for valuation.¹⁸⁷ According to Customs, pre-1979 case law, such as *United States v. Getz Bros. & Co.*,¹⁸⁸ did not govern valuation issues raised under the Trade Agreements Act.¹⁸⁹

The Court of Appeals for the Federal Circuit correctly characterized Customs' rationale as legally unsound, finding that the TAA did not change the operative language of Section 402.¹⁹⁰ Therefore, Customs had no reason to distinguish cases decided prior to the TAA. In *United States v. S.S. Kresge Co.*¹⁹¹ and its progeny, the courts clearly and consistently held that appraisement should not be based on the second tier transaction if the first tier transaction satisfies the requisite statutory elements of Section 402.¹⁹² Even Customs recognized that the operative language of Section 402 did not change after enactment of the

185. See *supra* note 11 (defining middleman as one who buys at one price for purpose of reselling at higher price).

186. See *supra* notes 63-81 and accompanying text (discussing Customs rulings on middleman pricing).

187. See *supra* notes 63-81 and accompanying text (discussing Customs rulings on middleman pricing); see also *supra* notes 39-59 (discussing enactment of TAA).

188. 55 C.C.P.A. 11 (1967); see *supra* notes 110-13 and accompanying text (discussing *United States v. Getz Bros. & Co.*, 55 C.C.P.A. 11 (1967)).

189. See C.S.D. 81-72, 15 Cust. Bull. at 880 ("[W]hile judicial decisions construing provisions of the old and new laws are pertinent, they are in no way binding upon this agency when construing similar provisions under the TAA."), *revoked on other grounds*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981).

190. 982 F.2d at 511; see *supra* notes 39-59 and accompanying text (discussing legislative history of Section 402); see also *supra* note 7 (discussing statutory requirements of Section 402).

191. 26 C.C.P.A. 349 (1939).

192. See *supra* notes 96-114 and accompanying text (discussing judicial cases on middleman pricing decided prior to enactment of TAA); see also *supra* note 7 (discussing statutory requirements of Section 402).

TAA.¹⁹³

Customs' reliance on the legislative history of Section 402 was equally misplaced. Nothing in the legislative history of Section 402 supported application of a "most direct cause" test.¹⁹⁴ Although the legislative history of Section 402 stated that valuation generally would be based on information readily available in the United States,¹⁹⁵ it does not follow that the transaction value of imported merchandise has to be based on the transaction that "most directly causes" merchandise to be exported to the United States.¹⁹⁶ Customs itself ruled that the situs of a sale is irrelevant to determining whether the transaction qualifies as a sale for exportation to the United States.¹⁹⁷ Reliance on the legislative history of Section 402 was simply an attempt to justify an otherwise unjustifiable policy.

B. *Nissho Iwai Clarified Customs Valuation Law, Bringing Duty-Savings Within the Reach of U.S. Importers*

By holding that an importer is entitled to appraisement based on the lower of two viable transaction values, the Federal Circuit clarified the law applicable to customs valuation of import transactions involving middleman pricing.¹⁹⁸ A significant shortcoming of the Federal Circuit's decision in *E.C. McAfee Co. v. United States*¹⁹⁹ was its failure to address the validity of Customs' "most direct cause" test. Customs limited *McAfee* to its

193. See C.S.D. 81-72, 15 Cust. Bull. 876, 880 (1980) ("It is significant that [the definition of transaction value of imported merchandise] and the definitions of export value under the old and new laws contain the identical language 'for exportation to the United States.'"), *revoked*, Customs Ruling Letter No. 542,643 (Oct. 19, 1981); see also *supra* notes 39-59 (discussing legislative history of Trade Agreements Act).

194. See *supra* notes 39-59 and accompanying text (discussing legislative history of Section 402).

195. *Statement of Administrative Action*, *supra* note 6, at 456; see *supra* notes 39-59 and accompanying text (discussing legislative history of Section 402).

196. See *supra* notes 82-92 and accompanying text (use of "most direct cause" test may result in basing transaction value on first tier transaction).

197. General Notice, 26 Cust. B. & Dec., No. 8 at 13 (Jan. 27, 1992) ("[T]he situs of a sale is not relevant to the determination of whether merchandise is 'sold for exportation to the United States' within the meaning of 19 U.S.C. § 1401a(b)(1)."); see *supra* note 7 (discussing requirements of transaction value of imported merchandise).

198. See *supra* note 179 (quoting court's clarification of customs valuation law concerning transactions involving middlemen).

199. 842 F.2d 314 (Fed. Cir. 1988); see *supra* notes 114-29 and accompanying text (discussing *E.C. McAfee Co. v. United States*).

facts and continued to use the "most direct cause" test.²⁰⁰ *Nissho Iwai* clarified the proposition originally articulated in *McAfee* which stated that importers were entitled to the benefit of the lower of two viable transaction values and that Customs' test was improper. In the two Court of International Trade decisions rendered subsequent to *Nissho Iwai*, the Court of International Trade ruled that an importer was entitled to valuation based on the first tier transaction.²⁰¹ Customs has since established guidelines for applying *Nissho Iwai* to import transactions.²⁰²

Moreover, the Federal Circuit in *Nissho Iwai* established a flexible standard for determining whether future transactions qualify as a sale for exportation to the United States.²⁰³ In *Nissho Iwai*, the Federal Circuit held that goods need only be "clearly destined" for the United States to meet the requirements of Section 402.²⁰⁴ An importer should be able to meet the requirements of *Nissho Iwai* if the design, marking, specifications, or other features of the goods or transaction indicate that the goods were manufactured for sale to the United States. As a result, U.S. importers buying from unrelated middlemen may realize considerable duty-savings since Customs will appraise imports based on the lower price associated with the first tier transaction. At least one estimate indicates that importers could potentially

200. Customs Ruling Letter No. 544179 (Apr. 1, 1988). Customs stated:

[I]t is Headquarter's position that the holding of [*McAfee*] is clearly limited by the language of the court to the facts which are peculiar [sic] to this case . . . Accordingly, insofar as Headquarters is concerned, the principles set forth within the subject court case should only be applied with regard to the importation of made-to-measure clothing when the distributor and tailor are located in the same country. Further, all field offices should be satisfied that the clothing involved is in fact made-to-measure.

Id.; see *supra* notes 114-29 and accompanying text (discussing *E.C. McAfee Co. v. United States*, 842 F.2d 314 (Fed. Cir. 1988)).

201. *Synergy Sport International, Ltd. v. United States*, No. 91-11-00836, slip op. 93-5 (Ct. Int'l Trade Jan. 12, 1993); *Generra Sportswear, Inc. v. United States*, No. 88-07-00474S (Ct. Int'l Trade June 29, 1993) (order granting plaintiff's motion to remand entries to district directors for reliquidation); see *supra* note 171 (discussing Court of International Trade adherence to holding of *Nissho Iwai*).

202. See *supra* note 170 (quoting Customs' guidelines on applying *Nissho Iwai* to import transactions involving middlemen).

203. See *supra* notes 174-75 and accompanying text (discussing "clearly destined" requirement of *Nissho Iwai*).

204. *Nissho Iwai American Corp. v. United States*, 982 F.2d at 509; see *supra* note 7 (discussing statutory requirements of Section 402).

save hundreds of millions of dollars under *Nissho Iwai*.²⁰⁵

C. *Limitations on Obtaining Duty Savings Under Nissho Iwai*

The availability of substantial savings under *Nissho Iwai* is limited by several factors. First, the Federal Circuit did not provide guidance on what constitutes "clearly destined."²⁰⁶ Thus, it is not clear what proof the court requires to demonstrate that merchandise sold from a non-U.S. manufacturer to a non-U.S. middleman is destined for the United States. Presumably, however, merchandise manufactured according to specifications provided by the U.S. importer or U.S. government standards should meet the clearly destined test.

Second, the ability of the importer to save duties depends on the importer's ability to persuade the middleman to disclose the price the middleman paid to the non-U.S. manufacturer. In order to base appraised value on the sale between the non-U.S. manufacturer and the non-U.S. middleman, the importer must know the value of that transaction. It is unlikely that an importer will learn the value of the transaction between the non-U.S. manufacturer and non-U.S. middleman since the middleman buys from the manufacturer for the purpose of reselling the merchandise to the importer at a higher price.²⁰⁷ An importer may expect a middleman to be hesitant to reveal his profit margin. If the importer does substantial business with the middleman, however, the importer may have some leverage to obtain the value of the transaction between the manufacturer and the middleman.

Third, to temper the effects of *Nissho Iwai*, Customs may scrutinize the relationship between the importer and the middleman to determine if a principal-agent relationship exists. If Customs determines that the middleman is an agent of the importer, Customs may deem the middleman's profit to be a selling commission, which is dutiable under Section 402.²⁰⁸

Finally, importers purchasing from middlemen that are re-

205. Louise Lucas, *U.S. Tax Ruling Will Slash Hong Kong Firms' Bills*, SOUTH CHINA MORNING POST, Jan. 22, 1993, Business, at 2.

206. See *supra* notes 174-5 and accompanying text (discussing "clearly destined" requirement of *Nissho Iwai*).

207. See *supra* note 11 (defining middleman).

208. See *supra* note 9 (discussing additions to price paid or payable).

lated²⁰⁹ to the importer must consider the adverse tax implications of reducing dutiable value.²¹⁰ Section 1059A of the Internal Revenue Code prohibits an imported product purchased from a related²¹¹ overseas party from being carried at an inventory value greater than the amount at which it is valued for transaction value purposes.²¹² Thus, an importer should only argue for reducing appraised value if the duty savings are greater than the increased tax liability resulting from a lower cost of goods sold. Given the generally low rates of duty, importers buying from related middlemen may not benefit from *Nissho Iwai*.

CONCLUSION

Section 402 case law requires Customs to calculate appraised value based on the price charged by the non-U.S. manufacturer to the non-U.S. middleman if there are two sales that qualify as the basis for appraised value. Accordingly, in *Nissho Iwai* the Federal Circuit correctly rejected Customs' practice of denying importers the benefits of appraised value based on the manufacturer's price. As a result, *Nissho Iwai* brought considerable duty-savings within the reach of importers. While there are limits on the application of *Nissho Iwai*, importers should adequately examine their import transactions to determine whether they qualify for duty-savings.

Michael E. Roll*

209. See *supra* note 7 (defining "related parties").

210. 26 U.S.C. § 1059A (1988).

211. 26 U.S.C. § 482 (1988 & Supp. III 1991). Congress limited application of Section 1059A of the Internal Revenue Code to those parties that are related within the meaning of Section 482 of the Internal Revenue Code. *Id.* Section 482 of the Internal Revenue Code defines related parties as:

two or more organizations, trades, or businesses (whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests

Id.; see *supra* note 7 (noting tax implications of transaction value of imported merchandise between related parties); cf. *supra* note 7 (defining "related parties" under Section 402).

212. 26 U.S.C. § 1059A. Section 1059A prevents a company from inflating the inventory value of imported merchandise to increase the amount of its cost of goods sold deduction and simultaneously reducing the value of goods from its related foreign supplier to reduce customs duty liability. *Id.*; see *supra* note 7 (discussing transaction value of imported merchandise).

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