# TAB

# A

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September 4, 2002

**BY HAND DELIVERY**

The Honorable Robert C. Bonner
Commissioner of Customs
U.S. Customs Service
Customs Headquarters
Attention: Office of Regulations and
Rulings
799 9th Street, N.W.
Washington, DC 20229

**Re: NAFTA Advance Ruling Request**

Dear Commissioner Bonner:

On behalf of BHP Billiton Diamonds Inc. ("BHP Billiton"), which is headquartered in Vancouver, British Columbia, Canada,[1] and in accordance with section 181.91 *et seq.* of the regulations of the U.S. Customs Service ("Customs"),[2] we respectfully submit this request for an advance ruling under Article 509 of the North American Free Trade Agreement ("NAFTA"). Specifically, we request that Customs issue a ruling that diamonds that are mined in Canada and cut and polished in Belgium, India, Israel, or another third country are of Canadian origin for purposes of the NAFTA Marking Rules, and, accordingly, should be marked "Made in Canada" when imported into the United States.

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[1] The registered office address of BHP Billiton Diamonds Inc. is 2300-1111 West Georgia Street, Vancouver, British Columbia, V6E 4M3, Canada.

[2] 19 C.F.R. § 181.91 *et seq.* All citations to the Code of Federal Regulations ("C.F.R.") are to the 2002 version thereof.

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This request concerns subject matter for which a NAFTA advance ruling is appropriate. The regulations provide that Customs shall issue NAFTA advance rulings concerning, *inter alia*, "[w]hether the proposed or actual marking of a good satisfies country of origin marking requirements under part 134 of this chapter and under the Marking Rules set forth in part 102 of this chapter."[3] Because this request requires Customs to determine the appropriate country-of-origin marking under the NAFTA Marking Rules set forth in part 102 of the Customs regulations, the request concerns subject matter for which a NAFTA advance ruling is appropriate.

Moreover, this NAFTA advance ruling request concerns only *prospective* transactions. BHP Billiton has not yet shipped diamonds mined in Canada and cut and polished in a third country to the United States. Thus, as contemplated in the Customs statute and regulations, BHP Billiton seeks to fully understand the consequences of its planned transactions prior to their consummation.[4] Moreover, to the best of BHP Billiton's knowledge, Customs has never considered an identical transaction, nor have the issues raised herein ever been the subject of judicial review.

Thus, it is within the sound administration of the NAFTA and the NAFTA Marking Rules for Customs to issue an advance ruling in response to this request. Moreover, because BHP Billiton is prudently awaiting an advance ruling from Customs prior to undertaking its planned transactions, BHP Billiton respectfully requests that Customs issue a ruling as expeditiously as possible, but not later than 120 calendar days from today, as provided in the regulations.[5]

## I. FACTUAL BACKGROUND

BHP Billiton has mined diamonds in the Lac de Gras area of the Northwest Territories of Canada at the EKATI™ Diamond Mine since October 1998. The first diamond-bearing mineral deposits on the property were discovered in 1991. The opening of the mine in late 1998 followed a comprehensive mine approval and development

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[3] 19 C.F.R. § 181.92(b)(6)(vii).

[4] Id. § 181.92(b)(

[5] Id. § 181.99(a)(1)

process involving a multi-million dollar investment.[6] The first sale of diamonds from the EKATI™ mine took place in January 1999.

Prior to the opening of the EKATI™ mine, almost all diamonds sold in Canada and the United States originated from mines in Africa, Australia, and Russia. Today, the EKATI™ mine produces approximately U.S.$400 million worth of rough diamonds a year, or about 5 percent of total world production, by value. With two additional mines in Canada owned by companies other than BHP Billiton scheduled to become operational within the next three years, Canada's share of world production of rough diamonds is expected to increase to 12 percent by 2005.[7]

Diamonds are pure carbon in a crystalline form. Natural diamonds originate far below the surface of the earth, at depths of 200 kilometers or more, where high temperatures and extreme pressures cause diamond crystallization. Volcanic eruptions brought diamonds to the earth's surface millions of years ago. Most natural diamonds are found in deposits of a rare variety of ultrabasic igneous rock called kimberlite. The majority of kimberlite deposits have no diamonds or so few as to be uneconomic to mine. Less than 100 kimberlite deposits in the world have been profitably exploited since kimberlite diamonds were first discovered almost 130 years ago.

The most substantial operation in the production of a "finished" (*i.e.*, cut and polished) diamond ready to be made into jewelry is the extraction of the rough diamond from a kimberlite deposit. BHP Billiton estimates that, excluding exploration, permitting, and mine development costs, which are substantial, approximately 85 percent of all costs involved in the production of a polished diamond relate to the mining and the on-site processing of the kimberlite ore necessary to extract rough diamonds. Thus, cutting and polishing the rough diamond to create a finished diamond accounts for approximately 15 percent of the total production costs.

Although cutting and polishing diamonds requires specialized skills, these skills are not unique to any one country. Expert cutting and polishing capability exists in many countries, including Belgium, India, Israel, Thailand, Russia, the Philippines, the United States, and, to a lesser degree, in Canada, where a small but burgeoning industry exists.

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[6] See http://ekati.ca

[7] See http://www.gov.nt.ca/RWED/diamond/industry.htm

Moreover, although excellent visual acuity, manual dexterity, and proper computer programming can contribute to the shape and brilliance of a finished diamond, a diamond's inherent value is based on its weight, clarity, and color. These characteristics are innate in the rough diamond and cannot be fundamentally changed through cutting and polishing.

BHP Billiton intends to ship rough diamonds extracted from the EKATI™ mine in the Northwest Territories, Canada, to diamond cutters in Belgium, Israel, India, Russia, Thailand, or some other third country. Diamond cutters in these countries will cut the rough diamonds and polish them into their finished form. BHP Billiton will then export the finished (*i.e.*, cut and polished) diamonds from their place of finishing to the United States. Either BHP Billiton, an affiliated company or joint venture, or an unaffiliated customer will act as the importer or record. The specific U.S. port(s) of entry at which the cut and polished diamonds will be imported has not been determined. BHP Billiton proposes to mark the imported diamonds, or their immediate containers, "Made In Canada," and to represent the diamonds as "Canadian diamonds." In lieu of words, given the small size of the product, BHP Billiton alternatively proposes to mark the diamonds on their girdle with a lasered brand designating their Canadian origin, such as a stylized maple leaf.

Non-industrial, unworked (*i.e.*, rough) diamonds are classified under subheading 7102.31.0000 of the Harmonized Tariff Schedule of the United States ("HTSUS"). Other non-industrial diamonds, including cut and polished diamonds for use in jewelry, are classified under subheading 7102.39.0010, if weighing not over 0.5 carat each, or subheading 7102.39.0050, if weighing over 0.5 carat each. Thus, cutting and polishing a rough diamonds involves a change from subheading 7102.31 to subheading 7102.39, but not a change in chapter or heading.

## II. THE NAFTA MARKING RULES REQUIRE DIAMONDS MINED IN CANADA AND PROCESSED IN A THIRD COUNTRY TO BE MARKED "MADE IN CANADA"

Section 304 of the Tariff Act of 1930, as amended,[8] provides that, unless excepted, every article of foreign origin (or its container) imported into the United States shall be marked in a conspicuous place as legibly, indelibly, and permanently as the nature of the

[8] 19 U.S.C. § 1304.

article (or its container) will permit, in such manner as to indicate to the ultimate purchaser in the United States the English name of the country of origin of the article. Section 134.1(b) of the Customs regulations defines "country of origin" as

> the country of manufacture, production, or growth of any article of foreign origin entering the U.S. Further work or material added to an article in another country must effect a substantial transformation in order to render such other country the country of origin within this part; however, for a good of a NAFTA country, the NAFTA Marking Rules will determine the country of origin.[9]

Thus, the NAFTA Marking Rules determine whether a good is a "good of a NAFTA country."[10] A "good of a NAFTA country" is an article whose country of origin is Canada, Mexico, or the United States as determined by the NAFTA Marking Rules.[11]

The NAFTA Marking Rules are set forth in Part 102 of the Customs regulations. Section 102.11 sets forth a hierarchy of rules for determining country of origin that must be followed in order. According to section 102.11(a), "[t]he country origin of a good is the country in which

> (1) The good is wholly obtained or produced;
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> (2) The good is produced exclusively from domestic materials; or
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> (3) Each foreign material incorporated in that good undergoes an applicable change in tariff classification set out in section 102.20 and satisfies any other

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[9] 19 C.F.R. § 134.1(b) (emphasis added).

[10] Id. § 134.1(j).

[11] Id. § 134.1(g).

> applicable requirements of that section, and all other applicable requirements of these rules are satisfied.[12]

Under the first prong, when goods are wholly obtained or produced in a specific NAFTA country, that country will be regarded as the country of origin of the merchandise. Under the second prong, when goods are produced exclusively from domestic materials originating in a particular NAFTA country, that country is regarded as the country of origin. Under the third prong, if a good is neither wholly obtained or produced in a single country nor produced in a country exclusively from domestic materials, the country of origin is the country in which a "tariff shift" (a change in classification from one HTS provision to another) took place, if that shift is enumerated in section 102.20.

If no tariff shift takes place, or a change in tariff classification takes place but this shift is not listed in the applicable provision of section 102.20, the determination of country of origin is based on the next rule in the hierarchy of rules enumerated in section 102.11. The next rule enumerated in the hierarchy under section 102.11(b) states that the country of origin will be the country of origin of the single material that determines the "essential character" of the merchandise.

Application of these criteria to the facts of this case dictates that the country of origin of diamonds mined in Canada and cut and polished in a third country is Canada.

### A. Diamonds Mined In Canada And Cut And Polished In A Third Country Are "Wholly Obtained Or Produced" In Canada

Under the NAFTA Marking Rules, the country of origin of an article is the country in which the article was "wholly obtained or produced."[13] The Customs regulations define "a good wholly obtained or produced" in a country to include "[a] mineral good extracted in that country."[14] A diamond is a mineral good, and a diamond mined in Canada has been extracted in Canada. Therefore, a diamond mined in Canada

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[12] Id. § 102.11(a).

[13] Id. § 102.11(a)(1).

[14] Id. § 102.1(g)(1

is "a good wholly obtained or produced" in Canada within the meaning of U.S. Customs regulations. Thus, under the NAFTA Marking Rules, the country of origin of a diamond mined in Canada is Canada.

The NAFTA Marking Rules make clear that a good must be considered "wholly obtained or produced" unless a "foreign material" is incorporated into the good. "Foreign material" is defined as "a material whose country of origin as determined under these rules is not the same country as the country in which the good is produced."[15] Further, "material" is defined to include only "a good that is incorporated into another good as a result of production with respect to that other good, and includes parts, ingredients, subassemblies, and components."[16] The definition of "foreign material" does not include labor employed in a third country to process the product.

In this case, the rough diamonds will be cut and polished in a third country. Cutting and polishing does not involve the incorporation of any foreign material into the rough diamond. To the contrary, cutting and polishing merely involves the application of labor and the *removal* of diamond material from the rough diamond. No material whatsoever is *added* during the cutting and polishing processes. Thus, because no foreign material is incorporated into the diamond in a third country, the cut and polished diamonds are "wholly obtained or produced in Canada," *i.e.*, they are of Canadian origin.

### B. Alternatively, Diamonds Mined In Canada And Cut And Polished In A Third Country Are "Produced Exclusively From Domestic Materials"

To the extent that Customs would not consider a diamond mined in Canada and cut and polished in a third country to have been "wholly obtained or produced" in Canada, then Customs should determine that such products are nevertheless of Canadian origin because they are "produced exclusively from domestic materials."[17] As discussed above, no "material," as that term is defined by the Customs regulations, is added to diamonds mined in Canada through the processes of cutting and polishing. Accordingly,

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[15] Id. § 102.1(e).

[16] Id. § 102.1(l).

[17] Id. § 102.11(a)(2).

under the NAFTA Marking Rules, diamonds mined in Canada and cut and polished in a third country also are of Canadian origin under the second prong in the hierarchy.

### C. Alternatively, Processing In A Third Country Does Not Result In An Applicable Change In Tariff Classification

Even if Customs found that cutting and polishing in a third country rendered a diamond mined in Canada no longer wholly obtained or produced in Canada and no longer produced exclusively with domestic materials, application of the third prong in the hierarchy of the NAFTA Marking Rules indicates that the country of origin is not the country in which the diamond was cut and polished.

In cases where "foreign materials" are added to a good prior to sale to the ultimate purchaser, the regulations require Customs to examine whether the good undergoes an applicable change in tariff classification as set forth in section 102.20 of the Customs regulations.[18] The tariff shift requirement applicable to headings 7102-7103 of the HTSUS, which include diamonds, reads as follows:

> A change to heading 7102 through 7103 from any other chapter.[19]

A rough diamond is classified under subheading 7102.31.0000 of the HTSUS, and a cut and polished diamond is classified under subheading 7102.39.0010 of the HTSUS if weighing not over 0.5 carat each, and subheading 7102.39.0050 if weighing over 0.5 carat each. As noted above, in order for the country of origin of a diamond mined in Canada and cut and polished in a third country to be considered as being the third country under the NAFTA Marking Rules, the cutting and polishing in the third country must result in a change in classification to heading 7102 through 7103 from any other chapter.[20] Cutting and polishing, however, merely change the tariff classification at the six-digit, subheading level, from 7102.31 to 7102.39. Cutting and polishing do not result in a change to heading 7102 from any other chapter. Accordingly, cutting and polishing

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[18] Id. § 102.11(a)(3)

[19] Id. § 102.20(m)

[20] Id.

diamonds do not effect the required change in tariff classification specified in section 102.20 of the Customs regulations that is necessary to confer origin in the country where the diamonds are cut and polished.

### D. The Rough Diamond Imparts The Essential Character To The Cut And Polished Diamond

Where the country of origin of a good cannot be determined based on the hierarchy set forth in section 102.11(a) of the regulations, the determination must be based on the next rule in the hierarchy, which is set forth in section 102.11(b), which reads, in pertinent part, as follows:

> Except for a good that is specifically described in the Harmonized System as a set, or is classified as a set pursuant to General Rule of Interpretation 3, where the country of origin cannot be determined under paragraph (a) of this section:
>
> (1) The country of origin of the good is the country or countries of origin of the single material that imparts the essential character to the good . . .[21]

The NAFTA Marking Rules provide "Rules of Interpretation" to determine the single material that imparts the essential character of a good. The Rules of Interpretation, which are set forth in section 102.18 of the Customs regulations, state the following:

> (b)(1) For purposes of identifying the material that imparts the essential character to a good under § 102.11, the only materials that shall be taken into consideration are those domestic or foreign materials that are classified in a tariff provision from which a change in tariff classification is not allowed under the § 102.20 specific rule or other requirements applicable to the good. For purposes of this paragraph (b)(1):

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[21] Id. § 102.11(b)(1).

> (iii) If there is only one material that is classified in a tariff provision from which a change in tariff classification is not allowed under the § 102.20 specific rule or other requirements applicable to the good, then that material will represent the single material that imparts the essential character to the good under § 102.11.[22]

The regulations provide that, for purposes of identifying the material that imparts the essential character to a good, the only materials that shall be considered are those materials that are classified in a tariff provision from which a change in tariff classification is not allowed under the specific rule in section 120.20 applicable to the good. Moreover, if only one material meets this criterion, then that material will represent the single material that imparts the essential character to the good.

When it published the final NAFTA Marking Rules in 1996, Customs responded to an interested party's request for clarification "as to whether the country of origin of a single component which has not undergone the applicable change in tariff classification will always be found to impart the 'essential character' to the product."[23] Customs responded in the affirmative, stating:

> In response to the question of whether, if there is only one component in a good which is classified in a provision from which a change in tariff classification is not allowed under the §102.20 rule, that one component always will determine the country of origin, the answer is yes for the following reason. The specific tariff (tariff shift in most cases) rules were developed with the specific view of not allowing a change in tariff classification from materials that can impart the essential character to the good. *In those instances in which the tariff shift rule excludes a particular tariff provision,*

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[22] Id. § 102.18(b)(1)(iii).

[23] *Rules for Determining the Country of Origin of a Good for Purposes of Annex 311 of the North American Free Trade Agreement*, 61 Fed. Reg. 29,932, 28,938 (June 6, 1996).

> *Customs has determined that the processing required to shift from the tariff provision to the provision for the good is not, in itself, sufficient to result in a change in the essential character of the materials classified in the provision from which a change is not allowed.* Therefore, unless the good is classified as a set, if a good is made from a single material that is classified in a tariff provision from which a change is not allowed, the single material will be found under §102.11(b) to impart the essential character to the good, and the country of origin of that material will be the country of origin of the good under Part 102.[24]

Thus, from the outset of its administration of the NAFTA Marking Rules, Customs made clear that it is impossible for the essential character of a good containing a single component to be imparted by anything other than that single component if that component is classified in a tariff provision from which a change in tariff classification is not allowed under section 102.20. The tariff shift provisions of section 120.20 determine, for purposes of the NAFTA Marking Rules, the level of processing that is sufficient to change the essential character of a single material. If a the tariff shift provisions are not satisfied, then the essential character of a single material has not changed.

Several published rulings illustrate Customs' interpretation of this rule. For example, in a ruling involving the country of origin marking of metal tubes manufactured in the United States and exported to Mexico for bending, cutting, and polishing prior to importation of the finished tubes into the United States,[25] Customs found that there was no applicable change in tariff classification within the requirements of section 120.20. Thus, Customs was required to determine the essential character of the finished product under section 102.11(b). Applying the Rules of Interpretation, Customs stated:

> Because the finished metal tube consists of only one material, and because that material is classifiable in a tariff provision from which a change in tariff classification is not allowed under the applicable rule in 19 CFR 120.20(o), the U.S. origin

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[24] Id. at 23,938 (*emphasis added*).

[25] HQ 560038 (Feb. 7, 1997).

> tube is the single material which imparts the essential character to the finished good pursuant to section 102.18(b)(iii).[26]

Accordingly, because the single material constituting the finished product was U.S. origin and did not undergo an applicable change in tariff classification in Mexico, Customs determined that the finished product imported into the United States was U.S. origin under the NAFTA Marking Rules.

Similarly, in a ruling involving the marking of footwear assembled from Canadian components in China,[27] Customs recently found that the Canadian components (rubber boot bottoms) did not undergo an applicable tariff shift in China. Applying the Rules of Interpretation, Customs determined that the Canadian rubber boot bottoms imparted the essential character to the finished product. Accordingly, the country of origin of the finished product under the NAFTA Marking Rules was Canada, and the product was required to be marked "Made in Canada" upon entry into the United States.

A Customs "Informed Compliance" publication on the application of the NAFTA Marking Rules to imports of monumental and building stone is also instructive.[28] In that publication, Customs applied the NAFTA Marking Rules to determine the country of origin of stone (*e.g.*, marble or granite) that is quarried in one country and cut and polished in another country. In all cases, when the processing of the stone in a third country was insufficient to result in a change in tariff classification under section 120.20 of the NAFTA Marking Rules, Customs determined that the rough stone imparted the essential character of the finished product and that, therefore, the country of origin was the country in which the stone was quarried.

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[26] Id.

[27] NY H8691 (Jan. 29, 2002)

[28] U.S. Customs Service, *What Every Member of the Trade Community Should Know About: NAFTA Country of Origin Rules for Monumental & Building Stone* (December 1999) (available for downloading at http://www.customs.ustreas.gov/imp-exp1/comply/icp.htm).

Customs has published numerous additional rulings under the NAFTA Marking Rules in which it was necessary to determine the component that imparted the essential character to the imported merchandise. Customs uniformly has applied the Rules of Interpretation to find that, if there is only one material in a good that is classified in a tariff provision from which a change in tariff classification is not allowed under the §102.20 rule, that one component will *always* determine the country of origin.[29]

In this case, rough diamonds will be exported to a third country, where they will be cut and polished prior to entry into the United States. No materials will be added to the rough diamonds in the third country. Thus, the product consists of one material. That one material will not undergo a change in tariff classification that is allowed under section 120.20(m). Thus, Customs has determined that cutting and polishing a rough diamond are not sufficient acts to result in a change in the essential character of the product under the NAFTA Marking Rules. Under the Rules of Interpretation for determining the essential character of a product, the single material that imparts the essential character to a cut and polished diamond is the rough diamond. Accordingly, diamonds mined in Canada and cut and polished in a third country are of Canadian origin under the NAFTA Marking Rules and must be marked "Made in Canada" when imported into the United States.

## III. CONCLUSION

The NAFTA Marking Rules provide a hierarchy of rules for determining the country of origin of merchandise produced within the NAFTA territory. At each step in the analysis required by the NAFTA Marking Rules, application of the rules to the facts of this case indicate that diamonds mined in Canada and cut and polished in a third country are deemed to be of Canadian origin. First, such diamonds are "wholly obtained or produced" in Canada, based on Customs' definition of that term. Second, such diamonds are of Canadian origin because they are produced exclusively from Canadian materials, with no "foreign materials" added at any stage of production. Third, cutting and polishing in a third country does not result in an applicable tariff shift, which would, if satisfied, confer origin in the third country. Fourth, under Customs' regulations, as applied in numerous recent rulings, a diamond mined in Canada clearly imparts the

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[29] *See, e.g.*, HQ 962603 (May 14, 2002); HQ 561736 (June 22, 2001); NY G86713 (Feb. 8, 2001); HQ 561823 (Sept. 14, 2000); HQ 561074 (Jan. 15, 1999); HQ 735363 (July 18, 1994).