

United States International Trade Commission

**THE CONCEPTS AND PRINCIPLES
WHICH SHOULD UNDERLIE
THE FORMULATION OF AN
INTERNATIONAL COMMODITY CODE**

Draft Report on Investigation No. 332-73

**to Both Houses of the Congress and to the President Pursuant
to Section 608(c)(1) of the Trade Act of 1974**

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UNITED STATES INTERNATIONAL TRADE COMMISSION

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INTRODUCTION

This report to both Houses of the Congress and to the President on the concepts and principles which should underlie the formulation of an international commodity code has been prepared in connection with U.S. International Trade Commission Investigation No. 332-73, initiated on February 4, 1975, in accordance with section 608(c) of the Trade Act of 1974 (Pub. L. No. 93-618, approved January 3, 1975). That section directs the Commission to undertake an investigation under section 332(g) of the Tariff Act of 1930 (19 U.S.C. 1332(g)) which would provide the basis for--

(1) a report on the appropriate concepts and principles which should underlie the formulation of an international commodity code adaptable for modernized tariff nomenclature purposes and for recording, handling, and reporting of transactions in national and international trade, taking into account how such a code could meet the needs of sound customs and trade reporting practices reflecting the interests of United States and other countries, such report to be submitted to both Houses of Congress and to the President as soon as feasible, but in any event, no later than June 1, 1975; 1/ and

(2) full and immediate participation by the United States International Trade Commission in the United States contribution to technical work of the Harmonized System Committee under the Customs Cooperation Council to assure the recognition of the needs of the United States business community in the development of a Harmonized Code reflecting sound principles of commodity identification and specification and modern producing methods and trading practices. 2/

1/ The U.S. International Trade Commission and the U.S. Department of Commerce are jointly conducting a related study pursuant to sec. 608(b) of the Trade Act of 1974 that will identify "the appropriate principles and concepts which should guide the organization and development of an enumeration of articles which would result in comparability of United States import, production, and export data."

2/ The Customs Cooperation Council (CCC) is presently undertaking a project to develop a Harmonized Commodity Description and Coding System (HCC) for use in facilitating (1) customs administration, (2) the analysis of trade information, and (3) the preparation and processing of

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The foregoing provisions reveal the interest of the United States in the international efforts already in progress under the aegis of the Customs Cooperation Council (CCC) in Brussels, Belgium to develop a modern international product nomenclature designed to meet the diverse customs, statistical, and transportation needs of the United States and other countries.

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transport documentation. The CCC, a 75-member intergovernmental organization with headquarters in Brussels, Belgium, was created to study problems of tariff classification, valuation, and customs administration. The responsibility for the formulation of the HCC has been assigned to the Harmonized System Committee (HSC). The following countries, economic union, and international organizations are members of the HSC:

Countries and Economic Union

Australia	India
Canada	Japan
Czechoslovakia	United Kingdom
European Community	United States
France	

International Organizations

Customs Co-operation Council (CCC) - Nomenclature Committee
Customs Co-operation Council (CCC) - Secretariat
Economic Commission for Europe (ECE)
European Trade Promotion Organizations Conference (ETPO)
General Agreement on Tariffs and Trade (GATT)
International Air Transport Association (IATA)
International Chamber of Shipping (ICS)
International Standard Organization (ISO)
International Union of Railways (UIC)
North Atlantic Treaty Organization (NATO)
United Nations Statistical Office (UNSO)

A. THE PROLIFERATION OF PRODUCT CLASSIFICATION SYSTEMS

Since the close of World War II, a significant number of product classification systems have emerged as instruments for regulating, recording, and measuring economic activity, both at national and international levels. At the national level product nomenclatures are used for the imposition of customs tariffs, the collection of data on imports and exports, the determination of freight charges for each mode of carrier, and the collection of statistics on the volume of domestic production and/or shipments. Some countries, including the United States, use separate systems for each specific purpose. Other countries have adopted the Brussels Tariff Nomenclature (BTN) and the Standard International Trade Classification (SITC) as the basis for the imposition of customs duties and the collection of data on imports and exports. These two systems have also been employed by a number of countries for collecting information on domestic production. However, where the BTN and SITC have been adopted, each country has created subheadings which frequently differ from those used in other countries, and even differ within each country depending upon the particular aspects of trade (imports, exports, domestic production) for which the system is used. In those cases where the international system has not been employed, concordances are used to report, in terms of the international system, data which were collected under a different system.

Since there is no universally accepted freight tariff classification system, each major mode of carrier maintains its own product code. The

codes employed for freight purposes are markedly different from one another and from those used for customs and statistical purposes.

The major existing classification systems contain significant differences in organization; in the scope of their product classifications, and in the application of interpretative rules, if any, governing these classifications. The methods employed to administer these systems also vary from consistently effective enforcement by qualified personnel to voluntary compliance without means for effective enforcement. Little effort has been made toward maintaining and improving many of these systems to take into account significant changes in economic conditions, technology, and commercial trading practices.

B. THE NEED FOR AN INTERNATIONAL COMMODITY CODE

The use of a multitude of different systems has several important, and often costly, consequences for both national and international trade. The use of discordant national systems for collecting and reporting data on imports, exports, and domestic production and the resulting lack of comparability in international trade data seriously hamper the analysis of trade and production information by trade analysts, economists, business planners, trade negotiators, and policymakers. It has been stated that "incompatible data are useless data." ^{1/} Concordances used to achieve comparability between different codes are not an adequate substitute for the collection and reporting of data under comparable systems, particularly where comparable information is sought at a detailed level of prod-

^{1/} Wassily Leontief, "Theoretical Assumptions and Nonobserved Facts," The American Economic Review. Vol. LXI, No. 1 (March 1971), pp. 1-7.

uct refinement. The difficulties associated with identifying product definitional and other differences between systems and in obtaining sufficient information to reconcile those differences make the use of concordances at their best an unreliable tool in economic analysis. These difficulties are further compounded by the fact that the various systems are ordinarily administered by different organizations or agencies with little or no opportunity for--or inclination toward--substantive coordination between them.

The multiplicity of codes for ship, plane, truck, and rail traffic, for customs tariffs, and for the collection of statistical data on trade also imposes considerable and unnecessary burdens upon traffic managers, freight forwarders, administrative officers, customs brokers, and others concerned with the planning of commercial shipments, the preparation and processing of related trade documentation, and the enforcement of customs and related laws. The difficulties associated with the repetitive reclassification of goods are particularly acute with regard to international shipments involving intermodal transport and the transshipment of goods through the customs territory of several countries. The great number of these codes and their lack of substantive comparability make efforts at introducing cost and time efficiencies in the movement of goods difficult and curtail the effective use of automated data-exchange systems for this purpose.

The benefits of an international commodity code adaptable for a number of generally compatible national and international uses may be summarized as follows:

1. The use of a single system as a base for the collection and reporting of relevant data on imports, exports, and production at the national level would--
 - (a) facilitate the publication of useful trade data;
 - (b) permit more reliable analysis of national trade information; and
 - (c) make feasible the implementation of a centralized and efficient program for the administration and authoritative and enforced interpretation of national systems.
2. The use of a single uniform commodity code adapted for national and international transport purposes could result in--
 - (a) the achievement of a substantial reduction in the costs and time spent in reclassifying goods as they move from the purview of one classification system to another, in the verification of product classifications, and in the administration, without consequent loss of effectiveness, of various classification systems; and
 - (b) the further standardization of transport documentation and the automated transmission of detailed product information by the use of a single product identification number throughout a commercial transaction.
3. The use of a single product code for international trade purposes would--
 - (a) permit the analysis of comparable international trade data;
 - (b) promote a greater degree of certainty and understanding in the negotiation, application, and interpretation of trade agreements; and
 - (c) relieve countries and organizations from the burdens of reporting trade data which were collected under different and discordant systems to international bodies or agencies.

C. CONCEPTS AND PRINCIPLES WHICH SHOULD UNDERLIE THE FORMULATION
OF AN INTERNATIONAL COMMODITY CODE

The difficulties in the formulation of an international commodity code are as manifest as the potential benefits. If completed and implemented, the code would be used by or be of benefit to a substantial cross section of transport, industrial, and governmental interests, including customs administrators, trade statisticians, analysts, economists, policymakers, carriers, importers, exporters, and manufacturers. Input from all these sources would, therefore, be necessary if the system is to satisfy, to the extent practicable, the multitude of interests concerned. The difficulties incident to recognizing numerous and diverse national interests are magnified when considering the formulation of a comprehensive code on an international level. Practical problems of formulation and subsequent implementation, such as reaching agreement on universally accepted product definitions, on terms which have uniformly recognized and understood meanings in international trade, on useful levels of product refinement and in conforming existing tariff systems, trade laws and regulations, and international agreements to the code, are significant.

In directing the Commission to report on the concepts and principles which should underlie the formulation of an international commodity code, the Congress indicated that the code should be "adaptable for modernized tariff nomenclature purposes and for recording, handling, and reporting of transactions in national and international trade" ^{1/} Thus, the code should serve three fundamental purposes: (1) It should be suitable

^{1/} Sec. 608(c)(1), Trade Act of 1974 (Pub. L. No. 93-618)(1975).

for use by various countries and customs unions for determining the rights and obligations of importers and exporters as to applicable rates of duty and other import and export restrictions and controls; (2) it should provide the basis for collecting detailed product data regarding each country's imports, exports, and production; and (3) it should facilitate the preparation and processing of transportation documentation.

A characteristic common to most product nomenclatures is that they are intended to capture and to differentiate in varying degrees of specificity the host of articles which enter into commerce. The key to successful development of the system, therefore, lies in the extent to which the products of commerce are set forth in sufficient detail within a complete, systematic, and administrable structure reflective of current and anticipated technologies of production and peculiarities of trade.

The concepts and principles which should underlie the formulation of an international commodity code suitable to satisfy the above purposes are commented on below.

1. It should be complete

The code must comprise a complete system of product descriptions or categories covering all articles of trade. The basic core or framework must provide for the appropriate classification of every known article, as well as articles yet to be developed, under either specific or general categories.

2. It should be systematic

The overall organization of the code is of critical concern since poor organization can make it unnecessarily complex and can unduly ob-

struct the use of the system. To the extent practicable, the various product categories should be systematically arranged in logical sequence and each individual product category identified with its own distinctive number. The organization and the numbering system should be as simple as possible and should be correlated. The use of a nonconsecutive numbering system should also be employed to permit new product classes to be inserted into the system in logical sequence and to avoid undue constriction in the number of possible provisions. A detailed alphabetical index and explanatory materials should also be provided.

3. It should constitute an enforceable legal document

It follows that the core or framework of the code must be organized and formulated as an enforceable legal document capable of adaptation to reflect import and export restrictions and controls and suitable for legislative enactment, administration by customs and transport officers, and judicial review.

4. It should consist of mutually exclusive provisions which are clearly stated

Each product should be provided for in the system in one, and only one, provision. Duplicative and overlapping product categories, although sometimes unavoidable, greatly complicate interpretation and should be kept to a necessary minimum and, then, with their classification priorities clearly expressed. In addition, the wording of the product categories and of the system or organizational framework within which they are set should be plain, clear, and unambiguous so as to insure the prompt classification of merchandise with reasonable certainty and predictability.

5. It should be capable of uniform application

The adoption of the code by a number of nations and organizations would render it a document of significant commercial importance. It is important therefore that it be capable of uniform application. To the extent practicable, articles should be properly classifiable within the system by reference to their intrinsic characteristics, without reliance upon extrinsic factors such as subsequent or intended use or the process of manufacture. In addition, the system should avoid the use of rules of interpretation which are not susceptible of uniform application and which thereby cannot yield uniformity of result.

6. It should conform to the realities of trade

The product distinctions explicitly or implicitly recognized in the system and the product definitions contained therein should be compatible with and reflect accepted international trade practices of product differentiation.

It is important in this respect to note that the objective of a single nomenclature for trade and transport purposes is a means to an end and not an end in itself. Its primary purpose is to improve the procedures for processing commercial transactions and to promote the collection of comparable trade information. These objectives cannot be realized solely from the universal use of the same system, for comparable but meaningless data are as useless as incomparable data. For this reason it is imperative that the code be developed as a modern system, reflective of existing and anticipated concepts of trade practice and responsive to sound principles of product definition and identification.

7. It should be simplified

Care should be taken not to complicate future administration or use by the promulgation of provisions which render the system unduly complex. In seeking the development of a complete system, consideration should be given to the ease with which classification decisions can be made.

8. It should be adaptable for individual uses

It is recognized that the needs to which the code are to respond differ depending upon (1) the specific purposes for which the system is to be applied, and (2) the requirements of the individual user. The code should, therefore, be adaptable to meet the individual requirements of potential users.

D. DEVELOPMENT OF AN INTERNATIONAL COMMODITY CODE

The current confusion arising from the many discordant product codes is not a basis for concluding that the solution lies in the creation of one comprehensive international product nomenclature that would automatically satisfy on a continuing basis the individual requirements of each and every user at both the national and international levels. To the contrary, the development of such a system appears to be impracticable. The differences in trade policy at the national level with respect to regulating imports and exports and obtaining relevant economic data to measure such trade will necessarily impose limitations on the degree of product refinement possible in the international product nomenclature. The refined product detail required for transportation documentation at the international level also introduces structural

nomenclature rigidity which is incompatible with the flexibility requisite to the implementation of requirements of national trade policy and trade analysis.

These conflicts might reasonably be resolved by the development of a basic international commodity code with, for example, four-digit item numbers for product classes to which (1) a national numerical suffix could be added for national trade purposes and (2) an international numerical suffix could be added to provide the necessary product detail for freight documentation purposes. There are distinct advantages to be gained from such an arrangement. The basic international code could be designed to reflect only that degree of product detail or refinement not incompatible with the diverse national trade requirements, thereby permitting each country to retain at the national level the flexibility to adapt the code to that country's unique needs through the use of appropriate national numerical suffixes. On the other hand, for freight documentation purposes, the greater requisite product detail could be provided at the international level with appropriate uniform numerical suffixes for use at both the national and international levels. The basic international code with its various national trade adaptations or suffixes and such nomenclature with its uniform transportation suffixes would require separate identification on invoices and other commercial documents to avoid conflict and confusion in their use.

The following illustrates how the basic international product nomenclature with four-digit item numbers may be adapted with two-digit suffixes for national trade purposes and also for use as an international transport nomenclature: 1/

National Trade Nomenclature		
International commodity code item	National trade suffix	Article description
7862	--	Widgets:
	10	Colored but not drilled.....
	20	Drilled, whether or not colored
	30	Other.....

International Transport Nomenclature		
International commodity code item	International transport suffix	Article description
7862	--	Widgets:
		Not packaged for retail sale:
	10	Oval or round.....
	15	Rectangular or square.....
	20	Other.....
		Packaged for retail sale:
	40	Rectangular or square.....
	80	Other.....

1. Organizational framework of the code

One of the primary considerations in the formulation of the system is organizing its provisions within a framework which permits its adaptability to individual needs and which facilitates its use.

1/ Nothing in the text or in this illustration is intended to suggest the number of digits which should be used in the basic international product nomenclature or in either the national trade suffixes or the international transport suffixes. In all cases, no more and no fewer digits than are essential to the purpose at hand should be utilized.

a. The major subdivisions or schedules.--The subdivision of complete product nomenclatures into a small number of broad, reasonably coherent and logical product schedules is common nomenclature practice that facilitates the user's ability to identify quickly the product classes of interest. The product content of each of the various schedules could be based upon such broad distinctions as the animal, vegetable, or mineral nature of the products, or their status as textiles, chemicals, metals, machines, electrical goods, and so forth.

If the number of these individual schedules is kept at less than 10, it may be possible--as a further assist to the user--to have the first digit of the product's item number the same as the number of the schedule in which the product is provided for. In addition, if there are, say, seven or eight schedules to the complete code, a country using it would be able to provide additional schedules at the national level for special and temporary classification provisions without increasing the number of digits in the basic product numbering system.

b. The benefits of a hierarchical or tabular arrangement.--Inasmuch as many differences in individual needs manifest themselves in the area of necessary levels of product refinement or detail, it is appropriate that the code be developed within a hierarchical or tabular arrangement in which areas of product distinction are initially set forth in broad product classes and subsequently refined in their detail by the creation of subclasses. The subclasses should exhaust, but not extend, the product coverage of the primary heading. The tabular arrangement of the system visually reveals to the user the interrelationships between coordinate and subordinate product headings and facilitates the user's ability to understand and interpret them.

The following illustrates how article provisions are set forth in a hierarchical or tabular scheme:

```

Wood pulp; rag pulp; and other pulps derived
from cellulosic fibrous materials and suitable
for papermaking.....
  Mechanically ground wood pulp, except screenings:
    Unbleached.....
    Other.....
  Chemical wood pulp, except screenings:
    Sulfite:
      Unbleached.....
      Other:
        Special alpha and dissolving
        grades.....
        Other.....
    Sulfate:
      Unbleached:
        Hardwood.....
        Softwood.....
      Other:
        Special alpha and dissolving
        grades.....
        Other:
          Hardwood.....
          Softwood.....
    Other.....
  Other.....
  
```

The use of a tabular system permits the creation of as many levels of product refinement as may be necessary to reflect individual needs.

c. The numbering system.--In the numbering of the article provisions in the system, it is desirable that the use of numerical suffixes be employed to reflect the classification of merchandise at the refined level. An example follows:

```

123.  Metal coins
      40    Gold coins
      60    Silver coins
      80    Other
  
```

The code number for metal coins would be 123 while the number for gold coins would be 123.40, i.e., the five-digit number formed by appending

the two-digit suffix for gold coins to the three-digit number used to designate the primary or main heading..

The numbering arrangement should not employ more digits than necessary, since too many would increase the margin of error in reporting and would interfere with efforts to accommodate the numbering of further levels of detail that may be introduced at the national level. It is believed that a numbering system in the basic international code which reflected more than one level of primary headings and one level of inferior headings (as illustrated above) would be too cumbersome to adequately accommodate further extension required for national needs. In addition, during the formulation of the basic international nomenclature, effort should be made to maintain a reasonable balance in the number of provisions at each desired level in order to make the most efficient use of the numbering system.

2. The development of product classes

The article provisions contained in the code can be prepared only after a diligent factual investigation by qualified experts. For this purpose, it will be necessary to consult with experts from the world trade community. It is clear that the development of a sound and commercially responsive nomenclature constitutes a highly technical undertaking requiring a considerable amount of factual interchange between persons familiar with the subject matter. It is unlikely, therefore, that a suitable system can be developed through a process of formal meetings. Simply stated, a product code cannot be successfully "negotiated."

It is apparent that during the course of formulating the system problems will continually arise with respect to terminology, standards of product differentiation, and the extent of product refinement or detail which should be recognized at the international level. The inability to resolve these differences would undoubtedly undermine the purposes of the system. Under the circumstances, each potential user must be willing to accept a reasonable degree of accommodation and compromise in the formulation of the system.

3. International body or agency for the development of the code

The breadth of potential applicability of the code necessitates its development under the auspices of an international body or agency whose staff is competent to deal with the technical matters involved and whose membership represents a reasonable geographic and economic cross section of the trading world. The organization should have at its disposal an experienced technical staff which would be responsible for the preparation of drafts of the code.

As noted previously, many of the major existing commodity codes contain significant differences in organization and product classification treatment, undoubtedly as a result of each having been formulated in order to serve its own unique and individual purposes. No existing code, therefore, can fully accommodate the individual needs presently being satisfied by the multitude of existing systems. Under the circumstances, a code suitable for adaptation at national and international levels for customs, statistical, and transport purposes should be formulated as a

new system to insure its responsiveness to the uses for which the code is intended to be employed. Although existing systems may be generally discordant, many evidence useful elements of organization, systematicness, and descriptive technique. Thus, no existing system should be overlooked in the search for useful provisions and techniques for designing and developing the desired international product nomenclature.

4. Process of formulation

The course of the development of the code should include the following:

1. An agreement on standards and guidelines which should control the development of the code.
2. An agreement on an overall organizational outline of the code and its numbering scheme.
3. For each major segment of the code, the convening of groups of experts to prepare initial drafts including appropriate explanatory materials and the adaptations necessary to assimilate freight tariff codes.
4. A period for review and comment by potential users.
5. Examination by technical staff of submitted comments and, when appropriate, the preparation and submission of further drafts.
6. Periodic plenary sessions to review progress.

It is recognized that, as work proceeds, the technical working group by common assent may develop techniques for expediting the work on the product code to insure its completion and adoption at the earliest practicable date.

E. MAINTENANCE AND ADMINISTRATION OF THE INTERNATIONAL CODE

Under the best conditions, unintended and anomalous classifications occur when the realities of trade have been overlooked or misinterpreted in the framing of product categories, or when new products are introduced after the system has been made effective. In addition, it is apparent that once the system is implemented, differences of opinion will arise among the various users as to the classification of specific articles under the system. Differences in the interpretation and application of the system result in inconsistency of classification treatment, which undermines the purposes of a uniform code. Under the circumstances, it is essential that administrative machinery be created for the purposes of (1) achieving uniformity in the application of the system and (2) according periodic, if not continuous, review of the code in order to keep its provisions reflective of technological progress in trade.

At the national level, suitable procedures and facilities would have to be established to provide for the centralized administration of the code and to consider the desirability of proposed amendments to improve the system. In addition, an international supervisory body should be created for the same purposes. The responsibility of this international body should be governed by the terms of a formal convention to insure that the system is properly maintained and kept up to date.

F. FURTHER CONSIDERATIONS

The uniform application of an international commodity code adapted for customs, statistical and transport purposes would represent a significant development toward facilitating trade and trade analysis. However, it would not satisfy all the needs incident to the availability of comparable trade data. During the development of the basic international nomenclature, the related matters of the application of uniform systems of measurement and valuation should not be overlooked.