

June 10, 1998

UNITED STATES INTERNATIONAL TRADE COMMISSION
Washington, DC 20436

MEMORANDUM TO THE COMMITTEE ON FINANCE OF THE UNITED STATES
SENATE ON PROPOSED TARIFF LEGISLATION¹

Bill no., sponsor, and sponsor's state: S. 1854 (105th Congress), Senator Thurmond (SC).

Companion bill: H.R. 3507 (105th Congress), Representative Spence (SC).²

Title as introduced: To suspend temporarily the duty on certain electrical transformers for use in the manufacture of audio systems.

Summary of bill:³

The bill would suspend through December 31, 2002 the general rate of duty on certain electrical transformers for use in the manufacture of audio systems. These goods fall in subheading 8504.31.40 of the Harmonized Tariff Schedule of the United States (HTS).

Effective date: The 15th day after enactment.

Retroactive effect: None.

Statement of purpose:

Senator Thurmond made a statement for the *Congressional Record* (March 24, 1998, pp. S2489-90) when he introduced the bill. He indicated that electrical transformers and other parts used to manufacture audio loudspeakers are currently being imported into the United States and that the U.S. tariffs on these parts may be eliminated as part of the Information Technology Agreement II that is being negotiated under the auspices of the World Trade Organization. The statement went on to indicate that suspending the duties on these parts would enable a South Carolina industry to be competitive in world markets.

¹ Industry analyst: John Cutchin (202) 205-3396; attorney: Jan Summers (202) 205-2605.

² The House bill would suspend the general rate of duty through the end of 2001.

³ See appendix A for definitions of tariff and trade agreement terms.

Product description and uses:

Transformers: A transformer is an electrical device used to transfer electrical energy from one alternating-current circuit to another by means of magnetic coupling. A typical transformer consists of two or more coils of insulated electrical conductors (e.g., the input and the output winding⁴) that are arranged (wound) around a laminated core of iron or steel sheets, so that a current flowing through the input winding produces an electrical current in the output winding via magnetic induction. Depending upon the number of turns (revolutions) in the input and output winding⁵ and their proximity to each other, a transformer can raise or lower the input voltage or current, or change the phase angle, impedance (opposition of a circuit to current flow), or voltage insulation level of the input current. In audio applications, transformers are principally employed to lower standard residential, commercial, or industrial line voltage from 220/110 volts to voltages of from 3 to 48 volts. Transformers may also be used within an audio device to raise or lower this second range of voltages to a level required by an individual audio component.

Tariff treatment:⁶

<u>Product</u>	<u>HTS subheading</u>	Col. 1-general <u>rate of duty</u>
Certain transformers.....	8504.31.40	6.6% ⁷

Structure of domestic industry (including competing products):

Certain transformers: Transformers: U.S. producers that manufacture transformers for use in audio systems are a specialized subset of SIC industries 3612--Power, Distribution, and Specialty Transformers--and 3677--Electronic Coils, Transformers, and Other Inductors. In general, this industry segment is composed of a large number of relatively small companies that each produce a fairly narrow line of low voltage (under 250 VA) transformers for very specific applications, along with a smaller group of medium- to large-size companies that supply high volumes of high-labor-content, commodity-type transformers. These types of transformers are either assembled in Mexico from U.S. and foreign-made components or sourced from low-wage-rate suppliers in the Pacific Rim (notably China, Taiwan, and Hong Kong).⁸

⁴There can be multiple output windings used in conjunction with the input winding.

⁵For example, if there are 100 turns in the input winding and only 50 in the output winding the incoming voltage level will be reduced by one-half. The reverse is true when the output winding has more turns than the input winding.

⁶See appendix B for column 1-special and column 2 duty rates.

⁷This rate of duty was "bound" at this level during the Uruguay Round of multilateral trade negotiations, so that no staged reductions in the U.S. rate of duty are scheduled.

⁸U.S. imports under HTS subheading 8504.31.40 totaled \$302 million in 1997. Imports from Mexico accounted for 52 percent of the total, compared with 10 percent for China, 7 percent for Taiwan, and 6 percent each for Hong Kong and Japan.

Altogether, some U.S. industry sources have indicated that as many as 1,500 commercial concerns may be engaged in the production of various types of custom-designed or commodity-type transformers with audio applications.⁹ Very few of these companies, however, have annual sales approaching \$10 million; audio equipment sales would generally represent only a small portion of their total business.

Private-sector views:

The Commission contacted six companies that produce the subject transformers and a trade association that represents numerous additional U.S. producers.¹⁰ As of the date of preparation of this report, one of these companies (Prem) had submitted a formal response to the Commission's inquiries (see appendix C).

U.S. consumption:

Certain transformers:	<u>1995</u>	<u>1996</u>	<u>1997</u>
	-----(\$1,000)-----		
U.S. production.....	(1)	(1)	(1)
U.S. imports.....	234,097	241,852	301,788
U.S. exports.....	57,553	75,224	72,920
Apparent U.S. consumption.....	(1)	(1)	(1)

¹Not available; due to the fragmented nature of the U.S. industry, the large number of very small U.S. producers that do not report their operations, the lack of statistical detail to identify specific applications and power ratings, and the considerable amount of final assembly performed by U.S. producers abroad, no meaningful official or privately-gathered statistical data exist on U.S. production or shipments of transformers rated at less than 1 kVA for use in the manufacture of audio systems.

Principal import sources: Mexico, China, Taiwan, Hong Kong

Principal export markets: Canada, Singapore, Philippines, Mexico

⁹Telephone conversations with U.S. industry representatives during May 12-14, 1998.

¹⁰Mid Wesco Enterprises, Chicago, IL; Cramer Coil and Transformer Co., Inc., Saukville, WI; Northlake Engineering, Inc., Bristol, WI; Lenco Electronics Inc., McHenry, IL; Prem Magnetics Inc., McHenry, IL; Custom Magnetics Inc., North Manchester, IN; and PCPCI--The Transformer Association, Sherborn, MA. All contacts were made during May 12-14, 1998.

Effect on customs revenue:¹¹

Future (1998-2002) effect:¹² Total customs revenue loss exceeding \$20 million (assuming 6 months of duty suspension during 1998).

1998	$(\$153,000,000 \times 40\%) \times 6.6\% = \$4,039,200$ [Monthly estimated loss = \$336,600]
1999	$(\$160,650,000 \times 40\%) \times 6.6\% = \$4,241,160$
2000	$(\$168,682,500 \times 40\%) \times 6.6\% = \$4,453,218$
2001	$(\$177,116,625 \times 40\%) \times 6.6\% = \$4,675,879$
2002	$(\$185,972,456 \times 40\%) \times 6.6\% = \$4,909,673$

Retroactive effect: None.

Technical comments:

As presently worded, the “end use” terminology (transformers “for use in the manufacture of audio systems”) in the proposed article description may be difficult for the U.S. Customs Service¹³ to administer. A particular transformer can be used in a variety of related electrical applications, so that any single use (such as with audio systems) would not preclude its use with unrelated electrical or electronic apparatus. Consequently, with no other defining parameters specified in the proposed nomenclature, it is conceivable that a significant volume of imported merchandise could be inappropriately entered under the duty suspension provision.

To assist in narrowing the scope of goods for which the suspension might be claimed, the Commission suggests (based upon conversations with industry representatives¹⁴) that the article description be amended to include only “transformers having a power handling capacity rated at less than 250 VA”, rather than the current “less than 1 kVA” (meaning 1,000 VA).

¹¹Actual revenue loss may be understated if a significant increase in imports occurs during the duty suspension period.

¹²The estimated level of U.S. imports in 1998-2002 is based upon a 5-percent annual increase in dutiable imports under HTS 8504.31.40, which totaled \$145.9 million in 1997. The 40-percent multiplier represents an estimate of the percentage of imports that will be entered as being “for use in the manufacture of audio systems.”

¹³The General Classification Branch of the U.S. Customs Service issued a memorandum in connection with the proposed language of new subheading 9902.85.xx on May 20, 1998 (appendix C).

¹⁴Telephone conversations of May 11, 1998, with officials of the Bose Co., Framingham, MA.

APPENDIX A

TARIFF AND TRADE AGREEMENT TERMS

In the **Harmonized Tariff Schedule of the United States** (HTS), chapters 1 through 97 cover all goods in trade and incorporate in the tariff nomenclature the internationally adopted Harmonized Commodity Description and Coding System through the 6-digit level of product description. Subordinate 8-digit product subdivisions, either enacted by Congress or proclaimed by the President, allow more narrowly applicable duty rates; 10-digit administrative statistical reporting numbers provide data of national interest. Chapters 98 and 99 contain special U.S. classifications and temporary rate provisions, respectively. The HTS replaced the **Tariff Schedules of the United States** (TSUS) effective January 1, 1989.

Duty rates in the **general** subcolumn of HTS column 1 are most-favored-nation (MFN) rates, many of which have been eliminated or are being reduced as concessions resulting from the Uruguay Round of Multilateral Trade Negotiations. Column 1-general duty rates apply to all countries except those enumerated in HTS general note 3(b) (Afghanistan, Cuba, Laos, North Korea, and Vietnam), which are subject to the statutory rates set forth in **column 2**. Specified goods from designated MFN-eligible countries may be eligible for reduced rates of duty or for duty-free entry under one or more preferential tariff programs. Such tariff treatment is set forth in the **special** subcolumn of HTS rate of duty column 1 or in the general notes. If eligibility for special tariff rates is not claimed or established, goods are dutiable at column 1-general rates. The HTS does not enumerate those countries as to which a total or partial embargo has been declared.

The **Generalized System of Preferences** (GSP) affords nonreciprocal tariff preferences to developing countries to aid their economic development and to diversify and expand their production and exports. The U.S. GSP, enacted in title V of the Trade Act of 1974 for 10 years and extended several times thereafter, applies to merchandise imported on or after January 1, 1976 and before the close of June 30, 1998. Indicated by the symbol "A", "A*", or "A+" in the special subcolumn, the GSP provides duty-free entry to eligible articles the product of and imported directly from designated beneficiary developing countries, as set forth in general note 4 to the HTS.

The **Caribbean Basin Economic Recovery Act** (CBERA) affords nonreciprocal tariff preferences to developing countries in the Caribbean Basin area to aid their economic development and to diversify and expand their production and exports. The CBERA, enacted in title II of Public Law 98-67, implemented by Presidential Proclamation 5133 of November 30, 1983, and amended by the Customs and Trade Act of 1990, applies to merchandise entered, or withdrawn from warehouse for consumption, on or after January 1, 1984. Indicated by the symbol "E" or "E*" in the special subcolumn, the CBERA provides duty-free entry to eligible articles, and reduced-duty treatment to certain other articles, which are the product of and imported directly from designated countries, as set forth in general note 7 to the HTS.

Free rates of duty in the special subcolumn followed by the symbol "IL" are applicable to products of Israel under the **United States-Israel Free Trade Area Implementation Act** of 1985 (IFTA), as provided in general note 8 to the HTS.

Preferential nonreciprocal duty-free or reduced-duty treatment in the special subcolumn followed by the symbol "J" or "J*" in parentheses is afforded to eligible articles the product of designated beneficiary countries under the **Andean Trade Preference Act** (ATPA), enacted as title II of Public Law 102-182 and implemented by Presidential Proclamation 6455 of July 2, 1992 (effective July 22, 1992), as set forth in general note 11 to the HTS.

Preferential or free rates of duty in the special subcolumn followed by the symbol "CA" are applicable to eligible goods of Canada, and rates followed by the symbol "MX" are applicable to eligible goods of Mexico, under the **North American Free Trade Agreement**, as provided in general note 12 to the HTS and implemented effective January 1, 1994 by Presidential Proclamation 6641 of December 15, 1993. Goods must originate in the NAFTA region under rules set forth in general note 12(t) and meet other requirements of the note and applicable regulations.

Other special tariff treatment applies to particular **products of insular possessions** (general note 3(a)(iv)), **products of the West Bank and Gaza Strip** (general note 3(a)(v)), goods covered by the **Automotive Products Trade Act (APTA)** (general note 5) and the **Agreement on Trade in Civil Aircraft (ATCA)** (general note 6), **articles imported from freely associated states** (general note 10), **pharmaceutical products** (general note 13), and **intermediate chemicals for dyes** (general note 14).

The **General Agreement on Tariffs and Trade 1994** (GATT 1994), pursuant to the Agreement Establishing the World Trade Organization, is based upon the earlier GATT 1947 (61 Stat. (pt. 5) A58; 8 UST (pt. 2) 1786) as the primary multilateral system of disciplines and principles governing international trade. Signatories' obligations under both the 1994 and 1947 agreements focus upon most-favored-nation treatment, the maintenance of scheduled concession rates of duty, and national treatment for imported products; the GATT also provides the legal framework for customs valuation standards, "escape clause" (emergency) actions, antidumping and countervailing duties, dispute settlement, and other measures. The results of the Uruguay Round of multilateral tariff negotiations are set forth by way of separate schedules of concessions for each participating contracting party, with the U.S. schedule designated as Schedule XX.

Pursuant to the **Agreement on Textiles and Clothing (ATC)** of the GATT 1994, member countries are phasing out restrictions on imports under the prior "Arrangement Regarding International Trade in Textiles" (known as the **Multifiber Arrangement (MFA)**). Under the MFA, which was a departure from GATT 1947 provisions, importing and exporting countries negotiated bilateral agreements limiting textile and apparel shipments, and importing countries could take unilateral action in the absence or violation of an agreement. Quantitative limits had been established on imported textiles and apparel of cotton, other vegetable fibers, wool, man-made fibers or silk blends in an effort to prevent or limit market disruption in the importing countries. The ATC establishes notification and safeguard procedures, along with other rules concerning the customs treatment of textile and apparel shipments, and calls for the eventual complete integration of this sector into the GATT 1994 over a ten-year period, or by Jan. 1, 2005.

Rev. 8/12/97

APPENDIX B

**SELECTED PORTIONS OF THE
HARMONIZED TARIFF SCHEDULE OF THE UNITED STATES**

(Appendix not included in the electronic version of this report.)

APPENDIX C

OTHER ATTACHMENTS

(Appendix not included in the electronic version of this report.)

105TH CONGRESS
2D SESSION

S. 1854

To suspend temporarily the duty on certain electrical transformers for use
in the manufacture of audio systems.

IN THE SENATE OF THE UNITED STATES

MARCH 24, 1998

Mr. THURMOND introduced the following bill; which was read twice and
referred to the Committee on Finance

A BILL

To suspend temporarily the duty on certain electrical
transformers for use in the manufacture of audio systems.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SUSPENSION OF DUTY ON CERTAIN ELEC-**
4 **TRICAL TRANSFORMERS FOR USE IN THE**
5 **MANUFACTURE OF AUDIO SYSTEMS.**

6 (a) IN GENERAL.—Subchapter II of chapter 99 of
7 the Harmonized Tariff Schedule of the United States is
8 amended by inserting in numerical sequence the following
9 new subheading:

“	9902.85.04	Electrical transformers having a power handling capacity less than 1 kVA for use in the manufacture of audio systems (provided for in sub-heading 8504.31.40)	Free	No change	No change	On or before 12/31/2002	”.
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1 (b) **EFFECTIVE DATE.**—The amendment made by
2 subsection (a) applies with respect to goods entered, or
3 withdrawn from warehouse for consumption, on or after
4 the 15th day after the date of enactment of this Act.

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