

## **THE TRADE AGREEMENTS ACT**

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As a follow-up to our last installment on federal contracting, this article focuses on one area of compliance that applies to most suppliers of goods to the U.S. Federal Government -- The Trade Agreements Act ("TAA").

### **Understanding the TAA**

The TAA applies to procurements of specified products by most federal agencies that have a dollar value exceeding \$194,000. For procurements to which it applies, the TAA supersedes the Buy American Act and governs the acquisition. Congress passed the TAA to comply with its responsibilities under the Agreement on Government Procurement ("AGP"), a multilateral agreement negotiated under the auspices of the General Agreement on Tariffs and Trade. The AGP is also commonly referred to as the Government Procurement Agreement. In short, the TAA requires federal agencies to treat the products of countries that have signed the AGP as favorably as American-made products. The Act also prohibits the purchase of products made in countries that have not signed the AGP.

In addition to the TAA, the United States Trade Representative has waived the Buy American Act and other discriminatory provisions for products from countries that have signed reciprocal trade agreements akin to the AGP. These reciprocal trade agreements are known as Free Trade Agreements ("FTAs") and include NAFTA (the North American Free Trade Agreement) and FTAs with Chile, Singapore and Australia, to name a few. FTAs often apply to procurements at a lower threshold. For example, the Australia FTA applies to a supply contract exceeding \$67,826, meaning that the Buy American Act is waived and products from Australia can be supplied under that particular contract without penalty.

The TAA and the FTAs together essentially classify products into three categories. First, a product is domestic if it has been produced in the U.S. Second, a product is a "designated country end-item" if it was manufactured in one of the many countries that have signed the AGP or an FTA. Third, a product is a "non-designated country end-item" if it was made in a country that has not signed the AGP or an FTA. For the purposes of the TAA and the FTAs, an item is manufactured where it was "substantially transformed" into the end product, even if its components parts were manufactured elsewhere.

If an offeror certifies that its products are manufactured in a non-designated country, then the agency is prohibited from buying those products in the absence of a waiver, which is rarely granted. In the meantime, U.S.-made and "designated country end-items" are treated equally, with no penalty added to the non-U.S. manufactured products.

### **Status of Various Countries under the Trade Agreements Act and FTAs**

There are approximately 100 countries which are considered designated countries under the various reciprocal trade agreements. If a country is not on this list, notably China for example, then the country is a non-designated country and products from that country may not be purchased in a federal procurement that exceeds the \$194,000 threshold. As a side note, GSA Schedule contracts have historically been treated as exceeding that threshold because GSA looks at the total value of all GSA Schedule contracts combined and not just the value of an individual GSA Schedule contract or individual order under any one contract.

### **The Substantial Transformation Test**

As noted above, an end item is manufactured where it was "substantially transformed" into the end product, even if its component parts were manufactured elsewhere. Thus, if a manufacturing process here in the United States or other designated country is deemed a

substantial transformation, then the country of origin for the manufactured product will be the United States or other designated country. A substantial transformation occurs when articles lose their identity and become articles having a new name, character or use.

In determining whether the combining of parts or materials constitutes a substantial transformation, the issue is the extent of operations performed and whether the parts lose their identity and become an integral part of the new article. In general, an assembly process will not constitute a substantial transformation unless the operation is "complex and meaningful", which depends on the nature of the operation, including the number of components assembled, number of different operations involved and whether a significant period of time, skill, detail, and quality control are necessary for the assembly operation. Thus the simple acts of attaching handles to pots or rubber soles to leather shoe uppers have been found not to constitute a substantial transformation. However, even more complex assembly operations, such as a 20-step assembly of a fan, have failed to meet the test because the parts were not physically altered, the assembly process did not require large amounts of skilled labor or specialized equipment, and the cost of the process was low. If we were to add soldering and galvanizing to the assembly process, then the likelihood of a substantial transformation finding increases significantly. Unfortunately, where the line is between substantial transformation and no substantial transformation is far from clear since each case is extremely fact dependant.

### **An Ounce of Prevention**

There are certain things a contractor could, and should, do to ensure compliance with the TAA and the FTAs, as applicable. For example, if you manufacture your own products, then first and foremost make sure the country in which they are manufactured is on the list. There are some countries that you would think would be on the list but aren't. For instance, Australia, an

Iraq Coalition partner, was only added to the list just recently. If your products are manufactured in a country that is not on the list, then remove them from the contract immediately if possible. GSA, for the most part and to its credit, has been allowing contractors to quickly remove these items from GSA Schedules without further penalty.

If a product is not wholly manufactured in one country but perhaps is assembled in a country from parts of one or more countries, or involves various production stages in multiple countries, including one non-designated country, then you should analyze the entire manufacturing process to determine whether the process meets the substantial transformation test. Again, the substantial transformation test is very fact dependant, so it would be best to involve legal counsel in this process.

If you are a dealer selling the products of other manufacturers, you still have to be TAA compliant. That is, the responsibility rests with you, not the manufacturer, to produce TAA compliant goods. To protect yourself, we suggest that you ask the manufacturer to certify where the products were made and tell you of any changes.

Finally, once you have determined that the products are compliant, you should regularly check to make sure you are still compliant. This means periodically checking the list of designated countries to make sure your country of manufacture is still on the list and/or analyzing any changes in the product manufacturing process to ensure that the substantial transformation test is still being met.

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