

# **QUARTERLY BULLETIN**

**1983  
Volume 2**

**Bureau of Alcohol,  
Tobacco and  
Firearms**

**Department of the Treasury**



# Bureau Rulings

## Subpart A—ALCOHOL

**27 CFR Part 250.35: TAXABLE STATUS**

(Also 27 CFR Part 250.200)

*Distilled spirits produced in the United States and transferred to Puerto Rico for processing are articles produced in Puerto Rico within the meaning of 26 U.S.C. § 7652 if such distilled spirits have undergone a substantial change in identity.*

**ATF Rul. 83-4**

The Bureau of Alcohol, Tobacco and Firearms (ATF) has been asked whether distilled spirits originally produced in the United States and transferred to Puerto Rico for further treatment are articles produced in Puerto Rico within the meaning of 26 U.S.C. § 7652 under the circumstances described below.

Situation #1. Distilled spirits are produced in the United States at 190 degrees of proof and are transferred from the United States to Puerto Rico. The spirits are then subjected to a distillation process pursuant to which esters, aldehydes, and other contaminants are totally removed. The proof of the spirits may or may not be increased. The distilled spirits are then returned to the United States as neutral spirits grain or are charcoal filtered and then returned to the United States as vodka.

Situation #2. Distilled spirits are produced in the United States at more than 160 degrees of proof but less than

190 degrees of proof. Such spirits lack the characteristics attributed to whiskey, brandy, rum, or gin and are substantially neutral in character. The spirits are transferred from the United States to Puerto Rico and are then subjected to a redistillation process which increases the proof of the spirits to 190 degrees or above. The distilled spirits are then returned to the United States as neutral spirits.

Section 7652(a)(1), Title 26, United States Code, provides:

(1) Rate of tax. Except as provided in section 5314, articles of merchandise of Puerto Rican manufacture coming into the United States and withdrawn for consumption or sale shall be subject to a tax equal to the internal revenue tax imposed in the United States upon the like articles of merchandise of domestic manufacture.

Section 7652(a)(3) provides:

(3) Deposit of internal revenue collections. All taxes collected under the internal revenue laws of the United States on Articles produced in Puerto Rico and transported to the United States (less the estimated amount necessary for payment of refunds and drawbacks), or consumed in the island, shall be covered into the treasury of Puerto Rico.

The terms "articles of merchandise of Puerto Rican manufacture" as used in section 7652(a)(1) and "articles produced in Puerto Rico" as used in section 7652(a)(3) have the same meaning. *Commonwealth of Puerto Rico v. Blumenthal*, 642 F.2d 622 (D.C. Cir. 1980), cert. denied, 451 U.S. 983 (1981). As to the extent of treatment

necessary to constitute "manufacture," the Supreme Court has said:

Manufacture implies a change, but every change is not manufacture, and yet every change in an article is the result of treatment, labor and manipulation. But something more is necessary, as set forth in *Hartranft v. Wiegmann*, 121 U.S. 609. There must be transformation; a new and different article must emerge, "having a distinctive name, character or use." *Anheuser-Busch Brewing Association v. United States*, 207 U.S. 556, 562 (1908).

For tax purposes in order for distilled spirits originally produced in the United States to become "articles produced in Puerto Rico" after treatment in Puerto Rico, such spirits must undergo a substantial change in identity. Token treatment is not sufficient. The spirits must undergo substantial changes in taste, aroma and chemical composition. In short, a new and different article must emerge.

However, for labeling purposes, 27 C.F.R. § 5.36(a)(3) provides that a bottler who treats neutral spirits with activated carbon may, in lieu of the phrase bottled by, indicate on labels that the vodka was "produced by" such bottler.

In situation #1, the distilled spirits did undergo a change as esters, aldehydes and other contaminants were removed. However, the spirits were "neutral spirits" when they were shipped to Puerto Rico and "neutral spirits" when they were returned to the United States. See, 27 C.F.R. § 5.22(a). The changes in taste, aroma and chemical composition were not substantial. A new and different article did not emerge as the distilled spirits produced in the United States did not undergo a substantial change

in identity as a result of their treatment in Puerto Rico. *Held*, the distilled spirits transported to the United States are not articles produced in Puerto Rico within the meaning of section 7652(a)(3).

In situation #2, the distilled spirits originally produced in the United States were subjected to a redistillation operation in Puerto Rico that increased the proof of the spirits. Though the spirits were changed to the extent that there was a rise in proof, after redistillation the spirits still lacked the taste, aroma and other characteristics of whisky, brandy, rum, or gin, and were neutral spirits within the meaning of 27 C.F.R. § 5.22(a). Therefore, the changes in taste, aroma, and chemical composition were not substantial. A new and different article did not emerge as the distilled spirits produced in the United States did not undergo a substantial change in identity as a result of their treatment in Puerto Rico. *Held*, the distilled spirits transported to the United States are not articles produced in Puerto Rico within the meaning of section 7652(a)(3).

The provisions of section 7652(b), pertaining to the taxation of articles coming into the United States from the Virgin Islands, are in all essential aspects identical to the provisions of section 7652(a). Accordingly, this ruling applies to the classification of products entering the United States from the Virgin Islands.

Under the authority contained in 26 U.S.C. 7805(b), this ruling will be applied to distilled spirits redistilled in Puerto Rico as described herein after May 9, 1983.