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United Nations Conference on Trade and Development
Division for Africa, Least Developed Countries and Special Programmes (ALDC)

5th Meeting of the Continental Free Trade Area Technical Working Group on Rules of Origin

Lessons learned from WTO LDC negotiations on ad valorem percentage criteria

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Recalling Paragraph 1.3 of the Bali Decision

- Given the limited productive capacity in the LDCs, it is desirable to keep the level of value addition threshold as low as possible, while ensuring that it is the LDCs that receive the benefit of the preferential trade arrangements.

- It is noted that the LDCs seek consideration of allowing foreign inputs to a maximum of 75% of value in order for a good to qualify for benefits under LDC preferential trade arrangements.

- *Note: The precise percentage may vary depending on the calculation methodology used in different schemes.*

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Recalling Paragraph 1.1 of the Nairobi Decision

- Paragraph 1.1 of the Nairobi Decision requires preference-granting members ***"adopt a method of calculation based on the value of non-originating materials***".

- At the same, it allows ***"Preference-granting Members applying another method to continue to use it***", recognizing "***that the LDCs seek consideration of use of value of non-originating materials by such preference-granting Members when reviewing their preference programme."***

- It also requires the Preference-granting Members to consider developing or building "***on their individual rules of origin arrangements applicable to imports from LDCs, allowing the use of non-originating materials up to 75% of the final value of the product, or an equivalent threshold in case another calculation method is used, to the extent it is appropriate, and the benefits of preferential treatment are limited to LDCs*"** as well as "**consider the deduction of any costs associated with the transportation and insurance of inputs from other countries to LDCs."**

Questions

- What levels of threshold are WTO members using that are as low as possible, while ensuring that it is the LDCs that receive the benefits of the preferential trade arrangements?
- Which WTO Members are closer to the 75% threshold proposed by the LDCs ?
- What is a desirable level of percentage taking into account the global value chains (GVCs) ?
- Is it realistic to set a level of percentage that is not arbitrary or is it preferable to adopt another methodology for certain sectors ?

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Some Caveats

- The LDCs are not arguing that the percentage criterion is their preferred criterion to determine substantial transformation.
- The issue at stake is to determine a level of percentage that is commercially viable for businesses and investors taking into account GVCs
- Such level of percentage may vary depending on the sector at stake
- In some sectors and as recognized by the Decision the percentage criterion may not be the most appropriate method and other methods may be adopted.

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1. What levels of threshold are WTO members using ? (i)

Country / group of countries	Methodology	Numerator	Denominator	Level of Percentage	Yes / No	Distance from LDC proposed level
United States (GSP)	Value added by addition: direct costs of processing + value of originating materials	Cost of materials produced in preference-receiving country plus the direct cost of processing carried out there	Appraised value of the article at the time of entry into the United States	Minimum 35%	NOT using	10% + issue of freight and insurance and methodology of calculation
United States (AGOA)	Same as above with the exclusion of textiles and clothing	Same as above	Same as above	Minimum 35%	NOT using	10% + issue of freight and insurance and methodology of calculation

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1. What levels of threshold are WTO members using ? (ii)

Country / group of countries	Methodology	Numerator	Denominator	Level of Percentage	Yes / No	Distance from LDC proposed level
New Zealand	Value added by addition	Cost of materials + expenditures in other items of Factory or work cost in New Zealand or LDCs	Ex- factory cost	50%	Not using	25% + issue of freight and insurance
Australia	Value added by addition	"allowable factory cost"	Ex-factory cost	50%	Not using	25% + issue of freight and insurance
TPKM	Value added by addition	Production process	FOB price	50%	Not using	25% + issue of freight and insurance

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1. What levels of threshold are WTO members using ? (iii)

Country / group of countries	Methodology	Numerator	Denominator	Level of Percentage	Yes / No	Distance from LDC proposed level
European Union (EBA)	Maximum Value of non-originating materials	Value of non-originating material	Ex-works price	Maximum 70%	Yes	5% + issue of freight and insurance
Japan	Maximum Value of non-originating materials	Value of non-originating material	FOB price	Maximum 40%	Yes	35% + issue of freight and insurance
Canada	Maximum Value of non-originating materials	Value of non-originating material	Ex-factory price	Maximum 60% for LDCs, 80% with cumulation	Yes	Comply but :15% + issue of freight and insurance
Norway	Maximum Value of non-originating materials	Value of non-originating mat erial	Ex-works price	Maximum 70%	Yes	5% + issue of freight and insurance
Switzerland	Maximum Value of non-originating materials	Value of non-originating material	Ex-work price	70%	Yes	5% + issue of freight and insurance

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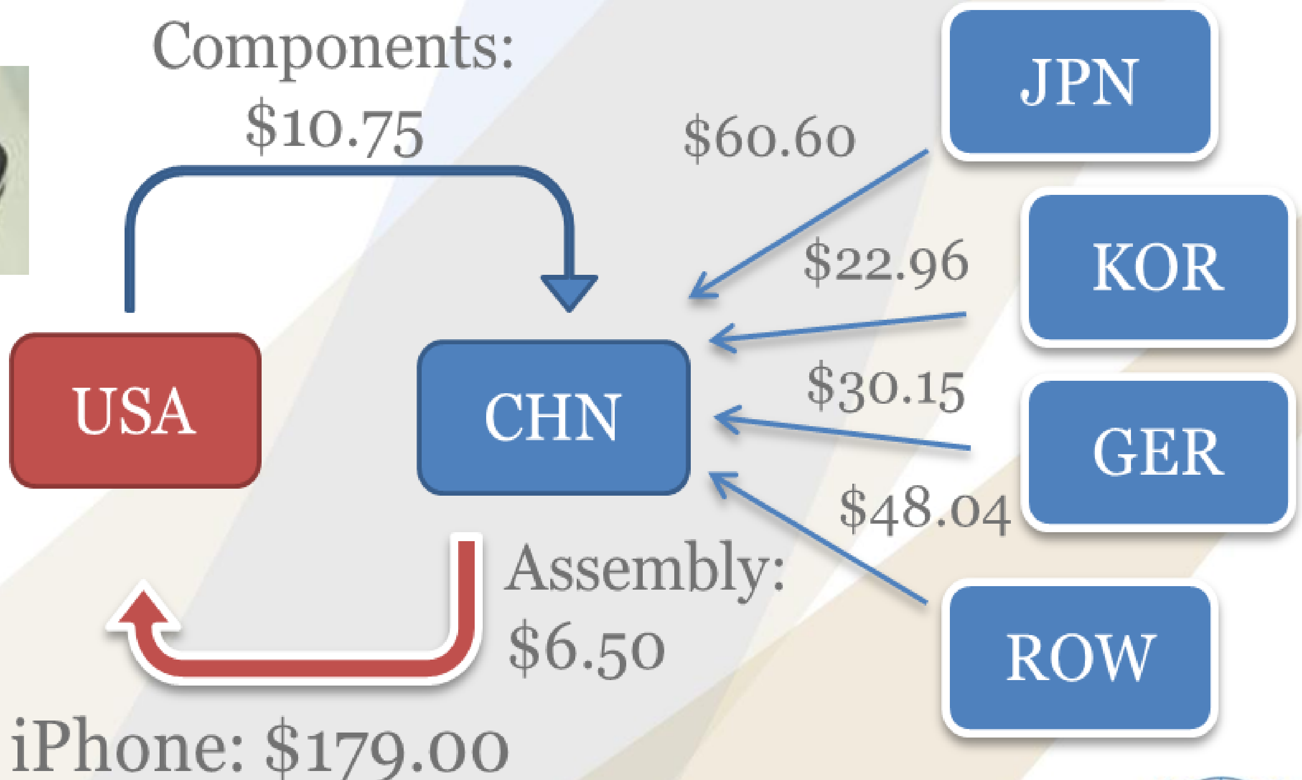
What levels of threshold are WTO members using ? (iv)

Country / group of countries	Methodology	Numerator	Denominator	Level of Percentage	Yes / No	Distance from LDC proposed level
Eurasia CU	Maximum Value of non-originating materials	Value of non-originating material	Ex-works price	Maximum 50%	Yes	25% + issue of freight and insurance
China	Calculation by subtraction of non-originating materials	FOB price minus value of non-originating material	FOB price	Minimum 40%	Yes	15% + issue of freight and insurance
India	Calculation by subtraction of non-originating materials	FOB price minus value of non-originating material	FOB price	Minimum 30%	Yes	5% + issue of freight and insurance
South Korea	Maximum Value of non-originating materials	Value of non-originating material	FOB price	Maximum 60%	Yes	15% + issue of freight and insurance
Thailand	Calculation by subtraction of non-originating materials	FOB price minus value of non-originating material	FOB Price	50%	Yes	25% + issue of freight and insurance

Level of percentage - Example: i-Phone

What is a desirable level of percentage taking into account the global value chains ?

Retail price:
$500.00
(Profit
margin:
64%)



Source: Xing and Detert, 2010

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Level of percentage - Example: i-Phone

What is a desirable level of percentage taking into account the global value chains ?

a)	*Material and components*	*172.5 €*
b)	*Direct costs of processing*	*6.5 €*
c)	*Profits producer (assumed ~8%)*	*14 €*
	Total cost (Ex-Works Price)	*193 €*

- *EU:* $\frac{VNOM}{EW} = \frac{(a)}{EW} = \frac{172.5}{193} = 89.4\ \% > 70\%$ → Non-Originating
- *CAN:* $\frac{VNOM}{EW} = \frac{(a)}{EW} = \frac{172.5}{193} = 89.4\ \% > 60\%$ → Non-Originating
- *USA:* $\frac{VOM+DCP}{EW} = \frac{(b)}{EW} = \frac{6.5}{193} = 3.4\ \% < 35\%$ → Non-Originating
- *LDCs:* $\frac{VNOM}{EW} = \frac{(a)}{EW} = \frac{172.5}{193} = 89.4\% > 75\%$ → Non-Originating

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What is a desirable level of percentage taking into account the global value chains ?

- **One lesson learned**: The EU carried out an impact assessment study and set the level at 70% of non originating materials: the new rule generated trade effects
- The experience and the examples show that the level of percentage vary depending on the industrial sectors
- Modern rules of origin contained in FTAs show that the percentage criterion is mostly used in combination with a CTC and is seldom used as a stand alone criterion
- The large majority if not the totality of FTAs does not use anymore a percentage criterion as a stand alone criterion

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Recommendations

– LDCs would recommend the following best practices:

1) Whenever it is used, the level of percentage should be calculated according to the LDCs proposal of not more than 75% of non originating materials out of the ex-works price with deduction of cost of insurance and freight

2) Notwithstanding this, in some sectors, other methodologies such as CTC and Specific working or processing may be used to better reflect the processing stages of the GVCs

3) The presentations on item (3), CTC, and Item (4), specific working or processing, will provide useful examples on alternative methodologies to define substantial transformations for those sectors

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Thank you for your attention

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