



**United Nations Conference on  
Trade and Development**

Division for Africa, Least Developed Countries  
and Special Programmes ( ALDC )

Government of  
the Netherlands



## Executive Training on Negotiating and Drafting Rules of Origin

### Measuring restrictiveness of RoO (1)

- Lessons learned from utilization rates
- Examination of LDC submission at the CRO

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# Background (I)

- Hong Kong Ministerial Decision on DFQF contained wording :
  - RoO need to be *"transparent and simple, and contribute to facilitating market access"*
- Between 2006 and 2013, LDCs proposals on rules of origin by Zambia (2007), Bangladesh (2011) and Nepal(2013)
- WTO Ministerial Decision on Preferential Rules of Origin (RoO) in 2013 entrusted the CRO with:
  - *"Review annually developments in preferential rules of origin applicable to imports from LDCs."*
  - Agenda item in the CRO: *"Intensify efforts in the CRO to exchange information regarding existing preferential rules of origin for LDCs."*

## Background (II)

- The Decision on preferential rules of origin for LDCs is a not binding decision, it provides guidelines.
- However Members agreed to have an agenda item to engage in a transparency and out-reach exercise on preferential rules of origin where a *"contribution to this dedicated agenda item would be the paper to be submitted by the LDCs about their specific challenges."*
- The CRO mandate is to review NEW or modified rules of origin.

# Current challenges and status of the Decision

- The world has changed: Globalization of production and emergence of global value chains
- MFN reductions lowering the preferential margins
- Limited recognition of extreme need to reform RoO for LDCs:
  - Changes in the Canadian RoO in 2003
  - EU reform of RoO entered into force in 2011
  - US GSP has not changed its RoO since 1974, nor Japan
- LDCs have little industrial base and certain RoO are demanding antiquated industrial processes

→ Can the Decision and discussions in CRO leverage additional reforms in RoO ?

# Starting points

- LDC Group does not argue for harmonizing RoO
- RoO should be trade creating permitting full utilization of trade preferences
- Change in RoO in EU and Canada have generated a market response in terms of FDI and trade flows

# Possible improvements

- Form

*"Way in which the RoO are written using different methodologies."*

- Substance

*– "Degree of restrictiveness of a RoO with respect to an existing value chain context."*

# Lessons learned from "form"

- Different *forms* to draft a RoO:
  - Change in tariff classification
  - Percentage criterion
  - Working or processing requirements
- Emergence of lessons learned and best practices on how to draft the *form* of a RoO using the percentage criterion

# Form: Percentage Criterion

Criterion	Calculation	Application or criterion
<b>Minimum amount of value added</b>	Percentage of direct processing + cost of local originating material out of ex-factory price	US GSP, AGOA, Australia, New Zealand
<b>Maximum amount of imported material</b>	Percentage of foreign inputs out of the ex-works price	EU EBA, Japan (Denominator: FOB price)
<b>Value of materials ("Build-down")</b>	Subtraction of the value of imported material from the ex-works price out of the ex-works price	US-CAFTA

# QUAD comparison

	EU EBA	JAPAN GSP	Canada GSP	US GSP	AGOA
<b>Numerator</b>	Value of non-originating materials	Value of non-originating materials	Value of non-originating materials	Cost of material of beneficiary developing country + direct processing cost	Cost of material of beneficiary developing country + direct processing cost
<b>Denominator</b>	Ex-works price	FOB price	Ex-factory price	Appraised value	Appraised article value
<b>Percentage level</b>	Maximum of 70% of imported inputs	Maximum of 40% or 50% of imported inputs	Maximum of 60%	Minimum of 35%	Minimum of 35%

- Major reforms by EU and Canada in 2011 and 2003, respectively.
  - EU: Increase the maximum allowance of foreign import to 70% and allow single stage transformation
  - Canada: Reduce the minimum limit of value added to 40%

- US GSP has not changed its RoO since 1974, neither Japan since the 70'.

# Issues of the Percentage Criterion

- **Limitations of the Percentage Criterion**
  - Affected by exchange rates
  - Level of percentage arbitrarily set
  - Cost of labor relatively cheap; turn asset into penalty
  - Requires accountancy expertise
- **Adequate percentage level**
  - Depend on the product and the production processes
  - Need to consult with the private sector

# Suggested practices (FORM)

- Percentage criterion for determining a substantial transformation:
  - Method Based on Value of Non-Originating Materials :

$$LVC = \frac{EW - VNM}{EW} \times 100$$

- Method Based on Value of Originating Materials :

$$LVC = \frac{VOM}{EW} \times 100$$

- Percentage level
  - 15-25% or even lower for certain product categories
- Transport costs
  - Percentage criterion-based rules should take costs of freight and insurance into account when determining value of materials
  - Especially for landlocked and islands LDCs

# Recording lessons learned using utilization rates

- Preferential RoO are industry-related
  - Example: European industrial context vs. context of Central Africa
- Commercial viability of RoO depends on the industrial context
- Market response of RoO in a given context can be seen in the **Utilization Rate**

# Recording lessons learned using utilization rates

- Two ways of collecting data on utilization rates
- Customs based : the ratio among goods eligible for FTA treatment with those that have effectively received it

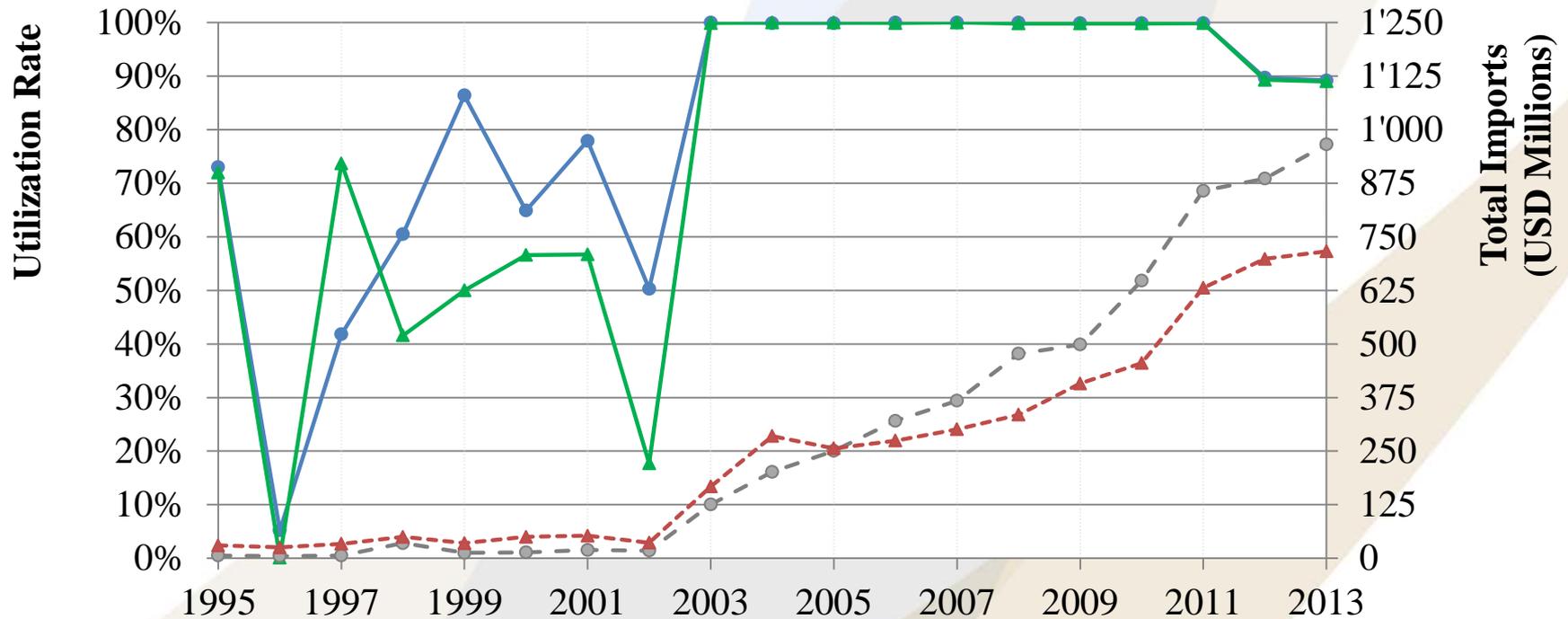
$$\text{Utilization rate} = \frac{\text{Imports receiving preferential treatment}}{\text{Imports covered by the preferential agreement}} * 100$$

- Companies questionnaires
- One difficulty:
  - Utilization rates by customs are not publically available for the majority of countries

# Trade effects of Canadian reform

## Canadian imports from LDCs and GSP utilization rates

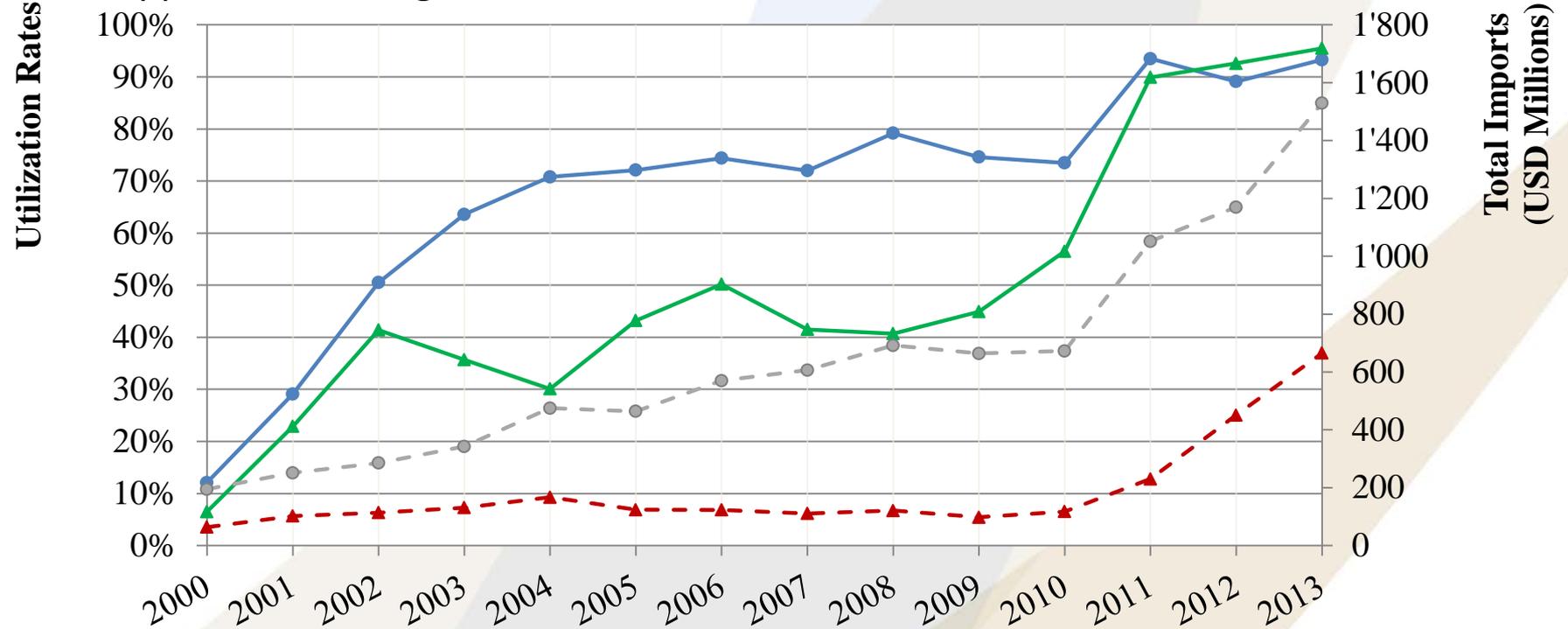
Art of apparel & clothing access, HS 61 knitted/crocheted and HS62 not knitted/crocheted



# Trade effects of EU reform

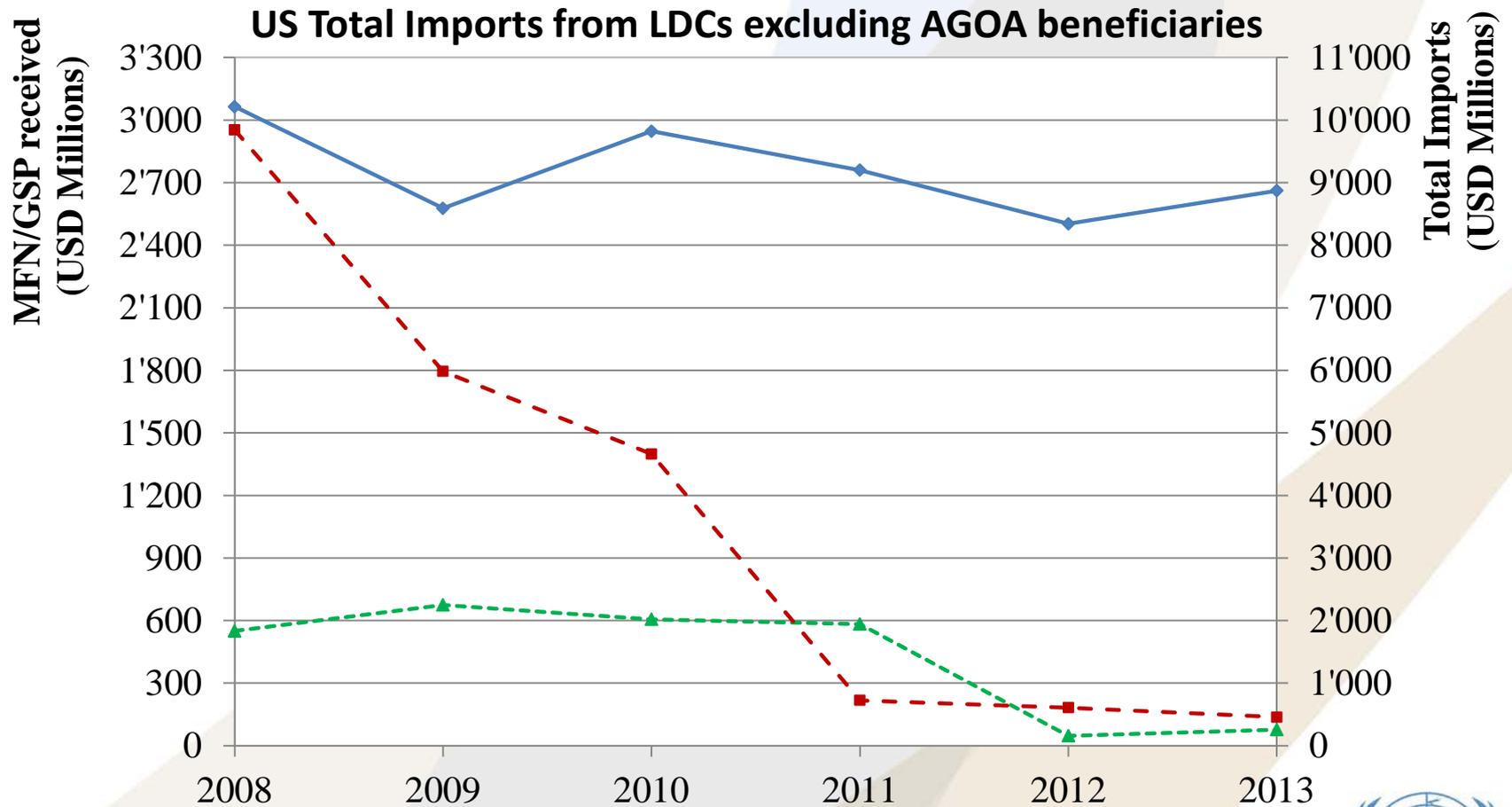
## EU imports from LDCs and GSP utilization rates

Art of apparel & clothing access, HS 61 knitted/crocheted and HS62 not knitted/crocheted



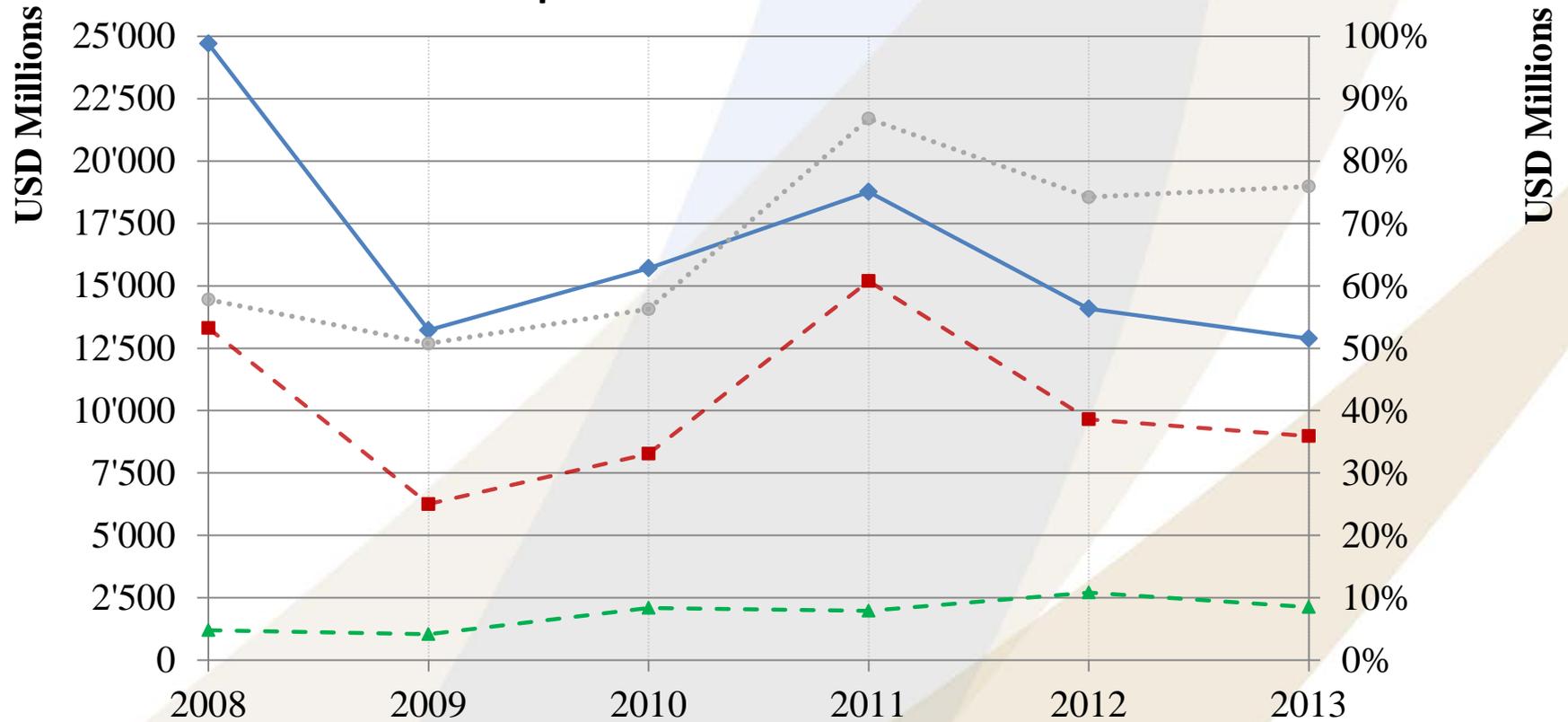
- Utilization Rate HS 61 (left axis)
- ▲— Utilization Rate HS 62 (left axis)
- -●- - Total Imports HS 61 (right axis)
- -▲- - Total Imports HS 62 (right axis)

# Utilization rate - US GSP



# Utilization rate - AGOA

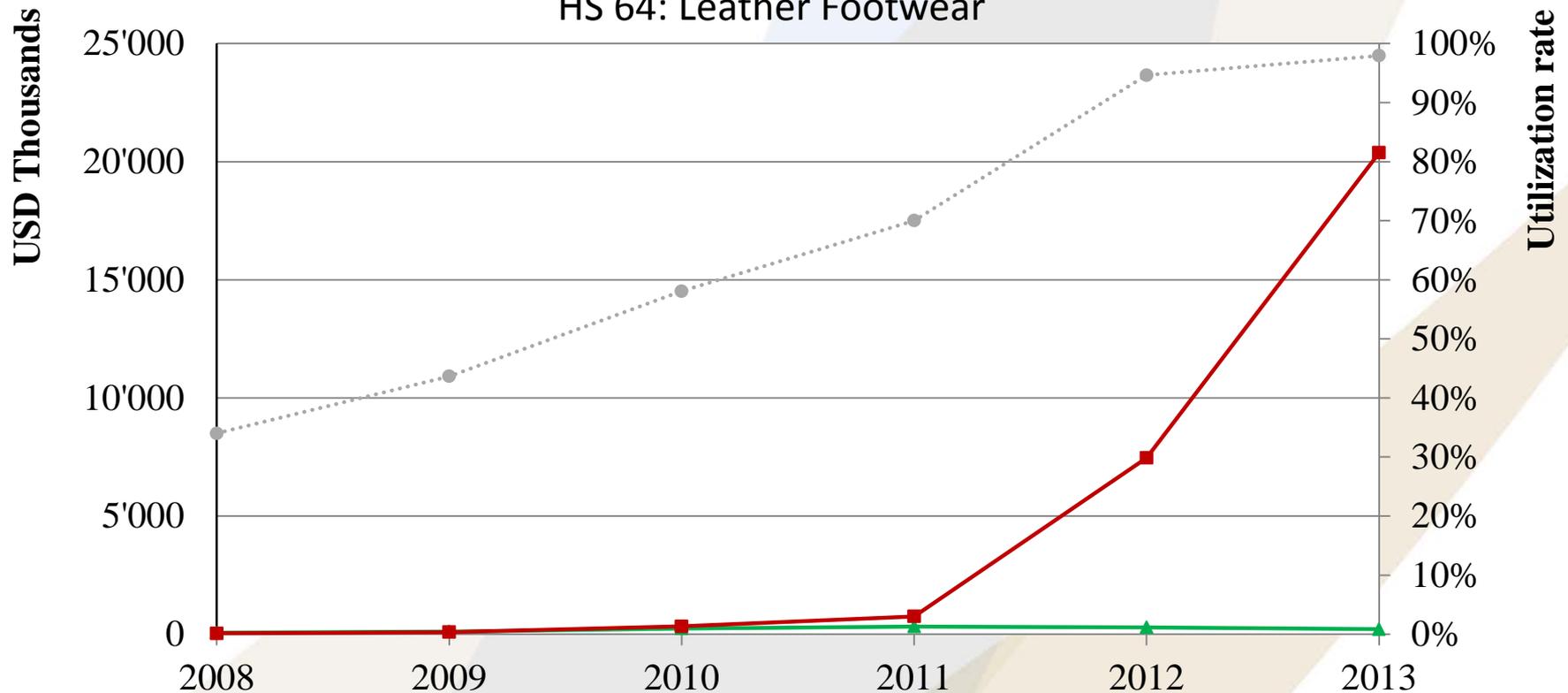
## US Total Imports from LDCs AGOA Beneficiaries



- ▲- MFN Received (left axis)
- AGOA Received (left axis)
- ◆- Total Imports (left axis)
- AGOA Utilization Rate (right axis)

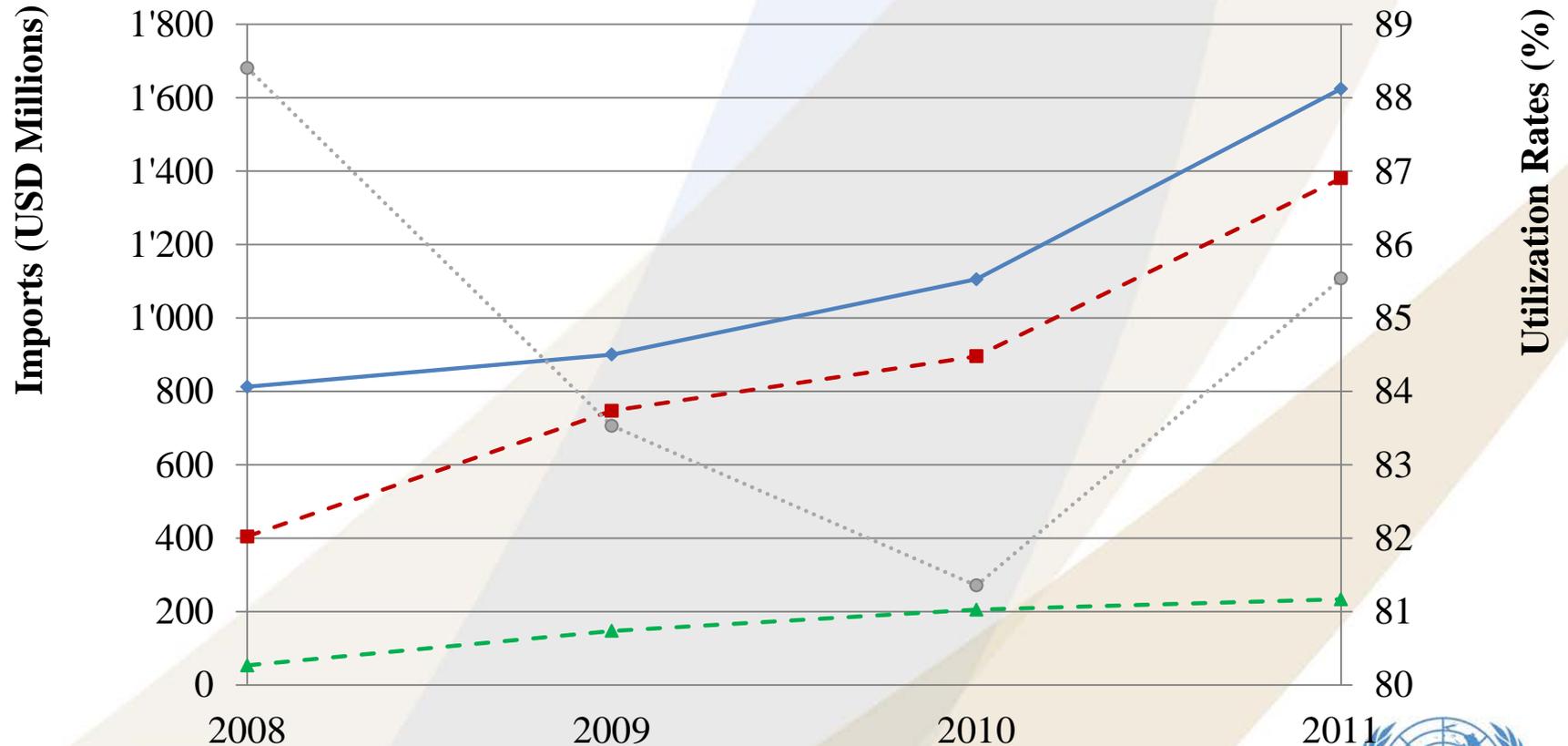
# Utilization rate - AGOA

US Total Imports from LDCs AGOA Beneficiaries  
HS 64: Leather Footwear



# Utilization rate - Japanese GSP

## Japanese Imports of Non-Agricultural Products from LDCs and Utilization Rates



# Suggested practices (SUBSTANCE)

- Reforms of RoO reflecting global value chains and commercial reality:
  - Robust evidence from EU and Canadian to engage in reform: Rise of utilization rates and overall imports
  - Unequivocal evidence that a market response in LDCs is generated
  - Forms of market response: Relocation of factories to LDCs, increased manufacturing capacity, more skilled jobs creation and backward linkages
- US and Japan as well as other preference giving countries are invited to consider appropriate reform of the *substance* and form of their rules of origin

# Future contributions by LDCs in form of papers to the next CROs

- Further Develop CTC concept according to the wording of the Decision
  - HS is not designed for RoO purposes
  - Identify product/sectors where simple CTC with/without exceptions could be used
- More research in setting appropriate levels of substantial transformation
  - Facilitate insertion into global value chains
- Research on best practices of certification requirements related to RoO
  - Avoid non-manipulation requirement for landlocked or island countries
  - Reduce costs related to certification requirements: Share experience on lessons

**Thank you for your attention**

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