



United Nations Conference on Trade and Development

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

Government of the Netherlands



Drafting rules of origin

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21 April Florence ,Italy

The issues we wish to address

- There is not a model of drafting Rules of origin (RoO)
- In spite of a number of studies there is no evidence on the best method for origin determination, the best level of percentage and the best practices for certification
- There are a number of lessons learned...



The determinants in defining the substantive requirements of preferential RoO

- To ensure that benefits are confined to products genuinely manufactured in the parties and avoid trade deflection
- RoO should be matching the existing manufacturing capacity.
Excessive stringency = low utilization and distortions on supply chains



Parameters for designing an FTA Model RoO

A) Index of restrictiveness:

RoO should reflect actual manufacturing ensuring sourcing from most efficient suppliers

B) Index of technical soundness:

RoO should be technically sound, producing the same outcome, transparent, easy to administer and to comply with



The Technical methods to draft RoO

- Kyoto conventions divide products in two categories
- Wholly obtained products defined in a « standard» list
- Products with non-originating inputs: Substantial transformation
- *Defining the indefinable:* How to determine substantial transformation ?



Defining substantial Transformation: Menu 1.0

1) Percentage criteria based on

- a) value added
 - i) by addition
 - ii) by subtraction
- b) Max import content
- c) value of materials based on ex-works, FOB price

2) Change of tariff classification:

- a) CTH, CTH with exceptions,
- b) Tariff shift at CTSH with exceptions and regional value content

3) Specific working or processing:

Manufacture from ...



Some Criteria for defining substantial transformation: Menu 2.0

- Across the board criteria,
- Across the board with selected product specific
- Product specific only



Some preliminary technical points and principles

- Alternative rules may be devised but have to be co-equal in terms of stringency
- 35% value added and simple CTH are not co-equal
- Change of tariff classification implies a tariff line approach
- In some cases simple CTH or CTSH is extremely liberal, in others cases, extremely stringent



HS is not designed for origin purposes

- Fresh vegetables 0701 Dried vegetable 0712
- Diamonds Worked or unworked same heading 71.02
- In machinery and electronic sector at times parts are classified in the same heading ,other times, in separate headings



HS Code number	Description of goods	Origin criteria
Chapter 25	Salt; sulphur; earths and stone; plastering materials, lime and cement	
25.07	Kaolin and other kaolinic clays, whether or not calcined	Options proposed by delegations: <ul style="list-style-type: none"> ■ Chapter rule ■ WO ■ Proposals as indicated at the splits below
ex 25.07 (a)	Calcined	CTHS
Ex 25.07 (b)	Other	Options proposed by delegations: <ul style="list-style-type: none"> ■ Chapter rule ■ CC
25.18	Dolomite, whether or not calcined; dolomite roughly trimmed or merely cut, by sawing or otherwise, into blocks or slabs or a rectangular	Proposals as indicated for subheadings
2518.10	Dolomite not calcined	The country of origin of the goods shall be the country in which the dolomite of this subheading is obtained in its natural or unprocessed state
2518.20	Calcined dolomite	CTSH



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Alternative rules of origin and co-equality

- Heading 851830-headphones
- Heading 851890–parts of headphones
- ASEAN PSRO for headphones subheading 851830: A regional value content of not less than 40 percent; or A change to subheading 8518.30 from any other subheading
- Assembly of parts of headphones 851890 into complete headphones is origin conferring as there is a change of subheading
- The 40 % rule is redundant



Example of HS written rules (NAFTA style)

- RoO for Cotton yarn
- A change to headings 5201 through 5207 from any other chapter except from heading 5401 through 5405 and through 5501 through 5507



Example of HS written rules (NAFTA style) commented...

- RoO for Cotton yarn
- A change to headings 5201 through 5207 (cotton fibres and yarn) from any other chapter* except from heading 5401 through 5405 (Man made filament fibres) and through 5501 through 5507 (Man made staple fibres)

*Cotton yarns and cotton fibres are classified in Chapter 52

- EC way: Manufacture from originating natural fibres



RoO in EU-Canada FTA

RoO for Cotton yarn:

- Spinning of natural fibres or extrusion of man-made fibres, accompanied by spinning
- A change to a set of subheading 8214.20 from within this subheading, whether or not there is also a change from any other heading, provided that the value of the non-originating component products of subheading 8214.20 does not exceed 25 per cent of the transaction value or ex-works price of the set



Drafting RoO: the factors to be considered...

- Set a negotiating proposal on the basis of a text
- Limit RoO negotiations on a tariff line basis
- Introduce liberal RoO by adopting a modern formulation of a percentage rule based on value of materials
- Do not overrate cumulation



Percentage criterion: value added vs. value of materials

- The disadvantages of value added calculation
- Itemization of cost to the single unit of production. It requires accounting, and discretion may be used in assessing unit costs.
- Currency fluctuations may affect the value of the calculation.
- Low labor costs in developing countries may result in low value added and instead of being a factor of competitiveness may penalize LDC producer



Comparison of calculations

- *Product Costs:*
 - *Value of originating materials* \$30.00
 - *Value of non-originating materials* \$40.00
 - *Other product costs* \$20.00
- *Labour Reference Period costs* \$10.00
- *Total cost of Good A, per unit* \$100.00
-

Value added:deduct not allowable costs

- *Sales promotion, marketing and after-sales service cost* \$5.00
- *Royalties* \$2.50
- *Shipping and packing costs* \$3.00
- *Non-allowable interest costs* \$1.50
- *Total excluded costs* \$12.00

Total cost of Good A, per unit: $100 - 22 = \$88$

Example of value added calculation

- *The value for net cost (\$88) and the value of non-originating materials (\$40) are needed in order to calculate the regional value content. The producer calculates the regional value content of Good A under the net cost method in the following manner:*

- $$\text{RVC} = \frac{\text{NC} - \text{VNM}}{\text{NC}} \times 100$$
- $$\text{RVC} = \frac{88-40}{88} \times 100$$
- $$\text{RVC} = 54.5\%$$

Value of materials calculation

Method Based on Value of Non-Originating Materials

$$RVC = \frac{VNM}{EW} \times 100 = > \dots \%$$

Method Based on Value of Originating Materials

$$RVC = \frac{VOM}{EW} \times 100 = < \dots \%$$

Where:

RVC is the regional value content, expressed as a percentage;

EW is the Ex Works price;

VNM is the value of non-originating materials that are acquired and used by the producer in the production of the good;

VOM is the value of originating materials acquired or self-produced, and used by the producer in the production of the good.



Adjustments to Value of materials criteria

The calculations method adopted is based on adjustments made to the value of materials permitting :

The deduction of the CIF when the percentage is based on a maximum allowance of non-originating materials

and

The addition of inter- regional inland costs of transport when the percentage is based on the value of originating materials

- This method of calculation of the value of materials used in manufacturing may greatly facilitate compliance with the rules of origin.



The issue of the level of percentages

Various methods and analysis may be considered:

- A methodology elaborated by UNCTAD, evidence from recent studies, consultations with the private sector.
- The EC Impact Assessment contained simulations based on the UNCTAD methodology on the trade creation derived from using different percentages of 50% of local content and 30 %. Trade creation results from the simulation exercise were far greater under 30% level of percentage.
- The LDCs are proposing percentages of 15 % for the originating materials and 75 % for the non originating materials



A RoO Protocol: main features

A protocol on rules of origin consists of two documents:

1. The main text
2. The template of product specific rules of origin.



The Template

- It may not be necessary to negotiate a full set of product specific rules of origin exhaustively covering all products
- The parties either may not show significant trade in some of the HS headings or the tariff rate is MFN duty free in others.
- Attention may be therefore focused on the product specific - rule of origin where a significant trade flows and high preferential margins has been showed in the template.
- To this end the template may contain exhaustive information on the preferential margin ,the amount of trade flows recorded for that specific heading or chapter from the different parties and a proposed simplified product -specific rule of origin.



Some examples (I)

- Sub-heading 847330 of the Harmonized System classifying parts and accessories of computers was one the most imported and most exported item among ASEAN countries and China.
- A change to heading 8473 from any other heading.
- This rule may mean that all assembly operations performed in China to manufacture sub-components from parts imported from ASEAN will not be considered as originating in China since the finished product is classified in the same heading
- Cumulation in this case may play a role



Some examples (II)

- HS sub heading 841430 classifying compressors were the fifth most exported products to ASEAN by China.
- Matching this finding with China's imports from the World, it was observed that HS 8414 90 -parts of compressor- ranked as the 36th most imported product from USA and Japan
- Thus, a rules of origin such as:
- *"A change to subheading 841430 from any other subheading, except from subheading 8414.90"*
- may entail that the compressors exported to ASEAN utilizing parts imported from Japan and USA will not comply with rules of origin requirements



Thank you for your attention

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