

Drivers of Utilization Rates (URs) and Rules of Origins: Myths, Facts, and Work Ahead

**Eight Global Review of Aid for Trade “Empowering Connected, Sustainable Trade”:
How can exporting countries improve utilization of US Trade Preference Programs?**

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Myth: Preferential Margins (PM) as driver of URs

- PMs are **one** of the elements of a firm decision to locate production in a beneficiary country
- Profit margins and trade volumes in a specific industry may be more important than preferential margins.
 - High profit margins in fashion industry permit to forego significant PM
 - High volumes in USMCA trade on cars make a PM of 2.5% attractive
 - Minimal PM in steel products where profit margin are reduced.
- Firm level research shows that the PM *is less significant than the import transaction value i.e., tariff savings* (Inama and Ghetti, 2020; Kasteng, 2020)
- Overlapping trade preferences strengthens the argument: firms are profit maximizers and use the best combination of preferential margins and RoO (i.e. PM are not considered in isolation of RoO)

Real drivers of utilization rates

Fact #1: Leniency (Stringency) of Rules of Origin

Leniency or Stringency of PSROs drives URs

- The LDC paper at CRO (2014) prepared with UNCTAD showed that more lenient rules of origin criteria introduced by EU and Canada reforms led to higher utilization rates, trade volumes and locating industries in beneficiaries
- The methodology used to meet the rules of origin requirements matter i.e., use of non originating or originating materials requires less accounting than a value-added method
- Level of percentage, CTC, or working of processing: **what is matters is what kind of manufacturing it takes to comply related to the sector**

Lessons Learned and Caveat

- Leniency or stringency of a given PSRO must be measured against manufacturing requirements related to firm's location and supply of inputs

Real drivers of utilization rates

Fact #2:

Rules of Origin Administrative Requirements

- As identified in research and argued by LDCs, **documentary evidence of origin** is a formidable obstacle to URs deriving from:
 - Certificate of origin stamped by Certifying Authorities versus self- certification
 - Evidence of direct consignment
 - Restrictive allowance of third country/party invoicing
 - Suppliers declarations
 - Accounting segregation
- All in all, **it is a firm level decision** (Inama & Ghetti, 2020)

Firms' decision to use trade agreements

Level of duty preference;

Margins in the industry;

Flexibility in sourcing and manufacturing decisions;

Company culture and organization;

Estimated implementation costs

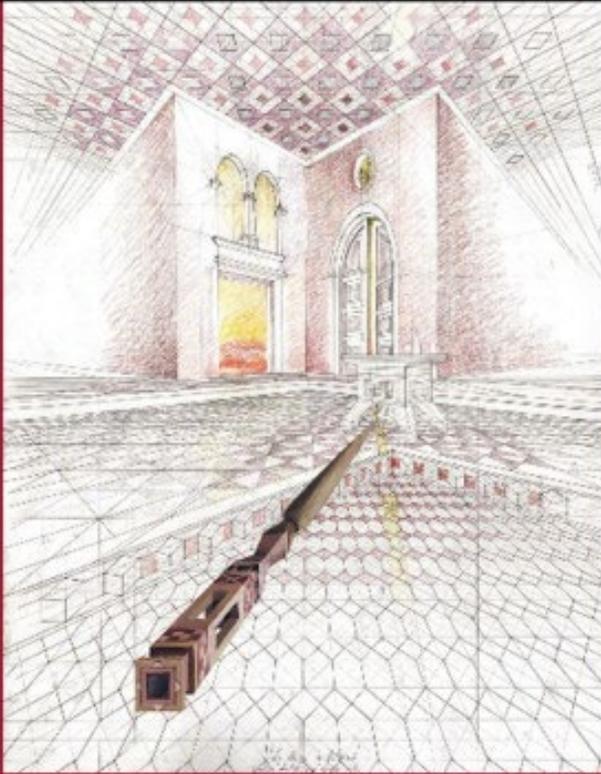
Challenges

- Low or high URs are like the result of a medical test, they need to be read by professionals to identify the correct diagnosis and link to rules or origin considering sectors, firms, and markets involved.
 - No magic solution
- Link between utilization rates and rules of origin offers a merciless picture of the use of a PTA.
 - Denial mode: Governments and trade officials are wary of recognizing such link
- Research and literature on rules of origin have so far paid scarce attention to how rules of origin operate in the real world.
 - New research should be actionable, to be used by governments seeking to cooperate on rules of origin to facilitate trade (Hoekman and Inama, 2018)
- Transparency: disaggregated data on utilization rates are often not available
 - URs are a public good that should be made widely available and accessible

Work Ahead

- T20 paper with ADB on the need to resume initiatives on RoO at multilateral level
- Research and capacity building on convergence of PSRO and best Practices on certification in collaboration with ADB
- Publication of the first study on COMESA interregional trade preferences
- Assessment of Rules of Origin in African Continental Free Trade Area

Rules of Origin in International Trade



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CAMBRIDGE

Resources

- **Rules of origin in International Trade** (2022) Stefano Inama, Cambridge University Press.
<https://www.cambridge.org/core/books/rules-of-origin-in-international-trade/999ED0B7C1BA1B612CAB1193615369C9>
- Getting to better rules of origin for LDCs using utilization rates - from the WTO Ministerial decision in Hong Kong (2005) to Bali (2013), Nairobi (2015) and beyond, Geneva. UNCTAD/ALDC/2019/3, eISBN: 978-92-1-005550-5
<https://unctad.org/webflyer/getting-better-rules-origin-ldcs-using-utilization-rates>
- Compendium of technical notes prepared for the LDC WTO group on preferential rules of origin (2020). UNCTAD/ALDC/2020/6
<https://unctad.org/webflyer/compendium-technical-notes-prepared-least-developed-countries-wto-group-preferential-rules>
- **UNCTAD-COMESA Study: Utilization rates of African RECs** (forthcoming)

Additional Resources I

- **Crivelli, P. and S. Inama. 2021.** “Improving market for LDCs: The impact of the EU Reform of Rules of Origin on Utilization Rates and Trade Flows under the Everything But Arms Initiative (EBA)”, *UN LDC5 Conference paper*
https://www.un.org/ldc5/sites/www.un.org.ldc5/files/t6_inama_eu_reform_2021_16_helsinki_final_20210816_clean.pdf
- **Crivelli, P., Inama, S., and J. Kasteng. 2021.** “Using utilization rates to identify rules of origin reforms: the case of EU free trade area agreements”, *EUI RSC*, 2021/21, Global Governance Programme-437
<https://cadmus.eui.eu/handle/1814/70396>
- **Ghetti, PP. and S. Inama, 2020.** The Real Cost of Rules of Origin: A Business Perspective to Discipline Rules of Origin in a Post COVID-19 Scenario, *Global Trade and Customs Journal*, Vol. 15, Issue 10, pp. 479-486,
<https://kluwerlawonline.com/journalarticle/Global+Trade+and+Customs+Journal/15.10/GTCJ202008>

Additional Resources II

- **UNCTAD website of utilization rates** of trade preferences granted by QUAD countries available at: <https://unctad.org/topic/trade-agreements/trade-preferences-utilization>
- **UNCTAD-EUI platform of experts**, researchers, practitioners, government officials and the private sector to discuss developments in the area of RoO and URs on an annual basis (June 2019, February 2020, October 2021)
 - Rules of Origin | Interview Series: <https://globalgovernanceprogramme.eui.eu/rules-of-origin-interview-series/>
 - Trade Facilitation and Rules of Origin: <https://globalgovernanceprogramme.eui.eu/trade-facilitation-and-rules-of-origin/>
- Ongoing cooperation with researchers from the **Asian Development Bank** on studying RoO and URs in the Asian region and especially mega-regionals (CPTPP and RCEP).
 - Crivelli, P. and S. Inama. 2021. Making RCEP Successful Through Business-friendly Rules of Origin. Asian Development Blog. <https://blogs.adb.org/blog/making-rcep-successful-through-business-friendly-rules-origin>.
 - Inama, S., P. Crivelli, and P.M. Ha, 2022. The Low Use by Firms of ASEAN Trade Preferences: Will RCEP Follow the Same Destiny? An Agenda for Rescue to Reform Rules of Origin in the Asian and Pacific Region. Global Trade and Customs Journal, 17(6). <https://kluwerlawonline.com/JournalArticle/Global+Trade+and+Customs+Journal/17.6/GTCJ2022033>
 - Crivelli, P., S. Inama, and M. Pearson. 2022. An Analysis of the Product-Specific Rules of Origin of the Regional Comprehensive Economic Partnership. Manila: Asian Development Bank <https://dx.doi.org/10.22617/TCS220167-2>

Thank you!

