Rules of Origin
Preference Utilization

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WTO Webinar
19 May 2021

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Preference Utilization

• Why do we care?
  • Excessive unused preferences mean that an FTA is not providing the benefits it promised

• Rules of Origin (RoO) are cited as a barrier to preference utilization
  • Not entirely fair: General FTA knowledge, risk management, AND RoO

• Why?
  • RoO noncompliance—If it’s not originating, it shouldn’t use preferences
    • Firms may choose not use preferences for a variety of reasons.
  • Sourcing burden—Higher costs to produce an originating good
    • This is the whole point of RoO
  • Compliance burden—Higher transaction costs
    • What paperwork is needed? Where to get information?
    • Compliance risk—Don’t know if it’s originating, don’t want to risk it
Sourcing Burden vs. Other costs

• Higher production costs from sourcing originating materials are undoubtedly real, by may not be the most relevant in terms of preference utilization decisions.

• Is preference utilization even a conscious decision?
  • Knowledge of FTAs has been shown to be limited

• Other factors boil down to information management
  • What is the rule?
    • HS issues: classification challenges and HS revisions
    • What does it mean? (RoO language is legalistic and complex) Is that all? (Chapter notes, section notes, packing and packaging, sets and assortments, indirect costs, intermediate materials, de minimis, RVC calculation methods, valuation of materials and their adjustments, cumulation, etc.)

• Information from suppliers (and their supply chains!)
• Risk – 2% tariff savings versus fines and verification costs.
Utilization rates have been shown to vary widely across countries and agreements.

Carerre and de Melo (2004) used utilization rates in NAFTA as a factor in calculating the costs of RoO compliance.

IDB and ADBI surveys

- Knowledge: There is an FTA? What is an FTA?
- It is not always SMEs that have the biggest RoO problems – MNEs’ suppliers are often SMEs
- Another challenge is utilization of multiple agreements.

Cadot et al. (2014) analysis of utilization rates in several Latin American countries indicate that utilization increases in preference margin, firm size, and time.

Jonas Kasteng on at Swedish National Trade Board – company size and preference margins matter less, transaction size, experience and administrative costs matter more.
Complexity of RoO
To Harmonize or not to Harmonize?

The siren song of harmonization

• What should NOT be harmonized: the PSRO
  • The PSRO in bilateral agreements are adapted to the export supplies of the signatories. **One size does not fit all.** This is true across agreements and across products.

• What can and should be harmonized
  • Definitions – Special goods (sets, accessories, packaging, etc.)
  • Procedures – Direct shipment, Time periods, appeal stages, etc.
  • RVC calculation methods – Should only need two methods: minimum originating content and maximum non-originating content. That’s it.
  • Documentation requirements – What information is sufficient to demonstrate compliance?
How to reduce the compliance burden?

We must leverage technology
• Traceability of materials combined with origin documentation
• Tools to facilitate assessment of compliance
  • RoO are expressed in technical language that is not easily accessible to non-experts
• Information security / Avoiding disintermediation / Blockchain

Simplification and transparency
• Harmonization of mechanisms and procedures
  • GTPA, EU/Swiss/et al. RKC proposal

Capacity Building
• Training every potentially exporting SME may be too much
• Developing capacity in chambers, export promotion agencies, and certifying entities can really add value
Thank You

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