Rules of Origin Under U.S. Trade Preference Programs

World Trade Organization

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U.S. Trade Preference Programs

- Unlike most other WTO members, the United States has five preference programs
  - Former Trust Territory of the Pacific Islands (Northern Mariana Islands, Marshall Islands, Federated States of Micronesia, Palau), 1948
  - Generalized System of Preferences (GSP), 1976
  - Caribbean Basin Economic Recovery Act (CBERA), 1984
  - African Growth and Opportunity Act (AGOA), 2000
  - Trade Preferences for Nepal, 2016
- Note that some programs are based on a geographic area, but GSP is not
- Some countries are beneficiaries under more than one program (e.g., Caribbean + GSP, AGOA + GSP, Nepal + GSP)

U.S. Trade Preference Programs

- Each preference program has different product coverage
  - AGOA: 5,351 tariff lines
  - GSP: 5,138 tariff lines
  - Nepal: 77 tariff lines
  - CBERA (including CBTPA, Haiti HOPE) 5,674 tariff lines
- Rules of origin under U.S. preference programs are based on whether a good is a “product of” the beneficiary country and the regional value content (RVC) requirement, not tariff shift

U.S. Trade Preference Programs

- Caribbean Basin Economic Recovery Act (CBERA) has three parts
  - The base CBERA preference program is permanent
  - The Caribbean Basin Trade Partnership Act (CBTPA) preferences will expire on 30 September 2030
  - Haiti preferences will expire on 30 September 2025
- African Growth and Opportunity Act: Expires 30 September 2025
- Nepal Trade Preferences: Expires 31 December 2025
- GSP: Expired 31 December 2020 (GSP has expired several times - historically GSP renewal has allowed refunds for duties collected during the lapse)

Rules of Origin Under U.S. Preferences

- The United States applies a rule of origin based on whether good is a “product of” the beneficiary country and the amount of originating content in the good as a percentage of the good’s value
- Generally speaking, non-textile products utilize the rule of origin that requires an RVC of 35 percent
- $(Cost\ of\ local\ materials + Direct\ cost\ of\ processing) \div Appraised\ value\ of\ Good\ \geq 35\ percent$
- Apparel products under AGOA and other programs are generally subject to a simple “cut-and-sew“ (third-country fabric) rule
- Under some preference programs, cumulation with other beneficiaries in the geographic region or with the United States is permitted

Trade Data

- General trade data, as well as data on preference utilization can be found at the website of the U.S. International Trade Commission
- Searches can be customized to create groups of countries, specific goods, time periods, use of preferences
- The service is free, but requires the creation of an account

  Dataweb.usitc.gov
- The U.S. also submits annual reports to the WTO as required under its waivers for AGOA (WT/L/1117), CBERA (WT/L/1115), and Nepal (WT/L/1119)

Domestic Reporting on Preference Programs

- **CBERA:** The U.S. International Trade Commission (USITC) publishes a biannual report, most recently in September 2021. The Office of the U.S. Trade Representative (USTR) also publishes a biannual report, most recently in December 2021.
- **AGOA:** USTR publishes a biannual report, most recently in June 2020. The next report will be published in June 2022. USITC published a report on trade and investment in March 2020. In January 2022, it began work on a new report on AGOA usage and trends.
- **Nepal:** USTR publishes an annual report on preference utilization, most recently in December 2021.
- **GSP:** USTR includes information on utilization in the USTR annual report

Effects of U.S. Trade Preferences

- The U.S. has identified numerous industries that have developed to take advantage of trade preferences.
  - Apparel, Sub-Saharan Africa: Provisions that allow the use of third-party fabrics have allowed Kenya, Lesotho, and Madagascar to take advantage of AGOA preferences
  - Apparel, Haiti: Haiti's apparel exports have grown significantly under CBI preferences and reached 95 percent of total Haitian exports to the United States in 2020. Industry estimates that CBI is responsible for the creation of over 54,000 garment factory jobs in Haiti as of the end of 2020.
  - Travel goods, Southeast Asia: Travel goods were added to GSP for all GSP beneficiaries in 2018; currently the largest GSP import category.
  - Rum, Jamaica: Jamaica is currently the leading global supplier of rum to the United States.

Utilization of Trade Preferences

- The U.S. has observed that trade preferences are not always utilized, even for goods where origin is easy to establish
- Kidney beans (0713.33.40) from Belize:
  - U.S. MFN tariff 1.5 cents/kg
  - Utilization has varied significantly between 2017 and 2021. Non-utilization in 2020 was 2.2 percent, in 2021 it was 20.2 percent.
- Crude petroleum (2709) from Nigeria and Angola:
  - U.S. MFN tariff 5.25 cents/bbl or 10.5 cents/bbl
  - AGOA preferences are utilized less than half the time. In 2021, AGOA was used for 41.3 percent of U.S. imports (by value). In 2020, that figure was 38.5 percent.
  - Is this related to the relatively small tariff on petroleum as a percentage of the price?

Utilization of Trade Preferences

- The base tariff rate may have an effect on utilization of preferences
- Vanadium oxide, 2825.30 (used in the production of strengthened steel): U.S. tariff rate is 5.5 percent
  - 2021 imports from AGOA beneficiaries: $20.4 million under AGOA (90% of total imports), $1 million under GSP, $1.2 million no program claimed
- Men's and boys' undergarments, other than cotton, 6107.99: U.S. MFN tariff rate 14.9 percent
  - 2021 imports from AGOA beneficiaries: $3.2 million under AGOA (99.9% of total imports), $836 no program claimed
- T-shirts, 6109.10: U.S. MFN tariff 16.5 percent
  - 2021 imports from AGOA beneficiaries: $43.4 million under AGOA (86.2% of total imports), $6.9 million no program claimed

To What Extent do Trade Preferences Affect Exports to the United States?

- 6107.99, total 2021 U.S. imports: $165 million
  - Top 5 exporting countries to the U.S. account for $148.1 million (89.8 percent). Only the exporter in fifth place ($3.4 million) receives preferences
  - <u>AGOA accounts for less than one percent of total U.S. imports</u>
- 6109.10, total 2021 U.S. imports: $5.1 billion
  - Top 10 exporting countries to the U.S. account for $3.5 billion (68 percent). Five of the top 10 are U.S. FTA partners, first unilateral trade preference beneficiary is #13 (Haiti).
  - Eight of top 20 exporters receive some sort of trade preference (e.g., FTA), ***but not the third country fabric allowance***
  - <u>Unilateral trade beneficiaries (Haiti, AGOA) account for $222 million (4.4 percent) of U.S. imports</u>

Modifying Rules of Origin

- Rules of origin under U.S. preference programs are defined in the legislation
- Rules of origin in U.S. FTAs can be modified with the agreement of the other party (except textiles)
  - Changes in the Harmonized System
  - Changes in sourcing
- Changes to U.S. FTA rules of origin can be made administratively, but require an analysis by the USITC, a formal agreement, and a presidential proclamation

Factors Affecting Utilization of Preferences

- *U.S. Trade with Sub-Saharan Africa: Recent Trends and New Developments*, USITC Publication 5043
- Eligibility for preferences
- The presence of foreign direct investment (FDI) in the sector
- Consumer demand for the product in the United States
- Expanded production capabilities, and cost advantages in production.
- Foreign-domestic partnerships in certain industries

Questions to Consider

- What factors affect the utilization of trade preferences? (e.g., knowledge, degree of preference, expiration)
- Why is utilization affected even for certain goods that are wholly obtained?
- What is the relationship between MFN tariff rate and preference utilization? Do higher MFN rates create more incentive for preference utilization?