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Origin and Beyond: Trade Facilitation Disaster or Trade Facilitation Opportunity?

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Abstract

This paper explores several mechanisms by which the barriers imposed by rules of origin may be reduced through effective trade facilitation efforts. Also discussed are the functional similarities of a variety of other requirements on international trade with rules of origin, including environmental, security, and consumer safety certifications. We argue that all of these requirements rely fundamentally on the management of information regarding materials and suppliers used in the production of internationally traded goods.

JEL Classification: F02, F15, F23, F53

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1. INTRODUCTION

Over the last three decades, the countries of Latin America (LAC) and East Asia have nearly all, to varying degrees, embraced development strategies based on opening markets, promoting exports, and attracting foreign investment. Intra-regional, cross-regional, and extra-regional trade has grown in importance. Trade between Latin America and Asia exceeded 300 billion United States (US) dollars in 2008, a sign of the growing importance of this interregional economic relationship.

In the early years of pursuing and supporting these strategies, the primary policy-based obstacles to commerce that had to be addressed were high tariffs. But as these countries have joined the General Agreement on Tariffs and Trade (GATT)/World Trade Organization (WTO) and negotiated an ever-increasing number of regional trade agreements (RTAs), tariffs per se are not the trade barriers that they once were. These steps have brought about considerable growth in trade, and have helped the countries of these regions to take greater advantage of the evolving global trading system.

As the importance of tariffs as primary trade barriers has receded, these successes have revealed, and in some cases caused, a new set of obstacles. The important policy obstacles to address now revolve around the concept of trade facilitation, both in its traditional sense as relates to customs procedures at borders, but also in the context of managing and administering compliance with at-border and behind-the-border requirements on the part of importers, exporters, producers, and even reaching back to their suppliers.

Baldwin (2006) has described the nature of the global trading system that has evolved over the past several decades, highlighting the causes and consequences of proliferating RTAs. In this framework, these agreements serve as a useful mechanism for promoting further trade liberalization by signatory countries. But they also leave in their wake an uncoordinated tangle of inconsistent, difficult to decipher, and at times contradictory regulations and restrictions on international trade. This mess, then, calls out for tidying up at the multilateral (i.e., WTO) level, thus promoting a “multilateralization” of the regionally established tariff reductions.

Because RTAs are negotiated in different contexts at different times, they inevitably stipulate different rules for application of the tariff preferences that they establish, as well as divergent standards and other requirements for selling different products on different national markets. In order for exporting firms to benefit from the negotiated tariff preferences in multiple foreign markets, they must be able to manage these diverse rules and regulations.

The information required in order to process an international sale and movement of goods, taking advantage of the preferential tariffs that are negotiated, and complying with the vast array of environmental, security, and consumer safety requirements, is becoming quite significant. This amounts to a before-the-border “thickening.” Even where all of the needed information is readily available, the administrative costs of organizing and communicating this information to customs and other border agencies constitute an implicit barrier to trade.

One of the most important of such issues is the rules of origin (RoO) of the rapidly expanding network of RTAs. RoO are the criteria established in preferential trading arrangements for determining the degree to which materials from countries that are not party to an agreement may be used in the production of goods within a member country, without those goods being considered ineligible for tariff preferences. These RoO can be quite complex to understand and administer, even for sophisticated multinational firms, to say nothing of small- and medium-sized enterprises (SMEs). The situation can become even more difficult when these rules vary across the different markets that the firms wish to serve.

In addition to RoO, countries are applying a growing set of regulations geared toward promoting consumer and environmental safety, among other issues, which, although they

apply equally to imports and domestic products, add an additional layer of complexity to international trade transactions, and complexity is cost. Many of these measures, despite their obvious merit in principle, are going up in reaction to high profile, politically charged events, and their implementation is being mandated faster than common sense would seem to indicate. As a consequence, a wide array of costly testing and certification is required where there is little capacity to do so, and in many cases no logical purpose, as the goods in question are swept up in well-intentioned but overly broad regulations.

As we seek mechanisms to ameliorate these problems, we see that trade facilitation must include, but is larger than, the traditional issues (and WTO focus) of Articles V, VIII, and X of the GATT. While these are important, advances on these issues alone would be insufficient to the needs of modern international trade. To be of practical use, trade facilitation measures must be designed and implemented with a private sector perspective in mind. The practical issues of certificate formats, value content calculation methods, supplier information requirements, and administrative peculiarities present a wide array of obstacles that go beyond the traditional trade facilitation issues.

The remainder of this paper is structured as follows. Section 2 addresses the determination and governance of RoO in the global trading system, as well as the implications of this lack of organization and some possible approaches that might better order and facilitate trade. Section 3 looks beyond RoO to other forms of regulation that impose on trade the same type of informational requirements as origin, and that must be considered in any origin-related trade facilitation endeavor. Section 4 concludes and offers some recommendations of policies that could lead to better facilitation of trade on origin-related matters.

2. GOVERNANCE OF RULES OF ORIGIN IN A SPAGHETTI WORLD

The world map of the RoO “spaghetti bowl” is, at this point, well documented.¹ It is expected that by 2011 there will be nearly 400 RTAs in force. This averages out to more than two per WTO member, though in fact some countries are more prolific in their trade negotiations than others. The LAC and East Asia regions in particular have come to have rather dense networks of overlapping RTAs. For LAC, this is rapidly reaching a saturation point, with nearly all of the important bilateral relationships (in terms of trade value) covered by such agreements. East Asia is not yet at such a point, but is signing and implementing agreements at a rapid clip, such that already these issues are on the horizon.

This is also not just a question of the number of agreements, but of their size and quality. In both regions, countries have signed and are implementing agreements with major trading partners (e.g., People’s Republic of China, US, India, Republic of Korea, European Union [EU]), in addition to a growing array of smaller partners. As a consequence, significant fractions of these countries’ trade are regulated by the dispositions of these growing networks of agreements.

At the global level, the effect of these overlapping networks of RTAs is that we find duty-free treatment has potentially been established, in principle, for a significant majority of world trade. However, this duty-free treatment is subject to the RoO of each particular RTA. As the rules differ across agreements, and even where rules are the same, the eligible suppliers differ, we see that compliance starts to be a significant concern for traders.

We say “potentially” because the rules of the agreement apply only to those goods for which preferential treatment is requested. If the costs of complying, and demonstrating compliance, with the prerequisites for preferential treatment exceed the value of the preferences, then the obligation to comply with these requirements regarding the RoO and the certification thereof

¹ See, for example, Estevadeordal, Harris, and Suominen (2007).

disappears as the goods enter and pay the most-favored-nation tariff. While this reality imposes a helpful upper limit on the distortionary potential of RTAs, it also limits the degree to which the tariff reductions can boost trade.

The evolving literature on “multilateralizing regionalism” referenced above is based on the expectation that agreeing to and applying better central governance of RTAs from the multilateral system under the WTO can lead to smoother operation of trade on a global basis. It is worth asking, however, whether we are equally likely to achieve some sort of “regionalization of multilateralism” wherein the growing influence of regional trading institutions may slow the adoption of global standards and such regional blocs cater more to their perceived interests than to global efficiency. In this scenario, it will be the responsibility of the regional institutions to work both individually and together, under the auspices of the WTO or otherwise, to reduce the costs of trading both within their spheres of influence, and across blocs.

The WTO is still the forum of choice for efforts to harmonize global standards on this and other issues. It is unlikely that any bloc or blocs will carry enough economic weight to displace the global institution, but it is also likely that regional arrangements will have increasing influence over the agenda. The ability of regional blocs to establish the rules that apply to important segments of international trade will translate into stronger voices in multilateral discussions. It is thus important that these arrangements find efficient solutions to the more pressing problems facing operators in the world today.

This scenario is as applicable to investment and intellectual property issues, for example, as it is to RoO, though it is the latter on which we focus here. As we discuss below, whatever the mechanics by which it is achieved, if trade costs are to be further reduced, procedural simplification and administrative costs as pertain to RoO must be a priority.

2.1 Implications of RoO Anarchy

While it is true that in some minority of simple cases, where an exporter produces only one product for all customers over time, and with most materials sourced domestically, the costs of the complications from origin inconsistency may not be so bad. But for the majority—producers with dynamic, flexible, fast supply chains—the complexities and constraints of the tangle of overlapping rules can impose costs that exceed the value of the tariff preferences that compliance confers, especially if the margin of preference is low. In such situations, the value of the agreement (or agreements) is lost.

Note that this applies to corporate affiliates not just in one country or region, but within whole multinationals (i.e., from a centralized global perspective). The complexity of origin compliance has in many cases led to the centralization of origin management within corporate structures, especially where supply chains are global. As such, the decisions to claim preferences (or not) can be made not on a case by case basis, but as global corporate policy, and thus affect global preference utilization.

Even where the tariff preferences are substantial enough to merit the compliance efforts, the cost can be significant for large multinational firms that manage fragmented production networks across multiple countries. To the extent that these costs reduce competitiveness, they serve as a brake on international trade and investment.

These costs are also present across and between companies and their suppliers. Indeed, when suppliers are not wholly-owned subsidiaries of the final producer, the costs are even greater, because it is less likely that efficient channels exist for transmission of the suppliers’ origin information. In order for final producers to accurately evaluate their own origin compliance, they require complete information on the origin of their materials, both those they produce themselves and those purchased from unaffiliated suppliers.

Making compliance determinations then involves crawling back up the supply chain, identifying materials used and their suppliers, as well as the originating status of each material sourced from each supplier. At this point, pricing and sourcing confidentiality and sensitivity issues can arise. In fact, it cannot always be taken as given that it is in the interest of suppliers to provide complete information to their clients, as this information could in some cases jeopardize their relationship, for example by identifying subcontractors that the producers could then contact directly, cutting the supplier out of future transactions.

At present, there is no end in sight for the increasing complexities of the global origin spaghetti bowl. The topic, at least, is beginning to generate discussion, both in chambers of commerce and among policymakers. But such discussions are just beginning, and there is no emerging consensus on practical solutions.

One sort of solution that has been put forth deals with the definition of cumulation in RTA RoO. Because RTAs are most frequently negotiated bilaterally, the preferences apply only to goods that are originating in one or the other partner to the agreement. However, once a group of countries comes to have all or most of its constituent bilateral relationships covered by bilateral agreements, situations arise where materials exported from one country to another can enter duty free, but if they are subject to further processing in another country within the group before being sold to the same final destination, the final good in question may not meet the applicable origin requirements, even though each of its constituent parts, if exported directly from their respective countries of production, would have entered duty free. In this case, the problem lies not so much in the definition of the specific origin criteria in any one of the RTAs involved, but rather in the absence of provisions for cumulation of origin among countries within this tangle of agreements.

Solutions that have been put forward² involve finding mechanisms for implementing such cumulation provisions. This can take the form of replacing a collection of agreements with a single agreement covering all countries, or other more piecemeal arrangements that can produce similar effects with less extensive negotiations, but result in less reduction in overall complexity. However these problems are to be addressed, the issues of implementation and administration at the border remain.

2.2 Origin Administration

Administration of RoO involves both private actors and the public sector. It includes all of the documentation and record-keeping requirements established by an agreement and its regulations, all of the customs procedures associated with proving origin, and all of the procedures and potential sanctions deriving from ex post facto verification of origin. In practice, this is in addition to the design of supply chains that contemplate sourcing from within a given cumulation zone in order to comply with rule requirements. It is one thing to comply with the requirements. It is another thing to substantiate this compliance in such a way as to be able to prove compliance to the necessary government agencies.

Apart from the differing rules and inconsistent cumulation zones across overlapping RTAs, there is also much divergence in methods and procedures for administration of origin. At the global level, other than a few guidelines in the Revised Kyoto Convention, there is significant multiplicity of administration procedures without multilateral disciplines. Not only do procedures and protocols differ across countries, but they can differ in a single country depending on the agreement under which goods are imported. This generates both costs for customs in terms of time and resources, and consequently uncertainty for business.

It is worth pointing out that this is a problem for both preferential RoO, which have been the focus of our discussion in this paper, and also non-preferential RoO, which are vital for the administration of countervailing duties and antidumping measures. Firms trading in goods

² See Cornejo and Harris (2007) and Harris (2008) for similar but different approaches to this problem.

subject to such measures in any of their export markets, even if the measures are not aimed at goods from the firms' countries, must be able to adequately document and substantiate that the goods exported do not originate from countries subject to the compensatory duties. Chaos in the definition of the non-preferential rules across countries, as well as uncertainty regarding the application and/or interpretation of the rules in different countries leads to the same difficulties as seen in the case of preferential RoO.

2.3 Unilateral Solutions to a Two-Dimensional Problem

Given the tremendous variation in rules, cumulation zones, and administration procedures relating to compliance and administration of RoO within the two regions, and globally, it is reasonable for business to face significant uncertainty. This uncertainty relates both to compliance, where rules are unclear or interpretations are inconsistent, and to administration, where procedures are unclear, customs officials lack capacity, or legal provisions are incomplete.

This sort of uncertainty is an important barrier to trade. If even a perfectly designed supply chain, which sources only from eligible countries and ensures compliance with processing requirements, can still result in payment of tariffs due to misinterpretations or misapplications of rules by customs, then the additional costs of designing the supply chain represent a failed investment. Where this risk is large or where the potential tariff savings are significant, if investors cannot ensure proper application of the rules by the public sector then the investments may not occur, or the tariff preference may not be pursued. This is a loss both for the investors themselves, and for the countries that could have attracted such investment. And uncertainty due to application of the rules by customs is not the only, or even the most important source of uncertainty.

International trade transactions that are not between subsidiaries of the same corporation face the central origin dilemma: balancing the rights and obligations of the producer and the importer. The only entity that has sufficient information regarding a product's compliance with origin requirements is the producer, but in almost all cases the person responsible for payment of tariffs is the importer. The producer's interest is to obtain the best price for his goods, and he thus has an incentive to represent them as eligible for duty-free treatment whether or not this is actually the case. The importer, facing some likelihood of verification by officials of the importing country, therefore must take into account the potential tariff obligation and penalties in the event that verification cannot be satisfied.

For the importer, then, the preparation of entry documents involves much more than determining the transaction value (visible on the importer's general ledger) or determining the proper tariff classification (possible just by looking at the product), because origin relies heavily on exporter information, which may be faulty, either through fraud or negligence. Whatever the particular underlying circumstances, the issue of origin liability for importers is real.

Furthermore, most agreements allow for post-entry verification of origin up to five years after goods are imported, and verification actions rarely concentrate on a single transaction, but rather on a series of importations of longer time frames. The combined tariffs, interest, and penalties for which an importer can be liable based on multiple years of faulty origin information can quickly reach into the millions of US dollars.

In this context, the public sector has a role to play in designing the origin procedures, with a view to ensuring proper collection of revenue. Again, there is no single global trend toward an emerging consensus, but rather an ongoing series of experiments with different methods in different countries.

There are then two primary factors to consider when designing policies and procedures for mitigating the risks implicit in these situations. The first revolves around origin certification methods, and the second focuses on standards for importer-exporter contracts.

In some sense, importer liability has been exacerbated by origin self-certification methods as they have been implemented by a number of countries, most significantly the US. Under these systems, in most cases a certificate of origin may be issued by the producer, the exporter, or the importer, but only the last of these can be required to sign such a certificate or face the loss of tariff preferences, as well as become liable for additional penalties. Furthermore, the agent that issues the origin certificate is required to maintain the necessary documentation that substantiates the certificate of origin. But still, having either the exporter or, optimally, the producer issue the certificate is still not a shield from liability for the importer, who is in all cases responsible for the duties.

This arrangement does solve problems that can arise in other certification systems, as it is difficult for customs agencies to pursue agents outside the country of import to collect duties and penalties, whereas the importer is generally resident in the country of import. But by concentrating responsibility in the importer, the resulting imbalance of rights and responsibilities can serve as a disincentive to the utilization of preferences, and thus to a reduction in the potential benefits of the agreement.

In addition to the US, the EU is in the process of moving from reliance on origin-certifying entities to self-certification. This is happening precisely due to a rash of problems with certificates of origin issued by certifying entities in countries that benefit from EU tariff preferences. Existing EU law regarding importer reliance on entity-issued certifications holds that the importer is not liable if the certificate proves to be false, under the argument that importers have a reasonable expectation that such certifications are accurate.

When in several recent high-profile cases such certifications have been shown to be highly inaccurate, importers have used this defense in order to be liable for duties only, and not for penalties, and with more limited retroactive application. As a result, the EU seems to be moving toward a system of self-certification by authorized economic operators, who are essentially pre-screened and authorized exporters or importers that have been pre-qualified by EU customs to certify the origin of their goods. (Importers who do not qualify as authorized economic operators must still rely on entity-issued certificates.)

One solution to the uncertainty for importers is to include a clause in the sales contract to explicitly give the importer the right to recover any tariffs or fines incurred due to faulty origin-related information provided by the exporter. Such contract clauses have witnessed a significant proliferation in recent years. As origin can be reviewed by customs up to five years later, there is ongoing contingent liability for the exporter. This solution works relatively well for importers who are large multinational corporations, as these firms have the capacity to pursue enforcement of such contracts in the country of export. For smaller importers, this is more of a challenge, and as such not necessarily a complete solution.

Despite these ad hoc solutions by individual importers, the general result of the uncertainty generated by the variation in rules and administrative capacities is preference liability paranoia for firms and traders. This can be especially hard on the SMEs, for whom the capacity constraints are the most severe. What can be done?

A first step might be the adoption of the above-mentioned origin liability contract clauses in the model contracts of the International Chamber of Commerce. These model contracts are used widely in international trade transactions, and identification of best practices in assignment of origin-related liability and application of such best practices in these model contracts will not only help the contracting parties, but will also serve as an educational tool for courts that will eventually face such contract enforcement cases in the event of discrepancies.

A second idea would be to legally link origin certificates issued by exporters to export declarations for purposes of fraud liability. The goal of this approach is to create a legal mechanism under which exporters may be sanctioned for negligent or fraudulent certification of origin, as such a certificate would form part of a legal document in the exporting country,

in particular the export declaration. Indeed, most of the relevant data for origin purposes should be present on the export declaration as well, and so these documents, taken together, would provide a legal foundation for holding exporters liable for erroneous origin certifications.

A number of further short-term and long-term measures merit consideration. First, developed countries should initiate origin administration standardization under the duty-free, quota free process for least developed countries (LDCs). This is a moral duty as much as a practical economic consideration. Furthermore, the volume of trade that can be associated with the LDCs is sufficiently small, even with significant facilitation, so as to present marginal potential for politically difficult dislocation in domestic markets. Indeed, this may be the perfect context for a proof of concept in broad international coordination of administrative procedures, as the relatively small volume of trade in question lowers both the political and the economic costs of such an endeavor.

Additionally, both governments and private organizations should support e-origin solutions. These include stand alone systems such as the Inter-American Development Bank's (IDB) Understanding and Using Rules of Origin system,³ as well as the advance of e-commerce origin determination systems including supplier communications programs developed by private sector business software firms. To the degree that these technologies could be integrated into electronic single windows⁴ and electronic origin certification systems, their utility would be even greater, especially for SMEs. On a related note, because certainty regarding the proper classification of both products and materials is vital to correct application of origin rules, Harmonized System artificial intelligence systems, wherein linguistic and taxonomy software facilitates identification of the correct tariff classification, should form part of this agenda.

3. BEYOND ORIGIN

3.1 Multiplier Benefits of RoO

Origin, from the private sector perspective, is essentially about supplier management. In order for a product to comply with the origin requirements, suppliers must be located in eligible countries and use materials that also originate in eligible countries so that the components they produce count as originating materials when used in subsequent production. Strategically then, what firms need to look for are not just low cost suppliers, but low cost suppliers that are properly located and are origin literate, so that they can provide the necessary compliance information regarding the materials that they supply.

But there is more to supplier management than just origin, and these other elements are starting to be linked into origin management systems. For example, supplier credit risk has been an important issue for firms during the recent financial crisis. The sudden and unexpected implosion of a major supplier can have significant adverse effects on a business, so monitoring and ensuring the capacity of suppliers to maintain access to credit must be an element of the firm's strategy.

And there is more. The objective is RoO management, but in the end the method for accomplishing this is complete process- and input-visibility. The issue is fundamentally one of information, and once systems are put into place to manage this information, it becomes

³ See www.originaftaidb.org for the Dominican Republic-Central American Free Trade Agreement version. The IDB has also created modules for Peruvian and Colombian agreements, and is working to expand coverage further.

⁴ "Electronic single windows" are essentially web sites that bring together all the information necessary for importers and exporters to comply with trade procedures, obtain certifications and licenses, and file documents, thus eliminating the need to visit multiple government offices for each purpose.

relatively straightforward to include additional elements in the dataset. This is important and useful for issues relating to supply chain security, consumer safety, and environmental protection.

3.2 The Province of Provenance

Many modern consumer protection and environmental regulations are requiring ever greater amounts of information regarding the place, method, and materials used in the production of goods. This “traceability” requirement, and the necessary related supporting documentation, can pose a major challenge to international trade. SMEs will also have to confront these challenges, whether they are exporting directly, or are part of a larger supply chain for products that must demonstrate compliance with these standards. Firms will have to keep informed about the requirements, which are constantly changing and evolving, and be able to demonstrate and certify compliance.

There are many examples of this. In the EU, a new set of regulations for chemical products known as REACH (for Registration, Evaluation, and Authorization of Chemical products) came into force in 2006. This requires that all chemical products undergo extensive analysis before being authorized for sale in the European marketplace, with the burden of proof on the producer to show that the product does not pose a health or environmental hazard. These requirements apply not only to industrial chemicals, but to cosmetics, cleansers, and a large number of other consumer products. Having products tested by authorized laboratories and obtaining the required certifications in order to demonstrate REACH compliance can be a significant investment, and once made it is important that this information and certification be available, whether in connection with a final product or materials to be used as ingredients in other products.

Other examples include:

- Traceability of fish and fish products exported to the EU. Requirements have been put in place that will obligate importers to demonstrate that the method of fishing did not involve illegal harvests or otherwise present dangers to protected species. Maintaining documentation of the fishing process is no different, conceptually, from maintaining documentation of other production processes that are more germane to origin compliance.
- Product standards (e.g., US wood and other consumer standards). In the US, important requirements have been legislated⁵ for wood products in order to protect endangered timber species and biodiversity. Under this law, imported wood and wood products, such as furniture and paper, must declare the source of the wood used, and certify that it was harvested legally and is not an endangered species. This again is a matter of supply chain management. The identification of the source of materials, especially for wood products where the manufacturer is unlikely to be the harvester of the timber in question, is difficult for the manufacturer as he is unlikely to have easy access to the necessary information. Including such sourcing information along with origin compliance information makes sense.
- Country of origin markings and other most-favored-nation applications. Further product information that is origin related, but distinct from origin, includes country of origin marking rules. These are the criteria that regulate the “Made in” tags and labels on products. Note that there is not a necessary relationship between preferential origin rules and the applicable marking rules. A good may comply with the RoO for a preferential agreement and enter duty free, but not be eligible to carry a “Made in” marking for the country that exported it. Conversely, a product

⁵ Legislation known as the Lacey Act.

may be marked “Made in” without meeting the origin criteria to qualify for the preferential tariff rate.

- Geographic designations of origin. These matter for products like Tennessee whisky, Peruvian or Chilean *pisco*, Mexican tequila, Parma ham, and champagne. To properly carry such designations, these goods must have been produced in their respective geographical areas. In case of a verification or enforcement action, importers and/or distributors must be able to document and prove that this is the case.
- “Buy America” and “buy China” regimes. In the context of public procurement programs, there are often restrictions on the nationality of goods eligible for procurement. This is the case of the “buy America” restrictions on some elements of the recent federal stimulus package in the US, and similar programs around the world. These programs tend to specify their own criteria for what constitutes “national” products eligible for public procurement, but the evaluation and documentation procedures are substantially identical.

As a further illustration of the interrelation of these issues, it is interesting to note that, in the Vietnamese government, RoO administration and product quality and safety policy are managed by a single trade ministry department. While this might seem to be combining unrelated fields of expertise, in fact it is recognition of the fact that these issues share a fundamental information management issue. In order to make claims in the international marketplace regarding quality or safety, exporters must be able to document their supply chains, identifying suppliers of key materials used.

This is no different from documenting compliance with RoO for preferential tariff treatment. As better systems and procedures are developed for management and presentation of origin-related information, it will only be sensible to include these other certifications and qualifications in the same systems. All will be necessary, and there are cost savings to be had by streamlining the information management and communication procedures and technologies.

4. CONCLUSIONS AND RECOMMENDATIONS

4.1 From “Ugly Duckling” to “Swiss Army Knife”

RoO are something of the “ugly duckling” of the international trading system. They tend to be technically complex, difficult for nonspecialists to understand, and suspected (not always unfairly) of being a mechanism for maintaining protective measures in a hidden corner of RTAs. Origin compliance can be costly, and the complexity can serve as a disincentive for the development of sophisticated and efficient international supply chains.

But in the evolving international trading system, the traceability of goods and materials is becoming indispensable, not just for purposes of preferential origin, but for environmental protection, consumer safety, and security purposes as well. Indeed, preferential origin may become incidental in the development of traceability systems, a by-product of tracking protocols developed for other purposes.

But that would seem to be putting the cart before the horse. Documentation and administration of preferential origin is an immediate concern, and systems are already in place or being developed that allow firms to manage origin. The logical sequence would be to turn the ugly duckling into a management tool that incorporates more aspects of the traceability agenda, becoming the all-purpose “Swiss army knife” of international trade traceability.

Information management tools designed for tracking and analyzing suppliers, supply chains, and rules can readily incorporate non-origin-specific information that must be maintained regarding these suppliers and supply chains for non-origin purposes, such as certification of wood products for export to the US, REACH certification for export to the EU, or carbon footprint in any future imposition of carbon taxes on international trade. The key is to recognize that traceability for these other purposes is an extension of the same origin-related information management challenges firms already face.

With this key similarity in mind, we identify three areas in which action is desired:

Reform of Origin Rules: Allow coequal RoO and extend cumulation. Coequality of RoO means that countries should identify a set of alternative RoO that can be considered of equal value in terms of establishing origin. Then, instead of limiting firms to a single alternative qualification method, give firms the option to choose among two or more substantively equivalent criteria for showing origin. This would provide greater flexibility to firms without undermining the purpose of the rules. This reform is most needed in unilateral preference schemes for promotion of development in LDCs.

Extension of cumulation involves permitting materials that qualify as originating in one country that benefits from preferences in a second country to be used in production of a subsequent good in a third country that benefits from the same preferences, with those materials being considered as originating in the third country. A first context in which this should be applied is in generalized system of preferences programs, allowing cumulation among beneficiaries and subsequently allowing cumulation across preference programs, both unilateral and reciprocal.

Reform of Origin Administration: Standardize origin administration and better define origin liability. These two issues are related. First, firms need predictability and transparency in the administrative aspects of origin compliance and documentation, both preferential and non-preferential. As discussed above, this allows for lower costs for firms, reducing the origin-related barriers to trade. Second, in cases where these administrative processes identify noncompliance, it is necessary to be able to clearly and predictably assign liability for duties, as well as any penalties. If importers act in good faith on fraudulent origin information provided by exporters, they should not be liable for penalties. The absence of well defined rights and responsibilities in claims of preferential market access lead to fears of onerous origin liability, and this uncertainty can serve as a disincentive to international trade and investment. Because importers and exporters generally reside in different international jurisdictions, coordination among governments, for the application of penalties for fraudulent claims by exporters as well as for the enforcement of contracts that do clearly define rights and obligations regarding RoO, is of vital necessity.

Embrace E-origin Traceability: Develop and promote integrated information systems. Because RoO, as well as the myriad environmental, security, and consumer safety certifications that have arisen in recent years, are all essentially information management issues involving the identification and tracing of materials and suppliers, the solution must lie in better integrated electronic information systems. While it is not necessarily the role of governments to develop such systems, governments, through customs administrations, should be prepared to encourage their development by others. This encouragement could take the form of a disposition to work with developers of systems in evaluating the sufficiency and reliability of information provided for purposes of compliance with customs requirements, possibly even to the extent of integrating private systems with public systems to allow the rapid transmission of information between them, thus giving greater certainty to international transactions and faster customs clearance times.

Trade facilitation as regards origin and other similar certifications of production processes is fundamentally an issue of information, and of defining which parties are responsible, and

liable, for which elements of that information. The objective should be to develop and integrate systems for managing this information in a way that promotes efficient production, allowing sourcing of materials from the broadest possible set of suppliers at the least administrative cost, thus promoting the economic success of firms and the safety and satisfaction of global consumers.

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