

Implications of Changing the ASEAN Rules of Origin

Executive Summary



In free trade agreements, rules of origin define requirements for determining when a good is considered the product of a party to the FTA and therefore eligible for preferential tariff treatment. Determining origin can be difficult when more than one country has contributed to the manufacturing of a good. Most origin regimes use some combination of four basic approaches to defining origin as none provides a perfect solution. At present, ASEAN's rules of origin are based largely on processing that results in a change in the *value* of the good. What are the implications of switching from a regime based on value addition to one based on processing in the ASEAN FTA area that results in a change in the tariff classification (CTC) of non-ASEAN input materials? The study focuses on the economic and administrative aspects of granting originating status when production results in a good that has a different tariff classification than non-ASEAN raw materials used in production.



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Using the CTC approach as a primary basis for rules appears preferable from an economic and administrative perspective. It offers benefits for border officials and traders alike. Because it is based on the tariff classification of goods, border officials will find it easier to implement and this could lead to simpler verification measures than is the case with the value-added approach. Though CTC will not be simple in all cases, it can be especially advantageous for small firms in advancing use of preferences and reducing traders' cost of compliance.



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Previous studies have reported that ASEAN preferences are underused. We found that the low margin of preference gives traders little incentive to assume the cost of compliance necessary to obtain preferences. At least initially, such costs include site visits and information verification. These may be negligible for big companies but are a serious impediment for new and small companies, which often do not even know about preferences as information about them and how to obtain them is scant. In addition, some traders decide not to apply for preferences because they fear audits, are reluctant to disclose financial information, and cannot meet onerous recordkeeping requirements.

ASEAN rules of origin have three conditions for preference eligibility: direct consignment, regional, final processing in the ASEAN area, and value content. The first two are not difficult to demonstrate or verify, so it appears that the value

condition drives up compliance costs. When the margin of preference is low, compliance costs discourage use of the CEPT. In effect, they lower the margin of preference and make preferences less attractive. When margins of preference are low, compliance costs must be reduced to make ASEAN preferential treatment more attractive. The “best practices” and proposed program for implementing new rules of origin provided in the companion paper on ASEAN Rules of Origin strategy address these issues.