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**THE EUROPEAN COMMUNITY'S PREFERENTIAL
RULES OF ORIGIN**

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**Expert Group Meeting on enhancing the export
competitiveness in textiles and clothing of the countries
of the ESCWA region**

Beirut 3-5 November 1999

The European Community's preferential rules of origin

Presentation by

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I. Introduction

This presentation will be divided into four parts.

I will begin by outlining in general terms the EU's preferential rules of origin for textiles and garments.

Next I will examine a feature of rules of origin known as *cumulation*. I will do this in the context of the EU-PLO Agreement rather than the EU-Jordan Agreement as you may have expected from the background papers for this meeting. Although the agreement with Jordan has been signed it is not yet in force and has not yet appeared in the Official Journal of the European Communities. Using the Palestinian Agreement, which has been published in the Official Journal¹, makes it easier for me to provide some useful bibliographical references in the printed version of my presentation. The rules of origin in the two agreements are essentially the same.

In the third section of my presentation I will look at the rules of origin applying in the EU's preferential agreements with the Maghreb countries, using the EC-Tunisia Agreement² as my reference point and highlight the differences between those rules and those applying in the context of EU-Palestinian trade.

And in the final section I will take a look into the future for rules of origin covering the whole of the Mediterranean area.

But first, why do we have preferential rules of origin and why is it important that they are understood and respected?

If the EC is to give preferential tariff access to its markets to goods from its trading partners, it needs to be certain that the tariff advantages are being enjoyed by goods that are truly of the partner country and not goods that are substantially products of countries with which we do not have preferential agreements eg Korea, Japan, the USA. The role of rules of origin is therefore to identify the products that are of the trading partner country.

To show that their products satisfy the rules of origin exporters must provide their customers with a certificate of origin, known in the context of preferential trade as a *proof of origin*^c. All preferential arrangements allow for these certificates to be checked for validity'. If the Community Customs office finds that the products covered by a certificate did not satisfy the rules of origin, the importer in the Community is required, under Community Customs law, to pay customs duty at the full rate, which for most garments, for example, is around 12% of the value of the consignment. A customer faced with such a bill for back duty is likely to ask his supplier for compensation. If not forthcoming he will, at the very least, think twice about placing any further orders. It is vitally important therefore for exporters proposing to use the benefits of the preferential rules of origin to make sure that they understand those rules and ensure that the products they sell as meeting those rules, do so.

1. The 'basic' rules of origin for textiles and garments

Anyone who has examined a typical origin protocol to be found in an Official Journal of the European Communities will probably declare the rules to be incomprehensible. I must admit that in some of the detail they are very complex. But for the most part, for the textile products that are likely to be exported from this region, they are relatively straightforward.

There is a very useful rule of thumb that when applied will often provide the answer to the question 'Does my product satisfy the rules?'. It is often referred to as the *two stage process rule*. If imported material is processed through two distinct stages of manufacture then the resulting product will have satisfied the rules of origin. For example, let us look at the case of a woven cotton shirt. If to make that shirt yarn is imported and woven into fabric (one stage) and the fabric then made up into garments (second stage) then the finished shirt will have satisfied the rules of origin. This rule is stated in the protocol as '*manufactured from yarn*'

Most knitted garments also satisfy the '*sufficient working or processing*' requirement by being manufactured from the yarn stage. The ubiquitous T-shirt is a typical garment that is subject to this rule^d.

If the product to be exported to the Community is cotton fabric then stage one is to produce the yarn and stage two weave the fabric. These two stages of fabric manufacture represent the basic concept of a product undergoing sufficient working or processing to acquire '*originating status*' and would typically be stated in the rules of origin as '*Manufacture from natural fibres*'^e.

There are of course variations on those general themes. For example if you are producing printed fabric you can skip the normal first stage (weaving the fabric) and start from imported unprinted fabric, put it through at least two preparatory or finishing processes and print it and the end product will have satisfied the rules of origin if the value of the unprinted fabric does not exceed 47.5% of the ex-works price of the finished fabric^b. The printing and other processes carried out on the imported unprinted fabric are seen as representing sufficient working or processing.

Similarly an embroidered garment can be made from unembroidered fabric rather than from the yarn stage which is the case for an unembroidered garment. This time the value added must be 60% or put another way the value of the unembroidered fabric used must not exceed 40% of the ex-works price of the finished garment^c.

Just as printing and finishing of fabric is seen as equivalent to the two stages of processing needed to confer origin, so the manufacture of an embroidered garment from unembroidered fabric is considered to represent sufficient working or processing.

The final thing I would say about the basic rules of origin is that they are common across most of the Community's preferential trading arrangements. So they will appear in identical terms in, for example, both the EC-PLO Agreement and the EC-Tunisia Agreement.

2. Bilateral cumulation

So far we have looked at situations where both stages making up sufficient working or processing take place in the same country. The EC's rules of origin now make it possible for only one stage of processing eg fabric to garment, to take place in the country of final production. This is possible through a feature of the rules of origin known as 'cumulation'.

In the context of their trade with the EC, each of the countries in this region enjoys a form of cumulation known as 'bilateral' cumulation^d. Under this provision products from the Community meeting the origin rules in their own right - products that are described as originating products - may be used as if they were products originating in the country where the final product is manufactured. For example, we saw earlier that to make a garment that satisfies the origin rules it is necessary first to weave the fabric and then make-up that fabric into a garment. Under the bilateral cumulation provisions, by using a fabric of Community origin, the garment will satisfy the rules of origin by making-up alone.

There is therefore a considerable advantage to the garment manufacturer in using fabric of Community origin if his primary market for the finished product is the EC.

Many retailers in the Community are encouraging their suppliers to consider the advantages of the Community's preferential trading arrangements and in particular the provisions of bilateral cumulation. Lower production costs give the countries of this region an immediate advantage. By using Community originating materials that advantage can be turned into a very significant commercial edge over competitors because their finished products will then enter the Community market at zero rates of customs duty, a saving of around 12%.

3. EU - Maghreb cumulation

In the background papers sent to me in advance of this meeting I was advised that this session on rules of origin will include an analysis of the terms of the Euro-Mediterranean Partnership agreements concluded between the EU and each of the North African Countries on the one hand and with Jordan on the other. The rules applicable to the EC-Jordan Agreement are the bilateral cumulation rules I have already outlined and are similar to the rules contained in the published EC-PLO Agreement. The rules of origin to be found in the EC's Agreements with the Maghreb countries are based on a form of cumulation known as 'full cumulation'.

Where bilateral cumulation is the adding together of products that already have originating status, full cumulation provides additionally for the aggregation of any working or processing carried out in one country within a given group of countries with working and processing carried out in another^d.

Using the example of a woven shirt, full cumulation would allow fabric to be made up in the EC (or Morocco or Algeria) from imported yarn and for that yarn to fabric stage (which in itself does not create a fabric satisfying the rules) to be added together with the making up into a shirt in Tunisia. The finished shirt would satisfy the two stage criteria by the adding together of the stages carried out in the two countries and could be exported to the Community where no duty would be charged.

4. The future

The Euro-Mediterranean Partnership was launched at Barcelona in November 1995 and set a target of 2010 for the introduction of a free trade area encompassing the Community and its partners. The idea is that this will be implemented through a framework of new agreements not only between the

Community and its Mediterranean partners but also between the partners themselves. This new partnership would focus, *inter alia*, on harmonising rules and procedures, in particular with a view to the progressive introduction of cumulation of origin.

As we have seen, the Community's current agreements with its partners in the Eastern Mediterranean area are based on bilateral cumulation of origin, that is to say cumulation between the Community and the other party to a particular agreement. Regional cumulation will build on that basic concept and allow, in addition, cumulation between the countries in the zone. This is often referred to as '*diagonal cumulation*'. This means for example that fabrics of Egyptian origin may be used in Palestine to make garments that will then qualify for preferential tariff access to Community markets.

But such a system of regional cumulation will only function fairly if all partners in the zone apply the same criteria for determining origin. This means that each country will need to draw up an agreement with each of the other countries in the region that mirrors, in terms of the rules of origin to be applied in trade between them, the rules contained in their own agreement with the Community. Once these agreements are in place, cumulation of origin among the countries of the region can begin.

That begs the question, 'What do we mean by *the region*?'

The original proposal of the European Commission was that cumulation throughout the Mediterranean would be phased. The first phase would involve the setting up of two hubs, one comprising the Maghreb countries in North Africa, the other comprising the partner countries to the East.

Some Mashraq countries however expressed an interest in cumulation from the outset with the Maghreb countries. A new approach therefore needs to be found.

If there is to be cumulation throughout the Mediterranean, what type should it be? After all the Maghreb countries have a system of full cumulation in place. Elsewhere only bilateral cumulation is in use.

Technical solutions are always possible. But along with the technical solutions comes the need for additional administrative mechanisms. These are best introduced progressively. Certainly this has been the Community's experience gained over very many years of preferential trading partnerships.

For example, the Community and its EFTA and Central and Eastern European partners have established a pan-European cumulation zone which is based on the concept of diagonal cumulation between each of the partner countries'. This in

itself was a development of earlier bilateral cumulation agreements. The development of the 'Europe' Agreements around a system of full cumulation is currently under consideration.

We have, or are in the process of establishing, new bilateral agreements between the EC and its Mediterranean partners. The next step would be the introduction of a system of diagonal cumulation. There is no technical reason why this could not be introduced from the outset encompassing both ends of the Mediterranean rather than the two hub approach originally proposed by the Commission. This would allow fabric originating, say, in Egypt, ie fabric that has gone through two stages of processing, to be made up into garments in Tunisia and for those garments to gain preferential tariff access to the EC market.

Full cumulation calls for the introduction of additional administrative co-operation mechanisms and a greater level of involvement by the commercial operators themselves. If agreements are to function successfully, it is vitally important for all those involved to have a clear understanding of their roles and responsibilities. Experience has shown that this is best achieved through the progressive introduction of cumulation. This will be the line taken by the Commission who can be expected to resist any proposals for full cumulation across the Mediterranean as a whole.

Conclusions

The scope for using the EC's preferential rules of origin to enhance the competitiveness of textile manufacturers in this region is, I would suggest, considerable. The EC's rules of origin when looked at in their entirety are complex. But do not be put off by that. For the most part, for the products that are likely to be the principal textile exports from this region, the rules present little or no difficulty. Bilateral cumulation with the EC is there now to be taken advantage of. Regional diagonal cumulation would greatly enhance those opportunities for increased trade.

The jury is still out on the question 'who benefits from full cumulation?'. My personal view is that it is the Community rather than its partner countries. So if I may finish with some advice it would be this. Negotiate for what is 'achievable' - diagonal cumulation - and avoid delaying its implementation by seeking full cumulation from the outset.

¹ OJ L 187 Volume 40 dated 16 July 1997.

² OJ L 97 Volume 41 dated 30 March 1998.

³ See Article 15 et seq of Protocol 3 of the EC-PLO Agreement OJ L 187 of 16 July 1997.

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- ° See Article 30 et seq of Protocol 3 to the EC-PLO Agreement.
 - ° The Customs Code (Council Regulation 2913/92 OJ L 302 Vol 35 19.10.92) and its Implementing Regulation (Commission Regulation 2454/93 OJ L 253 Vol 36 11.10.93).
 - ° See rule for goods of Tariff Chapter 62 shown in Annex II to Protocol 3 of the EC-PLO Agreement OJ L 187 Vol 40 of 16.7.97.
 - ° See rule for goods of Chapter 61 in Annex II to Protocol 3 of EC-PLO Agreement.
 - ° See rule for cotton fabric of tariff headings 5208-5212 Annex II to Protocol 3 to EC-PLO Agreement.
 - ° See rule for cotton fabric of tariff headings 5208-5212.
 - ° See rule for women's clothing ex Chapter 62 Annex II to Protocol 3 to EC-PLO Agreement.
 - ° Article 3 of Protocol 3 to EC-PLO Agreement.
 - ° Article 5 of Protocol 4 to the EC-Tunisia Agreement (OJ L 97 Volume 41 dated 30 March 1998).
 - ° See for example Decisions 3/96 and 1/99 of the Association Council amending Protocol 4 to the Europe Agreement establishing an association between the EC and the Czech Republic (OJ L 343 Vol 39 31.12.96 and OJ L 38 dated 12.2.99)