Chapter 4

Towards an Enabling Set of Rules of Origin for the Regional Comprehensive Economic Partnership

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Chapter 4

Towards an Enabling Set of Rules of Origin for the Regional Comprehensive Economic Partnership

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With overlapping, multiple free trade agreements (FTAs), such as the case of the Association of Southeast Asian Nations (ASEAN) and the various ASEAN+1 FTAs, complications could arise that run counter to the economic integration objectives of the East Asian Region. Forging the Regional Comprehensive Economic Partnership (RCEP) amongst ASEAN and its FTA partners is a next logical step. How facilitative the rules of origin (ROO) provisions are could prove crucial in maximising the potential benefits. This chapter revisits the nature of ROO in ASEAN and the various ASEAN+1 FTAs to examine the surrounding constraints and issues as well as to provide recommendations on a beneficial set of ROO for the RCEP, and serve as input for policy makers and negotiators.

1. Introduction

The global arena in recent decades has witnessed a rise in regional and bilateral free trade agreements (FTAs). Asia came in late but has now become very active in FTA engagement, with the Association of Southeast Asian Nations (ASEAN) at the hub of most of the FTA activity. (Kawai and Wignaraja, 2010) This Asian trend arose from a combination of factors, including, amongst others: (1) the growing FTA alliances in other parts of the globe, (2) the 1997 Asian financial crisis, and (3) the protracted World Trade Organization (WTO) impasse. The first brought about the need for ASEAN FTAs in the region as a defensive mechanism. The second highlighted the need for regional cooperation. The WTO impasse created a need for an alternative mechanism more abreast with the pace of globalisation and the dynamism of the East Asian region. Perhaps the more proactive and compelling motivation, which is related to the last point, is the growing importance of production networks in the region (Urata, 2004). It was only a matter of time before market-driven regionalisation took the more formal route of forging regional agreements. Currently, there are six major FTAs involving ASEAN and the other East Asian countries: ASEAN, the ASEAN–Korea FTA (AKFTA), the ASEAN–China FTA (ACFTA), the ASEAN–Japan Comprehensive Economic Partnership (AJCEP), the ASEAN–Australia–New Zealand FTA (AANZFTA), and the ASEAN–India Free Trade Agreement (AIFTA).

The formation of these agreements could be viewed as a feasible step towards deepening East Asian integration, especially with ASEAN as a hub. However, having separate ASEAN+1 FTAs could create problems of its own, such as the oft-cited complication of a noodle bowl effect. This side effect could ultimately run counter to the underlying objectives of these FTAs, which include creating a more integrated market and production base, leveraging on each other's strength, and lowering the cost of doing business. Indeed, the more FTAs a country or region is engaged in, the more complex the web it creates that could add to the cost of doing business. This concern has particular bearing on the overlapping rules of origin (ROO) utilised by respective FTAs. Forging the Regional Comprehensive Economic Partnership (RCEP) amongst ASEAN and its FTA partners is a next logical step. And the ROO regime the RCEP adopts could prove crucial in maximising the potential benefits and attaining the objectives of East Asian regional integration.

In this chapter we aim to provide inputs for policy makers and negotiators, and recommendations on the beneficial set of ROO for the RCEP. Towards this end, we start in the next section with the underlying principles and objectives of the RCEP to provide the context of the discussion and formulation of the recommendations. In Section 3 some background on the basic ROO used in FTAs and the nature of ROO in ASEAN and the various ASEAN+1 FTAs is discussed. This section uses the findings and datasets from previous ERIA studies by the author on ROO in the East Asian region. In Section 4 we provide the analysis of the constraints and issues in formulating the best practice ROO for the RCEP, leading to our recommendations.

The study also benefitted from interviews and/or surveys of key people from both industry and government to validate the findings and recommendations. These provided further insights, suggestions, and better understanding of the difficulties and problems currently faced in dealing with ROO.

2. Underlying Principles and Objectives

In negotiating the RCEP, the central objective of the parties, as stated in the RCEP negotiation framework, is 'to achieve a modern, comprehensive, high-quality and mutually beneficial economic partnership agreement amongst the ASEAN Member States (AMS) and ASEAN's FTA Partners'. Along these lines, the guiding principles include the following:

- The RCEP will have broader and deeper engagement with significant improvements over the existing ASEAN+1 FTAS, while recognising the individual and diverse circumstances of the participating countries.
- The RCEP will include provisions to facilitate trade and investment and to enhance transparency in trade and investment relations between the participating countries as well as to facilitate the participating countries' engagement in global and regional supply chains.

ROO are integral to any FTA. Any FTA would have a (negotiated) set of ROO to ensure that trade preferences from the agreement are enjoyed primarily by the contracting parties. Only goods that comply with the agreed-upon ROO can enjoy duty-free preference

provided by the FTA. While there should be rules to distinguish members from non-members, these ROO could act as trade barriers themselves. The more restrictive the ROO are, the greater the trade barrier, conceivably to the extent of eroding the preferential benefits from the FTAs. The problem becomes more complex when there are overlapping, multiple FTAs, such as in the case of the ASEAN and the various ASEAN+1 FTAs. Setting the ROO should thus not be just about trade deflection.[1] Perhaps even more so, it should be trade facilitating as well. In addition, considering global developments and the current regional context, there is less need for restrictive ROO. Sustained global trade liberalisation made possible under the General Agreement on Tariffs and Trade (GATT)/WTO has already substantially brought down most-favoured nation (MFN) tariffs. Moreover, the RCEP is a big group of countries with intraregional trade comprising more than half of its total trade. As such, ROO in the RCEP should be more concerned about trade facilitation, in line with its objectives.

3. ROO in the ASEAN and the ASEAN+1 FTAs

The issue of determining origin was not given much attention under the GATT/WTO in the early stages, leaving individual country with the right to determine their own rules for the purpose of applying non-preferential MFN tariffs. This right to determine the applicable ROO is even more strongly argued for in the Generalised System of Preference (GSP) by donor countries as the preferences are unilaterally granted. The same practice applies to ROO in preferential trade agreements.

With the rise in international production sharing and technological innovation in transportation and telecommunications, origin determination has become increasingly difficult. Very few products today can claim to be solely produced in one country. This has made ROO a key concern in FTA negotiations.

1. Trade deflection occurs when a non-FTA member is able to enjoy the preferential tariffs that supposedly only FTA members are eligible for. Without restricting ROO, this could happen through trans-shipment of products from a non-FTA member to high-tariff FTA member through a low-tariff FTA member. Even if the tariff for a product is relatively high for all the FTA members, trade deflection could still occur if the product enjoys duty-free importation (or duty-drawback) under some manufacturing incentives programme.

3.1. The Basic ROO used in FTAs

Discussions were held in GATT/WTO about harmonising the non-preferential ROO, but no multilateral discipline was agreed upon, mainly because of the clause 'equally for all purposes' in the proposed Agreement on Rules of Origin (ARO).[2] Nonetheless, the Kyoto Convention (originally adopted in 1973 and revised in 2000) provided general concepts for determining origin, used also as guidelines for ROO in most trading arrangements. First, goods can be categorised as either wholly obtained (produced) or non-wholly obtained (produced). This yields the first basic ROO – the 'wholly obtained' (WO) criteria. WO would apply to goods that are produced or 'obtained' domestically and is thus a clear basis for conferring origin.

For non-wholly obtained goods, determination takes into account whether a minimal operation was carried out or if the process involved *substantial transformation*. Minimal operation refers to simple processing that is negligible enough for the goods to still merit originating status. Packaging, for example, would not change the status of origin of the product. Rules of origin for non-wholly obtained goods are based on *substantial transformation* criteria.

Three basic approaches are used to determine whether *substantial transformation* has occurred to merit originating status. The first is the *value-added criterion (VA)*, which requires a (minimum) percentage of value added created at the last place of the production process. The second is the *tariff-heading criterion*, also referred to as change in tariff classification (CTC), which requires that processing in the exporting country results in a product classified under a different heading in the customs tariff classification of the Harmonized System of Tariff Nomenclatures than its intermediate inputs. The third is the *specified process rule (SPR)* or *technical test*, which determines, on a case-by-case basis, specific production activities or specific processing operations that may confer originating status. This could be a 'positive test', which would confer originating status if certain production or sourcing processes are complied with, or a 'negative test' which specifies that certain production or sourcing processes would not confer originating status

2. Balestrieri, 2014.

(UNCTAD, 2002). A prime example of the SPR is the so-called *yarn forward* (sometimes from fiber to fabric) or *a two-step rule* for textile and garment products.

3.2. Wholly obtained (WO)

The WO as ROO is obviously very restrictive if applied to mean 100 percent VA (regional or local) in products at higher levels of processing (stages of production). However, following the Kyoto Convention, with listing of wholly obtained products (usually in Chapters 1 to 15 of the HS code) and in waste and scraps, some FTAs identify in their Product Specific Rules (PSRs) the HS lines that are WO, which almost makes conferring origin of these goods automatic when classified under these HS codes. For some FTAs, specifically the AJCEP, the concept behind WO is operationalised as CTC.[3] Hence, WO and CTC for Chapters 1 to 15 could be equivalent in practice (with regards to ease/cost of compliance).

Table 4.1 shows the main ROO for Chapters 1 to 15. There is convergence for the ASEAN Trade in Goods Agreement (ATIGA), the ASEAN–Korea Free Trade Agreement (AKFTA), and the ASEAN–Australia–New Zealand Free Trade Agreement (AANZFTA), using generally WO while AJCEP uses Change in Chapter (two-digit classification). In contrast, the ACFTA still applies the general rule of RVC(40). From the point of view of manufacturers, for these chapters, these rules would most likely result in the same eligibility for compliance. As such, what type of ROO the RCEP should adopt should not be the issue as long as it takes into account what is most efficient and easiest to administer.

3. In most cases, for ROO a change in chapter (CC) is required (sometimes with limitation as to where change is coming from) and in other cases, simply a change in tariff heading (CTH).

Table 4.1: Main ROO for Chapters 1 to 15 in ATIGA and ASEAN+1 FTAs

Chapter	Heading	Product Description	ATIGA	AKFTA	ACFTA	AJCEP	AANZFTA
1		live animals	WO	WO	RVC(40)	CC	WO
2		meat of animals	RVC(40) or CC	WO	RVC(40)	CC excfrch1*	CC
3		fish, live, chilled frozen	WO	WO	RVC(40)	CC	WO
4		milk, cream, butter, cheese	RVC(40) or CTSH	WO	RVC(40)	CC	RVC(40) or CTSH
	407	eggs in shell	WO	WO	RVC(40)	CC	WO
	410	honey	WO	WO	RVC(40)	CC	WO
5	501	human hair, unworked	WO	WO	RVC(40)	CC	WO
6		other live plants and flowers – live, cut, foliage, parts	RVC(40) or CTSH	WO	RVC(40)	CC	RVC(40) or CTSH
7		Vegetables – fresh, chilled	WO	WO	RVC(40)	CC	WO
8	801	coconuts – desiccated	RVC(40) or CC	WO	RVC(40)	CC	RVC (40) or CC
	802	other nuts, in shell	WO	WO	RVC(40)	CC	WO
	803	Bananas, including plantains, fresh or dried	RVC(40) or CC	WO from any AKFTA Party	RVC(40)	CC	RVC(40) or CC
	804–810	other fruits and nuts, fresh	WO	WO	RVC(40)	CC	WO
9		coffee, tea	RVC(40) or CC	WO	RVC(40)	CC	RVC(40) or CC
			RVC(40) or CTSH	RVC(45)	RVC(40)	CC	RVC(40) or CTSH
		spices	RVC(40) or CC	WO	RVC(40)	CC	RVC(40) or CC
10		wheat, rice, other cereals	WO	WO	RVC(40)	CC	WO
11		flour, groat, pellets, etc.	RVC(40) or CC	WO	RVC(40)	CC	RVC(40) or CC

			RVC(40) or CC	WO from any AKFTA Party	RVC(40)	CC	RVC(40) or CC
		starches	RVC(40) or CC	CC or RVC(40)	RVC(40)	CC	RVC(40) or CC
12		soya beans, ground nuts, oil seeds, etc.	WO	WO	RVC(40)	CC	WO
		flour and meals of seeds	RVC(40) or CTH	WO	RVC(40)	CC	RVC(40) or CTH
		seeds for sowing	RVC(40) or CC	WO	RVC(40)	CC	RVC(40) or CC
		plants & parts primarily for perfumery, pharmacy, insecticide	WO	WO	RVC(40)	CC	WO
13		vegetable gums, resins	WO	WO	RVC(40)	CC	WO
		saps and extracts	RVC(40) or CC	WO	RVC(40)	CC	RVC(40) or CC
14		bamboos, rattan, etc. for plaiting	WO	WO	RVC(40)	CC	WO
		for stuffing	RVC(40) or CC	WO	RVC(40)	CC	RVC(40) or CC
15		fats and oils from plants and animals	RVC(40) or CC or SPR by refining	CTH or RVC(40)	RVC(40)	CC	RVC(40) or CC or SPR by refining

Note: * excluding change from Chapter 1.
Source: Author's tabulation.

3.3. Regional Value Content (RVC)

A major advantage of the RVC is that, in essence, it is a direct measure of *substantial transformation.* Nonetheless, the problems with the use of RVC are well known. Most often cited is that it is subject to exchange rate and price fluctuation, which leads to uncertainties and adds to compliance and administration costs. Another major difficulty is that firms are hesitant to disclose price and cost data and other required information. Even for large

firms, this could entail substantial costs, especially for those with multiple products. There could, for example, be a need for separate accounting and extra personnel to take care of proving origin. There are even greater difficulties for small and medium enterprises (SMEs). Most SMEs, especially in least developed countries (LDCs), lack sophistication and know-how in accounting and finance as well as a formal organisation with a readily available flow chart. Required documentation for export and origin determination may not be easily produced.

Other rules, however, might not make some products eligible for the FTA preference. In addition, there is an advantage of RVC for goods using numerous inputs or components.

The RVC is most commonly used as ROO in ATIGA and the ASEAN+1 FTAs for electronic and automotive products. As an illustration, table 4.2 presents the ROO for Chapter 87 (automotive products) in ATIGA and the ASEAN+1 FTAs.

Table 4.2: ROO for Automotive Products (Chapter 87) in ATIGA and the ASEAN+1 FTAs

ATIGA	**HS lines**
RVC(40) or CTH	9
RVC(40)	66
RVC(40) or CTH or Specific Rule	1
AKFTA	**HS lines**
CTH or RVC(40)	51
RVC(45)	25
ACFTA	**HS lines**
RVC(40)	76
AJCEP	**HS lines**
RVC(40)	47
RVC(40) or CTH	29
AANZFTA	**HS lines**
RVC(40) or CTH	22
RVC(40)	50
RVC(40) + CTSH	3
RVC(40) or CC	1
HS 87 group total HS lines	**76**

Source: Medalla (2011).

3.4. Change in Tariff Classification (CTC)

With difficulties faced in the use of RVC, many FTAs also make use of CTC as a rule for determining origin. Again, the advantages are well known. These include the simplicity in application and verification as well as the clarity and predictability of the method. The main disadvantage is that it relies on the use of the Harmonized System, which is not designed to reflect degree of substantial transformation. Many products with enough originating materials may not qualify because the level of classification between inputs and outputs remains the same. It could also be a disadvantage to firms using numerous inputs. In addition, the HS code used could sometimes be interpreted differently across countries. This interpretation can sometimes be people dependent, that is, it would depend on the customs official receiving the goods. Any such problems could of course be resolved in due course, but they would already have entailed losses for the importer/exporter.

3.5. Specific Process Rule

Bearing in mind the objectives of the RCEP, it should ideally be used only as a supplemental test of origin because of its rigidity and the difficulty of defining a process test for the enormous array of products. Moreover, with technological change occurring more and more rapidly, such rules should be continuously updated to accommodate changes in production methods and promote deeper regional integration, with freer flow of products and factors of production. The negotiation process to come up with SPRs could also be more susceptible to industry lobby groups dictating outcomes in their favour, because drafters and administrators would have to rely upon the industry for technical information (La Nasa, 1995). SPR should be used sparingly for these reasons, but most FTAs have commonly used SPRs for certain products, notably textiles and garments.

On the whole, that there are advantages and disadvantages to the various criteria points to the need to provide exporters with some options.

4. Profile of ROO in the ASEAN and the ASEAN+1 FTAs

ATIGA and ASEAN+1 FTAs use a General Rule (GR) for ROO. ATIGA, AANZFTA, AKFTA, and AJCEP share the same GR of coequal rule of RVC or change in tariff heading (CTH). Product-specific rules are refinements of the GR resulting from the ROO negotiations. An interview with a government official describes the process for some FTAs as a series of steps. The initial step entails going through the entire list of products from which first of all the GR is determined and agreed on and a second step involves negotiating PSRs, which are a result of more in-depth negotiations.

In the case of ASEAN, at its early stage, the AFTA ROO adopted RVC(40) as the general rule. However, studies found low utilisation of AFTA and identified difficulties in the RVC criterion as one of the reasons for it. Hence, subsequent reforms were sought and implemented, amongst them the introduction of CTC as a coequal rule. In ATIGA, which was implemented in 2009, the general rule adopted is the coequal rule of RVC(40) or CTH, substantially relaxing its ROO regime.

Nonetheless, PSR negotiations could lead to either more restrictive ROO (protection) or more liberal ROO (exporter-led). Usually, if this leads to the adoption of additional specific requirements (e. g., about a specific process or where inputs/materials come from), they become more restrictive.

Medalla (2011) provides a mapping of the ROO of ATIGA, ASEAN–China FTA (ACFTA), AKFTA, AJCEP, and AANZFTA. On the whole, the study finds numerous types of ROO used across ASEAN and ASEAN+1 FTAs, even after grouping together similar types in one category. As such, there could be more variation within each grouping. (See Table 4.3.)

The variation arises within and amongst FTAs because of the differences in the application of the basic ROO discussed above. In general, the variation is due to the following:

- The basic ROO could be used in some combination. This could be of two types: either in a more liberal manner as options (the so-called coequal rules) or in a more restrictive manner as ‘plus’ rules where two or more rules need to be complied with.
- For SPR, there would different specific processes required for different products across different FTAs. This usually happens in the case of textiles and garments.

- For RVC, there could be a variation in the cut-off level used. For example, RVC(40) – regional value content of no less than 40 percent or RVC(35) –regional value content of no less than 35 percent.
- For CTC, there would be variation in the level of classification where change is required. For example, a change in chapter (CC), a change in tariff heading (CTH), or a change in tariff subheading (CTSH) across products and across different FTAs.
- On top of these, there could be additional specific requirements specified for different products for different FTAs. For example, CTSH 'except change coming from some classification or provided the materials are sourced' accordingly, etc.

Table 4.3: Frequency by Type of ROO Used in ASEAN+1 FTAs

ROO Type	ATIGA	AKFTA	ACFTA	AJCEP	AANZFTA
Single Rule					
WO	185	458	8	3	294
CC		61	1	735	248
CTH		4		137	107
CTSH				8	
RVC(<40)		36			
RVC(40)	147	22	4659	219	68
RVC(>40)		6			
CC with exception*				258	3
CTH with exception*				20	10
Various**		3			43
Liberal Coequal Rule					
RVC(40) or CTH	2782	4076	122	3057	2204
RVC(40) or CTH or SPR					24
RCV(40) or CTSH	706	61		33	1072
RVC(40) or CTH or RVC(35) + CTSH	125				195
RVC(40) or CTH or Textile Rule	340				6
RVC(40) or CC or Textile Rule	453				
Subtotal	4406	4137	122	3090	3501
% share in total	84.3%	79.2%	2.3%	59.2%	67.0%
Less Liberal Coequal Rule					
RVC(40) or CC	437	487	7	126	583
Various**	49	10	427	628	367
Total # of 6-digit HS(2002) Lines	5224	5224	5224	5224	5224

Source: Medalla (2011).

As expected, ACFTA uses RVC most extensively as it uses RVC(40) as the general rule. There have been some concessions for some products (mainly in textile and garments) where reforms were introduced in these PSRs that make use of other options. In contrast, AJCEP relies more on CTC. This follows the principle that CTC is simpler and likely to be easier to apply and comply with. However, AJCEP uses a lot of exceptions either in terms of specifying where change can (or cannot) come from and where certain sources of inputs should come from.

As mentioned above, ATIGA has been undertaking ROO reforms, which came up with PSRs that are generally intended to encourage better utilisation of the FTA. As a result, ATIGA has more HS lines with coequal rule using 'RVC(40) or CTSH,' which are more liberal than the general rule [RVC(40) or CTH]. AANZFTA, which was concluded later, provided for even more HS lines with the more liberal coequal rule of 'RVC(40) or CTSH.'

5. Analysis and Recommendations

Medalla (2011) found significant convergence amongst four of the five East Asian FTAs covered in the study (ATIGA, AKFTA, ACFTA, AJCEP, and AANZFTA).[4] This is indicated by the share of (6-digit) HS lines with the same, or nearly the same, ROO. In particular, 28 percent of HS lines have the same ROO for four out of the five FTAs. Moreover, for almost the same number of HS lines, there is near convergence with three FTAs having the same ROO and one or two FTAs having more liberal options (usually using CTSH instead of CTH). In total, there is near convergence in more than half (55 percent) of the HS lines for four out of the five FTAs. This arises mainly from their use of the common general rule – RVC(40) or CTH. (See Table 4.4.)

[4.] The discussion excludes the ASEAN–India FTA, which at the time of writing still only used the general rule of CTSH+RVC35.

Table4.4: ROO Convergence Incidence (excludes ASEAN–India FTA)

Level of convergence	# of 6-digit HS lines	% of Total
For all 5 FTAs	**181**	3.5%
Near Convergence (with more liberal options in some cases)	137	
Same ROO for 5 FTAs	44	
For 4 FTAs	**2,871**	55.0%
Near Convergence (with more liberal options in some cases)	1,407	
Same ROO for 4 FTAs	1,464	28.0%
For 3 FTAs	**630**	12.1%
Near Convergence (with more liberal options in some cases)	312	
Same ROO for 3 FTAs	318	
For 2 FTAs	**1,027**	19.7%
Near Convergence (with more liberal options in some cases)	728	
Same ROO for 2 FTAs	299	
Different ROO across FTAs	**515**	9.9%
Total # of HS Lines (6-digit)	5,224	100.0%

Source: Medalla (2011).

1. Implications for the RCEP

Multiple FTAs (e.g. bilateral FTAs, ASEAN, ASEAN+1) and corresponding multiple ROO create many problems. For one, it could create confusion for exporters about which FTA and ROO to use. Even for large companies with the competence to cope with ROO, this could increase costs if they have to deal with multiple countries in ASEAN (both as exporter and importer). These companies would need to have more complicated accounting methods, more detailed information, and a more comprehensive database[5] and would usually need to deploy a designated team or employ a third party to manage the additional requirements. On the part of the authority that issues the Certificate of Origin (COO), it could make the process of issuance of the COO more complex, requiring greater competence to examine, verify, and issue COO. Hence, multiple, non-uniform ROO across

[5] The firm would need proper attribution of which inputs go to what outputs and markets, which is difficult given multiple products and joint production processes.

multiple FTAs could result in increased costs. Indeed, according to the survey of firms carried out for this study,[6] firms considered the harmonisation of ROO to be very useful.

For the RCEP, however, it is not only harmonisation that matters. In particular, harmonisation upwards of the various ASEAN+1 FTAs is critical.

The case of Japan could be instructive for the RCEP. Japan has bilateral FTAs with most ASEAN countries. At the same time, it has a regional FTA with ASEAN–AJCEP. Thus, an ASEAN country exporting to Japan has two options for using trade preference – AJCEP or the Japan Bilateral EPA (JBEPA). The exporter, if given the right information, would choose whichever would yield larger benefits. This would depend on two factors:

- the difference in the margin of preference (MOP) between AJCEP and JBEPA;
- the ease/cost of complying with the respective applicable ROO.

Currently, there is very little utilisation of AJCEP in ASEAN countries that have a bilateral FTA (JBEPA) with Japan. The main reason is the faster reduction in tariffs for the bilateral FTA and thus a larger MOP, but this is also possibly due to a more liberal ROO in the JBEPA (Medalla, 2011). Eventually, for both AJCEP and JBEPA, there would be zero difference in the MOP when tariff reduction schedules are both completed (assuming that they have the same tariff coverage for tariff reduction). Thus, when that time comes, only the ROO with the same MOP would matter. The FTA with the best (i.e. more liberal and easier to comply with) ROO would prevail. If the ROO for the bilateral FTA (JBEPA) are more liberal on the whole, AJCEP will become, in effect, only nominal. Of course, it could be mixed. Some products could have a more liberal ROO in JBEPA than AJCEP and vice versa for other products. The result, in any case, is that AJCEP added another layer of ROO, and no harmonisation is effected. Thus, for AJCEP to be more than nominal, it should harmonise the ROO of its bilateral FTAs at the most liberal ROO. This does not mean a uniform ROO across products since different products have different characteristics and sensitivities.

In parallel, there are the various ASEAN+1 FTAs and the proposed RCEP amongst the same countries. Hence, there could be similar implications for the RCEP and ASEAN+1

[6] A report on the survey/interviews is found in the Annex of this chapter. Our findings are consistent with the results of a survey of firms carried out by JETRO on FTA utilisation of Japanese firms.

FTAs. If the RCEP harmonised the ROO of the various ASEAN+1FTAs at less liberal ROO, the result could be either:

- the RCEP adds another layer of ROO (and FTAs); or
- the RCEP is only nominal, at least from the perspective of ASEAN, which already has an FTA with all the negotiating parties of the RCEP.

For the dialogue partners, there could still be additional advantages from the RCEP even with less liberal ROO, because there are no existing bilateral FTAs amongst them (except for Japan–India). Even then, the benefits for these countries are fewer as cumulation is limited with restrictive ROO.

Hence, the bottom line is that ideally, the RCEP should adopt the most liberal ROO per product amongst ATIGA and the various ASEAN+1 FTAs.

There are, of course, the usual difficulties in harmonisation upwards (seeking the most liberal ROO amongst the ASEAN Trade in Goods Agreement [ATIGA] and ASEAN+1 FTAs). The protectionist pressures for some products could be strong. Some products could be more difficult than others in terms of finding a common, liberal ROO. The choice of which is the optimal ROO will also be more difficult if there is a wide divergence in the ROO of the different ASEAN+1 FTAs. There are also technical and administrative concerns to consider.

Nonetheless, harmonisation upwards should not be a problem for ASEAN. Indeed, it is in its interest that the RCEP should harmonise to the most liberal ROO, as discussed above. The difficulties might lie with ASEAN's dialogue partners – in particular China, Korea, and Japan – which have no FTA amongst them and tend to lean more towards less liberal ROOs than ASEAN. Will the dialogue partners be willing to accord liberal ROO to ASEAN (as this could imply a more liberal ROO than provided under the respective ASEAN+1 FTA) and to each other? Australia and New Zealand had been generally leaning towards liberal ROO in partnership with ASEAN countries. The results of email interviews conducted with New Zealand policy makers are consistent with this observation (i.e. that New Zealand would seek the most liberal ROO regime for the RCEP). Australia would most likely be similarly

inclined. How amenable will the other ASEAN dialogue partners be to relaxing the ROO for contentious products?

Some product groups are more difficult than others (e.g. textile and garments) in terms of harmonising to the most liberal ROO in the RCEP. Some dialogue partners might find it more difficult than others, especially India and China.

Table 4.5a: ROO for Chapters 25 to 39

Chapter	Product description	ATIGA	AKFTA	ACFTA	AJCEP	AANZFTA	# of HS lines w/ these ROO	Total # of HS lines in category
25	iron pyrites, graphites, quartz, calcium phosphates, etc.	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTH	**68**	**70**
26	iron, other meta, ores, and concentrates	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTH (GR)	24	**36**
	– slag, dross, scaling, and other wastes from metal manufacturing	WO	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	Origin shall be conferred to a good of this subheading that is derived from prod'n or consumption in a Party	12	
27	coal, lignite, petroleum oils, gas, etc.	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTH	41	**43**
	– waste oil	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	Origin shall be conferred to a good of this subheading derived from prod'n or consumption in a Party	2	
28	Inorganic compounds	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTSH	171	181

29	Organic compounds	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTSH	293	300
30	glands, blood, medicaments, other pharmaceuticals	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTSH	29	29
31	fertilizers	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTSH	25	25
32	tanning, dyes, coloring substances, essential oils	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTSH	40	46
33–34	Cosmetics and other beauty products	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTH	34	53
		RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTSH	19	
35–38	Casein, albumins, gelatins, peptides, rosin and resin acids, insecticides, fungicides, pickling preparations, etc.	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	GR /CC exc CH4/ CTH	RVC(40) or CTSH	44	129
		RVC(40) or CTH	RVC(40) or CTH	RVC(40)	CTH	RVC(40) or CTH	76	
	Heading 3825 – wastes, sludge	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	Origin shall be conferred to a good of this subheading derived from prod'n or consumption in a Party	9	
39	Polymers, silicones, etc., in primary forms	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	RVC(40) or CTH	58	62
	Wastes, parings, and scraps	RVC(40) or CTH	RVC(40) or CTH	RVC(40)	RVC(40) or CTH	Origin shall be conferred to a good of this subheading derived from prod'n or consumption in a Party	4	

Table 4.5b: Summary for ROO in Chapters 25 to 39

	# of HS lines w/ these ROO	Total # of HS lines in category
# of HS lines in selected chapters	949	974
% share in total HS lines – all products (5,224 lines)	18.2%	18.6%
# of HS lines with convergence for 4 ASEAN+1 FTAs at RVC40 or CTH (GR)	629	
% share in total HS lines of product group	64.6%	
# of HS lines with near convergence for 4 ASEAN+1 FTAs, with AANZFTA more liberal at RVC40 or CTSH	922	
% share in total HS lines of product group	97.1%	

Source: Author's tabulation.

In Chapters 25 to 39, for example, ATIGA, AJCEP, AKFTA, and AANZFTA already have the same ROO for 64.6 percent of tariff lines. (See Table 4.5a and Table 4.5b.) It is different only for AANZFTA as it adopts a more liberal coequal rule of RVC(40) or CTSH. Hence, there is already some convergence for more than 97 percent of the HS lines in these chapters. It would be ideal if all adopt the AANZFTA ROO. This would be a point for negotiation. ASEAN should join Australia and New Zealand in pushing for the AANZFTA ROO in these HS lines. Note also that these chapters already comprise more than 18 percent of the total number of HS lines.

The same could be said for Chapters 1 to 15. (Refer back to Table 4.1.) The ROO used are mainly WO. AJCEP and ACFTA differ. In the case of AJCEP, the ROO used is CC (or CTH in a few cases), but as previously noted, WO and CC are not different in substance for these chapters. ACFTA uses RVC(40), which is theoretically more liberal than WO or CC. In practice, however, for these chapters which cover mainly primary products, the RVC(40) may be similar to WO or CC in terms of ease of compliance. Hence, the possibilities are to choose either WO or CC or adopt a coequal rule between the two.

The textile and garments sector is amongst the most contentious. It employs many different ROO across FTAs, using two-step rules in many cases.

Table 4.6: Examples of Different ROO used in Chapters 50 to 63: Textile and Garments

GR or Textile Rule
GR
RVC(40) or Textile Rule
CC+SPR
CC
CTH except from specified subheadings + SPR
GR or Textile Rule requiring 2 processes
CTH except from specific subheadings + SPR or other SPR
CTH or Textile Rule requiring 2 subsequent processes
CC or RVC(40)
RVC(40) or Textile Rule or CC
RVC(40) or Textile Rule or CC with SPR
CC with specific limitations, or RVC(40)
RVC(40) or Textile Rule
Manufacture from yarns, provided that the necessary process stipulated in the appendix is undertaken

Source: Medalla (2011).

This is also indicated by the lack of convergence in ROO for textile and garments in ASEAN and ASEAN+1 FTAs. (See table 4.7.)

Table 4.7: Incidence of ROO Convergence in ASEAN and ASEAN+1 FTAs for Chapters 50 to 53: Textile and Garments

	Chapters 50–63: Textile and Garments	**# of 6-digit HS lines**	**% share**
Convergence for 3 ASEAN+1 FTAs		98	11.6%
	Near Convergence at RVC(40) or CTH for ATIGA, AKFTA, and AANZFTA, with additional coequal Textile Rule option for ATIGA	95	
	Convergent at WO for ATIGA, AKFTA, and AJCEP	3	
Convergence for 2 ASEAN+1 FTAs		728	85.8%
	Near Convergence at RVC or CC for ATIGA & AKFTA, with additional coequal Textile Rule option for ATIGA	183	
	Convergent at RVC or Textile Rule For ATIGA & ACFTA (in some with additional option for ATIGA)	290	
	Convergent at RVC(40) or CC for AKFTA & AANZFTA (GR for ATIGA)	15	
	Near Convergence at RVC or CTH for ATIGA and AKFTA, with additional co-equal Textile Rule option for ATIGA	240	
Different ROO across FTAs		22	2.6%
	Total # of HS lines	848	

Source: Medalla (2011).

However, there are some positive developments that could help. For example, the trend in new FTAs indicates that ROO regimes are becoming more liberal as exemplified by ATIGA and AANZFTA. There is also some convergence in origin certification procedures (OCPs) across the RCEP countries. The COO forms used are identical, and the procedures for verification requirements for COO issuance are similar (Medalla, 2011). In addition, as noted in the discussion, there is significant convergence amongst ATIGA, AANZFTA, AKFTA, and AJCEP. Most notably, a majority of the ASEAN and ASEAN+1 FTAs already use the same GR. ACFTA and AIFTA are the exceptions. Moreover, in the working groups of ASEAN, there are ongoing efforts to simplify and harmonise OCPs. Finally, firms have been gaining more experience in ROO and FTAs.

To summarise the main points from the discussion:

- Harmonisation matters. Multiple, non-uniform ROO across multiple FTAs could result in increased costs. Indeed, in the survey of firms done for this study, firms consider the harmonisation of ROO to be very useful.
- For the RCEP, however, it is not only harmonisation that matters. In particular, harmonisation upwards of the ROO of the various ASEAN FTAs is critical.
- There are difficulties in harmonisation upwards. Amongst the factors to consider are the technical and administrative concerns (question of implementability), the protectionist pressures against liberal rules, and the fact that some products are more difficult than others.
- However, there are positive developments that help:
    - The trend in ROO becoming more liberal as exemplified by ATIGA and AANZFTA (Medalla, 2011)
    - Firms gaining more experience in ROO and FTAs
    - Convergence in origin certification procedures across the RCEP countries (Medalla, 2011)
    - Use of same GR in all of the ASEAN FTAs, except ACFTA and AIFTA
    - Significant convergence amongst ATIGA, AANZFTA, AKFTA, and AJCEP
    - Ongoing efforts to simplify and harmonise the origin certification procedures

Finally, we go back to the central objective of the RCEP, which is 'to achieve a modern, comprehensive, high-quality, and mutually beneficial economic partnership agreement amongst the ASEAN Member States (AMS) and ASEAN's FTA partners'. Accordingly, ROO in the RCEP should be more concerned about trade facilitation than trade deflection.

2. Recommendations[7]

A key recommendation for the RCEP is to use as its GR the coequal ROO of RVC(40) or CTH. It is already the GR for ATIGA, AJCEP, AKFTA, and AANZFTA. Starting with a GR is similar to adopting a negative list approach. Whereas for the past FTAs there was probably a need to go over all the product lines intensively before adopting the coequal rule of RVC(40) or CTH, which is considered fairly liberal, the same bottoms-up approach is not as necessary for the RCEP, as these countries would already have learned lessons from these previous FTAs. Choosing the GR already commonly used by the majority of the ASEAN FTAs provides a practical approach towards a liberal set of ROO. India and China will have to make the biggest adjustment, but this is where harmonisation upwards would have the biggest impact. Adopting this GR is supported by industry, especially exporters who are the users of the FTAs. (See annex 1 of the study.)

Going down to the PSRs, the general guideline for negotiation is along the same lines: lean towards more liberal rules. There are two general approaches that could be used to this end. Medalla (2011) found the ROO of ATIGA and AANZFTA to be the least restrictive. One possibility is to use either ATIGA ROO or AANZFTA ROO as a template. Another is to pick and choose the best (least restrictive) ROO amongst the ASEAN FTAs by HS line. This is what would be ideal to bring about harmonisation upwards. If a particular choice for the best ROO is not clear (or difficult to agree on), another option would be to make the PSRs for the particular HS line of the respective ASEAN+1 FTA coequal. Hence, if the PSR for a particular HS code is WO for three of the ASEAN FTAs, CC for one, and RVC(40) for another, the proposed ROO for the RCEP could be WO or CC or RVC(40) for this HS line.

[7] This part greatly benefits from interviews and a survey undertaken by the author.

Either option could be difficult to adopt. Some products could be very contentious. To address this concern, a first step could be to trim down the list of contentious products where more in-depth assessment could be undertaken. Usually, the use of specific requirements in the ROO would be the source of contention. As much as possible, the RCEP–ROO should avoid the use of additional specific requirements.

The advantage of a large grouping of countries, such as the RCEP, is that cumulation becomes inherent as a basis for conferring origin. Originating products could now come from anywhere in the member parties. Cumulation could be impeded, however, if certain ROO provisions specifically add limitations (e.g. source of certain raw materials). To avoid this, the cumulation principle should be made explicit in the RCEP. Indeed, interviews with firms and policy makers have consistently brought out the importance of cumulation.

The FTAs provide for a minimum value of imports that would not require a CO. This is US$200 for the ASEAN+1 FTAs. Raising the minimum value could be a very important provision with a potentially substantial impact, especially for SMEs.

Similarly, a waiver of CO (ROO) for products with MFN tariffs below 5 percent is another measure to consider. Medalla (2011) pointed out that for the majority of countries in East Asia, more than 70 percent of tariff lines for nonagricultural products are already below 5 percent. This could have a huge potential impact on intraregional trade in general. SMEs, in particular, would benefit from the reduction in the costs to utilise the FTA for exporting and importing.

The difficulty in complying with the applicable ROO (and the degree of restrictiveness) depends not only on the type of ROO used but also on the OCP being followed. In this regard, a significant degree of harmonisation has been implemented amongst the ASEAN and ASEAN+1 FTAs with reform efforts to streamline procedures. First, they use almost identical CO forms [8] with the same cells and format for required information. All require COO on a per-shipment basis. The requirements on pre-export verification are also similar (Medalla and Rosellon, 2011). However, implementation across countries differs in a key element – the Certification Issuing Authority.

For ASEAN, China, and India, the CO-issuing authority is a designated government agency. On the other hand, Japan, Korea, Australia, and New Zealand have given the

[8] ATIGA uses form D; ACFTA, form E; AKFTA, form AK; AJCEP, form AJ; and AANZFTA, form AANZ.

authority for issuing the CO to their designated private chambers of commerce and industry. For Japan and Korea, the government (the Ministry of Economics, Trade, and Industry or METI for Japan and Customs for Korea) can also issue COO. With its huge trade volume, Japan especially sees the need to use the large network of the Japan Chamber of Commerce and Industry (JCCI).[9] This makes for greater visibility and availability of the service to industries. The same rationale holds for Korea. It would be very useful, therefore, to include this provision in the RCEP.

In the firm survey carried out for the Philippines, the majority of firms covered preferred the COO to be issued by a government agency. There is reliance on the official channel to provide credibility and trust. The COO are thus more readily accepted. Firms also receive assistance from government in meeting or fulfilling the documentation requirements of the CO. As part of its reforms, the Bureau of Customs (BOC) official interviewed mentioned that the bureau is looking at transferring the authority to another agency (e.g. the Philippine Tariff Commission) to lessen its workload. The Tariff Commission has the expertise in HS tariff classification and industry operations. The BOC official indicated that it has not considered transferring the CO-issuing authority to the industry chamber. On the other hand, the Philippine Chamber of Commerce and Industry (PCCI) does not appear to be keen either to take over the function as this requires new capacity and some familiarity with the functions and responsibility. Nonetheless, this third party certification should be an option in the RCEP as is the current practice.

A major recommendation that has been put forward to further improve the ROO process, and consequently FTA utilisation, is self-certification.

Using the self-certification method has advantages and disadvantages. The first advantage is a reduction in the cost of complying with third party certification (CO issuer) in terms of man-hours needed. A second advantage is the time factor. The elimination of third party certification saves time in the application process for CO issuance itself. In addition, there is potential time-saving from possible interruption if there are questions on the CO in the destination country. With third party certification, the response time would be subject to the third party issuer's office hours, which in turn could lead to substantial delays. One of the respondents in our interviews, for example, explained that this

[9] Twenty-two chamber chapters all over Japan have the capacity and authority to issue COO.

happened to their early shipments when the CO was questioned in the receiving country. It proved costly because there was no office in the country of CO issuance when the shipment arrived. From that time onwards, they rescheduled the shipping date to avoid the same problem. If self-certification is allowed, there would be greater flexibility since questions on the CO can be responded to immediately.

However, there could also be disadvantages in the use of self-certification. There is the issue of trust and credibility. In this regard, measures must be put in place to ensure the veracity of the CO. Complying with these requirements could entail additional costs for the exporter.

There are generally two stages in the OCP: pre-export verification and CO issuance. The first stage usually has two steps (the pre-export verification process). In sum, there are three steps in the OCP:

1. Firm registration (requirements specified by country, subject to verification)
2. Origin verification (by product)
3. CO issuance

In the ATIGA and the various ASEAN +1 FTAs, the system adopted is third party certification (by the CO authority, either the authorised government agency itself or the authorised chamber/industry association). The CO-issuing authority is involved in all of the three steps.

At the high end of the spectrum, self-certification would be fully allowed or accepted as in the case of the North America Free Trade Area (NAFTA). In NAFTA, there is no authority to check the authenticity of the declaration. It is purely based on the exporters' declaration. As a result, NAFTA employs rigid ex-post checks and verification. This could be one source of difficulty for both the exporter and the receiving country of export destination. As such, some FTAs adopt a 'hybrid' self-certification process. In this regard, the common practice is to involve a 'third party' (i.e. the assigned CO authority) to be involved in the first step. This is the case, for example, in Japan's self-certification in its FTA with Switzerland. Exporters should first register, subject to verification and approval by a 'third party.' In the case of the Singapore–Australia FTA and the pilot self-certification for ATIGA, a third party is involved in both steps 1 and 2. Once steps 1 and 2 are complied

with, the exporter could issue its own CO (step 3). This approach has the advantage of being more credible to receiving countries, as it involves some third party verification prior to exportation. At the same time, it provides less cumbersome procedures (lower cost) for exporters since COO from a third party are no longer needed for every shipment.

Officials in Japan and New Zealand also expressed that they have no problem receiving self-certified COO because they have a working risk assessment system.

In addition, there is always the post-audit verification system. This is one possible area where problems could arise for exporters. Even one instance of post-audit verification could be very costly, especially if done indiscriminately. As such, the Japan Automotive Manufacturers Association (JAMA) proposes that there should be no direct verification (with the trader/manufacturer). That is, the verification request should be dealt with between governments.

Self-certification and third party certification have advantages and disadvantages. Some problems could be addressed by adopting some form of hybrid self-certification. Giving firms a choice between this and a third party certification scheme could be adopted in the RCEP. Indeed, there are ongoing discussions on and there is pilot testing of the use of self-certification in ASEAN. And dialogue partner countries are already using the system.

One question that has been raised is: should traders be allowed to register for self-certification? A legitimate point is that the knowledge of origin status lies with the manufacturer, not the trader. As such, it could be vulnerable to possible abuse. On the other hand, this could be very advantageous for SMEs. A possible compromise is to allow traders to be included to a limited extent. For example, there should be a clear, verifiable relationship between the trader and the manufacturer. In addition, the process could start with traders with proven track record. Hence, ways to include traders on a very selective basis should be explored.

Finally, the RCEP–ROO should use the facilitative provisions already found in ATIGA and the ASEAN+1 FTAs. Based on responses by the firms (and policy makers) surveyed/interviewed, these provisions are considered to be very useful (See annex 1.) They are the following provisions in particular:

- More liberal use of *de minimis* provision, as it pertains to CTC.

A *de minimis* provision is valuable not only in simplifying administration, but more importantly, in reducing the cost of compliance in the use of the CTC rule for exporters.

- Third party invoice and back-to-back CO

Enabling provisions for intermediary trade, especially given the importance of global production networks and supply chains, could be crucial. For example, within a supply chain, a batch of goods could pass through a number of countries. A simple case is when a batch of good enters first one member country in the chain and then some portion is later re-exported to another member country. In this case, a back-to-back CO (a fresh CO is issued on the basis of the original CO from a member country) would greatly facilitate the process. Another case could be where the production could involve several FTA member countries and the goods exported to another FTA member country. The goods produced and exported qualify as originating using the relevant FTA–ROO criterion, but the invoice for an input comes from a third party. In this case, allowing the use of a third party invoice is important.

- Use of Advanced Ruling

On the ground, there could always be cases where there would be different interpretations of certain rules, often related to the particular person in charge present and interpreting the rules. For example, in our interviews/survey, a common source of difference in opinion is the applicable HS code for a product. There was also an anecdotal case of different interpretations of 'third party'. A provision for advanced ruling that would allow the entry of the goods without further unnecessary delay (final decision upon later review) would be a useful trade-facilitating provision.

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