

Cumulation and Utilization

Jeremy T. Harris
WCO Global Origin Conference
12 March 2021

All opinions are my own and do not represent the Inter-American Development Bank

What are the Barriers to Utilization?

- Why do we care?
 - Excessive unused preferences mean that an FTA is not providing the benefits it promised
- Rules of Origin (RoO) are cited as a barrier to preference utilization
 - Not entirely fair: General FTA knowledge, risk management, AND RoO
- Why?
 - RoO noncompliance – If it's not originating, it shouldn't use preferences
 - Distributors of goods from many sources generally don't have the needed information
 - Sourcing burden – Higher costs to produce an originating good
 - This is the whole point of RoO
 - Compliance burden – Higher transaction costs
 - What paperwork is needed? Where to get information?
 - Compliance risk – Don't know if it's originating, don't want to risk it

Economic Literature Analyzing Utilization

- Utilization rates have been shown to vary widely across countries and agreements.
- Carerre and de Melo (2004) used utilization rates in NAFTA as a factor in calculating the costs of RoO compliance
- IDB and ADBI surveys
 - Knowledge: There is an FTA? What is an FTA?
 - It is not always SMEs that have the biggest RoO problems – MNEs' suppliers are often SMEs
 - Another challenge is utilization of multiple agreements.
- Cadot et al. (2014) analysis of utilization rates in several Latin American countries indicate that utilization increases in preference margin, firm size, and time
- Jonas Kasteng on this panel has recently done some excellent work.

To Harmonize or not to Harmonize?

The siren song of harmonization

- What should NOT be harmonized: the PSRO
 - The PSRO in bilateral agreements are adapted to the export supplies of the signatories. One size does not fit all.
- What can and should be harmonized
 - Definitions – Special goods (sets, accessories, packaging, etc.)
 - Procedures – Direct shipment, Time periods, appeal stages, etc.
 - RVC calculation methods – Should only need two methods: minimum originating content and maximum non-originating content. That's it.
 - Documentation requirements – What information is sufficient to demonstrate compliance?

How does Cumulation affect Utilization?

How does cumulation affect utilization?

- Cumulation lowers the sourcing burden
 - The wider the set of countries from which originating materials may be sourced, the more likely that lower-cost providers become eligible
- Broader cumulation may **increase** the compliance burden
 - The effort (cost) to properly document a sourcing pattern that has materials from more countries is greater, with higher risk of information errors and unexpected tariffs
- Augier et al. (2005, 2007) find that continental cumulation expanded trade between EU spokes by between 7% and 22%, and that countries excluded from PECS saw trade lowered by up to 70%.

How can cumulation be broadened?

Basic question: Do you need harmonized rules to cumulate?

- A New Agreement – Cut the Gordian Knot, set up a new origin regime with more members (Pacific Alliance, PECS, AfCFTA)
- Expanded (Canadian) Cumulation – Treat common third parties as if members, therefore the rules of the “final” agreement apply
- Extended – Any material that would be duty-free if imported directly is cumulable

Cumulation with more countries and/or rules will increase complexity

- A single new agreement simplifies, but imposes a large up-front negotiation cost
- Connecting existing agreements increases information costs.

Cumulation without harmonization of rules?

- The goal is to enable broader cumulation (reducing surcing burden) without massive new negotiations
- The challenge is that for this to work effectively there must be significantly better visibility of supply chains to demonstrate compliance in order to manage that burden.
- Self-certification/cutting paperwork does not improve information
- But increasing the documentation burden reduces utilization
- So how do we reconcile this?

How to reduce the compliance burden?

We must leverage technology

- Traceability of materials combined with origin documentation
- Tools to facilitate assessment of compliance
 - RoO are expressed in technical language that is not easily accessible to non-experts
- Information security / Avoiding disintermediation / Blockchain

Simplification

- Harmonization of mechanisms, procedures, etc. (GPTA)

Capacity Building

- Training every potentially exporting SME may be too much
- Developing capacity in chambers, export promotion agencies, and certifying entities can really add value

Thank You

Jeremy T. Harris

jtheremy@gmail.com