Committee on Rules of Origin

UTILIZATION RATES UNDER PREFERENTIAL TRADE ARRANGEMENTS FOR LEAST DEVELOPED COUNTRIES UNDER THE LDC DUTY SCHEME

NOTE BY THE SECRETARIAT[1]

1 INTRODUCTION

1.1. Utilization rates offer a useful analytical tool for the examination of trade preferences in general and of rules of origin in particular. Very high rates of preference utilization signal that exporters are able to meet origin requirements and make effective use of preferential trade benefits. On the contrary, low levels of preference utilization may indicate that preferential origin requirements cannot be met and that they could be operating as a trade barrier.

1.2 For this reason, paragraph 4.3 of the 2015 (Nairobi) Ministerial Decision on preferential rules of origin for least-developed countries (LDCs) stated that the Secretariat may calculate the rates of utilization of Preferential Trade Arrangements (PTA) for LDCs. Such calculations may help Members identify and promote trade-facilitating origin practices.

1.3. This note builds on previous notes by the Secretariat on preference utilization rates (G/RO/W/168 and G/RO/W/168/Rev.1). It is an attempt to take forward the work of the Committee on Rules of Origin with regard to the linkages between preference utilization and origin requirements.

2 DEFINITION OF PREFERENCE UTILIZATION AND METHODOLOGY FOR THE CALCULATION OF UTILIZATION RATES

2.1. A previous note by the Secretariat defined the concept of "preference utilization rates" and explained the significance of using that concept as an analytical tool to examine preferential rules of origin for LDCs (section 2 of G/RO/W/168/Rev.1). As stated in that note, preference utilization refers to the proportion of trade, which is eligible for trade preferences, and which, in practice, receives preferential treatment. This definition assumes that preferential treatment may only occur if there actually is a preference. In other words, in order for a preferential tariff margin to be implemented, the Most-Favoured Nation (MFN) tariff rate for a product cannot be zero.

2.2. The Committee on Rules of Origin (CRO) has adopted, at the end of 2016, modalities for the calculation of utilization rates as recommended in paragraph 3.2(a) of document G/RO/W/161. The methodology compares the value of imports which "reportedly" benefitted from preferences with the value of total imports "eligible" for such trade preferences.

[1] This document has been prepared under the Secretariat's own responsibility and is without prejudice to the positions of Members or to their rights and obligations under the WTO.

Table 1: List of PTAs included in the analysis

Preference-granting Member	PTA	Year
Australia	GSP-LDC	2016
Canada	GSP-LDC	2016
Chile	LDC-specific	2015
European Union	GSP-LDC	2016
India	LDC-specific	2015
Japan	GSP-LDC	2016
Korea, Rep. of	LDC-specific	2016
Norway	GSP-LDC	2016
Switzerland	GSP-LDC	2016
Chinese Taipei	LDC-specific	2016
United States	GSP-LDC	2016
	AGOA	2016

Source: Preferential Trade Arrangements database (http://ptadb.wto.org)

2.3. The LDC preferential arrangements reviewed in this report have been notified under the "Enabling Clause" in the case of developed country Members[2] and under the 1999 waiver for developing countries.[3] The LDC schemes which could be reviewed in this note are those for which tariff and import data is available according to the requirements of the PTA Transparency Mechanism[4]. Currently, such information is available as follows:

i. Trade data for 2016 is available for the schemes of the following WTO preference-granting Members: Australia; Canada; European Union; Japan; Republic of Korea; Norway; Switzerland; Chinese Taipei; Thailand; and the United States (both US-GSP and AGOA). Data for Chile and India concern 2015; and

ii. Trade data is currently not available for the following WTO preference-granting Members: Armenia; China; Iceland; Kazakhstan; Kyrgyz Republic; Montenegro; New Zealand; Russian Federation; Tajikistan; and Turkey.

2.4 A full report of the tariff and import data available for each preference-granting Member is available in document G/RO/W/163/Rev.4.

3 USING PREFERENCE UTILIZATION RATES TO EXAMINE PREFERENTIAL RULES OF ORIGIN

3.1. Preference utilization rates are a useful indicator to analyse the impact of administrative prerequisites related to trade preferences, such as origin requirements. In fact, customs will only grant preferential treatment (i.e. the exemption or the reduction of import duties) to goods which are deemed to "originate" in the beneficiary country. The criteria which determine when a good "originates" or not in the beneficiary country vary from one preferential scheme to the other but can be summarized as follows:

(i) a good must be wholly obtained in the beneficiary country or comply with minimum substantial transformation requirements to change its origin (that is, general or product-specific rules of origin);

(ii) a good must demonstrate compliance with such requirements, particularly by being accompanied by a certificate of origin matching specific prescriptions (i.e. certificate of origin, e-Certificates, self-certification, etc.); and

(iii) a good must be directly consigned from the beneficiary country to the preference-granting country to avoid any risks that it is further processed in third or transit countries (i.e. direct transportation requirements or exceptions to it).

[2] Paragraph 2 of the Decision of 28 November 1979 on Differential and More Favourable Treatment Reciprocity and Fuller Participation of Developing Members.

[3] Waiver Decision initially adopted by Members in 1999 (WT/L/304), and extended until 30 June 2019 (WT/L/759).

[4] According to that Decision (WT/L/806), preference-granting Members must notify the list of tariff lines for which a tariff preference is available for LDCs; and the value of imports, at the tariff-line level under such or other preferences.

3.2. These three requirements must be simultaneously met so that customs officials in the importing country may grant preferential treatment to a product. Hence, low preference utilization *could* indicate that these requirements are too demanding and cannot be met in a number of cases. Conversely, a high utilization rate *necessarily* indicates that origin requirements can be met and are thus not hindering preferential trade.

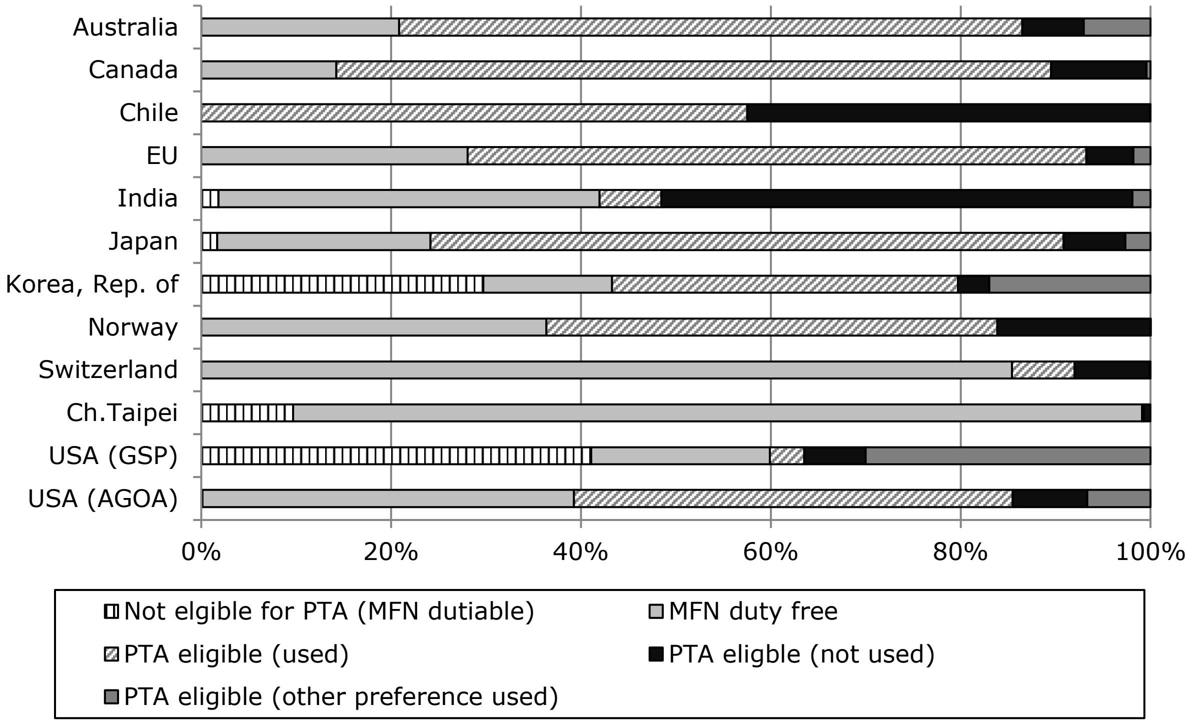
3.3. However, other factors, not related to rules of origin may also explain low rates of preference utilization. One very significant factor is the existence of several competing preferential schemes. In fact, sometimes, exporters have the choice between different preferential schemes: one or more non-reciprocal schemes (PTAs, such as a GSP for LDCs) and one or more reciprocal schemes (regional trade agreements, RTA). For example, the United States "African Growth and Opportunity Act (AGOA)" co-exists with the United States General System of Preferences (GSP). Likewise, Australia grants trade preferences to Cambodia both under the "Australian System of Tariff Preferences" (ASTP) and under the ASEAN-Australia-New Zealand free trade agreement (AANZFTA). Similarly, the European Union (EU) grants preferences to some LDCs through its GSP-LDC Scheme ("Everything but Arms", EBA) as well as through the reciprocal Economic Partnership Agreement (EPA). In the presence of such competing preferential schemes, exporters will prefer to trade under whichever scheme is most beneficial. As a result, low preference utilization under one scheme does not necessarily indicate problems related to origin requirements in a specific scheme and could rather be the result of trade being channelled through other schemes available. Section 8 of document G/RO/W/168/Rev.1 contains more detailed notes about each preference-granting Members' trade with LDCs.

3.4. For this reason, it is important to interpret utilization rates in light of other such factors. A comprehensive view for each preferential scheme depends on the specific patterns between each preference-granting Member and LDC beneficiaries (see, for instance, the factors described in section 8 of G/RO/W/168/Rev.1).

3.5. Graph 1 illustrates total trade between beneficiary LDC countries and each preference-granting Member from the viewpoint of the duty category:

i. First, trade could take place outside of the scope of a preferential scheme, typically on products that are not covered by the preference. Preferential rules of origin cannot be a concern for this category because they do not apply (MFN conditions apply).
ii. Second, trade could concern tariff lines for which the MFN tariff rate is zero ("MFN duty free"). In this case, irrespective of whether these lines are covered or not by a preferential scheme, no preferential tariff treatment may be granted. As a result, there can be no preference utilization. Moreover, preferential rules of origin should also not hinder trade in such products.
iii. Third, trade could occur in tariff lines that are subject to preferential treatment. The focus of the Bali and Nairobi Decisions is non-reciprocal trade preferences for LDCs ("preferential trade arrangements", PTA). For imports which are eligible for such preferences, some imports effectively received preferential treatment ("PTA eligible (used)"). For this category of imports, one has to conclude that there were no difficulties in meeting origin requirements. If preferences could not be granted, however, there could be two alternatives: first, preferential requirements could not be met ("PTA eligible (not used)"); or other preferential schemes may have been used ("PTA eligible (other preference used)").

Graph 1: Import of WTO preference granting Members from LDCs (2016)



Source: WTO Integrated Database (2018)

3.6. From the point of view or rules of origin, it is interesting to focus on the portion of trade which is eligible for preferences but which does not use them. If a preferential tariff margin is available but is not used, the question which arises is whether origin requirements are operating as a trade barrier. In other words, origin criteria, documentary requirements or transportation requirements may be the reason why such preferences are not being used.

4 FOCUSING ON "UNDERUTILIZATION" TO IDENTIFY SPECIFIC DIFFICULTIES RELATED TO PREFERENTIAL RULES OF ORIGIN

4.1. The interest of focusing on underutilization (as opposed to focusing on overall utilization) is that this approach could help identify, in a more specific manner, areas for further attention and investigation. As a result, identifying sectors with underutilization or "pockets of underutilization" as precisely as possible vest a strategic interest for an examination of preferential rules of origin to guide the analysis of trade patterns and identify overly restrictive origin requirements.

4.2. While useful, identifying pockets of underutilization and investigating the reasons which could explain them can, nevertheless, be a difficult exercise. A number of variables may need to be considered, including:

(i) First, a link with rules of origin can only be established if the analysis is made at the most disaggregated level. In fact, because rules of origin are often designed at the product-level, a correlation with origin requirements could only be made if utilization rates (or underutilization rates) are analysed at a similarly disaggregated level;
(ii) Second, the number of exporting firms and the value of trade may vary greatly from one year to the other or from one country to the other. Annual trade variations can induce different conclusions about utilization rates. As a result, any analysis would be more reliable if it considered data over a longer period;

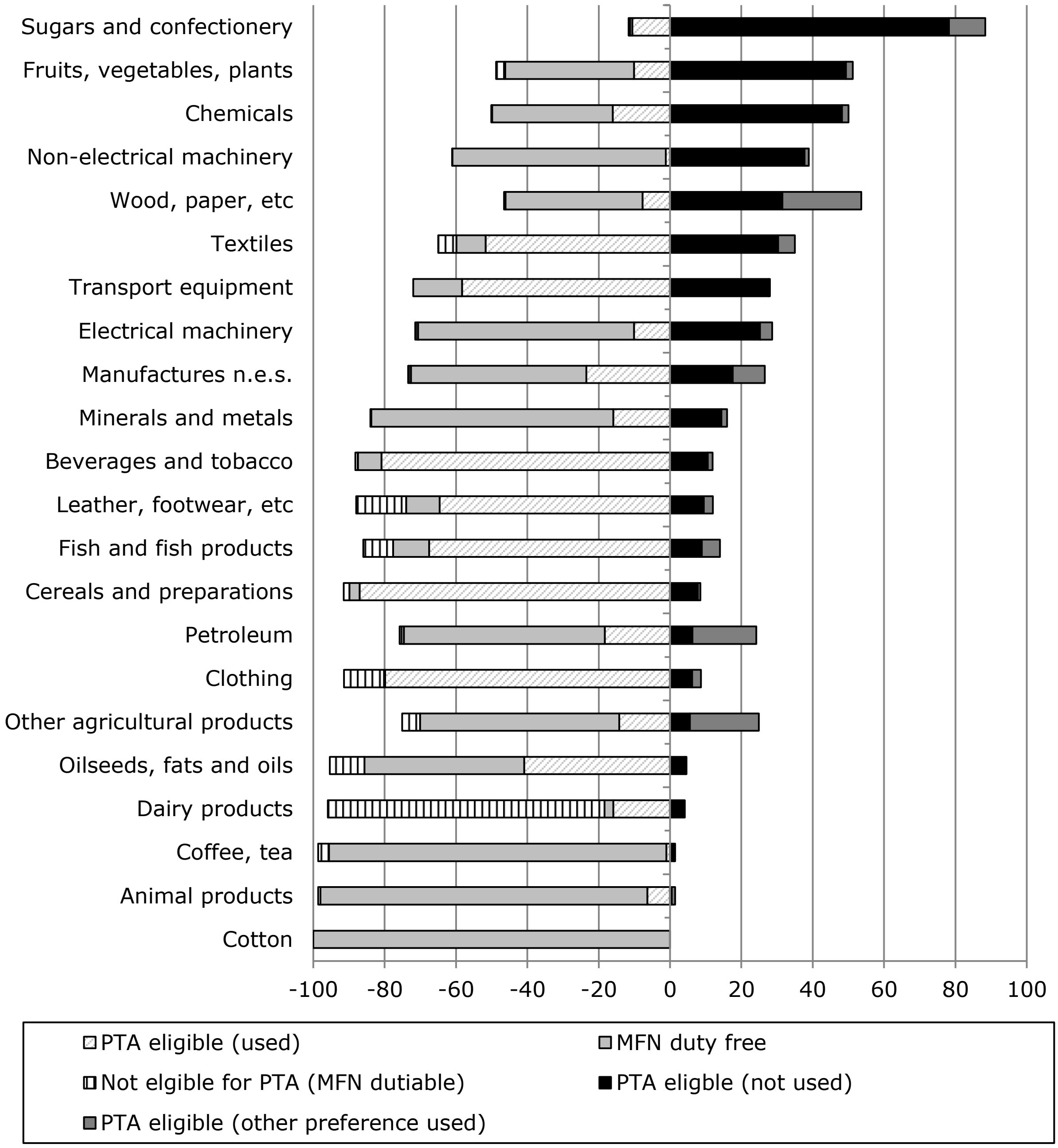
(iii) Third, the ability to comply with origin requirements could vary from one LDC to another and from one firm to another. One firm may meet the origin requirements of a preference-granting Member while other firms might not. This is because firms have different trade integration profiles, different productive capacities to access originating suppliers and different capacities to access technology and undertake the manufacturing operations that meet substantial transformation criteria. As a result, utilization rates should be calculated for each beneficiary LDC and should be complemented with an assessment of firm-specific and country-specific circumstances.

4.3. Bearing in mind these objectives and difficulties, Graph 2 below depicts preference utilization rates across different sectors.[5] It shows the proportion of trade, for each sector, which utilizes preferences and which does not.

4.4. As can be seen from the graph, virtually all product groups or sectors have "pockets of underutilization". However, the significance of underutilization varies greatly from one group to the other. Underutilization can be very significant in some cases. For instance, close to 50% of all LDC exports of "fruits, vegetables, plants" and "chemicals" do not receive preferential treatment despite being eligible for preferences. This proportion reaches close to 80% in the case of "sugar and confectionary products". In other words, only about 20% of all the sugar and confectionary products exported by LDCs meet origin (and administrative) requirements while 80% of sugar exports from the LDCs do not.

[5] These sectors correspond to categories used in other databases, research and publications prepared by the WTO. The specific product categories of each sector with the corresponding Harmonized System (HS) codes can be found here: http://stat.wto.org/idbdata/MTN_product_classification_e.pdf.

Graph 2: Underutilization of LDC preferences: sectoral overview (%, 2016)



Source: WTO Integrated Database (2018)

4.5. Interestingly, as the graph shows, the largest pockets of underutilization concern products or sectors which typically are subject to simple origin requirements. For instance, the first two items with the largest proportion of underutilization are products which are subject to "wholly obtained" rules of origin: "sugars and confectionery" (HS Chapter 17) and "fruits, vegetables, plants" (HS Chapters 07, 08, 13, 14 and Subheadings 1105-06, 0601-03, 1211 and 2001-08).

4.6. Conversely, some of the sectors that tend to be more sensitive for preference-granting Members have higher rates of utilization (or constitute small pockets of underutilization). For instance, almost 90% of all LDC exports of "clothing" meet origin requirements and therefore use trade preferences.

4.7. It should be noted, however, that the bars in Graph 2 show percentages (proportions of utilization or underutilization) and do not indicate trade values. As a consequence, a small pocket of underutilization may actually conceal large trade values which are being denied trade preferences. In this regard, the sectors that have the highest value of trade which is not utilizing preferences are: "minerals and metals" (14.4% of exports do not use preferences, worth US$2,068 million) and "clothing" (6.2% underutilization but worth US$1,999 million of exports). Table 1 compares underutilization rates and the value of trade not receiving preferences.

Table 2: Underutilization – sectoral overview

Product Group	Share of imports (%)	Value of imports (million USD)
Minerals and metals	14.4	2,068.2
Clothing	6.2	1,999.3
Fruits, vegetables, plants	49.3	1,485.5
Petroleum	6.3	993.2
Textiles	30.3	529.5
Chemicals	48.2	365.4
Leather, footwear, etc	9.5	241.0
Wood, paper, etc	31.5	224.0
Transport equipment	27.5	176.7
Fish and fish products	8.9	169.5
Sugars and confectionery	78.2	124.6
Beverages and tobacco	10.6	99.8
Electrical machinery	25.2	67.4
Other agricultural products	5.6	66.9
Manufactures n.e.s.	17.6	65.0
Non-electrical machinery	37.7	57.0
Cereals and preparations	7.8	25.4
Coffee, tea	1.2	14.1
Oilseeds, fats and oils	4.2	13.5
Dairy products	4.1	0.2
Animal products	0.5	0.1
Cotton	0	0

Source: WTO Integrated Database (2018)

4.8. Some of the reasons that may explain such patterns may relate to the fact that all LDCs and all preference-granting countries are being considered together. Therefore, the rates may be influenced by the trade patterns of the beneficiary LDCs with the greatest values of trade. For this reason, Annex 1 provides a country-by-country break-down. Its examination can provide additional information regarding the specific pockets of underutilization and the specific sectors which have a particular importance for each least-developed beneficiary country and for each preference-granting Member. For each least-developed beneficiary country, the table presents two columns:

i. Column (1) shows the share of imports eligible for LDC preferences but not receiving preferential treatment (non-utilization rates); and
ii. Column (2) shows the value of imports eligible for LDC preferences but not receiving preferential treatment (in thousand USD).

ANNEX 1 – UNDERUTILIZATION: COUNTRY-BY-COUNTRY BREAKDOWN

(1) Share of imports eligible for LDC preferences but not receiving preferential treatment (%)
(2) Value of imports eligible for LDC preferences but not receiving preferential treatment (in thousand USD)

WTO LDCs	Australia		Canada		Chile		European Union		India		Japan	
	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)
Afghanistan	73.0	69	74.7	610	100.0	12	53.5	3,634	100.0	288,516	100.0	33
Angola	100.0	6	100.0	22	1.4	825	56.7	44,650	100.0	106,995	100.0	160
Bangladesh	6.9	30,449	10.6	123,580	96.7	45,609	4.2	751,355	100.0	640,663	5.9	66,487
Benin	100.0	6	84.5	14	-	-	6.2	350	95.4	62,056	100.0	35
Burkina Faso	100.0	2	27.7	4	100.0	9	9.5	1,155	100.0	216,770	56.3	218
Burundi	100.0	1	100.0	1	100.0	303	12.8	42	100.0	110	100.0	59
Cambodia	38.7	21,460	10.9	89,031	97.7	24,163	8.5	426,979	98.1	48,746	15.3	82,560
Central African Republic	100.0	3	100.0	4	100.0	25	99.0	694	100.0	832	100.0	2
Chad	100.0	1	100.0	12	100.0	4	100.0	1,206	100.0	1,519	-	-
DRC Congo	53.0	18	100.0	46	-	-	62.0	6,437	100.0	46,017	6.4	32
Djibouti	100.0	11	100.0	1	-	-	96.2	5,921	100.0	516	-	-
Guinea	100.0	3	86.8	30	-	-	74.6	2,636	100.0	258,674	27.2	63
Guinea-Bissau	-	-	100.0	0	-	-	100.0	502	100.0	468	-	-
Haiti	90.8	1,525	60.8	14,257	100.0	176	14.1	2,419	100.0	3,282	100.0	3,644
Lao People's Democratic Republic	80.7	754	19.5	1,387	100.0	209	16.2	36,289	100.0	98,407	27.3	2,439
Lesotho	31.9	212	27.3	1,521	-	-	29.1	931	100.0	4,943	71.7	152
Liberia	100.0	4	100.0	47	100.0	22	91.9	4,737	100.0	31,944	-	-
Madagascar	86.1	2,703	28.0	2,150	100.0	211	98.6	38,459	22.4	29,732	5.5	4,511
Malawi	-	-	100.0	125	100.0	20	3.9	9,715	100.0	62,061	0.4	18
Mali	100.0	2,837	99.4	86	100.0	17	18.3	1,185	99.6	168,726	73.3	23
Mauritania	100.0	11	100.0	46	100.0	507	3.0	7,380	100.0	15,474	3.1	3,529
Mozambique	100.0	89	82.2	16	100.0	66	6.5	73,694	99.7	344,119	50.7	3,046
Myanmar	51.2	1,554	24.7	12,794	99.4	791	5.7	55,195	99.3	844,333	5.0	21,144
Nepal	36.9	652	46.6	2,477	97.7	172	8.0	7,436	100.0	381,805	47.8	4,033
Niger	100.0	677	83.5	66	-	-	18.7	783	100.0	321	100.0	613
Rwanda	100.0	13	69.5	85	100.0	0	52.8	1,175	41.4	464	98.3	289
Senegal	100.0	101	87.9	596	100.0	154	12.1	38,760	99.4	227,396	24.7	1,559
Sierra Leone	100.0	1,127	100.0	504	100.0	77	70.4	1,405	100.0	15,837	100.0	62
Solomon Islands	85.8	238	100.0	75	-	-	0.2	108	100.0	67,652	99.8	2,227
Tanzania	100.0	55	64.0	448	100.0	566	2.7	9,766	94.0	674,730	52.3	3,813
The Gambia	-	-	100.0	33	100.0	0	5.8	672	100.0	3,763	-	-
Togo	100.0	14	32.4	245	-	-	28.1	10,425	100.0	130,753	74.4	8
Uganda	100.0	16	93.0	156	100.0	362	2.2	3,662	84.4	20,677	33.7	434
Vanuatu	100.0	50	100.0	6	100.0	22	75.1	1,236	100.0	294	98.7	70,007
Yemen	-	-	100.0	4	-	-	34.0	2,609	100.0	5,117	100.0	821
Zambia	100.0	170	34.7	6	100.0	0	22.3	22,920	6.9	32,801	8.3	67
Grand Total		***64,831***		***250,488***		***74,324***		***1,576,522***		***4,836,513***		***272,086***

WTO LDCs	Korea, Rep. of		Norway		Switzerland		Chinese Taipei		USA (LDC)		USA (AGOA)	
	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)
Afghanistan	100.0	18	-	-	98.9	2,344	-	-	85.2	1,432	†	†
Angola	51.1	96	-	-	100.0	1	-	-	100.0	467,603	19.0	467,603
Bangladesh	14.2	38,675	23.9	51,741	54.0	238,490	57.1	3,416	†	†	†	†
Benin	49.1	48	-	-	73.3	343	-	-	43.4	64	91.7	64
Burkina Faso	100.0	2	†	†	97.9	640	-	-	22.0	187	98.2	187
Burundi	16.4	51	†	†	100.0	-	-	-	0.6	2	†	†
Cambodia	77.6	27,212	46.5	18,560	59.1	73,912	90.5	5,727	22.7	53,607	†	†
Central African Republic	100.0	1,010	†	†	100.0	30	-	-	97.8	270	†	†
Chad	-	-	†	†	-	-	-	-	100.0	8	0.1	1
DRC Congo	0.1	145	100.0	1	71.7	69	-	-	10.8	12,211	†	†
Djibouti	11.5	62	†	†	100.0	1	-	-	42.7	39	95.4	150
Guinea	100.0	77	-	-	42.3	40	-	-	46.8	236	98.8	246
Guinea-Bissau	-	-	†	†	-	-	-	-	-	-	-	-
Haiti	97.8	836	100.0	51	100.0	3,967	100.0	0	95.4	701	†	†
Lao People's Democratic Republic	48.9	2,825	85.0	955	80.0	4,774	100.0	63	†	†	†	†
Lesotho	54.6	43	-	-	†	†	-	-	93.8	900	0.4	1,094
Liberia	100.0	219	100.0	3	100.0	157	-	-	56.0	122	93.4	127
Madagascar	8.5	6,053	85.7	828	60.2	8,613	100.0	24	42.8	2,060	14.9	13,020
Malawi	14.3	3,739	-	-	100.0	44	100.0	0	77.1	504	23.5	512
Mali	100.0	34	100.0	1	96.6	264	-	-	42.5	78	95.9	166
Mauritania	0.5	148	†	†	100.0	90	-	-	100.0	9	0.1	28
Mozambique	95.9	2,966	100.0	15	48.5	16,840	100.0	0	43.4	9,111	94.0	9,072
Myanmar	91.5	8,673	23.6	2,062	74.9	26,694	97.5	3,822	94.9	59,139	†	†
Nepal	60.5	958	25.5	442	58.4	4,356	50.5	105	19.4	2,246	†	†
Niger	100.0	74	-	-	100.0	124	100.0	4	97.9	729	99.6	475
Rwanda	36.8	505	†	†	100.0	3	100.0	7	57.1	251	52.6	587
Senegal	67.4	796	100.0	208	28.8	2,354	19.2	7	17.1	201	95.0	167
Sierra Leone	100.0	290	†	†	-	-	100.0	0	94.4	3,097	87.0	2,328
Solomon Islands	100.0	4	†	†	5.5	568	-	-	2.7	32	†	†
Tanzania	6.4	2,388	16.6	116	24.8	4,075	5.3	1	47.7	355	2.7	406
The Gambia	100.0	9	-	-	-	-	-	-	73.3	43	†	†
Togo	100.0	19	-	-	34.1	62	-	-	73.7	308	96.2	377
Uganda	16.2	1,170	3.9	35	19.3	449	-	-	25.2	250	84.7	257
Vanuatu	100.0	38	†	†	-	-	100.0	2	92.7	57	†	†
Yemen	100.0	2,689	†	†	100.0	4	100.0	54	19.0	19	†	†
Zambia	0.1	102	11.1	51	100.0	6,435	-	-	13.7	276	98.5	287
Grand Total		***101,972***		***75,068***		***395,746***		***13,234***		***616,151***		***497,151***

Source: WTO Integrated Database, 2018

Note:

- Fields showing '-' indicate that no imports from specific LDC beneficiaries have been recorded.
- Some LDCs may be excluded from some of the programmes. Country exclusions are marked with [†] in the table.
- All schemes shown concern the LDC duty scheme (with the exception of the US-AGOA).