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Impact assessment on

Rules of origin for

the Generalised System of Preferences (GSP)

Waiver

This report commits only the Commission services involved in its preparation. The text is prepared as a basis for comment and does not prejudge the final form of any decision to be taken by the Commission.

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GLOSSARY

Preferential tariff treatment (or preference)	Reduced or zero import duty which is granted provided that goods originate in a beneficiary country
GSP	Generalised System of Preferences
EBA	Everything But Arms – a special arrangement under GSP for LDCs, granting them duty- and quota-free access for most products
LDC	Least Developed Countries
Beneficiary countries	Countries eligible for preferential tariff treatment under the GSP scheme (as listed in the GSP Regulation – Regulation 980/2005)
Competent authorities:	The authorities competent for the issue and verification of proof of origin
(Certificate of origin) Form A:	Form used to claim the benefit of GSP preference
HS or Harmonised System	Harmonised Commodity Description and Coding System
Wholly obtained	Natural products from a beneficiary country and goods made entirely from them (not containing imported non-originating elements)
Sufficient working or processing	The conditions which products made using imported, non-originating materials or components must fulfil in a beneficiary country in order to be considered as originating there
Cumulation of origin	A facilitation which allows the countries in the cumulation zone to cooperate in order to comply with the rules. Originating products of country A may be further processed in country B and counted as originating.
Regional cumulation of origin	A specific type of cumulation in GSP, applicable to three separate regional groups
Minimal operations	Working or processing operations regarded as insufficient to confer origin or the minimal level of processing that has to be carried out in cumulation.
Value added	The value which must be added to non-originating materials in order to obtain origin
Ex-works price	The price paid for the product ex-works to the manufacturer in whose undertaking the last working or processing is carried out, provided that the price includes the value of all the materials used, minus any internal taxes which are, or may be, repaid when the product obtained is exported
Utilisation rate	The proportion of imported products for which preference is claimed, compared to all those which are eligible for it.

1. PROCEDURAL ISSUES AND CONSULTATION OF INTERESTED PARTIES

1. On 16 March 2005, the Commission adopted a communication entitled "The rules of origin in preferential trade arrangements: Orientations for the future" (hereafter "the communication")[1]. This contained three elements: appropriate rules determining the acquisition of origin; efficient management and control procedures; and a secured environment for legitimate trade. With regard to the first element, the communication acknowledged that further analysis of the suitability of a value added method for determining origin was required. The communication was a general document concerning all preferential trade arrangements, but it envisaged that the first applications should be to priority, development-oriented arrangements such as the Generalised System of Preferences (GSP). The purpose of this impact assessment is to support a draft regulation for the reform of GSP rules of origin.

2. An inter-service group was set up in September 2005, in which the following DGs were represented: Trade; Enterprise and Industry; Fisheries and Maritime Affairs; Agriculture and Rural Development; Development; Enlargement; EuropAid Cooperation Office; European Anti-fraud Office; Health and Consumer Protection; External Relations; Budget; Legal Service; Secretariat-General. The group decided that a full impact assessment was required, covering not just the value-added method, but also the procedural elements in the communication. The group met six times.

3. The reform of GSP rules of origin is included as a simplification initiative on the Commission's work programme for 2007[2].

4. Three studies on the use of a value-added method by outside consultants were commissioned: a general study by Olivier Cadot, Jaime de Melo and Emmanuel Pondard of ADE s.a.[3] (hereafter "ADE"); one focusing specifically on textiles, by Prof. Dr. Michiel Scheffer of Saxion Hogescholen[4] (hereafter "Scheffer") and one concerning the fisheries sector by a consortium comprising Oceanic Développement (France) and MegaPesca Lda (Portugal)[5] (hereafter "Oceanic/MegaPesca"). All consultants were required to consult stakeholders (beneficiary countries and industry representatives).

5. The Commission services carried out a specific consultation to test ideas for certain options concerning sensitive agricultural products with 27 organisations representing the sectors concerned in the Community. These organisations were

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[1] COM(2005) 100.

[2] COM(2006) 629, 24.10.2006.

[3] "Evaluating the Consequences of Shift to a Value-added method for Determining Origin in EU PTAs", July 2006 (Letter of Contract No. 2005/103984, Framework Contract AMS/451 - LOT No. 11).

[4] "Study on the application of value criteria for textile products in preferential rules of origin", October 2006 (Tender 06-H13).

[5] Contrat Cadre FISH/2006/20, Specific Convention N° 3 "Rules of Origin in Preferential Trade Arrangements: New rules for the fishery sector".

contacted by letter in March 2007 and given one month in which to respond (see Annex [1]. 16 did so.

6. The Commission services also consulted European federations on the thresholds to be applied to industrial products. A letter was addressed to them on 11 June 2007 (see Annex [2]).

7. The Communication was the Commission's response to a major consultation exercise (Green Paper) on rules of origin launched at the end of 2003[6]. It was published on the Commission's web-site and there was a 3-month consultation period. Responses were received from private companies, European trade and business organisations, national and local trade and business organisations, consultancy groups, authorities of Member States and of third countries, international and regional organisations, a research centre and a non-governmental organisation. A summary of the results was also published on the internet[7].

8. Both before and after the adoption of the communication, the Commission services have had many meetings with representatives of thirds countries and of trade associations. In addition, in May 2005 and November 2006 two conferences were held with representatives of GSP beneficiary countries in Brussels to inform them about the communication and the options, and to hear their views.

9. The respondents to the Green Paper almost unanimously agreed that rules of origin were too complex and needed to be changed. However, there was no agreement among respondents about how best to do this. At the conferences with beneficiary countries it likewise appeared that the current rules were considered unsatisfactory.

10. The Impact Assessment Board considered this impact assessment at its meeting on 29 August 2007. In response to its opinion, delivered on 31 August 2007, a glossary has been added, a point on the budgetary impact for the EU has been added and some other textual amendments have been made. In addition, a more comprehensive executive summary has been provided. However, the time available did not permit all issues (such as that the reasoning underlying the assumptions made concerning utilisation rate, the benefits and drawbacks of changes to cumulation, and the assessment of employment, social and environmental impacts resulting from the expected trade deflection) raised by the impact assessment board to be fully addressed. The Commission services do not underestimate the importance of these elements but consider that the information and analysis already included are already substantial.

2. WHAT IS THE PROBLEM?

2.1 GSP and the purpose of rules of origin

1. GSP[8] is a preferential trade arrangement which grants reduced or zero import duty to products originating in 179 beneficiary countries. It is an arrangement with a

[6] COM(2003) 787, 18.12.2003

[7] http://ec.europa.eu/taxation_customs/resources/documents/origin_consultation_final.pdf

[8] Currently implemented by Council Regulation (EC) No. 980/2005 (OL L 169, 30.6.2005, p. 1).

development focus, aiming to facilitate the full insertion of developing countries into the world economy, supporting their economic and social development through better access to the Community market and strengthening regional economic integration. It contains three arrangements:

– The general arrangement, which grants a range of reductions and suspensions for the products listed in the annex to the regulation;

– a special incentive arrangement for sustainable development and good governance ("GSP Plus"), which provides additional benefits for 15 vulnerable countries implementing certain international standards in human and labour rights, environmental protection, the fight against drugs, and good governance;

– a special arrangement for least developed countries (EBA), which grants duty- and quota-free access for all products except arms originating in the 49 Least Developed Countries (LDCs).

2. Table 1[9] shows the average GSP preferences and global trade value of GSP preferential imports into the EU.

3. GSP is granted unilaterally by the Community and beneficiary countries range from the very large and relatively advanced (such as China) to tiny islands and the world's poorest countries. However, a "graduation" mechanism provides for the removal of preferences for countries (except those benefiting from EBA) whose exports reach a determined level in any sector. For this reason China, although still a GSP beneficiary, is excluded from preference for many sectors.

4. The countries which make greatest use of GSP are not unexpectedly the largest and most economically developed countries (see volumes of exports in column 5 of

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[9] Source: ADE study.
Notes: Computed from EUROSTAT. TRAINS data was used for tariffs equivalents of specific tariffs and tariff-rate-quotas for agricultural products.
[a] : Thousand euros
[b] : Value of imports eligible for preferences
[c]: Total number of tariff lines (over all countries) to the EU at HS-8 level. See annex 2 of the ADE study for the exclusion of tariff lines due to missing data.
[d]: Import value of preferences according to filing status requested at EU customs (i.e. on the assumption that the requested status was granted)
[e]: Value of actual preferences $\sum_{ij}\left(t_i^{MFN} - t_i^{PREF}\right)M_{ij}$. Does not include special regimes for ACP(37) and ACP(41).
[f]: Import-weighted figures in parenthesis (weighted by imports at HS-8 level)
[g]: See volume II, chapter 1 of the ADE study for definition of the construction of the index
[h]: Maximum value-content of imports when applicable (see text for interpretation).
[k]: Value of imports under the special Cotonou regime (bananas, rice, sugar).
[l]: Value of misclaiming computed as $\sum_{ij}\left(t_i^{CLAIM} - t_i^{ELIG}\right)M_{ij}$ where t_i^{CLAIM} is the tariff applicable to the status claimed and t_i^{ELIG} is the eligible status for the claiming country. A '+' is entered for overclaiming ($t_i^{CLAIM} > t_i^{ELIG}$) and a '-' for underclaiming ($t_i^{CLAIM} < t_i^{ELIG}$)
[m]: Value of imports for GSP (92) countries under tariff lines that claimed either GSP or ACP status when these lines were not eligible for GSP status (corresponding value preference in parenthesis)

Annex 3[10]). LDCs tend to export mainly textiles and clothing and footwear, and (where they have the natural resources) processed agricultural and fisheries products.

Country range / *Description of the value*	**GSP but neither ACP nor EBA (92)**	**ACP but not EBA (37)**	**EBA and also ACP (41)**	**EBA but not ACP (9)**
EU imports[a]	152.191.986	11.718.363	4.847.399	1.566.684
GSP eligible[b]	100.584.679	All lines	All lines	All lines
tariff lines [c]	99.262	10.934	7.376	3.494
Imports under preference: of which[d]	14.021.313	133.884	14.174	760.523
GSP(ACP)	(6.446.738)	(1.747.487)	(677.104)	(1.837)
Value of preference [e]	487.037	6.332	2.844	90.280
GSP(ACP)	(439.086)	(168.953)	(64.428)	(290)
Value of Mis-claiming[l]	1.398	8.361	0	0
Overclaim(underclaim)	(-261.978)	(0)	(0)	(0)
Value of imports (overclaiming) for ineligible GSP lines[m]	1.269.032 (41.533)			
Import Value under Special ACP regime[k]	6.118	381.932	54.083	0
Average MFN tariff[f]	5,08% (2,27%)	4,75% (1,71%)	4,18% (1,50%)	7,91% (11,90%)
Average Preferential tariff[f]	2,66% (1,15%)	0,17% (0,01%)		

Table 1: Preferences and their value in the EU market, 2004
EUR (000)

5. The rules of origin are a tool serving on the one hand to ensure that the activity which takes place in the beneficiary country represents a real economic input and that the benefit of the tariff preferences goes to the intended beneficiaries, and on the other hand to prevent abuse. As such, they are an essential component of Community trade policy.

[10] Source: UNCTAD. The data in Annex I present the utilisation rates with regard to the most exported products from both GSP and EBA countries. Exports of products subject to MFN duty equals zero and which are not covered by the GSP preferences are not taken into account. The figures do not refer to smaller quantities of exports even if low export value could also imply problems in the fulfilment of the origin rules. However, a full analysis of all the headings lines for a large number of countries goes beyond the scope of this impact assessment. Generally the attention is focused on the most exported goods as the economies represent already a certain level of specialisation and intend to maximise the benefits of the existing natural resources, for the purpose of this document called wholly obtained products. It is impossible to set up a system of rules of origin where every country will produce everything. The objective is, on the other hand, to tie permanently the economies of the developing countries with the global economy in order to maximise their internal economic potentials.

6. Rules of origin consist of two parts: substance and procedures:

   – Substance means the conditions for goods to be considered as originating in the beneficiary country. To qualify for preference, products must be "wholly obtained" in it (essentially, natural products or products obtained therefrom) or have undergone "sufficient working or processing" there. For this purpose, the present rules lay down a product-by-product list of requirements as well as detailed conditions for cases in which origin may be "cumulated" with other countries. Fuller details are given in Annex [4].

   – Procedures means the system of administrative cooperation for the management and control of origin. Proof of origin must be given, usually by means of a certificate of origin Form A stamped for each individual export by the competent authorities of the beneficiary country. These authorities are also responsible for carrying out subsequent verifications. Fuller details are given in Annex [5].

2.2 The nature of the problem

1. **The preferences for some products are under-used in some cases.** Statistics show relatively low use rates by many of the least developed countries (LDCs) and other vulnerable countries (Annex 3) – utilisation rates for the top fifteen exported products). Although many factors affect investment decisions and the ability to export under preference (including geography and infrastructure, the available workforce and political stability), it appears that one reason is that rules of origin may act as a barrier to trade for such countries, because exporters there are unable to comply with them because they are complex and/or too stringent.

2. The under-utilisation cannot be ascribed to the preferences duty rates not being low enough for LDCs, since they already enjoy zero duty for virtually all their exports.

3. Rules of origin do not affect all sectors equally; the utilisation rates vary substantially from sector to sector. For agricultural and fishery goods they are high (80-100%). This is because these goods are generally "wholly obtained", i.e. extracted mineral products, harvested vegetables, live animals etc. The lack of these products among the most exported goods seems not to be caused by the stringency of origin rules, as their main objective is to support the use of local raw materials produced in a given country.

4. From the figures in Annex 3 it appears that there are problems in complying with the origin conditions in the industrial sectors. The sector with the lowest utilisation rates is the clothing industry, namely Chapters 61 and 62 of the Combined Nomenclature (CN) (the rate varies from 0 to 50%, even though there are differences at the heading level and a strong differentiation between countries). At a first glance it appears that there are also anomalies with regard to other industrial products exported in large quantities from developing countries (chemicals, machinery and transport equipment). The under-utilisation in these sectors affects more developed GSP countries (Brazil, Russia, Indonesia, Malaysia or Thailand, for example). There are only traces of exports of those products from the LDCs (and the utilisation rates are zero, i.e. they seem not to be able to use the preferences at all).

5. Rules of origin do not affect all beneficiaries equally, but tend to penalise the smaller and least developed countries, which have less integrated economies.

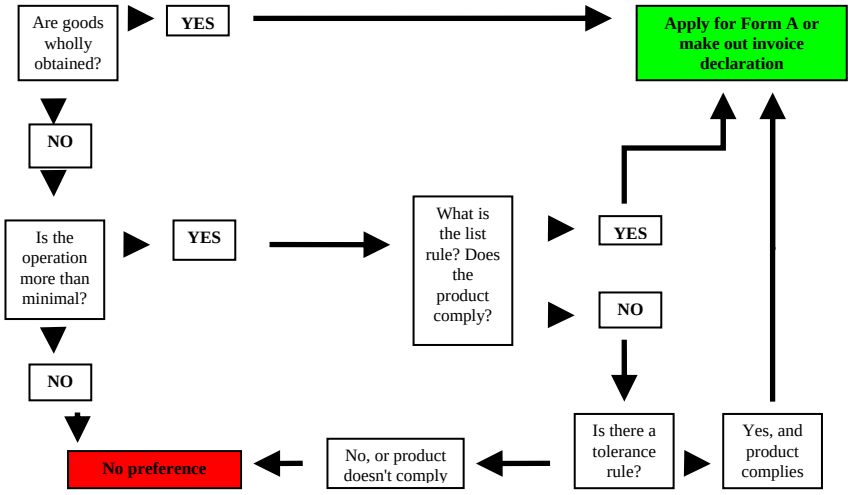
However, other, larger countries are able to export extremely large volumes to the Community despite the current rules of origin. See table 2, and in particular columns 5 and 7.

Partner	Year	HS4	HS Heading Description	Imp Total (EUR 000)	Potential Coverage Rate (%)	Utilization Rate (%)
1	2	3	4	5	6	7
India	2005	2710	Petroleum oils, etc, (excl. crude)/ preparations thereof, nes	845.900	100	**79,3**
India	2005	6204	Women's or girls' suits, ensembles, jackets, dresses, skirts, etc	623.655	100	**86,7**
India	2005	6109	T-shirts, singlets and other vests, knitted or crocheted	564.927	100	**89,1**
India	2005	6403	Footwear, with rubber, plastics, leather... soles, leather uppers	493.445	100	**92,5**
India	2005	6206	Women's or girls' blouses, shirts and shirt-blouses	378.187	100	**89,9**
India	2005	6302	Bed linen, table linen, toilet linen and kitchen linen	340.517	100	**91,8**
India	2005	8703	Motor cars and other motor vehicles principally designed passengers	324.108	100	**83,4**
India	2005	7113	Jewelles and parts of precious metal,metal clad with precious metal	267.337	100	**86,9**
India	2005	6205	Men's or boys' shirts	236.301	100	**82,2**
India	2005	8708	Parts and accessories of the motor vehicles of headings 87.01 to 87.05	217.137	100	**85,5**
India	2005	2933	Heterocyclic compounds with nitrogen hetero-atom(s) only/ nucleic acids	195.962	100	**18,5**
India	2005	6110	Jerseys, pullovers, cardigans and similar articles, knitted or crocheted	194.941	100	**86,5**
India	2005	0306	Crustaceans, fresh, chilled or frozen	187.854	100	**79,3**
India	2005	6406	Parts of footwear/ removable in-soles, etc/ gaiters, leggings, etc	181.393	100	**87,9**
India	2005	3204	Synthetic organic colouring matter and preparations and products	171.903	100	**83,5**
Sri Lanka	2005	6204	Women's or girls' suits, ensembles, jackets, dresses, skirts, etc	136.899	100	**23,3**
Sri Lanka	2005	6109	T-shirts, singlets and other vests, knitted or crocheted	91.284	100	**55,9**
Sri Lanka	2005	6203	Men's or boys' suits, ensembles, jackets, blazers, trousers, etc	80.488	100	**38,6**
Sri Lanka	2005	6110	Jerseys, pullovers, cardigans and similar articles, knitted or crocheted	78.848	100	**53,7**
Sri Lanka	2005	4012	Retreaded or used pneumatic tyres of rubber/ solid or cushion tyres, interchangeable tyre treads and tyre flaps, of rubber.	68.884	100	**75,5**
Sri Lanka	2005	6108	Women's or girls' panties and similar articles, knitted or crocheted	59.542	100	**60,7**
Sri Lanka	2005	0902	Tea	58.000	100	**66,4**
Sri Lanka	2005	6212	Brassieres, girdles, corsets, braces, suspenders, garters, etc	54.457	100	**48,5**
Sri Lanka	2005	6116	Gloves, mittens and mitts, knitted or crocheted	41.573	100	**24,9**
Sri Lanka	2005	4015	Articles of apparel and clothing accessories, of vulcanized rubber	38.399	100	**96,4**
Sri Lanka	2005	0304	Fish fillets and other fish meat, fresh, chilled or frozen	33.684	56,2	**83,9**
Sri Lanka	2005	4011	New pneumatic tyres, of rubber	32.922	100	**81,6**
Sri Lanka	2005	6206	Women's or girls' blouses, shirts and shirt-blouses	28.150	100	**9,4**
Sri Lanka	2005	6104	Women's or girls' suits, ensembles, etc, knitted or crocheted	26.732	100	**45,7**
Sri Lanka	2005	2401	Unmanufactured tobacco/ tobacco refuse	23.725	100	**4,0**

Table 2: Volumes of import in the EU market from India and Sri Lanka and the respective utilisation rates and their value

1. Graphic 1 below and point 1 of Annex [4] show how for exporters of products which are not wholly obtained the complexity is particularly acute, since it is a multi-step process: they must contend not only with a product-by-product list of rules (and in some cases, alternative rules) defining the level of processing required

to confer origin, but also a number of exceptions and conditions (minimal operations which can never confer origin, tolerances, etc.), all giving rise to repeated problems of interpretation, without mentioning the possible use of cumulation.



Graphic 1: Deciding whether products originate or not

2. There are in fact currently 545 different list rules used for the various preferential arrangements in which the EU is involved, corresponding to 509 different categories of products[11], plus 107 alternative rules. There is no common indicator or tool to measure what is 'sufficient processing', which means that the origin requirement can discriminate between products or manufacturing processes which are similar. Nor are the rules easily adapted to the appearance of new products, new processes or changing trade patterns. Annex [6] indicates some of the problems of interpretation encountered, while the following table 3 shows the breakdown of use of various criteria amongst the total number of list rules (alternative rules are not included):

WO	CTH	SP	VP	WO+CTH	WO+VP
29	98	150	128	4	4
5,3%	18%	27,5%	23,5%	0,7%	0,7%
CTH+VP	**SP+VP**	**WO+CTH+VP**	**Sets+VP**	**NR**	**TOTAL**
94	28	2	2	6	545
17,2%	5,1%	0,4%	0,4%	1,1%	100%

Table 3: Current rules for sufficient working or processing, by type.

WO= manufacture from wholly obtained or already originating products
CTH= change of tariff heading or subheading (positive or negative test)
VP= value percentage
SP= specific process

[11] For some categories of products, two or even three rules are offered at the choice of the exporter (not to mention possible 'alternative rules').

NR= 'no rule' (*'manufacture from any heading'*)

3. The ADE study demonstrates the correlation between the strictness of rules of origin and low use rate. This trend is also amply confirmed by anecdotal evidence. On the other hand, in cases where rules of origin have been relaxed, experience shows that the use rate can go up: for example, when the EU reduced the processing requirement for textile products from three stages to two, and following specific initiatives by other donor countries such as the USA and Canada).

4. The rules for "wholly obtained" products are relatively clear, but not free of all difficulty: for example, the case, illustrated in point 4 of Annex [4], of the conditions for fishing vessels catching fish outside the territorial waters of the beneficiary country. These rules are not always easy to interpret or apply to concrete cases and it is particularly difficult to establish the ownership of companies, where several holding companies may be concerned.

5. Cumulation is a facilitation of the normal rules, which allows the processing required to be carried out in a group of countries instead of the beneficiary country alone. GSP regional cumulation aims at encouraging economic cooperation and thus promoting regional integration, but sustained anecdotal evidence shows that it too is under-used[12]. Because of its strict and complex conditions, described in point 2 of Annex [3], it has proved hard to apply in practice. The allocation of origin in this context is particularly important, since different countries are subject to different levels of preference.

6. **Cost.** Participation in preferential trade causes costs for enterprises as well as for public administrations. The current system of rules of origin is seen as burdensome and excessively complicated. The complexity of multiple rules adds to costs for all parties.

7. The administrative costs of rules of origin are those which are incurred by enterprises for the determination of the preferential status of exported products, its permanent control and the issuing of proofs of origin. The administrative costs of any substantial reform affect different stakeholders. As the GSP rules of origin concern an autonomous system of unilateral preferences, the possible costs can be evaluated from the perspective of:

   - economic operators;

   - public authorities.

8. The ADE study concludes that there is an average total compliance cost of 3.2%[13]. It further observes that using its "restrictiveness index" compliance costs can be broken down into two components: *"an industry-specific distortionary cost due to the RoO's effect on input sourcing −forcing a minimum of sourcing from the preferential trading zone as opposed to potentially cheaper sources outside− and an administrative (paperwork) component which we assume, for simplicity, to be the same across industries."* By this means it arrives at *"an average administrative*

[12] There is no requirement to indicate the use of cumulation on Form A (even if some countries do). Consequently, the Community does not hold statistics on the use of regional cumulation.

[13] Point 2.3 in part I

cost of 2.5% (in ad-valorem equivalent) with a standard deviation of 1.7%, suggesting that the distortionary component would be around 0.7%." Other studies conclude that the compliance costs are at least this high and in some cases higher.

9. **Control system is not appropriate.** It has also become apparent that the control procedures of rules of origin, described in detail at Annex [5], are at the same time burdensome for both operators and administrations and weak in terms of breakdown of responsibilities. The current, entirely paper, system of certifying the originating status of products is based on the principle of direct verification by the authorities of the export country for each and every consignment when the certificate is issued. In fact, the demands of trade make this impossible. Rather, as with most of the other information declared about the goods, origin is essentially checked after the event and even then not systematically. The intervention of the authorities at the initial certification stage is therefore burdensome for both exporter and administration and at the same time gives the importer a false sense of security, since he assumes checks have been made when they have not.

10. At the other end of the system, the administrative cooperation mechanism is intensively used. However, there is a significant number of verification requests sent by the authorities of the Member States to which no reply is received. Figures received by the Commission show that in some cases a quarter to a third of requests go unanswered or are answered only after the deadline has expired. Moreover, there are recurrent difficulties for operators in terms of both time and money at import because beneficiary countries fail to update in time the information they are required to provide on stamps and issuing authorities.

11. **Loss of own resources**. Customs cannot refuse the benefit of preferential tariff treatment when there has been no reply to a verification request made at random. This means a loss to the Community's Own Resources when the origin is incorrect. However, even when it is known that preference has been claimed incorrectly or as the result of fraud, the importer (the debtor) is frequently able to claim that he should not pay the customs debt which becomes due, because there was an error by the competent authorities and he was acting in "good faith"[14]. (see point 3 of Annex [5])

12. **Problems in applying sanctions.** Article 17 of the GSP regulation provides for the temporary withdrawal of preferences "in cases of fraud, irregularities or systematic failure to comply or to ensure compliance with the rules of origin of products and the procedures related thereto, and to provide the administrative cooperation as required". However, at present the Community has no regular knowledge of what is happening in beneficiary countries, making it difficult either to apply sanctions or to offer help.

13. **Need for consistency.** Although they were never intended or designed to implement specific policies, rules of origin must be consistent with the overall objective of the arrangements they serve. GSP is a development-oriented regime, and its rules of origin should therefore be simple to understand and apply and offer operators the possibility of real access to the preferences on offer.

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[14] Article 220 of Council Regulation (EC) No. 2913/92 establishing the Community Customs Code, as amended.

2.3 What are the underlying drivers of the problem?

1. **Rules of origin are old and have not followed evolutions in world trade.** The present rules were initially drawn up in the 1970s and they have not materially changed much since, whereas the commercial world has. They were also based on the need to protect Community industry and on the premise that beneficiary countries should be encouraged to build up their own industries in order to comply. In most cases, this has not happened. Instead, there has been a trend towards the globalisation of production, but rules of origin have not been adapted to this. At the same time, compliance costs are high and the paper-based procedures are outdated.

2. **Developing countries need to be better integrated into the world economy.** Ensuring a better integration of developing countries into the world economy, in particular though improved access to the markets of developed countries, was part of the Doha Agenda for Development. Although these negotiations are currently suspended, supporting developing countries in this way was always a part of the commercial policy of the Community. Indeed it remains the top priority of Community trade relations and according to the communication should inspire the revision of its preferential rules of origin. The need for changes was highlighted, in particular, not only in the context of the preparation of the new GSP for the period 2006-2015[15], but also in the Commission's reflection on the future of the textile sector[16].

3. **Lower preferential margins combined with high compliance costs make preferences unattractive**. As a result of successive rounds of trade agreements, preferential margins are much smaller than they used to be. When this is combined with high administrative and compliance costs as suggested by ADE and Scheffer, it becomes no longer worthwhile to use the preferences on offer. The ADE and Scheffer studies suggest that where the preferential margin is less than 5%, there is no incentive to use the preference and this is in line with other studies (e.g. Carrère and de Melo (2006)).

4. The dilemma of LDCs is well illustrated by the information received from countries requesting derogations from rules of origin. Such countries have little or no domestic fabric production, which means they have to import it (so failing to comply with the "two stages of processing" rule) and add only between 27% and maximum 40% in value, too little to be able to use regional cumulation. Moreover, the market often dictates that they use fabric from particular countries, for price or quality reasons. However, many other factors beside rules of origin are also at play.

5. Cumulation can support regional economic integration, but it cannot create it. There needs to be a real will among the partners to work together. Conversely, however, if cumulation exists but cannot be used because the conditions are too strict, it can act as a disincentive to work together.

6. Electronic procedures are increasingly used in both the commercial and administrative worlds, and they are both fast and efficient as well as cheaper than paper-based ones. Neither administrations nor operators in beneficiary countries can

[15] COM(2004) 461 final, 7.7.2004.

[16] COM(2003) 649, 29.10.2003.

understand why they should be obliged to continue to use paper-based procedures for the sole purpose of proving and controlling preferential origin.

7. **The "good faith" issue.** A series of ECJ judgements has led to a rising number of "good faith" claims by importers. Indeed, the latest[17] implies that in most cases where the third country does not reply to an application for subsequent verification, recovery will be impossible. It is then the Community taxpayer who ultimately foots the bill. Knowing this, there is no incentive for the authorities in the exporting country to check that the rules have been applied properly. Nor do many importers carry out further checks of their own with regard to the origin.

2.4 Who is affected, in what ways, and to what extent?

1. Importers, exporters and administrations in beneficiary countries, importers, exporters and administrations in the Community, the Community's own resources and consumers are all affected by the weaknesses in the present rules of origin.

2. If beneficiary countries cannot comply with the rules of origin their products will be more expensive and less competitive. This could lead to investment being withheld, withdrawn or going elsewhere, resulting in businesses failing to thrive, greater unemployment and poverty. On the other hand, improved access to EU markets should allow these countries to develop their economies through increased exports.

3. The costs of customers and ultimately consumers in the Community are increased if it is not possible to claim the benefit of preferential tariff treatment.

4. A continuance of the status quo would in theory continue to afford Community manufacturers of goods similar to those made by beneficiary countries a certain level of protection. However, this protection is somewhat illusory given the success of competitors in other, larger third countries, whose success would be likely to continue. On the other hand, Community firms also lose out like local ones when thanks to the globalisation of production they have manufacturing facilities in beneficiary countries and cannot access the preference.

5. Administrations in beneficiary countries are affected not only because of difficulty in understanding the rules, but also because the obligation for them to issue a certificate of origin for almost every export uses resources which they could otherwise devote to more effective controls.

6. Complicated and unclear rules may result in proof of origin being wrongly issued (or alternatively, no proof of origin issued when a preference could in fact be claimed) and a consequent threat to the own resources of the Community.

7. Administrations in the Community are affected because of their responsibilities for checking and control, but also because of the resources needed to try to recover duty when preference is wrongly claimed.

8. The own resources of the Community are also at risk when a beneficiary country has difficulty complying with its obligations and the fact goes undetected.

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[17] Judgement of the Court of 9 March 2006 in case C-293/04 "Beemsterboer"

2.5 EU right to act

1. The GSP Regulation defines autonomous preferential tariff measures on the basis of Article 133 EC. This regulation refers, for the definition of the concept of originating products and the procedures related thereto, to the provisions on origin in Commission Regulation (EEC) No. 2454/93.

2. Commission Regulation (EEC) No. 2454/93 implements Council Regulation (EEC) No. 2913/92 establishing the Community Customs Code, which is based on Articles 26, 95, and 133 of the Treaty.

3. Consequently, rules of origin are a matter of exclusive Community competence.

3. WHAT ARE THE OBJECTIVES?

1. Overall

   - General objective: Contribute to promoting the sustainable economic development of beneficiary countries, particularly LDCs and other vulnerable countries, by facilitating exports through appropriate rules of origin which are resistant to fraud.

2. Revision of rules for the determination of origin.

   - General objective: Rules of origin which are simple in presentation and application with appropriate administrative burden and costs for operators and administrations, and which facilitate legitimate trade.

     - Specific objective: Increased preferential exports from beneficiary countries in the sectors concerned.

       - Operational objective: Create a new rules of origin system which is simpler, more transparent, more flexible and development-friendly.

         Indicator: GSP utilisation rates.

         Indicator: Operators perceive that the system is less burdensome and simpler.

3. Conditions for the cumulation of origin

   - General objective: Contribute to regional economic integration through acquisition of origin in well-defined and possibly wider zones of cumulation of origin.

   - Specific objective: Conditions for cumulation which are simple in presentation and application and offer an incentive to source materials within the cumulation zone.

   - Specific objective: Simple rules and procedures ensuring that cumulation is facilitated while containing adequate mechanisms to combat fraud.

Indicators: Increase in the use of cumulation by legitimate operators.

4. Procedures for management and control of rules of origin.

   - General objective: Appropriate division of responsibilities between exporters, importers and administrations.

     - Specific objective*:* Improved control mechanisms.

     - Specific objective: Prevent illicit use of preferential conditions by non-beneficiary countries and counter fraud.

       - Operational objective: More transparent rules of origin containing appropriate mechanisms to prevent fraud.

         Indicators: Importers able to claim preferences on the basis of reliable evidence; Reduction in the number of cases of fraud; Reduction in number of "good faith" claims in the years following implementation of new rules; More satisfactory response rate to verification requests in cases where it is low.

     - Specific objective: Reduced administrative burden for exporters.

5. Instruments to ensure compliance by the authorities of beneficiary countries with their obligations.

   - General objective: Preferential arrangements function as intended.

     - Specific objective: The authorities of beneficiary countries are complying with their obligations.

       - Operational objective: Monitoring system established and running on an annual basis.

     - Specific objective: Ensure proper understanding of rules by administrations and operators.

       - Operational objective: Immediate updating of guide for users Support given where required through technical assistance.

4. POLICY OPTIONS

4.1 Revision of rules for the determination of origin – sufficient processing of goods which are not wholly obtained

Summary of options

1. *Status quo*
2. *Across-the-board criterion, based on value added expressed as a percentage of the ex-works price:* ***A.*** *Basic threshold 60%, with 50% for LDC industrial products; special conditions for agricultural and fisheries products* ***B.*** *Basic thresholds of 45% (GSP) and 30% for LDCs; special conditions for agricultural and fisheries products*
3. *Across-the-board criterion, based on a change of HS tariff heading or change of tariff sub-heading*
4. *Adapt the current rules on a product-by-product basis*

4.1.1 Option 1 - The status quo

1. The present rules are based on a list of sufficient working or processing operations which vary from product to product, coupled with provisions on so-called minimal operations and tolerance rules. It may be described as a tailor-made approach.

4.1.2 Option 2 - A single, across-the-board criterion, based on value added

1. A single criterion for determining the origin of goods based on the value added in the beneficiary country (or, where appropriate, regional group) concerned could be applied across-the-board to most products which are not wholly obtained. However there could be alternative or additional criteria for certain sensitive sectors (agricultural and fisheries products, textiles and clothing) to take account of the specific nature of those sectors and prevent abuse or distortion of trade. The same method could also be used for cumulation purposes. There could be differentiated thresholds to take account of the needs of specific sectors or certain groups of countries.

2. This option could be based on ex-works price (defined as today as "the price paid for the product ex-works to the manufacturer in whose undertaking the last working or processing is carried out, provided that the price includes the value of all the materials used, minus any internal taxes which are, or may be, repaid when the product obtained is exported"). The calculation method would be as follows:

$$\text{Value added} = \frac{(\text{Ex-works price} - \text{Value of Non-Originating Materials})}{\text{Ex-works price}} \times 100$$

The communication favours the use of "net production cost" as the basis for calculation of value added (a calculated value designed to exclude variables such as profit and include only those elements really reflecting the contribution of the beneficiary country) but this is widely perceived to have a number of disadvantages, in particular complexity for operators and administrations, high compliance costs

(over twice as costly as an ex-works-based method) and the danger that operators would avoid using the preference for fear of having to reveal their profit margins.

3. The Scheffer study indicates that in the textiles sector a relatively high threshold would be required to be equivalent to the current rules (i.e. two stages of processing), 80% or 90% in some cases, but in the main between 55% and 70% and it is only around the 50% level that it would be possible to qualify through single transformation. However, he also notes that value addition varies greatly from product to product.

4. Scheffer also concludes like ADE that a lower threshold could be offered to LDCs, to give them a head-start to industrialisation, although he favours only a temporary derogation on the AGOA model.

5. Bearing in mind the considerations in paragraphs 1 to 4 above, two options for thresholds are suggested for the purpose of this impact assessment:

   – (A) 60% (equivalent on average to the current rules) for non-LDCs and 50% for LDCs, but with specific conditions for sensitive agricultural products and alternative conditions for fisheries products;

   – (B) in order to provide relaxation, thresholds of 45% for non-LDCs and 30% for LDCs, but with specific conditions for sensitive agricultural products and alternative conditions for fisheries products.

   These options are described in full at Annex [7].

4.1.3 Option 3 - A single, across-the-board criterion, based on a change of HS tariff heading or change of tariff sub-heading

1. Change of tariff heading (CTH) or, for greater relaxation, a change of tariff sub-heading rule (CTSH) could be applied across the board to all products.

4.1.4 Option 4 - Adapt the current rules on a product-by-product basis

1. The current product-by-product approach could be retained, but the list could be "cleaned" to remove the most complex elements and offer targeted relaxation of individual rules, for example by removing additional or double conditions which have been added over the years.

4.2 Revision of rules for the determination of origin – conditions for wholly obtained fisheries products

Summary of options
1. *Status quo*
2. *Simplify the present conditions*
3. *Allow cumulation of the conditions*

4.2.1 Option 1 - Status quo

1. The present cumulative conditions concerning the registration, flag, ownership, master and officers and crew of the fishing vessel would all remain.

4.2.2 Option 2 - Simplify the present conditions

1. The criteria could flag, registration and simplified but adequate conditions regarding property, the crew conditions being removed.

4.2.3 Option 3 - Allow cumulation of the conditions

1. It could be allowed to cumulate the conditions for fisheries vessels between the members of a regional cumulation group, so that for example the vessel could have the flag of one country but the master and officers could come from a different one. This option could be applied on its own or in combination with option 2.

4.3 Option 4 - Conditions for cumulation of origin

Summary of options
1. *Status quo*
2. *Allocate origin on the basis of value added alone* ***A.*** *25%* ***B.*** *10%*
3. *Simplify the present conditions*
4. *Extend the scope of cumulation*

1. It should be borne in mind that since cumulation is a facilitation of the normal rules, both the need for and scope of it depend on the decision taken on the normal rules. It may be argued that the stricter the normal rules, the greater the need for cumulation. Conversely, the more relaxed they are, the less cumulation may be relevant.

2. The ability of cumulation to encourage regional integration is likewise dependent on the level of the sufficient processing threshold. If that is very relaxed, and beneficiary countries can effectively source anywhere, then the very incentive for regional integration is lost.

3. Full cumulation for would be inappropriate for GSP, because different beneficiary countries are subject to different levels of preference, and this could result in circumvention.

4.3.1 Option 1 - Status quo

1. In both bilateral and regional cumulation, a more than minimal operation must take place in the country of last working or processing. In the case of regional cumulation, it is also required that the value added there must be greater than the highest customs value of the originating products used coming from another country of the group. If these conditions are not both fulfilled, a fallback rule applies: the goods have instead the origin of the country of the group accounting for the highest customs value of the originating products used.

4.3.2 Option 2 - Allocate origin on the basis of value added

1. The allocation of origin in cumulation could be based on value added alone, using the same method as for determining whether non-originating materials have been sufficiently worked or processed.

2. The value threshold for cumulation purposes would need to be lower than the sufficient processing threshold in order to provide an incentive to source within the region. Bearing in mind the sufficient processing thresholds suggested earlier (60% and 45%/30%), the following cumulation thresholds are suggested for the purpose of this impact assessment:

   – (A) 25%;

   – (B) 10%.

4.3.3 Option 3 - Simplify the present conditions

1. The present double condition in GSP regional cumulation could be simplified by removing the value addition condition.

4.3.4 Option 4 - Extend the scope of cumulation

1. Two of the present regional cumulation groups (ASEAN and SAARC) could be allowed to merge, as has already happened with the central and South American countries. This could take place on its own, or in combination with option 1 or 2.

2. A more radical possibility would be to allow cumulation between all GSP countries.

4.4 Procedures for management and control of rules of origin

Summary of options
1. *Status quo*
2. *Evidence of origin provided directly by registered exporters only*
3. *Introduce certification by approved exporters only*
4. *Introduce certification by the exporter only (no prior approval or registration)*

4.4.1 Option 1 - The status quo

1. The current system amounts to a "public-private partnership". With certain minor exceptions, the beneficiary country exporter makes a declaration concerning origin for every single consignment using certificate of origin Form A (movement certificate EUR.1 for Community operators exporting for the purpose of bilateral cumulation). However, this must be certified by the competent authorities of the country concerned in order to be valid. Only original, paper certificates bearing original stamps may be used. For certain low value consignments, an invoice declaration may be used instead.

2. When issuing certificates, for the purposes of verifying whether or not the origin rules have been met, the authorities "shall have the right to call for any documentary evidence or to carry out any check which they consider appropriate".

3. At a later stage, either at random or because they have reasonable doubts, the competent authorities of the Member States may ask the authorities of the exporting country to carry out a subsequent verification of the proof of origin. This may lead to preference being refused where it transpires that the products were not in fact entitled to the preference claimed (as well as, in many cases, a claim by the importer that he should not have to pay because there was an error by the authorities and he acted in "good faith".).

4.4.2 Option 2 - Evidence of origin provided directly by registered exporters.

1. Evidence of origin could be given through statements on origin (which as with options 3 and 4 below could be electronic) by exporters who have been registered with the competent authorities of the country concerned. "Registered" means provide certain details enabling them to be identified. Once registered, exporters would make out the statements themselves and transmit them directly to their customers in the Community.

4.4.3 Option 3 - Evidence of origin provided directly by approved exporters

1. Statements on origin would be provided directly to importers by approved exporters. The competent authorities of the country concerned would make checks beforehand, and that the exporter would have to provide certain guarantees and accept various conditions laid down by the customs authorities. This possibility

already exists in GSP, but only for Community exporters exporting for the purpose of bilateral cumulation. This option would therefore consist in making an existing alternative into the rule.

4.4.4 Option 4 - Introduce certification by the exporter only (no prior registration or approval)

1. Exporters could certify the origin themselves, without any requirement for prior registration or approval by the authorities. It already exists to a limited extent in the current rules, for exporters of goods worth less than €6,000.

2. In such a system, the authorities could remain responsible for subsequent controls. However, it could also be envisaged that verifications would be made directly by the authorities in the Community, for example through questionnaires sent to exporters.

4.5 Instruments to ensure compliance by the authorities of beneficiary countries with their obligations

Summary of options
1. *Status quo*
2. *Establish a programme to monitor the arrangements and provide assistance and/or impose sanctions or safeguards where required*

4.5.1 Option 1 - Status quo

1. There is no established, regular system for checking that countries are able to comply with their obligations.

2. The Commission has published a guide for users on GSP rules of origin on its web-site. Technical assistance may also be provided, but on an ad hoc basis.

4.5.2 Option 2 - Establish a programme to monitor the arrangements and provide assistance and/or impose sanctions or safeguards where required

1. There could be established:

   – the systematic monitoring of the capacity of the authorities concerned to comply with their obligations.

   – appropriate information, training and technical assistance on preferential rules of origin, in order not only to remedy but also if possible to prevent any deficiencies.

5. ANALYSIS OF IMPACTS

5.1 General considerations

1. The range of products which would be affected by changes to GSP rules of origin is more limited than it would at first appear. There are many products for which the

preferences are not in reality relevant, either because the products are subject to zero duty anyway, or because the preferential margin is so low that it will always be cancelled out by compliance costs. In addition, most beneficiary countries concentrate their efforts on a relatively small number of products and are unwilling or unable to diversify.

2. The reader's attention is drawn to the fact that the ADE, Scheffer and MegaPesca studies employ a variety of methods in their analysis, including historical analysis, case studies, interviews with stakeholders and econometric analysis. The assumptions underlying certain theoretical calculations are explained in detail in each study.

3. The ADE study concludes that between one quarter (at a minimum) and three quarters of the tariff lines do not benefit from economically significant preferences. If the compliance costs associated with proving origin exceed 2% of the value of the exported product, then half the tariff lines benefiting from GSP status would not justify seeking preferential status. Utilisation rates are positively correlated with preferential margins notwithstanding the fact that the elasticity of preference use to increases in preferential margins is rather low: a doubling of the preferential margin from 5% to 10% only raises utilization rates by 5 percentage points. On such a large sample it can be stated that meeting origin requirements gets harder as preference margins increase.

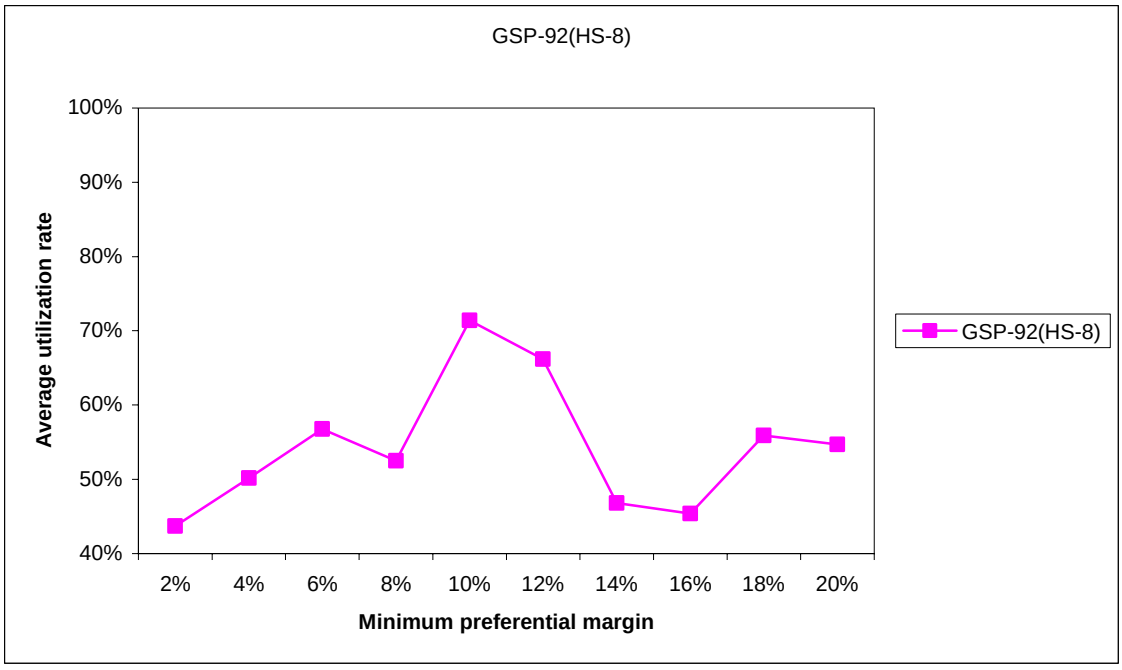

Figure 1.3: Low elasticity of the use of preferences related to the level of preferences. Source: ADE study

4. The products where rules of origin can help to make a difference are those where the preferential margin is larger. A look at the remaining preferences shows that these are mainly sensitive products and indeed those on which developing countries tend to concentrate their efforts, namely textiles and clothing (especially the latter, as the MFN duties in the case of yarns are already low and equal to 4%), fisheries, agricultural transformed products, footwear, machinery and mechanical appliances, transport industry. Taking into account the compliance costs at a level of 3%, it can be stated that for products of HS Chapters 25, 26, 30, 43, 47, 48, 49, 71, 75, 80, 83,

86, 89 and 97 it is not worth claiming the preferences at all, as those sectors are already liberalised (i.e. the preference in the most extreme of cases – EBA treatment[18] – is lower than the compliance costs).

5. Considering a level of 5% of preferences under the most beneficial treatment (EBA), the importance of rules of origin on trade relations and trade flows diminishes, with some exceptions,[19] for products of Chapters 26, 27, 33 40, 45, 46, 65, 66, 67, 68, 72, 73, 74, 78, 79, 82, 88, 90, 91, 92, 94, 95 and 96. Considering this, it is clear that the origin rules are somehow neutral for the allocation of investments and for possible development and impact on the EU industry. As far as these products have already a low worldwide duty rate, the interest in getting preferential origin should be minimal. The costs of obtaining the preferential status and, in addition, transport costs decrease significantly the importance of rules of origin with regard to the development objective and reduce the trade deflection risks to a minimum. For the above-mentioned sectors the reasons for lack of development need to be sought elsewhere (i.e. lack of infrastructure, lack of skilled labour force, high transport costs due to geographical location, energy supply constraints, lack of political stability, corruption and instability of currencies).

6. It is important to distinguish between rules of origin and the policies they serve. The policy aims are set by the GSP regulation. If these are contested, the remedy must be sought at that level (for example by changing the level of preference or by excluding certain products or sectors from it). That is outside the scope of this impact assessment. Rules of origin cannot have separate aims which are not present in the trade policy itself.

7. Although a technical tool, rules of origin can have significant social, economic and other implications according to whether they are more or less strict. To avoid repetition, since the considerations are the same irrespective of the method used to determine origin, before the analysis of specific options there follow some general observations on the social and environmental impacts of rules of origin as well as their administrative costs and the impact of relaxation for the EU budget.

8. Strict rules of origin were normally devised to protect Community production, so relaxation should in principle result in more imports, to the possible detriment of Community industry. However, nowadays production is not concentrated in single countries, but is globalised and this is a trend not likely to be reversed. Moreover, investment is also globalised, so often it is actually Community firms which own

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[18] Products of HS Chapter 93 "*Arms and ammunition; parts and accessories thereof*" are not taken into account as excluded under EBA.

[19] Exceptions for Chapters: 26 (3 products with a specific duty EUR/TNE), 27 (1 product at HS 10-digit with an MFN duty higher than 5%), 33 (7 products at HS 10-digit with an MFN duty higher than 5%), 34 (1 product at HS 10-digit with an MFN duty higher than 5%), 40 (2 products at HS 10-digit with an MFN duty higher than 5%), 45, 46, 65 (2 products at HS 10-digit with an MFN duty higher than 5%), 66 (2 products at HS 10-digit with an MFN duty higher than 5%), 67, 68, 72 (3 products at HS 10-digit with an MFN duty higher than 5%), 73, 74 (4 products at HS 10-digit with an MFN duty higher than 5%), 78 (5 products at HS 10-digit with an MFN duty higher than 5%), 79 (3 products at HS 10-digit with an MFN duty higher than 5%), 82 (8 products at HS 10-digit with an MFN duty higher than 5%), 88 (2 products at HS 10-digit with an MFN duty higher than 5%) 90 (12 products at HS 10-digit with an MFN duty higher than 5%) 91 (6 products at HS 10-digit with an MFN duty higher than 5%) 92, 94 (6 products at HS 10-digit with an MFN duty higher than 5%), 95, 96 (4 products at HS 10-digit with an MFN duty higher than 5%).

the production facilities in beneficiary countries (as illustrated by the fisheries sector, where Community firms own not only the factories, but also the fishing vessels). It also needs to be borne in mind that strict rules are not necessarily bad for development, if they encourage local sourcing of materials. Equally, while lenient rules could generate an increase in exports, it might not last, and it might not be in the interest of a country's longer-term industrial development. If there were no incentive to source locally or regionally, there would no vertical integration and there would be a loss of employment if local suppliers were to go out of business because they could not compete on price.

5.2 The social impact of rules of origin

1. "Social impact" is not just about the number of jobs, but also about wages and living and working conditions, which may be higher or lower, depending on the nature of the manufacturing operations involved. Moreover, in some areas of industry, notably certain parts of the textiles and clothing sector, the workforce is often predominantly female, and the jobs are either a valuable supplement to the family income or a means of achieving some measure of financial independence for the women concerned. These considerations are neither objectives nor indicators for the purpose of this impact assessment but they are a corollary effect of the implementation of the trade policy. In addition, to be of real, long-term benefit the employment needs to be permanent and not precarious. It may legitimately be asked whether in LDCs and other vulnerable countries it should be considered that any job is a good job.

2. It is not only people in exporting beneficiary countries who may be affected, but also those in the Community and in other beneficiary countries. Increases in production and employment in one country may represent pure growth, but on the other hand they may represent a transfer of activity from the Community or from one beneficiary country to another.

3. An illustration of the distinction between a trade policy and its rules of origin is the fact that the GSP *arrangements* already contain a distinct social element in GSP Plus, the full title of which is the "special incentive arrangement for sustainable development and good governance"[20]. Under this, additional benefits are available for vulnerable countries which apply a variety of international conventions, including ones on core human and labour rights. However, this does not apply to LDCs, which get zero duty anyway under EBA simply by being LDCs. Nor is it available for more advanced countries, which are considered too wealthy to need additional incentives, and are even excluded from GSP for certain products. On the other hand, Article 16(1)(a) of the GSP regulation still gives some incentive for EBA and general arrangement countries to respect certain standards, since it provides for the temporary withdrawal of preferences in the event of "serious and systematic violations of principles laid down in the conventions listed in Part A of Annex III [which concern core human and labour rights], on the basis of the conclusion of the relevant monitoring bodies". Indeed, the Commission has temporarily withdrawn access to GSP from the Republic of Belarus because of

[20] This replaced three separate special arrangements, including one for the protection of labour rights, which existed under previous GSP regulations.

alleged violations of the freedom of association and of the right to collective bargaining there[21].

4. It would be inappropriate to seek to use rules of origin as an indirect means of providing an incentive for LDCs to improve labour rights, for example, which the GSP regulation has seen fit to exclude. If need be, the remedy should be sought elsewhere: for example, through international pressure in the appropriate fora. Moreover, commercial pressure from customers – and Community firms when they are also the owner of the exporting company - may also be an effective agent for change.

5. As regards the question of whether the jobs are genuinely new jobs, or a transfer of jobs from the Community to a beneficiary country – or between beneficiary countries, the Scheffer study notes (point 7.0, p. 108) that "The results from a CGE Model shows that the overall impact of changes of rules of origin is relatively small, both in its impact on imports into the E.U, as in affecting trade flows between developing countries and the E.U. A reform will work insofar that it will slow down the exports of China, especially". The Commission services also point out that the globalisation of production in recent years has become irreversible. It is consequently highly unlikely that maintaining strict rules would either ensure the long-term viability of Community industry, or result in beneficiary countries building up their own integrated industries, when they have so far (with but a few notable but still partial exceptions) failed to do so.

6. Business craves above all stability and predictability. The Scheffer study recommends having temporary (even if renewable) derogations as with AGOA, in order to provide a platform for development. However the Commission services wonder whether it would be more appropriate to have more relaxed rules for certain groups of countries on a permanent basis.

7. Besides these general considerations, specific concern has been expressed about the effect of relaxation on employment and social standards in the fishing sector, if it were to lead to fishing by fleets with less stringent standards or paying lower wages than the Community fleet or the beneficiary country directly concerned, or to an increase of illegal fishing. Such fears underscore the importance of appropriate management and control procedures. However, rules of origin are and will remain without prejudice to Community rules in other areas. Countries would remain free, where applicable in the context of fisheries agreements, to apply whatever measures are needed to combat illegal fishing, and also to enforce their employment laws, just as they do today.

5.3 The administrative costs of rules of origin

1. While the rules of impact assessment concentrate on the effect on persons in the Community, given its subject matter this impact assessment should also consider the administrative costs in third countries. GSP covers a wide variety of countries of differing wealth and infrastructure and it is impossible to generalise: only examples may be given.

[21] Council Regulation (EC) No. 1933/2006 (OJ No. L 405, 30.12.2006, p. 35.

2. Since GSP is a unilateral arrangement, the direct cost effect in the Community of changes to rules of origin is more limited than in the case of bilateral arrangements, since the only exports are for the purpose of bilateral cumulation of origin. Community operators are mainly concerned by changes at import (in particular, the question of perceived greater liability for them caused by the introduction of statements on origin be registered exporters). It is in beneficiary countries that the effect of changes would be more widely felt.

3. Administrative costs are the costs incurred by enterprises, public authorities and citizens to provide information, and these may be recurring or one-off costs. This means not just the obvious cost of the procedures, but the costs implied by the rules of substance themselves. There must always be an appropriate cost-benefit balance between the rules for the determination of origin and the procedures necessary for their control. If procedures are too costly or too complex, that on its own may dissuade operators from using the preference, while administrations do not have limitless resources at their disposal and must justify how they use them. If on the other hand the procedural provisions are weak, that can lead to an increase in abuse or fraud, to the detriment not just of public finances, but also of the interests of genuine exporters and importers.

4. Economic operators need people who know rules of origin, verify whether the preferential origin conditions have been fulfilled and engage in contacts with the competent authorities. In a company such people deal normally with accountancy, export-related issues and logistics. In order to benefit from the preferences granted, these people are required to carry on different activities for every consignment of exported goods. The accounting department normally deals with the preparation of appropriate calculations, technicians are consulted on whether or not the specific production process matches the one described in the specific rule and finally export or logistic departments take care of the preparation of the documents. Based on the best knowledge of practices concerning the contacts of the customs authorities with economic operators, it can be assumed that these activities take in average about one hour for each consignment. As the GSP scheme is an autonomous regime, the majority of these costs concern enterprises from the beneficiary countries and the following analysis therefore concentrates mainly on them. Community firms and administrations are also concerned where goods are exported for the purposes of bilateral Cumulation, but to a much smaller extent.

5. Considering three realistic cases concerning three beneficiary countries issuing one million, 250,000 and 10,000 FORM A certificates per year (a big, a medium and a small country), the costs for the economic operators are respectively of one million, 250,000 and 10,000 working hours per year. Taking as a best estimate a cost of 5 EUR per requested certificate, the yearly costs for the operators are respectively of 5 million EUR, 1.25 million EUR, 50 000 EUR[22]. From the point of view of importers, they do not incur extra origin-related costs in addition to those incurred for other customs purposes when an import into the European Union takes place.

[22] The figures given have to be considered as assumptions based on best knowledge and estimates of practices. In reality, the costs vary significantly and depend on the value, quantity of exported goods; in many cases they are already accompanied by different registration fees (renewed on a yearly base or valid for longer periods). Concerning issuing delays, the costs can also differ significantly.

6. As regards the administrative costs for public administrations, generally, the customs administrations of the Member States do not issue many certificates for GSP purposes (only in case of application of the bilateral cumulation provisions, where proof of origin may in any case be given by an invoice declaration made out directly by any approved Community operator). However, the procedures linked to the control activities also require time (post verification practices and control of importers). In the exporting countries, on the other hand, the costs incurred are generally shared by customs authorities and other entities like ministries of trade, finance or economy). Generally, following the assumption concerning the cost of issuance of one certificate, the income of the issuing authorities corresponds to the costs of the operators, always a yearly basis.

7. Point 5.1 indicates that the number of goods that would be affected by relaxing rules of origin is in fact relatively limited, either because goods are subject to zero duty anyway or because the advantage conferred by the preference is so small that it is balanced or even outweighed by the compliance costs. Some operators in the latter category could benefit from a change in rules of origin, but for many others the situation will not change whichever system is used.

8. The studies contain some estimates of compliance costs. In section 2.3 of Volume 1, ADE indicates average compliance costs of 3.2% for the current rules. The Scheffer study notes that "Brenton gives an estimate of the compliance costs of rules of origin mounting up to 4% of export value, so partly offsetting the benefit granted. DeMelo[23] estimate a compliance cost up to 6% in order to meet NAFTA rules of origin." The Scheffer study further notes that depending on the cost components included or excluded in the value calculation, a value added method can place a high administrative burden on the exporter and customs authorities, with the administrative cost for the exporter of a system based on net production cost being over twice that of a system based on ex-works price (point 6.4.1).

5.4 The budgetary effect

1. The reform of GSP rules of origin, which will be linked with their relaxation, will have a budgetary effect. An increase in imports at preferential rates will reduce the amount of duties collected. This will occur irrespective of the option chosen, other than the status quo.

2. The budgetary effects measured by comparing the MFN and GSP rates for given headings. The average rates have been used for this analysis and the following presumptions have been made:

   - commercial circumstances remain unchanged;
   - absolute value of trade does not increase;
   - trade creation effect causes deflection of trade flows from countries covered by MFN rates to GSP countries.

3. The budget effect falls into a range between 195 mln and 488 mln euros, so does not exceed 500 mln euro. This is the maximum: in reality it would be lower. MFN duties

[23] De Melo J. (2006) "Are Different Rules of Origin Equally Costly: Estimates from NAFTA" CEPR DP#4437, (with Céline Carrère), forthcoming in conference volume (2006).

concern 9 countries only. Preferential rates are granted for other countries. In practice, the trade deflection effect would concern MFN countries partly. Such deflection would concern other countries as well but there preferential rates already exist for them.

4. The budget effect is presented in Annex [8] by heading and by chapter.

5.5 The environmental impact of rules of origin

1. Preferential rules of origin have never been a tool for delivering environmental objectives. However, the GSP Plus arrangements also concern a number of environmental conventions and similar considerations apply to the environmental impact of rules of origin as to their social impact.

2. Having said this, it is clear that as far as preferential tariff treatment results in economic development, the setting up and operation of new factories cannot but have an effect on the environment.

3. Nonetheless, pollution caused by production processes would exist wherever an industry was located, in an LDC, in a larger developing country or in the Community. It is also clear that the environmental cost of transporting products from third countries is inevitably greater than would be the transport costs of products manufactured in the Community (an issue popularly known as "food miles"). To that extent, it may be said that if relaxation of rules of origin led to a boost in manufacture and an increase in preferential exports, then there would be an increase in pollution. It is impossible to quantify the extent of this (it depends on whether the factories would be new or additional, how modern they were, whether more ships or aircraft were needed to transport the products or not), but given the countries involved - LDCs are by definition mainly small economies, countries such as China being excluded from GSP for many sectors - it would be likely to be limited in overall terms. In addition, it depends whether increased exports from beneficiary countries represented an actual increase in world production, or simply a transfer of production from one place to another. Given that the ADE study suggests that the main effect of relaxing rules of origin would be to slow down the growth of Chinese exports, it follows that any increase in developing countries' exports (particularly from China's Asian neighbours) would represent more a local and limited shifting of pollution than an increase in it.

4. Specific concern has been expressed about the effect of any relaxation in rules of origin on fish stocks, it being feared in certain quarters that it could lead to an increase in illegal fishing, particularly given that the use of preferences for fisheries products by certain countries is already high. Such fears underscore the importance of appropriate management and control procedures. However, as already noted, rules of origin are and will remain without prejudice to Community rules in other areas. They have nothing to with quotas to preserve fish stocks countries will remain free, where applicable in the context of fisheries agreements, to apply whatever measures are needed to combat illegal fishing. Bans to protect certain species could still be imposed. There is also an important safeguard in the GSP regulation itself: Article 16(1)(e) provides for the temporary withdrawal of preferences in the event of "serious and systematic infringements of the objectives of regional fishery organizations or arrangements to which the Community is a member concerning the conservation and management of fishery resources.

5.6 Revision of rules for the determination of origin – sufficient processing of goods which are not wholly obtained

5.6.1 Option 1 - The status quo

1. If the present rules were maintained, the existing problems in their interpretation and application would remain: in many cases, complexity, inability of exporters in many countries to comply, either because of burdensome procedures or the stringency of the rules themselves.

2. Not all the present rules are complex: for example, the basic two stages of processing rule for textiles is not a difficult concept to grasp. However, the "printing" rule for textiles has been a subject of notorious complications and the rules take no account of new technologies or processes which are introduced.

3. Countries which can already comply with the present rules would continue to do so, but the others would in all probability never succeed, because infrastructure problems or lack of investment would prevent them from ever developing the necessary industrial base. This is amply demonstrated by the experience of derogations from GSP rules of origin for certain textile products, which have in fact become quasi-permanent, being prolonged several times without the countries concerned ever making the desired industrial progress, or even being able to benefit fully from the derogation.

5.6.2 Option 2 - A single, across-the-board criterion, based on value added

Impact	Option 2A (Value added: thresholds 60%/50%)	Option 2B (Value added: thresholds 45%/30%)
Exporters in beneficiary countries	Threshold is equivalent to current rules, so no change, however due to differentiation of the stringency of the rules in different sectors; a limited increase of utilisation rates is foreseen.	General relaxation should increase exports by 1,38% on a yearly basis.
Importers in the Community	No increase in competition	Imported products more competitive but taking into account the low trade creation effect, impact on Community producers should be limited.
Consumer	No change	Lower prices if the benefit of increased profit margins is passed on
Social effects in exporting countries	No change	More jobs but their nature depends on the scale of transformation
Social effects in the Community	None.	Effect on jobs in the Community likely to be minimal
Beneficiary country administrations	Need to adjust control methods in some cases	Need to adjust control methods in some cases
Community administrations	Need to adapt to a method based on value, but only one method to apply for all products	In control terms, same as for option 2A. However, the more achievable the threshold, the less likely that operators will try to commit fraud.
Other beneficiary countries	No change.	Some production could be displaced
Environmental effects in the Community	None.	None.
Environmental effects in beneficiary countries	No change.	Larger carbon footprint through increased use of transport, additional pollution from more production facilities

Table 4: Summary of economic, social and environmental impacts of options 2A and 2B

1. ADE concluded that the EU was right to envisage simplifying the current system. They further concluded that its major drawback was the practical complexity of its implementation (particularly if the net production cost method envisaged by the communication were used), especially for small firms (and hence for low-income countries) but also for customs administrations. Other drawbacks included disclosure issues (again related to the net production cost method) and exchange-rate fluctuations. They also thought it a natural criterion for giving preferential treatment for LDCs, which could be granted a more favourable threshold.

2. ADE favoured a single threshold for all products, on the grounds of simplicity. It feared that otherwise a Pandora's box of demands for special treatment would be opened that would, in all likelihood, make it difficult to stick to a consistent value-added based approach.

3. ADE constructed a "restrictiveness index" to show the degree of severity or relaxation of rules of origin, as well as calculating the costs of the system and any change. These suggest that in fact the effect on Community industry of relaxing GSP rules of origin would be extremely limited, although that is not to say it would not have specific effects in particular sectors: in Volume 1, point 2.5 they state "As shown in the results in table A.3.3, these secondary effects can be expected to be very negligible for EU producers, even for industries where GSP countries have a substantial market share (we supposed that preferences and the MLC content were applied to a market where the GSP had 25% of the EU market). Thus, even if there might be some significant adjustments in some small market segments, in general even for the sectors where the preferential margin is 10 percentage points, repercussion effects in the EU market will be small. Of course this is so, because most of the displacement will take place with MFN suppliers who are likely to be producing closer substitutes than EU producers".

4. The two options have different economic consequences, both in development terms for the beneficiary countries and impact on the Community. The future in ten or even five years' time is unpredictable, but an economic analysis of the consequences can however be presented. As the objective of the GSP scheme is development, the major indicator of a positive impact of a reformed scheme of rules of origin is the utilisation rate of the preferences granted under the scheme. Increased utilisation of the preference will create a situation in which the trade between the beneficiary countries and the Community will increase. We assume that in case of Option 2B with low value added thresholds, the consequent utilisation of preferences will be the highest (full utilisation). On the other hand, by applying higher value added thresholds (Option 2A) the correspondent increase in utilisation rate should be minimal (utilisation increased by 40%). The trade creation effects of the two different options are presented in Annexes [9] (LDCs) and [10] (GSP)[24].

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[24] Source: UNCTAD. The formulas used to calculate the trade creation effect for each scenario are as follows:
OLD = MFN/100;
NEW = PREF/100;
OTH1 = OTH;
OTH2 = OTH * 0.4;
TC1 = OTH1 * (- MELAS) * ((NEW - OLD) / (1 + OLD));
TC2 = OTH3 * (- MELAS) * ((NEW - OLD) / (1 + OLD));
where:
MFN - MFN Applied rate in per cent (column H in the tables prepared by NL)
PREF- Relevant preferential rate (GSP or LDC) in per cent (column I)
OTH - Value of imports receiving MFN treatment
MELAS - Elasticity of import demand
TC1 - Trade creation for the full utilization scenario
TC2 - Trade creation for the 40 % utilization scenario
It has to be underlined that with reference to options 2A and 2B that the calculation of the trade creation effect based an increase of use of preferences is an assumption by the authors.

5. The trade creation effect shows the value of trade created in a year by each option in terms of the increased utilisation of the preferences. This calculation does not take into account the possible trade deflection effect, as far the levels of the thresholds chosen as options guarantee substantial transformation.

SIMULATION OF TRADE CREATION EFFECT GSP (92) – (all ACP and remaining LDC)		
HS CHAPTER	**FULL UTILIZATION OPTION 2B - THRESHOLDS 30/45% EUR (000)**	**40% UTILIZATION OPTION 2A - THRESHOLDS 55/60% EUR (000)**
FISHERY (aggregated values)		
Chapters 03 and 16 (without headings 1601 and 1602)	**47.753**	**19.101**
AGRICULTURE (aggregated values)		
Chapters from 01 to 24 (excluding 03 and 16 but including headings 1601 and 1602)	**41.936**	**16.774**
TEXTILES & CLOTHING (aggregated values)		
Chapters from 50 to 60 (textiles)	20.290	8.116
Chapters from 50 to 63 (clothing)	431.468	172.587
Chapters from 61 to 63 (T&C)	**411.178**	**164.471**
ALL PRODUCTS	**1.503.005**	**601.202**

Table 5: Summary of trade creation effect of options 2A and 2B on HS Chapter level for the GSP countries

SIMULATION OF TRADE CREATION EFFECT LDC (9) – ACP LDC		
HS CHAPTER	**FULL UTILIZATION** **OPTION 2B - THRESHOLD 30/45%** **EUR (000)**	**40% UTILIZATION** **OPTION 2A - THRESHOLD 55/60%** **EUR (000)**
FISHERY (aggregated values)		
Chapters 03 and 16 (without headings 1601 and 1602)	**8.058**	**3.223**
AGRICULTURE (aggregated values)		
Chapters from 01 to 24 (excluding 03 and 16 but including headings 1601 and 1602)	**7.689**	**3.076**
TEXTILES & CLOTHING (aggregated values)		
Chapters from 50 to 60 (textiles)	593 931 704	237 572 684
Chapters from 50 to 63 (clothing)	943 177	377 272
Chapters from 61 to 63 (T&C)	594 874 881	237 949 956
ALL PRODUCTS	**618 480 020**	**247 392 013**

Table 6: Summary of trade creation effect of options 2A and 2B on HS Chapter level for the EBA countries

6. The overall trade created on a yearly basis following Option 2A is of almost 850 000 000 Euro (including GSP and LDC beneficiaries), while for Option 2B the effect is higher: over 2 100 000 000 Euro. The latter value, if compared with the total EU imports from the beneficiary countries in 2004 (Table [2]) represents a 1.38% increase.

7. It is interesting to evaluate the impact of option 2B on the specific sectors that could be considered as the most sensitive today. This option reflects the major improvement with regard to rules of origin and constitutes the most ambitious change from the current status quo. While the trade creation in the agricultural and fishery sectors is only the 4.97% of the total created trade, the impact in the textile and clothing sectors is much more relevant, reaching 48.38% of the total trade generated, clothing being 97.93% of the total trade created from chapters 50 to 63. Differences arise also when considering the LDCs in comparison with the remaining GSP countries. For the LDCs clothing (Chapters 61 to 63) sector represents 97.03% of the total trade generated by the full utilisation of preferences, while the effect is much more diluted for the other GSP countries, where clothing represents only 27.36% of trade potentially generated.

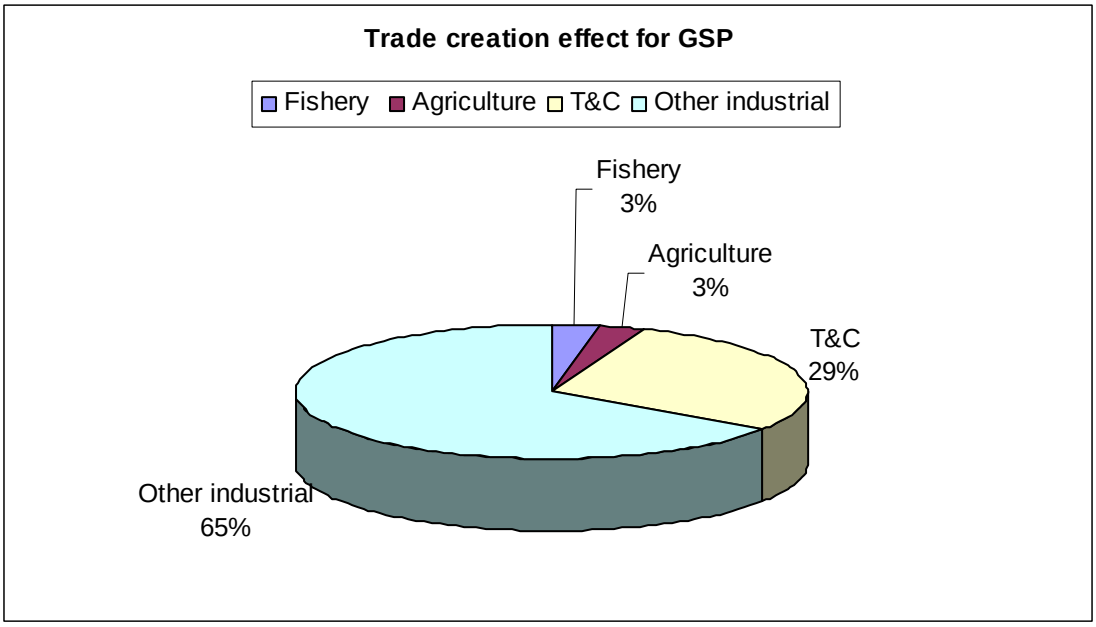
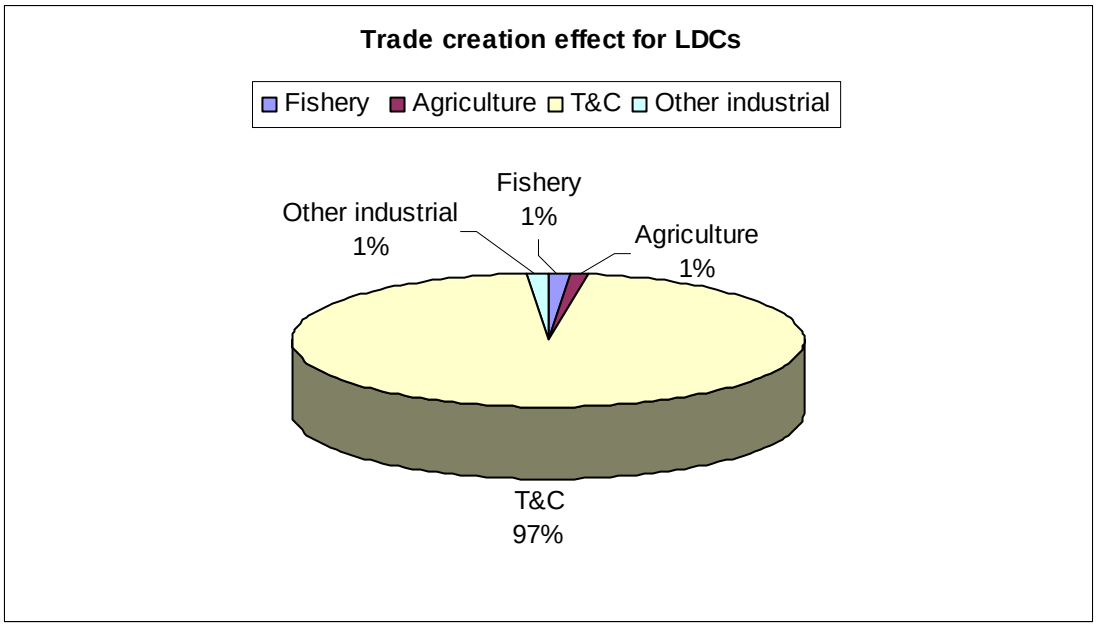


Chart 1: Trade creation effects for specific sectors for GSP beneficiaries



Charts 2: Trade creation effects for specific sectors for LDC beneficiaries

8. The trade creation effect exercise is a simple theoretical instrument that can however lead to certain conclusions anticipated previously. Rules of origin can be an element of trade policy aiming at development of developing countries. However, their impact is limited in comparison with the existing trade flows between the EU and the beneficiary countries. Moreover, the figures confirm that any change in rules of origin has a differentiated impact on different sectors of production. Clothing in particular, but also agricultural and fishery products, are of the utmost importance, especially for LDCs, in order to increase their export volumes, while for the GSP, countries which are more advanced in building

integrated industrial production chains, the theoretical full utilisation of preferences could have a wider effect among the HS sectors. This dispersion effect confirms that the utilisation rates for many products are rather high and those countries do not have major problems in exporting under preferences in compliance with the current rules.

9. The Scheffer study likewise concludes that trade trends justify a modification of rules of origin. However at the same time it notes that rules of origin are only one of several factors and their ability to create or alter trade flows should not be overestimated, and that historically they were never designed to promote development. Indeed, he notes that "A reform will work insofar that it will slow down the exports of China. and that "the overall impacts of changes of rules of origin are relatively small, both in impact on imports into the E.U, and in trade flows between developing countries and the E.U. A reform will work insofar that it will slow down exports from China, especially in a 70% value added scenario". He further notes that while countries with an integrated supply chain have gained market share since 2000 and even more in 2005, the position of smaller countries has eroded, especially in woven products where double transformation in combination with tolerance rules sets a high mark for making products eligible for preference. He points out that "Too many countries have not been able to establish apparel exports, especially ACP countries." and that "In view of their performance in AGOA and with Canada, rules of origin can be considered an important factor in offering a head start to industrialisation, but not in promoting regional and vertical integration and hence a sustainable industrialisation. The impact on the donor country is limited as trade diversion is mainly at the expense of dominant suppliers."

10. Scheffer concludes that a value added method is feasible, as a value criterion has industrial significance. However, it has advantages and disadvantages. An advantage is its technological neutrality vis à vis the different steps in the chain. On the other hand, he shared ADE's concerns about the net production cost method, as well as about exchange rate fluctuations.

11. Scheffer concludes from the AGOA experience that a single transformation rule or a value criterion with a similar effect is beneficial to the least developed countries. He points out[25] with regard to AGOA that *"The nature of industrialisation is however constrained by the temporary nature of the AGOA regime and the dependence of these countries of external capital": there are "factories based on simple machines, a refined division of labour and hence the mobilisation of unskilled workers, trained to perform effectively simple operations under foreign supervision. These factories are sometimes considered as night shifting factories, easily installable and easily removable"*. He further notes that *"In terms of trade effects the AGOA system has two impacts: a trade diversion from Asia to Africa in terms of origin and from EU to USA in terms of destination. There is no vertical integration, not even in a regional setting. However the industrialisation has a direct employment impact especially on women employment, and any industrialisation has to start with labour intensive processes, as there are few other local advantages."*

[25] Point 1.3.1

12. The Commission services note that the EU needs to aim at something which is sustainable, and that its existing experience with derogations is not encouraging.

13. Rules based on value should not result in a tightening of the rules, since that would run counter to the communication. Where the rules are already lenient, it is usually because the Community market is in need of such imports, or that Community production of such goods is lacking.

14. Taking the results of the ADE study as a benchmark, the Commission services analysed what were the agricultural products for which a value condition of 60% alone would suffice, and what were those for which additional conditions would be required in order to encourage the maintenance of local sourcing and so promote development and what those additional conditions might be. They consulted a number of representative organisations to test these ideas (see Annex [1])

15. The Commission services' analysis showed that a single value added criterion across the board posses no problems from a conceptual viewpoint for agricultural products and allows for a great simplification with respect to current provisions.

16. Today most agricultural rules are based on the "wholly obtained" principle, i.e. in principle "100% value added" but subject to a tolerance for the use of non-originating materials (10% of the final ex-works price of the product for GSP, and 15% in the case of the Cotonou agreement). The Commission services concluded that foreign contents around 15%-20% may be considered as an average estimation for all agricultural products; which, conversely, represents an added value of between 75-80%. Thus a 60% threshold across the whole range of agricultural products would represent a relaxation of a quarter compared to the current average level. However, this could result in a tightening for certain products, particularly those based on a CTH rule (e.g. representatives from the vegetable oil industry noticed that current rules for soya oil require only the crushing of the soya beans, which would be equivalent to not more than 20-25% value added).

17. While most of the relevant bibliography suggests that making rules of origin more development-friendly means a significant relaxation in the strength of the conditions for obtaining the origin status, it has to be borne in mind that the economy of developing countries relies heavily on agriculture, at least for a large part of their population. As indicated by UNCTAD[26]:

    "Commodity production and trade have a significant bearing on sustainable livelihoods of the poor, as well as on the export and growth performance of the large number of commodity-dependent developing countries". "Over the pass decade, commodity export dependence and export concentration have not decreased significantly in developing countries, indicating the importance of actions in this area in improving export performance of these countries".

18. In addition, another important aspect of the economic welfare of these commodity-dependent countries is the fluctuation of the world prices of the products on which their exports depend. UNCTAD also noted major falls in the prices of some commodities of major export interest to developing countries, such as coffee, cotton

[26] UNCTAD/DITC/TAB/2005/1 – Developing countries in international trade 2005: Trade and Development index.

and sugar between 1998 and 2002, with direct consequences for earnings and poverty levels.

19. At the same time, the consolidation of trans-national holdings has become a main driver of the international trade; UNCTAD also notes:

    "Parallel to the price decline, developing countries exporter of agricultural commodities have been faced with additional difficulties arising from their weakening position in global value chain. Increased concentration and vertical integration of different stages of the supply chain have strengthened the bargaining power of a few Trans-National-Companies and large distribution networks in a number of commodity markets."

20. Therefore, it appears that the relaxation of rules of origin should be taken cautiously when referring to basic raw agricultural products and their immediate derivatives. With the aim of ensuring sustainable development in developing countries, so that fragile communities are not put in danger[27], distinctions between agro-commodities and other products and goods may be needed, namely on different approaches as regards relaxation of the origin conferring rules.

21. The fluctuations in commodity prices and the unstoppable monopolistic trend in the international trade of these materials make unrealistic or biased any limitation in value terms in the use of foreign materials. A more prudent and precise approach is to fix the upper limits of the content of foreign materials on a volumetric basis. This is also consistent with the tariff classification system in which certain products containing one or more materials on a variable scale are classified according to their composition in weight or volume terms. There seems to be no reason for the current GSP threshold to be lower than the one for the Cotonou Agreement. Allowing 15% by weight of non-originating material to be used would offer a degree of flexibility for agricultural products and also represent a slight relaxation as far as GSP is concerned.

22. The Oceanic/MegaPesca study concluded that a value added method would not be suitable for fisheries products because of the wide variations in value added within the industry. It concluded in particular that:

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[27] 'Kenya has faithfully complied with its basics commitments on agriculture in belief of the benefits from freer trade. The results of implementation, however, have been extremely disappointing. The reform process has neither helped the sector nor improved food security. The annual average growth of our agriculture value added fell from 3.3 per cent during the 1980s to 1.4 per cent in the 1990s without compensating growth in the industrial or the services sector. Increase in imported foodstuffs displaced rural farmers from the domestic market. Without alternative source of income, farmers have found difficulties in purchasing imported foodstuffs however cheap they may be, hence exacerbating poverty, food insecurity and malnutrition in Kenya' – Government of Kenya statement to the WTO's Committee on Agriculture 12 March 2001.

'*Food imports …. Have futher demoralised the small-scale farmers. Having produced maize, rice, soybeans, rabbits, sheep and goats, Ghana's farmers cannot obtain economic prices for them, even in village markets. Their produce cannot compete with imported maize, rice, soybean, chicken and turkey. Farmers are producing as much food but receiving lower prices. Smallholder incomes have fallen and malnutrition among the rural poor has risen'* – Trade and the Hungry, John Madeley, Brussels 1999.

Christian Aid believes that the arguments for yet more liberalisation in agricultural trade ignore the millions of rural poor who are significantly dependent on agriculture for their livelihoods and food supply.

- for all but one of the samples of products assessed, value added thresholds of 50-60% could not be met (table in executive summary, p. 2, refers).

- there seemed to be a generic problem with the added value criteria when applied to seafood. The reason for this is high raw material costs, exacerbated by the effect of extracting usable meat and failure to reach such a threshold was particularly prevalent for the type of labour intensive primary processing most suited to developing nations;

- there would be radically different outcomes for different species groups, with a high impact on tuna canning but minimal impact on shrimp producers. This made a “one-size-fits-all” system problematic;

- the high proportion of costs attributable to raw material also leads to excessive sensitivity of value added to changes in raw material costs, themselves very variable and subject to changes in exchange rates (all beyond the producer’s control);

- In order to be achievable, the value added thresholds would have to be set closer to 25%-30%. While this would not necessarily increase the risk of "product laundering" because such a limit still requires significant processing going well beyond simple trading activities or those designed purely for preservation, there could still be potentially significant and relatively immediate effects in relation to sustainable development and the environment (points 6.5.5 and 6.5.7 of the study refer):

    - Raw material supplies would be sourced more widely with price the governing factor. This would discriminate against the EU fleet which is bound by access agreements to fish responsibly and favour the vessel operators who cut the most corners – i.e. those who pay least to their crew and tend to adopt IUU fishing practices. As most fish resources are regarded as fully exploited, the outcome would be a substitution of the responsible by the less responsible, with clearly detrimental effects on the resource.

    - An indirect effect would be a reduction in the reliability of some key data. Traceability would, for example, diminish along the supply chain, particularly regarding the source of the initial raw material. As raw material sourcing ceased to be an issue, so would concern about its origin. The quality of resource data would decline correspondingly as would the reliability of SPS (food safety) information.

    - Another knock-on effect could be weakening of the value of Fisheries Partnership Agreements and subsequently EPAs. Should the EU fleet reduce or cease activity in preferred states’ EEZs, then the rationale behind these agreements would unwind.

    - The domestic fleets of some nations would also probably be damaged in some cases. This would be especially true in cases where a fleet is being built up and is struggling against established competition.

    - Linked to this, there would also be a negative effect on other primary producers-small scale fish and shrimp farmers. These could face foreign

competition that might undercut them. It seems then that the processor's gains would at least be partially offset by losses by primary producers.

23. The key question in relation to textiles and clothing is the double versus single stage transformation issue. Double stage transformation effectively obliges a country to build up its own backward linkage industry (i.e. produce the fabric itself) in order to get preference. With single stage transformation it could import the fabric from any country but the jobs could be less secure, less skilled and less well paid. According to the Scheffer study, the 60/50% scenario would mean the maintenance in effect of a double transformation requirement in most cases, which should mean little or no change compared to today. Only at 50% does China start to become an important supplier of textiles for further processing in third countries. However at the 30% level then single stage transformation is clearly possible. As well as estimating the overall effect in terms of trade, Scheffer is also able in tables 14, 15 and 16 of his study to give some estimates of production and employment effects in two scenarios (70% value added required and 50% value added required). These clearly show slight falls in the Community as well as in China (for clothing) and also in Bangladesh but on the other hand significant increases in some countries such as Sri Lanka. It may be assumed that these effects would be a bit larger with an even lower threshold. However, the effect on the EU should not be exaggerated, when most EU clothing imports already come from countries which do not even benefit from preference.

24. Representatives of the textile industry in the Community have expressed their opposition to the value added method and to relaxation, on the grounds of complexity and the likely impact on their industry.

25. Other products are less sensitive than agricultural and fisheries products and textiles and clothing. In many cases the rules are already based on value. However in the consultation on the treatment of industrial products (to which 30 associations replied), while there was some support for the use a value added method, the majority of respondents expressed their opposition both to a having a single method based on value and to having a single threshold. Among those opposed, when asked what threshold they would prefer if there were nevertheless a value added system, the majority preferred higher thresholds. As regards specific reasons for rejecting the value added method, the chemical and metal industries in particular cited significant and regular fluctuations in raw material prices.

26. Using the ex-works price as the basis for calculation is less costly for exporters than net production cost, since they would not have to keep two sets of accounts or make complex calculations. Ex-works prices are public and exporters would not be effectively forced to reveal their profit margins through their calculations.

27. Currency exchange rates do fluctuate, which could mean that products qualify one day, but the next, resulting in uncertainty for operators. This is not a new issue, although it is not tackled in the current rules. It could be mitigated by allowing exporters to use a reference period (using the average of their sales and imports over the previous year, for example) instead of having to re-calculate for every single consignment whether or not they met the threshold. Such a mechanism could allow the effect of exchange rate fluctuations could be smoothed over.

28. Commodity prices in some sectors are also subject to fluctuation, but this becomes more significant if the value threshold is high. If the threshold is set at a low level, then the product should still qualify even if prices vary.

29. In terms of costs, for those sectors where a value added rule is already used, either on its own or as an alternative (e.g. chapters 84 and 85), there would be no change. For those where it would be new, it should nevertheless be a concept with which all are familiar, since all traders need to be aware of their costs for commercial reasons. Moreover, they would have just one rule to consider, instead of several interacting with each other as at present. Scheffer, commenting on the textile sector only, where value is not currently much used, comments that "The compliance costs of a value system are significantly higher than the current system. If valuation requires an improvement of cost control, an auditing of cost price calculation the costs of compliance are between 1.5 and 3% in an ex works system. This means that for countries with only a reduction in duties a value system is neutral, hence it only benefits only countries with a 0% duty rate".

30. Some operations generate considerable value without bringing any real benefit to the beneficiary country, but possibly benefiting instead a non-beneficiary. Currently there is a list of minimal operations which can never confer origin. To dispense with it as the communication envisaged would be a simplification, but it would not be favourable to development if it merely encouraged "screwdriver"-type operations, where all the input was foreign and the manufacturer could change location at any moment. The communication envisaged dispensing with this list, the value thresholds alone being sufficient. This list does sometimes give rise to difficulties of interpretation. An alternative could be to approach the problem from the other end and to design instead a positive definition of "manufacture" which would ensure that operations which take place are genuine and economically justified. However, such a definition would also be liable to interpretation, only more so being new. The current list has the virtue of being familiar, as well as clearly excluding certain operations. In the scenario envisaged by the communication, exporters would be responsible for making out their own statements on origin and for this to work the rules need to be simple and clear. The list offers the best guarantee of this. In any event, it would be inappropriate to dispense with an important safeguard.

31. Both ADE and Scheffer mention the concern of some customs officers that a value-based method is harder to control (and hence more open to fraud). However, the authorities are not unused to dealing with rules based on value, and the efficiency gain from having a single rule to control instead of many different ones, with numerous additional conditions, cannot be overlooked. Once they had undergone any specialised training needed, they would it would be much simpler to have to control only one methodology. Moreover, it underscores the importance of fast and efficient management and control procedures.

32. As in case of any change of legal framework, additional costs would appear at the beginning for both the economic operators and public authorities, although after the start up period there should be reduction for operators. The accounting departments of economic operators would have to adapt to the new rules, but as the new system would be simplified (only one methodology applied), generally in a long-term perspective their internal origin-relates costs should be lower. If exporters declare

the origin themselves there would be no longer be the cost of obtaining official certification for every shipment[28]. So, based on best technical knowledge, it can be assumed that the time needed for preparing each consignment would be halved. For big countries issuing around one million certificates a year it means substantial savings (500 000 working hours saved). For smaller countries the savings would be proportionally lower (125 000 working hours for medium size countries and 5 000 working hours for smaller countries). For Community operators the potential change of the system of determination and certification of origin should be neutral. They issue a low number of certificates of origin for GSP counties (for cumulation purposes only).

33. It has to be underlined that although efficiency is an aim, the reduction of costs of customs administrations is not an aim of any reform of rules of origin. However, by changing the rules and the related procedures, the management system can better allocate its resources in order to comply with its own primary objective: security of trade flows and predictability of trade. Therefore, the customs administrations of the importing countries will continue to control the origin with a special focus on these activities, but basing themselves, instead of on certificates of origin, on the correctness of the statements of origin. They will not be engaged any more in issuing certificates for cumulation purposes. The situation looks different from the perspective of the beneficiary (exporting) countries. In those counties special offices or departments where exporters can obtain certificates have been created. In a system where exporters would declare the origin themselves, the revenues and costs of the public administrations would be reduced (issuance and verification of certificates of origin FORM A). On the other hand, an integrated system of registration and data-base management should be introduced. Based of risk management procedures, the first objective of the customs authorities of the exporting countries will be the verification of origin (i.e. the correctness of the statements of origin made by the operators). In case of verification procedures, the competent authorities responsible for those verifications will have to adapt their knowledge to the methodology chosen for the determination of origin, i.e. value added. In this case more accountancy skills will be required from officials involved in those verifications.

[28] The general costs of applying for an origin certificate have been presented in paras. 103-104. It has to be underlined, that registration costs existing under the current system will probably continue to exist under a system foreseeing the registration of the exporters, as it is likely foreseeable that the competent authorities will continue to apply registration fees. The savings will only concern the direct costs related to the issuance of the current proofs of origin.

5.6.3 Option 3 - A single, across-the-board criterion, based on a change of HS tariff heading or sub-heading

Impact	Option 3 (Change of tariff heading)
Exporters in beneficiary countries	Relaxation leads to increased exports in some areas.
Importers in the Community	Some imported products more competitive but overall the impact on Community producers should be minimal.
Consumer	Lower prices if the benefit of increased profit margins is passed on
Social effects in exporting countries	More jobs but their nature depends on the scale of transformation
Social effects in the Community	Effect on jobs in the Community likely to be minimal
Beneficiary country administrations	Need to adjust control methods in some cases. Should be familiar with tariff classification.
Community administrations	Benefit from having a single rule to control; familiarity with tariff.
Other beneficiary countries	Some production could be displaced
Environmental effects in the Community	None.
Environmental effects in beneficiary countries	Larger carbon footprint through increased use of transport, additional pollution from more production facilities

Table 7: Summary of economic, social and environmental impacts of option 3

1. A CTH (or CTSH) rule has the advantage of simplicity, being based on something well known and already used for customs purposes. However, therein also lies its greatest disadvantage, because the HS was designed for the classification of goods and not for origin purposes. For this reason, it would result in relaxation in some cases (such as textiles, where the double transformation rule would effectively be replaced by single transformation), while paradoxically resulting in stricter rules in other cases (for example, in the fisheries sector peeling and freezing whole raw fresh shrimp would not count as processing on these criteria (a tariff jump of only 0306-2 to 0306-1) whereas simply freezing whole fish would (a jump from 0302 to 0303). In addition, the HS is amended periodically most recently in 2007) and when this happens it can be necessary also to amend the rules of origin.

2. Moreover, a CTH rule is all or nothing. It would not be possible to tailor it to suit the needs of individual countries or groups of countries, such as LDCs.

3. Using change of tariff sub-heading (CTSH would have the same advantages and disadvantages, only more so. Moreover in areas such as textiles where CTH would already result in relaxation, CTSH would not allow more operators to benefit from preference.

4. The consultants ADE consider that "Should the EU opt for this alternative, it would be very difficult to stick to uniformity, as the temptation to reintroduce the use of

various levels of aggregation, leading (back) to complexity and capture", the across-the-board rule would be likely to break down in the face of pressure from particular interest groups.

5. A CTH rule would require the retention of special provisions on insufficient operations which can never confer origin, since while CTH sometimes entails radical change, in other cases it does not. The tolerance rule has also always applied to CTH. To dispense with this would be a simplification, but it would also constitute a tightening of the conditions running counter to the aims of the communication. Moreover, it would also be necessary to continue to maintain separate rules in order to decide on the allocation of origin in cumulation.

6. The advantage of a method based on CTH is that in case of a repetitive processing operation where the inputs do not change, the verification of origin can be made once and not for every consignment. On the other hand, producers of more complicated goods need to know the classification of every single material used in production. This requires the engagement of personnel with specialised knowledge.

7. For public administrations, the impact in terms of administrative costs would be similar to what is described for the value added option. The simplification given by the choice of only one methodology will impose a specialisation of the competent authorities for the carrying out of the control procedures.

5.6.4 Option 4 - Adapt the current rules on a product-by-product basis

Impact	Option 4 (Adapt the current rules on a product-by-product basis)
Exporters in beneficiary countries	Relaxation leads to increased exports in some areas.
Importers in the Community	Some imported products more competitive but impact on Community producers should be minimal.
Consumer	Lower prices if the benefit of increased profit margins is passed on
Social effects in exporting countries	More jobs but their nature depends on the scale of transformation
Social effects in the Community	Effect on jobs in the Community likely to be minimal
Beneficiary country administrations	Need to adjust control methods in some cases
Community administrations	No change.
Other beneficiary countries	Some production could be displaced
Environmental effects in the Community	None.
Environmental effects in beneficiary countries	Larger carbon footprint through increased use of transport, additional pollution from more production facilities

Table 8: Summary of economic, social and environmental impacts of option 4

1. An attempt to "clean" the current product by product list to remove its more obvious complexities would be a piece-meal approach. The advantage lies in stability for operators, who would have a familiar legal basis. On the other hand, all the disadvantages of the current system, described earlier, would be perpetuated. Where a change was required to take account of technological evolutions of production processes it would involve a new, time-consuming exercise to change the rules. In such a case the economic operator would find himself exporting without complying with the preferential rules and lose the preferences until the moment when the legal framework was updated.

2. Although there could be some simplification and relaxation, it would not necessarily of itself result in making rules of origin more development-friendly. There are also two, somewhat contradictory considerations. Firstly, the additions which have been made over the years have normally been inserted at the behest of particular interest groups in the Community, and these same interest groups would be likely to react to their removal. On the other hand, some apparent "complications" are not really complications at all, but the result of attempts to clarify the rules where difficulties of interpretation had arisen.

3. However, if in such a scenario the two stages of processing rule for textiles and clothing were changed to a single transformation criterion, the trade creation effect would be likely to be similar to that of a 30% value threshold in option 2B.

4. In any event, such an exercise would be incomplete unless it also addressed other aspects of the rules which have been criticised as being too complex or too difficult to comply with, such as tolerance rules and cumulation.

5. In terms of costs for traders and administrations, there would be unlikely to be much change from the current situation, because the delivery mechanism would be unchanged.

5.7 Revision of rules for the determination of origin – conditions for wholly obtained fisheries products

5.7.1 Option 1 - Status quo

1. The difficulties of interpretation currently experienced, particularly with regard to the ownership requirement, would remain.

5.7.2 Option 2 - Simplify the present conditions

1. The Oceanic/MegaPesca study concludes that from the point of view of both the EU fleet and developing countries, removal of the crew condition "would remove a constraint that was generally seen as benefiting no one". However it did note that there was a disadvantage in some countries (e.g. western Africa) where it could either result in a reduction in employment prospects or put pressure on crews to accept less advantageous terms (or be replaced).

2. The flag is the most visible symbol of nationality, but neither this nor registration is sufficient evidence on its own to indicate a genuine economic link. The ownership of a vessel is the factor most likely to indicate an economic link. Simplifying the conditions for ownership by requiring only that the vessel is at least 50 % owned by nationals of or by companies having their head office in the beneficiary country or a Member State would give the authorities something tangible but nevertheless simple to measure.

5.7.3 Option 3 - Allow cumulation of the conditions

1. It is illogical to allow regional cumulation of origin for materials, on the grounds that it will encourage regional economic integration, while at the same time refusing the possibility for the conditions relating to fishing vessels. The question could be asked how it would be ensured that social or employment norms were respected in respect of crews coming from another country. However, as noted earlier, it is not and never has been the job of rules of origin to guarantee these and nothing would prevent countries applying their laws in the same way they do so today.

5.8 Conditions for cumulation of origin

5.8.1 Option 1 - Status quo

1. The difficulties of interpretation and application experienced currently in GSP regional cumulation would remain.

5.8.2 Option 2 - Allocate origin on the basis of value added

1. Cumulation is a facilitation of the normal rules, to encourage the use of Community materials or of materials originating in the same cumulation zone. However, it also

aims to encourage the development of the country of last working or processing. A genuine working or processing operation should take place there adding real economic value, not mere transhipment or something close to it. While a method of allocation based on value added should offer a genuine measure of what takes place, there are operations which can add significant value without bringing any real economic benefit for the country, and thus do not fulfil the aim of development or regional integration. This is a particular problem in the context of GSP regional cumulation, where different countries in the same group can have different levels of tariff preference (in the SAARC group, there are GSP general arrangement, GSP Plus and EBA countries), and especially for products such as sugar, which are subject to specific Community regimes. In order to guard against this it would be necessary to retain a list of minimal operations which can never confer origin.

2. Although the Scheffer study notes some success in regional cumulation, other anecdotal evidence from many meetings with representatives of beneficiary countries suggests that LDCs are frequently unable to add sufficient value, because of their lack of industrial capacity. Unfortunately, apart from the anecdotal evidence there is no ready way of measuring it from figures available in the Community, because Community rules do not require the use of cumulation to be indicated on the certificate of origin. Nevertheless a lower value threshold than exists today should lead to increased use of regional sourcing.

3. There would not necessarily be a direct effect on Community industry, in the sense that the products would be manufactured anyway, but as a consequence of facilitation of cumulation they might be manufactured in a different country, or using materials of a different origin.

4. However, cumulation cannot be seen in isolation, but only against the background of the normal rules. Cumulation is needed because countries are unable to comply with rules of origin on their own. But in a context where the sufficient processing threshold were very low, it would no longer serve any real purpose, since operators could easily source anywhere. Indeed, it would become just an irrelevant complication. If there were a 30% sufficient processing threshold which allowed an an operator to import and use fabric from anywhere he liked, he would no longer have any reason to use cumulation.

5. This option would represent a radical change for bilateral cumulation, where currently all that is required is that a more than minimal operation takes place in the country concerned. It would be inconceivable to have new rules based on two conditions (value added plus a more than minimal operation) since this would certainly not be a simplification and would be stricter as well. Since it appears necessary to maintain a list of minimal operations irrespective of whether a value threshold is used, this should be kept as the sole condition for bilateral cumulation. It is in the Community's interest to encourage the use of its own materials.

5.8.3 Option 3 - Simplify the present conditions

1. Removing the present value addition condition in regional cumulation would be a simplification. Origin would be conferred on the sole condition that a more than minimal operation took place in the country concerned. This option should certainly stimulate the use of cumulation, provided there remained any incentive to use cumulation following the decision taken on the sufficient processing threshold.

However, given the sensitivity of products such as sugar and the differences in preferences it would have to be examined whether this should still benefit from cumulation, or be excluded, in particular because of the risk of circumvention.

2. Bilateral cumulation is based on the existence of a more than minimal operation alone. Although it might be possible to clarify certain elements in the list of minimal operations, it would not be possible to reduce the condition further. It follows that this option would have no impact as regards bilateral cumulation trade flows.

5.8.4 Option 4 - Extend the scope of cumulation

1. Cumulation should take into account two main factors. Firstly, its usefulness to beneficiary countries: does the cumulation concern countries which are willing and able to cumulate origin with each other? Secondly, is it possible to control it? If it is not, there is an increased risk of fraud from the use of materials which do not in fact originate in the zone.

2. While the Commission is open to considering the merger of regional cumulation groups, if they so request, a merger of regional cumulation groups can succeed only if the countries concerned genuinely want it: integration cannot be forced. At present, one country is known to favour joint ASEAN-SAARC cumulation strongly, but others are ambivalent or even opposed, because they fear increased competition. In addition, even if the countries of these groups do make such a request, there would be little real impact in terms of increased exports to the Community unless there were also appropriate simplification and relaxation of the conditions for cumulation.

3. In order to counter fraud and diversion of trade, cumulation of origin has always been subject to two important conditions: the existence of identical rules of origin in the parties (since otherwise one party might admit the use of materials which another would not, resulting in unequal treatment) and adequate administrative cooperation mechanisms. Regional cumulation is a form of diagonal cumulation, which is possible only because all parties agree to apply the same rules for the purposes of GSP exports (whatever other preferential arrangements they are also involved in) and because there is a network of agreements concerning administrative cooperation. Both each individual group as a whole and its individual members make undertakings to ensure adequate administrative cooperation, not only with the EU, but between themselves. However there is no such link between beneficiary countries outside of these groups and without this, the cumulation would be uncontrollable.

4. In a situation where stringent sufficient working or processing rules apply, allowing cumulation between all GSP countries could be equivalent in effect to a general relaxation of the rules on sufficient working or processing. However the traditional regional focus of GSP would be lost, while as already suggested the attraction of such cumulation is much reduced if the rules on sufficient working or processing are relaxed. At the same time, it must also be borne in mind that identical rules of origin would no longer exist if there were different sufficient processing thresholds for different countries. Consequently the number of countries actually able to cumulate would be much lower in practice than in theory.

5.9 Procedures for management and control of rules of origin

5.9.1 Option 1 - The status quo

1. Although superficially attractive for operators, since the form being issued by the competent authorities seems to convey official approval, it is fact nothing of the sort. All the present difficulties would remain: a paper-based system in a world dominated by electronic procedures (both on the commercial side and in terms of other dealings with customs), burdensome for both exporters and their authorities, costly in many cases, a lack of effective controls and, ultimately a financial burden on the Community taxpayer rather than the person responsible.

5.9.2 Option 2 - Evidence of origin provided directly by registered exporters

1. Permitting statements on origin to be given directly by the exporter would ensure that they were given by the person who is in the best position to know the origin of the goods. However, such a system could work only if the rules were easy to understand.

2. The authorities for their part would be able to concentrate on carrying out controls. However, in order to carry out such controls effectively, they need to have information about the operators with whom they are dealing. Requiring exporters (save for a limited number of very small exporters, where it would be too burdensome a requirement) to register with the authorities as a condition of being able to export under the arrangements would ensure that they had certain basic knowledge about operators (names, addresses, activities), which would enable them to target controls on the basis of risk analysis techniques. While it has been objected that a registration requirement would always be burdensome on exporters, it would be a once-off requirement, after which operators could make statements on origin without further recourse to the authorities. Moreover, beneficiary countries would not necessarily have to set up new systems: in many, operators are already required to register with the authorities for other purposes. In such cases, there is no reason why the authorities could not graft the requirement for registration in order to be able to export under preferential trade arrangements onto existing structures, provided this allowed all the information needed for rules of origin purposes to be obtained.

3. For importers, the consequence of having to rely solely on statements of origin given by the exporter, which had not been checked by the authorities of the beneficiary country, would be that they would no longer be able to blame an error by those authorities if it subsequently transpired that the statement was wrong or should not have been made. Consequently, they would have to pay the duty due themselves.

4. ADE, Scheffer and Oceanic/MegaPesca all draw attention to opposition on the part of Community importers to having statements on origin given directly by registered exporters. They fear becoming liable for mistakes in a way they perceive they are not at the moment because of the "good faith" provisions. ADE consider[29] (that "If

[29] Executive summary, p. x

it does not discourage the use of preferences, at least it may reduce the pass-through of margins to suppliers, again defeating the objective of the reform.".

5. However, changing to a system based on statements on origin by registered exporters would not remove all protection for importers. The authorities would retain a role and to that extent also the concept of "active errors" by the authorities, albeit the provision ought to be used much less. In particular, the provisions on special situations in Article 239 of the Community Customs Code would remain. On the other hand the responsibility of exporters for the statements they make as well as the responsibility of importers to exercise due care – both of which already exist today, even if somewhat obscured – would be clearly established. It is also pointed out that this option envisages a system of prior registration, not prior authorisation by the authorities – in other words, they would register but not carry out prior checks. Importers should still take appropriate steps to guard against the possibility of a statement of origin turning out to be incorrect.

6. Statements on origin, under this or either of the two following options, could be given electronically. This would bring origin certification into line with the modern commercial (and customs) world.

7. For such a system to work, all parties would need to have confidence in the system, and in particular operators would at least need the security of knowing that their suppliers were indeed registered with the competent authorities. For this purpose, a computerised tool would be needed, so that the authorities in the beneficiary countries could keep the list of registered operators up to date and importers could check that their suppliers were registered before declaring the goods for release for free circulation.

8. The computerised tool should be as easy as possible for operators to use and for the customs authorities to manage. It would also have to take into account some of the structural problems of developing countries. Therefore, the Commission considers that third countries requiring access to the data-base should be considered as having nothing more as a computer infrastructure than access to the internet through a well-known browser supporting SSL certificates. Moreover, the proposed user interface should allow for the widest possible browser base. Further information on the system envisaged by the Commission (to be called REX), its features and costs are given in Annex [11].

9. Such a system would be a major simplification for exporters, since they would no longer have to go to the authorities to get a certificate of origin stamped for every single consignment. Instead, there would be a once-off registration procedure. In some countries, there is a (high) charge to issue certificates of origin. Even if those authorities imposed a registration fee, regular exporters should still see a substantial reduction in their costs.

10. However, occasional exporters or those exporting very low value consignments could lose out and it would appear essential to exempt them from the registration requirement.

11. In terms of resistance to evasion or fraud, no system can ever be completely fraud-proof. What can be sought is a system that is as resistant to fraud as possible. The introduction of this option would make appropriate use of computer technology and risk analysis to identify operators and target those presenting the greatest risk.

12. However, the implementation of such a system, with the investment in informatics which it implies, both in the Community and in third countries, could not take place immediately. It seems likely, given the need to set up the system and educate users (there would need to be training actions for administrations, probably on a local or regional level, though as noted in Annex 11 these are not costed yet), that it could not be implemented until 2011, whereas the new rules for the determination of origin, which are the key to increasing use of the preferences on offer, need to be introduced much sooner. It would thus be necessary to continue to apply the present procedural rules temporarily. It would also be preferable, in order to avoid confusion for operators, for all beneficiary countries to begin using the system at the same time. However, if need be a staged implementation could be considered, according to the technical capabilities of beneficiary countries.

5.9.3 Option 3 - Introduce certification by approved exporters only

1. This is a possibility which already exists in GSP, but only for Community exporters exporting for the purpose of bilateral cumulation.

2. Approval offers certain guarantees to importers, because the authorities of the exporting country will have carried out certain checks before approving an operator and will also have imposed certain conditions. However, no system can ever offer absolute guarantees. There is a danger that importers would rely on the statements on origin because the exporters had been approved, without making adequate checks of their own and, in the event of a customs debt subsequently becoming due, claim that they should not have to pay because the authorities made an error in granting approval. Thus the objective of re-balancing responsibilities and reducing the number of "good faith" claims would not be met.

3. Although exporters would not encounter any delays at the time of export, the approval procedure before exports could begin could be time-consuming and it would undoubtedly be more burdensome for both exporters and administrations, the more so for exporters if administrations chose to pass on the cost.

5.9.4 Option 4 - Introduce certification by the exporter only (no registration or approval)

1. This is the "purest" form of exporter certification. There would be no barriers of red tape for exporters as far as their origin declarations were concerned. Nor would there be any uncertainty about where responsibility lay. As with other forms of direct certification by exporters, it would be essential for the rules of substance to be as easy as possible to understand, in order to reduce the risk of errors occurring.

2. Such a system would have serious disadvantages from the viewpoint of controls. Anyone could issue a statement on origin and the authorities – who would remain responsible for subsequent verifications - would have no prior knowledge of the firms they were supposed to control. It is also possible, as has been suggested for other options, that some importers may refrain from using preference if they fear becoming liable. However they could always make reasonable checks with their suppliers before purchasing, just as they would with regard to other aspects of their transactions, and they would have to balance such a decision against the commercial risk of changing supplier or putting up prices.

3. If controls were to be carried out on the basis of questionnaires addressed directly to exporters by the authorities in the Community, this would certainly reduce the quality of post-clearance checks, since there would be no opportunity for the authorities to cross-question operators at the time of the control.

5.10 Instruments to ensure compliance by the authorities of beneficiary countries with their obligations

5.10.1 Option 1 - Status quo

1. In the absence of regular information, by the time evidence justifying a warning notice or temporary withdrawal of preferences is found, much damage has already been done.

2. The Commission's guide for users on GSP rules of origin and and its general web pages on rules of origin have been successful initiatives. However, in order to be fruitful technical assistance needs to be timely and well targeted, as well as properly resourced. At present, it is provided reactively not proactively.

3. If the status quo remained, problems would continue to be identified too late.

5.10.2 Option 2 - Establish a programme to monitor the arrangements and provide assistance and/or impose sanctions or safeguards where required

1. Even if nothing changed, it is clear that all parties need to know whether the authorities are doing their job properly.

2. The provisions in the GSP regulation on the temporary withdrawal of preferences cannot be implemented unless the Community knows what is really happening. It can only know this if it actually checks that beneficiary countries can comply with their obligations.

3. If operators learn that a country is being monitored, they may conclude that there is something wrong and that they should avoid doing business with it. However, monitoring should be routine and it should not be viewed as a prior supposition of failure. Nor should it be seen as a weapon or a punishment. Rather, it is a tool to help the arrangements work better and actually for the benefit of operators. If problems are identified early, they can be solved before they take on more serious proportions. On the other hand, if serious problems are identified, a warning notice can be published or appropriate sanctions can be applied. For these reasons, monitoring cannot exist in isolation, but needs to be backed up by appropriate training and technical assistance.

4. The establishment of a monitoring system – which does not require a change in the law – as well as training and technical assistance has implications in terms of resources for the Commission.

6. COMPARING THE OPTIONS

6.1 Revision of rules for the determination of origin - sufficient processing of goods which are not wholly obtained

1. The following table 9 summarises the pros and cons of the various options.

Table 9 - Comparison of options: Revision of rules for the determination of origin – sufficient processing of goods which are not wholly obtained

Option	+	-	Comments
1. *Status quo*	- Rules are adapted to needs of individual sectors - Familiarity for operators	- Old, no development aim - Complex: rules vary from product to product - Inequality: similar products treated differently - Process of several steps (minimal operations, list rules, tolerance rule and separate calculation for cumulation) - New products require new rules. - repeated requests for interpretation or amendments.	
2. *Across-the-board criterion, based on value added*	- Simple concept - Could also be used for allocating origin in cumulation - transparent - flexible - Operators are familiar with costs, already use them for commercial and customs purposes - Authorities have only one rule to check - Applicable to all products, including new ones - Flexible: degree of relaxation easily and transparently changed by raising or lowering the threshold. Option B (the most liberal) would result in limited trade creation without major impact in the Community.	- Susceptibility to exchange rate fluctuations - Adjustments needed for certain sensitive sectors - Customs officers say hardest method to control - Need to maintain list of insufficient working or processing operations - Problem of transfer prices applied between related companies	

Option	+	-	Comments
3. *Across-the-board criterion, based on a change of HS tariff heading or change of tariff sub-heading*	- Simple concept - Goods must be classified for tariff purposes anyway	- HS not designed for origin purposes - Rules of origin may need to be changed whenever HS changes - Need for separate rules on cumulation - Need to maintain list of minimal operations - Inflexible - "Take it or leave it" – additional relaxation not possible - Old – the basis for origin rules many years ago, but required many adaptations	
4. *Adapt the current rules on a product-by-product basis*	- Specific products can be targeted - Can be adapted for development goals - Familiarity for operators - stable results	- Scope for genuine simplification not always evident - Piece-meal approach, fails to address other complications such as tolerances - A time-consuming exercise	

2. The present GSP rules of origin are complex and difficult to apply for traders and administrations alike. This was clear from the responses received to the 2003 Green Paper. In addition, both ADE and Scheffer concluded that rules of origin should be reformed.

3. The current rules are familiar to operators and administrations and they are not all complex. However, if one considers the rules as a whole the complexities of applying them are more evident, and their continuation would only perpetuate the many difficulties of interpretation and application which exist.

4. The present rules were never designed with development in mind. Insofar as it could be argued that they could nevertheless encourage development, because countries would have to develop their industries in order to comply with them, this has failed. For example, while larger countries like India can comply with the two stages of processing rule for textiles, by and large smaller countries have simply been unable to develop the necessary backward linkage. Bangladesh has succeeded to some extent, but still cannot produce enough fabric domestically to meet demand. The derogations granted under GSP were supposed to allow the countries concerned time to develop their industries to the point where they could comply with the normal rules, but in practice this has never happened and the derogations have just been continually prolonged. It is hard to see how the present rules could encourage development in the future, when they have failed to do so before.

5. "Cleaning" the current rules would be an exercise fraught with difficulties. It could offer piece-meal opportunities for relaxing the conditions by targeting specific rules in sensitive sectors, for example textiles and clothing. However in terms of overall simplification it would effectively be tinkering at the edges when the whole edifice is in need of attention. Nor are the opportunities for simplification always evident. It would be wrong to assume that any relaxation is necessarily good: an apparently evident relaxation might not be beneficial, if it only encouraged over-reliance on a dominant supplier instead of local or regional sourcing. In sum, this method would offer some opportunity to promote development (although it would not be possible do differentiate between GSP general arrangement and EBA countries) but its impact in terms of simplification would be limited, and it would be unlikely to satisfy exporters, importers or administrations on this count.

6. This leaves the two "radical" approaches, i.e. a value-added rule or a CTH rule. These across-the-board approaches would sweep away the current structures. They would also have the advantage of using familiar concepts, even for those operators who never have to apply them at present.

7. A single CTH rule would certainly be a major simplification and, being based on tariff classification, it has the merit of being familiar to operators and administrations. Tariff classification is a necessary customs tool which must be used anyway when goods are imported and exported. However, the tariff was never conceived for origin purposes and it would be an all or nothing approach, which would not permit any differentiation between LDCs and other developing countries. It may also be seen as a step back into the past, rather than a step into the future. Many years ago, CTH was the basic rule, but more and more modifications or

alternatives had to be introduced in order to take account of particular situations. It has to be wondered whether this would not happen again.

8. As regards value added, no businessman can fail to be aware of his costs. Although it has been objected that value-based rules are the hardest for the authorities to control, administrations are nevertheless used to dealing with costs and value, in particular to assess duties and taxes. Moreover, much depends on how the rule is defined. A method based on a comparison between the ex-works price and the value of the non-originating materials used is conceptually straightforward. In addition, even with more than one threshold, the simplifying factor of there being a single method should not be under-estimated.

9. In order to be able to help promote development, rules must not only be simple – because operators will refrain from using the preference if they cannot understand them or the procedures are too complex – but also flexible, so that a differentiation can be made between countries or groups of countries. The only across-the-board method that would allow such differentiation is one based on value added, because the degree of relaxation (or protection) afforded could be easily changed by lowering or raising the threshold.

10. Changing to a single value-added method would not of itself promote development. This depends on the level at which the threshold(s) is (are) set. It is logical to begin using as a reference a threshold that would be broadly equivalent in effect to the current rules. This needs to be considered very carefully, because a low threshold might provide a short-term boost, but could be bad for a country's development in the longer term, if it removed all incentive to source materials (raw or intermediate products) regionally or locally. A single threshold covering all products would undoubtedly be best in terms of pure simplicity, but in practice the different and specific features of various sectors militate against it.

11. Concerning the impact of rules of origin on Community industry, it should not be assumed that because rules of origin have historically played a protective role, leaving them unchanged will be the most appropriate solution for it, because it would maintain that protection. China (a GSP beneficiary, but excluded from preference for many sectors, including textiles and clothing), as well as Korea (graduated from GSP in 1997) and Taiwan (never a GSP beneficiary), have developed their economies not because of rules of origin, but in spite of them. They are all able successfully to enter the EU market. There is no reason to suppose that this trend would not continue. Leaving the rules unchanged would however be likely to continue to work against smaller developing countries without disturbing at all the largest suppliers, whereas if the rules were changed, and in particular relaxed in appropriate cases, some products might be produced in LDCs or other vulnerable countries instead of in their larger competitors.

12. The evidence produced by the studies suggests that relaxing rules of origin would produce a growth in exports from affected countries, but it would be a mitigated growth and the effect on Community industry would be likely to be very limited**.** The conclusions of the studies seem to be confirmed by the trade creation exercise carried out for the two different value added threshold options.

13. As regards administrative costs, there must always be an appropriate cost-benefit balance between the rules for the determination of origin and the procedures

necessary for their control. Costs for operators are high and should be reduced, but it cannot be the aim of any reform to reduce administrations' costs, but only to ensure that they are able to carry out their management and control responsibilities effectively. In the long term, the introduction of clearer, simpler rules and in particular a single methodology as far as possible should yield savings for operators and administrations alike. There will also be major savings for operators in terms of both time and money if this is coupled with changes on the procedural side allowing operators to make out statements of origin themselves once registered, instead of having to go to the authorities for every single export to get a certificate stamped.

14. If operators could more easily comply with the rules legitimately, this should reduce the number of cases of fraud. In any event, whether the rules are relaxed or whether they remain as they are, the need for control procedures to be robust is the same.

15. ***Conclusion and recommendation: There is evidence to show that preferences are under-used in some sectors and that part of the reason for this is rules of origin which are too complicated and/or too restrictive. Rules of origin therefore need to be changed. However, taking into consideration the current level of liberalisation, for the majority of sectors changing rules of origin will have no impact at all and to this extent rules of origin have to be considered as being neutral. It is shown that even relaxed rule would not create major negative impacts for operators in the Community.***

16. ***The only method which could deliver both formal simplification and greater flexibility to promote development is one based on value-added. To meet the greater development needs of LDCs, there could be a lower threshold for products originating in them. For certain sensitive products in the agricultural sector, additional conditions are required in order to support development and avoid circumvention. However, the value added method would seem unsuited to the fisheries sector. The value thresholds and additional (or for fisheries products alternative) conditions need to be supported by a list of minimal operations which can never confer origin, to that the operations which take place are genuine and economically justified and to avoid mere transhipment.***

6.2 Revision of rules for the determination of origin – conditions for wholly obtained fisheries products

1. It is essential to ensure that there is a real link between the fishing vessel and country of export. However, the present rules are complex and the crewing requirement is mainly seen as benefiting no one. Ownership best reflects a real economic link between vessel and country, but the present rule has given rise to particularly difficult questions of interpretation, so it should be simplified.

2. It is illogical – and against the objective of regional cumulation - to allow cumulation of materials while simultaneously banning cumulation of the conditions relating to fishing vessels.

3. A clear distinction must be made between rules of origin, which exist solely to determine whether a product may be considered as originating or not, and other rules relating to fisheries, which rules of origin do not affect in any way. Simplifying these rules as envisaged would have no impact on policies relating to conservation of fish stocks or on employment conditions.

4. ***Conclusion and recommendation: The present rules in this area should be simplified by deleting the crew requirement and by simplifying the conditions relating to ownership where a company is involved. It should also be allowed to cumulate the conditions between countries of the same group in the framework of GSP regional cumulation of origin.***

6.3 Conditions for cumulation of origin

1. The following Table 10 summarises the various options.

Table 10 - Comparison of options: Conditions for cumulation of origin

Option	+	-	Comments
1. *Status quo*	- Rules are adapted to needs of individual sectors - Familiarity for operators	- Old, no development aim - Complex: rules vary from product to product - Inequality: similar products treated differently - Process of several steps (minimal operations, list rules, tolerance rule and separate calculation for cumulation) - New products require new rules. - repeated requests for interpretation or amendments.	
2. *Allocate origin on the basis of value added alone*	- Same method as for determining sufficient working or processing - transparent - flexible - Operators are familiar with costs, already use them for commercial and customs purposes - Authorities have only one rule to check	- Susceptibility to exchange rate fluctuations - Customs officers say hardest method to control - May lead to circumvention, through countries being used a staging posts for transhipment, with no real economic benefit. - major change if applied to bilateral Cumulation	
3. *Simplify the present conditions*	- Removing one of the conditions for GSP regional cumulation would both simplify and relax	- Difficulties in interpretation of "minimal operations" would remain - May lead to circumvention	
4. *Extend the scope of Cumulation*	- More countries able to cumulate	- Cumulation supports integration, cannot create it - Some beneficiary countries oppose more cumulation - If "global" cumulation, tantamount to a general relaxation of rules – no targeting of specific groups countries is possible	

2. Cumulation is an element of rules of origin that cannot be disregarded. However, it is a facilitation meant to encourage economic cooperation, not the basic rule. In examining rules of origin, it is therefore important to look first at the basic rules (wholly obtained and sufficient working or processing) before moving to consider cumulation.

3. Bilateral cumulation is currently based on there being a more than minimal operation in the partner country concerned. To apply a value added rule in conjunction with a list of minimal operations would complicate rather than simplify and could make the rule harder to comply with as well. Insofar as it is decided to maintain a list of minimal operations it would seem appropriate to continue to use this for the purpose of allocating origin in bilateral cumulation.

4. The evidence shows that as regards GSP regional cumulation, the rules do not work. This is partly because the members of the groups are also competitors, and partly because the conditions are too strict. The allocation of origin in regional cumulation is particularly important where the tariff preference on offer differs from country to country. It would be possible to simplify the conditions for cumulation in a "cleaning" of the current rules, but it would still involve having a special rule for the purpose. Currently, the calculation of value added in regional cumulation is different to the calculation of value in the existing rules where such a rule applies. The option of the value-added method described above would however allow the use of the same method for both determining what is sufficient processing and allocating origin within regional cumulation. The cumulation threshold would need to be set at a level which would encourage cumulation within the zone, while also ensuring that a real economic activity takes place. However it has already been suggested that for other purposes it would be necessary to retain a list of minimal operations. If this rule is maintained, then it could be asked whether it would be appropriate to remove the value added condition completely and base the allocation solely on the existence of a more than minimal operation.

5. ***Conclusion and recommendation: Cumulation is intended to encourage economic cooperation within the zone. In order to do so, it needs to be based on rules which both offer a sufficient incentive to source within the zone rather than outside, and at the same time reflect a genuine economic activity in the exporting country. In the event of a stringent rule for sufficient working or processing value added offers a measure of such activity but to guard against circumvention a list of minimal working or processing operations would be required. On the other hand, if the sufficient working or processing rule is very low, then the cumulation threshold would have to be so low as to be pointless but at the same time be a complication. In this case the requirement to carry out a more than minimal working or processing operation should suffice and this is to be preferred.***

6. ***In the case of bilateral cumulation the origin is currently allocated solely on the basis of a more than minimal operation. The simplest solution would be to maintain the status quo.***

6.4 Procedures for management and control of rules of origin

1. The following table 11 summarises the pros and cons of the various options.

Table 11 - Comparison of options: Procedures for management and control of rules of origin

Option	+	-	Comments
1. *Status quo*	- Importers trust official stamp	- Burdensome for exporters - Recurrent problems with uncommunicated stamps - Authorities in third countries unable to control properly at export - False sense of security for importers - Burden on taxpayer from non-recovery decisions	
2. *Evidence of origin provided by registered exporters*	- Simple for exporters - Exporters in best position to know origin - Authorities know who they are dealing with - Once-off registration procedure - Registration a "light" procedure - Clear division of responsibilities - Facilitates risk analysis	- Importers fear liability for debt - Poorest countries able to set up computerised system?	Many countries already have registration or approval systems
3. *Introduce certification by approved exporters only*	- Simple for exporters - Exporters in best position to know origin - Authorities know who they are dealing with - Once-off approval procedure - Facilitates risk analysis	- Importers fear liability for debt - Poorest countries able to set up computerised system? - Prior approval is burdensome	Importers are already liable for debt in principle Many countries already have registration or approval systems Transitional period and appropriate information and support would be needed to help all parties to prepare
4. *Introduce certification by the exporter only*	- Simple for exporters - Exporters in best position to know origin	- Importers fear liability for debt - Authorities do not know who they are dealing with - Hard to apply risk analysis	

2. In terms of resistance to fraud, the need for robust procedural rules is the same, whether the rules of substance are changed or not. The present procedural rules suffer from several weaknesses, notably slow, paper-based procedures and a system of control at export whose application can at best be described as patchy and fails to offer the guarantees it should.

3. There is no doubt that the present rules on proof of origin are extremely burdensome for exporters. For virtually every single consignment, they must get proof of origin (certificate of origin Form A) stamped by the competent authorities of their country. Not only can this be time-consuming, but it is known that in many countries it can also be expensive, for the authorities concerned charge fees.

4. Many importers feel they can rely on these proofs of origin because they have been issued by the competent authorities. They do not make any further checks, overlooking the fact that under customs rules both they and their suppliers are in principle liable for the accuracy of the origin declarations they make. As a result of the jurisprudence of the Court of Justice and changes in Community law, this has led to an increase in the number of cases where importers have been able to claim that they should not pay duty found to be due as a result of checks, because there was an error by the authorities and they themselves had acted in "good faith". This means losses to the Community budget and, by extension, the Community taxpayer.

5. The authorities of many beneficiary countries are unable and/or unwilling to carry out meaningful checks at the time of export. Stamping the forms is not genuine control, but a rubber-stamping exercise. Therefore importers should not rely just on them, and the competent authorities in the Community cannot do so either, for there have been too many cases where post-clearance verification has revealed the proof of origin to be incorrect. Moreover, certificate of origin Form A can only be on paper, since the rules do not permit the use of electronic forms, even though some countries would prefer to use them. The use of electronic means for providing evidence of origin would be in line with both commercial and administrative trends and speed up and facilitate the carrying out of checks.

6. The Commission and the Member States – as well as the operators who face the delays and financial consequences – face continual problems because beneficiary countries fail to communicate new stamps.

7. The authorities of beneficiary countries are obliged to make post-clearance checks, both on their own initiative and at the request of the authorities of the Member States. It would appear that they could devote more resources to this task if they did not have to concentrate on stamping papers at export.

8. Since entitlement to preferential tariff treatment depends on origin, it is impossible simply to do away with evidence of origin. The alternative to proofs of origin stamped by the authorities is a system where the evidence is given directly by the exporter. This has the advantage that the origin declaration would be made by the person in the best position to know how the products were made. This is in principle the case already, but it is somewhat obscured by the fact that the authorities then have to stamp the form. However, in order for such a system to work, the rules of origin need to be easy to understand and apply, or operators may decide it is not worthwhile using the preference.

9. While there would be no role for the authorities at export in such a system, it would be inappropriate to leave them out of the system completely. There do need to be controls, to ensure that the rules are being applied properly and that preference claims are genuine. The authorities of a country are should know the companies they are dealing with. If controls were based solely on a questionnaire by the authorities of the importing country, that advantage would be lost. However, in order to be effective, controls should be properly targeted, and not purely at random. For this reason, the authorities should apply risk analysis techniques, as used in the Community and by administrations around the world. For this purpose, it would be appropriate to require exporters to be registered with the competent authorities in order to export.

10. A system where operators certify origin themselves is not entirely new, since the existing rules already allow the use of invoice declarations in certain low value cases. Insofar as these have worked and been controllable, there is no reason not to extend the principle more generally.

11. As far as Community importers are concerned, a system such as this would make their responsibility clear, and the consultants suggest they fear becoming liable for customs debts they do not have to pay at present. However, importers certainly take steps to protect their interests in other aspects of their transactions, both for commercial reasons and because of official requirements. There is no reason why they should not also take appropriate steps to make checks with their suppliers about origin matters.

12. However, it would be unfair to make what importers perceive as new impositions on them without offering them in return some guarantees about the system. A computerised network containing a list of registered operators would enable importers to check that their suppliers were registered, while further measures could be taken as discussed below.

13. The setting up of a computerised system and the establishment of lists of registered exporters date would entail a certain investment for administrations. It would take some time to set up but would offer clear advantages once it was established.

14. Moving to such a system would be a major simplification for exporters, since they would no longer have to go to the authorities to get a certificate of origin stamped for every single consignment (bearing in mind also that in some countries, there is a charge to issue certificates of origin, which can be quite high). Instead, there would be a once-off registration procedure.

15. ***Conclusion and recommendation: No system can ever be completely fraud-proof. All that can be attained is a system that is as resistant to fraud as possible. What offers the best opportunity for this is a system where the rules to be applied are clear and simple, evidence of origin is given by the person in the best position to know, the respective roles of all parties are clear and well-defined and the authorities are able to act effectively and quickly, making appropriate use of modern informatic technology and risk-analysis techniques. The introduction of statements on origin given directly by registered exporters with the contemporaneous introduction of a comprehensive data-base system, leaving the authorities free to concentrate on controls, is the most suitable way to achieve this. However, it could not be implemented immediately, but would require some***

years to allow administrations in the Community and in beneficiary countries to put the necessary technology in place. In the meantime, the present rules would have to remain in place, but their proper application could be supported by the programme of monitoring actions envisaged below.

6.5 Instruments to ensure compliance by the authorities of beneficiary countries with their obligations

1. The rules of origin of preferential trade arrangements rely on mutual trust and cooperation between the authorities of the parties. At present the Community provides information through its web-site on rules of origin as well as its guide for users on GSP rules of origin and such initiatives have been received favourably. It also carries out some monitoring actions and provides some technical assistance, but it is done on an individual basis and is reactive, not proactive.

2. In the GSP regulation there are provisions allowing the temporary withdrawal of tariff preferences if the authorities of beneficiary countries are not correctly carrying out their duties in controlling rules of origin. The Commission may also, as it has indeed done on a number of occasions in the past, publish warning notices to importers, when it has reason to believe that proofs of origin are being incorrectly issued. However, in order to apply such measures it is necessary to know for certain what is actually happening. Mutual trust is a good concept, but trust needs to have a firm foundation.

3. The establishment of a periodic monitoring system would give administrations and operators greater trust in the operation of the system by partner countries. It should also allow problems to be identified early and appropriate corrective action to be taken through targeted training or technical assistance. It would require extra staff resources but there would be compensation in terms of better controls by the authorities and more correct application of the rules by operators.

4. ***Conclusion and recommendation: all parties need to know whether the authorities are doing their job properly. There needs to be a systematic, permanent programme of monitoring actions allowing the targeted selection of countries. No change in the law is required for this but it would be more transparent to include it. This should be backed up by information, training and technical assistance where required, as well as the application of safeguards or sanctions where this is necessary.***

6.6 Overall conclusion

1. The three areas covered by the communication and by this impact assessment are closely linked. Simplification and appropriate relaxation of the rules for determining origin need to be supported by adequate management and control procedures, all parties need to know exactly what is required of them and it is necessary for there to be confidence in administrations. Conversely, efficient management and control is facilitated by rules which are easy to understand and apply. The changes to the three areas all need to be made, even if they cannot start to apply at the same time. To propose procedural changes on their own, without also offering simpler and more relaxed rules on the substance, would be ill perceived by partner countries.

7. MONITORING THE OPTIONS

7.1 Revision of rules for the determination of origin

1. The prime objective is to contribute to promoting the sustainable economic development of beneficiary countries, particularly LDCs and other vulnerable countries, through appropriate (i.e. simple and, where needed, relaxed) rules of origin. This will be seen especially through an increase in the utilisation rates.

2. Changes in the volume of preferential imports from beneficiary countries and the preference utilisation rate can be measured though Community trade statistics. It will need to be seen, first, whether there is an increase after new rules enter into force, and then whether this is sustained over a period of several years.

3. The objective of a reduction in the number of different conditions to be complied with can be measured immediately through a reading of the specific proposals made by the Commission. The best judges of whether changes to the rules really are simpler will be the arrangements' users – the operators who wish to use the preferences and the administrations who must control them.

4. The Commission could review the operation of the new rules after three years and if need be propose further adjustments to the rules in order to achieve the objectives.

7.2 Conditions for cumulation of origin

1. The objective being to increase where it is low the proportion of preferential exports produced through cumulation, this can be measured through information obtained from beneficiary countries. Community statistics currently identify the country of origin but not whether cumulation was applied to obtain the origin. It would be necessary to require exporters to indicate it in future.

7.3 Procedures for management and control of rules of origin

1. The objective is an increase in exports under GSP without a concomitant increase in fraud, together with fewer requests for interpretation after new rules are bedded in and a reduction in costs for exporters.

2. The incidence of fraud can be measured through the number and size of cases which OLAF and national fraud services have to deal with.

3. Statistics on the handling of verification requests will be collected in the framework of monitoring actions and will show whether these are handled more quickly or not.

4. Applying one methodology and removing the need to go to the authorities for each every consignment should certainly reduce costs for exporters. Registration, being a once-off exercise, should be considerably less burdensome. This would be mainly reflected in export volumes. This could also be reflected in prices, but on the other hand exporters might try to take more profit. It is therefore impossible to tell anything about this from prices, which are in any event subject to such a wide variety of competing factors. On the other hand, a survey could be carried out after a certain period of operation to find out exporters' perceptions of changes in their costs.

7.4 Instruments to ensure compliance by the authorities of beneficiary countries with their obligations

1. The results of monitoring actions can be continuously evaluated. Each one will show whether or not the authorities of partner countries can comply with their obligations.

2. The results of monitoring actions may also show whether any preventive or corrective action (training, technical assistance) is needed or whether any previously undertaken has been successful or not. A temporary increase in the need for training or technical assistance should not be taken as a sign that implementation of the new rules is problematic. In the short term, it is inevitable that partner countries will need adequate training in order to implement the new rules. But also it is intended that monitoring should allow problems to be identified – and resolved – early, before serious damage is done ("prevention is better than cure" principle).