

## Executive Summary

### Rules of Origin Regimes and Impact on Business in the APEC Region

This report offers a detailed analysis of Rules of Origin (RoO) regimes within the Free Trade Agreements (FTAs) in the APEC region. It builds on and complements research comparing and contrasting APEC region FTAs prepared by the University of Southern California Marshall School of Business in 2006.

Though intended to facilitate free trade, promote local investment, and protect sensitive local industries from “unfair” competition, there is increasing evidence that preferential RoO regimes are overly complex and imposes unintended consequences for business. The divergence of RoO provisions across FTAs, their restrictiveness, the complexity of the rules, and requirements for compliance have increased business transaction costs, and limited their use. Over 60% of APEC region business executives interviewed stated that RoO-related issues occurred frequently. These concerns ranged from the challenges of interpreting and complying with RoO provisions to strategic investments considerations of deciding whether or not to even invest in an economy.

Our research included the following:

- A comprehensive line by line analysis of Rules of Origin regimes within 25 Free Trade Agreements across the APEC Region.
- Creating a comparative catalog of Rules of Origin (available on CD)
- Indepth interviews with over 80 business executives knowledgeable about ROO in 13 economies and in 10 different industries.
- Developing detailed case studies of the impact of RoO on the Automotive and Food Industries

## Key Findings

***Rules of origin are unnecessarily difficult to understand and interpret. Significant variances exist among rules of origin provisions across APEC region.*** These differences coupled with the lack of a standard for interpreting HS codes make rules of origin certification challenging and costly for business. Companies, in particular SMEs, are forfeiting the benefits of free trade preferences, and paying the tariff, because the origination process is too burdensome.

***Applying rules of origin is a non-trivial expense for businesses.*** Companies that apply rules of origin must invest in and develop significant capabilities to do so. Businesses must make significant investments in IT infrastructure and human capital just to prove origination. Additional expenses are incurred by companies that must assist their suppliers in the product certification effort (e.g., record keeping and reporting).

***Rules of origin complexity (and costs) are compounded when companies operate across multiple Free Trade Agreements or within overlapping agreements.*** No two rules of origin regimes are alike within the region. These differences across free trade agreements make it all but impossible for businesses to realize synergies from IT systems, administrative procedures, and subject matter expertise.

## Implications for the APEC Region

***Rules of origin are being used as a barrier to entry in some industries.*** RoO complexity and compliance hurdles demand real resources and organizational capabilities. Typically this means it is large companies with the scale and resources who capture the intended benefits of free trade agreements. FTAs may have unintentionally created a competitive advantage for the big company to use to further out compete the small.

***Complex rules of origin can increase company costs to a point where they can not justify the expense of pursuing the intended benefits of FTAs.*** Companies often do not apply rules of origin because there is little to no benefit from doing so. In many cases, companies (both large and small) can not justify the cost associated with meeting rules of origin requirements. As a result, the benefits of Free Trade Agreements within the APEC region are not used.

***The proliferation of Free Trade Agreements, and the increasing global expansion of business supply chains, connect in a way that makes standardization and harmonization of rules of origin regimes a priority.*** Businesses will seek economic solutions which maximize their short and long-term profits regardless of the intended goals of FTAs. Where they do overlap economic growth results. Where they do not, numerous unintended consequences, for both business and economies, result.

### ... for Trade Officials

***Expand the proposed model measures to include the remaining most commonly used measures.*** The proposed standards need to be more consistent with the current FTAs across APEC to truly be a "model" standard.

***Include the commonly used measures and keep them consistent with the proposed model measures standard in free trade agreements.*** This will ensure that all future free trade agreements will be consistent with all other agreements in the APEC region.

***Provide additional training to customs officials and SMEs on rules of origin administration and HS code interpretation as needed.*** Certification issues will persist across the region as long as product certification is open to interpretation. Small and medium-sized businesses and organizations either lack the knowledge, experience, and/or size to administer the process effectively.

### ... for Business Executives

***Provide suppliers with free advice and expertise on product certification and documentation.*** Suppliers bear most of the costs and little of the benefit of the origination process. Educating suppliers on how to certify their products can help improve the efficiency of the certification process, reduce disputes, and lower additional costs in the long-run.

***Make rules of origin optimization someone's job.*** As companies grow, global sourcing and sales will become more and more important. Companies must start developing subject matter expertise now in order to stay competitive in the APEC region.