Trade Developments

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Rules of Origin

Frequently Asked Questions

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What are rules of origin?

Rules of origin are criteria used to determine the "nationality" of a product. A product's raw materials or components might come from a number of countries, but customs officials must determine the product's origin to decide how to treat it, including what tariff to charge, as the product enters their jurisdiction.

Why do we need to know the origin of a product?

Some products are eligible for favorable treatment based on their origin. Favorable treatment usually consists of no tariff or a lower tariff than would normally apply. Favorable treatment often stems from benefits that industrialized countries offer to developing countries under preferential trade arrangements. Most industrialized countries maintain a Generalized System of Preferences (GSP) to benefit developing country exporters. The United States extends additional benefits under the Caribbean Basin Initiative (CBI), the Andean Trade Promotion and Drug Eradication Act (ATPDEA), and the African Growth and Opportunity Act (AGOA). The European Union has offered special benefits to former colonies in Africa, the Caribbean, and the Pacific under its Lomé Convention and in 2001 implemented its Everything But Arms program for least-developed countries. Favorable treatment is also a feature of free trade agreements (FTAs). The United States has FTAs with Israel, Canada and Mexico, Jordan, and prospectively with Chile and Singapore. The European Union has FTAs with its associated members and a number of developing countries. Some developing countries have concluded FTAs among themselves.

More generally customs officials also use rules to determine origin for other policies that discriminate among exporting countries. For example, quotas often regulate trade flows, and specific quota amounts are frequently allocated to individual countries. Goods can incur antidumping actions or countervailing duties (charged to counter export subsidies) depending on their origin. Regulations on government procurement often specify how to treat goods based on their country of origin. Determinations of country of origin are also important for trade statistics and the "made in" marks and labels attached to consumer goods.

How do transshipments of goods affect origin determinations?

Recognizing that goods often move from one country through another before reaching their final destination, international trade agreements prohibit an importing country from discriminating against a product of one country simply because the product was shipped through another. They do not, however, allow exporters to circumvent preferential trade agreements by claiming favorable treatment for transshipped goods that, according to the relevant rule of origin, are not produced in a country that is an intended beneficiary of preferential treatment. Such circumvention often disadvantages beneficiaries by unfairly filling their quotas. Preferential trade arrangements may carry stiff penalties for circumvention, especially for textiles or apparel transshipped through the CBI region or through an ATPDEA or AGOA beneficiary, for example, from China.

How do governments administer the rules and ensure compliance?

In the United States, importers seeking preferential tariff treatment for a good must have available documentation that confirms the good meets the rule of origin. Documentation includes a Certificate of Origin supported by production records and information on place of production, machinery used, and workers employed. "Visas" certifying origin must accompany shipments from AGOA countries, which must provide documentation supporting the issuance of the visa at the request of the United States. The U.S. Customs Service is required to send production verification teams to AGOA countries, and to conduct origin verifications and possibly site visits for CBI and NAFTA beneficiaries. AGOA legislation authorized resources for the U.S. Customs Service to provide technical assistance to sub-Saharan African countries to increase enforcement.

Who decides the rules?

National governments determine rules of origin that their customs officials apply, but those rules are subject to the WTO Agreement on Rules of Origin. It requires that WTO members' rules of origin be transparent and based on a positive standard, stating what does confer origin rather than what does not; be administered in a consistent, uniform, impartial, and reasonable manner; and not restrict, distort, or disrupt international trade. A WTO committee is working to establish a single set of rules for non-preferential trading conditions to be followed by all WTO members under all circumstances. A Common Declaration annexed to the Agreement stipulates that the general principles and requirements for non-preferential rules of origin contained in the Agreement also apply to preferential rules of origin.

In the United States, Congress has defined rules of origin in legislation establishing various preferential trade arrangements. FTA partners agree on rules of origin in negotiating an agreement. Congress must approve FTAs before they are implemented. In all instances, the U.S. Customs Service will issue regulations promulgating the rules.

How do the rules generally work?

A simple, common rule stipulates that a good entirely produced or obtained in a country is a good of that country. But many goods contain components from multiple countries. This is addressed by another common rule that stipulates that each "foreign" component used in a good undergo a change in tariff classification (tariff "transformation") as a result of production that occurs in a single country. For example, workers in Jordan might use lumber from the Philippines and Brazil to build a "Jordanian" table. Tables fall under a different tariff classification than lumber. An alternative rule addressing the problem of foreign components considers local content. For example, a CBI rule states that at least 35 percent of an article's value must come from a CBI country to qualify for CBI tariff treatment.

Are there exceptions?

Most U.S. preferential arrangements and FTAs contain rules of origin for specific products or classes of products, such as textiles and apparel. For example, the CBI program provides duty-free, quota-free treatment for apparel cut in a CBI country from U.S. fabric made from U.S. yarn and assembled there with U.S. thread. A NAFTA rule stipulates that peanut butter must be made from Mexican peanuts to be considered Mexican peanut butter, even though peanuts and peanut butter fall under different tariff classifications and even though Mexican peanut butter processors might have bought their peanuts from the United States. In effect, rules of origin often place rigorous requirements on eligibility for favorable tariff treatment.

Are there controversial aspects of rules of origin?

As preferential trade arrangements and FTAs proliferate, each with different rules of origin, customs administration and private sector recordkeeping can become more burdensome. Anecdotal evidence suggests that for some low-tariff products that are not price-sensitive, the cost of recordkeeping may outweigh the benefit of favorable tariff treatment.

Some countries have charged that specific rules of origin can disrupt trade. For instance, Japan has complained that Japanese-owned auto assembly plants in North America have difficulty meeting NAFTA's requirement for 62.5 percent local content. Consequently, vehicles produced there might not qualify for tariff-free trade among NAFTA countries.

Some developed countries, especially the European Union, allow FTA partners to count as local content production from any of their FTA partners. For example, the European Union has FTAs with Norway and Poland. A Norwegian exporter could count Polish content as contributing toward the Norwegian content of his product in meeting the EU-Norwegian FTA rules of origin. Some argue that this disadvantages the United States or Japan in the Norwegian market. The United States and its partners have not provided for this "cumulation" calculation among FTAs.

GLOSSARY

Content

Content rules establish a minimum proportion (by value or volume) of a product that must be domestically or locally produced in order to obtain a benefit such as favorable tariff treatment. A common rule in U.S. preferential trade arrangements and some FTAs is 35 percent local content.

Most-Favored Nation Status

MFN is the "normal" non-discriminatory tariff applied to imports. Countries expect that their exports will be treated as favorably by the importing country as the exports of the most favored exporter. Preferential trade arrangements provide treatment more favorable than MFN treatment and are therefore an exception from MFN status. MFN is also sometimes called "Normal Trade Relations."

Preferential Trade Arrangements

These are programs by which industrial countries extend market access to developing countries that is more favorable than MFN access. Benefits are considered unilateral in that U.S. products do not necessarily enjoy preferential access to developing countries' markets. U.S. preferential trade arrangements include the GSP, CBI, ATPDEA, and AGOA.

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