EEC CUSTOMS LAW: RULES OF ORIGIN
AND PREFERENTIAL DUTY TREATMENT

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Introduction
Lady Grisell Baillie was a strong-minded Scottish noblewoman who in 1731 embarked on the grand tour of Europe at a somewhat advanced age. She bequeathed to her heirs a charming and helpful guide to travel on the Continent, full of thrifty and prudent recommendations about how to ease the difficulties of moving a modest household and an ever-increasing load of domestic equipment, furniture, souvenirs and paintings around Europe. In particular, she described the tiresomeness of coping with "the searchers," customs agents who stopped and examined all goods and persons entering countries, principalities and even cities and towns, collecting duties and tolls and enforcing currency controls ("No money gose (into) France but the new French Louis... you must hide what you have and show only a little"). In Champagne, "We was searched overly" and at Châlons "we was stopd 3 days by the impertinence of the Bourro." In Rome, she recommended giving one Festoon to ensure "very sivil" treatment, and a mild inspection, provided that no prayer books or heretical material were found. However, at Valenciennes... we had little trouble by immediately giving a little money, and without hesitation telling them at the same time we gave the money that they might search if they pleased for we had nothing counterfeit nor any Merchandise which is the question they ask." But "some times they search very narrowly, and if they find it you lose it, but a little money given in time generally prevents it."

Two hundred and fifty years after Lady Grisell's travels, only a limited amount of literature in the English language exists to assist traders and legal practitioners in coping with customs regulations in Europe. It is the purpose of this article and those that may follow it to describe certain of the groups of customs rules which regulate trade in the European Economic Community.

The first part of this article will examine in general terms the significance and effect of rules of origin in the international trading arrangements to which the Community is a party. These rules are of enormous economic importance for the Community and its trading partners, in that they deter...
mine what products shall and shall not be entitled to duty-free or reduced
duty treatment on importation into the EEC or a country with which the
EEC has a preferential trade agreement. However, there appears to be almost
no non-governmental literature in English specifically concerning EEC rules
of origin. The second part of the article will examine, among other things,
the complexities of the rules dealing with "cumulation of origin," particularly
in trade between the EEC and EFTA, and will consider possible changes in
these rules. It will be noted that important sections of the EEC/EFTA rules
are so impenetrably obscure in their drafting that it is not easy to describe
them as meaningful or intelligible, but an effort will be made to state the
drafters' intention in the light of current practice.

The EEC's preferential trading arrangements

The EEC is party to preferential trade arrangements involving over 140
countries. These preferential trading arrangements may be grouped into the
following four main political and geographic categories, but as will be seen
the rules of origin applicable within each of the categories are not identical.

First, the free trade agreements between the EEC and its industrialised
neighbours, the remaining seven members of EFTA (Austria, Finland, Ice-
land, Norway, Portugal, Sweden and Switzerland, often called the rest-
EFTA countries). Under these agreements, industrial (i.e. non-food) pro-
ducts and some food products exported to the EEC from an EFTA country
or vice versa are entitled to duty-free treatment on importation, provided
that the relevant rules of origin are satisfied. Secondly, the co-operation and
association agreements with ten of the Mediterranean neighbours of the
Community (Cyprus, Israel, Malta, Egypt, Jordan, Lebanon, Syria, Algeria,
Morocco, Tunisia). Three of these agreements either provide for preferen-

4 The leading general authority on EEC customs law, although now somewhat
There are a number of publications on rules of origin issued by the Commission,
including "Explanatory Notes on the Rules of Origin for Trade with the African,
Caribbean and Pacific States and the Overseas Countries and Territories" (O.J.
1976 C185) and an annual *Practical Guide to the use of the European Commu-
nities Scheme of Generalised Tariff Preferences* which includes a chapter on rules of origin.
H.M. Customs and Excise have issued a variety of notices on EEC customs rules,
including *European Economic Community Preferences: Rules of Origin, Notice
No. 828; European Economic Community Exports: Preference Procedures, Notice
No. 827; European Economic Community Preferences: Imports, Notice No. 826;*
and others such as *Notices 810, 825 and 343.* The Caribbean Community
Secretariat has published a guide entitled *Exporting to the EEC under the Lomé
Convention* (Guyana, 1976).

5 Austria O.J. 1972 L300/3, rules of origin at 38; Finland O.J. 1973 L328/1, rules
of origin at 49; Iceland O.J. 1972 L301/3, rules of origin at 106; Norway O.J. 1973
L171/1, rules of origin at 45; Portugal O.J. 1972 L301/166, rules of origin at 288;
Sweden O.J. 1972 L300/196, rules of origin at 131; Switzerland O.J. 1972 L300/190,
rules of origin at 224. (All of the foregoing have been occasionally amended.)

6 There are exceptions to this general principle in the case of Iceland, Norway and
Portugal, which enjoy a number of advantages by comparison to the other four
EFTA states, but the EFTA agreements are otherwise broadly parallel.

7 Cyprus: O.J. 1973 L133/1, rules of origin at O.J. 1977 L339/19; Israel: O.J.
1975 L136/1, rules of origin at O.J. 1975 L136/126 and O.J. 1979 L80/1; Malta:
O.J. 1971 L61/2, rules of origin at O.J. 1976 L111/11; Egypt: O.J. 1978 L266/1,
tial access to the EEC for most industrial and some food products originating in the exporting Mediterranean country, with more modest concessions in favour of EEC exports to such country (Cyprus, Israel and Malta), and seven provide only for non-reciprocal access to the EEC. Within the seven, the agreements with the Maghreb countries (Algeria, Morocco and Tunisia) provide for a degree of multilateral co-operation among the three countries in satisfying the rules of origin, but the remaining four (the Mashraq countries) do not have such a feature. The third, and much more varied, group of preferential trading partners comprises the 58 African, Caribbean and Pacific signatories of the Lomé Convention. Because of their historical links with different EEC Member States and the unique nature of the Lomé Convention, the applicable rules of origin are the least restrictive of all. It is customary to treat along with the Lomé Convention the Overseas Countries and Territories, the dwindling number of colonial territories and possessions of the Member States often known by the acronym of OCT or PTOM (pays et territoires d'outremer), the products of which have access to EEC markets on terms similar to Lomé Convention products. The particular political status of the Faroe Islands makes it difficult to categorise, but the Community's treatment of Faroese products may reasonably be treated along with the EFTA countries (and, in particular, Norway) rather than with the Overseas Countries and Territories. The fourth group consists of the countries to which the EEC accords tariff preferences subject to quantitative limitations (which are very strict in certain cases) known as quotas and ceilings under the Generalised System of Preferences (GSP), a non-reciprocal unilateral grant of preferential tariff treatment (usually duty-free) to the industrial products of any developing country which requests to be accorded GSP status by the EEC. There are approximately 130 GSP beneficiaries varying widely in size, political system and economic development. The GSP is available to many countries which already have specific agreements with the EEC, such as the Lomé Convention signatories and some of the Mediterranean countries already listed. However, since the terms applicable under the GSP are less favourable than under the various bilateral agreements, exporters prefer to seek the benefits of the latter rather than the former. Since some EFTA countries operate generalised systems of preference of their own for developing countries, Lomé Convention exporters may still want to bear in mind "quasi-GSP" opportunities in, say, Scandinavia.

In addition to the foregoing groups, there are three other agreements which remain in force but are of limited significance for the present article. In

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8 Lomé I: O.J. 1976 L256/1; Lomé II: signed in the Togolese capital on October 31, 1979, not yet published in the Official Journal.


10 The GSP regulations for 1980 are to be found at O.J. 1979 L328/1, and the rules of origin applicable thereto at O.J. 1979 L340/1.
1963 and 1964 respectively, the EEC entered association agreements with Greece and Turkey. Both agreements envisaged the ultimate achievement of a customs union, and were therefore posited on the assumption that common external tariffs would apply, so that rules of origin would be of no importance. In other words, since all third country goods entering the EEC, Greece or Turkey would pay customs duty at the same rate, and since trade within the EEC, Greece and Turkey would be duty-free, there was no need to have rules of origin governing eligibility for EEC-Greek or EEC-Turkish preferences. Greece will become a Member State on January 1, 1981, and the Turkish agreement has been subject to a number of significant changes: both agreements need not be further considered for present purposes. In 1970, Spain and the EEC entered a limited preferential trade agreement, providing for a number of concessions by each side. Spain's candidacy for EEC membership is well-advanced, but the 1970 agreement as amended will govern EEC-Spanish trade for some time to come. The Spanish agreement is the sole survivor of what might be called the old generation of preferential trade agreements. Its rules of origin are old-fashioned in a number of respects: for example, the list of insubstantial processes which cannot confer origin is not contained in the rules of origin themselves, but at the beginning of the annexed lists. The rules of origin of the Spanish agreement will therefore be referred to only for historical purposes. One may hope that their antiquarian interest will not be regarded as a bar to their modernisation, possibly by an exchange of letters, at an early date during the current EEC-Spanish negotiations on accession and interim commercial measures, so that traders can have a more intelligible set of standards by which to assess their eligibility for duty preferences. This is all the more desirable as Spain has recently concluded a trade agreement with the EFTA countries.

Classification, valuation and assessment of duty
Each preferential trade arrangement accords duty-free or reduced duty treatment only to those products "originating" in the beneficiary country or group of countries. Before examining the question of what constitutes origin, two other customs operations should be understood. When a customs officer is presented with goods for clearance, he must first determine what they are. The process of classification in the EEC is governed by the Common Customs Tariff, which categorises in the 99 Chapters of its nomenclature every object which may be physically traded in commerce, beginning at Chapter 1, Heading 01.01 (live horses, asses, mules and hinnies), proceeding through 65.07 (spring frames for opera hats and other headgear items) to 99.06 (antiques of an age exceeding 100 years). Classification questions have been a fruitful source of referrals to the European Court by national courts, especially German ones. The various rules for applying the nomenclature, and

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EEC CUSTOMS LAWS: ORIGIN AND PREFERENTIAL DUTY

Drawing between alternative classifications, are not the subject of this article, but it will be seen that correct classification is of considerable significance for origin purposes.

The next step is valuation. The basic text for this purpose is Regulation 803/68 as amended, and the European Court is not infrequently called upon to decide valuation questions arising out of Regulation 803/68. When the customs officer has determined, on the basis of the invoice price or otherwise, the value of the item in question, and on the assumption that the product comes from a third country with which the EEC has no preferential trading arrangement, he applies the so-called "conventional" percentage duty set forth in the CCT for the appropriate tariff heading to obtain the amount of customs duty payable. However, if the import comes from a country with which the EEC has a particular arrangement providing preferential duty treatment for goods of the particular classification in question, he will apply such preferential treatment after satisfying himself that the goods satisfy the rules of origin applying to trade between the EEC and the country in question.

Tariff treatment to protect shipping

Over the years, preferential treatment has been accorded to importations in a variety of ways, reflecting current economic and political concerns. The English Parliament dabbled in ways of protecting English shipping interests as long ago as 1381, and after various false starts there was enacted the Navigation Act of 1660 which, with many amendments over the years, laid down the basic principles of British mercantile policy in force until 1825. During the 160 years of the Navigation Acts, the importation into England or Crown colonies in Africa or America of foreign or colonial goods was either prohibited or made significantly more burdensome if the vessel carrying the cargo was not English-built, English-owned, manned by an English master and a crew three-quarters or two-thirds English. For example, "All Druggs imported directly from the place of their growth in English-built shipping, to be rated one-third part of what is charged in the Book of Rates, and no more." Many exceptions were provided by statute over the next 160 years: Irish and Scottish trade was gradually subject to fewer discriminations; some traditional patterns of trade were exempted from the extra

17 A new valuation Regulation will emerge shortly as the result of the new valuation code adopted as part of the Tokyo Round MTN accords concluded in Geneva in 1975.
18 Valuation cases can raise important issues involving substantial economic and financial consequences. For two recent examples see Case 65/79, Public Prosecutor v. Chatain (not yet decided); and Case 111/79, Caterpillar Overseas v. Belgian Tax Authorities (not yet reported).
19 e.g. where the invoice price is not a reliable point of departure, by examining the price of comparable goods in comparable transactions.
20 The Act of 5 Ric. 2, stat. 1, c. 3, 1381.
21 12 Cha. 2, c. 18, 1660, to be read along with 12 Cha. 2, c. 4, 1660 and the so-called Act of Frauds, 1662 14 Cha. 2, c. 11.
22 12 Cha. 2, c. 4, 1660, a precursor of the CCT in setting out all possible categories of import and the duties applicable thereto. Hawk hoods were liable to a duty of £1.6.8 per gross.
duties; and a few, limited, liberalisations were granted to foreign trade with
the colonies. From 1822 onwards, the Navigation Acts were gradually re-
placed, and Britain entered a network of reciprocal treaties concerning ship-
ing with its European neighbours.23

The purpose of the mercantilist legislation just described was protection
of the interests of English and latterly British shipping. There was no inten-
tion to encourage indigenous manufacture and exportation to Great Britain.
However, as notions of trade changed, and as the cost, risk and difficulty of
transport decreased, the modern concept developed of conferring duty pre-
ferences on the basis of origin.

General considerations concerning origin criteria

When the Community decides to grant reciprocal duty-free treatment to
industrial exports from a given country or group of countries it is necessary
to strike a balance between, on the one hand, being so excessively strict that
only local handicrafts would be deemed to originate in the beneficiary country
or group of countries (and bicycles entirely manufactured in a beneficiary
country, but equipped with tyres made from natural rubber tapped in the
orient, would be excluded), or on the other hand so lax that almost any export
from the beneficiary country or countries would be deemed to originate even
if its connection with the local economy were very slight (so that the bicycles
would be deemed to originate even if they were made in Japan and were
merely painted in the beneficiary country before re-export to the EEC). In
the case of the EFTA agreements, there is a desire to foster and develop
traditional currents of trade among the European democracies, while restrict-
ing the reciprocal benefits of duty-free treatment to those goods which are
significantly connected with European industry. In the Community's non-
reciprocal trade arrangements with the developing world, which are less
significant in volume terms for the EEC than EFTA trade, but which are
crucial to the export chances of the third world countries concerned, rules
of origin can be of great importance for the development of weak economies.
American, European and Japanese investors can be more readily attracted
to establish factories in, for example, a Lomé Convention country, if the
output of those factories may enter the EEC without payment of customs
duties. Likewise, the host country wishes to see genuine manufacturing
activities, not merely cosmetic efforts to give the impression of an indigenous
contribution to the final result. However, the host country would generally
be satisfied with a lesser degree of connection with the local economy than
the EEC demands, and indeed developing countries have frequently repro-
ached the Community for imposing rules of origin which are too strict
for newly-created industries. The Community's practice of according deroga-
tions from the rules of origin to newly-established industries on an ad hoc
basis will be mentioned in Part II of this Article.

23 The various enactments from 1660 to 1782, including the celebrated Sugar Act
of 1764 and the Tea Act of 1773 (concerning the drawback of customs duties on tea
exported to the American colonies) are mentioned and placed in historical and
I am grateful to the librarian of H.M. Customs and Excise at King's Beam House,
and his staff, for the assistance they have given in this connection.
Preferential and non-preferential origin

Modern rules of origin accord duty preferences by ascribing origin on the basis of what was done in the exporting country in the process of making the finished product. All systems of attributing origin are intended to associate a product with a given country; however, rules of origin for preferential trade purposes are intended principally to exclude "non-deserving" products from entitlement to preferences, and to include only those sufficiently connected with the exporting state's economy. There will always be some country of non-preferential origin; there may be a country of preferential origin. It often arises that a product does not satisfy these tests and does not have preferential origin, or does not come from a country to which preferential treatment is accorded. Nevertheless, it is necessary to determine the origin of imports for other purposes than eligibility to duty preferences. The Community has an interest in the compilation of accurate external trade statistics; safeguard measures, such as antidumping actions, are usually implemented on a national basis (bicycle chains originating in Taiwan, for example); very importantly, when a Member State is authorised under Article 115 of the Treaty of Rome to take safeguard measures to exclude from Community treatment, say, zip-fasteners originating in Japan, it is necessary to decide whether zip-fasteners made in another Member State from Japanese components can be regarded as of Japanese origin (and therefore can be refused entry into the first Member State) or of Community origin (and therefore entitled to the benefits of the Treaty's provisions on free movement of goods); and for other purposes also it is desirable for there to be a common means of determining the origin of goods. Council Regulation 802/68 fulfils this function. It establishes criteria which Member State customs officers shall follow in determining origin where no specific rules of origin, applicable to the particular import, exist. Since each of the preferential arrangements to which the EEC is a party incorporates its own set of rules of origin, Regulation 802/68 has no application to the determination of preferential origin, although it has procedural significance in a number of respects.

Article 5 of Regulation 802/68 provides that a product should be deemed to originate

"in the country in which the last substantial process or operation that is economically justified was performed, having been carried out in an undertaking equipped for the purpose, and resulting in the manufacture of a new product or representing an important stage of manufacture."

That Article contains a number of elements: (1) substantiality of the operation; (2) economic justification; (3) adequacy of the equipped-ness of the place of manufacture; (4) (i) new product, or (ii) important stage in the manufacturing process. They are phrased to be cumulative (with the alternative under 4 (i) and 4 (ii)), although good sense suggests that any one individually ought to be enough to associate the product significantly with the

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24 O.J. 1977 L242/5, held invalid by the European Court in Cases 34/78 and 114/78, see note 30, post.
26 Notably Art. 5 of Reg. 802/68.
exporting economy. It would seem absurd to argue that a substantial operation was not economically justified or that even although economically justified the place of manufacture was inadequately equipped. The explanation, as with some of the other obscurities of the origin rules, lies in the fact that the rule when first formulated was a pastiche of several Member States' different rules, which were pressed into one rule which was not altogether internally consistent.

There is not usually any particular advantage to be derived from claiming, say, Australian as opposed to Canadian origin, so that deflection of trade or cosmetic attempts to characterise Canadian goods as Australian are rather rare. However, controversies can arise as to whether a particular kind of product is entitled to be regarded as of Community origin, either for export to third countries or for purposes of safeguard measures under Article 115, where exclusion from Community treatment is authorised. Under Regulation 802/68, the Commission has the power, in collaboration with the Member States, to promulgate specific regulations for particular products, determining the processes to be accomplished in order for the products to be deemed to have non-preferential origin under Regulation 802/68. About a dozen such regulations have been adopted, of which Regulation 749/78, dealing with textile products, is of particular significance in light of the Community's series of self-limitation agreements with various textile-exporting countries. For example, if a Thai exporter discovered that his country's exports of textiles to the Community had already reached the maximum to which Thailand had subscribed, the exporter might be tempted to claim that his goods originated in another country which had not yet reached its maximum. A determination of origin under Article 5 of Regulation 802/68 would be made by the application of Regulation 749/78. In the context of a deepening world economic recession, and the tendency to take safeguard action to avoid competitive pressure, access to foreign markets can be as important as access on favourable duty terms, since duty rates are already low for most products. It should be noted that the taking of safeguard action against products, especially textile products, which originate for preferential purposes in the exporting country, is hedged about with consultations and special procedures for the Community. Taking safeguard measures against products not benefiting from a preferential trade agreement's protection is a much

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28 O.J. 1978 L101/7, as corrected.

29 Agreements have been reached with, inter alia, Argentina, Bangladesh, South Korea, Macao, Pakistan, Sri Lanka and Thailand (all in O.J. 1979 L298), and Brazil, Uruguay and Haiti (all in O.J. 1980 L70).
more autonomous matter: another indication of the importance of the distinction between the two types of origin.

The Community's discretion in adopting such specific regulations is not, of course, unrestricted. The European Court has had occasion to examine the fairness of the regulation on zip-fasteners which was alleged to be overly restrictive in according origin, and which was indeed held by the Court to be invalid.80

Origin for preferential purposes

When examining any particular trading pattern, it is necessary to determine the origin of the product under the rules of origin applicable to the particular export-import transaction. In some cases, the Community may wish to be generous to a young economy; in others, stricter rules are appropriate since local industry is fully developed. Thus the rules of origin applicable under the Lomé Convention are different to the rules of origin applicable under the EEC/Austria association agreement. That being said, however, the general layout and the philosophy behind the various rules of origin are similar. In order to understand the current form of the various rules, a brief historical review will be helpful.

History of EEC preferential rules of origin

The first free trade agreement entered into by the Community had no rules of origin. The Yaoundé Convention,32 signed between the original six Member States and 18 French-speaking African and Malagasy states in 1963, granted duty-free treatment to a limited number of products "originating" in the associated states. Protocol 3 to the Convention envisaged the adoption of rules of origin within six months, but this aspiration was not realised. As a result, each EEC Member State applied its own rules of origin in deciding whether the associated states' exports were eligible for Yaoundé Convention treatment. There were thus five separate methods in force (Belgium and Luxembourg applying the same rules). The position was probably not as aberrant as it may today sound, since most of the products in question were tropical fruits, determining the origin of which was not difficult. Putting it otherwise, the Community's indigenous industries did not urgently need protection in the form of tightly-drafted rules of origin.

When the Yaoundé Convention was approaching expiration in 1968, the Community was also contemplating what came to be the first generation of Mediterranean agreements, of which only the Spanish agreement is still in force, being signed in 1970, and the expansion of its African association plans to include three English-speaking newly-independent states. Kenya, Tanzania and Uganda (which signed the Arusha Convention in 1969).33

33 J.O. 1966, 1431.
34 In order of signature: Burundi, Cameroun, Central African Republic, Congo (Brazzaville), Congo (Leopoldville), Ivory Coast, Dahomey, Gabon, Upper Volta, Madagascar, Mali, Mauritania, Niger, Ruanda, Senegal, Somalia, Chad and Togo.
35 J.O. 1970 L282/55.
There was no particular difficulty in assigning origin to agricultural products, or handicrafts produced exclusively in the exporting country, though common criteria were obviously desirable. However, it was imperative that a workable system of origin which would be sufficiently sophisticated to cope with industrial products be developed. It has already been observed that for such products Regulation 802/68, dealing with non-preferential origin, incorporated the notion of last substantial transformation, creation of a new products, and other criteria, each being borrowed from a different Member State's system. This test was not sufficiently strict for preferential trade: any product essentially made in the United States or Japan could be finished in the beneficiary country, shed its United States or Japanese origin and thus gain preferential access to the EEC. This might be reasonable for some products, but not for others. A specific rule for every manufactured object would be far too cumbersome. If the working in the beneficiary country substantially enhanced the value of the imported items, would this be a satisfactory basis to accord origin? The EFTA Convention in particular had a generalised 50 per cent. added value test, with some specific rules for particular products. However, it was realised that merely using added value could place cheap labour countries at a disadvantage. If a Swiss worker spent a day working on a piece of non-Swiss leather to make a shoe, the value of the leather would be trivial by comparison to the value of the finished shoe. Not so if the worker was in a landlocked country in the Sahara.

During the negotiations among the Member States and their trading partners, the idea materialised of looking to the tariff heading of the finished product by comparison to the tariff heading of the non-originating components as a way of deciding whether there had been a substantial processing. On this theory, if there was a change in tariff heading, a "new product" would presumably have been created and it would be reasonable to accord origin. This test had the advantage of being easily understandable and avoided the need to have a separate rule for each product, although it was realised that some specific rules would be necessary for particular products, and the Member States were invited to submit lists of products they considered to require a special rule. Another major problem, which has by no means been resolved satisfactorily even today, was to decide on workable and fair cumulation rules, governing the origin status of a product which has been advanced to completion in several countries successively. If a product originates in one country, should processing in another country involving non-originating parts or materials deprive the product of origin, and if so under what conditions? Should origin be acquired gradually in several countries, or should each country have to satisfy the rules individually in order for the end product to be originating?

The topic of rules of origin was, in the words of the First General Report of the Commission of the three Communities, "longuement débattu". In any event, the first set of rules of origin emerged in Decision 5/66 of the Council of Association between the Community and the associated African

\[\text{\textsuperscript{24} p. 393. See also the Eighth and Ninth Reports of the EEC Commission, at p. 350 and p. 289 respectively.}\]
and Malagasy states. More complete rules followed: Yaoundé II, Arusha and Spain, Morocco, Tunisia, Malta. These rules did not settle all the problems, and were not always easy to read. For example, since some of the various Member States' special rules for particular products were expressed positively and some negatively, these exceptions were combined into separate positive and negative lists, although it would have been possible to draft a single list of exceptions which would have been much easier to follow.

The accession to the EEC of three EFTA Member States (Denmark, Ireland and the United Kingdom) on January 1, 1973, and the signing of association agreements with the seven remaining "non-acceding" EFTA countries, was the next major challenge for the Community's system of preferential origin. The EFTA countries were accustomed to a value added test, coupled with specific tests for particular products, and would have preferred to retain this system. However, the newly-developed Community system prevailed, and to the seven EEC-EFTA agreements were annexed origin protocols which contained more elaborated versions of the Yaoundé/Mediterranean agreements, with some modifications. Since the EEC-EFTA agreements, the second generation of Mediterranean agreements (which are still in force) and two Lomé Conventions have been signed.

For the purposes of examining in greater detail the various rules of origin, it will be most useful to select one of the bilateral, reciprocal agreements such as those with Cyprus, Israel or Malta. References hereafter will therefore be to the Israeli agreement, which covers a rather wider range of products than the Cypriot or Maltese agreements.

**Products wholly obtained or sufficiently processed: the basic rule**

Article 1 of the Rules of Origin provides that products shall be deemed on importation into the EEC to originate in Israel if they are "wholly obtained there," or if they were "obtained in Israel by the manufacture of products other than those wholly obtained in Israel ... provided that the said products have undergone sufficient working or processing." Conversely, products will be deemed by Israel to originate in the Community if such products were "wholly obtained in the Community," or were obtained in the Community by the manufacturing of non-Community products which have undergone sufficient working or processing.

**Products wholly obtained**

Products are wholly obtained if, in essence, they have been produced exclusively with the natural resources and labour of the exporting country.

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36 J.O. 1971 L135/1.
38 J.O. 1970 L182/1.
41 J.O. 1971 L136/1.
42 In Community jargon, opinion is divided as to whether the proper acronym for the remaining members of EFTA is EFTA, rest-EFTA, AELE (the French version), or PNA (Pays non-adhérents).
The following list is illustrative and probably exhaustive of what will be deemed to be wholly obtained in either the exporting country or the Community:

(a) mineral products extracted from their soil or from their seabed;
(b) vegetable products harvested there;
(c) live animals born and raised there;
(d) products from live animals raised there;
(e) products obtained by hunting or fishing conducted there;
(f) products of sea fishing and other products taken from the sea by their vessels;
(g) products made aboard their factory ships exclusively from products referred to in subparagraph (f);
(h) used articles collected their fit only for the recovery of raw materials;
(i) waste and scrap resulting from manufacturing operations conducted there;
(j) goods produced there exclusively from products specified in subparagraphs (a) to (i).

The foregoing rules, although they are self-explanatory in a number of respects, do present a number of unsettled issues. Fisheries products present special problems in that the nationality of the flag, the crew, the master and the owners is relevant, as well as the physical position of the boat or factory ship. Fisheries are examined in Part II of this Article.

In the wholly obtained rules, (a) provides that mineral products will be wholly obtained in the exporting country if extracted from its soil or from its seabed. One may question whether seabed means the seabed underlying the country's territorial waters, or under one of the various contiguous zones claimed by the country for fishing or other purposes. Arguably, the geology of the seabed could be relevant, so that if there were a rift on the ocean floor, the minerals extracted from the high seas side of the rift might not belong to the category of wholly obtained products. One may likewise ask if nodules resting on the ocean floor are to be regarded as 'extracted' from it. It is submitted that a broad interpretation of the rule is appropriate, and that if the extracting is done in an area claimed, regulated or controlled by the government of the country in question, all minerals won in such area should be deemed as wholly obtained.

Rule (h) accords wholly obtained status to "used articles collected there fit only for the recovery of raw materials." Thus, empty tins of food, bottles, wrecked cars and other items of domestic and industrial detritus fit only for "recycling" are covered, since they have no function other than to yield up their component raw materials. This means that the cans containing a shipment of canned corned beef canned in the United States could become wholly obtained in Israel once emptied and fit only for the recovery of the tin and other metals they contain. However, is wholly obtained status lost if the item could be put to another purpose without destruction in the process? For example, if the wrecked car has a tyre which could be retreaded or melted down, or a cylinder block which could be rebored or melted down, are the
tyre and the block ineligible for wholly obtained treatment? Again, it is submitted that a narrow view is not appropriate.

Waste and scrap products are also covered by rule (i) which mentions "waste and scrap resulting from manufacturing operations conducted there." If the manufacturing operation is carried out on an originating material, the leftovers of that operation are obviously entitled to origin. If the operation produces an originating product, the leftovers should be entitled to originating status also. But if the manufacturing process is conducted on non-originating materials, the question arises of whether it confers origin. Further, what is the status of valuable by-products which result from a manufacturing process but are superfluous to it? Putting the question differently, does the rule focus on the fact that the goods in question are waste or that they result from manufacturing operations? It is submitted that if the goods are clearly waste or scrap, and cannot be used as they are without further recovery or recycling operations, they should be deemed to be wholly obtained irrespective of the nature of the manufacturing activity, of the status of its fruits, or of the status of the materials processed. However, if the goods are in their own right commercially disposable distinct by-products, they should not be entitled to originating status. Thus, gold left over when a jeweller makes a bracelet, or steel left over after the stamping out of parts from steel sheet, would be waste or scrap, albeit valuable, whereas a petrochemical by-product of the manufacture of ethanol would not be. The former would be deemed wholly obtained, whereas the latter would not.

Manufactured products

In the modern world, there are few industrial products which are the fruit of only one country's industry. Raw materials, paint, bolts, special components and other items may need to be procured in other countries, or parts procured locally may have had some foreign input. Other than for agricultural products (which are often excluded from the full benefit of free trade arrangements) and handicrafts (such as textiles) the test of "wholly obtained" is rather rarely met. For industrial products it is usually necessary to consider whether, in making the final product, enough has been done locally to satisfy the rules.

Sufficient working or processing

Sufficient working or processing is by far the most important of the various provisions governing origin criteria. The point of departure is a comparison of the tariff classification under the Brussels Nomenclature of the end product of the manufacturing operation with that of any imported non-originating items incorporated in that process. The idea is that if non-originating products (i.e. imports) are processed to such a degree that the finished product bears a four-digit tariff classification different from each of the non-originating parts or components, this is in itself an indication that a substantial change has been effected in the country of manufacture. Thus, where a South African diamond falling under CCT heading 71.02 and unworked Australian gold falling under CCT heading 71.07 are combined in,
Israel to produce a diamond ring falling under CCT heading 71.12, the finished product bears a different tariff classification than each of its component parts, ingredients or materials. There has thus been a change of tariff heading, and in most cases the requirements of preferential origin would be satisfied.

It should be noted that a change in four-digit tariff heading is indispensable. It is not enough to change sub-heading, for example from 85.21 D I (wafer not yet cut into chips) to 85.21 D II (other microcircuits).

The exceptions: Lists A and B

For most industrial products a change in tariff heading is enough to confer origin for preferential purposes. To this basic principle there are two major exceptions, and the products covered by these two special rules are set forth in Lists A and B which are annexed to each set of rules of origin. As well as a change in tariff heading, List A products must clear an additional hurdle (an added value test, an affirmative specific processing test or a negative specific processing test or a combination of these) before being deemed originating; List B products benefit from a derogation in the event that they satisfy some test other than a change in tariff heading. For example, if the South African diamond mentioned above were imported uncut into Israel, and were there cut and polished, this would confer Israeli origin under List B.

Specific processing tests

An additional requirement will be imposed in the event that the product figures in List A to the particular set of rules of origin. Specific processing tests can be quite straightforward to apply, whether they are positive or negative. For example, paper in rolls or sheets is classified under CCT heading 48.06; paper cut to size or shape is classified under heading 48.15. Merely cutting to size rolls of paper under heading 48.06 does yield a finished product falling into the new heading of 48.15, but since the product obtained figures in List A annexed to the EEC/Israel rules of origin, it will obtain origin only if the particular working or processing required in List A has been satisfied. For products falling under heading 48.15, the requirement is that the manufacturing operations be conducted upon paper pulp. Thus, if...
EEC CUSTOMS LAWS: ORIGIN AND PREFERENTIAL DUTY 181

Paper pulp is imported into Israel, is there transformed into paper and then into cut paper, it will enjoy preferential Israeli origin because there will have been (a) a change in four-digit tariff heading and (b) compliance with the additional test set forth in List A. However, if the paper is imported in rolls, the additional test of List A will not have been satisfied, and the product will be deemed of Israeli origin under Regulation 802/68 (for statistical purposes), but not of Israeli origin for preferential purposes under the EEC/Israel agreement. If the pulp is made in Israel from Israeli wood, and then transformed into paper in Israel, the paper will be of Israeli origin on the basis that it was wholly obtained in Israel.

List A also contains negative specific processing conditions providing that certain working or processing cannot confer origin even if there is a change in tariff heading. For example, a shoe (CIT heading 64.01) will not be entitled to originating status if it is manufactured from non-originating imported, uppers which lack only an outer sole to be a finished shoe (CIT heading 64.05).

List A's negative conditions can be rather challenging. For example, for certain sugars and artificial honeys (CIT heading 17.02), the negative test is simply "Manufacture from any product." This means that even if there is a change in tariff heading, no amount of processing which yields artificial honey in heading 17.02 will confer origin. The only way that the product may achieve origin is if it satisfies the wholly obtained rules.

Bakery products (CIT heading 19.07) are also subject to a negative provision: "Manufacture from products of Chapter 11. Chapter 11 products are flours. Therefore manufacturing bread from non-originating flour does not confer origin. Wheat flour (CIT heading 11.01) is itself subject to a negative provision: "Manufacture from cereals. Therefore grinding non-originating wheat into flour does not confer origin. One might draw the conclusion that bakery products can never originate save by virtue of the wholly obtained rule, but this would be too pessimistic. The negative provision does not prohibit manufacture from any non-originating product, but manufacture from Chapter 11 products which do not originate. Manufacture from non-originating Chapter 10 products (that is, imported grain which is ground into flour in the exporting country) would confer origin. Thus, bread may have some non-originating input, whereas the sugar and artificial honey products mentioned above may not.

List B, as noted above, constitutes a derogation from the general principle that a change in tariff heading is necessary in order for origin to be conferred. List B provides, for example, that articles of ivory falling under heading 95.03 will be entitled to originating status even if they are manufactured from "worked ivory," also falling under heading 95.03. Similarly, the crushing of earth colours (CIT heading 25.09) to yield calcined or powdered colours (also heading 25.09) will be enough to confer origin under List B.

Added value tests

A good indication that the local economy has contributed significantly to the manufacture of the finished product is present when the finished product
is significantly more valuable than the imported non-originating components. Added value requirements are provided for a number of specific products, either as an additional test (List A) or as an alternative means of qualifying (List B) for origin.

Determining whether the added value tests prescribed by List A, List B or both have been satisfied can involve calculations of some complexity. The easiest is where it is necessary merely to determine whether the value of the non-originating products exceeds a certain percentage of the value of the finished product. For example, there is a List B provision for most products of the chemical and allied industries (CCT Chapters 28 to 37), to the effect that origin will be conferred, despite there being no change in tariff heading, by “working or processing in which the value of the non-originating products used does not exceed 20 per cent. of the value of the finished product.”

Two examples may be mentioned from List A. Knives and cutting blades for machines (CCT heading 82.06) are deemed to enjoy originating status only if (1) there has been a change in tariff heading between the imported components and the finished product, and if (2) the value of the materials and parts which are imported does not exceed 40 per cent. of the value of the finished product. Aluminium window frames falling under heading 76.08 will be entitled to origin only if non-originating parts used in their manufacture fall under different tariff headings, and if the value of these non-originating parts falling under other tariff headings does not exceed 50 per cent. of the value of the finished frame.

The simple percentage test just described may be accompanied by an additional percentage test, which requires that of all the components included in the manufacture of a product, imported components not exceed a certain level. Such additional percentage tests apply in the case of sophisticated machines manufactured by assembly, where certain of the elements of the machine are crucial to its functioning. The additional percentage test may be applied to all the components or to the critical element.

Refrigerators (heading 84.15) are subject to a double percentage test, both calculated on the value of the whole machine and all of its components, expressed in List A as follows:

“Working, processing or assembly in which the value of the non-originating materials and parts used does not exceed 40 per cent. of the value of the finished product, and provided that at least 50 per cent. in value of the materials and parts used are originating products.”

Sewing machines are also subject to a dual test, but in this case the calculation of the value of the components for the second percentage test is made on the value of a part of the finished machine. For a sewing machine to have preferential origin: (1) the totality of the value of the non-originating materials and components must not exceed 40 per cent. of the value of the finished product; (2) the thread tension, crochet and zigzag mechanisms must themselves be originating products; (3) at least 50 per cent. of the materials and components used in the assembly of the sewing machine head (other than the motor) must themselves be originating products, and (on a reading
of List A alone); (4) there must be a change in tariff heading in the sense that every imported non-originating component must bear a different tariff heading than that of the finished machine (heading 84.41). However, the requirement of a change in tariff heading can be avoided since sewing machines also figure in List B, which contains the identical three conditions just mentioned. Thus a change in tariff heading may be dispensed with.

A number of other products figure in both Lists A and B to the EEC/Israeli rules of origin and are subject to dual percentage tests. Microphones, loudspeakers, amplifiers (heading 85.14) and radiotelegraphic and radiotelephonic transmission and reception apparatus, TV and radio transmission apparatus and other electronic apparatus (heading 85.15), gramophones, TV sets, tape recorders and the like (heading 92.11) figure in both Lists A and B so that: (1) the totality of the value of the non-originating materials and components must not exceed 40 per cent. of the value of the finished product; (2) at least 50 per cent. in value of the materials and components used in making the final product must be originating; and (3) the value of any non-originating transistors must not exceed 3 per cent. of the value of the finished product. The 3 per cent. transistor percentage may not be cumulated, so that where a TV set worth 100 on leaving the factory is assembled in Grenoble from Japanese and EEC components, the Japanese components of all types may not exceed 40 in value, of which three may be transistors and 37 other components. However, if labour, fuel, overheads and profit represent 30, the totality of the value of the components is 70 (100 total minus 30 non-component elements), and the permitted ceiling of Japanese components will be 35 (50 per cent. of 70, the value of all the components), of which not more than three may be transistors and the balance other components.

List B's derogations from the requirement of a change in tariff heading include one "bagatelle" provision. Incorporating non-originating materials and parts worth not more than 5 per cent. of the value of the finished product will not deprive that finished product of origin, notwithstanding the fact that it bears the same tariff heading as the non-originating part, for the following products only: boilers, machinery, mechanical appliances, etc., of Chapters 84 to 92, in boilers and radiators of heading 73.37, and in the products contained in headings 97.07 (fish-hooks and fishing tackle) and 98.03 (fountain pens, ball-point pens and pencils).

As already noted, there is another broad List B provision, requiring 80 per cent. added value, for certain products of the chemical and allied industries. Medicaments (heading 30.03) also figure in List A, where a 50 per cent. value added test applies. As a result, medicaments obtain preferential origin: (1) if there is no change in tariff heading, provided that the value of the non-originating materials is not more than 20 per cent. of the value of the finished product, or (2) if there is a change in tariff heading, provided that the value of the non-originating materials is not more than 50 per cent. of the value of the finished product.\(^4\)

\(^4\)The rules concerning minimal or insubstantial processes may possibly be relevant to medicaments if they are not made under controlled conditions. See further in the text at "simple operations inadequate to confer origin," below.
Elements to be used in calculating value

The calculation of added value should be a neutral one, devoid of extraneous political or economic considerations. The fact that the end product is fashioned on a machine tool made in Japan and operated by an American worker in a factory owned by a Brazilian company having a branch in the beneficiary country is not relevant. The test simply examines how much has been done in the beneficiary country, not by whom or with what equipment it has been done.

The relevant bases for valuing on the one hand non-originating materials and components, and on the other hand the finished products, are defined, not completely conclusively, as follows:

— for the materials and parts: the customs value at importation into the country of manufacture, or if this is not known or their origin is unknown, the "earliest ascertainable price paid for such products in the country of manufacture";

— for the finished products: their ex-works price, less taxes refunded on exportation (such as value added tax).

There are two further explanations of this formulation in the rules. The Explanatory Notes (printed immediately before List A and List B) state that "ex-works price means the price paid to the manufacturer in whose undertaking the last working or processing is carried out, provided the price includes the value of all products used in manufacture," and that "customs value" means value for customs purposes under the Brussels Convention of 1950. The Lists themselves have a footnote in very small print, stating:

"In determining the value of materials and parts, the following must be taken into account:

(a) In respect of originating materials and parts, the first verifiable price paid, or the price which would be paid in case of sale, for the said products on the territory of the country where working, processing or assembly is carried out;

(b) in respect of other materials and parts, the provisions of Article 4 of the Regulation determining:

(i) the value of imported products

(ii) the value of products of undetermined origin.

This means that to make the calculation of whether a percentage value added test is satisfied, one should take the declared value at importation of all the non-originating materials, and should compare that to the price obtained by the manufacturer for his product in the country of manufacture, if it is sold there, or elsewhere if it is exported. Thus, if the manufacturer can command a high profit for his product or has high fixed costs reflected in the sales price, this will tend to favour the product's being deemed to originate in the country of manufacture (unless of course there is a dual percentage value test, in which case the value of all components and materials will be compared with the value of the imported ones). Where the manufacturer sells at differing prices to different customers, it would be illogical for the product to be entitled to preferential treatment in one case but not in
the other. However, the possibility does exist. Where the ex-works price is affected, upwards or downwards, by special relations between manufacturer and customer, the price to be taken as definitive is the price on an arm’s-length basis: in other words, the price as it would be adjusted in the case of a declaration of customs value.

It is not necessary to consider the origin of fuel or catalysts needed in operating the production process, and this is confirmed by the explanatory notes to the Lomé II Convention. However, materials actually consumed in the manufacturing process should be considered as parts incorporated in the final product, so that if a non-originating reagent is used in the production of some chemical, the cost of the reagent counts “against” origin being obtained.

It must be stressed that the foregoing examples and calculations are based on the EEC/Israel agreement. Although the philosophy and method of making calculations are the same in other agreements, there are significant differences in each set of rules of origin.

Simple operations inadequate to confer origin

A number of simple processes will not be accepted as conferring origin even if they do bring about a change in the tariff heading of the product in question. The most modern available formulation of these insufficient operations is to be found in the new Lomé Convention:

(a) operations to ensure the preservation of merchandise in good condition during transport and storage (ventilation, spreading out, drying, chilling, placing in salt, sulphur dioxide or other aqueous solutions, removal of damaged parts, and like operations);

(b) simple operations consisting of removal of dust, sifting or screening, sorting, classifying, matching (including the making up of sets of articles), washing, painting, cutting up;

(c) changes of packaging and breaking up and assembly of consignments;

(ii) simple placing in bottles, flasks, bags, cases, boxes, fixing on cards or boards, etc. and all other simple packaging operations;

(d) affixing marks, labels or other like distinguishing signs on products or their packaging;

(e) simple mixing of products of the same kind where one or more components of the mixtures do not meet the conditions laid down in this Protocol to enable them to be considered as originating either in an ACP State, in the Community, or in the countries and territories;

(ii) simple mixing of products of different kinds unless one or more of such components of the mixture meet the conditions laid down in this Protocol to enable them to be considered as originating either in an ACP State, in the Community, or in the countries and territories and provided that such components contribute in determining the essential characteristics of the finished product;

(f) simple assembly of parts of articles to constitute a complete article;

(g) a combination of two or more operations specified in subparagraphs (a) to (f);

(h) slaughter of animals.”

Operations a, b, c and d are fairly straightforward warehousing activities and do not give rise to any particular problem. Operations e and f, simple assembly and simple mixture, can pose more difficult problems. Adding non-originating salt to water to obtain a saline solution is not a complex matter, even although the finished product may have a tariff heading different from its two components. Clipping together a wooden part, a metal part and a plastic part to yield a fourth product may involve a change in tariff heading, but is not a complex operation, and might (depending on the full facts) be caught by the insubstantial exclusion. However, mixing three pharmaceutical active ingredients under precisely controlled temperature, pressure and sterile conditions may well be very complex indeed. It should be noted that the simple assembly rule is deemed to apply only where each of the assembled parts is non-originating, so that the presence of one originating component removes the threat of the rule. It might be tempting to look at each individual operation in a chain of production and argue that each operation taken individually was simple. It is submitted, however, that the better rule is to consider whether or not the entirety of the operations can be viewed as simple, and as a guide to this, to consider whether they could be done domestically by unskilled persons. To the extent that skill, special equipment, special conditions, or a high degree of control and precision are necessary, the finished product should be eligible to be considered under the normal rules of sufficient working and processing, and the provisions on insubstantial operations should not apply.

The older rules of origin have a provision on simple mixing which is less felicitous than the new Lomé Convention rule, and which could unfairly exclude otherwise eligible products if strictly applied:

“Simple mixing of products, whether or not of different kinds, where one or more components of the mixtures do not meet the conditions laid down in this Annex to enable them to be considered as originating either in the Community, in the countries and territories or in an ACP state.”

The 1979 Lomé Convention text should correspond to administrative practice under the other, older, agreements, but it is believed this is not always so. It is submitted that a change to the more appropriate modern rule would be desirable.

The minimal processing exclusion can have effect to deprive products of origin if they otherwise would have qualified. Even if a List A or List B test is satisfied, the origin rules as a whole will not be satisfied. That being said, however, the effect of the Article on minimal or insubstantial processes is very limited: minimal operations cannot confer origin, but they cannot affect origin already attained in the country of manufacture. Thus, labelling an originating product will not remove its preferential origin, although label-
ling alone would not confer it even if, improbably, a labelled product bore a heading different to an unlabelled one.

Summary of ways by which origin may be obtained
Origin may be obtained on the following basis:
(1) Wholly obtained in the country of exportation, that is to say, mined, grown, caught or worked there exclusively from local products and in the country of exportation. No matter how primitive or elaborate the degree of local working, the end product will be entitled to origin.
(2) By sufficient working or processing, if the finished product incorporates parts or materials which do not originate under the wholly obtained rule in the country of exportation. This basic principle can be broken down into the following sub-principles:
   (a) If the finished product bears a four-digit CCT heading different from all the imported non-originating components, parts or materials, there has been sufficient working or processing as a general rule;
   (b) If the finished product figures in List A, it will enjoy originating status only if, as well as the change in tariff heading, the specific positive or negative requirements of List A are satisfied;
   (c) If the product is mentioned in List B, it will, notwithstanding the general principle that a change in tariff heading is necessary, be eligible for originating status if the specific tests laid down in List B are satisfied.

Note
Part I of this Article has reviewed in general terms the significance and structure of the basic origin rules. Part II will describe the specific rules concerning fisheries products, drawback, direct shipment, proof of entitlement to preferential treatment, cumulation, retention and multilateral acquisition of preferential origin; and will consider possible improvements in the rules, particularly those applying to trade between the EEC and EFTA.
EEC Customs Law: Rules of Origin and Preferential Duty Treatment — Part II

By Ian S. Forrester *

The first part of this article noted the economic importance of rules of origin for the EEC's system of preferential trading arrangements, and examined the two basic ways by which a product may be deemed originating for preferential purposes in the exporting country or countries, namely "wholly obtained" from local product and labour, or manufactured through "sufficient working or processing" effected locally on parts and materials which in whole or in part are non-originating. The second part of this article will examine the EEC's preferential rules of origin applicable to fish products and oil products, the rules on drawback, transportation and documentation, and the rather complex problems of cumulation.

Fish products

The origin of a catch of fish for preferential purposes can depend on the waters in which the fish were caught, on the characteristics of the boat doing the catching or on the place where the fish were cleaned, filleted, partially or wholly cooked, seasoned and canned. The rules concerning the status of fish products are quite precisely articulated in each set of rules of origin, and are almost parallel, save that the rules under both Lomé Conventions and under the Maghreb agreements are, as is often the case, more liberal than the others.

We will first examine the rules for wholly obtained status applicable to fish products. Of the 10 categories of products regarded as wholly obtained in a particular country or countries, listed in modern rules of origin, three are relevant to fish: (e) "products obtained by hunting or fishing conducted therein," (f) "products of sea fishing and other products taken from the sea by their vessels," and (g) "products made abroad their factory ships exclusively from products referred to in sub-paragraph (f)." There is no difficulty in finding that a trout caught in a river in Scotland and smoked there is entitled to "wholly obtained" status. However, the application of the rules becomes more difficult when sea fish are involved.

The first Explanatory Note annexed to each of the origin protocols provides that the territory of the exporting state or group of states shall include the territorial waters thereof. As a result, if fish are caught inside

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the territorial waters of a country to whose produce the EEC accords duty preferences, irrespective of the nationality of the catching boat, the fish will be entitled to originating status as wholly obtained in the state whose territorial waters were involved. This provision has the perhaps surprising consequence that an Egyptian boat fishing in Israeli waters would catch fish eligible for EEC duty preferences as originating in Israel.

For fish caught on the high seas, the words "their vessels" are determinative. The various rules of origin stipulate that only those vessels which are closely connected with the beneficiary state or states may be regarded as able to catch originating fish on the high seas. For example, Explanatory Note 4 to the EEC-Israel origin protocol defines vessels in the following terms:

"The term 'their vessels' shall apply only to vessels:
— which are registered or recorded in a Member State of the Community or in Israel;
— which sail under the flag of a Member State of the Community or of Israel;
— which are at least 50 per cent. owned by nationals of Member States of the Community or of Israel or by a company with its head office in one of those States, of which the manager or managers, chairmen of the board of directors or of the supervisory board and the majority of the members of such boards are nationals of the Member States of the Community or of Israel and of which, in addition, in the case of partnerships or limited companies, at least half the capital belongs to those States or to public bodies or nationals of the said States;
— of which the captain and officers are all nationals of the Member States of the Community or of Israel;
— of which at least 75 per cent. of the crew are nationals of the Member States of the Community or of Israel."

Identical (mutatis mutandis) provisions are to be found in all the other protocols, except for three. In the Lomé Convention, the rules on the place of registration, the flag and the ownership of the boat remain virtually the same. However, the requirements as to the nationality of the master and officers and of the crew are different: the rules of origin will be satisfied if "at least 50 per cent. of the crew, captain and officers included, are nationals of States party to the Convention." The Maghreb agreements (with Algeria, Morocco and Tunisia) also contain similarly liberal rules on the nationality of officers and crew. By contrast, the GSP rules of origin are more restrictive. The catching boat must satisfy the flag, the ownership and the normal, more restrictive, nationality require-
ment as to the particular exporting GSP state on its own account, without any other GSP state's contribution. Moreover, Community or mixed Community and GSP boats will not satisfy the origin rules. This provision is in accordance with the general principle that Community products cannot earn GSP preferences on reimportation into the EEC, an issue further examined under Cumulation below.

Factory ships, on board which catches are processed or prepared, are treated on the same footing as fishing boats, provided that they satisfy the applicable flag, ownership and nationality requirements. As a result, frozen or filleted fish prepared and packaged on a factory ship for sale to the consumer can be eligible for originating status as wholly obtained in the country whose flag is flown by the factory ship, provided that the catching boat satisfies the rules of origin and that the factory ship is on the high seas or in its own territorial waters.

Fish which is not eligible for wholly obtained status must be examined under the sufficient working or processing tests. Fresh fish, live or dead, is classified under Chapter 3 of the Nomenclature and processed fish under Chapter 16, so that processing does involve a change in tariff heading. However, the various origin protocols have a List A provision for processed fish in heading 16.04, providing that production from non-originating Chapter 3 products will not confer origin. As a result, fish not originating through being wholly obtained is not eligible for originating status by canning or preserving.

The fishing fleets of developing countries may have difficulty in producing "originating" fish products suitable for consumption on European markets, but the Community has declared its willingness to grant derogations, on a temporary basis, from the rules of origin to fishery products, and has done so on one occasion in favour of canned tuna from Mauritius. The topic of derogations is further examined below.

It should be borne in mind that even if a product is listed in a particular origin protocol, this does not mean that originating goods are automatically eligible for duty preferences, curious though this may seem. The various origin protocols are virtually identical in their provisions, but the trade treaties to which they are attached vary considerably in the products they cover and the duty concessions they accord. Under the rest-EFTA agreements, for example, most food products, including fish, do not enjoy duty preferences. However, the Community has entered into a number of ad hoc arrangements concerning fish products with the Faroe Islands, Iceland, Norway and Portugal, each of which accords some limited preferences to a limited number of fish.

Oil and petroleum products

The Member States have been unable to agree on what rules should be used to determine the origin of oil products, although there are a number of broad similarities. As a result, each of the origin protocols has annexed to it a List C, containing those products excluded from the application of the rules. They include most mineral oils and their derivatives, hydrocarbon fuels and miscellaneous petroleum wastes, additives and derivatives.
In determining the origin of these products, the Member State in which customs clearance takes place applies its own particular rules of origin. Denmark, Germany, the Benelux countries and the United Kingdom (with some variances in the case of Belgium and Luxembourg) consider that minerals originate in the country where they are extracted or from beneath its territorial waters or exclusive economic zone. France and Italy also consider unrefined oils as originating in the place of extraction. However, refined or processed mineral products are assigned origin on quite different theories. Germany and the Netherlands use a test similar to the last substantial economically justified test contained in Regulation 802/68 and examined in the first part of this article. Belgium and Luxembourg use a simpler formulation of the same idea. Italy assigns origin to the country of processing or refining, unless the operation is a minimal or insubstantial one more in the nature of preservation than refinement, in which case origin remains with the country of extraction. Denmark, Ireland and the United Kingdom have their own change of tariff heading test, plus a brief List A and a brief List B. Finally, France insists that even refined mineral oil originates in the country of extraction.

Since List C products are not regulated by the origin protocols, it was until recently the case that the Member States' national certificates of origin were used. The second Lomé Convention and the Yugoslav agreement provide for the use of Community certificates, and the practice will presumably be expanded.

**Drawback**

The classical purpose of free trade agreements was reciprocally to encourage manufacturing, exporting and trading activities among the countries concerned, by according duty preferences. This may sound somewhat commonplace, but it is of significance for the rules concerning drawback, which in the customs context connotes the practice of not collecting customs duties on imported parts or components destined for local processing and onward exportation, or of refunding customs duties already levied on the components once the finished product is exported. In the case of the EEC's most competitive trading partners, the EFTA countries, there are prohibitions on drawback which prevent a finished product from enjoying double preference on importation into the EEC, both from the customs duty which would otherwise have been due in the country of manufacture, and from the EEC duty not levied on originating products. For example, if the Austrian customs authorities were to issue documents attesting to the originating status of items assembled under duty free conditions in Austria, this could lead to the development of an artificial pattern of trade between, say, Japan, Austria and the EEC, whereby Japanese components were shipped to Austria but no Austrian customs duty was levied on them (or duty levied was refunded on proof of exportation of the end products) and they were then assembled for shipment thereafter to the EEC, where no EEC duty would be due if the sufficient working or processing tests were a satisfied. The end product made in Austria would enjoy a competitive advantage over an identical
product made in the EEC, on the Japanese components of which EEC duty would have been levied. The result would be the same if the Austrian authorities were to refund import duty levied on the components on proof that they had been shipped to the EEC, or otherwise out of Austria. Drawback or remission of any kind from customs duty is proscribed by Article 23 of the various rest-EFTA origin protocols, as amended.²

A further explanation of the meaning of drawback is offered in the Explanatory Notes:

"'Drawback or remission of any kind granted from customs duties' shall mean any arrangement for refund or remission, partial or complete, of customs duties applicable to products used in manufacture, provided that the said provision concedes, expressly or in effect, this repayment or non-charging or the non-imposition when goods obtained from the said products are exported but not when they are retained for home use."

There is no prohibition on drawback under the GSP, the Lomé Convention, the arrangements for the Overseas Countries and Territories, the agreements with the Mashraq countries, the Maghreb countries, Cyprus, Malta or Spain, and the Israeli agreement merely provides that the anti-drawback Article will enter into force on January 1, 1984, "Unless the Joint Committee decides otherwise." The rationale for this distinction is that the purpose of trade agreements with developing countries is to encourage and not to hinder trading and industrial activities, whereas in the context of the more highly-industrialised, or competitive, neighbours of the Community it is felt that prohibiting drawback is simply a method of avoiding distortions of trade by obtaining double exemption from customs duties. Article 23 of Annex B of the EFTA Convention (the treaty governing free trade among the EFTA Member States), as amplified by Explanatory Note 8, also contains a prohibition on the granting of drawback in similar terms to the EEC proscription.

A finished product has been tainted by drawback in the sense that the customs authority of the place of manufacture has levied customs duty on the imported components only in the event that the finished product was destined for local consumption, and has not levied duty when the finished product has been exported. In this case, the problem is curable retrospectively by payment of the customs duty remitted or refunded in the place of manufacture, or by the payment of the duty which would normally be due on non-originating products in the country of ultimate destination.

The newly-published agreement with Yugoslavia,³ which is in a number of respects more clearly-drafted than, for example, the EFTA agreements, contains a joint commitment to avoid deflections of trade (Art. 29) and the Community has annexed thereto a declaration reserving the right to request "measures to exclude in respect of worked products the refund of customs duties or the grant of exemption from customs duties in any form whatsoever."

² O.J. 1977 L341/34, for the Austrian example.
³ O.J. 1980 L130/1.
It is perhaps also worth noting that drawback is not prohibited where the commodity accorded the drawback is not entitled to duty preferences under the agreement in question. A Scottish mink farmer might therefore try to claim drawback of duty on grain from the United States which is fed to his mink, whose skins are then shipped to Switzerland as wholly obtained in the EEC. Presumably if this practice gave rise to distortions of trade or competition, consultations would be initiated to resolve the problem.

Finally, there are special EEC customs regimes, beyond the scope of this article, which are analogous to drawback arrangements. Inward processing is the term given to the temporary duty free importation into the Community of products for transformation, assembly or other working. Outward processing is the temporary exportation from the Community of goods for processing elsewhere, and which are then reimported into the EEC on payment of EEC customs duty on the added value. In fact, inward processing is the Community equivalent of a drawback system, since it permits duty free importation of raw materials or components, manufacturing activities and onward shipment without Community duty being payable. In the context of the GSP, since the EEC origin products shipped to GSP countries count as third country elements in calculating added value, for example, an outward processing regime may be a convenient way of achieving manufacture in a low-cost country, with a mitigation of the EEC customs duty consequences (on the added value instead of the full value of the product reimported into the EEC).

End products made in inward processing operations in the EEC may be cleared for consumption in the EEC or in EFTA on payment of the EEC duty not collected on the third country components when they entered the EEC. If they are exported outside the EEC and EFTA, no EEC duty is payable.

Direct shipment

One of the difficulties in administering a system of duty preferences granted upon proof of satisfaction of restrictive origin criteria is the risk that shipments may be substituted and that documentation may be falsified or duplicated. Fraud is made more difficult if goods are shipped directly from the place of their production to the country of consumption. Each of the origin protocols attached to the various preferential trading agreements to which the EEC is a party requires direct transportation. Article 5 of the origin protocol attached to the Lomé Convention states the rules clearly:

"1. Products whose transport is effected without entering into territory other than that of the parties concerned are considered as transported directly from the ACP States to the Community or from the Community or the countries and territories to the ACP States. Goods constituting one single consignment may be transported through territory other than that of the ACP States or the Community or the countries and territories, with, should the occasion arise, transhipment or temporary warehousing in such territory, provided that the
crossing of the latter territory is justified for geographical reasons or the needs of transport and that the products have not entered into commerce or been delivered for home use and have not undergone operations other than unloading, reloading or any operation designed to preserve them in good condition.

Interruptions or changes in the method of transport due to force majeure or consequent upon conditions at sea shall not affect the application of the preferential treatment laid down in this Protocol, provided that the goods have not, during these interruptions or changes, entered into commerce or been delivered for home use and have not undergone any operations other than those designed to preserve them in good condition.

2. Evidence that the conditions referred to in paragraph 1 have been fulfilled shall be supplied to the responsible customs authorities in the Community by the production of:

(a) a through bill of lading issued in the exporting beneficiary country covering the passage through the country of transit;
(b) or a certificate issued by the customs authorities of the country of transit:
   — giving an exact description of the goods;
   — stating the dates of unloading and reloading of the goods or of their embarkation or disembarkation, identifying the ships used;
   — certifying the conditions under which the goods remained in the transit country;
(c) or failing these, any substantiating documents.

The other preferential agreements make similar provision, the result of which is that for a product to be eligible for duty free treatment on importation into the EEC, it must be shipped there in a single voyage or voyages which are reasonably direct from the place of production to the place of customs clearance in the EEC. This does not mean that a product from Peru must move in a straight line round the globe to enter the port of Bordeaux. If there are no regular shipping connections and if air transport is direct but too expensive to be contemplated, the shipment may, for example, be sent by sea first to Los Angeles and there transhipped for the voyage to the EEC. However, it would not be acceptable for the goods to be shipped to Los Angeles, cleared through American customs and then cleared out of the United States once more in order to be shipped to the EEC. Proof must be shown that, so far as may reasonably be expected, the consignment moved steadily and directly from the beneficiary country to the EEC.

However, particularly in the case of shipments from countries where the transport infrastructure is poorly developed, the customs authorities of Member States ought not to be restrictive in examining what constitutes “direct transport.” Provided that they can assure themselves that the goods in question have either been en route or under the supervision of customs authorities in a port or ports of transhipment, no infringement of the direct transport rules should be found.
Proof of entitlement to preferential treatment, certificates and their issuance

In order for a product to be eligible for preferential treatment, it must be accompanied by the appropriate document, describing the shipment's contents, asserting the product's eligibility to preferential treatment as an originating product (but not, other than under the GSP, indicating the grounds for the assertion), and giving other details. This document must be signed by the exporter and endorsed by the customs authority of the exporting country. Although formerly each preferential trade arrangement provided for a different certificate attesting to the origin of products eligible for preferential treatment in the context of that arrangement, there are now only three principal documents, of which one is used for exports from GSP countries and one or other of the remaining two is appropriate for the bilateral or multilateral arrangements to which the EEC is party. The layout, dimension and contents of the forms are prescribed in detail, and they must bear a serial number and green guilloche pattern (anglice: wavy lines) to deter forgery.

Importations under the GSP are accompanied by a Form A Certificate, unless they are of modest value. The Form A is also accepted by the EFTA countries (save Iceland and Portugal, which do not subscribe to the EFTA GSP), Japan, Canada, the United States and Australia for purposes of their own GSP system. The form is apparently straightforward in the information it requires, save that there is a considerable difficulty for the exporter, who must indicate on which theory he considers the goods are eligible for originating status, by means of the code letters A, B, X or P, depending on the circumstances (wholly obtained, change of tariff heading, List A or List B). To assist him, the unfortunate exporter is offered nine lines of text encapsulating the principles set forth in the 50 pages of the two parts of this article. Since this text obviously is inadequate to answer the problems he may have, access to the Official Journal containing the relevant Regulations or to one or other of the national or EEC-sponsored manuals is necessary, but very likely to be impossible. It could well be that the exporter's proper response to the inquiry would be A, B, X, or B and X, or A and B, but he could hardly be blamed for answering A? B? X? or even CUMUL?, a cypher explored in greater detail under Cumulation.

The shorter form APR may be used for shipments, by post, of relatively modest value. The current ceiling for use of the APR is 1,420 European Units of Account (£947). The form is less detailed than the Form A and does not require to be stamped by the exporting authority. In actual practice, the APR form is used rather infrequently. It should also be noted that small consignments (worth less than 90 EUA) not imported by way of trade may be accorded GSP preference without either Forms A or APR being produced.

Although it used to be the case that each bilateral or multilateral

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4 In Yugoslavia, other public authorities are empowered to endorse and verify movement certificates. This is also the case under the GSP.
5 An example may be found at O.J. 1979 L349/47.
6 An example may be found at O.J. 1979 L349/51.
preferential arrangement provided for its own distinctive origin certificate, with the exception of trade between Spain and the original six Member States, where the old-style AE. 1 form (or AE. 2 in the case of small consignments) has not yet been replaced, all other preferential importations into the EEC must now be accompanied by an EUR. 1 or EUR. 2 form.

The EUR. 2 form, which is the counterpart of the APR form, may be used for consignments not exceeding a given value: the ceiling for imports from EFTA is 2,400 EUA and from the second Lomé Convention and Yugoslavia is 1,420 EUA. The ceiling in a number of cases is still denominated in UA instead of EUA, resulting in variations between Member States. There are also provisions exempting consignments of small value (165 EUA for postal packages and 480 EUA for items in travellers' luggage) from the need of even the EUR. 2 form. The EUR. 2 form can, in EFTA trade only, be used for all methods of transport (not just the post).

The EUR. 1 movement certificate is the document to be used in connection with most preferential imports into the EEC. It is short by comparison to its economic significance, and contains no description of the steps by which the shipment became eligible for preferential treatment. However, the application for a movement certificate which is submitted by the exporter when he presents the EUR. 1 for customs endorsement calls for a description of "the circumstances which have enabled these goods to meet the above conditions."

It is up to the exporter to furnish sufficiently convincing proof to the local customs authorities that the processes which he has effected locally are sufficient to confer origin or alternatively that the goods in question satisfy the wholly obtained requirement. The customs authorities of the exporting state should make such inquiries and spot checks as they deem appropriate, and upon being satisfied should stamp the proffered certificate. Provision is made for verification to be effected where the importing customs officers have doubts (or wish to make random checks) about the goods' eligibility for preferential status, and the reverse of the certificates or forms can be used for the inquiry and response.

On occasion, customs officers in countries which are unfamiliar with the technicalities of the rules of origin are reluctant to commit themselves by stamping the EUR. 1 certificate or Form A prepared by the exporter and submitted for countersigning. The Community has been sympathetic to the difficulties of exporters in such circumstances, and has organised a number of visits and instruction programmes for traders and customs officers to explain the workings of the Community's rules of origin, but much remains to be done in this direction. Another inconvenience which exporters may encounter is that the customs officers in the exporting country may wish to be helpful and may be all too ready to issue or endorse certificates attesting to the product's eligibility for preferential treatment. The rules of origin are unquestionably complicated and it is, to say the least, not difficult to make a mistake. The exporter may well be

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7 An example may be found at O.J. 1977 L341/46.
8 An example may be found at O.J. 1977 L341/42.
in perfect good faith in seeking the local authorities' confirmation of the eligibility of his product to preferential duty treatment at the hands of the EEC, or the customs officer may simply misread his instructions, or may have no adequate instructions. This can have serious consequences for the exporter or for his European importer, since the goods in question are not eligible for duty free treatment, and duty otherwise payable has not been paid. It is submitted that the appropriate action to be taken by the importing EEC customs authorities is not unilaterally to deny preferential treatment in doubtful cases, but to seek confirmation of the facts from the exporting customs authorities and if need be to proceed to consultation at the EEC level in Brussels. Where a pattern of trading has continued for several years, assumptions have developed and methods of dealing have become accepted, the importing customs officials should not lightly interfere with such pattern of trading by refusing preferential treatment. Moreover, it would be quite wrong for an importer to be charged or threatened with making a false declaration on the basis of an erroneously issued EUR.1 certificate, unless there were clear indications of fraud in the obtaining of the certificate, or in other very unusual circumstances. The provisions of the French customs code, which tend to find criminal offences in anodyne circumstances where the importer has not been guilty of anything which would be prosecuted as an offence in, for example, the United Kingdom, should not be invoked in circumstances where the worst that can be said of the importer is that he is doing business with an exporter who was issued movement certificates by a customs officer who misunderstood the applicable rules of origin, or even that the exporter, without the importer's knowledge, misrepresented the facts to the customs officer.

If a manufacturer in one EEC country wishes to claim EFTA preferences for his exports, he may need information about components he has purchased elsewhere in the Community, in order to determine his products' eligibility for originating status. For this purpose, he may request his supplier to furnish an information certificate under Council Regulation 1908/73, a document which calls for much of the information the customer/manufacturer needs, but not necessarily all. It is signed by the supplier and endorsed by his customs authorities.

Cumulation

The rules concerning cumulation define the basis on which products originating in the EEC or in a country or countries with which it has preferential trading arrangements may retain or may lose the right to preferential treatment notwithstanding further processing after the original origin has been "earned" or may, even if non-originating, acquire origin. Putting it otherwise, the cumulation rules state the terms on which an end product may enjoy originating status even although the normal origin rules would not confer origin on the basis of the work done in the country of last processing. A simple problem would concern a stone handicraft, made from marble quarried in Italy, carved in Switzerland
and reimported into the EEC. A more complex example would involve a German electric motor shipped to Switzerland for incorporation in the manufacture of a washing machine which is assembled from components originating in Finland, Portugal, Japan and France, then exported to the EEC: on what basis may the washing machine receive preferential treatment?

No cumulation (GSP)

Beginning with the most simple case, that of the Generalised System of Preferences, we find that no cumulation is permitted, save in limited circumstances where regional groupings of GSP countries are involved. Under the GSP, products of Community origin are treated as if they were third country products. If imported and processed in GSP countries, but not sufficiently processed within the meaning of the rules of origin to acquire preferential origin in the particular GSP country, they are not regarded as enjoying preferential GSP origin on reimportation into the EEC. They may perhaps retain non-preferential Community origin under Regulation 202/68, but are not eligible for preferential treatment under the GSP. (It should not be forgotten that an outward processing regime might be the means of alleviating this difficulty.) Moreover, the GSP countries in which working or processing is carried on must satisfy the rules of origin individually, without it being possible for a product to satisfy the rules of origin through processing partly in, say, Brazil, and partly in Afghanistan or, less improbably, in Paraguay. The satisfaction of the rules of origin must be effected in each GSP beneficiary individually, whether the wholly obtained criteria or the sufficient working or processing criteria are being relied upon. Derogations from this principle, but sharply circumscribed derogations, exist in favour of three regional groupings of GSP countries, among which it is possible to retain origin where more than one state makes a contribution to the process of production. Cumulation rules for these regional groupings will be examined further below.

Bilateral cumulation (Mediterranean agreements)

Moving from no cumulation to the simplest form of cumulation, "bilateral cumulation," we examine the agreements with Cyprus, Egypt, Israel, Jordan, Lebanon, Malta and Syria. Under these agreements, preferential origin is accorded by the Community to products wholly obtained in the exporting country, and to products manufactured in the exporting country in the process of making which the non-originating parts and components have undergone sufficient working or processing, as this has been explained, in the first part of this article (change in tariff heading, List A, List B, and so on). However, if the non-originating parts or components worked or processed in the exporting country originate in the EEC, then bilateral cumulation applies, with the result that the requirement of "sufficient working or processing" in the exporting country does not apply to the EEC origin inputs, which can then be considered as wholly obtained in Israel, and the end product is deemed to originate there. For example, where a pharmaceutical intermediate (such as an opiate alkaloid,
BTN heading 29.42) is manufactured in the Community and is then shipped to Israel where it is further refined, diluted, assayed and put in dosage form to make a medicament falling into heading 30.03, the finished product is automatically eligible for preferential treatment on reimportation into the EEC, because the EEC element counts in favour of preferential origin. The percentage rules applying to medicaments (a 50 per cent. added value requirement in List A, and an 80 per cent. added value List B derogation) could not apply to deprive the finished medicament of preferential treatment on its importation into the EEC. The result would be different if the EEC element had come from, say, the United States.

If Japanese electronic components are assembled in Israel to make a loudspeaker falling under heading 85.14, that loudspeaker will be eligible for preferential tariff treatment on importation into the EEC only if there has been a change in tariff heading (i.e. if the finished product bears a different four-digit tariff heading to each of the Japanese components) and if the three percentage value tests described in the first part of this article (total value of non-originating materials not to exceed 40 per cent. of the value of the finished product, 50 per cent. by value of all the components to be originating, and value of the non-originating transistors not to exceed 3 per cent. of the value of the finished product) are satisfied. By contrast, if the components are imported from Germany into Israel and assembled there into a loudspeaker, the finished product on importation into the EEC will be deemed to have Israeli origin even if the value of the German components exceeded the limitations applicable to third country components. If the product is made from EEC, Israeli and Japanese components, the value of the Japanese components must be set against the ex-factory price of the finished product to determine whether the List A tests are satisfied. Mutaatis mutandis, the rule that EEC origin components are credited "in favour" of preferential origin for purposes of satisfying the sufficient working or processing test applies equally to traffic patterns involving exports from the Community to, and reimportation from, Cyprus, Egypt, Israel, Jordan, Lebanon, Malta and Syria. Trade in the opposite direction (such as Cyprus-EEC-Cyprus) is also subject to the same rule, to the effect that preferential origin is not lost if Cypriot parts are processed in the EEC into a finished product which is then re-exported to Cyprus. However, traffic patterns like Cyprus-EEC-Cyprus are likely to be relevant only to trade involving the EEC and Cyprus, Israel and Malta, since only these countries accord reciprocal duty preferences to EEC products.

In the cases of Egypt, Jordan, Lebanon and Syria, EEC exports to those countries do not receive duty preferences because of their EEC origin. Although the rules of origin do provide that Egyptian components imported into the EEC for further processing there need not satisfy the sufficient working or processing rules in order for the finished product to be regarded by Egypt as originating in the Community, the benefits of such recognition are at the moment slight. Trade in the opposite direction (EEC-Egypt-EEC) would probably be done under an Egyptian drawback arrangement, so that no Egyptian duty would be payable, and no EEC duty would be due on the added value (unlike the GSP case where the
absence of bilateral cumulation makes it necessary to use the less favourable method of an EEC outward processing regime).

It should be noted that the cumulation under the seven agreements in question is exclusively bilateral between the Community and the particular Mediterranean country, and there is no possibility of origin being acquired progressively by processing in, say, Lebanon, Syria and Cyprus successively, or in the case of a traffic pattern such Malta-EEC-Israel.

**Total cumulation in a multilateral context**

In the cases of the agreements between the EEC and the three Maghreb countries, "total," "integral" or "full" cumulation is permitted. A product will be eligible for duty free treatment on importation into the EEC as originating in, for example, Morocco if it was wholly obtained in Morocco, or if it was manufactured in Morocco by the sufficient working or processing of parts or components from third countries, or if the finished product is the result of working or processing in Morocco of parts, components or other products manufactured (but not necessarily originating) in Algeria, Tunisia or the Community, or in third countries. Thus, a piece of wood cut down and roughly shaped in Algeria may be further finished in Morocco and carved and painted to yield an ornament in Tunisia: the finished ornament will have Tunisian origin. The result is even more dramatic in the case of products seeking origin on the basis of sufficient working or processing. The effect of Article 1 (2), 1 (3), and 1 (4) of the three Maghreb origin protocols is to make the three countries, along with the Community, one territory for the purposes of satisfying the rules of origin. Article 1 (2) pragmatically states that "... working or processing carried out in Algeria, in Morocco or in the Community shall be considered as having been carried out in Tunisia, when the products obtained undergo subsequent working or processing in Tunisia." Where products originate under the rules due to processing in two or more countries successively, they shall be deemed to originate in the country of last working or processing (unless the last working was one of the minimal operations insufficient to confer origin). A value added test involving the Maghreb countries is thus made by comparing the value of the finished product with the value of the parts or components imported from third countries plus the value of the third country elements in any parts or components imported from the Community, Algeria, Morocco or Tunisia, but not originating there. For example, where a Japanese component is mounted on a board in Algeria, but this does not confer Algerian preferential origin, and the mounted part is incorporated in the production process in Tunisia, the value of the Japanese component imported into Algeria counts against preferential origin being acquired in Tunisia.

The Lomé Convention cumulation rules are the Maghreb cumulation rules writ large. The Lomé Convention countries are regarded as a single territory for purposes of acquiring origin. In other words, a tree cut down in Gabon may be sawn into logs in Niger, roughly finished, in Nigeria, trimmed and sandpapered in Mali, prior to assembly and varnish-
ing in Ethiopia, and will be regarded as a table of Ethiopian origin entitled to Lomé Convention preferences. For purposes of satisfying the sufficient working or processing criteria, the entire group of the Lomé Convention signatories, the PTOM overseas countries and territories and the nine Member States are regarded as one territory, so that the result is the Maghreb system of total cumulation on a much vaster scale. The potential administrative difficulties of this system are considerable, and there is no doubt that monitoring the amount of value added in six different countries could present grave difficulties for the customs authorities of the Lomé Convention countries, and of verification for EEC customs authorities. In practice, however, such dramatic examples of the total system of cumulation prevailing under the Lomé Convention are rare.

It would seem to be possible for a product which is originating on the basis of sufficient working or processing effected in several Lomé Convention countries successively to satisfy any applicable added value test either cumulatively or sequentially. Satisfying the test cumulatively would involve keeping account of the value of the third country components incorporated in the various Lomé countries, and comparing that value with the value of the finished product. Satisfying the test sequentially would involve looking at each Lomé country separately: if the processing carried out on a Japanese part in Gabon is sufficient to confer Gabonese origin on the resulting product, that product when processed in Niger would be of 100 per cent. preferential origin, and the Japanese element would be eliminated from consideration. The sequential and cumulative methods could be combined, so that if the processing in Niger involved the incorporation of a United States component but did not confer Niger origin, the United States part would count against preferential origin being obtained, but the item imported from Gabon would count for all its value in favour of preferential origin being obtained.

The system of total multilateral cumulation, where origin may be progressively acquired in several countries, is to be distinguished from what is often called the "ticket of entry" system, which provides for the retention of origin, subject to conditions, as opposed to its acquisition, when a component has acquired preferential origin in one country and is then further processed in another. As will be seen in due course, the rules on EFTA and on GSP regional groupings follow the latter principle.

Diagonal cumulation (the rest-EFTA agreements)

The most difficult set of cumulation rules is to be found in the rest-EFTA agreements. Bilateral cumulation exists between the EEC and the EFTA countries individually, so that an EEC-Austria-EEC, Austria-EEC-Austria or Austria-Switzerland-Austria traffic pattern is duty free in a straightforward fashion. It is the so-called "diagonal" cumulation rules which are most challenging. The GSP rules on regional groupings echo the most restrictive aspects of these rules, but without the bilateral ameliorations which are available in the rest-EFTA case. The purpose of the diagonal cumulation provisions is to avoid too readily depriving of preferential treatment products which when processed in one EFTA country
undergo working or processing in another EFTA country or in the EEC before onward shipment within the 16 EEC and EFTA countries, and which would otherwise be denied preferential treatment because they did not originate under the origin rules in the country of last processing. Before examining the texts in detail, certain general observations are appropriate.

Trade among the EEC Member States is duty free (until Greek accession); trade between the EEC and each EFTA country is virtually duty free for originating products; bilateral cumulation applies between the EEC and the several EFTA countries individually, and between the EFTA countries, so that a trade pattern such as EEC-Austria-EEC is duty free both at the Austrian border and at the EEC border on the way back. However, since trade among the EFTA countries is also duty free for originating products, there should be a mechanism whereby triangular trade such as EEC-Austria-Finland or Austria-Finland-EEC or Austria-EEC-Finland is rendered economically feasible without the hindrance of customs duty at the second border crossing. Under the normal rules of origin, a product will be eligible for preferential treatment only if the processes which conferred origin were performed in the country of last processing. In the case of an EEC-Austria-Finland traffic pattern, it is clear that if the Austrian processing is enough to confer Austrian origin even without the EEC components counting in favour of origin, the finished product will be regarded by Finnish customs as originating in Austria and will be accorded duty free treatment. However, if the Austrian processing is significant enough to deprive the EEC component of origin but insufficient to confer full Austrian origin under the EFTA Convention's rules of origin (identical in effect to the EEC-EFTA rules), a mitigation of the consequences (Finnish customs duty's exigibility) is provided by Article 2 of the EEC-EFTA rules and of the EFTA Convention.

Article 2 of the EEC-Finland agreement (the other rest-EFTA agreements are, mutatis mutandis, identical) states:

“1. Inasmuch as trade between the Community and Austria, Iceland, Portugal, Sweden and Switzerland, and between Finland and the latter five countries, and also between each of those five countries themselves is governed by agreement containing rules identical to those in this Protocol, the following products shall also be considered as:

A. products originating in the Community: those products referred to in Article 1 (1) (the basic wholly obtained or sufficiently worked or processed text) which, after being exported from the Community, have undergone no working or processing in any of those six countries or have not undergone sufficient working or processing there to confer on them the status of products originating in any of those countries by virtue of provisions corresponding to those of Article 1 (1) (b) or (2) (b) of this Protocol contained in the agreement referred to above, provided that:

(a) only products originating in any of those six countries or
in the Community or in Finland have been used in the course of the working or processing;

(b) where a percentage rule limits, in the List A or B referred to in Article 5, the proportion in value of non-originating products that can be incorporated under certain circumstances, the added value has been acquired in each of the countries in accordance with the percentage rules and with the other rules contained in the said lists without any possibility of cumulation from one country to another;

B. products originating in Finland: those products referred to in Article 1 (2) which, after being exported from Portugal have undergone no working or processing in any of these six countries or have undergone working or processing insufficient to confer on them the status of products originating in any of those countries by virtue of provisions corresponding to those of Article 1 (1) (b) or (2) (b) of this Protocol contained in the agreements referred to above, provided that:

[identical paragraphs (a) and (b)].

2. For the purpose of implementing paragraph I (A) (a) and (B) (a), the fact that products other than those referred to in that paragraph are used in a proportion not exceeding in total value of 5 per cent. of the value of the products obtained and imported into Finland or the Community does not affect the determination of origin of the latter products, provided that they would not have caused the products exported from the Community or Finland in the first place to lose their status of products originating in the Community or in Finland had they been incorporated there.

3. In the cases referred to in paragraph I (A) (b) and (B) (b) and paragraph 2, no non-originating product may be incorporated if it undergoes only the working or processing provided for in Article 5 (3)."

The portions especially relevant to the problems of diagonal cumulation are italicised above. Article 2 of Annex B of the EFTA Convention provides the analogous EFTA language.¹⁰

These texts are of imperfect clarity. The writer submits that it cannot be seriously contended that their meaning is clear. However, there is a high degree of unanimity about the intentions of the drafters of the language in question.

The two critical portions of the cumulation rules in Article 2, each of which has given rise to a distinct family of obscurities and unreasonable consequences, are those italicised "... without any possibility of cumulation from one country to another"; and

"... the fact that products other than those referred to therein are used in a proportion not exceeding in total value 5 per cent. of

¹⁰ The EFTA Convention text is not precisely identical, but in view of its length and the minor differences, it is not set forth here.
the value of the products obtained . . . does not affect the determination of origin of the latter products, provided that they would not have caused the products exported . . . in the first place to lose their status [as originating products] had they been incorporated there.”

Both of these texts apply to triangular trade between the EEC and EFTA such as EEC-Austria-Sweden, Sweden-EEC-Austria, or Austria-Sweden-EEC, and to trade within the three regional groupings of GSP beneficiaries, followed by export to the EEC. We shall for the moment examine the EEC-EFTA situation, since trade between the EEC and EFTA is of course much larger than trade between the EEC and the GSP. The application of the diagonal cumulation rules to the GSP regional groupings is significantly harsher than is the case with EEC-EFTA trade because of the absence of bilateral cumulation in trade between the EEC and the GSP.

Diagonal cumulation: the neutral calculation

Examining the first of the two critical texts in detail, it will be observed that this text applies only to products which in order to obtain origin must satisfy a percentage value added test (whereas the second text applies where a specific processing test or a change in tariff heading test must be satisfied).

Assume that a component of a machine is manufactured in the EEC and that the component satisfies either the wholly obtained or the sufficient working or processing tests to be deemed of EEC origin for purposes of EEC-Austrian trade. The component is then shipped to Austria duty free and is used in the manufacture of a machine. In order for the machine to enjoy preferential Austrian origin, there will normally be a requirement of a change in tariff heading as well as a percentage value added test. Let it further be assumed that the finished machine is subject to a change of tariff heading plus a List A requirement that the value of the non-originating components does not exceed 40 per cent. of the value of the finished product. If the work done in Austria on the EEC component is so valuable that the price of the finished machine is very much higher than the price of the imported components, so that the imported component plus the value of any other non-Austrian components is less than 40 per cent. of the value of the finished machine, it is clear that the finished machine will have Austrian origin whether it is shipped to the EEC or Sweden, and that it will be entitled to duty free treatment on the basis of having earned what might be called “full” Austrian origin.

In the event that full Austrian origin is not acquired, but no third country element is incorporated in the process, the machine will still be entitled to duty free treatment on importation into the EEC because of the fact that there is bilateral cumulation in EEC-Austrian trade.

The diagonal cumulation rules apply when the product has not acquired full Austrian origin, and is then shipped on to another EFTA country. The linguistic and philosophical difficulty of the diagonal cumulation system
may be seen when a machine (not being entitled to full Austrian origin on the basis of work done in Austria or Austrian components incorporated) is shipped to Sweden. The "without any possibility of cumulation from one country to another" language quoted above is interpreted by Commission and by national experts as meaning that in determining the eligibility of the Austrian machine to preferential treatment on importation into Sweden, the appropriate calculation is not to compare the ex-factory value of the machine with the value of any United States or Japanese parts incorporated in Austria (so that the EEC component counts "in favour" of origin), but is on the contrary interpreted as meaning that the EEC component shall count "neutrally," neither in favour of origin nor as a wholly non-originating component counting against origin. To apply the principle, the value of the EEC component is deducted from the ex-factory value of the machine in Austria and the resultant diminished value must then be compared with the value of any third country parts or components.

The result is that the amount of third country components which may be incorporated into the machine in Austria without detracting from eligibility for Austrian preferential origin is lower than would be the case if the EEC component counted "in favour" of preferential origin. For example, if the EEC component is worth 50 and in Austria it is incorporated into an Austrian machine whose ex-factory value is 100, and if in the process United States components worth 25 are incorporated, the machine will be eligible for duty free treatment on reimportation into the EEC, because the non-qualifying components are worth only 25 of the 100 of ex-factory value (bilateral cumulation meaning that the EEC part counts in favour of preferential origin). It will not be eligible for preferential treatment on importation into Sweden because the EEC element of 50 would be disregarded in the calculation, with the result that the United States element would be worth 50 per cent. of the value added in Austria, disqualifying the finished machine from preferential treatment on importation in Sweden. When an Austrian component is incorporated in making a machine in Sweden which is in turn shipped to the EEC, or when the Austrian component is incorporated into a machine in the EEC which is then shipped to Sweden, the result is, mutatis mutandis, the same as in the EEC-Austria-Sweden example just analysed.

Curiously, the appropriate document which should accompany the product moving in a triangular traffic pattern and entitled to originating status because of the application of the diagonal cumulation rules is a movement certificate applicable to trade between the first and third points in the triangle, but issued by the customs authorities of the second. For example, in the case of a pattern such as EEC-Austria-Finland, the goods would be accompanied on the Austria-Finland leg by an EUR 1 form for EEC-Finland preferential trade, issued by Austrian customs. Conversely, for a traffic pattern such as Finland-EEC-Austria, the appropriate document is an EFTA Convention document issued by customs authorities in the Community. This paragraph assumes that the product's origin remains in the country of first processing. If full origin is acquired in the
second country, or if the allocation rules (examined further below) assign origin to the second country, the appropriate document would be the normal certificate applying to preferential trade between the second and third country.

The decision to structure the diagonal cumulation rules in this fashion, and to adopt the neutral cumulation system was not inadvertent. It was a political decision not to accord full access to preferential treatment to triangular trade touching two EFTA countries and the EEC.

The writer has a number of observations. First, and most obviously, the system of diagonal cumulation with the positive, negative and neutral calculation does not appear to be compelled by the wording of the texts. The language “without any possibility of cumulation from one country to another” might mean a number of things. For example it could mean that once could not successively accumulate preferential elements by adding to an EEC origin product in Finland a component that was 90 per cent. third country and only 10 per cent. Finnish, then adding some Swedish inputs, some Norwegian inputs and some Austrian inputs to arrive at the end of the day at a situation where the finished product had only 40 per cent. of United States components and would be eligible for preferential treatment in Portugal, despite the fact that preferential origin had not been retained in each country. With ingenuity, an assortment of other interpretations could be offered. There is no doubt that the present experts and the original drafters are agreed that the text was meant to provide for neutral cumulation, but the writer strongly submits that the system of neutral cumulation, as intended by the drafters and as applied and interpreted by senior national and Community experts, does not necessarily flow from the words in question.

Secondly, a reason for not permitting totally free trade between EFTA and the EEC for all products originating in the EEC or in an EFTA country and for machines incorporating such products is that it could lead to abuses. For example, it has been argued that where a machine is assembled in the EEC from five components, each coming from a different EFTA country and each incorporating Japanese materials worth 40 per cent., the Japanese value built into the finished EEC machine could be very substantial, yet the finished machine would unequivocally count as entitled to EEC origin on shipment to Portugal. However, if a manufacturer in the EEC or in an EFTA country chooses, he may at the moment treat each sub-component separately and as fully entitled to origin. In other words, the practice supposedly guarded against can at the moment be pursued in a single factory in a single country. The concept of subdividing each step in the production process to secure better results from the point of view of preferential origin is examined further below.

Thirdly, when applying the neutrality concept, any EEC component incorporated in the finished product in Austria is disregarded for purposes of the calculation, even if the EEC component was wholly obtained in the EEC, or even if there were only a tiny percentage of non-EEC components incorporated into it. There is no logical justification for assuming that the abuse is the norm and disqualifying from preferential
origin a product in the following circumstances: EEC component worth 80, assembled with a United States component worth nine in Finland to produce a machine which has an ex-factory value of 100. Of the inputs into that machine 91 per cent. would be associated with the Community or with EFTA and yet it would not be eligible for duty free treatment on importation into Sweden, since the third country element would exceed 40 per cent. of the value added in Finland.

Diagonal cumulation: the triangular 5 per cent. rule

The second family of complexities afflicting the origin of products moving in triangular traffic patterns is to be found in connection with products which must satisfy a specific processing requirement, as opposed to a percentage value added test, in order to acquire preferential origin. The rule is particularly important in the textile sector, where a mere change in tariff heading is insufficient to confer preferential origin, and two steps (such as spinning and weaving) are necessary to confer origin. For example, making up non-originating cloth into garments does not confer preferential origin under any of the sets of rules of origin, as the List A requirement concerning finished garments would not be satisfied.

The rule (which, for lack of better terminology, will be referred to as the triangular 5 per cent. rule) is confined to cases where there is no attempt to satisfy a percentage added value test and where the processing in the second country (the first country being the place of production of the part, the second being the place of incorporation of the part into the end product, and the third being the place of importation where the end product’s eligibility to preferential treatment is in question) almost but not quite incorporates only EEC or EFTA origin parts, or both. The triangular 5 per cent. rule means that the finished product will not lose preferential status if non-originating (say, Japanese) third country materials are incorporated, provided that such materials are not worth more than 5 per cent. of the value of the finished product, and provided that if the non-originating materials had been incorporated in the first country in the triangle, the product made in the first country would still have been eligible for originating status on importation into the second country. The best examples of the rule’s application are to be found in the textile sector.

A man’s cotton shirt (BTN heading 61.03) is subject to a List A specific processing requirement in each of the rules of origin, to the effect that manufacture from non-originating cotton fabric (BTN heading 55.09) will not confer origin, but manufacture from non-originating yarn (BTN heading 55.05 or 55.06) will confer origin. Putting it otherwise, only manufacture from originating fabric will confer origin on the finished shirt. Assume that fabric is made in Austria from originating yarn or from yarn spun there, the fabric is shipped to Finland to be made into a shirt, and the shirt is then shipped to EEC. The shirt will have preferential EFTA origin on entry to the EEC. However, if the Finnish shirtnaker uses United States buttons, the triangular 5 per cent. rule comes into play. If the buttons are worth more than 5 per cent. of the finished shirt it will be deprived of preferential origin. If the buttons are worth less than
5 per cent., it is necessary to examine whether incorporation in Austria into the Austrian product shipped to Finland would have deprived that product of Austrian preferential origin. Since fabric with buttons sewn on (improbable and pointless though such needlework would be) would be classified as fabric, and since the non-originating buttons would therefore bear a different tariff heading than the finished product, the requirements of List A, both as to change of tariff heading and specific processing (manufacture from yarn or raw cotton), would have been satisfied.

Likewise, if the cloth were dyed in Finland with Indian dye (BTN heading 32.04) worth less than 5 per cent. of the value of the finished shirt, preferential origin would not have been lost, as although dyeing non-originating cloth does not confer origin (no change in tariff heading), dyeing does not remove origin once attained.

However, the result would be different if the Finnish manufacturer decided to trim the shirt with especially high-quality cotton fabric (BTN heading 55.09) made in North Carolina. Even if the trimming were worth less than 5 per cent. of the value of the finished shirt, its incorporation would deprive the shirt of origin, since the trimming would originate in a third country and would have the same tariff heading as the Austrian cotton fabric. The incorporation in Austria of fabric not derived from cotton fibres in Austria would mean that the finished fabric would not bear a four-digit tariff heading different from each of the non-originating materials used in making it. As a result, the shirt made in Finland would not have preferential origin on export to the EEC.

There are a number of comments to be made about the triangular 5 per cent. rule. First, it does not appear to flow naturally from the words of Article 2 (2) and Article 2 (3) of the origin protocols, although concededly it is easier so to interpret it than is the case with the neutral calculation and Article 2 (1) (A) (b). Secondly, the 5 per cent. figure is very low indeed: a final product which seeks originating status on the basis of a specific processing rule or change of tariff heading rule is entitled to only 5 per cent. of third country content, whereas a product seeking originating status on the basis of a value added test in List A will usually retain origin up until 40 per cent. of the content is non-originating. The fact that the rule applies above all to textiles, a sensitive product, may explain its rigour. Thirdly, the manufacturer in the second country who buys parts or materials from the first country may not know how the first country's manufacturer satisfied the origin rules, and the latter may be reluctant to tell him for reasons of trade secrecy or otherwise. It may thus be difficult for him to know whether the incorporation in the first country of the non-originating parts he wishes to incorporate in the second country would have deprived the first country's output of originating status.

Bilateral and diagonal cumulation combined (EFTA)

Apart from the uncertainties and peculiarities about the working of the neutral calculation and the triangular 5 per cent. rules, there can be
difficulties under bilateral cumulation between the EEC and EFTA. If an Austrian manufacturer uses an EEC part in the production of a machine, the machine has preferential origin on reimportation into the EEC, because of the bilateral cumulation available to EEC-Austria-EEC trade, even if the value of the EEC part is very large. However, if the part incorporated is a Swiss part, the neutral cumulation system applies and the machine may lose origin if the value added in Austria is not high enough to confer full Austrian origin or to retain preferential origin by the operation of the neutral calculation. If both a Swiss and an EEC part are incorporated, the EEC element benefits from the bilateral cumulation rule, but certain authorities hold that the Swiss element may not do so, since EEC-Switzerland-EEC cumulation is governed by the Swiss-EEC agreement, and it is not theoretically acceptable for a single shipment to be governed by both the EEC-Switzerland and the EEC-Austria agreements, as the product may be accorded Swiss or Austrian treatment, but not both. It is submitted that there is no reason why a shipment may not benefit simultaneously from two agreements which are absolutely parallel and which form part of a supposedly homogenous network of free trade arrangements covering 16 countries.

Allocation of origin among one of several countries

It has been noted that products to whose manufacture more than one EFTA, Maghreb or Lomé Convention country has contributed are assigned origin in a particular country, and are not accurately described as enjoying, say, EFTA origin. The country of last processing will be the country of origin if full origin is conferred. However, if full origin is not gained, origin remains with the first country of processing unless it is located elsewhere by the operation of Article 3 of the EFTA origin protocols on the basis of the highest percentage of value contributed to the final product in the various countries of processing. The distinction will not usually have any real significance for the trader, since the product will be entitled to preferential treatment in any event. However, it might be important if safeguard measures, quotas or anti-dumping measures were taken against, say, artificial fibres originating in Switzerland: if the fibre originated in the EEC it would be immune from such measures.

By contrast, the Lomé Convention and the Maghreb agreements provide that origin shall be assigned to the country of last processing (provided that such processing is not one of the insubstantial processes insufficient to confer origin). However, where one or more GSP countries in a regional grouping contribute to the end product, the allocation of origin is made, as in the EFTA case, to the country contributing the highest percentage of value, a distinction of considerable importance when ceilings and other quantitative restrictions are involved.

Diagonal cumulation among GSP regional groupings, with no bilateral element

The diagonal cumulation rules just described in the context of EEC-EFTA trade apply also to cumulation among the three GSP regional
groupings which are permitted, in derogation of the general GSP rule, a
degree of co-operation in producing a finished product.

The groupings are the Association of South-East Asian Nations (ASEAN),
the Central American Common Market, and the Andean group, comprising
respectively the following countries: Indonesia, Malaysia, the Philippines,
Singapore, Thailand; Costa Rica, El Salvador, Guatemala, Honduras,
Nicaragua; Bolivia, Colombia, Ecuador, Peru, Venezuela. The effect of the
regional cumulation provision is to permit preferential GSP origin to
be retained where, for example, a product is made in Indonesia which
satisfies the GSP rules or origin, and then undergoes further processing
in Malaysia. If the Malaysian processing is sufficiently extensive to confer
Malaysian GSP origin, no problem would arise in any event. However,
if the Malaysian processing were insufficient to confer Malaysian origin,
as a general principle the product would have lost its Indonesian origin
through the processing in Malaysia, and would have acquired any other
GSP preferential origin. The regional cumulation provision in favour of
the ASEAN countries means that the finished product can retain preferential
GSP provided that either the triangular 5 per cent. rule or the neutral
calculation rule, as the case may be, is satisfied.

This means that if the product last processed in Malaysia is eligible
for origin on the basis of a specific processing rule, or a change in tariff
heading, any non-originating elements incorporated in Malaysia must not
exceed 5 per cent. of the value of the finished product, and must not
have deburred the Indonesian element from Indonesian origin had they,
improbably, been incorporated in Indonesia.

If the product last processed in Malaysia and incorporating an Indonesian
input is subject to a value added percentage rule, the same curious
interpretation of the diagonal cumulation language first inserted in the
EEC-EFTA agreements is applied by the EEC, despite some incredulity
on the part of the GSP states. As a result, the value of the finished
product is reduced by the value of the Indonesian element and any other
ASEAN inputs, and the resulting reduced value is compared with the value
of any non-ASEAN parts or materials. Only if the value of the non-
originating items is below the maximum allowed percentage will the
finished product be entitled to the endorsement “ASEAN Cumulation”
on the Form A origin certificate.

The position of the regional groupings is in fact worse than the EFTA-
EEC situation as regards cumulation, since no bilateral cumulation exists
under the GSP. (Japan and certain other countries operating a GSP do
permit what the EEC would call bilateral cumulation, calling the home
country input the “donor country element.”) The following example
demonstrates how strange can be the result: a product subject to a change
in tariff heading test and a List A percentage rule of 40 per cent. is
assembled in Singapore and has an ex-factory value of 100. It is assembled
from an EEC component worth 29, an Indonesian component worth 15,
Malaysian wire worth seven, a Philippine plastic casting worth eight and
a Japanese valve worth 16. Labour, overheads and profit in Singapore
account for 26. The value of the non-Singapore ASEAN parts is deducted
from the value of the finished product, leaving 70, of which 40 per cent. is 28. The total value of the EEC and the Japanese elements is 45, far more than the permitted ceiling, even although only 16 per cent. of the value of the finished product is associated with a third country. Even if the EEC element worth 29 had come from Indonesia, so that 59 was the value of non-Singapore ASEAN inputs, 16 the value of the Japanese input, and 100 the final value, the result would be very close: the 59 would be deducted from 100, leaving 41, of which 40 per cent. is 16.25, only 0.25 above the value of the Japanese element worth 16. On this hypothesis the product would depend for originating status on exchange rate fluctuations, tiny variations in the cost of raw materials and so on, and could enjoy origin in some weeks but not in others. The manufacturer could place himself out of harm's way by increasing the price of the end product, but this route may not be commercially acceptable.

Whether or not because of the restrictiveness of the cumulation rules, the use of the regional grouping provisions has been sparing. It appears that, particularly in the case of the ASEAN countries the provisions are used mostly in connection with the direct transportation rule. Since Singapore's port facilities are very advanced, many Malaysian and other ASEAN countries' products are shipped through Singapore to European markets.

Summary of cumulation rules

A product originating in the EEC, exported to an EFTA country, and reimported into the EEC, is accorded duty free treatment. The converse is also true. A Cypriot, Israeli or Maltese product imported into the EEC, or an EEC product imported into Cyprus, Israel or Malta, may make the return journey on a preferential basis, and the same is theoretically possible for trade with the Mashreq countries but practically less likely. There is no EEC-GSP-EEC cumulation of origin.

There is total cumulation among the Maghreb countries and the EEC, and among the Lomé Convention countries and the EEC. The Maghreb group and the Lomé Convention countries are in fact each regarded, with the EEC, as a single territory for purposes of satisfying the rules of origin.

Cumulation, other than bilateral cumulation, among the EFTA countries and the EEC bristles with complications. Where a triangular traffic pattern exists, the diagonal cumulation rule applicable to the finished product varies depending on whether the product is eligible for originating status on the basis of satisfying a percentage added value test or a change in tariff heading or specific processing test. In the former case, the "neutral" calculation is made, whereby inputs other than from the country or countries at the first corner of the triangle are counted either against origin (third country elements); or neither for origin nor against it (inputs elsewhere than from the three corners of the triangle, for example, from other EFTA countries); and only local inputs (or further inputs from the first corner if bilateral cumulation is available) count in favour of origin. In the latter case, the value of the non-originating input may not exceed 5 per cent. of the value of the finished product, and the inclusion of
the input in the production process in the first country should not have removed origin from that first country’s export.

The same rule is deemed to apply to the GSP regional groupings, but without the redeeming feature of bilateral cumulation.

The cumulation rules for triangular trade as expressed in the texts do not, it is submitted, necessarily support the exotic construction placed on them, and their results are often illogical.

**Derogations**

The Lomé Convention countries in particular have urged that the EEC should liberalise its rules of origin, and did propose that the non-originating parts’ value should be permitted to rise as high as 75 per cent. of the value of the finished product. The EEC has declined to abandon its established practices in a generalised fashion, but has indicated its willingness to consider application for specific derogations in appropriate cases. Article 30 (1) to (4) of the second Lomé Convention states:

“1. Derogations from this Protocol may be adopted by the Committee where the development of existing industries or the creation of new industries justifies them. The ACP State or States concerned shall, either before or when the ACP States submit the matter to the Committee, notify the Community of its request for a derogation together with the reasons for the request in accordance with Explanatory Note 10.

2. The examination of requests shall in particular take into account:
   (a) the level of development or the geographical situation of the ACP State or States concerned;
   (b) cases where the application of the existing rules of origin would affect significantly the ability of an existing industry in an ACP State to continue its exports to the Community, with particular reference to cases where this could lead to cessation of its activities;
   (c) specific cases where it can be clearly demonstrated that significant investment in an industry could be deterred by the rules of origin and where a derogation favouring the realization of the investment programme would enable these rules to be satisfied by stages;

(3) In every case an examination shall be made to ascertain whether the rules relating to cumulation of origin do not provide a solution to the problem.

(4) In addition, when a request for derogation concerns a least developed ACP State, its examination shall be carried out with a favourable bias having particular regard to,
   (a) the economic and social impact of the decision to be taken especially in respect of employment;
   (b) the need to apply the derogation for a period taking into account the particular situation of the least developed ACP State concerned and its difficulties.”

E.L.R. (4)—4
Derogations are usually granted where the exporting country has a developing industry still dependent on third country labour or materials, but with the prospect of becoming more independent in the foreseeable future. The Community's policy is to grant derogations on a year-by-year basis, to enable the new industry to develop a market in the EEC at the same time as it moves towards full compliance with the rules of origin.

Derogations have been accorded to fishing flies from Malawi and Kenya, canned tuna from Mauritius, textiles from Morocco, and to stewed steak, tape recorders, transformers, radios, and chocolates from Malta. The Maltese derogation was principally in compensation for Malta's loss of certain Commonwealth preferences.

Approved exporters; integrated manufacturing operations

The rules of origin contain a number of special features of particular interest to manufacturers or exporters of products in large quantities. First, under Article 13 of the EFTA origin protocols as amended, the "approved exporter" scheme is established. Exporters making frequent shipments who are able to offer "all guarantees necessary to verify the originating status of the products" may be authorised by their local customs authorities to complete movement certificates which have been pre-endorsed with the necessary stamps or signatures. The exporting customs authority is given the widest discretion in imposing such restrictions or conditions on approved exporters as it may deem appropriate. The approved exporter scheme has points of similarity to the pre-enlargement EFTA system of invoice declarations. Moreover, since it would be impossible in any event for every transaction to be individually verified, the scheme merely corresponds to practical reality.

For manufacturers of a range of products incorporating inputs from the EEC, EFTA and third countries in varying proportions, keeping track of the preferential status or otherwise of the finished product can pose considerable difficulties. If an EEC manufacturer buys copper wire from a Spanish supplier and a German supplier, or uncombed wool from farmers on both sides of the Pyrenees, the originating status of his end product for EEC-EFTA trade may vary. The manufacturer may try, if he has the accounting and administrative resources to do it, to follow the progress of each batch of originating materials through into the end product. Alternatively, and more pragmatically, he may simply note that over a given period, two-thirds of the materials used out of his stock were originating and deduce that two-thirds of the end product were in consequence originating. Indeed, it is difficult to see what other solution exists if the materials are commingled: a fabric can hardly be two-thirds

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12 O.J. 1979 L117/1.
13 O.J. 1979 L71/2.
15 Because of their vestigial importance, this article will not examine a kind of quasi-derogation from the normal rules of origin for trade in certain products between EFTA, Denmark, and the United Kingdom, which are set forth in Art. 25 of the amended EFTA origin protocols.
originating. In summary although the rules imply that segregation is required, in fact it may be impossible and should not be necessary.

The manufacturer of a product which is itself a combination of a number of sub-products (such as a radio, vacuum cleaner or the like) may choose to examine the origin of the final product as a whole, by comparing its value with that of the totality of non-originating components. Alternatively, he might find it more advantageous to examine the origin of each sub-product before its incorporation into the final assembly process. By this means, any non-originating value in an originating component is eliminated from consideration, and the component rates as 100 per cent. originating for the final calculation of the origin of the end product. This procedure of sequential review of origin of every discrete sub-component is certainly legitimate (although it may well be unpopular with competitors) where the sub-components have a distinct existence, albeit a brief one. However, is it legitimate where the operation is entirely integrated and automated, so that the sub-components exist only momentarily inside an assembly machine?

Proposals for reform

**EEC-EFTA negotiations**

The EFTA Convention as originally established accorded EFTA origin to goods which were wholly produced, produced by specified qualifying processes, or were made from non-originating "Basic Materials" or if the value of any non-originating components was 50 per cent. or less than the export price of the finished product. During the negotiations of the free trade agreements between EFTA and the EEC in 1971 and 1972 prior to the reorganisation of the Community's trading relationships in light of the accession of Denmark, Ireland and the United Kingdom, it was insisted upon by the Community that both the EEC and EFTA should follow the same rules of origin if there was to be free trade between the various EFTA countries themselves and between EFTA and the EEC. The representatives of the EFTA countries agreed, not without reluctance, to abandon their straightforward 50 per cent. value added rule, to adopt the more complex EEC system based on the change in tariff heading plus specific tests for particular products, and to abandon the EFTA system of invoice declarations.

It was agreed that the system of EEC-EFTA rules of origin would be reviewed in the light of experience, and in due course, in April 1975, the EFTA side recommended three major changes. Specifically, it was proposed that the diagonal cumulation system should be drastically changed, and for all products except textiles there should be an additional, optional, means of obtaining origin on the basis of 50 per cent. added value. The third proposal made by the EFTA countries was to simplify the documenta-

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14 The criticisms of, for example, the Austrian side, are set forth in some detail in the GATT's basic instruments and selected documents, Supp. 20, pp. 152-156 (1973). Similar criticisms were made by other EFTA countries, and by the U.S.A. which claimed the rules deterred the incorporation of U.S. materials.
tation necessary to entitle products to originating treatment, and to readopt the former EFTA system by using instead of a certificate of origin a declaration by the manufacturer or exporter on the invoice itself. It was generally conceded that the EEF-EFTA rules of origin needed improvement, and that complying with them did cause expense for manufacturers and traders and could have unreasonably restrictive consequences in particular cases. However, various Member States felt that the EFTA suggestions were too radical in moving to a 50 per cent, value added rule for nearly all products, and nearly all Member States were reluctant to accept the greatly simplified cumulation rules proposed by EFTA.

After extended discussion, the Commission took up the idea of moving to an alternative value added test for all machinery products (Chapters 84 to 92), where a value added test is particularly appropriate and where Lists A and B can be unworkable or produce unreasonable consequences. The Commission considered that the EFTA proposal should be further limited by moving to a 60 per cent, value added test instead of a 50 per cent, added value test for most products in Chapters 84 to 92, and a 70 per cent, value added test for a number of other products. On January 11, 1979, the Commission submitted to the Council a number of proposals for the reform of the rules of origin between the EEC and EFTA. The proposals would add an optional alternative means of acquiring origin for products falling into BTN headings 84 to 92, whereby if the value of non-originating components incorporated in the finished product is 40 per cent, or less of the value of the finished product (in most cases) or 30 per cent, of the value of the finished product (in the other cases), the product would have origin. If the product was eligible for origin under the existing rules, it would retain that origin.

In addition, the Commission proposed the abolition of the neutral calculation system and of the triangular 5 per cent, rule. Thus, in making an added value calculation, the value of the finished product would be compared, without deduction of "neutral" elements, with the value of parts, materials or components originating outside the EEC and EFTA. This would be an expansion to the multilateral context of bilateral cumulation. In applying a specific processing rule, one would simply compare the finished product with each of the parts or materials not originating in the EEC or EFTA.

The adoption of the Commission proposals in the near future is appropriate and desirable, and it indeed appears difficult to formulate persuasive objections. From the historical point of view, it may be noted that the system is not without precedent in Community experience, as the Yaoundé Convention cumulation rules were in some way comparable. The purpose of the rules of origin within the sixteen countries concerned should be to enhance trade between these countries and not to create artificial hindrances by depriving products of origin following complex calculations leading to results which could only be described as capricious. Whether a product or component originates in the EEC or originates in an EFTA country, the applicable trading rules should encourage the use of that product in making a machine in another EFTA or EEC country and the
onward shipment of that machine elsewhere for incorporation into yet another machine. The existing rules of origin tend to distort legitimate patterns of trade by the need to accommodate the needs of the rules, instead of enhancing trade while restraining abuses. They act as deterrents to complete freedom of trading across borders in Europe.

GSP reforms

The rigour of the neutral calculation system and the triangular 5 per cent. rule seems to be quite at variance with the Community's expressed intent of enhancing trade among the regional GSP groupings, and the extreme difficulty for the customs authorities of the developing world in understanding the rules must be acknowledged. Even if the EEC is unable for political reasons to accord total cumulation to the regional groupings on the style of the Lomé Convention, at the very least it should embark vigorously on a campaign of information, and should review to what degree the strictness of the diagonal cumulation rules can be mitigated.

Clarity and Intelligibility

Even if the legislative text proposed by the Commission is accepted, it will not make the rules of origin as they appear in the Official Journal intelligible or coherent. The concepts explained in this article and its predecessor are not impossibly difficult. It should be possible for the Community to agree on a text which clearly explains the working of the rules of origin to the trader. The explanatory notes appended to the various sets of rules of origin have grown longer and longer perhaps as awareness has spread of the public's uncertainty as to the rules agreed among national and Community experts. The rules at the moment are doubtless understood by senior customs officials and by many junior customs officials, but they are not intelligible for the trader or the trader's legal adviser. This situation should be remedied: even if it does not involve a complete rewriting of the legislative texts, a booklet of guidelines should be prepared which is authoritative and clear, giving practical examples. It is further suggested that the organisation of the rules of origin could be improved by grouping arrangements for administrative co-operation, documentation, transportation and the other rules in a logical sequence. The Lists A and B between them currently contain two positive lists and one negative list. As noted in Part I of this article, these three lists are a pastiche of Member State suggestions for lists, and continue to this day merely because no political initiative has been taken to adopt a single list. Although the new Yugoslav agreement is an improvement in drafting and coherence upon its predecessors, room for considerable further improvements remains. The predecessors also remain and should be clarified.

Conclusion

There is a natural wish to see Community rules clearly and intelligibly expressed to the extent this is possible, and this of possible, and this is of course difficult when 16 countries (plus the candidates Greece and
Spain) and six (or nine) languages are involved, and when there are doubt-
less shortages of time, staff and resources. The officials in the Customs
Union Service of the Commission are not unaware of the obscurities of
the rules of origin, and are extremely helpful and patient in answering
inquiries, but their job would be considerably eased if the texts were more
intelligible, or if there were published guidelines in default of agreement
on legislative texts. It should be recorded that although the writer warmly
and gratefully acknowledges counsel, criticisms and suggestions extended
to him by Customs Union officials and others in the course of preparing
this article, and on many other occasions, he is alone responsible for the
article's contents.

The beginning of Part I of this article alluded to the trials of Lady
Grisell Baillie in copying with customs barriers in the Europe of the
eighteenth century. It would be an exaggeration to compare her difficulties
to those of the manufacturer or importer dealing with the rules of origin.
However, in the Europe of the 1980s it ought to be possible for the
Community to do better.