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Significance of Rules of Origin in European Union's unilateral Generalised System of Preferences (GSP) for *Everything But Arms* system's beneficiaries[1]

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Abstract
Least developed countries (LDC) play marginal role in the global economy and in the global trading system. The international community has introduced a series of initiatives to provide these countries with more favourable market access conditions. One of them is the European Union's programme – the *Everything But Arms* (EBA) scheme providing duty-free and quota-free market access to all products except weapons and ammunition. Conditions for access to the EU market, are contingent not only upon the level of customs duty rates, but also rules of origin (RoO), as it is the latter that determines whether a lower rate of customs duty can be applied to imported goods or not. This article's aim is to assess the significance of the rules of origin of goods in the European Union's unilateral Generalised System of Preferences for the EBA system's beneficiaries, with special attention given to changes introduced in 2011. To meet the objective hereof, not only empirical methods were employed (indirect observation and description), but also general methods, including deduction and induction. The following research techniques were used: a cause and effect analysis, a comparative analysis and synthesis. The research is based on statistical data provided by Eurostat and UNCTAD.
Keywords: rules of origin, Generalised System of Preferences (GSP), *Everything but Arms* (EBA), the European Union (EU), least developed countries (LDC), customs duty.

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Znaczenie reguł pochodzenia towarów w Powszechnym Systemie Preferencji (GSP) Unii Europejskiej dla beneficjentów systemu *Everything but Arms*

Streszczenie

Kraje najsłabiej rozwinięte (LDC) nie odgrywają znaczącej roli w gospodarce światowej. Podjęto szereg inicjatyw, aby zapewnić tym krajom korzystniejsze warunki dostępu do rynku. Jednym z nich jest unijny program – inicjatywa *Wszystko oprócz broni* (EBA), zapewniająca bezcłowy i bezkwotowy dostęp do rynku wszystkich produktów z wyjątkiem broni i amunicji. Warunki dostępu do unijnego rynku uzależnione są jednak nie tylko od poziomu stawek celnych, ale także od reguł pochodzenia (RoO), gdyż to od tych ostatnich zależy możliwość zastosowania niższej stawki celnej stosowanej do towarów importowanych. Celem artykułu jest ocena znaczenia reguł pochodzenia towarów w ramach jednostronnego Ogólnego Systemu Preferencji Unii Europejskiej dla beneficjentów systemu EBA, ze szczególnym uwzględnieniem zmian wprowadzonych w 2011 roku. Aby osiągnąć postawiony cel, zastosowano nie tylko metody empiryczne (obserwacja pośrednia i opis), ale także metody ogólne, w tym dedukcję i indukcję. Zastosowano następujące techniki badawcze: analizę przyczynowo-skutkową, analizę porównawczą i syntezę. W badaniu wykorzystano dane statystyczne Eurostatu i UNCTAD.

Słowa kluczowe: reguły pochodzenia, Powszechny System Preferencji (GSP), Wszystko oprócz Broni (EBA), Unia Europejska (UE), państwa najsłabiej rozwinięte, stawka celna.

Non-reciprocal tariff preferences are an essential element of the special and differential treatment (SDT) of developing countries in a multilateral trading system. Reducing import tariffs in developed economies for developing ones should contribute to income from exports and investment, and consequently, be conducive to sustainable development and lower poverty. Hence, derogation from the GATT/WTO rules was introduced,[2] under which developed countries were permitted to grant tariff preferences to developing countries in the form of the Generalised System of Preferences (GSP).[3] The GSP enables developed countries to apply various rates of customs duty to each category of trading partners (e.g. developing and least developed countries, without violating Article I of the GATT, under which trading partners must be treated in a non-discriminatory and equal manner (most favoured nation, MFN). Tariff preferences are granted unilaterally and not negotiated with beneficiary countries. The very granting the tariff preferences or duty-free access to the market for goods originating from beneficiary countries does not automatically ensure that the trade preferences will be utilised effectively. Preferences depend on the fulfilment of a number of requirements related to rules of origin (RoO), which in many cases beneficiary countries are unable to meet (UNCTAD 2023b: p. 3).

The European Union (EU) introduced the GSP on 1 July 1971, being the first one ever in the world (UNCTAD 2023b: p. 7). In order to support least developed countries (LDCs),

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[2] The General Agreement on Tariffs and Trade (GATT), as of 1 January 1995 replaced with the World Trade Organisation (WTO). (see more: WTO 2023; UNCTAD 2023b).

[3] The Generalised System of Preferences (GSP) was established at the second session of UNCTAD conference held in New Delhi in 1968 and was targeted on developing countries. It was decided then that developing countries were incapable of competing with developed countries in the international trade system and customs tariffs would enable them to boost exports and increase profits on trade. This is necessary for the diversification of exports, increasing the economies of scale and reducing dependence on foreign aid (Kennedy 2012: p. 598).

in March 2001 the European Union launched the initiative *Everything but Arms* (EBA) as a part of the GSP.[4] Conditions for access to any market, including also the EU market, are contingent not only upon the level of customs duty rates, but also rules of origin (RoO), as it is the latter that determines whether a lower rate of customs duty can be applied to imported goods or not. RoO are rules (in the form of provisions of law) that make it possible to establish the economic nationality of goods in relation to a specific country or region and provide the proof of such origin.

The aim of the article, hypothesis and used methodology

This article's aim is to assess the significance of the rules of origin in the European Union's unilateral Generalised System of Preferences to the EBA system beneficiaries, with special attention given to changes introduced in 2011. A hypothesis formulated herein suggests that changes to the rules of origin of goods, which have been made over the past two decades, led to their simplification and relaxation for least developed countries in relation to specific groups of goods, which are of relevance from these countries' point of view. Consequently, this contributed to a higher preference utilisation rate and boosted trade. Nevertheless, this does not mean that rules of origin of goods do not serve for beneficiaries as barriers to preferential access to the EU market, specifically, for certain goods.

To meet the objective hereof, not only empirical methods were employed (indirect observation and description), but also general methods, including deduction and induction. The following research techniques were used: a cause and effect analysis, a comparative analysis and synthesis. The research is based on statistical data provided by Eurostat and UNCTAD.

Main assumptions of the initiative *Everything but Arms*

The GATT Enabling Clause of 1979 allowed not only preferences for all developing countries, but additional preferences for the least developed countries, as defined by the UN. In February 2001, the European Union launched an initiative for LDCs, which entailed duty-free and quota-free (DFQF) access to the EU market and covered all goods except for Chapter 93 of the Combined Nomenclature, i.e. arms and ammunition.[5] This concerns

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[4] The European Union provides three different GSP schemes: the general GSP scheme, the GSP+ (GSP Plus) scheme and the GSP-LDC scheme called the initiative Everything but Arms (EBA). (UNCTAD 2023b: p. 10).

[5] A list of least developed countries was compiled for the first time in 1971 by the UN. Throughout almost fifty years, the number of LDCs increased from 25 countries, as included in the 1971 list, to 50 countries between 2003 and 2007, and decreased to 46 countries in 2021. "As of 2021, forty-six countries are designated by the United Nations as least developed countries (LDCs). These are: Afghanistan, Angola, Bangladesh, Benin, Bhutan, Burkina Faso, Burundi, Cambodia, the Central African Republic, Chad, the Comoros, the Democratic Republic of the Congo, Djibouti, Eritrea, Ethiopia, the Gambia, Guinea, Guinea-Bissau, Haiti, Kiribati, the Lao People's Democratic Republic, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Myanmar, Nepal, the Niger, Rwanda, Sao Tome and Principe, Senegal, Sierra Leone, Solomon Islands, Somalia, South Sudan, the Sudan, Timor-Leste, Togo, Tuvalu, Uganda, the United Republic of Tanzania, Yemen and Zambia. [...] The list of LDCs is reviewed every three years by the

99.9% of imports to the EU from those countries (UNCTAD 2003: p. 34). As at 2023, 46 countries are covered by the EBA initiative.

The reduction of tariffs on bananas, rice and sugar was spread out in time, and was completed in 2009 (see: Council Regulation (EC) 416/2001). This means that neither (*ad valorem, ad spetiem*, compound) duties nor the entry price system are applied to imports to the European Union.[6] Therefore, the EBA initiative encompasses all agricultural products, including sensitive goods, covered by the common agricultural policy, such as meat, dairy products, fruit and vegetables, cereals, sugar and others.[7] For most of those products, the pre-EBA GSP provided for a percentage reduction of *ad valorem*, MFN rates, which meant that specific duties were not subject to reduction. The EBA preferences were incorporated under the Council Regulation No 2501/2001 into the Generalised System of Preferences as a special arrangement (see: Council Regulation (EC) 2501/2001). These preferences were granted for indefinite period of time, and what is more, they do not have to be reviewed periodically, which is the case with the GSP.

A beneficiary country ceases to be covered by the EBA if it has graduated from the LDC status and is no longer on the UN's LDC list. The European Commission reviews countries on an ongoing basis to verify their eligibility for the EBA and makes the decision on removing a country from the EBA after a three-year transitional period.

General characteristics of rules of preferential origin

Conditions for access to any market, including also the EU market, are contingent not only upon the level of customs duty rates, but also rules of origin (RoO), as it is the latter that determines whether a lower rate of customs duty can be applied to imported goods or not. RoO differ across countries and products. RoO are rules (in the form of provisions of law) that make it possible to establish the economic nationality of goods in relation to a specific country or region and provide the proof of such origin. Strict rules of origin received a lot of criticism from many researchers, as being too much exaggerated and impracticable, especially from the small and less developed countries' point of view. Some even call them "hidden protectionism" (Baldwin at al. 2009), as they can constitute significant non-tariff measures in trade (Hoekman, Inama 2017). Procedures for conformity with specific rules of origin generate extra costs, and consequently, can lead to the undesirable trade diversion effect in global value chains and the trade deflection effect, they also disrupt trade in

Committee for Development Policy (CDP), a group of independent experts that report to the Economic and Social Council (ECOSOC) of the United Nations." (UNCTAD 2022b: p. XI; UNCTAD 2021: p. X). It is expected that until 2026, seven countries will no longer be categorised into the LDC group. These will be such countries as: Bhutan (2023), Angola (2024), the Solomon Islands (2024) and São Tomé and Príncipe (December 2024), as well as Laos, Nepal and Bangladesh (2026). (United Nations 2023).

6 "Regarding fresh fruit and vegetables (28 tariff lines at a level of 8-digit CN code), the so-called entry price system (EPS) is deployed, which was implemented in 1995 and entails collecting customs levies calculated as the sum of ad valorem duty and extra specific duty (a so-called tariff equivalent) imposed when an import price is lower than an entry price" (Czermińska 2019a: p.56). Specific arrangements relating to the entry price system are contained, inter alia, in the document: Commission Regulation (EC) 1580/2007.

7 A greater scope of preferences for LDCs, with all the goods being covered, has been applied only by Australia (since 1 July 2003) and New Zealand (since 1 July 2001) (see: UNCTAD 2012: p. 12).

intermediate goods.[8] Less developed countries which have little potential for competing with other states cannot have access to cheaper semi-finished products or raw materials in the global value chain, as this can lead to a loss of tariff preferences due to the failure to comply with rules of origin.

Compared to other commercial policy instruments, such as customs duties and quotas, rules of origin are relatively less often the focus of research. This also follows from the fact that rules of origin change relatively rarely. Nevertheless, there are several works on the impact of the liberalisation of rules of origin on trade (Andersson 2016; Bombarda, Gamberoni 2013; Conconi et al. 2018), yet these researchers do not pay attention to least developed countries, where rules of origin are particularly onerous. In recent years, a few publications have been released on the significance of rules of origin to EBA beneficiaries and for trade (Crivelli, Inama 2021; Crivelli et al. 2021). Providing empirical evidence, the authors came to the conclusion that utilisation rates are conditional mainly on the strictness and/or complexity of rules of origin of goods. Tobias Sytsma (2021) focused on changes to rules of origin of apparel products under the EU Generalised System of Preferences to examine beneficiaries' preference utilisation rate. The author found that relaxing rules of origin for apparel products from least developed countries had a significant impact on preference utilisation rates. Some researchers limit their study to selected countries (Rahman 2014) or goods (Brenton, Özden 2009; Tanaka 2020; Curran, Nadvi 2015; Masum 2016; Habib 2016).

There are three elements of preferential origin which means the utilisation of reduced or zero rates of duty:

1) Meeting rules of preferential origin specified for a given product;
2) Providing a valid certificate of origin (prescribed by the regulations of an importing country, but issued by authorities of an exporting country);
3) Direct transport of goods from a beneficiary country to a country granting preferences. For transit, there must be "no manipulation", which has to be confirmed by a country of transit – commonly referred to as the Non-Manipulation Rule.

Rules of origin are an essential element that defines the scope of economic benefits following from preferential origin. The origin of goods is determined based on the rule that they originate from the country where they have been wholly obtained (WO) – this is a criterion applied to the majority of agricultural products, working or processing, if any, concerns wholly obtained materials; it also covers non-originating goods that have been worked or processed to the extent that is sufficient to accord the originating status in accordance with rules of origin set out for a given product or sector. The criteria allowing to consider processing sufficient to accord the originating status under the EU GSP are as follows:

1) "Tariff jump criterion" (change in tariff heading, CTH), meaning that the finished product that is obtained is classified under a four-digit heading of the Harmonised System nomenclature, which differs from that under which all non-originating materials used to manufacture that finished product are classified (European Commission 2016a; UNCTAD 2022a).

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[8] For more information on this subject see: Geraets et al. 2015: p. 296 et seq.

2) Percentage criterion (value or weight limitation), including the X% added value rule, namely, working or processing that leads to an increase in value by at least X% of the product ex works (EXW) price; it means a fixed maximum threshold for non-originating goods or a minimum threshold for goods originating from a country of processing.[9]
3) Technological criterion (specific forms of working or processing, SP), i.e. specific forms of working or processing which are required for non-originating goods (Czermińska 2019b: p. 339). Under the EU GSP, specific technical processes are used to meet required origin criteria for exports to the EU. Some of them are characteristic of particular product categories, e.g.: A. Timber products – planning, sanding, final joining and cutting; B. Textiles – weaving, spinning, printing and colouring. Similarly, as regards petroleum products, specific processes were defined, which are sufficient to accord the originating status under the EU GSP, and their details, including the HS code to which they apply are provided in Note 8 of Annex 22-03 to Commission Delegated Regulation (EU) 2015/2446 (see: Noida Special Economic Zone 2022: p. 14). With respect to certain goods, only one, or a combination, of the aforesaid criteria can be applied.

The percentage criterion is considered to be the least discriminatory and the simplest, compared to all other rules, in particular, when it applies to all goods. However, as regards its disadvantages, one has to mention a complicated calculation method and changes to prices and foreign exchange rates. For instance, when a "local currency depreciates, imported materials are relatively more expensive, which increases their relative share in the total value" , meaning that the value of non-originating goods exceeds the permissible threshold. Added value is also "subject to cyclical fluctuations of raw material prices or price changes during a recession" (Naumann 2009: p. 6).

The CTH methodology (a tariff jump) is generally the easiest to implement, but it has certain drawbacks. It is based on the HS nomenclature, which was not devised specifically for RoO. Hence, it happens that both "unprocessed and processed goods are classified under the same heading" (e.g. rough diamond and polished diamond are assigned the same four-digit HS code), whereas others, for which disaggregation is considerable, even very little processing (or no processing) can mean a "tariff jump" (e.g. fresh and dried vegetables have different four-digit HS headings). (Naumann 2009: p. 7).

EU reform of EBA Rules of Origin

As from 1 January 2011, there have been new, simplified GSP rules of origin in place, which were introduced by virtue of Commission Regulation (EU) No 1063/2010 of

[9] The European Union estimates added value using the indirect method, under which the non-originating material share in the total value of originating goods is determined as a percentage. The direct method is employed by the United States. When calculating added value, the US GSP system considers the cost or value of materials manufactured in a beneficiary country and the direct costs of processing (Bhattacharya, Mikić 2015: p. 23).

18 November 2010,[10] and implementing provisions in the form of Commission Delegated Regulation (EU) 2015/2446 of 28 July 2015 and Commission Implementing Regulation (EU) 2015/2447 of 24 November 2015. Prior to 2011, rules of origin were the same for each of the GSP subsystems and did not change substantially. The 2011 rules of origin brought in for LDCs mainly with respect to industrial goods are different, i.e. they are less stringent than the RoO applicable to the other GSP beneficiaries. Compared to the previous Regulation EU on GSP rules of origin, the following changes concerning the below three main areas were introduced, all of which apply to LDCs:

1) Changes to rules of origin for individual products, leading to the introduction of less stringent criteria for many sectors, in particular, with regard to least developed countries. The new Regulation also differentiates between developing beneficiary countries and least developed countries – where no such difference was specified under the previous legislation. Less stringent rules of origin of goods were set for developing and least developed countries in many HS chapters and headings, especially in the textile and clothing industry, as well as the machine-building and electronic industry.
2) Cumulation of origin. An important element of making the rules less stringent is cumulation of origin, which allows countries that are obliged to abide by identical rules of origin to collaborate in order to manufacture goods eligible for preferential treatment. The effect of cumulation is that materials originating from countries engaged in it are exempt from the obligation to satisfy the processing criterion that is a sufficient precondition for giving the originating status, which entails treating them as if they were originating materials. Thus cumulation of origin is the exception to the rule that preferential rules of origin apply to products from only one country, which benefit from preferences in a country of the consignee. The new Regulation contains changes to regional cumulation, it also introduced extended cumulation.
3) The reform modified the administration of rules of origin thoroughly. The origin certification system based on certificate of origin Form A was superseded after the end of a transitional period by statements on origin submitted directly by registered exporters. All exporters which export or intend to export to the EU under the GSP (including also under the EBA) are required to register in the system of registered exporters (REX) of the European Commission. An exporter registered in the REX system makes a statement on origin on their own, which serves then as a basis for applying tariff preferences to goods brought to the EU. "The paperless REX self-certification system has replaced the system where paper Form A certificates are approved by customs. From 1 January 2021 all GSP proofs of origin are made only by means of a REX statement on origin" (*Customs Manual* 2023: p. 56; see also: European Commission 2023b). Detailed rules concerning the issue of certificates of origin, declarations in invoices and Form A are laid down in Commission Implementing Regulation (EU) 2015/2447 of 24 November 2015.

[10] No longer in force.

As for the first group of changes introduced (rules of origin), the following modifications are the most significant from the least developed countries' perspective:

- The share of non-originating materials (used for the manufacturing of a finished product) from a country of processing which is an LDC has risen in the case of many industrial and processed agricultural goods (e.g. the automotive industry: for LDCs – a threshold of 70% of an ex works price for non-originating materials, the other GSP countries – 50% of an EXW price; similarly for chemical and related products). For machinery and electronics included in the HS chapter 84, the RoO which previously required CTH and the maximum share of non-originating materials amounting to 40% of EXW price was replaced by CTH or the maximum share of 70% of non-originating materials at an EXW price both for developing countries and LDCs (Crivelli, Inama 2021: p. 5).
- The relevant change is related to "the specific process criterion, when certain operations or stages in a manufacturing process have to be carried out on any non-originating materials used" (UNCTAD 2022a: p. 24). "In 2010, the European Union moved from a "double transformation" to a "single transformation" requirement for HS chapters 61 and 62 on apparel articles, the leading product groups traded under the European Union's GSP preferences" (UNCTAD 2023b: p. 16; see also: UNCTAD 2013: p. 4).

As regards apparel, the requirement for only the first processing was imposed on the group of countries in question. This requirement is related to the first processing in a beneficiary country, i.e. manufacturing from fabrics, which means that they go through the CMT (cut, make & trim) processes. Hence, there is no longer any requirement that fabrics must originate from a country of processing (which benefits from preferences). "This is an essential change, which allows for choosing the most competitive suppliers of fabrics, and this, consequently, has a bearing on the level of prices and contributes to enhanced competitiveness of exported goods" (Czermińska 2021). For the other system beneficiaries, it is necessary to carry out weaving operations accompanied by finishing, including trimming (see: Commission Regulation (EU) 1063/2010: Part II).[11] Textiles and apparel are the key sector for many GSP beneficiaries, whereas rules of origin applicable to this industry constitute a criterion for the assessment of RoO stringency (Naumann 2011: p. 8). That sector is considered in the EU to be sensitive, hence tariff barriers are quite high and the preferential access to the Union market entails a relatively huge preference margin – resulting from a difference between preferential and non-preferential treatment. The changes in the rules of origin are of great significance to exporters of products made of fabrics (Rahman 2014: p. 22).

Earlier, apparel manufacturers had been required by the EU rules of origin to use textiles originating from local sources. Under the then provisions, apparel producers from LDCs could be given an access to reduced rates of customs duty in the EU only when apparel products were made of textiles manufactured also in LDCs. Failure to meet that

[11] No longer in force.

rule of origin resulted in the application of non-preferential MFN customs duty rates. This rule prevented apparel producers in least developed countries from procuring textiles from low-cost countries, such as China or Taiwan.

A good example here is Bangladesh and apparel, which is a product being most often exported from this country to the EU. Using duty-free access to the EU market was traditionally limited by RoO requirements (before 2011), specifically, in the case of the export of finished apparel. The Union's RoO for the export of apparel required "two-stage conversion": from yarn, fabrics, to clothes. Bangladesh did not have strong backward links for textiles, in particular, for fabrics, therefore, it is dependent, to a large extent, on imported fabrics. This also precluded duty-free access offered under EBA (only approx. 28% of knitted material could benefit from a zero rate of customs duty, the remaining 72% was covered by an average MFN rate – 12.1%). As a consequence, Bangladesh-based exporters were losing potential competitive advantage. In the case of knitted material, Bangladesh has been able to build strong backward links over the years due to private investment in yarn and knitted material production. For Bangladesh, the Union's RoO played an important role in stimulating investment in activities related to backward linkage, although this was mainly limited to the knit sector (Czermińska 2023: p. 19; Rahman 2014: p. 14).

Cumulation of origin under the EBA initiative encompasses: (a) cumulation with a country granting preferences, in this particular case this is the EU (bilateral cumulation); (b) cumulation with EU GSP beneficiaries (regional cumulation); (c) cumulation with countries which signed free trade agreements with the EU (extended cumulation) and (d) cumulation with Norway, Switzerland and Türkiye.

Bilateral cumulation means that materials originating from the EU may be used for products manufactured in an EBA country, and subsequently, deemed as originating from that EBA country, provided that processing operations carried out in the EBA country go beyond minimum activities. The same applies to materials which come from an EBA country and are processed in the EU. Hence, this kind of cumulation means, for instance, that European materials can be used, undergo the working or processing process which is sufficient to gain the originating status; in practice, such cumulation can encompass mainly labour-intensive, but low-tech products. An example of goods that can benefit from bilateral cumulation includes apparel made in LDCs of materials purchased in the EU.[12] In practice, such cumulation can also refer to the import of materials originating from beneficiary countries to the Union, and their processing by European manufacturers (Piotrowski 2011: p. 54–55).

Regional cumulation was always included in the EU GSP rules of origin. Mercosur was added, as a new entity that benefits from regional cumulation. By virtue of the previous Regulation, the originating status was accorded to a country in which the last manufacturing operations were made, only if added value was higher than the customs value of raw materials imported from another member country of a regional organisation. In practice, that meant, for instance, that a manufacturer from Cambodia which desired to use fabrics originating from Thailand was not accorded the Cambodian originating status, as the value

[12] For more information on bilateral and regional cumulation of origin – see: Commission Delegated Regulation (EU) 2015/2446: art. 37.

of fabrics was higher than added value obtained in Cambodia. Under the new Regulation, the said requirement was eliminated on condition that working operations from other regional group member underwent working or processing going beyond minimum operations. Regional cumulation is functioning within one of four regional groups recognised by the EU GSP.[13] Materials coming from one member country of a group, which are further worked or processed in another country of the same group, are considered to be originating from that last country. The previously applicable conditions of regional cumulation of origin, divided into three groups of countries located in close geographical proximity, were seen as not only conservative, but also complicated and too stringent. The new rules of origin increased the number of groups covered by regional cumulation, introduced the fourth group of countries from South America, i.e. Mercosur. Moreover, at the request of an interested country, cumulation among group I and group III countries is possible, provided that a number of specific administrative requirements have been met. However, cumulation among group II and group IV countries was not introduced, despite the fact that Bolivia, Colombia, Ecuador, Peru enjoy the associated country status in Mercosur and benefit from a free trade area, yet they do not belong to a customs union. Regional cumulation among member countries of the same regional group can be applied only under the condition that working or processing carried out in a beneficiary country, in which materials are further processed or included, goes beyond minimum operations and, in the case of textile products, also beyond the operations specified in Annex 22-05 to Commission Delegated Regulation (EU) 2015/2446. If the aforesaid condition has not been met, a country of origin of products will be a regional group country having the biggest share in the customs value of materials used, which originate from other countries of a regional group (European Commission 2010: p. 17). Therefore, the utilisation of components among member countries of the same group is allowed in practice (e.g. Bangladesh may use components from Bhutan because both countries belong to group III). Attention must be given to the following principles: regional cumulation among member countries of the same group can be applied only when countries involved in cumulation are beneficiary countries at the time of export of a product to the European Union, not only eligible countries; when goods originating from one beneficiary country are further processed in another member country of that group, then goods can be deemed as originating from that last country (provided that processing goes beyond minimum operations). (European Commission 2019).

It needs to be highlighted that the countries mentioned as belonging to regional cumulation groups are countries eligible for the GSP (some of them are not beneficiaries). Both the provisions on bilateral and regional cumulation may be applied jointly (European Commission 2016b: p. 17). Currently, regional cumulation of origin covers only two groups that can benefit from it, namely: "Group I: Cambodia, Indonesia, Laos, Myanmar/

[13] Originally: "Group I: Brunei, Cambodia, Indonesia, Laos, Malaysia, Philippines, Singapore, Thailand, Vietnam; Group II: Bolivia, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua, Panama, Peru, Venezuela; Group III: Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, Sri Lanka; Group IV: Argentina, Brazil, Paraguay and Uruguay." (Commission Regulation (EU) No. 1063/2010: art. 86; this regulation is no longer in force). Out of these countries, Cambodia, Laos, Bangladesh, Bhutan and Nepal are LDCs.

Burma, the Philippines and Vietnam (it was GSP Plus beneficiary only until the end of 2022); Group III: Bangladesh, Bhutan, India, Nepal, Pakistan and Sri Lanka. The other two groups include only one country each (Group II: Bolivia and Group IV: Paraguay)", hence, cumulation among individual countries is possible only on request and under certain conditions (Gwardzińska, Chowaniec 2021: p. 12; European Commission 2023a).

Extended cumulation (with countries which signed free trade agreements with the EU) encompasses only industrial goods and processed agricultural products. Agricultural products classified under HS chapters 1-24 are excluded from extended cumulation. This cumulation of new type must be applied unilaterally, which means that it should enable exclusively the utilisation of materials in a beneficiary country, however, before it is granted, an interested beneficiary country should submit a request in writing to the Commission, which needs further to be examined, and that country should also satisfy specific requirements, including for co-operation between customs authorities and ensuring the proper application of Union provisions.

As regards cumulation with Norway, Switzerland and Türkiye, it covers goods categorised into HS chapters 25–97. Materials originating from Norway, Switzerland or Türkiye, which undergo more than a minimum operation in LDC benefiting from preferences are considered as coming from that beneficiary country and may be exported to the EU, Norway, Switzerland or Türkiye. This rule does not apply to agricultural products or products which are subject to derogation. "For this type of cumulation to apply, the EU, Norway, Switzerland and Türkiye need to grant the same preferential treatment to products originating in EBA countries" (European Commission 2019).

Instead of the provision on necessary direct transport, the non-manipulation rule was imposed, meaning that products cannot be altered, processed or subjected to operations other than operations designed to preserve them in good condition, products remain under customs supervision in the country (countries) of transit. Compliance requirement is deemed to be met, unless customs authorities have good grounds to believe otherwise; in such cases, customs authorities may request that the declarant present a proof of compliance, which may be submitted in any manner, including in the form of transport documents or specific proofs based on packaging marking or numbering (*Customs Manual* 2023).

Significance of changes in Rules of Origin of goods for EBA system's beneficiaries and for trade between them and the European Union

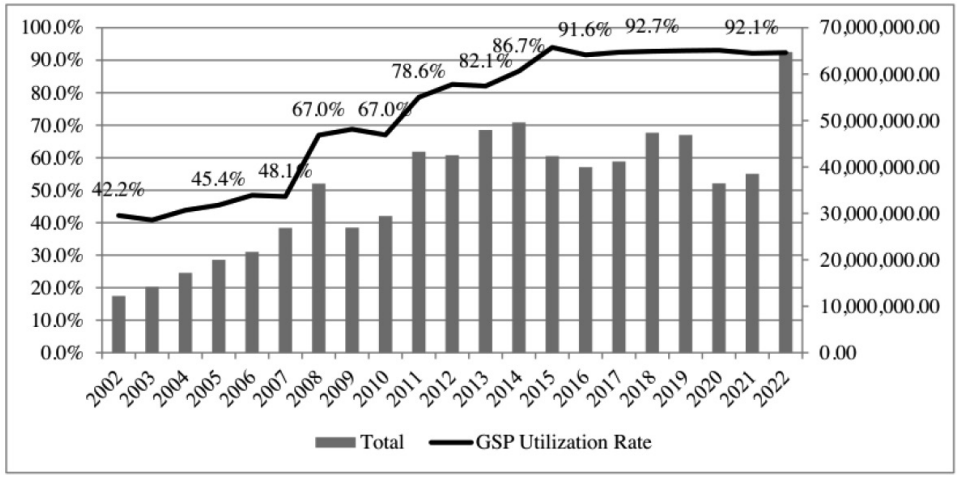
Whether a system of preferences is effective from the rules of origin perspective or not is reflected by the degree to which preferences are utilised, along with the structure of trade in goods. Whereas the degree to which preferences are utilised is demonstrated by the preference utilisation rate and utility rate.[14] Those rates may vary significantly, which depends

[14] The preference utilisation rate is defined as the share of preferential import value in the value of import eligible for preferences. Whereas the preference utility rate is the share of preferential imports in the total imports (European Commission 2019).

on the product coverage of preferences. If the preference utilisation rate is high, with the utility rate being low at the same time, then it can mean that the scope of preferences is narrow (many goods are excluded from the system), but preferences being offered are in line with the beneficiary's export structure. However, if that correlation is opposite, i.e. where the scope of goods covered by preferences is huge, yet the degree to which they are utilised is small, this can imply that preferences are not adapted to the beneficiary's export structure. As for the goods which are mainly imported by LDCs, these goods include, first and foremost, apparel and textiles (which accounted for approx. 58% of imports in 2021) (Eurostat data WWW).

It must be stressed that these are the groups of goods, in which RoO play a significant role for beneficiaries of tariff preferences. The starting point of the research is 2009 (before the changes in the rules of origin were introduced) and 2011, which was the first year, in which the new rules of origin came into effect. Subsequently, the volume of preferential imports for major GSP beneficiaries in consecutive years was presented in two-year cycles.

Figure 1: Volume of EU's Imports from LDCs (in thousand US dollars) and utilisation rate (in %).

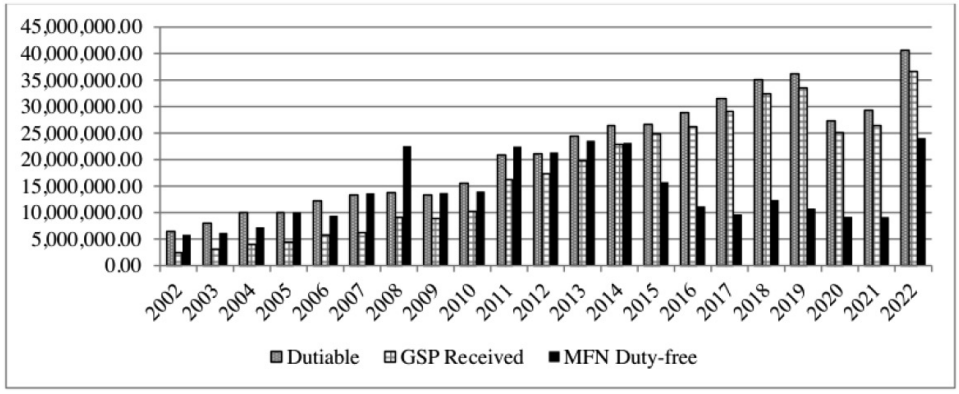


Source: own elaboration based on UNCTAD 2023a.

The volume of imports to the EU from LDCs shows a growing trend, but is subject to certain fluctuations (see: *Figure 1*). In this regard, 2022 reached a record high, when imports exceeded USD 60 billion (compared to approx. 12 billion US dollars in 2002). Whereas in the years 2002–2022, the utilisation rate of the EU GSP-LDC increased from slightly more than 40% to above 90%. When combined with the full extent of products covered by duty-free treatment (zero MFN rate, see: *Figure 2*), more than 90% of maximum value of preferences was in fact utilised under the Union GSP-LDC scheme. The driving factor behind that trend is the reform of rules of origin under the Union GSP-LDC. In 2010, the European Union shifted from a "double transformation" to a "single transformation" requirement for

HS chapters 61 and 62 on apparel articles – the groups of products that are leading in preferential import from LDCs (UNCTAD 2023b). The reform enabled exporting LDCs to use imported fabrics for the manufacturing of finished products, instead of using imported yarn. The RoO reform allowed for the greater utilisation of preferences under the scheme.

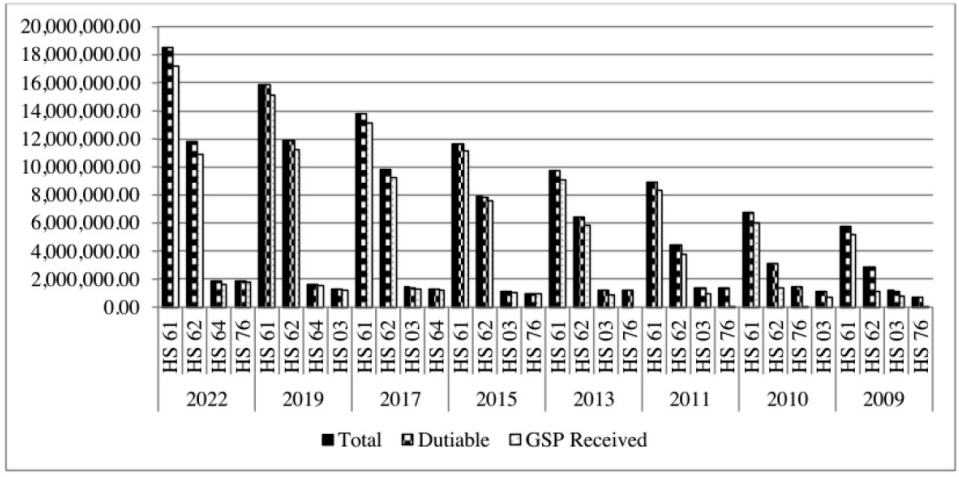
Figure 2: EU imports by tariff treatment from LDCs (in thousand US dollars)



Source: own elaboration based on UNCTAD 2023a.

Throughout the years, the value of dutiable imports from LDCs has been rising (non-zero rates of customs duties), but the value of imports covered by GSP preferences has been also on the increase (see: *Figure 2*). This applies, first and foremost, to articles of apparel and clothing accessories (HS chapters 61 and 62) (see: *Figure 3*).

Figure 3: Top four dutiable products imported by European Union from least developed countries (imports in thousand US dollars).

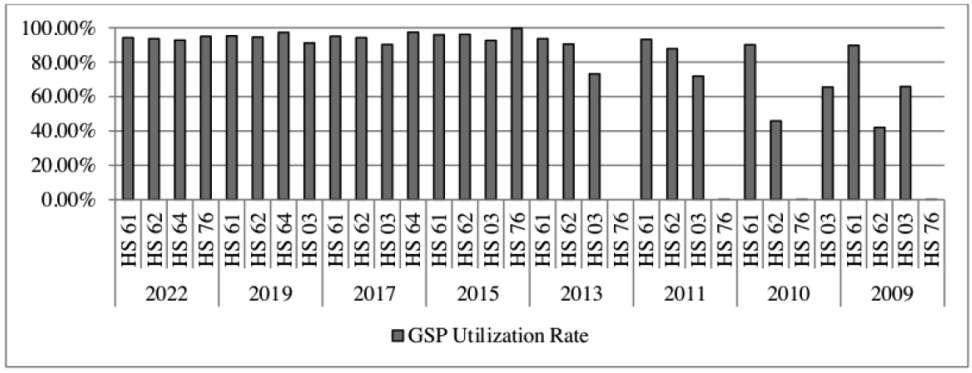


HS 61: Art of apparel & clothing access, knitted or crocheted.

HS 62: Art of apparel & clothing access, not knitted/crocheted
HS 03: Fish & crustacean, mollusc & other aquatic invertebrate
HS 64: Footwear, gaiters and the like/ parts of such articles
HS 76: Aluminium and articles thereof.
Source: own elaboration based on UNCTAD 2023a,b.

The largest exported product groups, classified at the HS chapter (2-digit) level, represent between 65 and 95% of total effective preference values under the GSP schemes are goods classified under HS chapters 61 and 62, i.e. articles of apparel and clothing accessories, knitted or crocheted (chapter 61) and articles of apparel and clothing accessories, not knitted or crocheted (chapter 62) (see: *Figure 3*). A considerable increase of exports of goods categorised as chapter 61 and 62 to the EU can be observed, as from the beginning of 2011 (the change to the rules of origin).

Figure 4: Utilisation Rate – Four Major Dutiable Products Imported by European Union from Least Developed Countries (in %)



HS 61: Art of apparel & clothing access, knitted or crocheted
HS 62: Art of apparel & clothing access, not knitted/crocheted
HS 03: Fish & crustacean, mollusc & other aquatic invertebrate
HS 64: Footwear, gaiters and the like/ parts of such articles
HS 76: Aluminium and articles thereof
Source: own elaboration based on UNCTAD 2023a.

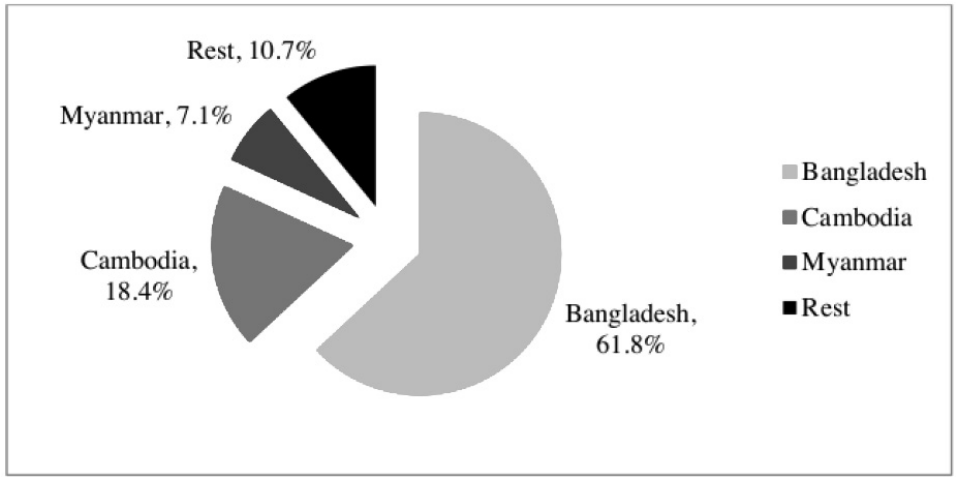
The utilisation rate for Art of apparel and clothing access, knitted or crocheted (HS 61), both prior to the change to the rules of origin and in the consecutive years, was high and fluctuated around 90%, over the years, it had showed a growing trend (90% in 2009, 94% in 2022).[15] The rise in utilisation rates of knitted or crocheted garments (HS chapter 61) has been moderated as the latter started from a much higher value than in the case of HS chapter 62 (see: *Figure 4*). For Art of apparel & clothing access, not knitted/crocheted

[15] It must be noted that an average MFN customs duty rate applicable to the import of textiles and apparel (HS 61 and HS 62), trade/free trade agreement with the European Union equals 9%.

(HS 62), the utilisation rate has risen considerably after the change to the rules of origin: 42% in 2009, 87% in 2011 (it doubled) to 94% in 2022. This results from introducing the requirement for only first processing in a beneficiary country, manufacturing from fabrics, which means that they go through the CMT (cut, make & trim) processes; and from the fact that there is no requirement that fabrics must originate from a country of processing (which benefits from preferences).

The distribution of the value of preferences of the EBA schemes is highly concentrated in a small group of products and exporters (UNCTAD 2023b). The major EBA beneficiaries are, in order of magnitude: Bangladesh, Cambodia and Myanmar (see: *Figure 5*). In aggregate, these three countries account for nearly 90% of the total EBA preferential imports.

Figure 5: Major beneficiaries of *Everything But Arms* arrangement in 2018* (share in %).



*based on the latest available report of the European Commission.

Source: European Commission 2020: p. 12.

"The biggest share of imports under EBA came from Bangladesh (61.8%), followed by Cambodia (18.4%); and Myanmar (7.1%). In terms of overall GSP beneficiaries, Bangladesh overtook India in 2018 (with EUR 16.8 billion preferential imports against EUR 16.4 billion from India)." (European Commission 2020: p. 11). In Bangladesh, textile & textile articles (HS section XI) comprise approx. 92% of exports to the EU (all the figures showed below are retrieved from UNCTAD data base). In 2009, the utilisation rate in this group of products stood at 78%, whereas in 2011, it rose to 95% (in 2022 – 95%). Hence, relaxing the rules of origin had a considerable impact on the greater use of preferences with respect to the major export goods. The similar effect is seen also for the other major EBA beneficiary, namely, Cambodia. As regards the main group of goods exported to the EU, i.e. Textile & textile articles (HS section XI), the utilisation rate in 2009 amounted to 70%, whereas in 2011, it rose to 89%. After 2011, Cambodia's export of apparel to the EU increased by 112%, which coincided with the rapid rise in import of textiles from China to Cambodia

(Tanaka 2020: p. 6). As for Myanmar/Burma, the effect of relaxing the rules of origin on trade volumes and preference utilisation rate is also observed. That country had been a beneficiary of tariff preferences since 2013 (before that date, preferences were removed for political reasons), the main group of exported goods includes also commodities classified under section XI. In 2013, the utilisation rate in this group of goods was 48%, but in the consecutive years it continued to grow, to reach 96% in 2022.

Conclusions

The GSP is an important development policy instrument that provides developing countries with better access to the European Union's market by applying lower (or zero) rates of customs duties to most of the goods. Special importance is attached to preferences granted to least developed countries. Characteristic feature of the GSP is the fact that these are unilateral preferences, meaning that they do not have to be reciprocated by the beneficiary. At the same time, the "benefactor", that is to say – in the case of the EU system – the European Union, decides about a preference margin and eligibility rules applicable both to countries and goods.

There are several factors that diminish the importance of preferences under the GSP to its beneficiaries. Those which are of key relevance include the rules of origin of goods. They mean that in order to benefit from preferences, economic operators must comply with complex rules of origin, which lead to higher costs relating to administrative procedures and specific technical requirements, e.g. concerning appropriate documentation, requirements for the transport of goods from countries that benefit from preferences, etc. The exporter will decide to incur extra costs if reductions in customs duties, and related benefits following from a reduction in customs duties under the GSP compensate for these costs. Furthermore, rules of origin are often excessively restrictive as regards basic criteria for using imported materials and components in developing countries' production.

With average MFN rates in the EU being low, tariff preferences are significant mainly in the event of tariff peaks (which occurs, among other things, for textiles, apparel and footwear). When justifying restrictive rules of origin in the clothing sector, it is argued that they are necessary to support actions having a clear added value in developing countries and promote integrated manufacturing processes. As for drawbacks of rules of origin, they include additional requirements that must be met in order to consider processing sufficient to accord the originating status (in addition to the percentage and technological criterion), namely, a "double tariff jump" in place of an ordinary change of the tariff heading.[16]

Rules of origin (before 2011) were perceived in the European Union as too complex and difficult to satisfy. The changes introduced in 2011 contributed to the simplification

[16] A double tariff jump, also referred to as two-stage processing, means, for instance, the making of fabrics from fibres (stage 1) and then the production of apparel (stage 2), or, for example, making apparel from yarn.

and relaxation of the rules of origin. Tolerance for values of non-originating materials, stipulated in the EBA, are less stringent. Cumulation of origin with goods originating from Norway, Switzerland and Türkiye makes it possible to apply the origin of goods included in chapters 25 to 97 of the Harmonised System. Regional and extended cumulation is also possible. The most significant change (given the structure of goods covered by LDCs' trade) refers to the relaxing of rules of origin applicable to apparel and textiles, in which case MFN rates remain at a relatively high level. Compared to the other GSP beneficiaries, the new rules of origin in this sector are less restrictive for LDCs. As regards apparel, the requirement for only the first processing was imposed on the group of countries in question. There is no longer any requirement that fabrics must also originate from a country of processing (which benefits from preferences). This is an important change, which allows for choosing the most competitive suppliers of fabrics, which in turn affects the price level and contributes to the increase in the competitiveness of exported goods.

Relaxing the rules of origin in this group of goods for EBA countries not only translated into a higher share of these countries in preferential trade in the EU, but also contributed to a higher preference utilisation rate. This refers, in particular, to Bangladesh and Cambodia, but also other LDCs. The elimination of customs duties on almost all goods under the EBA, accompanied by relaxed rules of origin, is beneficial to least developed countries, whose preference utilisation rate is also high. The major beneficiary is Bangladesh, which was able to adapt and take advantage of the opportunities for exporting textiles to the EU. A shift from the Union's three-stage RoO requirement (cotton, yarn, fabrics and apparel) to two stages (from yarn to fabrics and apparel) contributed to the growth of the knitting sector in Bangladesh.

RoO play an important role in using EBA preferences, especially by least developed countries. Nevertheless, the extent to which they are utilised depends on individual production and export capabilities of respective system beneficiaries. Where preference margins are high enough, rules of origin are significant indicator of preference utilisation. The European Union's example demonstrates that the reform of rules of origin by relaxing the requirements for the processing of apparel products has considerably increased the utilisation of GSP preferences in the case of LDCs' export.

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