

Automotive Rule of Origin

Background

Rules of origin (ROOs) set parameters for determining when imported goods are eligible for reduced duty rates under a free trade agreement (FTA). These rules are defined in each FTA and often differ from one another, producing varied outcomes on the same product.

There are basically two types of ROOs: tariff shift rules and regional value content (RVC). Tariff shift (TS) rules confer eligibility on a good when the classification of the non-originating materials and components of the product change to a classification of the finished good (i.e., component parts 8708 shift to vehicle 8703). RVC rules confer eligibility when a good contains: 1) at least a minimum percentage of regional value (build-up) or, 2) no more than a set percentage of non-regional value (build-down). Some FTAs require a TS, some require an RVC percentage, and some require various combinations of both.

Automotive ROOs are typically unique in FTAs. For example, an entire Annex of the North American Free Trade Agreement (NAFTA) was devoted to automotive trade and investment, with a section on ROOs focused on a net-cost method. Under the current Free Trade Area of the Americas (FTAA) draft negotiating ROOs text, there are three methodologies available in the calculation of regional value content (RVC) ROOs: net cost, adjusted value, and transaction value.

While the net cost method is “cost-based”, and relatively distinct in its application, adjusted and transaction value methods are “price-based” and quite similar to one another. The price-based methodologies allow for a wider range of inputs into the ROO calculation. As such, a higher percentage requirement under a price-based system is generally considered equivalent to a lower net-cost number. Some automotive manufacturers favor a net-cost only approach, while others prefer an adjusted value approach, or even a combination of both approaches. Given the varying investment patterns of the global automotive manufacturers, these positions can change contingent on the region where an FTA is being negotiated, and therefore fundamentally boil down to competitiveness issues between the global manufacturers.

NAFTA (1994)

Under this FTA, *only the net cost* method is utilized in calculating automotive ROOs. As of January 1, 2002, at least 62.5 percent of a passenger car or light truck's net cost must be of value originating in North America. All other vehicles must reach 60 percent North American content to qualify for zero duty rates. Unique to this agreement, the NAFTA requires manufacturers to account for (or “trace”) the origin of all materials used in the vehicle construction. For agreements which use the NAFTA ROO as a template, this tracing requirement has been dropped in the interest of increased simplicity and greater ease of administration.

European Union (EU)-Mexico FTA (2000)

Under this FTA, the automotive ROO is based on ex-factory price (adjusted value methodology). Automobiles, trucks and buses were subject to a 45 percent rule of origin from 2000-2001. In 2002, the requirement for autos increased to 50 percent and remained at 50 through 2004. The rule of origin for trucks and buses continued at 45 percent in 2002, and increased to 50 percent in 2003 through 2006. In 2005, autos will increase to 60 percent and remain at this level, while trucks and buses will increase to 60 percent in 2007, and remain at this level. Therefore, in 2007 and beyond, all vehicles must meet a 60 percent EU-Mexico ROO content to qualify for a zero tariff.

U.S.-Chile FTA (2003)

Under this FTA, *only the adjusted value* method is utilized in calculating ROOs for automotive products. The percentages for this FTA are adjusted value build-up: 30 percent and adjusted value build-down: 50 percent.

CAFTA (December 2003)

This FTA *utilizes two methods*: the net cost and adjusted value (build-up, and adjusted value build-down) approaches. The percentages are as follows: net cost: 35 percent; adjusted value build-up: 35 percent; and adjusted value build-down: 50 percent.

U.S.-Australia FTA (February 2004)

Forthcoming. (This text is not yet publicly-available.)