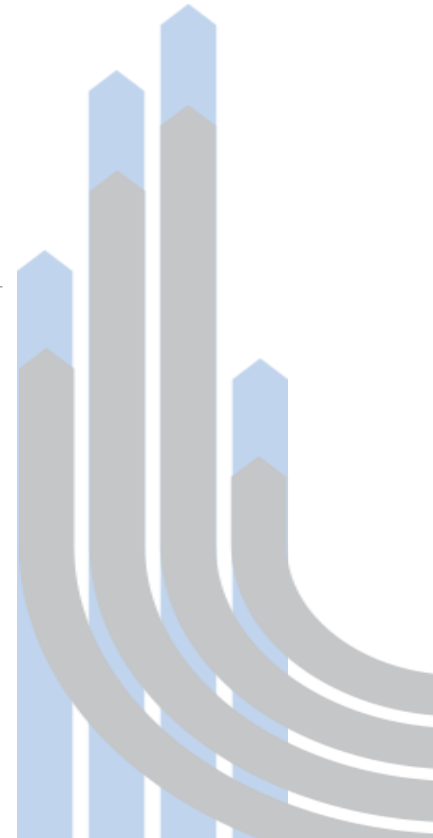


UK automotive & Brexit: International Trade and Rules of Origin

16 November 2017



- During presentations (10:00 – 10:30) everyone will be muted so that only the presenters will be heard.
- The presentation will be followed by a Q&A session. Click on the hand symbol to show that you have a question.
- If you are experiencing any technical problems please call 020 7344 1673.

SMMT Brexit Priorities

Single Market – To achieve automotive priorities on tariff-free trade and avoiding non-tariff barriers, government must demonstrate how it intends to secure a future trade agreement with the EU that affords the automotive industry the benefits currently enjoyed as members of the Single Market.

Customs – Under a new customs agreement with the EU, government should prioritise the free-flow of automotive goods at the border to avoid costs, maintain competitiveness and support the just-in-time manufacturing process. Key issues include continued application of common customs rules and procedures without burdensome checks or reporting.

Talent – Government must address the needs of the automotive industry in its ability to recruit and access talent when assessing how the UK ends freedom of movement and implements new immigration controls. Key issues include access to labour to fill skills gaps and the current ability for automotive companies to quickly and easily move employees to address operational issues or support project teams.

Regulation – Government should demonstrate how existing automotive regulation fits within plans for the 'Repeal Bill' and work through options for how future EU regulation affecting the UK automotive industry can be effectively implemented. Key issues include future influence on regulations affecting the UK automotive industry, the potential to create non-tariff barriers through regulatory divergence and the ability for the UK to type approve vehicles for the European market.

Trade – Clarity is needed on how the UK will treat both existing EU Free Trade Agreements and those currently under negotiation. Key issues include establishing solutions to issues around Rules of Origin, understanding how existing preferential access to markets can be secured as well as benefits from regulatory discussions between the EU and other key markets.



SMMT Brexit Priorities - Trade

Trade

Objective: Secure the UK's position in current EU trade agreements, those under negotiation and provide clarity on the UK's future trade strategy

In delivery of automotive priorities on trade, government should:

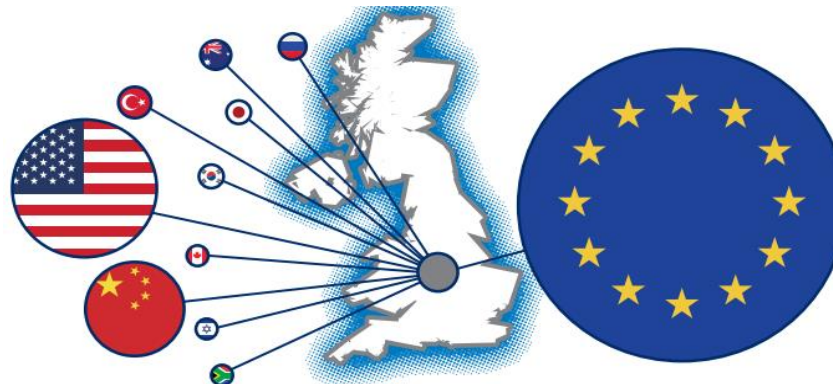
- Confirm “grandfathering” arrangements and continuity in trade relationships currently maintained through EU Free Trade Agreements (FTAs)
- Detail how intended benefits through FTAs currently under negotiation can be retained
- Outline a solution to maintain cumulation with EU automotive goods to resolve issues around Rules of Origin
- Provide clarity on its approach and priorities for future UK trade agreements

State of trade for UK automotive

Exports

TOP EXPORT DESTINATIONS FOR UK CARS

EU	57.5%	TURKEY	2.9%	JAPAN	1.8%	ISRAEL	1.2%
US	10.9%	AUSTRALIA	2.8%	SOUTH KOREA	1.7%	SOUTH AFRICA	1.1%
CHINA	7.0%	RUSSIA	2.0%	CANADA	1.2%		

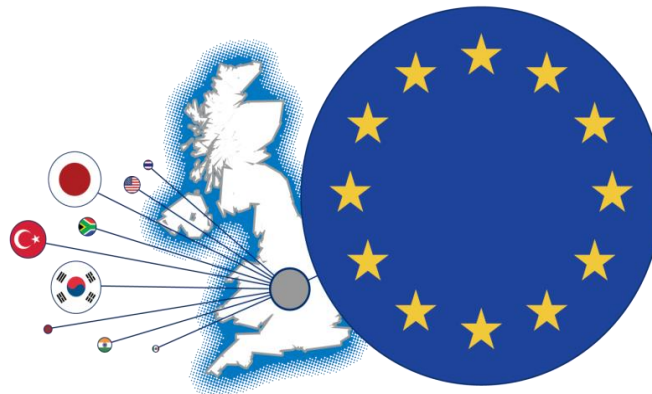


State of trade for UK automotive

Imports

UK NEW CAR IMPORTS BY ORIGIN

EU	81.8%	SOUTH AFRICA	1.5%	THAILAND	0.8%
JAPAN	4.6%	US	1.4%	MOROCCO	0.7%
SOUTH KOREA	4.3%	INDIA	1.2%	MEXICO	0.4%
TURKEY	3.1%				



What Are Rules Of Origin?

- “The criteria needed to determine the national source of a product” (WTO)
- Two types of origin:
 1. **Non-preferential origin:** uses include determining whether imports are subject to customs duties, anti-dumping measures, anti-subsidy measures, safeguards, quotas, labelling or origin marking and trade statistics.
 2. **Preferential origin:** to determine if imports qualify for preferential duty rates pursuant to a reciprocal trade agreement (e.g. EU-Korea Free Trade Agreement) or unilateral concessions (e.g. the EU Generalized System of Preferences for Developing and Least Developed countries)
- **WTO Harmonization Work Program:** Established in 1995 to harmonize non-preferential ROOs but no positive results; **each country has its own non-preferential ROOs.**
- Preferential rules of origin depend on single **Free Trade Agreement (FTA)** or unilateral preferential scheme.

Impact of Rules Of Origin

- Rules of origin are considered a particularly burdensome non-tariff barrier
- Complicated procedures and formalities apply

Table 1. Issues with burdensome regulations raised by EU exporter, by type

	Number of issues (product/destination/partner)	Share of Total (%)
A. Technical requirements	1,229	16.9
B. Conformity assessment	2,314	31.9
C. Pre-shipment inspections and other entry formalities	582	8.0
D. Trade remedies	41	0.6
E. Quantity control measures	215	3.0
F. Charge, taxes and price control measures	193	2.7
G. Finance measures	103	1.4
H. Anti-competitive measures	33	0.5
I. Trade related investment measures	10	0.1
J. Distribution restrictions	24	0.3
K. Restrictions on post-sales services	12	0.2
L. Subsidies	1	0.0
M. Government procurement restrictions	29	0.4
N. Intellectual property	13	0.2
O1. Preferential rules of origin and related certificates of origin	580	8.0
O2. Non-preferential rules of origin and related certificates of Origin	594	8.2
P. Export related measures	1,291	17.8
Total	7,264	100

Source: ITC business survey in the EU, 2015-2016.

Brexit Concerns for Automotive Sector

- Outside the EU Customs Union, ROO will become required for UK-EU trade, including components crossing the Channel multiple times, and finished vehicles.
- Businesses exporting goods between the UK and the EU will need to complete RoO documents
 - **Administrative burden:** ~2% of transaction values (HM Treasury)
- Even if zero-tariffs, some goods would need to pay duties if they do not qualify as originating in the UK or EU
 - **Costs on non-originating goods:** either from duties or using higher-cost inputs (~4% total costs, NAFTA)
- If there is no deal and default to WTO rules, UK exporters to the EU would still need to comply with 'non-preferential' RoO requirements
- Transitional arrangements will be needed, but unclear how such arrangements will ensure the current status quo in EU-UK and UK-FTA parties' trade.

Determining Origin: 2 Main Rules

Kyoto Convention - two basic criteria:

- a) **‘Wholly obtained’**: natural products and products made with no imported components
- b) **‘Sufficiently transformed’**: typically one of 3 methods:
 1. **Value added**: Prescribed threshold of maximum non-originating materials or minimum local content, e.g.:
 - the value of all non-originating materials used must not exceed a specified percentage of the ex-works price of the product (i.e. its price at the seller’s factory, so not including any additional costs such as transport);
 - The originating materials or processing operation carried out in a contracting party of a FTA must be equal or exceed a given percentage of the final value of the good.
 2. **Change of tariff classification**: the final product must be a different tariff classification (in the Harmonised System) than the materials used to make it;
 3. **List of manufacturing or processing operations**: origin of the product is conferred to the country where a specific operation has taken place.

Non-preferential ROOs for Automotive

- **Union Customs Code (UCC)**, approved in 2013, establishes EU legal framework for ROOs:
 1. Art 60 Non-Preferential ROOs;
 2. Art. 61 Preferential ROOs.
- Non-preferential ROOs for not “wholly obtained” products are normally set by the **EU Table of List Rules**.
- The primary rules for vehicles and components can be found under **Chapter 87** of the Harmonized System (HS), e.g.:

HS 2012 Code	Description of goods	Primary Rule
87.03	Motor cars and other motor vehicles principally designed for the transport of persons [...], including station wagons and racing cars.	45% value added rule*

* the increase in value acquired as a result of working and processing, and if applicable, the incorporation of parts originating in the country of manufacture represents at least 45% of the ex-works price of the product

- When the primary rule is not met, the country of origin of the good usually should be the country in which the major portion of materials originated, as determined on the basis of value.

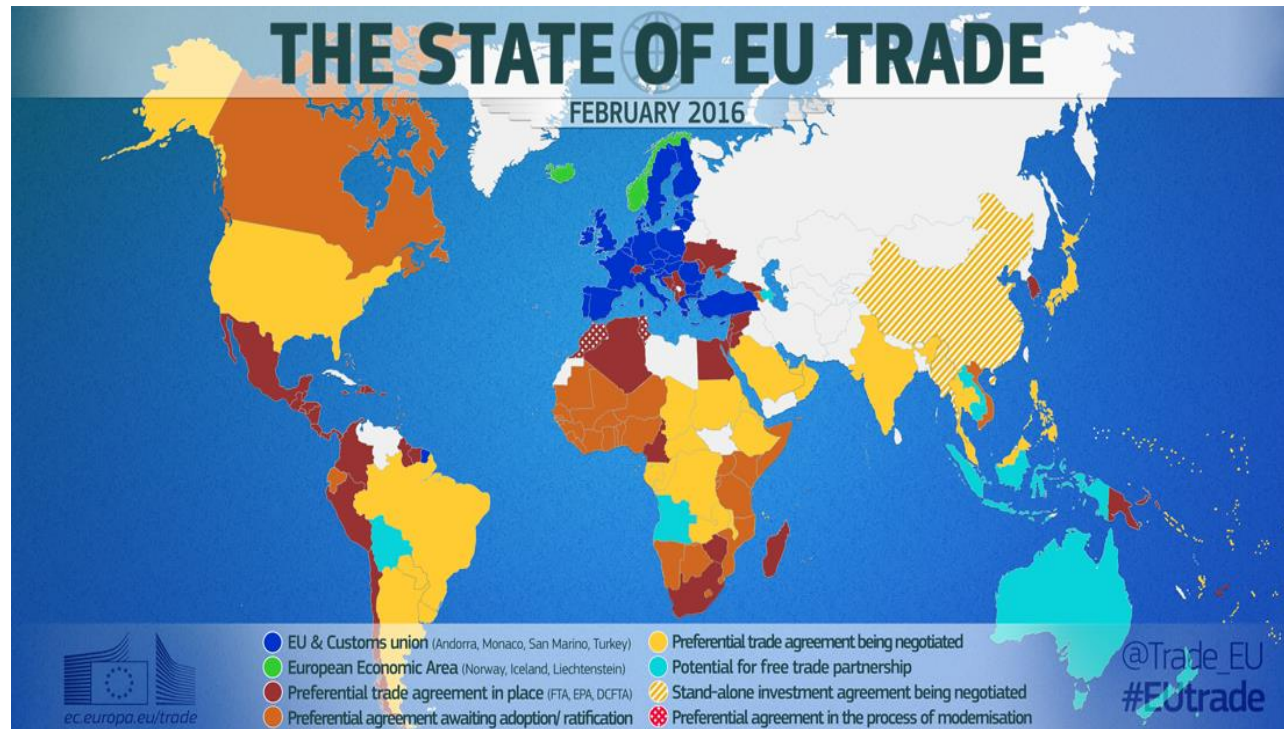
Preferential ROOs for Automotive

- **Pan-Euro-Mediterranean Convention (PEM)**: based on a network of FTAs having identical ROOs;
- In addition to **bilateral** cumulation, PEM allows for **diagonal or full cumulation** in FTAs between the EU, EFTA states, Turkey, Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Palestine, the Western Balkans, Moldova and the Faroe Islands;
- For the automotive sector: Commodities under HS codes 8701-8708:

HS heading	Description of goods	Rule
ex Chapter 87	Vehicles other than railway or tramway rolling-stock, and parts and accessories thereof	Manufacture in which the value of all the materials used does not exceed 40 % of the ex-works price of the product

- Contrary to non-preferential rules of origin, the PEM established a threshold on **non-originating materials (NOM)**.
- Vehicles failing to meet the 40% NOM threshold cannot qualify for preferential treatment in the PEM region (no residual or secondary rule).

Preferential ROOs for Automotive



- In addition to PEM, the EU has a large network of FTAs with **standalone ROOs protocols**;
- Among others, the EU has signed FTAs with Korea, Canada, Vietnam and the CARIFORUM.
- Potential future partners include Japan, MERCOSUR and Australia.

Preferential ROOs for Automotive

- While trading with FTA partners outside the PEM area, compliance with the **FTA-specific ROOs** is necessary to qualify for preferential treatment (e.g. zero tariff on auto exports to Korea)

EU-Korea FTA			
HS heading	Description of goods	(1) Rules	(2)
8701 to 8707 and 8712	Vehicles other than railway or tramway rolling-stock; bodies and chassis fitted with engines for the motor vehicles of headings 8701 to 8705; bicycles	Manufacture in which the value of all the [non originating] materials used does not exceed 45 % of the ex-works price of the product	
8708 to 8711 and 8713 to 8716	Parts and accessories for vehicles of headings 8701 to 8705 and 8711 to 8713; Motorcycles; Works trucks and parts thereof; carriages; baby carriages and parts thereof; Trailers and semi- trailers and parts thereof	Manufacture from materials of any heading, except that of the product	Manufacture in which the value of all the [non originating] materials used does not exceed 50 % of the ex-works price of the product

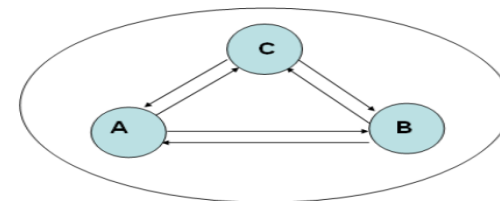
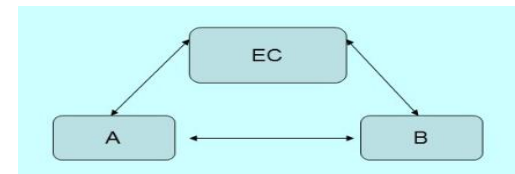
- Not only specific ROOs can change from treaty to treaty, FTA parties can also create ad-hoc solutions for ROOs **implementation**:
 - The recently agreed EU-Japan FTA establishes that for passenger cars (HS heading 8703) there is a staging period of 6 years, during which the threshold is at 55% max NOM the first 3 years and at 50% max NOM the following 3 years.

‘Originating’ v. ‘Local Content’

- **‘Local content’**: usually applied in the context of ‘Local Content Requirements’ imposed by governments for firms to be permitted to operate in an economy, or to qualify for government support or public procurement
- **‘Originating’**: usually the preferred term in ROO. An item could be entirely made from foreign materials or components but still qualify as originating. This happens, for example, when ROOs confer originating status depending on where a specific process has been carried-out (e.g. the operation of “diffusion” for integrated circuits confers origin regardless of the semiconductor’s source)
 - Differentiating between UK content and products originating in the EU can be particularly complex.
 - Local content and originating materials could be ascertained by checking the **Bills of Materials (BOMs)** throughout the supply chain

Cumulation of Origin

1. **Bilateral**: input originating in Country A can be treated as originating in Country B for exports back to Country A
2. **Diagonal** (or regional): input originating in Country A can be treated as originating in Country B for exports to Country C
3. **Full**: all processing carried out in Countries A, B, C or D can be included towards qualifying as originating in Country A for exports to any of the others



Typical ROO Rules

- **‘Minimal Operations’** - insufficient to confer originating status, even when combined (e.g. packaging, simple cutting, assembling or mixing)
- **‘Tolerance’** or **‘de minimis’** - if the non-originating materials do not exceed a percentage of the ex-works price (e.g. 10%)
- **Absorption principle:** once a product has obtained originating status all non-originating inputs used in its manufacture are considered to be originating
- **‘Direct transport’** - to ensure that the goods arriving in the country of import are the same as those which left the country of export
- **‘No Drawback’:** Most FTAs prohibit exemption from customs duties on imports from third countries to be used in the manufacture of goods to be exported to the other FTA Party, to prevent competition distortions.
- **Proof of origin:** exporters need to provide documentary, verifiable proof of the originating status of their goods.

Brexit: Potential Mitigations

- **Rules of Origin:** Pan-Euro-Mediterranean Regional Convention.
 - UK and EU27 exporters are already familiar with these rules
 - UK could benefit from cumulation with other Parties, as well as with third countries, once it concludes FTAs them based on identical rules
- **Cumulation:** ensure bilateral cumulation; aim for full cumulation or diagonal accumulation depending on the current arrangements
 - Full cumulation operates within EU, EEA and some other countries eg Maghreb
- **Proof of Origin:** the REX system allows self-certification by exporters, simplifying the process. EU intends to apply in all future FTAs: already in the EU-Canada FTA
- **Transitional arrangements:** to continue current arrangements until UK concludes FTAs with EU and third countries, and joins PEM Convention

Questions and Answers

Please click on the hand symbol to raise your hand if you have a question.

Please ensure that you are connected to the audio to ask a question.

Alternatively, you can type your question.



Email: **memberservices@smmt.co.uk** with your questions after this session.

Slides emailed to participants after this session.

Thank you

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