

Determinants and Impacts of Rules of
Origin in
Australia's Free Trade Agreements

By

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THESIS

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Uwe Kaufmann

Abstract

This thesis investigates the determination of the rates of utilisation of Australian free trade agreements (FTAs).

The topic is important and interesting because the utilisation rates show the usage of the agreements by traders. Low utilisation rates imply that trade agreements fail in their objective.

Following a review of relevant literature, the study presents data on the utilisation rates of Australia's preferential trade agreements (PTAs) over the time frame of 2000-9. This work requires some care in the definition of the utilisation rate, a matter which is discussed in detail in the presentation of this part of the empirical work. It is found that utilisation rates vary a lot. The variations appear to be related to low preferential tariff margins and the degree to which there are strict rules of origin (ROO). These rules are associated with FTAs to manage the problem of trade deflection (TD). The ROO schemes of five Australian FTAs are investigated and a ROO restrictiveness index is developed and applied to these five Australian trade agreements. The main findings are that all five ROO regimes differ significantly between the agreements, indicating that ROO are negotiated according to criteria beyond their role in managing TD.

A question of interest therefore arises about the set of important determinants of ROO. One hypothesis in the literature is that more restrictive ROO are negotiated in tariff lines with relatively high preferential margins. To examine and test this hypothesis in detail, a political economy (PE) model is applied. PE and TD factors are taken into account in a test of the relative importance of these different factors. The results confirm that TD concerns in form of potential transshipment are reflected by ROO design;

however this is the case only for the Australian agreements with its developing country partners. The results also show that more restrictive ROO are negotiated in tariff lines with high applied tariff rates and for commodities where a potential import penetration may occur. The higher the potential competition in the form of trade penetration and the higher market access in the form of low preferential tariff rates, the more restrictive are the negotiated ROO. Therefore, these results suggest that ROO are used as both a trade protection and as a tariff substitution tool.

The research then returns to the question of the impact of ROO on the utilisation rates and trade development in Australia's FTAs. An equation is estimated in which the relationship and impact of ROO and preferential tariff margins on the utilisation rates is tested.

To avoid endogeneity between tariff rates and ROO as identified in this thesis, the study employs the instrumental variable method by using the results of the determinants of ROO as an instrument.

Two main hypotheses are examined, namely (1) do more restrictive ROO increase trade costs and with that lower the application of preferential treatment in form of utilisation rates, and (2) do preferential tariff margins serve as an incentive to apply for preferential treatment.

The results show a strong negative relationship between the degree of restrictiveness of ROO and the utilisation rates and a positive relationship between preferential tariff margins, and utilisation rates.

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List of Abbreviations

ABS	Australian Bureau of Statistics
ACS	Australian Customs Service
ACTA	Australian Customs Tariff Act
ASTP	Australian System of Tariff Preferences
AFTA	ASEAN Free Trade Area
AUS-FTA	Australia United States Free Trade Agreement
APEC	Asian Pacific Economic Community
AV	Adjusted value
A\$	Australian dollars
BEC	Broad Economic Classification index
CER	Australia New Zealand Closer Economics Relation Trade Agreement
Chile/AUS-FTA	Chile Australia Free Trade Agreement
CTC	Change in tariff classification
CUs	Customs Unions
DFAT	Department of Foreign Affairs and Trade
FTAs	Free Trade Agreements
GATT	General Agreement on Tariffs and Trade
GDP	Gross domestic product
GSP	Generalized System of Preferences
HS	Harmonized System
JS-EPA	Japan-Singapore Economic Partnership Agreement
JETRO	Japan External Trade Organization
LDCs	Least Developed Countries
MFN	Most favoured nations
NAFTA	North American Free Trade Agreement
NC	Net cost
PACER	Pacific Agreement on Closer Economic Relations
PATCRA	Papua New Guinea Australia Trade and Commercial Relations Agreement
PE	Political economy

PTAs	Preferential Trade Agreements
OCTA	Office of the Chief Trade Adviser
OECD	Organisation for Economic Co-operation and Development
ROO	Rules of origin
ROO-i	Rules of origin restrictiveness index
RTAs	Regional Trade Agreements
RVC	Regional value content
SAFTA	Singapore Australia Free Trade Agreement
SPARTECA	South Pacific Regional Trade and Economic Cooperation Agreement
TAFTA	Thailand Australia Free Trade Agreement
TD	Trade deflection
TR	Technical requirements
TV	Transaction value
UNCTAD	United Nations Conference on Trade and Development
VNM	Value of non-originating materials
VOM	Value of originating materials
VUOM	Value of materials with uncertain origin
WCO	World Customs Organization
WTO	World Trade Organization