

Transitional preferential rules of origin under the PEM Convention

Introduction & background

On August 24, 2020 the European Commission adopted a legislative package of proposals regarding the Rules of Origin under the Pan-Euro-Mediterranean ('PEM' or 'PAN-EUR-MED') Convention. The new rules (or: transitional rules) are intended to modernize and update the rules of origin as described in the origin protocols of the trade agreements in the PEM region by making them more flexible and user-friendly. Economic integration and trade facilitation are the drivers of this initiative.

However, this package does not contain a formal amendment to the comprehensive PEM Convention. This concerns an amendment to the original origin protocols¹. The transitional rules will enter into force on September 1, 2021. Initially, the rules will apply between the EU and Switzerland, Norway, Iceland, Albania, Jordan and the Faroe Islands. The other partner countries will adopt the transitional rules at a later date.

The Dutch Customs Authorities ('DCA') have published guidance on the transitional rules. This guidance includes specific information regarding the rules of origin under the revised PEM Convention and, for example, instructions for accordingly submitting a customs declaration. This information was published on their website on August 23, 2021 and is included in the Dutch Customs Manual (*Handboek Douane*) under 'Notification 13'.

On August 25, 2021 the European Commission published a non-binding guidance document. The Commission will also publish a matrix regarding the adoption of the transitional rules among the trading partners. A reference to this matrix will be placed on the website of the Commission and the DCA in due course.

Rules of Origin – highlights of amendments

Highlights of the new rules include:

Full cumulation

Under the transitional rules, 'full cumulation' or 'full diagonal cumulation' is introduced for most products. In short, this means that the necessary operations/added value for a product to benefit from preferential tariffs can be split between several countries applying the transitional rules for most of the products. In this regard it is important that the countries involved in the supply chain/cumulation accept the transitional rules of origin.

Please note that the products in Chapters 50-63 can only benefit from full cumulation on a bilateral basis (i.e. when two countries involved in the cumulation agree to do so). Additionally, the proof of origin (EUR.1 or origin declaration) should include the following statement: "*Cumulation applied with [name of country/countries]*".

¹ The origin protocols of the following PEM countries: Albania, Bosnia and Herzegovina, Egypt, the Faroe Islands, Georgia, Iceland, Israel, Jordan, Kosovo, Lebanon, Liechtenstein, Moldova, Montenegro, North Macedonia, Norway, Palestine, Serbia, Switzerland, Turkey, and the Ukraine.

The following two criteria should be met in order to apply cumulation under the transitional rules:

- There must be a preferential agreement between the contracting parties participating in the acquisition of originating status and the contracting party of destination.
- The goods acquired their originating status by applying identical rules of origin.

Increased thresholds of tolerance

The thresholds of tolerance for non-originating materials will be increased from 10% to 15%. This threshold usually relates to the ex-works value of the products, with the exception of agricultural products. In the latter case, this percentage refers to the net weight of the products.

Duty drawback

Currently, a duty drawback prohibition applies under the PEM Convention. This means that duties on imported goods used for production in the EU cannot be reclaimed. Under the new rules, this prohibition will be lifted for most products. Consequently, savings opportunities may arise, for example when making use of an inward processing regime.

Accounting segregation

The revised PEM Convention introduces more flexible accounting segregation rules when using fungible materials. Currently, accounting segregation is only allowed for originating and non-originating materials if it can be demonstrated that considerable costs are incurred or material difficulties arise in keeping separate stocks. This requirement is no longer included under the transitional rules, which means there is now more flexibility. Materials are only considered to be 'fungible' when they are identical and interchangeable. This also means that they should have the same commercial quality.

In the Netherlands, the accounting segregation authorization is part of the Approved Exporter authorization.

Direct transport/non-alteration

Under the revised PEM Convention, the direct transport rule has been replaced with the non-alteration rule (also called 'non-manipulation') which offers greater flexibility in transporting goods through third countries. The direct transport rule complicates maintaining the preferential origin when goods pass through another territory. Non-alteration allows for transit through third countries if exporters can prove that the goods have not been 'manipulated' or altered during the transit. Splitting of consignments in a third country is also allowed, provided that the goods remain under customs supervision. In practice, non-alteration can be substantiated by, for example, requesting a certificate of non-manipulation.

Proof of origin

The proof of origin that can be submitted under the PEM Convention will be limited to the EUR.1 movement certificate or origin declaration issued by the exporter. A EUR-MED certificate therefore no longer applies. The EUR.1 certificate or origin declaration is valid for a period of 10 months (under the 'normal' rules this is four months). The wording "*transitional rules*" should be indicated in section 7 of the EUR.1 certificate if the transitional rules of origin are applied.

In addition, two new codes have been created in TARIC to be used in customs declarations:

- U075 for the EUR.1 movement certificate
- U076 for the origin declaration.

Impact on business & next steps

In summary, the new rules of origin under the PEM Convention provide greater flexibility and it is therefore worthwhile exploring the options available for using tariff preferences that may apply to your products upon importation into the EU. Our dedicated team of customs advisors has extensive practical experience with rules of origin and can assist you with the following matters:

- Potential savings opportunities arising from the transitional rules under the PEM Convention and, more specifically, in light of the duty drawback prohibition having been lifted
- Origin planning
- Submitting proof of origin
- Obtaining Binding Origin Information ('BOI') rulings from the DCA
- Assistance with applying cumulation.

If you have questions regarding rules of origin or other customs-related topics, feel free to contact our Trade & Customs team.

KPMG Meijburg & Co
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