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FTA with Asean, Korea in process

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India-Association of South East Nations (Asean) and India-Korea Free Trade Agreement (FTA) emerged from the Indian government's 'Look East' policy to tap growing markets in the East Asian nations.

Pursuant to signing up of FTA with Asean member countries and with Korea in August 2009, the Indian government has recently issued notifications giving effect to custom duty benefits to specified products under these FTAs; these duty benefits are effective from January 1, 2010. It should be noted that duty benefit available to eligible products under FTA, is with respect to basic custom duties; additional duties would continue to apply at the applicable rates.

Both agreements prescribe liberal rules of origin (ROO) as compared to earlier pacts executed by India, specifically from the value-added content perspective; eg, India-Singapore Comprehensive Economic Cooperation Agreement prescribes value-added content of 40% and change in tariff classification (4 digit) for non-originating materials; whereas both these FTAs require value addition of 35% and change in sub-tariff classification (6 digit) for non-originating materials.

A broad overview of the Asean and Korea agreement indicate that duty rates specified in the Asean pact generally are more beneficial to Indian importers as compared to duty rates under the Korea agreement.

However, specific comparison may show different results too, like Korea agreement seems to be beneficial for import of iron and steel products, whereas imports of sugar and sugar confectionary products and cocoa and cocoa preparations required for confectionery industry, photographic or cinematographic goods and machineries seem beneficial under Asean agreement.

From business planning perspective, it is imperative for the businesses to know the current rate of effective duty under the specific FTA, but it is also important to have a perspective on possible reduction in duty rates on import of raw material, inputs and finished products in the future; a full perspective will enable businesses to take strategic decisions based on the tax cost associated with import of goods into India. The tax cost will be vital to 'manufacture-vs-import' decision for products benefited by the change in tariff rates under the FTA.

For example, aluminium can manufacturers in India should expect more competition from 2014 because of duty-free imports of aluminum cans manufactured in Asean member countries. On the other hand, cost of inputs, such as aluminium coils, will come down because of the proposed gradual reduction of basic customs duty to 'nil' rate by the end of 2013.

In many cases especially under the Korea agreement, since the base duty rate of 2006 has been considered for the proposed reduction, the reduction in basic custom duty rates in subsequent years has not been factored into while notifying rates.

This may result in a scenario where the current rate of effective duty is less than the duty rate notified under the FTA, which makes the FTA a redundant exercise. For instance, machineries classified under HSN 8430 currently attract custom duty of 7.5% whereas the duty prescribed under the Korea agreement is 10.94%.

This is a good next step as a part of government's vision to integrate with the Eastern market. Though, there appears to be a convergence in local value-added content criteria under the two agreements, harmonisation of key definition like 'identical goods', 'goods', 'indirect materials', etc and alignment of method of calculation of local value added content could have eased out the situation for importers.

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