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IS INDIA HEADING TOWARDS TRADE PROTECTIONISM: AN ANALYSIS OF CAROTAR RULES?

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Abstract

With the announcement of Self-Reliant India Mission, the Government of India has announced several policy measures to promote domestic manufacturing to make India, as a hub of global manufacturing. One of its major policy measures is the introduction of Customs (Administration of Rules of Origin under Trade Agreements) Rules, 2020 (CAROTAR Rules). The objective of these rules is to regulate frivolous imports of the third country, which is routing to the Indian market via its FTA partners. These rules have created 'lots of hues and cry' among importing and exporting firms due to their regulatory, operational and business implications. This article examines key provisions of CAROTAR rules and their implications to India's foreign trade sector in general and exporting and importing firms in particular. Findings show that CAROTAR rules are highly protective and regressive in nature and designed to safeguard the domestic manufacturing industry. The intent and content of these rules clearly demonstrate that importing firms are subject to strict regulatory compliance to claim preferential benefit under India's existing trade agreements. New rules will increase the cost of importing inputs and components thereby affecting India's trade competitiveness.

Keywords: CAROTAR rules, free trade agreements trade protectionism, customs, imports, global value chains.

1. Introduction

The Covid-19 pandemic and resultant lockdown have led to severe fall in global demand and a supply-side shock to the world economy. The crisis has encouraged countries to pursue policies that enhance domestic manufacturing and make their supply chain more resilient. The Government of India (GOI) has made a clarion call for

"Self-Reliant India Scheme" to revive the ailing economy from the disastrous effects of Covid-19.

The Self-Reliant India Scheme emphasizes on the expansion and development of the manufacturing sector thus, stimulating the growth of the Indian economy. It focuses on five fundamental pillars: a) Economy, b) Infrastructure, c) System, d) Vibrant Demography, e) Demand. The Self-Reliant India Scheme complements to other initiatives such as Make in India, Digital India and Skill India. It also underpins the importance of disincentivizing the imports of those goods which can be produced indigenously. However, the government has categorically stated that reducing the import dependence needs not to be viewed as "import protectionism" or as "import substitution" (Financial Express, 2020). The objective of Self-Reliant India Scheme is to make India's domestic manufacturing sector competitive so that it can sustainably compete and participate in global supply chains.

In this context, a number of policy measures reflect that India is adopting inward-oriented policies that extend import protection to the domestic manufacturing sector. The most visible changes include policy restrictions on importable goods mandating licensing requirements, increase in tariff and non-tariff barriers. India has increased the import duties on many products. Average import tariffs have increased from 13 percent to 18 on industrial products covering almost 2500 tariff lines in recent years. Similarly; India has also imposed restrictions on imports of many product categories, for example, India has banned the import of air conditioners and refrigerants with the view to promote domestic manufacturing.¹ Likewise, India has banned imports of 101 military pieces of equipments to augment local defence manufacturing. Additionally, the GOI has advanced policies relating to non-tariff measures (NTMs). It has introduced Omnibus Technical Regulations (OTR) for machinery and electrical equipment's to ensure that domestic and imported products comply with mandatory standards, minimum acceptable safety standards and environment and performance standards.² The GOI has advised the Bureau of Indian Standards (BIS) to introduce mandatory standards for 5000 products to regulate imports of low quality and spurious products.³ Proliferated policies pertaining about NTMs are gaining lots of importance to restrict imports as they align with provisions on Technical Barriers to Trade (TBT) Agreement of the WTO. The import-restricting impact of such policies is far higher than traditional trade policy instruments.

A recent study by Export-Import Bank of India (2020) states that the Self-Reliant India Scheme can substitute imports of worth US\$186 in key product categories

¹ Directorate General of Foreign Trade (DGFT) Amendment in import policy of items under ITC HS 84 and 85, Notification 41/2015-2020, dated 15 October 2020.

² Govt to mandate BIS certification for safety of machinery; move to curb Chinese imports. Hindu Business line, 2 August 2020

³ Govt working on strategy on import regulation of non-essential items, Financial Express 30 December 2019

such as electronics, machinery, chemical and allied sectors. This discernibly highlights that India is embracing policies that are inward-looking and protective in nature. Chatterjee and Subramanian (2020) review a set of trade policy measures and argue that India is following protectionist policies by considering the fact that its domestic demand is not scalable to make the domestic firms globally competitive. They further argued that the size of the domestic market may be bigger in the case of specific product items but it is not true at the economy-wide level. Such policies will not help domestic firms to achieve economies of scale to become globally competitive. Moreover, India's growth story is strongly driven by export-led growth and certain imports are critical for manufacturing exports.

The Union Budget 2020 contains several measures to discourage import of finished and semi-finished products such as electrical appliances, mobile phones, commercial vehicles and electric vehicles (Ministry of Finance, 2020). The most significant development is that it brings a tectonic-shift in the country's policy orientation towards foreign trade by introducing the Customs (Administration of Rules of Origin under Trade Agreements) Rules, 2020 which aims to monitor the third-country imports under existing free trade agreements of India. It is believed that these rules are likely to have far-reaching implications to the India's foreign trade sector. Against this backdrop, this article is segregated into four parts. Section 1 provides a brief overview of India's existing free trade agreements, followed by an analysis of provisions relating to RoO therein. It further examines product-specific cases to understand how third-country imports are enjoying preferential benefits in India via its FTA partners. Section 2 provides the broader contour of CAROTAR Rules. Section 3 examines the key provisions of CAROTAR Rules and its implications to the India's foreign trade sector and how these rules are heading India towards an inward-orientation thus reversing the trends of three-decade of the steady opening of the economy. It further examines the scope and substance in undermining of the potential economic opportunities to integrate Indian economy with the 'global value chains'- (GVCs) through free/regional trade agreements. Section 4 summarizes the main findings.

2. India's Free Trade Agreements

India has embraced a calibrated approach towards FTAs in the late 1990s, as a part of its "Look East Asia Policy" (now called as Far Act East Asia Policy). This policy is a key driver for India's bilateral and regional economic engagements with the neighboring countries (Singh, 2015; and Karmarkar, 2013). India's proclivity towards FTAs was shaped by its long inward-looking and import-substitution policies. It is clearly reflected from its first phase of FTAs under "Early Harvest Programme" (Roy and Banerjee, 2013; Anuradha, 2011). India has signed a series of FTAs with neighboring countries such as Nepal, Bhutan, Afghanistan and Sri Lanka and has signed Agreement on South Asia Free Trade Area (SAFTA) with SAARC member states. Learning from the experiences of these trade agreements motivated India to embark on the path of

advanced trade agreements with South East Asian economies. India has inked a spate of bilateral and regional trade agreements with advanced economies such as Singapore, ASEAN, Thailand, Malaysia, Japan and South Korea. The main objective of these trade agreements is to promote the economic growth, employment generation, foreign exchange accumulation, trade expansion and export diversification to effectively utilise vast resources of the country and to speed up the process of socio-economic development.

Table 1. India's Trade Agreements

Bilateral Agreements	Regional Agreements
1. India-Sri Lanka FTA (2000)	1. India-ASEAN (2010)
2. India-Japan CEPA (2011)	2. Asia Pacific Trade Agreement (APTA) (1975)
3. India-Korea CEPA (2010)	3. Agreement of South Asian Free Trade Area (SAFTA) (2006)
4. India-Malaysia CECA (2011)	4. India-MERCOSUR (2009)
5. India-Nepal Trade Treaty (1950)	5. Global System of Trade Preference (1989)
6. India-Thailand EHS (2004)	
7. India-Chile PTA (2007)	
8. India-Afghanistan (2013)	
9. India-Singapore CECA (2005)	
10. India-Bhutan Agreement on Trade & Transit (2016)	
Unilateral DFTP Scheme (34 LDCs) (2008)	
Afghanistan, Bangladesh, Benin, Burkina Faso, Burundi, Cambodia, Central African Republic, Chad, Comoros, Eritrea, Ethiopia, Gambia, Guinea, Guinea Bissau, Haiti, Lao PDR, Lesotho, Liberia, Madagascar, Malawi, Mali, Mozambique, Myanmar, Niger, Rwanda, Senegal, Somalia, Sudan, Timor-Leste, Togo, Uganda, Tanzania, Yemen, Zambia	

Source: Department of Commerce, Government of India (as on 14 October 2020)

Table 2 provides an aggregate view of India's trade with the world and FTA partners. India's total export to world were US\$322.8 billion in 2019 while total imports in the same year were US\$480 billion thus resulting to a total trade deficit of US\$157 billion. India's exports with FTA partners were US\$ 72.3 billion in 2019 and imports were US\$101 billion with a trade deficit of US\$ 29.4 billion. It is important to mention that India's trade with FTA partners is significant and account one fifth of total trade of India. A large number of studies demonstrate that India's experience with FTAs has not been favourable in terms of trade and resulted in higher trade deficit (Saraswat et.al, 2017; Economic Survey 2016; Reserve Bank of India, 2019; Kher and Das, 2019). India's trade deficit has increased for prominent value-added sectors exhibiting a deteriorated quality of India's trade with its advanced FTA partners such as ASEAN, Japan, Singapore and South Korea. This has flagged serious concerns over the benefits of these trade agreements and their usefulness in larger industrial and economic development.

Table 2. India's Trade with FTA partners (US \$ billion)

	2015	2016	2017	2018	2019
Total Exports	263.9	261.0	295.9	324.0	322.8
Total Imports	390.8	356.7	443.9	509.3	480.0
Trade Deficit	-126.9	-95.7	-148.0	-185.3	-157.2
Exports to FTA partners	56.3	54.4	69.2	76.1	72.3
Imports from FTA partners	82.4	75.5	90.0	106.1	101.7
Trade Deficit with FTA partners	-26.1	-21.1	-20.7	-30.0	-29.4
% share of imports from FTA partners	21.3	20.9	23.4	23.5	22.4
% share of exports to FTA partners	21.1	21.2	20.3	20.8	21.2

Source: ITC Trademap, 2020

A common view is that India's inability to leverage trade agreements is because of the shallow depth and coverage of trade agreements (Wignaraja, 2012; Singh 2015). India's FTA are rather narrowly confined to trade in goods and have low coverage on other critical areas such as services, investment, competition, government procurement and trade facilitation (Karmakar S, 2013; Wignaraja, 2012). To put it in other words, India's trade agreements are not in line with 21st century trade agreements that contain advanced provisions related to 'WTO-plus' and 'WTO-extra' issues and emphasize on deeper regulatory disciplines that augment 'GVCs and production sharing agreements' (Baldwin, 2011). Further, India has not been able to effectively utilize its trade agreements and their average utilization rate is only 27 per cent (The Economist, 2014). Low usage of FTAs is due to lack of knowledge among exporters, high cost of regulatory compliance and other procedural hassles (The Economist, 2014). It is worthwhile to mention that limited trade gains from FTAs coupled with low level of integration in GVCs are not only because of shallow trade provisions negotiated under the trade agreements but, there are many other domestic factors that curtailed India's ability to benefit from international trade agreements (Bhattacharyya and Mandal, 2014; Francis, 2015; Sikdar & Nag, 2011). These include a weak domestic manufacturing sector, trade supply chain bottlenecks, inverted duty structure, business and regulatory hurdles (Puri, 2017; Sahoo and Bhunia 2014). The unfavorable experiences from various FTAs have dampened the interest of India's policymakers to pursue new trade agreements. India has refused not to join a mega-regional trade pact (Regional Comprehensive Economic Partnership) in the Asia-Pacific region. It has also slowed-down the pace of on-going trade negotiations with trade partners such as European Union, Canada, Australia, New Zealand and the United Kingdom.

2.1 RoO provisions under India's Trade Agreements: Key Issues

RoO has been one of the most important areas of international trade negotiations due to its far reaching trade and investment implications (Ratna and Das 2014). One of the main objectives of RoO is to ensure that goods produced and traded within an FTA area satisfy the local content requirement to claim the benefits of preferential tariffs. There are different types of criteria used in RoO. They can be broadly placed under wholly-obtained or wholly produced, substantial transformation (value addition) with a change in tariff classification (CTC) such as Change in Tariff Heading (CTH), Change in Tariff sub-heading (CTSH), and Change in Chapter (CC) to take the benefits of preferential treatment (Estevadeorda et al., 2003; Vermulst et al., 1994)

India adopted the conservative approach towards RoO under its different FTAs and negotiated differential criterion pertaining to value-addition and CTC (CUTS, 2015). Table 3 demonstrates India's provisions on RoO in its different trade agreements. RoO under India-ASEAN FTA is 35 per cent and CTSH at six-digit while in its FTA with Thailand; it is 40 per cent coupled with CTH at four-digit and in case of Sri Lanka, it is 35 per cent and CTH at four-digit. Further, India's approach towards product-specific RoO (PSR) is quite different across the negotiated trade agreements. There are only few trade agreements such as ASEAN, Japan and South Korea where India has negotiated product-specific RoO in certain product categories. This demonstrates that Indian policymakers have not followed a uniform approach for RoO under the various trade agreements.

One of key reasons for a muddled approach towards RoO in India's FTA is that its partners have varying trade profiles, trade specialization and comparative advantages. It is, therefore, challenging to adopt a standardized approach for RoO in all FTA partners. This view holds a lot of economic rationale given the diversity of India's FTA partners but it disregards the very basic fact that lack of uniformity in RoO across various trade agreements has severe economic implications for a large number of Micro, Small & Medium Enterprises (MSMEs), which play an important role in production and exports. The main implication is that varying RoO criteria under FTAs force MSMEs to set-up separate production lines for export manufacturing to different markets. This puts an additional financial burden on MSMEs to establish different lines of production to cater to varying FTA markets. This also disincentivizes them to achieve higher economies of scale and scope to become globally competitive. The complex and varying requirements for RoO impact firms' trade induced investment decisions and restrict the potential opportunities for domestic firms to plug in value chain networks through trade agreements. Firms tend to prefer RoO that facilitates them to move up on the value chain with a significant degree of cost optimization.

Table 3. Provisions on RoO in Selected India's Free Trade Agreements

India-ASEAN	35 % + CTH
Agreement on South Asia Free Trade Area	NOM $\leq$ 60% + CTH, PSR, 10% relaxation to LDC, 5% to SL
India-Sri Lanka FTA	NOM $\leq$ 65% + CTH
India-Malaysia CECA	[35% + CTSH] or PSR
India-Singapore	[35% + CTSH] or PSR
India- Nepal	[35% + CTSH] or PSR
India-Japan	[35% + CTSH] or PSR
India- South Korea	[35% + CTSH] or PSR
India-Thailand	[40% + CTH] or PSR

Source: Author's construction based on Department of Commerce website 2020.

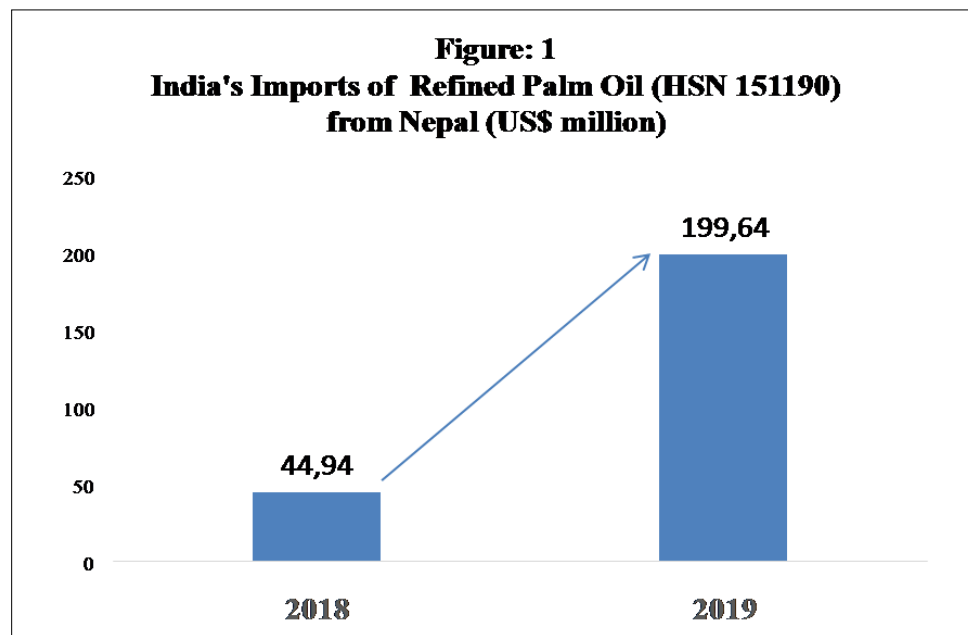
RoO under India's FTAs have received vociferous criticism in the view of undue benefits enjoyed by third-country imports via its FTA partners. Industry Associations, Chambers and Export Promotion Councils have made several representations to the Department of Commerce to check and monitor third-country imports under FTA partners (Rajya Sabha Secretariat, 2018; Chanda, 2017; Livemint 2019). Studies on FTAs have also raised similar concerns with regard to a sudden increase in imports of specific product categories from FTA partners (Saraswatet.al, 2017, Chanda, 2017;Francis 2020).Few of them stated that Chinese goods are moving into India via its FTA partners such as Bangladesh, Vietnam, Singapore and Sri Lanka (Business Standard, 2018; Hindu Business Line, 2019; The Wire, 2020).In this context, it is pertinent to analyse the product-specific cases to understand how the third country goods are entering into the India market via FTA partners.

Cases of Palm Oil, Electrical and Machinery products

India has witnessed a sharp rise in imports of palm oil from Nepal in the past one year. Prior to this, India's imports of palm oil from Nepal were negligible. Imports of palm oil (HSN 151190) were US\$ 44.94 million in 2018 and increased US\$199.64 million in 2019 with an annual growth rate of 344 per cent (Figure:1) This has emerged as a major concern for the domestic edible oil industry. An industry association Solvent Extractors Association (SEA) stated that a sharp increase in import of Palm oil from Nepal is because of transshipments of Malaysia and Indonesia consignment via Nepal to India to take the benefits of preferential tariffs.⁴ Import duty on palm oil (HSN 15119020) under India-ASEAN FTA and India Malaysia FTA are 45 per cent and 40 per cent respectively.

⁴ Krishana Prasain, Nepal's palm oil exports could suffer as India suspends import licences, The Kathmandu Post 2020. <https://kathmandupost.com/money/2020/05/14/nepal-s-palm-oil-exports-could-suffer-as-india-suspends-import-licences>

On the other hand, imports of palm oil under SAFTA attract merely 6 per cent import duty. This acts as an incentive to Nepalese exporting firms to source palm oil from Malaysia and Indonesia and to export it to India under the SAFTA. Nepalese exporting firms follow three steps to export palm oil to the Indian market. They first import crude palm oil, process and package it and export it to India; thus, fulfilling the customary requirement of value addition.



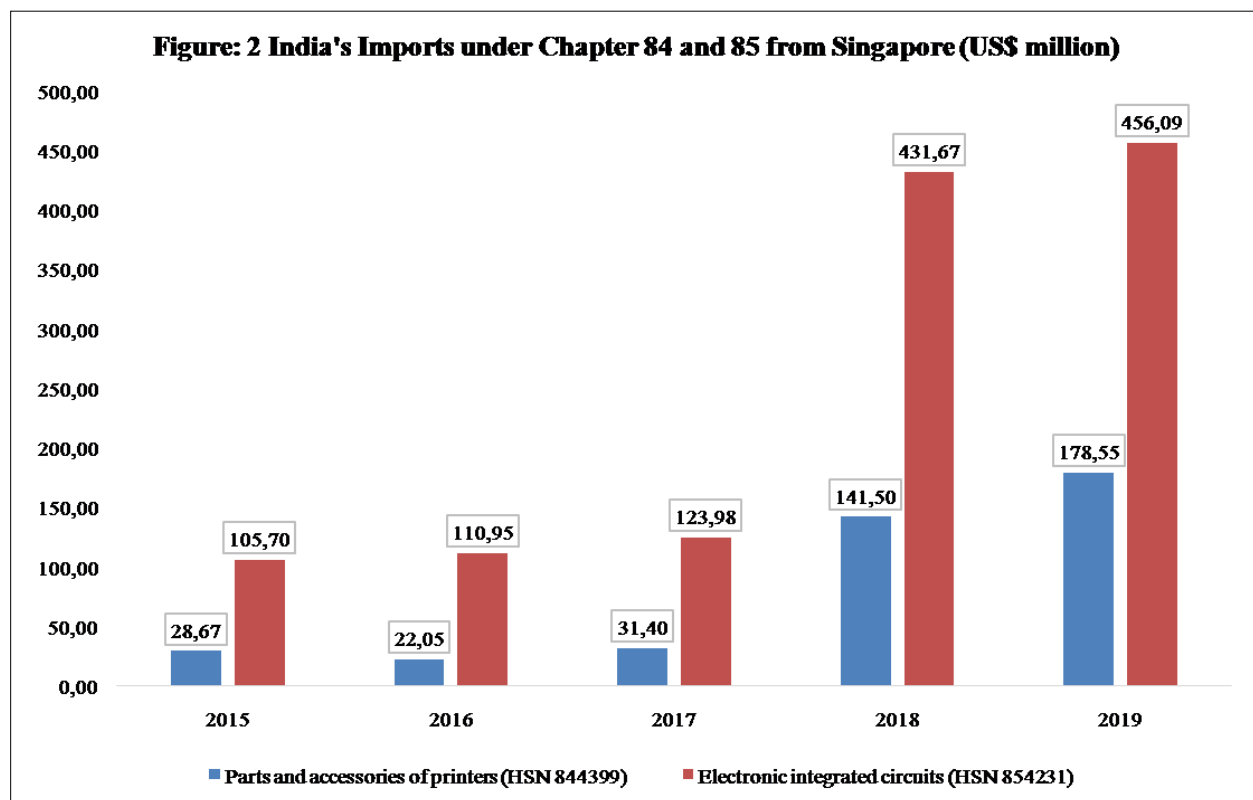
Source: ITC Trade Map 2020,

Nepalese exporting firms are flouting RoO requirements under the SAFTA to take the benefits of preferential market access due to differential in import duty structure. This is resulting inconsiderable revenue loss to the GoI. In the view of such malpractices, the Directorate General of Foreign Trade (DGFT), a trade policy formation and execution body, under the Ministry of Commerce and Industry, GOI has introduced "strict policy conditions for the import of Palm oil" in the country.⁵

Similarly, India has experienced a consistent increase in imports of parts and accessories of printers (HSN 844399 and electric integrated circuits (HSN 854231) from Singapore. India's imports of parts and accessories of printer (HSN 844399 and electric integrated circuits (HSN 854231) reached to US\$ 431 million and US\$ 456.1 million in 2019 from US\$ 28.6 and US\$ 105.7 million in 2015 with annual growth rate of 74 per cent and 58 per cent respectively (Figure: 2). It is noteworthy to elucidate that Singapore has limited domestic production capacity in these two products and its

⁵ Directorate General of Foreign Trade, Conditions on Import of Refined Palm Oil, Trade Notice No 2/2020-21, 13th April 2020.

exports to other global markets is reflecting a downward trend. Indian Electrical & Electronics Manufacturers' Association (IEEMA) has expressed their concerns regarding Chinese imports entering to Indian market through FTA partners (Financial Express, 2020; Economic Times, 2020). An increase in imports of these products reinforces the argument that Chinese exportable goods are making a backdoor to the Indian market via India's FTA partners. It is needless to mention that China is a dominant supplier of these products and occupies more than 60 per cent share in the global market of electrical and machinery products.



Source: ITC Trademap 2020

The aforementioned product-specific cases of possible diversion of goods via third- country provides interesting insights how non-FTA partner is flouting FTA rules to route its exportable goods into India. These cases corroborates that a third-country is moving goods via one FTA partner to another take the benefits of differential duty structure in different trade agreements (e.g. India-Malaysia CEPA and India Nepal Treaty of Trade). Third country goods are moving into India via its FTA partners (e.g. Chinese goods are moving into India via Singapore). These issues are highly pertinent to India's policymakers as it not only hurts the domestic manufacturing sector but also causes significant revenue losses.

The GOI is of the view that third-country imports entering the Indian market need to be monitored if India has to scale-up and strengthen its domestic manufacturing capabilities. It is a point of reference that cheap and low-quality imports routing through our FTAs partners are not only causing harm to the domestic manufacturing sector but they are curtailing the innate capacity of our domestic manufactures to expand, diversify and compete in global markets. This brings the importance of regulating frivolous third-country imports in the country to strengthen the domestic manufacturing sector under the Self-Reliant India Scheme. In the Union Budget 2020, the Finance Minister Nirmla Sithraman stated that "it has been noted that imports are increasing under FTAs by taking undue advantage of preferential tariff rates which in turn hurt India's manufacturing sector. It is therefore imperative to introduce a stringent check to regulate such imports and suitable provisions are being introduced through CAROTAR Rules 2020 under provisions of Custom Act 1962.

3. The CAROTAR Rules 2020

The Central Board of Indirect Taxes and Customs (CBIC) vide its notification No. 81/2020 - Customs (N.T.) dated the 21st August, 2020 introduced Customs (Administration of Rules of Origin under Trade Agreements) Rules, 2020.⁶ The objective of these rules is to restrict the misuse of preferential benefits to third-countries under India's trade agreements. The CAROTAR 2020 broadly outlines six rules. First rule relates to the information required and the procedure to be followed for claiming "*preferential tariff treatment*". It states that the importing firm, while filing the Bill of Entry⁷ (BOE), needs to provide information of imported goods. This includes CoO reference number, date of issuance of CoO, origin criteria, and the information of third-country origins under back to back CoO. Second rule pertains to "*origin related information*" and expresses that the importing firm should provide information in the Form I regarding the '*origin-criteria*' including regional value content and product-specific RoO. Additionally, it also states that importing firms need to maintain the record of all supporting documents, at least for the period of five years from the date of filing of BOE.

The third rule is regarding the "*requisition of information*" and asserts that if Customs Officer has any reason to believe that the information provided by importing firm is not accurate; the officer may ask to the importing firm to furnish the information within ten working days from the date of such information or document being sought. Fourth rule relates with "*verification request*" and states that Customs Officer may ask

⁶ Customs (Administration of Rules of Origin under Trade Agreements) Rules, 2020. Notification No. 81/2020 - Customs (N.T.) dated the 21st August, 2020, Central Board of Indirect Taxes and Customs.

⁷ A bill of entry is a legal document that is filed by importers or customs clearance agents on or before the arrival of imported goods.

or order an importing firm for the verification of CoO from the Verification Authority. The verification of the imported goods will be carried-out to determine the authenticity of the CoO and its compliance with RoO provisions under trade agreement. Fifth rule focuses on the "*treatment of identical goods*" and states that if the importing firm fails to origin criteria stipulated in trade agreement, the Principal Commissioner of Customs or the Commissioner of Customs may reject the goods for preferential benefits without any further verification. The officer may also reject other preferential claims filed by the importing firm prior to or after such determination for identical goods being imported from the same exporter. The last rule is regarding the "*miscellaneous provisions*" and provides for preventive and punitive action(s) to be taken by the Customs Officer, in case, the importing firm provides misleading or false information or else suppresses the information to be given in the CoO.

3.1 Implications of CAROTAR Rules to India's Foreign Trade Sector

In the reference of broad discipline as imposed under the CAROTAR Rules, this section analyses the implications to India's foreign trade. The CAROTAR Rules introduce overarching "provisions" to avail the benefit of preferential treatment on imported goods from FTA partners. This section examines how CAROTAR Rules will put burden on importing firms to ensure that they fulfill the RoO criterion for imported products

- The Section 28DA of the Customs Act 1962 states that an importing firm can claim preferential treatment by submitting the CoO in the stipulated form at the time of import of goods. It further extends regulatory powers to Customs Officials to seek verification of CoO from the Issuing Body of the exporting country as per the guidelines prescribed in the FTA. The CAROTAR Rules bring major changes in the Section 28A and states that the Customs Officials enjoy discretionary powers to reject the entitlements of preferential tariffs if an officer has "reason to believe" that origin criteria as negotiated under an FTA has not been fulfilled. It is worth exploring that the term "reason to believe" provides '*sweeping powers*' to the Customs Officer to adjudicate the eligibility of the preferential benefit. The term "reason to believe" is open for interpretation, therefore; the outcome could be influenced by the whims & fancies of the Custom Officer. The discretionary powers as extended to Customs Officer under the CAROTAR Rules will lead to rent-seeking attitude of Customs Officials and adversely affect the "Ease of Doing Business" in India.

- Rule 4 of the CAROTAR Rules elucidate that an importing firm should provide the "*origin related information*" of imported goods at the time of filing of Bill of Entry for import clearance. Further, the said rules states that the importing firm will be the "first query point" which means the new rules are shifting the responsibilities of Government to Government (G2G) activities to Business to Government (B2G), thus increasing compliance cost on an importing firm. It deserves the delving of policy-orientation and

future actions of GOI in detail. The CoO is issued by the Government Empanelled Agencies in the exporting country which undertake the mandated regulatory due diligence while issuing the CoO. It is therefore, the responsibility of Issuing Agency (ies) in the exporting country to ensure that exported goods must comply with rules as negotiated and framed under the respective trade agreement. It means if there is any issue related to accuracy of the information in the CoO; it should be dealt between G2G. Unfortunately, the new rules bring onus on the importing firm to ensure that the information given in the CoO is authentic and the imported goods meets the criterion stipulated for preferential treatment. Thus, the CAROTAR Rules are inconsistent with fundamental rules of origin-criteria compliance as negotiated in various trade agreements. This shift in the responsibility is a vis compliance on origin-criteria on importing firm puts more burden and compel it to multiply its efforts to obtain relevant information from the exporting firm/Issuing Agency. Further; the rules put all burden on the importing firm only vis a vis authenticity of information, compliance, cost so associated and punishes it if not so complied. Rules do not provide a fair level playing field to the importing firms to engage globally in a fair, transparent and rule-based manner.

- Rule 5 (a) is related to origin related information under the CAROTAR Rules and states that an importing firm shall maintain the information connected to Form I for every shipment for the period of at least five years from the date of import clearance and submits the same to the Proper Officer whenever desired. This includes the information pertaining to origin-criterion Wholly Obtained, Regional Value Content, Change in Tariff Classification and Change in Chapter. The new rules propose that importing firms need to provide the detailed information regarding the value of content, components used in manufacturing and other costs (labor cost, material used, overhead expenses, etc) if the imported goods are from the non-originating material. Even, the rule deserves analysis, explanation and understanding in detail. If the goods are manufactured with non-FTA partner country inputs, then there is a high probability that the exporting firm may not be willing to provide the confidential price with respect to intermediate inputs and components used in such exportable manufactured products. The information sought under Form I regarding the non-originating material used in exportable products is extensive, necessitating the minutest details which are not possible in globally inter-connected manufacturing operations. Further; the issue becomes even more complicated if the exporting firm refuses to share the information of the whole value chain, creating problems for the importing firm to prove that goods are "substantial transformed" to qualify for preferential benefits. The failure to obtain the required information may deprive the importing firm to avail the preferential benefits thus increasing the cost of imported products.

• Rule 5 (b) under the CAROTAR Rules states the importing firm shall maintain “supporting document” related to Form I for 5 years. It further states that an importing firm shall “exercise reasonable care to ensure the accuracy and truthfulness”. With respect to this provision, there is no clarity regarding the nature of “supporting documents” and what format and datasets shall be admissible. In the same manner, it is difficult to ascertain what parameters shall be used to determine “exercise reasonable care to ensure the accuracy and truthfulness”. Provisions laid down in the Rule 5 of the CAROTAR Rules lack clarity and give tractable administrative leeway to Customs Officers to use their discretionary powers to take the decisions on extending or not extending the preferential benefits to an importing firm.

• Rule 7 is regarding the identical goods under the CAROTAR Rules and states that if the importing firm “*do not meet origin criterion*” for the stipulated RoO in a trade agreement, the Principal Commissioner of Customs may, without verification, reject other claims of preferential tariff, filed prior or after such determination, for identical goods imported from the same exporting and importing firm”. This rule will have the implications to both importing as well as exporting firms. An importing firm may be importing the identical goods from the same exporting firm throughout the year. In case, it fails to comply with the origin-criteria of CoO due to some reason(s) for a particular imported consignment, it should not be penalized for all consignments which have been imported or are yet to arrive. This rule completely undermines the right of the importing firm to claim preferential benefits. From the exporting country perspective, this rule curtails the effective market access under a trade agreement. Further; this could also escalate to a very complicated situation for an exporting firm which supplies identical goods to 10 different importing firms in India. The failure of one firm not to meet the origin-criteria will lead to cascading deleterious effects on all other such importing firms, rejecting their claims for the preferential benefits.

• The CBIC has also notified amendments regarding provisional duty assessment under Section 18 of the Customs Act, 1962 and the CAROTAR Rules. All importing firms, henceforth, need to comply with notified amendments and CAROTAR Rules. Further, they are required to furnish 100 per cent differential duty as a security if a provisional assessment is undertaken by the importing firm when an investigation is initiated in terms of Rule 5. All types of importing firms including the one, availing Authorized Economic Operators status (AEO) and Status-Holders Entitlements can, no longer enjoy the benefits of self-certification. Further, the benefit of Approved Export Scheme of DGFT for CoO is not exempt from CAROTAR Rules and need to comply with. It is appropriate to mention that the importing firms under the AEO, Approved Export Scheme and Status-Holder Scheme are certified by Customs/DGFT on their proven track record of credibility for self-certification. In normal course; they are entitled to faster clearance(s) of their exportable as well as imported cargo and are not required to furnish duty amount/bank guarantees even under the provisional assessment. The

introduction of CAROTAR Rules defeats the very basic purpose of such trade facilitating schemes thus making import business more time-consuming and cumbersome.

- The CAROTAR Rules disregard the principles of free trade agreements as stringent checks on imports may deprive exporting firm(s) to get the benefits of preferential treatment. The said rules negate and subvert the very basic purpose of a trade agreement for which it was signed. Reciprocally; India's decision to put stringent checks on imports may provoke and instigate its FTA partners to undertake similar measures which will ultimately lead to trade protectionism, thus benefiting the business interests of other countries. Further, imports are critical for exports in 'value-chain led trade' and firms; relying on competitive intermediate inputs from FTA partners; will be subject to regulatory and compliance related burden, which will have a cascading effect on the cost of doing business in India. Indian trade firms can eventually become uncompetitive in value-chain led trade. One can argue that such import-dependent value-chain led export firms can leverage Advance Authorization or Duty-Free Import Authorization Scheme to duty-free imports of intermediate inputs to be used in exported products. To counter this argument; it is reasonably estimated that many of the exporting firms in India are MSMEs and lack managerial, procedural and technical capabilities to avail and comply with such duty-free schemes for imports of inputs and intermediates. Moreover, intermediates and other inputs imported for exportable products under Advance Authorization require dynamic linkage between exportable product and imported inputs to qualify for the duty-free benefits. Additionally; such duty-free schemes can be best leveraged by the export firms having assured export orders.

4. Conclusion

The article examined the CAROTAR Rules and their impact on the importing and exporting firms in India to avail the preferential benefits under FTAs. It maps the recent developments in trade policy and argues that India is heading towards a restrictive and protective trade regime by imposing restrictions in the import regime, hiking import tariffs and introducing non-tariff measures aimed at increasing compliance costs for importing firms. From a theoretical perspective, it underlines the specific concerns of availing duty-preference under existing FTAs especially the third-country imports. It further delves deep on issues of re-routing or channelizing of third-country import into the Indian market via its FTA partners, thus availing unjustified and unfair benefits of preferential treatment. It analyses the product-specific cases of Palm Oil, Electrical and Machinery in which India has witnessed a massive rise in imports from Nepal and Singapore. The article corroborates with data-evidence that the fact that Malaysian and Chinese goods are routing into Indian market via Nepal and Singapore to take the benefits of preferential tariffs. This is happening in a broad range of product categories where non-FTA partners are routing their shipments into India via FTA partners thus

adversely affecting the orderly growth and development of the domestic manufacturing sector. This issue has received immense importance under the Self-Reliant India Scheme and accordingly; the GOI has introduced CAROTAR Rules which stipulates stringent provisions and compliance-mechanism regarding the CoO to restrict third-country imports via India's FTA partners. New rules bring key amendments in the Section 28DA of the Customs Act 1962 pertaining to filing of BOE and regulatory compliance therein. These rules create the concerns for the importing firms as they shift the onus from G2G to B2G, thus making it mandatory for the importing firms to ensure that any CoO issued by notified agency(ies) of the exporting country must comply with RoO criteria of the mutually negotiated FTA. The responsibility for proving the genuineness and authenticity of CoO has been fixed on the importing firm. The said rules squarely oppose to the provisions of FTA in which responsibility vis-à-vis genuineness or authenticity of CoO lies with the issuing agency of the exporting country.

New rules further states that if the importing firm fails to comply with RoO, the preferential benefits will not be extended to it for the furtherance of business. Further; the benefits given for previous consignments for the last five years under preferential tariff will also be investigated and duty-benefit so availed; will be recovered with penalty and interest on duty saved. These rules seem to be highly regressive in nature and undermine the spirit of free trade and commerce, thus disrupting the orderly and fair development of the competitive supply chains. The CAROTAR Rules states that if an officer has 'reason to believe' that origin-criteria as negotiated under a trade agreement has not been complied, it extends discretionary powers to the Customs Officer to reject preferential benefits to any such importing firm. Further, the restrictive policy regime for the imports will have a detrimental impact on the firms that participate in value-chain networks through backward participation. They will curtail the potential scope of sourcing competitive imported intermediates, inputs, parts and components from low cost destination(s) thereby making the final products uncompetitive in the value-chain led foreign trade.

The CAROTAR Rules are against the fundamental principle of FTA that underpins the importance of 'free trade' These rules will lead to the erosion of preferential market access of the exporting countries and will force them to take similar measures to safeguard their commercial interests. This will ultimately lead to greater trade protectionism. Finally, the underlying intent and content of CAROTAR Rules flag several concerns for the importing firms and contributes to the uncertainty in the trading environment. They explicitly support the Self-Reliant India Scheme aimed at import protection, thus furthering the business cause of domestic manufactures. It will be noteworthy to see how import protection will help domestic firms to enhance their productivity and efficiency to compete in a liberalized and globalized market. Lastly; these rules will significantly affect ease of trading across borders and will lead to uncertainty in the overall trading environment of India.

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