KPMG

China Tax Alert

Issue 37, November 2020

Regional Comprehensive Economic Partnership – impacts for China and the Asia Pacific region

Summary:

- 15 countries have joined together to sign the largest ever free trade agreement, known as the Regional Comprehensive Economic Partnership ("RCEP") on 15 November 2020. RCEP may be considered as a framework for facilitating free and more streamlined trade arrangements between RCEP countries.

Overview

15 November 2020, and after a reported 8 year period of negotiations, 15 countries have joined together to sign the largest ever free trade agreement, known as the Regional Comprehensive Economic Partnership ("RCEP"). In its simplest form, RCEP may be considered as a framework for facilitating free and more streamlined trade arrangements between RCEP countries, recognising that the countries comprising RCEP consist of both developed and developing countries. It is also highly symbolic, coming at a time of recent trade tensions and tariffs.

RCEP brings together the 10 ASEAN states (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam) with 5 other partner countries (Australia, China, Japan, New Zealand and South Korea). According to the Joint Leaders statement signed on 15 November 2020, RCEP will "cover a market of 2.2 billion people, or almost 30% of the world's population, with a combined GDP of US$ 26.2 trillion or about 30% of global GDP, and accounts for nearly 28% of global trade (based on 2019 figures)."

At an earlier stage of the negotiating process, India had been a party though it later withdrew, but could potentially re-engage with RCEP in the near future. Interestingly, Hong Kong as a member of the World Trade Organisation is not a party in its own right to RCEP as of now, but has expressed a desire to join RCEP as its first new member economy. (Source: Comments attributed to the Acting Secretary for Commerce and Economic Development, Dr Bernard Chan, in the Legislative Council, 11 December 2019).

The global pandemic has heightened the need for many businesses to reconsider their supply chains, with a number of key trends emerging such as regionalisation, digitalisation, near-shoring, reshoring, and rebasing of manufacturing all being evident features. Customs and tariffs, government subsidies, the changing costs of and access to labor, and taxation are all having an impact on these decisions. RCEP will play a critical role in this assessment process, and even act as a trigger for supply chain reorganisations.

Key features of RCEP – regional impacts

1. In formal terms, RCEP comes into force when at least six ASEAN Member States and three non-ASEAN signatories ratify it into domestic law. Commentators have ranged in their predictions anywhere from 6 months to 2 years for this to occur.
2. The primary purpose of RCEP is to serve as an overarching mechanism for the bringing together of free trade between the 15 countries. That is, RCEP brings together a single set of rules and procedures for accessing preferential tariffs across the region.
3. In a practical sense, a key achievement of RCEP is that it harmonises disparate rules of origin concepts, thereby providing greater levels of certainty and consistency for business in managing their supply chains across the region. More specifically, RCEP provides:
   - Standardised rules of origin for all participating countries – rather than examining individual rules of multiple bilateral agreements;
   - Standardised direct shipment (consignment rules), though in some instances, these rules are more restrictive than existing bilateral agreement consignment rules which may impact on existing regional distribution hub arrangements;
   - An opportunity to include multiple countries in the calculation of origin rules and access to preferential duty rates, which is critical with global supply chains; and
   - Standardised documentation requirements which, once again, may be more prohibitive than some bilateral agreement documentation requirements.

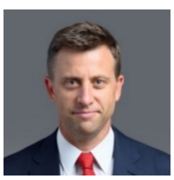
4. The benefits of harmonisation should not be under-estimated given the complexities of trade within the Asia Pacific region, especially as the trend for manufacturing shifts to less developed economies;
5. A key practical breakthrough with RCEP is the establishment of free trade for the first time between China and Japan, Japan and South Korea.
6. However, in seeking to achieve consensus amongst such a politically and economically diverse group of nations, certain compromises have inevitably occurred. For example, certain commentators have noted that RCEP does not remove tariffs on 39% of ASEAN's food exports, and in particular, many of Japan's agricultural tariffs still remain.
7. As against this, the scope of RCEP is very broad and in many respects, seeks to cover more ground than many traditional bilateral free trade agreements. In addition to trade in goods (including customs procedures, trade facilitation and standards, and trade dispute remedies) it also covers trade in services, including sectors such as financial services, telecommunications, professional services, and the temporary movement of business people. RCEP also includes chapters on investment, intellectual property, e-commerce, government procurement and competition (amongst others).
8. Although the immediate benefits of RCEP for the services sector are more modest, the framework of RCEP provides a platform through which foreign service providers are expected to be granted greater levels of market access. This is achieved through a transition from a 'positive list' approach (i.e. where certain services are permissible in a given country) to a 'negative list' approach (i.e. where services are permissible unless specifically excluded).
9. RCEP contains only limited change in the area of intellectual property protection and enforcement. However, in terms of e-commerce RCEP does contain new provisions which are intended to support small to medium enterprise engagement with e-commerce and the flow of data, promote privacy and consumer protection, and enable electronic authentication and electronic signature. Crucially though, the financial services sector is generally excluded from these measures.
10. RCEP does not cover areas such as environmental protection, government subsidies and the use of labor unions.

Whilst not removing the complexities of free trade agreement access and benefits in the short term, the hope is that RCEP will provide organisations greater long term certainty on the various rules of origin required to satisfy access to preferential duties, allowing them to streamline processes and procedures to qualify for a single agreement across multiple countries. The immediate priorities for organisations should be to examine the benefits (including phased preferential duty rates, documentation and direct shipment requirements) to determine if and when RCEP, once available, will be most advantageous to implement in place of the existing bilateral or multilateral free trade agreements they are currently utilising.

In summary, it remains to be seen whether the benefits of RCEP will truly be realised, with much of this being dependent on future decisions being taken by countries to adhere not only to the 'letter' of the agreements, but also to the 'spirit' and intent of RCEP. While the countries which are parties to RCEP may now account for around 30% of global GDP, this is anticipated to rise to nearly 50% by 2030. There is thus the potential for RCEP to serve as a major platform for global trade, but the major global platform. Perhaps most of all, the timing of RCEP could not have been more perfect, delivering a message of hope amidst a tide of challenges surrounding global trade cooperation.

Contact us:

National



Lachlan Wolfers
Indirect Tax Leader, KPMG China
KPMG Global Head of Indirect Taxes
T: +852 2685 7791
E: lachlan.wolfers@kpmg.com

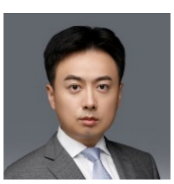
Northern Region

Eric Zhou
Trade and Customs Leader
KPMG China
T: +86 (10) 8508 7610
E: ec.zhou@kpmg.com

Eastern and Western Region

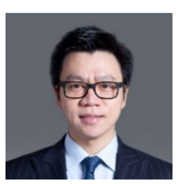
Rachel Tao
Director, Trade and Customs
KPMG China
T: +86 (21) 2212 3473
E: rachel.tao@kpmg.com

Southern Region



Philip Xia
Director, Trade and Customs
KPMG China
T: +86 (20) 3813 8674
E: philip.xia@kpmg.com

Hong Kong



Daniel Hui
Tax Partner
KPMG China
T: +852 2522 7815
E: daniel.hui@kpmg.com