Preparing for the implementation of the China-South Korea Free Trade Agreement (China-ROK FTA)

Background

On 25 February 2015, China and the Republic of Korea (ROK) initialled the text of the China-ROK Free Trade Agreement (China-ROK FTA), the most comprehensive FTA that China has negotiated. This FTA is seen as a boon for the development of advanced industries in both China and the ROK as demand for high-tech and high-quality products is projected to rise during the time till the FTA's full implementation. Since the announcement of this FTA, the ROK has already reported a surge of Chinese investments to strategically prepare for the cost savings it offers. For businesses eager to capitalize on this opportunity, the time to plan and act is now.

The official text is scheduled to be signed within the first half of this year, with implementation expected to follow in the second half. The text of the agreement, now only in English, will be translated into the official languages of the two countries before it is officially signed.

Salient points of the China-ROK FTA

- Matters relating to trade in goods have been the main focus of the FTA negotiations. China and the ROK agreed to eliminate tariffs on 90 percent of all goods, and 85 percent of imports by value within 20 years after the FTA becomes effective. Below is an overview of the tariff reduction schedule:

China	Republic of Korea
Adopt zero-tariff-rate on a number of electrical and electronic products including rice cookers, washing machines, refrigerators, medical equipment and parts for home appliances.	Phase out tariffs for motors and transformers in stages.
Liberalize trade in steel products such as cold-rolled steel, hot-rolled stainless steel and heavy plates.	Remove tariffs on articles for daily use such as handbags, golf clubs and other commonly imported goods.
Eliminate tariffs on 91 percent of all goods, and 85 percent of imports by value.	Eliminate tariffs on 92 percent of all goods, and 91 percent of imports by value.

Goods or sectors excluded from the tariff-reduction schedule are as follows:

a) Manufactured goods: automobiles and spare parts are not included either in the current tariff reduction or the foreseeable future of trade liberalization under this FTA

b) Agriculture and aquaculture products: rice, pepper, garlic, squid, anchovy, and octopus as well as other 20 kinds of aquatic items of Korea are excluded.

- The FTA will recognize products made in the Kaesong North-South Korean Industrial Complex as originating from the ROK, in a bid to accelerate economic integration in northeast Asia and promote peace and economic development in the region.
- The two countries shall establish a committee on Outward Processing Zones (OPZs) to guide the existing OPZ and make preparations for additional OPZs in the future.

Rules of Origin

- The general rule of origin under China-ROK FTA is that (unless otherwise stated) a good shall be considered as originating in either China or the ROK (each country referred to as a "Party") where:

  a) The good is wholly obtained or produced entirely in a Party

  b) The good is produced entirely in a Party, exclusively from originating materials; or

  c) The good is produced entirely in a Party using non-originating materials and conforms to Annex 3-A (publication pending)

- Goods listed in Annex 3-B (publication pending) which have undergone working or processing on materials exported from a Party, and subsequently re-imported to that Party for export to the other Party, in an area outside the territories of the Parties, shall be considered as originating, provided that:

  a) Total value of non-originating materials (VNM) shall not exceed 40 percent of the freight on board (FOB) price of the final goods for which originating status is claimed

  b) The value of originating materials exported from the Party concerned shall not be less than 60 percent of the total value of materials used in the processing of those goods.

- The Regional Value Content (RVC) shall be calculated as follows:

  RVC= (FOB-VNM)/FOB*100

  Where, RVC is expressed as a percentage and varies from 40 to 60 percent depending on the type of goods.

  For comparison: the Asia-Pacific Trade Agreement (APTA) adopts the following formula for calculating the content of non-originating materials:

  $$VNM/FOB*100 \leqslant 55\% \text{ (or } 65\%)$$

  Therefore, when applying for a certificate of origin to claim FTA benefits, domestic enterprises may choose whichever of the two FTAs (i.e., China-ROK FTA or the APTA) provides the greatest tariff reduction benefit.

- While the cumulative rules of origin in APTA require that "aggregate content originating in the territory of the Participating States is not less than 60 percent of its FOB value", the relevant provision for accumulation in the China-ROK FTA (Article 3.6) has no such limitation in percentage. Therefore, where originating goods or materials of a Party are incorporated into a good in the other Party, these goods or materials shall be regarded as originating in the other Party.
- The China-ROK FTA provides that the originating goods of the Parties claiming preferential tariff treatment shall be directly transported, or should comply with deemed direct-transportation principles. In the case of transit

or trans-shipment, transport documents such as the airway bill, the bill of lading, or the multimodal or combined transport documents covering the whole transportation route shall be submitted to the customs authority of the importing Party upon import declaration of the goods. In the case of storage or devanning of the containers in a Non-Party, the abovementioned transport documents as well as supporting documents provided by the customs authority of a Non-Party shall be submitted.

Origin Implementation Procedures

- The importer claiming preferential tariff treatment will follow this general process:
    a) Make a written statement in the customs declaration, indicating that the good qualifies as an originating good
    b) Possess a valid Certificate of Origin, at the time the above import customs declaration is made
    c) Submit the original Certificate of Origin and other documentary requirements related to the importation of the goods in accordance with their respective domestic laws and regulations.
- The importer can apply for refund of any excess duties, deposit, or guarantee paid as result of the good not having been accorded preferential tariff treatment no later than one year after the date of importation.
- A Party shall waive the requirements for the presentation of a Certificate of Origin for consignment of originating products of a customs value not exceeding USD 700 or its equivalent amount in the Party's currency. Waivers shall not be applicable when the importation forms part of a series of importations that may reasonably be considered to have been undertaken or arranged for the purpose of avoiding the submission of a Certificate of Origin.
- The importing Party shall not reject a Certificate of Origin only for the reason that the invoice was issued in a Non-Party, provided that certain requirements are complied with.

KPMG Services

With the FTA nearing its official signing and implementation, companies are advised to closely monitor developments and policies relating to the FTA. We recommend they review their list of goods (for import and export) as well as the relevant contracts to be more familiar with the status of their trade in goods. In addition, it is important for companies to train their customs staff or build an internal team to study and work on how they could benefit from this FTA.

KPMG's Global Trade & Customs Services Group in the Asia-Pacific Region is well-experienced in assisting enterprises in their utilization of free trade agreements and their compliance with the relevant Rules of Origin. In this regard, we can provide the following services:

- Consultation services for the application of the Rules of Origin and assessment of whether imported & exported goods enjoy preferential tariffs under the China-ROK FTA, or under other FTAs
- Assistance with applications for Certificates of Origin and receiving preferential tariff treatment
- Advisory and assistance with the planning and actual implementation of an FTA strategy
- Assistance or defense in case of challenges or disputes with the Customs authorities.

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