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# Japan tax alert

**Ernst & Young Tax Co.**

## Asia-Pacific countries sign Regional Comprehensive Economic Partnership (RCEP) Agreement

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## Executive summary

On 15 November 2020, 15 countries in Asia Pacific signed the Regional Comprehensive Economic Partnership (RCEP) Agreement at the fourth RCEP Summit. These countries include ASEAN member countries (i.e., Brunei, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam) plus Australia, China, Japan, South Korea and New Zealand.

Once it enters into force, RCEP will be the world's largest free trade agreement (FTA), which accounts for half of trade value of Japan and 30% of the global GDP. While ASEAN already has FTAs with the other 5 countries, it will be the first FTA available among China, Japan and South Korea. As China and South Korea are Japan's largest and third largest trading partners, respectively, and ASEAN and Australia are Japan's primary trading partners, RCEP may be a catalyst for the post-COVID economy in the member countries.

Although India left the RCEP negotiation in 2019 for concerns over impact of tariff elimination on its domestic industries, the Agreement provides that RCEP is open for accession by India from the date of entry into force. Ministers' Declaration on India's Participation in RCEP was also published at the RCEP summit.

RCEP will enter into force 60 days after the date on which at least 6 ASEAN signatory countries and 3 non-ASEAN signatory countries have completed ratification and notified the Depositary. Although this process may require some time, businesses should check if their exports and imports can benefit from duty elimination/reduction under RCEP and if they satisfy the rules of origin. If it is beneficial, businesses should begin the necessary preparation for using RCEP from the date of entry into force.

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# Duty elimination and reduction under RCEP

### 1. Market Access for Japanese exports

86%-100% of Japanese exports will be eligible for duty elimination or reduction under RCEP in ASEAN countries, Australia and New Zealand, while it is 86% in China and 83% in South Korea. While the duty elimination percentages in China and South Korea under RCEP are quite low compared to other existing FTAs, many of Japanese exports can nevertheless enjoy duty free access to China and South Korea with RCEP. While 8% and 19% of Japanese exports can be imported into China and South Korea duty free currently, 86% and 92% can be imported duty free under RCEP, respectively. The table below summarizes preferential tariff treatment under RCEP for certain major goods.

**Market Access of Japanese exports in China and South Korea**[1]

| Item | Importing Country | HS | Rate of duty | | | | | Rules of origin |
|---|---|---|---|---|---|---|---|---|
| | | | Base Rate | Year 1 | Year 2 | Year 3 | Final | |
| Beauty or make-up preparations | China | 3304.99 | 6.5% | No elimination/reduction | | | | CTH or RVC40 |
| | South Korea | | 6.5% | 6.1% | 5.6% | 5.2% | 0% from Year 15 | |
| Photographic film (instant print film in rolls) | China | 3702.31 | 5.0% | 0% from entry into force | | | | CTH or RVC40 |
| | South Korea | | 6.5% | 0% from entry into force | | | | |
| Men's or boy's shirts of cotton | China | 6205.20 | 16.0% | 14.5% | 13.1% | 11.6% | 0% from Year 11 | CC |
| | South Korea | | 13.0% | No elimination/reduction | | | | |
| Ferro-nickel | China | 7202.60 | 2.0% | 0% from entry into force | | | | CTH or RVC40 |
| Iron and non-alloy steel in ingots | China | 7206.10 | 2.0% | 0% from entry into force | | | | CTH or RVC40 |
| Engines for motor vehicles | China | 8407.90 | 18.0% | 16.90% | 15.8% | 14.6% | 0% from Year 16 | CTH or RVC40 |
| | South Korea | | 8.0% | No elimination/reduction | | | | |
| Gear boxes | China | 8483.40 | 8.0% | 7.5% | 7.0% | 6.5% | 0% from Year 16 | CTSH or RVC40 |
| | South Korea | | 8.0% | 8.0% | 8.0% | 8.0% | 0% from Year 20 | |
| LCD digital television | China | 8528.72 | 30.0% | No elimination/reduction | | | | CTH or RVC40 |
| | South Korea | | 8.0% | 7.5% | 6.9% | 6.4% | 0% from Year 15 | |
| Motor vehicles | China | 8703.23 | 25.0% | 15% (certain items are excluded) | | | | RVC40 |
| | South Korea | | 8.0% | No elimination/reduction | | | | |
| Bumper and parts thereof for motor vehicles | China | 8708.10 | 10.0% | 9.5% | 9.0% | 8.6% | 0% from Year 21 | CTH or RVC40 |
| | South Korea | | 8.0% | 7.5% | 6.9% | 6.4% | 0% from Year 15 | |
| Thermostats for refrigerators | China | 9032.10 | 7.0% | 6.4% | 5.7% | 5.1% | 0% from Year 11 | CTSH or RVC40 |
| | South Korea | | 8.0% | 0% from entry into force | | | | |

[1] Year 1 begins on the date of entry into force of the Agreement. The first day of the subsequent Years is 1 April of each year for Indonesia, Japan and the Philippines and 1 January of each year for the other member countries.

## 2. Market Access of RCEP-Origin Products in Japan

Under RCEP, Japan will eliminate or reduce tariff on 88% of products originating in ASEAN, Australia and New Zealand, 86% of products originating in China, and 81% of products originating in South Korea. For industrial goods (e.g., chemical products, textile products, etc.), applicable tariff will be eliminated immediately or will be reduced in stages from the date of entry into force of the Agreement. Rice, wheat, beef and pork, dairy products and sugarcane, which are considered as sensitive imports in Japan, were excluded from tariff elimination.

As RCEP will be the first FTA among China, Japan and South Korea, certain Chinese and South Korean goods can now enjoy lower tariff rate under RCEP when imported into Japan.

The table below summarizes preferential tariff treatment under RCEP for certain goods.

| Item | Importing Country | HS | Rate of duty | | | | | Rules of origin |
|---|---|---|---|---|---|---|---|---|
| | | | Base Rate | Year 1 | Year 2 | Year 3 | Final | |
| Orange juice containing added sugar | ASEAN, AUS, China, NZ | 2009.12.110 | 25.5% | 23.9% | 22.3% | 20.7% | 0% from Year 16 | CC |
| | South Korea | | | No elimination/reduction | | | | |
| Extracts, essences and concentrates of coffee (no sugar) | All RCEP countries | 2101.11.290 | | 0% from entry into force | | | | CC or RVC40 |
| Homogenised composite food preparations | ASEAN, AUS, China, NZ | 2104.20.000 | 12.0% | 11.3% | 10.5% | 9.8% | 0% from Year 16 | CC or RVC40 |
| | South Korea | | | No elimination/reduction | | | | |
| Food supplement with a basis of vitamins (sugar added, containing lactose, milk protein or milkfat) | All RCEP countries | 2106.90.261 | 12.5% | 11.4% | 10.2% | 9.1% | 0% from Year 11 | CTH or RVC40 |
| Colloidal precious metals | All RCEP countries | 2843.10.000 | | 0% from entry into force | | | | CTH or RVC40 |
| Tableware and kitchenware | ASEAN, AUS, NZ | 3924.10.000 | | 0% from entry into force | | | | CTH or RVC40 |
| | China, South Korea | | 3.9% | 3.5% | 3.2% | 2.8% | 0% from Year 11 | |
| Other articles of plastics | ASEAN, AUS, NZ | 3926.90.029 | | 0% from entry into force | | | | CTH or RVC40 |
| | China, South Korea | | 3.9% | 3.5% | 3.2% | 2.8% | 0% from Year 11 | |
| T-shirts of other textile materials | ASEAN, AUS, NZ | 6109.90.029 | | 0% from entry into force | | | | CC |
| | China, South Korea | | 7.4% | 6.9% | 6.5% | 6.0% | 0% from Year 16 | |
| Footwear with outer soles of rubber or composition leather for men | ASEAN, AUS, NZ | 6403.99015 | 30.0% or 4,300 yen/ pair, whichever is the greater | 20.3% | 18.9 % | 17.6% | 0% from Year 16 | CTH or RVC40 |
| | China | | | 20.6% | 19.5% | 18.5% | 0% from Year 21 | |
| | South Korea | | | No elimination/reduction | | | | |

### 3. Applicable rate of duty

The rate of duty applicable to goods imported under RCEP is different depending on the RCEP country of origin of the imported goods. The RCEP country of origin for an originating good is determined as follows:

a) The RCEP country of origin for an originating good is the country where the good acquired its originating status.

b) For originating good produced exclusively from originating materials, it is the exporting country, provided that the production process, other than minimal operations, occurred in that exporting country.

c) Notwithstanding, for an originating good identified by an importing country in its Appendix to Schedules of Tariff Commitments[2], the RCEP country of origin is the exporting country, provided that the good meets the additional requirement specified in that Appendix (e.g., valued added by 20% or more).

d) In the event that the exporting country of an originating good is not established to be the RCEP country of origin based on the above methods, the country that contributed the highest value of originating material used in the production of that good in the exporting country will be the RCEP country of origin.

## Rules of Origin

### Origin criteria

Rules of origin set out the requirements for a good to be considered as an originating good under RCEP, as well as cumulation, minimal operations and processes, De Minimis, direct consignment criteria, etc. The requirements for a good to be considered as originating good are if the good is:

(1) wholly obtained or produced in a member country,

(2) produced in a member country exclusively from originating materials from one or more of the member countries, or

(3) produced in a member country using non-originating materials, provided that the good satisfies PSR.

PSR may be wholly obtained (WO), change in tariff classification rule (i.e., CC, CTH or CTSH)[3], value added rule (i.e., Regional Value Content (RVC) of 40%) or chemical reaction rule (CR), depending on the good. For value added rule, the regional value content is calculated by using either of the following formulas:

(a) Indirect or Build-Down Formula: RVC = (FOB-VNM)/FOB×100; or

(b) Direct or Build-Up Formula: RVC = (VOM Direct Labor Cost+ Direct Overhead Cost + Profit + Other Cost)/FOB×100

### Proof of Origin

Importers may claim preferential tariff treatment under RCEP on the basis of a Proof of Origin. Proof of Origin can be any of the following:

(a) a Certificate of Origin issued by an issuing body

(b) a Declaration of Origin by an approved exporter

(c) a Declaration of Origin by an exporter or producer

With regard to (b) Declaration of Origin by an approved exporter, member countries will provide authorization to be an approved exporter on the conditions such as:

(1) the exporter is duly registered in accordance with the laws and regulations of the exporting country,

(2) the exporter knows and understands the rules of origin of RCEP,

(3) the exporter has a satisfactory level of experience in export in accordance with the laws and regulations of the exporting country,

(4) the exporter has a record of good compliance, measured by risk management of the competent authority of the exporting country,

(5) The exporter, in the case of a trader, is able to obtain a declaration by the producer confirming the originating status of the good for which the Declaration of Origin is completed by an approved exporter and the readiness of the producer to cooperate in verification and meet all requirements of rules of origin, and

[2] Schedules of Tariff Commitments and Product-Specific Rule of RCEP are based on 2012 edition of the Harmonized System.

[3] Change in tariff classification rule may exclude change from certain HS codes.

(6) the exporter has a well-maintained bookkeeping and record-keeping system, in accordance with the laws and regulations of the exporting country

With regard to (c) Declaration of Origin by an exporter or producer, Cambodia, Lao PDR and Myanmar will implement this no later than 20 years from the date of entry into force of the Agreement, while the other RCEP member countries will implement no later than 10 years. However, the implementation of (c) may be delayed for some ASEAN countries that have yet to implement such certification procedure for existing FTAs.

RCEP considers an inclusion of a declaration of origin by an importer as an additional Proof of Origin. It is likely that Japan Customs will implement this on imports to Japan from the date of entry into force of the Agreement.

## Action for businesses

Considering RCEP's potential benefits in comparison with existing FTAs, RCEP is not expected to replace the use of existing FTAs for many businesses. As such, businesses would find themselves using RCEP in addition to existing FTAs. As a result, compliance with FTA rules is expected to be more complex, and businesses would find FTA management more challenging.

Under RCEP, the Customs authority of importing country can conduct verification to determine whether an imported good qualifies as an originating good by means of a written request for additional information from importer, exporter, producer and the Customs authority of exporting country and a verification visit to the premises of the exporter or producer in the exporting country. Importer, exporter, producer and the Customs authority of exporting country are required to provide the requested information within 90 days at maximum. If the required information is not provided within this period, the Customs authority of importing country may refuse the use of RCEP.

While RCEP brings duty reduction opportunities and improved market access in the member countries, to continue to benefit from using several FTAs while staying compliant with FTA rules, businesses are encouraged to review their FTA operation and consider strengthening FTA management by taking advantage of technology and outsourcing service solutions.

For additional information with respect to this alert, please contact the following:

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