Uniform Customs Duty

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(Views are personal)

It can be shown that a single uniform import tariff implies that the effective protection for all producers is also equal to this single uniform tariff ('Towards a Competitive Economy: VAT and Customs Duty Reform', Arvind Virmani, Planning Commission Working Paper No. 4/2002-PC, April 2002). Thus all producers and all uses of capital and labour are equally protected. Such a system also eliminates the possibility of negative protection as well as arbitrarily high rates of protection. Such a system is neutral and equal for all value added by domestic producers, promotes efficiency and competitiveness and eliminates all administrative hassles and legal disputes about classification.

A single uniform rate of customs duty on all imports has many attractive features. It ensures that the nominal protection for all imports is the same thus eliminating all classification problems and disputes, resulting in substantial saving in administrative and legal costs. It also makes it much easier to administer the duty free import regime for exporters. As a single rate applies to all imports only a total value of imports needs to be specified in any advance license, making actual import 100% flexible. Similarly any draw back or refund only needs to have the value of imports used in export production. Most imports can in principle be on self-declaration basis with customs staff focusing their time and energy on checking smuggling (mis/non-declaration of quantity) and chronic misstatement of price. If in addition this rate is reasonably low the incentive for smuggling will be minimised and make the administrative problem of checking it, manageable.

There is much greater economic justification for a neutral customs duty regime than there is for a single uniform rate VAT (or CENVAT) with no exemptions, special excises or sales taxes. Such a regime will eliminate the continuous lobbying by special interest groups that now takes place and the special benefits to the rich and powerful that inevitably result from such lobbying. This is so because the benefit-cost ratio for an individual person/company is greater the larger its market share. The ability of Public sector units, whether in steel, oil or other sectors, to lobby for special protection through their administrative ministry and to thus distort the structure of customs duties has been amply demonstrated. As the cost of such lobbying is even less than for large private firms, the distortions can be even greater. This too would be eliminated.

The country should aim to achieve internationally comparable rates of import duty during the next 3-4 years and therefore recommend that a single uniform rate of basic customs duty of 5% be applied to all imported goods by 2008-9. All end-use exemptions should be abolished when this rate is achieved. ***At this point all anomalies would be removed with the exception of those arising from international agreements.***

The 'peak rate' should be reduced to 15% in 2005-6. A schedule of rate reductions should also be announced. The minimum duty on exempt items should be raised to 5% by 2006-7. The high rate exceptions to the peak rate should be specified in multiples of the peak rate and brought down in line with the peak rate till 2008-9. Thereafter the import duty on these items should be phased down to 5%.

The uniform rate of 5% will have the additional benefit of reducing our simple average tariff rates below those prevailing in neighbouring countries and in Vietnam & Thailand. Our economic interests will then become much more closely aligned with theirs. Indian industry and agriculture will have much less to fear from special free trade arrangements with our neighbours than is the case today. Similarly India would have a much better case for closer economic integration with ASEAN than it has today. We can then sign FTA agreements with any country without much danger of distorting bilateral and regional trade through trade diversion.

The 'peak' rate of duty, which is currently 20%, applies to manufactured goods, minerals and some agricultural goods. In addition many agricultural goods have rates that are higher than the peak rate. Overall, these rates are still among the highest in the world (43).

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