

## THE UK-INDIA TRADE SERIES

### THE INDIA – UK FREE TRADE AGREEMENT: A COMPREHENSIVE STEP TOWARDS INTEGRATING BILATERAL TRADE



India and the United Kingdom (UK) have announced the conclusion of negotiations and finalization of a comprehensive free trade agreement (FTA). As per the guiding principles of the WTO, the main objective of free trade agreements is to attempt to eliminate barriers to trade between economies. Seen in such light, the FTA is widely considered to be a model and represents a serious indication of deep economic integration between trading partners. The FTA not only aims to increase trade between the two countries across a range of sectors, including goods, services and technology, but there are also important and significant strides on other trade related aspects such as digital trade, facilitation, e-commerce and along with a Double Contributions Convention (DCC) tied with the FTA. Although the announcement sets out a set of agreed principles and a framework for the FTA, the actual terms of the FTA are still yet to be agreed.

## **Background**

In the backdrop of Brexit, an opportunity evolved to re-examine and adopt a fresh approach to securing comprehensive preferential trade for UK and its trading partners. The FTA has been a key objective of the Indian government and the UK Government. Securing beneficial conditions of market access for important goods and services between the countries being a key objective, India was also keen to extend the FTA benefits to secure enhanced conditions in relation to visas and taxes applicable for Indian nationals. The several and intense rounds of negotiations that the FTA has been subject of, reflects more of a win-win arrangement for both countries with potential reduction of trade and related barriers and restrictions. When executed, the FTA will be a “first of its kind” agreement for India and the UK. The FTA is expected to facilitate the target of doubling bilateral trade between India and UK by 2030.

## **Key Coverage Aspects**

**Trade in Goods:** The FTA, once finalised and becomes effective, aims at tariff elimination on around 99% of the tariff lines covering almost 100% of the trade value. The FTA opens opportunities for sectors such as textiles, marine products, leather, footwear, sports goods and toys, gems and jewellery as well as other important technically advanced sectors such as engineering goods, auto parts and engines and organic chemicals. There is expected to be special and immediate preferential tariffs on goods and components that will provide an advantage to medical technology companies as well clean energy market.

The key highlights of the FTA are as follows:

- Immediately on the FTA coming into effect, 64% of tariff lines will be eligible for tariff-free imports into India, which will include sophisticated manufacturing such as aircraft parts, scientific and technical measuring instruments.
- It will also include opportunities on tariff-free access for agri-food
- Imports from the UK of scotch whiskey, currently facing import duties of 150%, will see immediate cut in duties to 75% and staggered to 40% from year 10 onwards.
- Automobile sectors will see staged tariff reduction and market access starting with internal combustion engine (ICE) cars and transitioning to electric vehicles (EVs) and hybrid vehicles. Tariffs on cosmetics and toiletries such as soaps, shaving cream, face cream and nail polish will either be removed on day one or removed in staggered manner over 10 years. Currently, India levies customs duties ranging from about 60-100% on motor vehicles which is set to be reduced to about 10% over FTA period. This may be extremely beneficial for players who import the entire vehicle, however, where final vehicle manufacturing is completed in India, the exact benefits under the FTA will need to be assessed once the schedules are finalised.
- India is one of the fastest growing alcohol markets with per capita consumption of pure alcohol increasing from just 1.3 litres in 2005 to 2.7 litres in 2010, and an estimated 3.2 litres in 2023. Whisky exports from the UK to India were valued at approximately USD 139 million, even as they faced such a high import tariff of 150%. Meanwhile, India's whisky imports from across the globe surged nearly fourfold—from USD 46 million in 2010 to USD 212 million in 2020—highlighting a sharp rise in domestic demand.[1] An expected immediate reduction of import tariffs up to 50%, followed by a further phased reduction with respect to potable alcohols, is a significant development. It will promote greater imports of scotch whiskey and gin and will possibly reduce input costs for “Indian Made Foreign Liquor”. There is significant potential for windfall gains to artisanal and boutique names in this sector. In tandem, distribution, marketing and local partnerships will also be important factors.

[1] See <https://aakhya.substack.com/p/the-aakhya-weekly-145-india-the-uk>

**Trade in Services:** The main focus of the FTA will be on goods and, in particular, the issue of reciprocal access to professional services in India, does not appear to be accepted under the FTA. However, the FTA is expected to include provisions on enabling future cooperation. India has claimed to secure significant commitments on digitally delivered services for Indian service suppliers, particularly in professional services such as architecture and engineering, computer related services and telecommunication services, though the precise extent and impact of the FTA on trade in services will need to be analysed based on the actual provisions and commitments secured.

- The FTA is reported to provide beneficial treatment for many service sectors including telecommunications services, environmental services and construction services. As per the UK Government note, businesses in the covered sectors will not face restrictions such as limits on the number of businesses able to supply a service or need to set up a company or be a resident to supply their services in covered sectors.
- The FTA envisages a framework which is planned to be annexed for both countries to identify and encourage mutually interested UK and Indian relevant bodies to enter into negotiations on mutual agreements or arrangements for recognition of professional qualifications. These agreements or arrangements can streamline processes, but will not affect the autonomy of either country's relevant bodies to set, maintain and assess against the standards for their professions. In this regard, there is wide scope for market driven access increases through mutually beneficial engagements with actual stakeholders playing a key role.
- As regards financial services, the FTA contemplates important steps to support innovation in financial services, developing an efficient, safe and secure environment for cross-border electronic payments. On foreign direct investment, UK ownership or investment into Indian insurance or banking firms, foreign ownership is stated as being capped at 74%.
- The Indian government announced that the foreign direct investment cap in the insurance sector will be increased to 100%. This is yet to be implemented, but the two are clearly inconsistent. Perhaps it is the case that the FTA discussions did not take into consideration the FDI changes in the insurance sector, but when those changes are implemented we assume that all foreign investors, including those from the UK will be able to benefit from the higher cap.

**Temporary movement of natural persons:** The FTA will ensure that Indian and UK professionals can efficiently travel to attend conferences, transfer to an Indian branch of their organisation, and supply of service as part of a contract. This will benefit professionals and businesses across a wide range of sectors including engineering and architectural services, accountancy services, and management consultancy. Opportunities for talented and skilled Indians will open in the UK which is a major global centre for digitally delivered services due to its strong financial and professional services sectors and advanced digital infrastructure. There is also an assurance that that visa application processes will remain transparent, and that governments will not create unnecessary obstacles for professionals to travel, however no specific commitments are observed to allot long-stay visas or any new visa category.

**Digital Trade:** The FTA aims at reducing barriers to digital trade and promote compatibility of digital trading systems. Provisions will be finalised that support the use of electronic contracts and transactions as well as provisions on cross border data flows and data localisation, but without disturbing the standards of data protection applied by either countries. The exact details and commitments envisaged in the FTA will need to be carefully examined once the FTA is published.

**Government Procurement:** Under the FTA, UK companies are expected to get exclusive treatment under the 'Make in India' policy, which currently provides preferential treatment in government procurement to businesses which manufacture or produce in India. UK companies are expected to be treated as a class 2 supplier if at least 20% of their products or services are from the UK, granting them the same status that only Indian firms currently enjoy. However, the 'Make in India' preference will still apply for approved 'class 1' suppliers offering 50% or more of their goods or services from India. The government procurement provisions are likely to give UK businesses access to India's public procurement market, comprising approximately several thousand tenders significantly stimulating cross-border investment and transactions.

**Double Contributions Convention :** Along with the FTA, both countries have agreed to negotiate a reciprocal DCC which will seek to ensure that employees moving between the UK and India, and their employers, will be liable to pay social security contributions only in one country. The DCC may operate on similar principles to the UK's other Social Security Agreements such as with the EU, Switzerland, Norway, Canada, Japan, Chile and South Korea.

Preliminarily, it is sought that the DCC will not affect individuals' rights to access benefits from the country in which they pay social security contributions or the requirement to pay the UK immigration health surcharge. Currently, it is contemplated that the DCC will also ensure that employees temporarily working in the other country for up to 3 years will continue paying social security contributions in their home country, to prevent fragmentation of their social security record.

**Origin Requirements for goods:** The FTA is likely to have stringent rules of origin requirements, which will likely provide for not only specified value addition in the exporting country, but also specialised conditions such as to 'melt and pour' condition for iron and steel, etc. The philosophy appears to be "co-equal" rules which provide for product specific norms and conditions to provide higher adaptability to exporters to achieve compliance with origin requirement. Digital Certificate of Origin is also an aspect that may be pioneered under the FTA. The objectives are expected to prevent circumvention or third-country imports at concessional duty rates. For imports into India, enforcement measures concerning the origin requirements will be through the Customs (Administration of Rules of Origin under Trade Agreements) Rules, 2020 and importers will need to align their exporters to be in compliance with the aforesaid rules to secure the benefit of preferential tariffs.

**Next Steps and Outlook:** Now that the negotiations are concluded, the UK and India will work together to finalise the legal text of the FTA and produce the final treaty text which will be signed by the counterparts. The DCC will enter into force alongside the trade agreement. Entry into force will take place once both the UK and India have completed their ratification processes and may take some more months. The FTA is expected to support long-term investment, growth and overall trade facilitation and elimination of barriers by primarily promoting fair competition, better market access and a more level playing field to businesses. The FTA provisions may lead to reducing operational risks and attracting UK investments into India.

Several practical questions will also arise at the time of finalisation of the text, especially in respect of market access, rules of origin, tax treatment, and the DCC. Hence, businesses should watch this space and see how the final FTA terms unfold.

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