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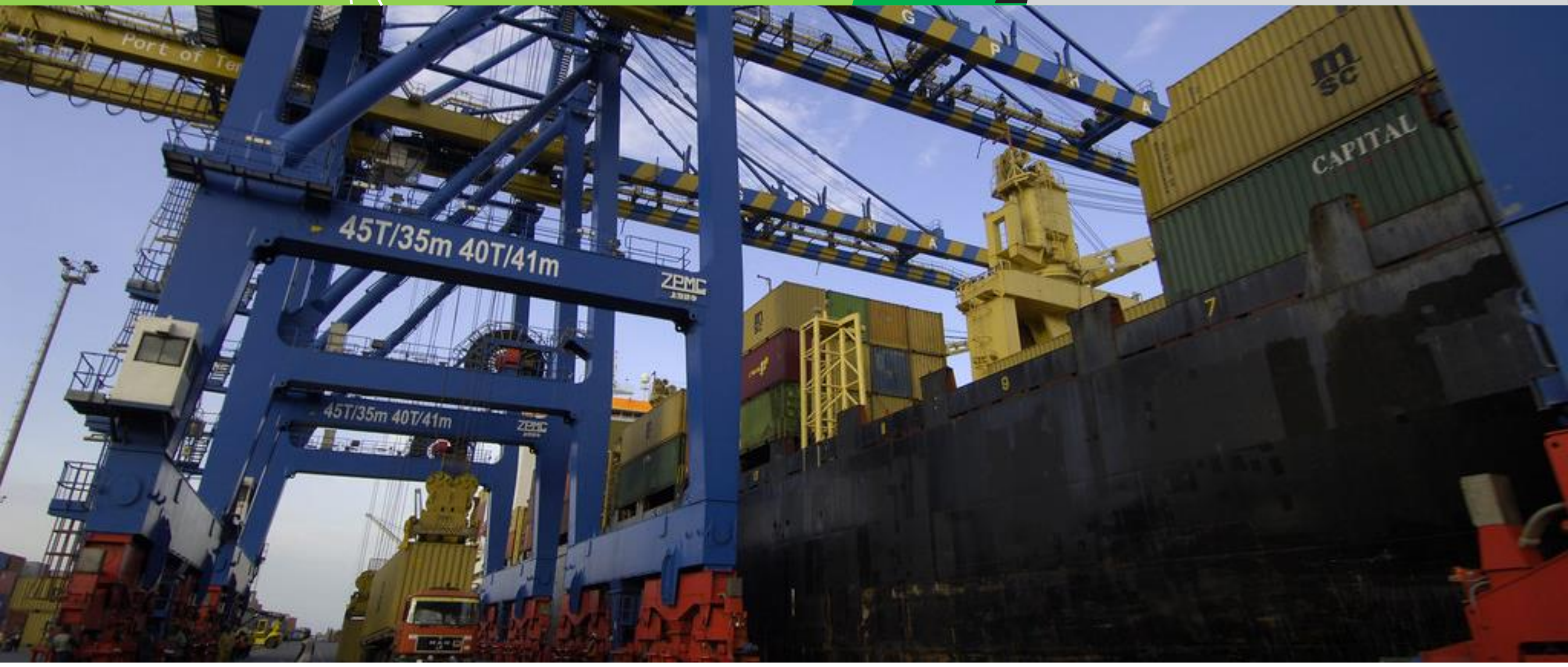

Briefing Paper

Comprehensive review of the East Africa Community (EAC) Common External Tariff: what are the salient issues?

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Summary

The process to comprehensively review the East African Community (EAC) Common External Tariff (CET) presents an opportunity for the region to strengthen its trade and related policies towards enhancing their competitiveness in global trade, while also being mindful of sustainability aspects such as climate change. This briefing paper highlights the salient issues in this regard.

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PROMOTING AGRICULTURE, CLIMATE AND TRADE LINKAGES IN THE EAST AFRICAN COMMUNITY – PHASE 2
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Introduction

The East Africa Community (EAC) is a regional economic community composed of Burundi, Kenya, Rwanda, South Sudan, Tanzania and Uganda, which aspires to foster economic, social and political integration within the member countries.

The EAC was originally founded in 1967 with three member countries of Kenya, Tanzania and Uganda, it was however dissolved in 1977 due to *inter alia* political differences at the time. In 1999 the community was revived by the three original members. Rwanda and Burundi joined in 2007 while South Sudan became a full member in 2016. With headquarters in Arusha Tanzania, decision-making in the EAC is intergovernmental and is carried out by the EAC Council of Ministers.

General objectives for the EAC integration include but are not limited to: Advancing sustainable development for members; Strengthening trade and economic ties of members; Maintaining peace and stability; Improving private and civil society engagement; as well as Good governance, etc.

In the integration process, the EAC set out to implement four pillars which are the formation of a: Customs Union, Common Market, Monetary Union, and ultimately a Political Federation.

To that end, the customs union which was adopted in 2005 established free trade of goods and services as well as a common external Tariff (CET), whereby members were to apply the same tariff on goods imported from all non-member states. The second pillar, the Common Market allows free movement of goods, services, persons, capital, and labor also provides for the right of establishment and the right of residence amongst the member states. Implementation of the Common market commenced in 2010, which was later followed by the adoption of the East African Monetary Union protocol in 2013, with a timeframe of 10 years within which the region would have adopted a single currency for member states. The final pillar of Political Federation aims to ensure *inter alia* common foreign policies, good governance and consolidation of all aforementioned pillars.[1]

Presently, the EAC is undertaking a comprehensive review process of the common external tariff (CET) so as to enhance its effective application. This brief note highlights the salient issues in this regard.

The Customs Union protocol and the Common External Tariff: Implementation and Challenges

The EAC Customs Union became effective in 2005, the Protocol under which it was established provides for a Single Customs territory with a CET aimed at achieving the following objectives:

- Creation of a stable, transparent and predictable tax regime within the EAC so as to enhance local and foreign investments within the region
- Promote production, investment and uniform trade policy regimes, which would also spur development and leverage the regional potential economically
- Simplify the tax structure within the region by creating a uniform tariff regime.

In order to facilitate implementation, internal Rules of Origin (RoO) were put in place to distinguish between goods produced in the region from those produced without. In addition, member countries agreed to provide exemption regimes as well as

[1] https://www.eac.int

sensitive products lists of products that would be outside the application of the CET. This was to take into account country specific situations. Never the less, it was envisaged that over time the exemptions would be reduced so as to make the CET more effective so that the region could better reap from the fruits of integration.

Presently, EAC-CET band structure is as follows: 0% for raw materials and capital goods, 10% for intermediate goods and 25% for final goods. Additionally, there is a sensitive items list with exceptions to the 'three-band rule' for specified commodities whose rates are beyond 25%.[2] The CET covers a total of 5,395 tariff lines at the 8-digit level, this is broken down as follows:[3]

- 0% for raw, capital and social goods, which cover 2,003 tariff lines or about 37.1%
- 10% for intermediate goods, that covers 1,152 tariff lines or 21.4%
- 25% for finished products covering about 2,176 tariff lines or about 40.3%; and
- 35-100% for sensitive products covering 64 tariff lines or about 1.2% of total tariff lines.

So as to redress some of the challenges that have arisen in implementing the set-out objectives, such as unilateral exemptions and CET fluctuations all through the period 2005 to 2015, it was decided to comprehensively review the CET to make it more effective. The main issue is that tariffs on critical items such as steel, cement, agricultural commodities and transportation equipment have been the most unstable'.[4] Moreover, in 2014, members adopted unilateral exemptions on more than a hundred tariff lines on goods such as vehicles, rice, and cement, etc.[5]

Figure 1: CET Instability

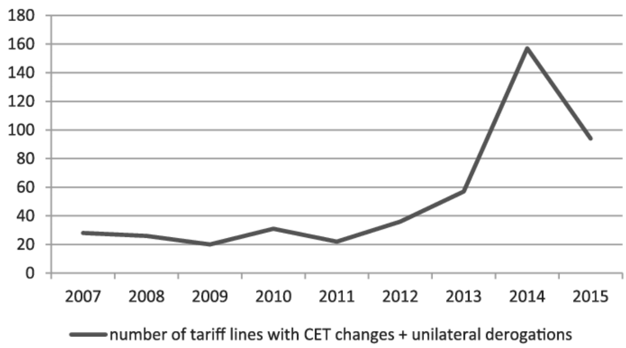

Figure: Data: EAC gazettes [6]

The unpredictability resulting from frequent fluctuations of tariffs hinders planning, investment, and trade growth in the region. Moreover, the current CET has not been contributing to progressive liberalization, thereby affecting the region's global integration and competitiveness. Besides, there are country differences that require specific considerations. For instance, landlocked countries such as Burundi, Rwanda, and Uganda face more transportation costs for both their imports and exports. The current CET has done little to reduce trade costs for the landlocked EAC members. These, among other reasons are the drivers of the ongoing re-negotiations to comprehensively review the CET.

At the time of its adoption, the CET was to cover the period 2005-2015, application was between the original member countries at the time: Kenya, Tanzania, and Uganda. Burundi and Rwanda joined the community in 2007 and implemented the CET from 2009, through a progressive process that had

[2] EAGC Proposed New CET Structure 05 03 2019_SEATINI

[3] EAC Common External Tarrifs – Presentation by Kiiza Kizito – Country Manager-Eastern Africa Grain Council

[4] https://journals.sagepub.com/doi/full/10.1177/2158244017748235#_i1

[5] https://journals.sagepub.com/doi/full/10.1177/2158244017748235#_i1

[6] https://www.researchgate.net/figure/Data-EAC-gazettes-Note-EAC-East-African-Community-CET-Common-External-Tariff_fig1_322620762 [accessed 27 Mar 2019]

been agreed. The institutional structure of EAC permits member states to use exceptions that allow them to protect domestic interests over regional interests. Thus, member countries have been able to apply flexibilities in implementation of the CET through exemptions.[7]

Among the exceptional circumstances that allows member states to derogate on CETs are Duty-Remission Schemes (DRSs) which allow member countries to select companies that will import some input goods for manufacturing as duty-free in order to boost exportation. Ideally, member states are supposed to provide evidence that the region is unable to adequately provide the input good for this exception to be applied, but this is barely respected.

Another challenge has been conflict of interest in the negotiations for the CET For instance, some manufacturing industries may advocate for higher tariffs because they wouldn't otherwise compete with cheaper imported options, while another sector using similar products as an input advocates for them to be cheaply imported so as to minimize their production costs. For example, some industries process intermediate steel and make final products such as iron sheets and would prefer to have steel cheaply imported; however, some other industries are engaged in production of raw iron into steel and would prefer higher external tariffs on intermediate steel imports so as to protect their own industries.

Importantly, the agriculture sector which is the main stay of livelihoods in the region requires a well-planned CET that would be helpful in ensuring optimal leveraging of the sector for development and poverty eradication efforts in the region.

Agricultural products are very sensitive and lower tariffs would greatly affect smallholder farmers who are the majority of the population. However, lowered tariffs on specific country interests would benefit citizens (the consumers) especially in countries faced with weather vagaries affecting agriculture production during certain periods. As a result, countries have often detracted from the CET to address immediate needs. For instance, Tanzania and Uganda have lowered tariffs on wheat during times of dire need. It is, therefore, common practice for countries to detract from the CET and it has become increasingly difficult to oppose national derogations in favor of regional benefits. The challenge is having national interests overlapping with regional interests thereby finding the opportune policy framework that would facilitate implementation of agreed Protocols including the CET becomes a necessity.

Furthermore, an analysis of the imports from the rest of the world into the region during the implementation period of the CET indicates that these have continued to grow, which shows that the present CET rates did not affect third-country imports.

In summary, below are the main challenges that have necessitated a comprehensive review of the CET:

- Drastic increase of imports mostly from Asia (especially China), which have raised concerns from consumers, specifically with regard to quality issues
- Increasing cases of misclassified imports (especially through established firms) that take advantage the current CET provisions, of which some are quite broad
- The need to redress provisions on allowance

7 https://journals.sagepub.com/doi/full/10.1177/2158244017748235#_i1

for countries to classify sensitive products; although the percentage coverage of such allowance in the present CET is quite low (64 tariff lines) in real terms, these are products that are of high economic value and therefore arbitrary rate of tax on them curtails the sectors, which needs to be redressed

- The issue of landlocked EAC member countries has also posed a major challenge in implementation of the CET given that majority (Burundi, Rwanda, South Sudan, and Uganda) are faced with higher costs of their imports, which would need to be considered in setting the rates
- Member countries' provisions of sectors/items on sensitive lists is not always respected, which creates uncertainty on tariff rates within the region
- Absence of comprehensive and cohesive trade and industrial policy in the region has resulted in unilateral decisions that affect implementation of the CET
- Another critical challenge is the issue of EAC Members belonging to other regional arrangements that have different requirements, which then disrupts implementation of the CET
- Institutional and regulatory frameworks within the region presently do not support effective implementation of the CET.

The comprehensive CET review will be an opportunity to redress the above challenges.

Mandate, Process and Objectives of the CET Comprehensive Review

The process of renegotiating changes of the CET was approved by the Council of Ministers, the main executive body of the EAC, as so required by the Agreement. Article 12:3 of the Protocol on the establishment of the East African Customs union provides that 'The Council may review the common external tariff structure and approve measures designed to remedy any adverse effects which any of the Partner States may experience by reason of the implementation of this part of the Protocol or, in exceptional circumstances, to safeguard Community interests.'[8] It is in this respect that EAC Members decided to comprehensively review the CET so as to remedy challenges presently experienced in its implementation.

The Structure for the negotiations entails a multi-institutional committee of the EAC (domestic) - High level task force -> Committee of senior government officials -> council of ministers -> summit of heads of state.

Prior to negotiations, member states submit their country positions on the matter in order to guide the process under negotiations, the criterion used is based on consensus as per the below provision:

> *"The Council of Ministers directed the EAC Secretariat to undertake a comprehensive review of the CET. The Secretariat was also instructed to form National Task Forces and National Steering Committees for the purpose of undertaking the review.*
>
> *Member countries formed a multi sectoral*

[8]https://www.ifrc.org/Global/Publications/IDRL/regional/Protocol%20on%20the%20Establishment%20of%20the%20East%20African%20Customs%20Union.pdf

National Force to undertake the review of the CET. The taskforce is composed of government Ministries, Departments and Agencies, Private sector (Apex bodies), civil society and academia among others. The taskforce held four consultative meetings to formulate principles to inform negotiation of the CET.

The National steering Committee (NSC) on the EAC CET Comprehensive Review is composed of Permanent Secretaries and Heads of Institutions and Apex civil society organizations. The NSCs are mandated to hold meetings periodically during the consultative process. The purpose of these meetings is to consider the principle of the CET review proposed by the Taskforce. The meetings provide guidance on the proposed structure and principles to guide the negotiations"[9]

The specific objectives of the Comprehensive CET review are the following:[10]

- "Review and align the tariff structure and rates to respond to the current economic environment in EAC
- Review EAC CET to respond to the global changes of trade on some products
- Propose measures for elimination of stays of application of CET that destabilize the harmonized CET
- Review the sensitive list and its rates taking into consideration of supply capacity within the region
- Propose safeguard measures that Partner States can apply in case of shortfalls or upsurge on identified products in a Partner State
- Proposes measures to address any inconsistence identifies in the CET."

Conclusion and Recommendations

The process to comprehensively review the EAC CET presents an opportunity for the region to strengthen its trade and related policies towards enhancing their competitiveness in the multilateral trading system, while also being mindful of sustainability aspects, given the climate change impacts in the region. Hence, the review process should take the following issues into account:

1. Country positions on the revised CET rates should be informed by an all-inclusive consultative process, in which stakeholders from the private sector, civil society and all relevant policy institutions are brought on board such that their aspirations are taken into account.
2. Given the significant role of women and the youth (presently the majority of population in the region) in economic activities in the region, proposed revision of the CET should take into account the gender and youth labour implications. Agreed outcomes should enhance opportunities for gender integration in the economic activities of the region as well as opportunities for the youth.
3. The reviewed CET should also be geared towards facilitating and promoting industrialisation, well in line with the EAC Industrialisation Policy and the African continental drive in this regard.
4. The CET should also be a means of promoting

[9] EAGC Proposed New CET Structure 05 03 2019_SEATINI

[10] EAGC Proposed New CET Structure 05 03 2019_SEATINI

creation of regional value chains, especially in the agriculture sector (which is predominant in the region) by promoting value addition and also connecting to international value chains. This will be critical for development efforts in the region.

5. The attainment of the Sustainable Development Goals (SDGs) should also be taken into account in revising the CET such that agreed rates are supportive of the other initiatives such as trade, climate change and social-economic aspects geared to improving livelihoods as per the SDGs.

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