When the Prime Minister of India and Sri Lanka met in New Delhi in June 2002, they took cognizance of the significant expansion of trade made possible by the ISLFTA. However, they also noted that there was much scope for expanding the areas of coverage of economic cooperation. Accordingly a Joint Study Group was set up to explore ways and means of deepening and widening economic cooperation through a Comprehensive Economic Partnership Agreement.

The CEPA is intended to address issues such as reduction of item under the negative lists, harmonization of customs procedures, standardization and trade facilitation. Additional features of this agreement would be the inclusion of trade in services, investment and economic cooperation. Such coverage would reinforce the bilateral framework established through the ISLFTA. Convergence of the two economies through globalization and the liberalization initiatives of the WTO will eventually erode the preferential margin between the two national that is now provided by the ISLFTA. Therefore, it is vital to negotiate the CEPA promptly to enable both India and Sri Lanka to exploit the comparative advantages provided by expanded bilateral trade during this window of opportunity.

CEPA, that encompasses trade in goods and services investment promotion and economic cooperation would serve to strengthen trade liberalization considerably. However, since, the ISLFTA already exists the CEPA could be implemented quickly to deepen economic cooperation between the two countries.
Goals for the India-Sri Lanka CEPA

A time table should be established by India and Sri Lanka, so that negotiation for the CEPA could take place in a timely and efficient manner. A suitable time frame for India and Sri Lanka to achieve the CEPA would be roughly 4 to 6 months. This time-frame is important as the ongoing multilateral trade linearization result in the rapid erosion for preferential duty margins under ISLFTA.

The CEPA will cover a broad range of linearization action and binding commitments regarding goods, services, and investment, as well as economic cooperation complementary to trade liberalization. In other words, the CEPA will widen and deepen the ISLFTA and supersede it in the near future. In this light the JSG is of the view that CEPA should be notified under Article XXIV of GATT and Article V of GATS in the WTO. Such notification will indicate that both countries are committed to further liberalization and are committed to meet the standards stipulated by the WTO.

Best Practices for the CEPA

A primary objective of the CEPA should be to maximize trade creation and minimize trade diversion. Among others the following best practices adopted by other nations and regional blocs may prove to be beneficial for Indo-Sri Lanka.

Non-Tariffs barriers

Trading across international borders entail many administrative costs and barriers that result from uncoordinated customs procedures, divergences in standards and requirements. This is presently one of the main anomalies that negate the scope of the India-Sri Lanka FTA. This situation could be effectively tackled through standardization and harmonization and mutual recognition at an overcome these costs and overcome these impediments through regional standardization and the introduction of Paperless trade. The possibilities of adopting such a stance at a bilateral level by India and Sri Lanka are examined in detail in the following chapters.

Private sector cooperation

The facilitation of private sector cooperation between the two nations is also an important element that should be considered in the CEPA. Though this, the
concerned Ministries provide the opportunities for stakeholders from the private sector to actively participate in negotiation through periodic consultative sessions. Furthermore, the private sector is also given opportunity to partake in the review of bilateral agreements and interact with counterparts through conferences and seminars. Sri Lanka and India will greatly benefit from the adoption of such a practice. These measures could be strengthened via the Business Chambers of the two countries and possible nodal points.

**Conclusion**

Moving forward with a comprehensive Economic Partnership Agreement (CEPA) to include border areas of services and investment in addition to trade in goods represents a logical approach to achieving deeper economic integration. The economic gains from CEPA will result in both countries enhancing their productivity and competitiveness in order to face the challenges of multilateral liberalization under the WTO.

It is also importantly to establish clear objective, a realistic time frame and an effective monitoring trade creation through the CEPA will greatly strengthen and deepen economic interrogation between India and Sri Lanka.

To sum up, this JSG report attempts to provide a blueprint for the deepening of economic integration, which has been initiated through the ISLFTA. The following chapters highlight the avenue for such a paradigm shift in line with the shared vision of the leadership of the two countries and the international obligations of India and Sri Lanka. In this context, the objective of the JSG is to:

* Develop and enhanced policy framework for trade in goods building upon the experience of the ISLFTA.
* Develop a policy framework for strengthening bilateral linkages, encompassing trade in goods and services, investment and other areas of economic corporation, to maximize the benefits of geographical proximity and close relation between India and Sri Lanka.
* Suggest parameters and modalities for the incorporation of trade in services in the ambit of CEPA.
* Identify measures to facilitate greater investment flows by addressing possible regulatory and operational constraints.
* Identify opportunities for enhancing economic cooperation in areas of mutual interest.

Summary of recommendations

The JSG recommends that the two countries:

* Enter into a comprehensive Economic partnership Agreement.
* Build upon the ISLFTA by deepening and widening the coverage and binding of trade in goods.
* Notify the resultant agreement of the WTO under GATT art XXIV.
* Enter into board negotiation covering all service sectors and modes of supply under the GATS framework.
* Notify the resultant agreement under GATS Art. V.
* Facilitate greater investment flows by addressing identified regulatory and operational constrains.
* Implement measures to enhance economic cooperation to complement trade and investment liberalization.
* Complete negotiation on the CEPA within 4-6 months.
* Establish institutional mechanisms to monitor the progress of the CEPA so that the objectives are realized.
* Facilitate interaction between, and participation of the private sector of the two countries in the negotiation of the CEPA and its implementation.

TRADE IN GOODS

2.1 Regional groupings are increasingly becoming an integral part of the present global trading system. More than 50 per cent of world trade is transacted within various forms of regional trade agreements (RTAs). RTAs have come to be accepted as second best options to free trade of multilateralism, and the India Sri Lanka free Trade Agreement (ISLFTA) should be viewed in this context.

Tariffs

2.2 Tariffs have the least trade distorting effects compared to other forms of restrictions on trade. Very high tariffs maintained for long periods would however render the domestic industry uncompetitive and inefficient. While multilateral tariff reduction is the first best solution,
bilateral/regional preferential of free trade arrangements have their own merit and could also contribute to the strengthening of the multilateral trading system. The free trade Agreement between India and Sri Lanka signed in December 1998 has demonstrated capabilities for trade creation leading to mutual benefit for both India and Sri Lanka. Trade creation can occur within a bilateral free trade area if production efficiency improves when a member of the free trade area imports more from the lower cost partner leading to a fall in less efficient domestic production. Consumption efficiency improves when consumers in one member of such an area can import at a price that is lower than the price of the domestic product. At the same time in the case of most developing countries, import tariffs constitute an important part of government revenue. They also serve the purpose of providing the necessary protection to the domestic industry.

2.3 Under the Uruguay Round (UR) India committed to bind tariffs for 62 per cent of its industrial products. In the pre-UR era, the binding was applicable for only 3 per cent of tariff lines. The UR commitments were expected to reduce India’s trade-weighted average tariff from 71.4 per cent to 32.4 per cent. Further, at the UR, India committed to bind rates on mineral and basic products at 25 per cent manufactures at 40 per cent, while consumer goods were not bound. Since the UR, modifications to the UR commitments have been effected owing to:

a) The information Technology Agreement (262 item);

b) Re-negotiation with principal trading partners under Article XXVII of GATT in respect of 15 items; and

c) Binding rates in the textile sector.

2.4 Under the Uruguay Round (UR), Sri Lanka committed to bind 97 per cent of agricultural products at 50 percent. In the pre-UR era, the binding of agricultural products was applicable for only 3 per cent of tariff lines at 6 digit level. Sri Lanka’s binding coverage of non-agricultural products as of today including the tariff commitments undertaken under UR is 28.3 per cent. In the pre-UR era, the binding of non-agricultural products was applicable only for 52 per cent of tariff lines at 6 digit level. In products as of today, including the tariff
commitments undertaken under UR is 28.3 per cent. In the pre-UR era, the binding of non-agricultural products, was applicable only for 5 per cent of tariff lines at 6 digit level. Pursuant to the Doha mandate to liberalize tariffs of non-agricultural products, Sri Lanka is in the process of consulting the relevant stakeholders to decide on further commitments, which would eventually increase the sector’s binding coverage.

2.5 The UR commitments in the agriculture area were expected to reduce Sri Lanka’s trade-weight average tariff from 66 per cent to 50 percent. Further, at the UR, Sri Lanka committed to bind rates of certain non-agricultural products, such as fish and fisheries products, leather and leather products, wood products, products of iron and steel and products of other base metals at 50 per cent.

2.6 Since the UR, Sri Lanka has made modifications to its UR commitments in the non-agricultural area, particularly in the textile sector, with a view to increasing the binding coverage. WTO bound rates of both countries with their present applied MFN rates are given in Annex 1 and Annex 2.

2.7 The JG took note of the substantial differences in the present levels of tariff bindings of India and Sri Lanka.

Assessment of trade under ISLFTA

2.8 A bilateral Free Trade Agreement was signed between India and Sri Lanka in December 1998 which became operational from March 2000. India has undertaken the following commitments.

a) Fixed duty concession of 50 per cent is granted on 233 tariff lines covered under tea.

b) Fixed duty concession of 25 per cent is granted on 528 items in HS chapters 51 to 56, 58 to 60 and 63.

c) Duty concession of 100 per cent is granted on 1,351 items upon entry into force of the Agreement.

d) Margin of preference of 50 per cent on the remaining items of 2,799 shall be increased to 100 per cent in two stages within three years of coming into force of the Agreement.
Tariff concessions are not granted for a total number of 429 items listed in the Negative list of India.

2.9 Sri Lanka has been undertaken the following commitments:

a) Duty concession of 100 per cent is granted on 319 items upon entry into force of the Agreement.

b) Margin of preference of 50 per cent on 839 items shall be deepened to 70 per cent, 90 per cent and 100 per cent respectively, at the end of the first, second and third years of entry into Force of the Agreement.

(Note: All items in this list are enjoying zero duty concession with effect from March 5, 2003)

c) For the remaining items of 2,724, the tariff shall be bought down by not less that 25 per cent before the expiry of three years and 70 per cent before the expiry of the sixth year and 100 per cent before the expiry of eight years, from the date of entry into force of the Agreement.

Tariff concessions are not granted for a total number of 1180 items, listed in Negative list of Sri Lanka.

2.10 The bilateral trade has touched US$ 1 billion in 2002. Exports from India to Sri Lanka grew from US$ 602 million in 2001 to US$ 835 million in 2002 (by 39 per cent) making India the largest supplier to the Sri Lanka market. Meanwhile, the value of exports from Sri Lanka grew from US$ 72 million to US$ 171 million during the same period recording a 138 per cent growth. Sri Lanka’s import/export ratio improved from 8.6:1 to 4.9:1 while the import coverage ratio, which measures the extent to which export proceeds can cover disbursements on imports, improved from 11.6 per cent in 2001 to 20.23 per cent in 2002.

2.11 India, which stood as the 22nd buyer of Sri Lankan goods during the 1990s emerged as the fifth largest buyer in 2002 accounting for 3.6 per cent of the value of total exports (US$171 million). The growth momentum of Sri Lanka’s preferential exports was propelled by copper related products which have collectively accounted for 63 per cent of the value of total preferential exports in 2002 as against 10 per cent in
the year 2001. Other preferential product also recorded a remarkable
growth rate of 192 per cent in the year 2002 as compared with the
growth rate 43 per cent in 2001. These include inter alia, waste paper,
dual inline memory modules (DIMMs), and furniture, pneumatic tyros,
multi wall paper sacks, marble slabs, and ceramic ware, jewellery and
ice cream machines.

2.12 The portion of Sri Lanka’s exports absorbed by India 2002 (US$)
million) is equivalent to 9.6 per cent of the value of Sri Lanka’s exports
to the USA (US$1762), Sri Lanka’s leading export market during the
same period.

2.13 In the assessment of the FTA the key issues which have arisen are:

a) Sri Lanka’s utilization of quotas for tea (15 million kg.) and
readymade garments (8 million pieces) remained below 5 per cent
quotas available. Limitation of entry points granted to preferential
exports of these items has inhibited their trade. Accordingly the number
of entry ports has recently been increased from 4 to 7.
b) During the period March 2002 to end 2002 Sri Lanka effected 4600
shipments to India under the FTA of which less than 50 consignments
were subject to unanticipated delays. Doubts expressed by Indian
Customs regarding the authenticity of certificates of Origin contributed
to delays in the case of certain shipments. Direct contact between
authorities of both countries and placement of FTA conversant nodal
officials at the entry points have been identified as measures to resolve
these problems.
c) The surge in Sri Lanka copper exports created a critical
circumstances situation which was resolved through discussion under
the consultative mechanisms in place under the ISLFTA.
d) Rigidities of the present Rules of Origin criteria, particularly the
requirement of 4 digit HS conversion were seen as inhibiting potential
exports from Sri Lanka despite high value addition involved.
e) Discriminatory sales taxes levied by certain Indian states adversely
affect some preferential exports from Sri Lanka. Tariff escalations
through special additional duties too similarly effect. The
competitiveness of such preferential exports.

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f) A factor which causes the trade balance to be heavily in favor of India is the asymmetry of economies between the two countries in terms of export base, excess capacity, and raw material supply base, degree of industrialization, lower freight charges and availability of skilled technical manpower. A realistic appreciation of Sri Lanka's capacities in the relevant sectors may render possible further deepening of certain preferences granted to them by India, e.g. enhancing the present concessionary rate for textile exports (25 per cent of the general rate).

g) Around one third of India's total exports to Sri Lanka are items that come under Sri Lanka exceed Ind. Rs. 100 million. Some of these items are onions, vegetables, masoor dhal, fruits, wheat, rice, sugar, portland cement, paper products, motor vehicles and auto parts. Sri Lanka's exports on India's negative lists approximately 6 per cent of its total exports at present. Items of significance are rubber, plastics, printed labels, and polyester and nylon yarn. Removal of further items of exports interest to either country from the others negative list is under consideration through the consultative mechanism provided under the FTA.

2.14 The JSG observed that possibilities of further enhancement of benefits for both countries utilizing hitherto untapped market opportunities available under the ISLFTA, show vast potential. However, several impediments which deter utilization of preferential access that is currently granted can also be observed. Additional flexibility in granting originating status, the need to phase out negative lists as far as possible as well as the need to ensure "National Treatment" as per WTO commitments, Mutual Recognition Agreement and conformity assessment procedures are areas that need to be addressed. In this regard, the JSG noted that further expansion of quotas granted in tea and readymade garments, which are of key export interest to Sri Lanka, will be favorably considered by India once the present quotas are nearing full utilization.

2.15 With further reduction of basic customs duty as a result of regional arrangements and multilateral liberalization under the WTO, the margins of preference that are currently enjoyed are likely to get gradually eroded rendering all preferences granted under FTAs and PTAs redundant. Therefore, it is of paramount importance to under
take fast track liberalization between the two countries under the framework of a CEPA.

2.16 Further liberalization of the goods trade under the CEPA, keeping in view the asymmetries of both economies, would lead to an overall increase in bilateral trade flows. Both countries would benefit from tariff reductions as this would reduce the cost of business, increase the competitiveness of domestic industries and enhance both countries' effectiveness as investment destinations.

2.17 A central objective in developing the CEPA is to broaden and deepen the existing ISLFTA in order to elevate trade between the two countries to their next level in the economic relationship. Both countries are committed to a CPEA that meets the conditions for trade in goods stipulated under GATT Article XXIV, including coverage of substantially all trade with no sector wholly excluded and with implementation to be completed in a timely manner. This process should progress towards phase out of the existing negative lists under the ISLFTA to their lowest conceivable levels, while ensuring that no new barriers that would impede further expansion of bilateral trade would be introduced. The asymmetries of the economies of India of most of the Indian states.

2.18 The agricultural sector accounts for 23 per cent of India's GDP, which is comparable to 20 per cent of Sri Lanka. But in terms of magnitude, the agricultural Sector GDP of Sri Lanka is 2.5 per cent of the Indian agricultural GDP and consequently is smaller than that of most of the Indian states.

2.19 Most countries, the developed as well as the developing, offer a measure of protection to their agricultural sectors. The WTO Doha Declaration has addressed the need to liberalize multi lateral trade in agriculture, with commitments to substantial improvement in market access, reduction/phase out of export subsidies and substantial reductions in domestic support. It is hopped that, despite the failure of the WTO Cancun talks, progress in this direction will continue to be made. The importance of according Special and Differential Treatment to the Developing Countries within these parameters to accommodate their adjustment needs has also been recognized by the WTO.
2.20 With trade liberalization, most of the quantitative restrictions have been abolished in both countries and formal instruments such as tariffs and other taxes have been kept low to moderate, including those protecting domestic primary and food processing industries. However, since rural labor absorption and food security needs are important factors for both countries at present, there are important exemptions. Restriction in the form of WTO-legal non tariff measures such as State Trading Enterprises (STEs), Tariff Rate Quotas (TRQs) specific tariff values for duty calculation, Sanitary and Python-Sanitary measures (SPS) continued to provide protection to specific sub sectors in both countries. For example, while import policies are restrictive with regard to rice, wheat and coarse grain, dairy products, edible oils and sugar in India at present, rice pulses, onions, potatoes and chilies are subject to restrictive import policies in Sri Lanka.

2.21 It is also significant that world prices in these product groups are highly cyclical. Several of these products have been in the low phase of such cycles in recent years. While noting the sensitivities and complexities involved in the management of policies for the agricultural sectors of both countries, the JSG recommends that long in-grained anti-import tendencies that offer redundant protection to products with low production cost of with low stakeholder interest would need to be rectified in both economies. Empirical investigation may reveal that several such products will not require much adjustment of policies, if competing imports are allowed. The JSG recommends that CEPA negotiations should facilitate further liberalization of agricultural trade and cooperation in the agricultural sector between India and Sri Lanka in the above context.

Rules of Origin

2.22 Rules of Origin (ROO) are criteria to determine the nationality of goods (Where they are made, produced etc.). They are crucial in any bilateral regional performance or free trade arrangement in order to prevent trade deflection (i.e. to ensure that such arrangement are not used to route third country products to the participating countries). The rigor of the preferential ROO would depend on the differential between the MFN and preferential rates of duty and the perceived risk of trade
deflection. In the ISLFTA, the total value of the material, parts, or produce originating from countries other than the contracting Parties or of undetermined originating used should not exceed 65 per cent of the FOB value of the products produced or obtained and the final process of manufacture is performed within the territory of the exporting contracting Party. Further, in respect of a product exported by Contracting Party and which has used Material, Parts or produce from the other Contracting Party shall not be less than 25 per cent of the FOB value of the products under export subject to the condition that the aggregate value addition in the territories of the Contracting Parties is not less that 35 per cent of the FOB value of the product under export. However, as can be seen in section 7 of Annex 4, conversion of HS heading at the 4 digit level, remains the main determinant of preference availability under the ISFTA.

2.23 Most FTA/PTAs have adopted conversion of HS heading at the 4 digit level as denoting sufficient transformation in a manufacturing process of ROO purposes. However across the board application of this rule imposes certain rigidities by which come products with value addition even higher that 40 per cent -50 per cent are denied originating status. MERCOSUR and NAFTA agreement have therefore built-in flexibility to overcome these rigidities and to stimulate the desired trade flows.

2.24 The JSG recommends that the CEPA negotiations should consider the following measures while maintaining the effectiveness of ROO criteria to ensure that only products with genuine value addition are granted originating status.

a) Abolition of the requirement of conversion at 4 digit level where Domestic Value Addition (DVA) exceeds 40 per cent of the FOB of the finished products.

b) Dispense with the HS conversion requirement where the CIF value of non-domestic input is less that 7 per cent of FOB value of finished product.

c) In order to encourage Indian and Sri Lankan exporters to source inputs from each other, imported inputs from either party should be
considered as domestic inputs of the finished products and the requirement of HS conversation may be dispensed with.

d) Depending on the level of value addition and the importance of products concerned in stimulating two way trade, the CEPA, should consider adoption of 6 digit HS conversion for identified groups of tariffs lines.

**Customs Procedures**

**Risk Management**

2.25 **India:** Since 1998, a Fast Track Clearance Scheme has been in place in India under which certain categories of importers have been allowed to pay duty and clear the imported goods on the basis of self-assessment of duty. Under the Indian EDI (Electronic Data Interchange) system, there is a 'green channel' facility under which identified importers, on the basis of past performance, are allowed waiver of examination of the imported cargo. For certain categories of cargo (gold, silver, books defense cargo, imports by universities and other public funded research institutions), the assessment is done through the "systems Appraisal". In these cases, the import document, after submission, is assessed for duty and the duty amount is calculated in the EDI system without intervention by customs officers. Large scale simplifications have been carried out in the export procedures as well. The JSG took note of the statement by the Indian Finance Minister, in his budget speech on 28 February 2003, of his intention to bring India's customs procedures on par with best international practices. He proposed to introduce a self-assessment scheme this year.

"Physical inspection of imported goods will be done by using risk assessment and management techniques on a computer-based system and not on the orders of customs examining staff. Further, the existing system of concurrent audit of import documents will be replace by post-clearance audit, as prevalent in developed countries.

2.26 **Sri Lanka:** In 1992 Sri Lanka customs introduced an Automated Cargo Clearance System with the assistance of UNCTAD. This project was
called ACCESS (Automated Customs Cargo Entry system for Sri Lanka) and the software used for this project was called ASYCUDA.

With use of ASYCUDA version 2.6, Sri Lanka Customs began automating the process of Customs Declaration (Cusdecs) in the areas of import, Export and Bonding. Certain modules like Manifest, Selectivity were not introduced due to practical problems and the project was fully completed in 1995.

The present version of ASYCUDA called ASYCUDA++ which runs on a UNIX platform supported by an oracle Data Base was introduce in 1998. In addition, The Sri Lanka customs has devolved two other independent software programmes to monitor the Container Clearance and Bank Guarantees in Bonding Procedures.

Under the ASYCUDA system there are number of selected DTI (Direct Trader Input) operators working with Sri Lanka Customs who lodge their Cusdecs from their offices to the Custom Data Base. The Customs work on expansion of this facility under a selectivity criteria process.

Further, Sri Lanka Customs with the cooperation of the Ministry of commerce and Consumer Affairs is presently working on EDI (Electronic Data Interchange) project. The basic steps such as procedures, message testing and office location were completed and it is expected to introduce this system (EDI) in the near future.

With the implementation of the EDI, it is envisaged to introduce an Automated Selective Module in ASYCUDA. Under this, the processing of Custom Declaration and the Clearance of Cargo will be subjected to the following four channels.

Green - No document check and no cargo check
Blue - No document check, no cargo check but subject to poet audit.
Yellow - Subject to document check but no cargo check.
Red - Subject to document check and cargo check.
With the Automated Selecting, it is expected to minimize the delays in the clearance process and enhance the uniformity in selection of consignments for examination.

2.27 **The JSG recommends;**

a) The adoption of a risk management system by India for customs clearance procedures. The JSG noted that India has already moved significantly in this direction. However, the time frame for its introduction, specific elements of risk management, and exceptions for goods coverage would need to be negotiated. Priority for implementation of trade facilitation measures including risk management should focus on ports that account for substantial bilateral trade, including Nhava Sheva, Chennai, Mumbai and Colombo. The list of imports could be augmented as modernization takes place.

b) Both customs Administrations should, as far as possible, administer their customs procedures based on risk management principles to focus on compliance efforts on high-risk goods and to clear low-risk goods from both India and Sri Lanka expeditiously through designated "Green Channels" with minimal physical examinations.

c) Both Customs Administrations could also exchange information on best practices relating to risk management techniques for customs clearance.

2.28 Both countries recognize that unless the integrity of the CEPA is maintained and all of its provisions, notably the Rules of Origin, are scrupulously observed, few economic benefits will accrue. While the Certificate of Origin procedures, established under the ISLFTA are included in Annex 4, additional verification procedures will be put in place.

2.29 The JSG noted India’s concerns regarding under-valuation of preferential trade. More direct means of communication between official and department of both countries should be established to address these concerns. In recognition of the Critical importance of this issue, the Sri Lanka Government has indicated that it would have no
objection to Indian Custom and/or Trade officials being based in Colombo to ensure effective implementation of the CEPA. The JSG recommends that a working Group consisting of appropriate officials of both Governments to be set up to examine and approve a verification procedure that would refine the issuance of Origin as well as validate their content. Once such a Join Working Group (JWG) set up a verification procedure that is acceptable to both sides, the validity of such certificates of origin should not be questioned. The Working Group should draw on models that are operational elsewhere and proven successful, keeping in mind that the objective of free flows of trade should not be hampered in any way.

2.30 There will still be need to have mechanisms for settlement of disputes that may arise due to the implementation of the CEPA. Currently the respective officials in both countries undertake this process periodically. The JSG recommends that the existing mechanisms for addressing issues and disputes that arise could be further strengthened. It also recommends that greater involvement of the private sector would facilitate resolution of many of the problems that arise.

**Trade Facilitation**

**Paperless Trade Documentation**

2.31 "Paperless Trading" refers to the electronic filling and transfer of trade-related information and document in relation to business application between each country and its trading community.

2.32 The Indian Customs authorities have an advanced automation programme for customs clearance of imported goods. The basic objective of this programme is to allow trade, transport and other regulatory agencies to interchange live electronic message pertaining to customs clearance by an EDI. The customs EDI system is geared to support various popular electronic communications methods (such as internet) and various technical standards related to communication and messaging so that EDI trading partners have choice and flexibility while not compromising on security. The status of implementation is as follows:
a) Electronic exchange of information and data taking place between customs and agencies like the Directorate General of Foreign Trade (DGFT) and the Directorate General of Commercial Intelligence and statistics (DGCI&S)
b) At Customs location in Delhi, airlines are filling the export general manifest (EGM), and the Apparel Export Promotion Council (AEPC) is transmitting quota details on a trial basis through the EC/EDI Gateway.
c) The message Exchange between Customs, banks and custodians (like port and airports) is taking place through Message Exchange Servers between the respective LANs.
d) The facility for the importer, exporter and Custom House Agents to use the E-Commerce Gateway for filling their document is due to be launched in April 2003.
e) Customs stations in Nhava Sheva, Chennai and Mumbai port are automated. In fact, as all major port, airports and inland container deports (ICDs) have been placed on automation, the scope for paperless trading system can be increased to more ports in a phased manner.

2.33 The JSG recognized that the adoption of "paperless trading" would enhance the efficiency of trade information flow and documentation exchange. However such electronic transfer should not compromise the confidentiality or integrity of information.

2.34 The JSG recommends that trade regulatory bodies of the respective parties work towards accepting electronic versions of current paper-based trade administrative documents submitted by private entities as supporting documents. The JSG further recommended that:
a) The private sector of both countries is encouraged to adopt paperless trading;
b) Priority be given for implementation of paperless trading in ports that account for substantial bilateral trade, including Nhava Sheva, Chennai land Mumbai.
Sri Lanka is also moving towards electronic paperless transactions.

Transparency
2.35 To improve transparency of customs laws and procedures, it would be desirable to have a provision for publication of all laws, regulation, judicial decisions and administrative rulings of general application related to requirements for imported or exported goods in both paper as well as in electronic medium.

2.36 In India, such laws and regulation that are duly published as gazette notification or public notice are commercially available as Customs Law Manual, and are also largely available on the Central Board of Excise Customs (CBEC) website (www.cbec.gov.in). This website contains all relevant Acts, tariff, rules, regulation, forms, notification and circulars relating to customs, central excise and service tax. Decisions of the Supreme Court of Indian and some of the High courts are available on their respective web-sites. In addition, a number of private publications and websites provide access to judicial decisions. It would be difficult for the Government of India to place all judicial decisions on the website or in paper format as the number of legal disputes in customs/excise related matters is very large and judgments are available from a wide number of judicial authorities like a large number of commissioners (Appeal) and different Benches of Central Excise and Gold Appellate Tribunal (CGAT), in addition to the courts. It would also be a one rouse burden because it would require very frequent updating/publication given the large number of judicial pronouncements that are made frequently.

2.37 In line with the general international obligations of the two countries relating to transparency under GATT Article X, the JSG recommends that India and Sri Lanka make available all laws, regulations, judicial decisions and administrative rulings of general application relating to requirement for imported or exported goods, wherever possible.

Mutual Recognition

2.38 In India, four organizations, the Bureau of Indian Standards (BIS), the Directorate General of Foreign Trade (DGFT), The Ministry of Health and Family Welfare (MoHFW) and the Ministry of Agriculture (MoA) are responsible for laying down import control requirements, while the Export Inspection Council (EIC) is responsible for export inspection and
certification of commodities. Details are in Annexes 3 and 4 of this chapter.

2.39 The Sri Lanka Standards Institution (SLSI) is responsible for the implementation of product standards in respect of most imports and some compulsory export inspection schemes. The Ministry of Health, Nutrition and Welfare and the Ministry of Agriculture and livestock cover health and hygienic standards related to foodstuffs, animal and plant material imports, respectively. Details are in Annexes 3 of this chapter.

2.40 To facilitate exports from India and simplify inspection procedures, a MOU was concluded between SLSI and EIC of India. Sri Lanka desires similar MOUs between the relevant bodies/organizations in India in respect of Sri Lankan exports to India. The JSG recommend that SLSI and any other relevant bodies in Sri Lanka should be enabled to conclude MOUs with the relevant bodies/organizations.

2.41 The JSG recommends that such MOUs should form the basis for commencing negotiations on MRAs at the earliest with a view to setting.

Investment Incentives: - To encourage foreign investment flows into these thrust areas, the BOI provides several investment incentives to new enterprises and existing enterprises going for expansion. The incentives offered to investors operating under the BOI Law are available to both foreign and local investors, provided the investment is undertaken through a company incorporated in Sri Lanka. The quantum of incentives offered depends upon the value of investment, the number of employment opportunities, and the level of export orientation. The package of incentives includes tax holidays, preferential taxation, and duty-free import of capital goods and raw materials (Annex 5).

Regulations have been framed under the BOI Act to grant specific incentives to new and existing enterprises satisfying specific eligibility criteria. These incentives generally involve a combination of exemptions relating to income tax, customs duty and foreign exchange
controls, which are conferred on an eligible company that enters into an agreement with the BOI.

The types of investments that qualify for incentives under Section 17 of the BOI Act are indicated below. More details are given in Annex 5.

* Manufacture of non-traditional goods for exports
* Export oriented services
* Manufacture of industrial tools and/or machinery
* Small scale infrastructure projects
* Information Technology (IT) and/or IT enabled services
* IT related training institutes
* Regional Operating Head Quarters
* Any large scale industrial, agricultural, construction or service or any other business activity
* Research and development
* Agriculture and/or agro processing other than processing of black tea
* Existing enterprises undertaking an expansion
* Rehabilitation of non-performing or under-performing enterprises
* Export Trading Houses
* Large-scale (new/existing) projects
* Large-scale infrastructure projects

Protection is provided to mutual investments through the following institutional mechanisms:

a. Constitutional Guarantee.
c. Sri Lanka is a founder member of the Multilateral Investment Guarantee Agency (MIGA) of the World Bank, which provides guarantees against non-commercial risks, such as those arising out of political instability and insecurity.
d. Avoidance of Double Taxation and Prevention of Fiscal Evasion Agreement.
The JSG recommends that reviews be carried out by the two governments to enhance the scope and effectiveness of the Bilateral Investment Promotion and Protection Agreement and the Avoidance of Double Taxation and Prevention of Fiscal Evasion Agreement.

Potential Areas for Investment Promotion in Sri Lanka

4.20 Despite fairly open direct investment policies maintained by both countries, bilateral investment flows have not grown to desirable levels that could produce mutual benefits, partly due to the lack of awareness of investment opportunities and existing administrative and regulatory controls mentioned above. Therefore, the following illustrative but not exhaustive list highlights some areas in Sri Lanka where Indian investors could exploit their comparative advantages.

- Port development
- ICT projects
- Rail transportation
- Petroleum exploration
- Power generation and transmission
- Film Industry
- Infrastructure in the tourism
- R & D (biotechnology and agricultural research)
- Land bridge connecting India and Sri Lanka
- Health and education

Furthermore, there exists a vast range of joint investment opportunities in both countries. These investments will enhance economic activities in both countries and improve competitiveness of their exports.

Outward Investment Policy Measures in Sri Lanka

Outward investments by Sri Lanka residents are currently governed by the Exchange Control Act under which all applications for investment abroad should be approved by the Minister of Finance following a recommendation from the Controller of Exchange. The Minister has delegated his power to approve outward investments to the Controller of Exchange and the Secretary to the Treasury up to certain limits, subject to guidelines approved by the Minister. However,
establishments approved by the BOI are not required to obtain permission under the Exchange Control Act to make investments abroad, to the extent that the investment is in respect of the business activities agreed upon with the BOI.

In granting permission to make investments abroad, the Controller of Exchange follows some guidelines approved by the Minister. The guidelines are mainly aimed at permitting foreign investments by resident establishments which have earned substantial amounts of foreign exchange in their existing business in Sri Lanka to enable them to extend their business for further promotion of export of goods and services from Sri Lanka. They would also ensure that the ventures have a reasonable chance of success.

New Foreign Exchange Management Act: The proposed Foreign Exchange Management Act (FEMA), which will replace the Exchange Control Act, relaxes some of the existing restrictions on outward foreign direct investment and has provisions to further liberalize investment abroad. The new Act makes provisions for the orderly management and regulation of foreign exchange with the objective of further liberalizing dealings in foreign exchange. Section 7 of the Act authorizes the Minister of Finance, in consultation with the Monetary Board of the Central Bank, to issue orders effecting further liberalization of the capital account without amending the FEMA.