



F. NO: 109/PET RESIN/CCP/2012
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POLICY NOTE

RATIONALIZATION OF DUTY STRUCTURE ON PET RESIN

1. The Competition Commission of Pakistan (the “Commission”) took notice of concerns raised on classification of Poly Ethylene Terephthalate (PET) Resins under Pakistan customs Tariff Code (PCT Code) and customs duty levied on them under Notifications SRO 507(I)/2007 and SRO 678(I)/2010 which, prima facie, give undue duty protection to the sole local manufacturer/supplier of PET Resins. The sole manufacturer of PET Resin is a vertically integrated unit having also presence in downstream market and this policy note examines whether resultant custom duty structure on PET Resin and its down stream products places the competitors of the sole manufacturer of PET Resin at a competitive disadvantage.
2. PET Resin is made by a combination of Pure Terephthalic Acid and Mono Ethylene Glycol in a Continuous Polymerization unit, which is subject to custom duty of 3% and 0% respectively. PET is the basic component used to manufacture different PET Resins such as PET Bottle Grade, PET Film Grade, and PET Yarn Grade etc. PET Bottle Grade is further processed to manufacture PET Bottles, which are largely used in Pakistan for the purposes of carbonated soft drinks and bottled water. PET Film Grade is processed to manufacture packing, covering, and wrapping material.
3. Currently, classification of PET Resins under PCT Code and rates of customs duty levied under the Customs Notifications SRO 507(I)/2007 and SRO 678 (I)/2010 SRO is as follows:

Product	PCT Code	Custom Duty
PET Yarn Grade	3907.601	3%
PET Bottle Grade	3907.602	9%
PET Film Grade (falling under the heading “Others”)	3907.609	20%

4. The nomenclature/classification of PET Resins or processed PET ¹ in Harmonized System Code (HS Code) which is followed all over the world is normally based on; (i) functions of the goods, (ii) polymer that they are made from, and (iii) method of manufacturing, which justifies the rate of duty imposed thereon. It has been observed that generally PET Resins are categorized and duty is levied based on their properties, particularly, Intrinsic Viscosity (“Viscosity”). For example, in India PET Resins having Viscosity not less than 0.64dl/g and not greater than 0.72 dl/g are categorized under one heading and charged with same rate of customs duty.² In United States PET Resins having Viscosity of .070 dl/g or more but not more than 0.88 dl/g are chargeable with same rate of duty³. Similar pattern has been observed in six other jurisdictions namely Sri Lanka, Canada, Vietnam, China, European Union and Bangladesh.
5. Another interesting feature that helps to understand the international trend in classification of PET Resins is the manufacturing process. PET Resins (PET Bottle Grade and Film Grade and yarn grade) are manufactured by using the same type of raw material; Terephthalic Acid, Ethylene Glycol and catalyst, all used in almost same stoichiometric proportion in same process of esterification and polycondensation carried out on the same plant.⁴ All three aforementioned PET resin fall under low viscosity resins category.⁵ Standard PET Yarn Grade and PET Film Grade have Viscosity of 0.64 dl/g whereas standard PET Bottle Grade has a little higher Viscosity of 0.80dl/g⁶ for the reason that it has to go through Solid State Polycondensation Process (SSP) to upgrade amorphous bottle grade chips to high quality bottle grade resin.
6. However, in case of PCT Code applicable in Pakistan it has been observed that PET Resins have been categorized based on product and not based on a rationale in sync with international trend. Therefore, Film Grade and Yarn Grade even though have identical Viscosity and manufactured through almost similar process using substantially similar raw material have been imposed with different customs duty at the rate of 20% and 3% respectively.
7. While reviewing the tariff structure of PET Resins over the period of time in Pakistan, it is observed that in the year of 2007 duty structure on PET Bottle Grade was reduced from 10% to 7.5 % vide SRO 643(I)/2007. Later on, customs duty on PET Bottle Grade was increased to 9% vide SRO 687(I)/2010. Fluctuation in customs duty rates has nowhere been rationalized in the relevant notifications.

¹ http://trade.ec.europa.eu/doclib/docs/2012/july/tradoc_149803.pdf

² <http://www.cbec.gov.in/customs/cst2012-13/chap-39.pdf>

³ <http://www.usitc.gov/publications/docs/tata/hts/bychapter/1210c39.pdf>

⁴ http://doc.isiri.org.ir/c/document_library/get_file?p_l_id=18472&folderId=21150&name=DLFE-21391.pdf

⁵ <http://www.epa.gov/ttnchie1/ap42/ch06/final/c06s06-2.pdf>

⁶ *Supra* 4

8. Hence, in view of foregoing, the classification PET Resins under PCT Code and diverse rates of customs duty levied on them through notifications seem to extend protection to a particular undertaking by imposing discriminatory rates on similar products, which has resulted into a situation of applying dissimilar conditions to equivalent transactions.
9. Another important aspect observed with respect to duty structure of PET Resins in Pakistan is adoption of a different tariff escalation modality. Generally, countries provide duty protection by imposing a high tariff on finished goods to restrict their inflow and protect local manufacturers. Whereas comparatively low rate of duty is levied on raw/intermediary material to encourage local production. For example, in case of our own Tobacco industry, imported raw material is charged with 5% customs duty whereas finished product is charged with 35% customs duty as given in the PCT Code. Similar incidents are found in marble industry, cosmetic industry and many others.
10. However, in case of PET Resins, customs duty levied on 'PET Film Grade' (raw material) is 20% and 'BOPET Film', which is a finished product it is 20%. Similarly, customs duty on 'PET Bottle Grade' (raw material) is 9%, whereas 'PET Preform' which is an intermediary product it is 20% and on finished product which is 'PET Bottle' the customs duty is 10%. Such duty structure encourages the imports of finished products rather than giving the incentive to manufacturers to produce locally. In case where the sole manufacturer of PET Resins who also has presence in the downstream market, such duty structure gives it an apparent advantage over its competitors by increasing cost of raw material used for production by other players/ competitors, in the downstream market. The increase in cost of production of competitors may be either through the ability of sole manufacturer to charge higher local prices for the raw material or incidence of higher tariff on raw/intermediary material that makes it difficult for competitors to compete in the downstream markets (BOPET Film and PET Bottle markets).
11. It needs to be appreciated that generally the rationale behind tariff protection is to ensure that local nasant/developing industries can prepare themselves to compete against their foreign counterparts. However, this incentive may compel the beneficiaries to seek more protection or longer periods of protection than warranted and therefore may inhibit the ability of undertakings to become competitive. In addition, such protectionism has the tendency of being abused by rent seeking interests and may result in low quality and inflated price. Therefore, it requires that parameters of duty protection are fair and goal oriented to achieve the desired outcome.

12. Duty protection invariably has an impact on the price and sets a higher trend in price. Higher price increases the cost of production of customers. In cases where customers are dependent on sole supplier/manufacturer to procure raw material to meet the local demand and also compete with it in the downstream market, the duty protection restricts competition and is likely to distort a level playing field in the downstream market. Such restricted competition may set a tendency for supplier cum competitor to engage in exclusionary behavior and once the competitors are driven out of market, end consumers may fall prey to rent seeking behavior of a monopolist.
13. If setting up a PET Resin plant necessitated duty protection to recoup the investment and allowing time to become competitive. Such protection cannot be absolute and has to be time bound, particularly, when undertaking enjoying the duty protection also enters the downstream market and becomes a competitor of its customers. Apart from presence in both upstream and downstream market, long duration of protection, positive growth and financial strength are the strong indicators to establish the fact that continuation of duty protection is unwarranted.
14. It is also pertinent to mention that adoption of a tariff policy which aims at providing a level playing field to all manufacturers to further grow and develop BOPET Film and PET Bottle industry would save foreign exchange by substituting imports of finished goods with local production. At the same time, it would encourage to export the surplus production, which would help in reducing the trade deficit of Pakistan.
15. The Commission is entrusted under the Competition Act, 2010 (the “Act”) with the duty to ensure free competition in all spheres of commercial and economic activity to enhance economic efficiency. In pursuance of Section 28 and 29 of the Act, which require the Commission to promote competition through advocacy and in view of foregoing we hereby advise and recommend that tariff structure of PET Resins, in particularly PET Bottle Grade, PET Film Grade and PET Yarn Grade needs to be rationalized and slashed down to a uniform rate to eliminate discrimination in terms of classification and rates of duty in order to create a level playing field for all the competitors in PET Bottle and BOPET Film markets.

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