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India- UAE CEPA: How duty free import of Gold, silver and diamonds will cause large revenue loss, and disrupt the domestic business

Global Trade Research Initiative

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Highlights

India-UAE CEPA allows unlimited imports of gold, silver, platinum, and diamonds from the UAE into India with zero tariffs in the coming years. This will lead to significant annual revenue losses (over Rs 63,000 crore), move import business from banks to a few private traders, and replace top suppliers with Dubai-based firms. It will also disrupt the domestic diamond and jewellery industry, with major imports coming from GIFT City, which has transparency issues. An urgent review is needed.

1. Most Gems and Jewellery imports of India will soon be through UAE

CEPA provisions allow unlimited imports of gold, silver, platinum, and diamonds from the UAE into India with reduced or zero tariffs in the coming years.

Currently, gold can be imported from Dubai at 5% duty, but this will drop to zero in three years if the alloy contains 2% platinum.

Silver imports from the UAE have surged due to an 8% duty under CEPA, compared to a 15% MFN tariff, resulting in a significant tariff arbitrage. India will reduce the duty on silver to zero over ten years, causing a revenue loss due to the shift of imports from other sources to the UAE.

2. Impact on Domestic Manufacturers

CEPA tariff concessions are hurting India's jewellery industry, with gold jewellery imports from the UAE increasing due to lower tariffs.

Zero tariffs on cut and polished diamonds under CEPA threaten India's domestic diamond industry, which currently benefits from zero duty on rough diamonds and a

5% duty on cut and polished diamonds. The removal of tariffs could lead to a decline in the domestic industry and a shift in processing activities to countries like China.

3. Revenue Loss

The zero-tariff policy under CEPA is projected to cause an annual revenue loss of Rs 63,375 crore due to duty-free imports of gold and silver, based on FY 2024 import levels.

4. Shifting business from Banks to Private Traders

Business is shifting from established importers like banks authorized by RBI and DGFT to many unscrupulous private traders.

Reputable global suppliers of bullion are being replaced by Dubai-based suppliers, many of which are owned by linked Indian importers.

5. Rules of Origin

Many imports do not meet Rules of Origin conditions, hence do not qualify for concessions, raising the strong possibility of money laundering. The value addition process for silver imports is questionable, with concerns about money laundering. This is the reason for the shift of silver imports from Indian ports to GIFT City exchange to benefit from concessional tariffs.

6. Issues with GIFT City Exchange:
Lack of transparency and potential manipulation in trades at GIFT City. There is a need for a CAG audit to investigate pre-arranged deals and invoice manipulation. Its license should be suspended until the audit is completed.

Report

1. Unlimited imports of duty-free gold, silver, platinum, and diamonds from UAE under CEPA

India-UAE CEPA contains provisions that allow unlimited imports of duty-free gold, silver, platinum, and diamonds into India over the next few years.

I. Gold- CEPA allows unlimited import of gold from Dubai at 5% duty now and at zero tariff in next 3 years if the imported metal contains just 2% platinum and 98% gold. This unwelcome bonanza comes from the Customs product classification rules, any alloy containing 2% or more by weight of platinum is treated as an alloy of platinum. This means that firms can import an alloy consisting of 98% gold and 2% platinum, and it will be classified as a platinum alloy. Under the India-UAE CEPA, India agreed to eliminate tariffs on platinum to zero over five years. Current tariff on platinum is 5% which means 10% arbitrage. In next three years unlimited Gold can be imported at zero tariff as platinum alloy containing 98% gold.

Platinum of value US$ 1.2 billion was imported from Dubai in FY 2023. Market sources say that imports through certain customs ports have begun again, signalling that soon, unlimited quantities of gold could legally enter India through this method. Such imports cannot be banned through Customs notification and Government must review CEPA provisions urgently as courts may strike down any retrospective amendments.

The above provision is in addition to CEPA allowing 200 tonnes of Gold at 1% concessional duty may from UAE.

II. Silver-Currently, India imports silver from the UAE at an 8% duty, while the MFN tariff is 15%, creating a 7% arbitrage. Under the India-UAE CEPA, India will reduce the duty on silver to zero over the next ten years. This tariff difference has led to a 5853% increase in silver imports from the UAE, rising from US$ 29.2 million in FY 2023 to US$ 1.74 billion in FY 2024, causing a revenue loss of Rs 1010 crore for India in FY 2024. In FY 2024, India imported US$ 5.4 billion worth of silver globally. As the tariff drops to zero over the next eight years, most silver imports are expected to come from the UAE, leading to a projected revenue loss of Rs 6700 crore. This surge in imports is driven solely by the tariff arbitrage.

III. Jewellery- The tariff concessions under CEPA will significantly hurt India's jewellery industry. Under the India-UAE CEPA, India agreed to reduce tariffs on gold jewellery by 1% each year, from 20% to 15% over five years, with a tariff rate quota (TRQ) or import limit of 2.5 tonnes. The current tariff is 17% with a TRQ of 2.3 tonnes. However, in the 2023 budget, the government increased tariffs from 20% to 25%, creating a higher tariff arbitrage under CEPA. This means there is now an 8% tariff difference, which will increase to 10% in the next two years.

This high tariff arbitrage has led to a massive increase in India’s jewellery imports from the UAE, which have risen by 290%, from US$ 347 million in FY 2023 to US$ 1.35 billion in FY 2024. The lower tariffs make UAE imports much cheaper than domestic products, causing domestic manufacturers to struggle to compete.

IV. Diamonds-The zero tariff on cut and polished diamonds under CEPA will significantly harm the Indian diamond industry. Currently, India imports rough diamonds, which are then cut and polished domestically before being exported. To promote this local industry, India imposes zero duty on rough diamonds and a 5% duty on cut and polished diamonds. However, under the India-UAE CEPA, cut and polished diamonds can be imported at zero duty if they meet a 6% value addition in Dubai.

India’s global exports of cut and polished diamonds are valued at US$ 15.9 billion. The removal of the 5% tariff will put immense pressure on the margins of the domestic diamond industry. Indian manufacturers will struggle to compete with zero-duty cut and polished diamonds imported from Dubai, potentially forcing many local businesses to shut down or relocate. Additionally, importers and traders will dominate the market, further disadvantaging domestic producers. China, meanwhile, is keenly welcoming Indian expertise in this area, which could lead to a shift in the diamond processing industry away from India.

2. Annual Revenue Loss

Annual revenue loss due to zero tariff import of Gold and silver from Dubai via CEPA could exceed Rs 63,375 crore in few years. India imported US$ 45.5 billion worth of gold and US$ 5.4 billion worth of silver in FY 2024. Under CEPA, unlimited gold (98% gold, 2% platinum) and silver can currently be imported with tariffs of 5% and 8% respectively. Starting in 2026, gold can be imported tariff-free, and silver from 2030. This zero-tariff policy will likely shift all of India's global imports through the UAE under CEPA. The government then is expected to lose Rs 63,375 crore in revenue from duty-free gold and silver imports, based on FY 2024 import levels.

Concessional tariff imports of gold, silver, and gold jewellery have already started from Dubai under CEPA. In FY 2024, 119.35 tonnes of gold bars were imported from Dubai under the concessional duty of 1%, valued at US $7.62 billion. Silver imports from the UAE increased dramatically by 5853%, from US$ 29.2 million in FY 2023 to US$ 1.74 billion in FY 2024. The import of gold jewellery from the UAE increased by 290%, from US$ 347 million in FY 2023 to US$ 1.35 billion in FY 2024.

3. Rules of Origin and Money Laundering Concerns in India's Precious Metal Imports

Most imports do not meet Rules of Origin conditions and hence do not qualify for concessions. To supply silver granules to India, Dubai firms import silver bars from Russia and other countries, convert them into granules, and claim a 3.5% value addition in this process. Less than 0.5% value addition accrues in this process.

However, whole operation is problematic because Silver bars command a higher price than silver granules of the same purity in the market. Silver bars are preferred for investment due to their standardized shapes and sizes, making them easier to trade.

Granules are less common and may be trickier to find buyers for. Granules are not brought by investors but only jewellers. Normal business of making silver granules from silver bars will not succeed as the finished product will sell at lower value in market than the raw material. Thus essentially, from market angle, the silver gains from UAE via GIFT city have negative value addition but they are showing positive value addition. Clearly money laundering angle need to be probed. The production process is taking place just to take benefit of concessional tariffs.

Yes bank, and RBL bank had earlier tried importing silver at concessional duty from Dubai using CEPA provisions. They faced problems as Customs officials at Chennai and Bengaluru ports have asked the banks to provide the proof of compliance with CEPA conditions, which importers have struggled to provide. This has led to shifting of all imports from Dubai from Indian ports to the GIFT City exchange.

Since December 2023, all silver imports from Dubai at concessional tariffs have been cleared through the customs at GIFT City exchange. The key concern is how imports cleared through GIFT City meet the rules of origin requirements specified in the India-UAE FTA when importers from other port fail to meet these.

4. Transparency and Trust: Investigating the GIFT City Exchange

Gold and Silver imports in India were previously regulated, with only agencies nominated by DGFT & RBI such as banks allowed to import. Private firms could not directly import bullion; they must procure it through nominated agencies. However in Dec 2023, the Department of Revenue allowed GIFT City to enable private traders to import bullion vide notification 66/2023/Customs, dated December 22, 2023.

The notification states that India UAE TRQ holders notified by IFSCA through the India International Bullion Exchange (IIBX) can receive physical delivery of their imports through IFSCA-registered vaults in SEZs. This decision has led to a significant increase in registrations at GIFT City for imports under CEPA.

There is a significant difference in how banks and GIFT City exchange register precious metal suppliers. Banks, under RBI oversight, check reputations and follow strict AML guidelines, registering international banks like HSBC, JP Morgan, ICBC, Standard Chartered, and Citi Bank.

IIBX has low credibility among global top bullion suppliers like JP-Morgan, Citi Bank, ICBC, Standard Chartered Bank. They have still not joined IIBX and prefer to do business with nominated agencies like banks. Only UAE based suppliers are registered with IIBX, many of these owned by Indian linked to importers in India.

The trades conducted at the GIFT City exchange lack transparency, raising serious concerns about pre-arranged deals and invoice manipulation. The GIFT City exchange urgently needs a CAG audit, and its license should be suspended until the audit is completed. A thorough audit by the CAG could uncover that many trades are pre-arranged between buyers and sellers.

Here's how the scheme works: a buyer in India places an order for a specific quantity of bullion on the IIBX platform in the morning. Despite waiting, the order remains unfilled. Then, a seller based in Dubai offers the requested quantity, and suddenly, a new buyer quickly purchases the entire quantity within seconds, even if they were last in the queue. Further investigation reveals that these buyers and sellers are from the same families. Each trade is pre-planned, with invoice and quote manipulation occurring over the phone before the trades are executed. This lack of transparency undermines the integrity of the trading process and necessitates immediate action.

For example, Buyer A wants to buy silver/gold at Rs. 100 and places a request on the platform. Buyer B wants to buy silver/gold at Rs. 101 and also places a request on the platform. Buyer C does not quote but waits for instructions from Supplier X in Dubai. Supplier X informs Buyer C over the phone that Buyer A and Buyer B have quoted Rs. 100 and Rs. 101, respectively. Following the instructions, Buyer C then quotes Rs. 102. At the same time, Supplier X offers goods at Rs. 102, which Buyer C immediately purchases. The trade is executed within seconds without complications because Buyer C from India and Supplier X from Dubai are related parties.

The GIFT City exchange has a few hundred registered members, but at board and general meetings, 4-5 private bullion dealers interfere in decision-making. This can be verified through a thorough investigation and by checking the entry register at the exchange entrance.

5. Issues Needing Immediate Investigation

- The provision allowing gold (98% gold, 2% platinum) to be imported as a platinum alloy at zero tariffs in three years due to CEPA's classification rules.

- The urgent need to review CEPA provisions to prevent the exploitation of tariff concessions for gold imported as platinum alloy, as courts may challenge any retrospective amendments.

- Investigate compliance with Rules of Origin conditions for silver imports, especially the dubious value addition claims by Dubai firms.

- The shift of all silver imports from Indian ports to the GIFT City exchange to take advantage of concessional tariffs needs scrutiny, especially regarding how they meet Rules of Origin requirements.

- Lack of transparency and potential manipulation in trades conducted at the GIFT City exchange, requiring a CAG audit and possible suspension of the exchange’s license.

- The practice of pre-arranged deals and invoice manipulation at the GIFT City exchange between related parties from India and Dubai.

- Low credibility of IIBX among top global bullion suppliers and the registration of only UAE-based suppliers, many linked to Indian importers.

- Possible money laundering activities related to the import of silver granules with negative value addition.

By addressing these issues, authorities can ensure the integrity of import practices, safeguard domestic industries, and prevent significant revenue losses. . .

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GTRI aims to create high-quality and jargon-free outputs for governments and industry on issues related to trade, technology and investment from the perspective of development and poverty reduction.

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Feedback

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