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INTERNATIONAL TRADE

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An e-newsletter from Lakshmikumaran & Sridharan, New Delhi, India

March, 2013 / Issue 22

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March
2013

Article

FDI in multi-brand retail – Consistency with international trade law

By **Bhargav Mansatta**

After much furore over opening up of the retail sector to foreign investment, Government of India (GOI) announced its decision to allow FDI upto 51% in multi-brand retail trading under the government route, subject to the terms and conditions as stipulated in Press Note No. 5 (2012 Series) dated September 20, 2012. GOI also allows 100% FDI in single-brand product retail trading by only one non-resident entity, whether owner of the brand or otherwise, under the government route subject to the terms and conditions as stipulated in Press Note 4 (2012 Series) dated September 20, 2012.[1]

The terms and conditions provided under the press notes may trigger inconsistency of the policy with the international trade law. One of the conditions reads as under [2]

(1) FDI in multi brand retail trading, in all products, will be permitted, subject to the following conditions:[3]

(i) .....

(ii) .....

(iii) ....

(iv) At least 30% of the value of procurement of manufactured/processed products purchased shall be sourced from Indian 'small industries' which have a total investment in plant & machinery not exceeding US $ 100 million. This valuation refers to the value at the time of installation, without providing for depreciation. Further, if at any point in time, this valuation is exceeded, the industry shall not qualify as a 'small industry' for this purpose. This procurement requirement would have to be met, in the first instance as an average of five years' total value of the manufactured/ processed products purchased, beginning 1st April of the year during which the first tranche of FDI is received. Thereafter, it would have to be met on an annual basis.

The aforesaid term can be categorised as 'local content requirement'. It is mandatory for the investor to source at least 30% of 'manufactured/processed' products from Indian 'small industries'.

The policy of FDI in retail will have to be in conformity with the obligations under GATT 1994 & Trade Related Investment Measure (TRIMs).

At the outset it needs to be noted that GATT 1994 which regulate trade in goods is applicable to requirements imposed by governments in an investment context in so far as such requirements involve trade-distorting measures.[4] Article III of GATT 1994 provides that imports be treated no less favourably than the same or similar domestically-produced goods once they have passed customs.[5]

1 See A.P. (DIR Series) Circular No. 32, RBI/2012-13/217, September 21, 2012, available at http://www.rbi.org.in/Scripts/BS_ApCircularsDisplay.aspx

2 Circular 1 of 2012-Consolidated FDI Policy, dated 10.04.2012,para 6.2.16.5, available at http://femaindia.in/dynamicimages/344_1_659634716409116591250.pdf

3 Similar condition is provided in case of single-brand product retail trading wherein FDI beyond 51% will be permitted only when 30% of the sourcing for goods is done from India. The characterization of such clause for the purpose of international trade law is likely to be no different from the condition under multi-brand retail.

4 See generally, GATT Panel Report,*Canada-Administration of the Foreign Investment Review Act,* BISD 30S/140, 1984, 25 July 1983 (hereinafter *Canada-FIRA*)

5 See Article III:1 and Article III:4 of GATT 1994.

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The aforesaid condition directly contravenes the principle of national treatment under Article III of GATT 1994. Mandatory requirement to source the products manufactured locally results in less favourable treatment to the imported goods.

TRIMs Agreement desires to promote investment while ensuring free competition. TRIMs do not provide for regulation of foreign investment *as such* but only intends to regulate trade related aspects of foreign investment.[6] Accordingly, Article 1 of the TRIMs Agreement provides that the 'Agreement applies to investment measures related to Trade in Goods (TRIMs) Only'. The law permitting FDI in multi-brand retail will undoubtedly qualify as TRIMs. Insertion of local content requirement will further ensure that the law is directly covered within the scope of TRIMs.

The Panel in *Indonesia — Autos*[7] held that local content requirements were necessarily trade-related:

"[I]f these measures are local content requirements, they would necessarily be 'trade–related' because such requirements, by definition, always favour the use of domestic products over imported products, and therefore affect trade.

An examination of whether these measures are covered by Item (1) of the Illustrative List of TRIMs annexed to the TRIMs Agreement, which refers amongst other situations to measures with local content requirements, will not only indicate whether they are trade-related but also whether they are inconsistent with Article III:4 and thus in violation of Article 2.1 of the TRIMs Agreement."

The aforesaid observation is categorical with regard to the characterization and position of the 'local content requirement' under both GATT 1994 and TRIMs Agreement. The law which is covered within the description of Annex to the TRIMs Agreement will necessarily be considered as inconsistent with Article III:4 of GATT 1994 and Article 2.1 of the TRIMs Agreement. A 'local content requirement' is specifically covered within the scope of Item (1) of the Illustrative list in the Annex to the TRIMs Agreement. As required under Item 1 of the illustrative list

i. requirement is in fact mandatory or enforceable under domestic law or under administrative rulings or when compliance with it is necessary to secure an advantage.

ii. the purchase or use by an enterprise of products of domestic origin or from any domestic source, whether specified in terms of particular products, in terms of volume or value of products, or in terms of a proportion of volume or value of its local production.

Local content requirement clearly satisfies the aforesaid criteria and is therefore inconsistent with Article 2.1 of the TRIMs Agreement and Article III:4 of GATT 1994.

Further, the policy on FDI in multi-brand retail discriminates domestic and foreign investors or domestic and foreign investments *per se* by its 'enabling policy clause'.[8] The clause provides as below:[9]

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6 Preamble, TRIMS Agreement

7 Panel Report, *Indonesia-Certain Measures affecting the Auto-mobile Industry,* WT/DS64, paras. 14.82–14.83

8 Enabling policy clause is not provided in single-brand retail.

9 *Supra* note 2

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(viii) The above policy is an enabling policy only and the State Governments/Union Territories would be free to take their own decisions in regard to implementation of the policy. Therefore, retail sales outlets may be set up in those States/Union Territories which have agreed, or agree in future, to allow FDI in MBRT under this policy…

India has signed eighty two bilateral investment treaties (BITs).[10] It incorporates national treatment obligation and is common in all the BITs. It provides as below:[11]

"Each Contracting Party shall accord to investments of investors of the other Contracting Party, including their operation, management, maintenance, use, enjoyment or disposal by such investors, treatment which shall not be less favourable than that accorded either to investments of its own investors or to investments of investors of any third State ."

Pursuant to the aforementioned provision, India is under an obligation to accord no less favourable treatment to foreign investments than what it accords to its own investors. The enabling policy contravenes the national treatment provision under the BIT. In all likelihood, not all states will permit implementation of the policy. Consequently, unlike domestic investors, foreign investor from a BIT country will not be allowed to set up shops in certain Indian states. This clearly provides less favourable treatment to the foreign investments than what is accorded to domestic investments. Existence of federal structure is not a permissible defence against the obligation under international agreement especially obligations arising out of international trade agreements.

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[10] List of Countries with which India has signed BITs, available at http://finmin.nic.in/bipa/bipa_index.asp

[11] Illustratively, See Article 4, BIT between India and United Kingdom. Atleast, three of the top five retailer companies of the world are based in UK, Germany and France. India has signed BIT with all the three countries.

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Trade Remedy News

Anti-dumping actions by India

Product	Country	Notification No.	Date of Notification	Remarks
Carbon Black used in rubber applications	Australia, China, Russia, Thailand	15/41/2010-DGAD	28-2-2013	ADD continuation recommended in mid-term review
Flat Base Steel Wheels	China	15/22/2011-DGAD	20-2-2013	ADD recommended to be increased in sunset review
Flexible Slabstock Polyol	USA, Japan	1/2013-Cus. (ADD)	4-2-2013	ADD extended for one year i.e. till Feb. 4, 2014 pursuant to initiation of a sunset review.
Nylon Tyre Cord Fabric	Belarus	15/28/2011-DGAD	20-2-2013	ADD mid-term review initiated
Phenol	EU, South Africa and Singapore	15/16/2011-DGAD	6-2-2013	Mid term review –ADD withdrawal recommended for imports from EU and Singapore while same to be continued against South Africa
Soda Ash	Russia and Turkey	14/3/2011-DGAD	9-2-2013	Definitive ADD recommended

Safeguard action by India

Product	Country	Notification No.	Date of Notification	Remarks
Hot rolled flat products of stainless steel of series 300	China	24 / 2013-Cus. (N.T.)	26-2-2013	Extension of time period till 25th May 2013 for completion of investigation and issuance of final findings

Trade remedy actions against India

Product	Country	Notification No.	Date of Notification	Remarks
Fatty alcohols and their blends	EU	2013/C 58/08	28-2-2013	ADD investigation partially re-opened
Frozen warm water shrimp	USA	News Release 13-018	7-2-2013	US ITC has made an affirmative preliminary determination of material injury.
Hot Rolled Steel Products	USA	News Release 13-016	4-2-2013	US ITC to conduct full five year sunset review for countervailing and anti-dumping duties

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WTO News

Solar panel products - US files dispute against India

The USA has requested for consultations with India on the domestic content requirements under the Jawaharlal Nehru National Solar Mission (NSM) for solar cells and solar modules. The US claims that India requires solar power developers to buy and use domestic solar cells and solar modules in order to benefit from participating in the Jawaharlal Nehru NSM programme and to enter into contracts under the NSM programme or with the National Power Company and resultantly receive certain benefits and advantages, including subsidies through guaranteed, long-term tariffs for electricity. As per document circulated on 11-2-2013 by the US, India's measures are inconsistent with:

- Article III:4 of the GATT 1994 because the measures appear to provide less favourable treatment to imported solar cells and solar modules than that accorded to like product originating in India;
- Article 2.1 of the TRIMs Agreement because the measures appear to be trade-related investment measures inconsistent with Article III of the GATT 1994;
- Articles 3.1(b) and 3.2 of the SCM Agreement because the measures appear to provide a subsidy contingent upon the use of domestic goods; and
- Articles 5(c), 6.3(a), and 6.3(c) of the SCM Agreement because the measures appear to cause serious prejudice to the interests of the United States through displacement or impedance of imports of U.S. solar cells and solar modules into India and through lost sales of U.S. solar cells and solar modules in India.

China's AD duties on EU X-ray scanners - Panel report issued

The Dispute Settlement Body of the WTO has issued its panel report in the dispute concerning imposition of anti-dumping duties by China on imports of certain security inspection equipment (X-ray scanners) from the European Union. The European Union had claimed that the anti-dumping duties imposed by China, and the underlying investigation conducted by the Chinese authorities, were inconsistent with various procedural and substantive provisions of the Anti-Dumping Agreement. The DSB Panel has found that China acted inconsistently with its obligations under Articles 3.1, 3.2, 3.4, 3.5, 6.5.1, 6.9 and 12.2.2 of the AD Agreement.

News Nuggets

India less aggressive on AD front

The Indian Economic Survey 2012-13, released before Budget 2013 last month, notes that India is less aggressive in using anti-dumping as a trade tool, as compared to Brazil, Argentina and Canada which head the list. During 2012-13, India initiated ten cases involving China, the European Union, Korea RP, Malaysia, Mexico, Taiwan, Thailand, Turkey, Saudi Arabia, and the USA.The report also emphasises on regional trade agreements and technology intensive exports to spur growth in view of the stalled WTO negotiations and slow down in world trade. It also states that while

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USA and China continue to be among top three trading partners, region wise, export to Asia, West Asia and Africa are on the rise.

Indus Waters Kishenganga Arbitration – Partial award in favour of India, rendered

The Court of Arbitration constituted in the Indus Waters Kishenganga Arbitration case rendered a partial award on February 18, 2013 on the dispute between Pakistan and India under the Indus Waters Treaty. The main points of contention were the legality of the construction and operation of an Indian hydro-electric project located in Jammu and Kashmir and the permissibility under the treaty of the depletion of the reservoirs of certain Indian hydro-electric plants below "Dead Storage Level."

Pakistan contended that as per the treaty India had to 'let flow' the waters without permitting any interference. Hence, diverting the water to a tributary generating power which is transported to other places was breach of the treaty. Pakistan sought an ambulatory reading of the provisions whereby the 1960 treaty and its modifications would prohibit India from using new techniques like drawdown flushing to control sedimentation or making other uses which were explicitly provided. It also urged that India had failed to carry out 'best endeavours' and not taken into account harm to the neighbouring state.

India argued that the treaty sought to control the water and use and not the electricity produced by the water. In its award the Court observed that an ambulatory reading would allow Pakistan to control rather than use the waters. No responsible project proponent, financing creditor or government agency would incur the expense or make the effort to construct a plant the viability of which would be subject to the unilateral will and action of another party.

In its partial award, the Court of Arbitration decided that India could divert water from the Kishenganga/Neelum river for power generation as envisaged in the treaty. However, India would have to maintain a minimum flow of water in the Kishenganga/Neelum River, at a rate to be determined by the Court in the final award.

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