

TAX FLASH NEWS

5 November 2019



India-USA Trade Dispute on Export Subsidies

In a significant setback to exports from India, World Trade Organisation (WTO) dispute settlement panel has held that India’s export promotion schemes prescribed under the Foreign Trade Policy, violate WTO rules.

This is a significant update for exporters from India availing benefits under export promotion schemes. Exporters would need to be cognizant of potential changes in duty/tax neutralization schemes for export, arising out of the latest WTO disputes panel decision, which could affect their margins and pricing in the medium to long term.

Background

USA had initiated a dispute in March 2018 with India at the WTO, alleging that India provided export subsidies, prohibited under the Subsidies and Countervailing Measures Agreement (SCM Agreement), under five schemes i.e.

- a. Export Oriented Units,
- b. Electronics Hardware Technology Park and Bio-Technology Park (EHTP/BTP) Schemes;
- c. the Export Promotion Capital Goods (EPCG) Scheme;
- d. the Special Economic Zones (SEZ) Scheme;
- e. the Duty-Free Imports for Exporters Scheme (DFIS); and the Merchandise Exports from India Scheme (MEIS).

The alleged export subsidies in the first four schemes were exemptions and deductions from customs duties and other taxes. In the case of fifth scheme, namely MEIS, the alleged subsidies were government-issued notes (“scrips”) that can be used to pay for certain liabilities vis-à-vis the Government and are freely transferable.

Arguments by USA alleging that schemes provided prohibited export subsidies inconsistent with Articles 3.1(a) and 3.2 of the SCM Agreement, were examined by the panel in detail. Article 3.1(a) mentions, ‘subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I’, as prohibited subsidies. Article 3.2 states that a member shall neither grant nor maintain such subsidies.

India’s argument in response, for special and differential treatment as a developing country under provisions of Article 27 of the SCM Agreement was not accepted. India’s argument that measures under the EOU/EHTP/BTP, EPCG, DFIS and MEIS schemes, fell under the exceptions from disallowed subsidies under a footnote of the SCM Agreement (Footnote 1) read with Article XVI of GATT and certain other provisions of the SCM Agreement, was also not accepted. For the SEZ scheme India did not invoke the argument of Footnote 1, but the other arguments invoked by it were also not found tenable by the panel.

WTO Panel Report: After hearing both sides the WTO Disputes panel gave its report on 31st October 2019.

The status of the alleged export subsidies as per the panel’s report is the following:

Sr. No.	Alleged Subsidies challenged by USA	Conclusions of the Dispute Panel
1.	Exemptions from customs duties on importation under the EOU/EHTP/BTP	Inconsistent with SCM Agreement

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2.	Exemptions from customs duties on importation under the EPCG Scheme	Inconsistent with SCM Agreement
3.	Exemptions from customs duties on importation and exportation, the exemption from IGST on importation, and the deductions from taxable income the SEZ Scheme	Inconsistent with SCM Agreement
4.	Exemptions from customs duties on importation under DFIS under certain conditions (numbered 10, 21, 36, 60(ii), 61 in Tariff Notification 50/2017 of Indian Customs)	Inconsistent with SCM Agreement
5.	Duty credit scrips awarded under MEIS	Inconsistent with SCM Agreement
6.	Exemption from central excise duty on domestically procured goods under the EOU/EHTP/BTP Schemes	Consistent with SCM Agreement
7.	Exemptions from customs duties on importation under DFIS scheme under certain conditions (numbered 28,32,33,101 in Tariff notification 50/2017 of Indian Customs)	Consistent with SCM Agreement

The report of the panel will have to be adopted by the Dispute Settlement Body (DSB) within 60 days of its circulation to its members, unless one of the parties notifies of its intent to appeal.

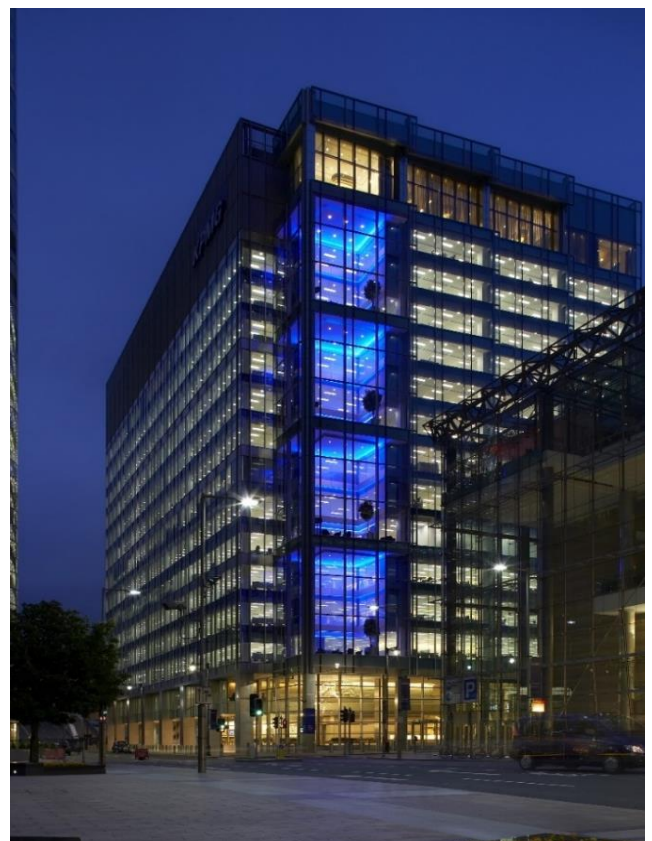
In its conclusions, the panel recommended that India withdraw the prohibited subsidies under DFIS within 90 days from adoption of the report; that it withdraws the prohibited subsidies under the EOU/EHTP/BTP Schemes, EPCG Scheme, and MEIS, within 120 days from adoption of the report; and that it withdraw the prohibited subsidies under the SEZ Scheme within 180 days from adoption of the report.

Our comments

While India is likely to go in appeal against the decision, the government may also look at amending the schemes to reduce potential challenges to export schemes in the future.

Implications for Indian exporters: If the Government of India lodges an appeal against the decision and the appeal too gets decided against India, then the maximum timeframe for withdrawal of/ amendments to, the schemes would lie between 6 to 9 months from now. In such an event, the government will have to amend the Foreign Trade Policy and the enabling Customs notifications. Such amendments would lead to loss of duty/tax neutralizations on inputs for export goods under relevant schemes. It is worthy of note that exporters would have priced their goods factoring in the benefits from duty/tax neutralizations. Cost increases on account of loss of such benefits would significantly reduce their margins. Exporters who have entered into long term supply contracts would need to evaluate the same and negotiate prices accordingly.

It is noteworthy that even before the WTO Panel report was available, the Government of India had, in September'19, begun consultations with exporters through industry chambers on new WTO compliant schemes for duty/tax neutralization. With the panel report available now, the government may re-examine its strategy. It would be worthwhile for exporters to examine options, engage with policy-makers and industry chambers, especially given the short timelines involved.



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