In May 2018, the World Trade Organisation (WTO) set up a panel to investigate the US's allegations against certain export subsidy schemes in India.

The US has over the last eight years made two primary allegations – first, India cannot provide export subsidies because it is no longer a low-income developing country. And second, India is required to phase out its export subsidies in the textiles sector, in which it has achieved export competitiveness in 2010.

Do these allegations have merit and what is likely to be the fate of India's export subsidy regime?

What makes India special?

As a rule, subsidies contingent on export performance have trade-distorting effects and are prohibited under WTO law. At the same time, they play an important role in the economic development programmes of developing countries, especially at the initial stages.

A compromise between these ideas led to the genesis of Article 27 of the Agreement on Subsidies and Countervailing Measures (ASCM), which provides for special and differentiated treatment for developing countries.

Under this regime, India, along with twenty other low-income developing countries, belongs to a special category of "annex VII(b) countries".

These countries are permitted to retain their export subsidies so long as their gross national income ("GNI") per capita at constant 1990 dollars does not exceed $1000 for three consecutive years. Further, if any Indian product achieves export competitiveness, i.e., its exports have a share in world trade of at least 3.25% for two consecutive years, export subsidies for that product must be gradually phased out over an eight-year period.

The year 2017 was a 12-month-period of reckoning for India's export subsidies – not only did it mark India's crossing of the $1000 threshold for the third consecutive year, but it also was the end of India's eight-year phase-out period following its export competitiveness in the textiles sector.

India crossing the $1000 GNI per capita threshold

In 2017, India officially "graduated" from the 'annex VII(b)' category. India now must get rid of its export subsidies – a fact that neither India nor US disagrees on. The only disagreement is about when.

India argues that it is entitled to an eight-year phase-out period starting 2017.

According to Article 27(2)(b) of the ASCM, developing countries, whose GNI per capita was above $1000 on the date of entry into force of the WTO Agreement, were given an eight-year period to phase out their export subsidies. It would seem reasonable to also extend this leeway to developing countries that cross the $1000 threshold after entry into force of the WTO Agreement, such as India.

There is only one problem with this claim – it has no basis in the text of the ASCM. Accordingly, US argues that India was required to end its export subsidies immediately upon its graduation from Annex VII(b). India tried to circumvent this requirement in 2011, when, along with five other developing countries, it proposed a clarification to Article 27, ASCM that the eight-year phase out period would apply equally to Annex VII(b) countries, once they graduate. However, other countries viewed this as a substantive amendment to the ASCM, which they were unwilling to accept.

State practice under the ASCM also seems to undermine India's claim. In 2001, the Committee on Subsidies and Countervailing Measures ("SCM Committee") allowed Annex VII(b) countries to seek ad-hoc extensions beyond the graduation date, if they reserved this right before 31 December 2001.

Four Annex VII(b) countries – Bolivia, Honduras, Kenya and Sri Lanka – made such a reservation. Arguably, these countries would not have considered such reservation necessary, if they believed they already had an eight-year phase out period. However, three out of the four countries making the reservation also supported the 2011 proposal clarifying that the eight-year phase out period applied to graduating Annex VII(b) countries. Thus, it is likely that their reservations were only taken in abundant caution and do not amount to an implicit acceptance that they had no right to an eight-year phase out period otherwise.

Regardless, the absence of a textual basis is an insurmountable obstacle for India's claim, especially given the WTO dispute settlement body's adherence to textualism and its reluctance to add to or diminish the rights of countries through the interpretation of WTO treaties.

In all likelihood, the WTO panel will conclude that India must dismantle its export subsidy regime immediately.

India achieving export competitiveness in the textile sector

In 2010, the WTO secretariat calculated that India's textile exports had crossed the 3.25% share in world trade for two consecutive years. Based on this, US made two claims – first, that India has taken no concrete action to phase out its export subsidies for textiles over an eight-year period till 2017 and second, that India has violated the standstill obligation in this phase-out period, by introducing new export subsidies, in the form of the Merchandise Exports from India Scheme, in 2015.

As to the first claim, India has an innovative response, hinged on an interpretative difficulty.

For calculating export competitiveness, Article 27.6 of the ASCM provides that "a product is defined as a section heading of the Harmonized System Nomenclature ("HSN")" (emphasis added). Under the HSN, sections and headings are distinct levels of classification. It is unclear whether Article 27.6, by referring to "section heading", requires products to be defined at the narrower "heading" level or the broader "section" level of the HSN.

Admittedly, regardless of how "product" is defined in the textiles sector, India has crossed the 3.25% threshold for two years as of 2010. However, the definition of "product" will impact the number of items for which export subsidies will have to be phased out. For instance, in the textiles sector, if there are 60 items under the narrower heading level and 100 items under the broader section level, then India needs to know whether it must phase out subsidies on 60 items or all 100 items. Until this interpretative difficulty about product classification is resolved, India refuses to commence the phasing-out process. Unfortunately, while taking this stance, India did not foresee that in exactly eight years it would graduate from the Annex VII(b) category. Thus, its product classification argument was rendered moot in 2017, since India lost the ability to have any export subsidies whatsoever.

This brings us to the second claim against India. Even if the phase out period started in 2010, India argues that there is no standstill obligation in Article 27.5 or 27.6 of the ASCM that prevents India from introducing new schemes. The only requirement is that these subsidies "be gradually phased out over a period of eight years." This can be contrasted with Article 27.4, ASCM which calls for the subsidies to be phased out in a "progressive manner".

The absence of a similar "progressive" requirement means that India does not violate any obligations by introducing new schemes, if all schemes are eventually done away with at the end of the period. Here, a textualist reading of the treaty, while unfavourable to India's claim for an eight-year phase out period after graduation, could be of some benefit.

Only a matter of time

India's export subsidy regime has provided fertile ground for some creative legal arguments and other not so creative ones. Unfortunately, its termination cannot be postponed any longer.

Perhaps the best indicator of India's lack of confidence in the strength of its own position is that it has already started working to replace its existing subsidy schemes with WTO-compliant incentive schemes.

Therefore, the question is not whether India's export subsidy regime has overstayed its welcome, but rather, what regime should take its place instead.

In arrangement with TheWire.in