Editorial

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Is India ready to face the WTO?

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WITH the removal of quantitative restrictions on import of urea from April 1, 2001 (QRs on import of other fertilisers were removed in 1992), there is an urgent need to take a look at the policy dispensation covering these to see if it is WTO-compatible.

Under Article III.4 of the WTO dealing with National Treatment, a member-government is required to accord the same treatment to an imported product as given to a domestic product in laws, regulations and rules relating to internal sales, offer for sale, purchase, transportation, distribution and so on. Is this requirement met in the context of fertilisers?

The Government directs sale of both the domestic and imported urea to the farmer at the 'same' price. In respect of decontrolled phosphate fertilisers too, the sale price is 'uniform'. While, there is no restriction on sale of 'p' fertilisers, in case of urea, supplies from both the sources are covered by distribution controls under the Essential Commodities Act (ECA). Therefore, the imported fertiliser gets the same treatment as the domestic product.

The Government runs a scheme of subsidy/concession support for urea and the decontrolled 'p' fertilisers. On urea, under the retention price scheme (RPS), it gives unit-specific subsidy to the extent of the excess of reasonable cost of production and distribution over the selling price. On 'p' fertilisers, a 'uniform' concession is given to the producers to cover the difference between the 'normative' cost and the selling price.

The Government is considering replacement of the existing unit-wise RPS for urea by a 'uniform' group-wise concession scheme based on the recommendations of the Expenditure Reforms Commission (ERC). This will result in the number of subsidy/concession rates being restricted to the number of groups (the ERC had proposed '5') as against '32' at present.

The five groups will continue up to March 31, 2006 with reduced rate of concession in Stage II and III. From April 1, 2006 (the beginning of Stage-IV), the Government will only give feedstock differential at 1,900 per tonne to LNG-based plants, including the naphtha-based plants that have switched to LNG. All other plants will not be entitled to any concession support.

In case of complex fertilisers, the Tariff Commission has recommended adoption of two groups for costing of 'N': (i) units based on imported ammonia and those using ammonia made from domestic gas and (ii) units using ammonia made from naphtha and fuel oil/LSHS. In the medium to long-term, however, all units will get concession at a 'uniform' rate.

Considering that the concession on domestic product is higher than on imports — in respect of both urea and DAP, this may be perceived as violating the National Treatment provision under Article III.4. The exporting countries may raise the issue at the WTO. The US has a major stake in the Indian DAP market. In recent years, there has been a drastic reduction in its exports to India primarily due to the increase in the differential concession. Therefore, it may be contemplating such an action!

A close examination of the Agreement, however, reveals that under Article III. 8(b), the subsidy given 'exclusively' to the domestic manufacturers is not precluded. Can India's subsidy/concession regime be WTO-compatible under this Article? In this context, a decision of the Dispute Settlement Body (DSB) in case of the European Community subsidy payments to the producers of oilseeds — on a complaint filed by the US — may be relevant.

In this case, the government fixed a 'target' price (this was not mandatory) for oilseeds which was higher than the import parity price (IMPP). Now, if the processor of oilseeds bought oilseeds from the domestic producer, he was entitled to get the difference between the target price and IMPP as subsidy.

Significantly, he would get this amount in full even when his actual payment to the producer was less than the target price.

The US challenged this dispensation at the WTO on the grounds that it gave a less favourable treatment to the exporter of oilseeds to the European Community and therefore, violated the Article III.4.

On the other hand, the European Community defended this as being a subsidy given 'exclusively' to the domestic producers and therefore, compatible with the WTO under Article III 8(b).

In its decision, DSB held that the stand taken by the European Community was not tenable as the arrangement did not rule out the possibility of even the processor of the oilseeds benefiting from the subsidy (this situation arose when the price actually paid by him was lower than the target price). Consequently, it could not be given the benefit of 'exclusivity' under Article III 8(b).

Drawing an inference in the context of fertiliser subsidy payments in India, the fertiliser producer is the counter-part of the oilseed producer in the European Community. And, the farmer (or the consumer of fertilisers) is the counter-part of the oilseed processor.

The 'target' price is the retention price, say, Rs 8,000 per tonne that the domestic producer should get. While, the farmer pays Rs 4,830 per tonne (selling price notified by the Government), the Government gives subsidy of Rs 3,170 per tonne to cover the difference. Since the entire subsidy amount goes to the producer, the dispensation may appear to be WTO-compatible under Article III 8(b).

On the other hand, if, we follow the economic benefit approach, the conclusion may be different. Under this, the price paid by farmer and price realised by the producer has to be compared with the IMPP of urea. Thus, if, the producer gets more than IMPP, the difference is subsidy to him. And, to the extent, farmer pays less than IMPP, he enjoys subsidy.

> Under the economic approach, India's subsidy regime may not be treated as WTO-compatible! There is an urgent need to pay attention to the conventional WTO-compatible mode — import duty for providing reasonable protection to the domestic fertiliser industry.

Currently, the IMPP of urea is about Rs 7,000 per tonne. In view of this, the subsidy to the producer is Rs 1,000 per tonne (Rs 8,000 – Rs 7,000). The farmer too gets a subsidy of Rs 2,170 per tonne (Rs 7,000 – Rs 4,830). Therefore, both the producer and the consumer share the benefit of subsidy. In case of DAP also, the situation is similar. Thus, under the economic approach, India's subsidy regime may not be treated as WTO-compatible!

During the transition, there will be 'five' concession rates under the ERC package. Of these, 'three' are for plants in the naphtha, fuel oil/LSHS and mixed feedstock groups, respectively. These are significantly higher than the concession for plants in the other 'two' groups based on gas (pre-1992 and post-1992) due to use of inferior feedstock and their higher cost.

Since the higher concession for these 'three' groups is intended primarily to offset their disadvantage due to inferior feedstock and vintage, the possibility of this being treated as industrial subsidy under the WTO is not ruled out. The exporters can take recourse to Article 6.3/7.8 of the Agreement on Subsidies and Counter-veiling Measures (ASCM). Likewise, the FDCR for plants based on LNG including naphtha-based plants that have switched to LNG from April 1, 2006 may also be actionable.

As a safeguard measure, the Government could show purchase from domestic manufacturers as 'Government Procurement' which, at present, is not WTO-covered. Considering that the entire urea production is sold at a 'uniform' price under its directive, there is a valid basis for this. As and when 'Government Procurement' is brought under the WTO's purview, it could seek exemption for fertilisers.

There is an urgent need to pay attention to the conventional WTO-compatible mode — import duty for providing reasonable protection to the domestic industry.

In case of urea, currently, the applied rate of Customs duty is a measly 5 per cent. At present, urea is 'unbound' item. During the current round of negotiations, the Government may retain its 'unbound' status to enable increase in the applied rate to the desired level.

Even if it has to declare a bound rate, this should be fixed at a fairly high 100-150 per cent. This is necessary in view of exorbitant prices of naphtha and fuel oil — about $7.0 per million Btu and $5.5 per million Btu in India as against a throw away price of less than $1.0 per million Btu for gas charged in exporting countries.

In case of DAP, currently, the applied rate of Customs duty is 5 per cent. Significantly, this is also the 'bound' rate on DAP.

Therefore, the applied rate cannot be raised unless the bound rate is increased first. For this, the Government will have to initiate proceedings as provided for under Article XXVIII.

The issue has to be discussed with countries holding initial negotiating rights (INR). For a host of agricultural commodities, including rice for which the bound rates were increased in 2000, the exercise was completed in 'four' years.

The ball should be set rolling right away.

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