FDI in Multi Brand Retailing: The Reality Check

Discussion Paper Towards fulfilment of internship with CUTS-CCIER (February – March, 2014)

1. INTRODUCTION

"***A big welcome and one of boldest steps. I hope this will be reflective of new era of reforms and re-instil investor confidence in India. Global retailers will now definitely get back to their drawing boards to explore India plans. Also, Indian retailers looking for expansion and fund raising will look forward to studying the fine print. Possibly first time in FDI regime, Centre has left to each State to decide whether it wants to opt-in for FDI in multi brand retail for their respective States***."

- Paresh Parekh**,** Tax Partner - Retail Practice, EY India[1]

In 2001, economist Jim O'Neill in his paper entitled '*Building Better Global Economic BRICs*' coined the acronym "BRIC"[2] which related to the shift in global economic power and the change in the political and economic potential of the countries. Goldman Sachs stated that the four BRIC countries were growing exponentially; however, they asserted that the true potential of the BRIC economies would become apparent by the year 2050 which would cumulatively eclipse the economies of the current richest economies of the world.[3]Afterthe publication of the paper, the international community tagged India and China as the next super-powers[4]. With all the stipulation and speculations surrounding India, foreign investors and institutions came swarming to India for investing into the magnanimous economy.

It came as no wonder when the Indian Government opened the sluice gate to the foreign investors to invest into the country.However, sensitivity with respect to FDI is witnessed in extreme polarity among Indians. Every time the Government opens the gates of the economy to the FDI, the issue is confronted with two divergent and polar arguments. FDI in retail trading came as no exception.

With this background, the paper aims to firstly understand the rationale of FDI especially that in multi brand retail sector (hereinafter referred to as MBRT) and analyse India's policy through interpretation of Press Note 5 of 2013 series[5] vis-à-vis WTO commitments of India and the FDI policy followed by the Government in the light of the provisions under the Indian Constitution. The second part of the paper shall attempt to assess the impact of the FDI in MBRT over the agrarians from a mirror perspective of producer and consumer; impact over MSMEs, consumption patterns, FMCGs, and a parallel analysis of the same with FDI in e-commerce and the Food Security Bill[6]. The third part shall evaluate FDI in MBRT from legal perspective[7] and implication on centre-state and states *inter-se* relations due the nature and manner of implementation of the policy[8]. The fourth part shall criticise the need and requirement of a regulator in the retail sector. Finally, the paper would end by drawing suggestions for the policy to make it more beneficial for the economy while maintaining the social balance for the purposes of sustainable development.

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[1]http://www.ey.com/IN/en/Newsroom/Ernst-Young-quotes-Announcement-on-FDI-in-multi-brand-retail .

[2]Brazil, Russia, India and China. The acronym was given by Jim O'Neill, on the basis of the PPP and GDP of these countries vis-à-vis the G-7 countries.

[3] Jim O'Neill, '*Building Better Global Economic BRICs*', Global Economics Paper No. 66, GE Global Economic website http://www.content.gs.com/japan/ideas/brics/building-better-pdf.pdf accessed on February 15th, 2014.

[4] Doug Bandow, 'Is India an Economic Superpower in the Making', Forbes, (2011) http://www.forbes.com/sites/dougbandow/2011/03/07/is-india-an-economic-superpower-in-the-making/ accessed on February 15, 2014; and The Economist, 'Chasing the Dragon', The Economist (2011) http://www.economist.com/blogs/dailychart/2011/10/comparing-india-and-china accessed on February 15, 2014.

[5] Press Note 5 of 2013 series discussed under the head *FDI in India and Multi – Brand Retailing: An Introduction*.

[6] The social implications are discussed under the head *FDI in Multi Brand Retail and Social Implication*.

[7] Discussed under the heading *FDI in Multi Brand retail: Legal Implications.*

[8]Center – State relations are discussed under the head *FDI Policy and Centre – State Relations*.

2. FDI IN INDIA AND MULTI BRAND RETAILING: AN INTRODUCTION

"***Foreign investment would bring attendant advantages of technology transfer, marketing expertise, introduction of modern managerial techniques and new possibilities for promotion of exports.***"

- New Industrial Policy of 1991[9]

The Liberalisationpolicy of 1991[10] led to influx of foreign players into the Indian economy and eventually in 1997 Indian Government opened the first sluice gate to channelize the FDI funds through Government route into the Indian economy. It is fact, that, FDI Policy is a natural successor of the liberalisation policy adopted by an economy.Prior to the understanding of FDI in general and FDI in MBRT *in specie* it is important to understand position of India as an economy in the present business perception. There lies no doubt that India is considered as one of the fastest growing economy after China, however, Indian abstinence to embrace global connectedness has resulted into dilapidation of the same. The GCI[11] has revealed some interesting facts as to India's position vis-à-vis other significant economies. India has an overall rank 62 out of 140 countries. India has a higher breadth (20 out of 140) than depth (119 out of 140) reflecting that India has limited intra-regional connectedness (owing to its poor relations with her neighbours especially with China and Pakistan) thereby forcing India to connect with countries at a remoter distance. However, the Index reflects India as one of the strongest economies in terms of trade where it scored 33rd position first in the region and 3rd out of world's 10 largest economies. In light of the above data it becomes obvious that India is pregnant with trade and investment possibilities and is a fertile ground to yield high profitability.

BOX 1 UNCTAD Interpretation of FDI

viz.,

a) It is an investment made by a resident of one economy in another economy and it is of lasting interest or long term nature; and
b) The investor has certain degree of significant influence on the management or control of the enterprise.

Source: UNCTAD Training Manual on Statistics for FDI and the Operations of the TNCs, Vol.I (2009).

FDI is more than merely buying securities of the entity wherein the funds are channelized, it revolves around the financing provided by the foreign investor and the investor by virtue of the FDI turns into an owner/ manager of the entity into which the FDI is directed. In case of a FDI, the gestation period of the investment so made is usually long. FDI is investment not just in the coffers of the entity but also in the fixed assets, personnel and management of the entity.[12]

FDI in India is sector specific in nature, and the approval is procured either by Automaticor by Government routes.[13] Also, the FDI is subjected to cap limit, i.e., the maximum amount of investment in a sector that can be made by the investor and a minimum amount in certain cases.[14]

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[9] Government of India, India's New Industrial Policy of 1991, available at http://business.webindia.com/polinwid.htm accessed on February 18th, 2014.

[10] In 1991 India faced an acute balance of payment crisis, which led India to pledge 20 tonnes of Gold to the Union Bank of Switzerland and 47 tonnes to the Bank of England as a part of bail-out deal with the IMF. Resultantly, IMF compelled India to undertake a series of economic reforms which affected the country's international and domestic trade dimension out of other measures that were thoroughly touched. This led to the liberalisation policy of the Government of India in 1991.

[11] Global Connectedness Index. All data is as per GCI 2012.

[12] Ibid.

[13] Automatic Route entails that the FDI is made without seeking prior approval of the Government of India or Reserve Bank of India. Government route entails activities that are not covered under the automatic route requiring a prior approval of the Government which is considered by the FIPB and the Department of Economic Affairs, Ministry of Finance. Both Automatic and Government routes need to comply with provisions of FDI policy.

[14] Where ever there is a requirement of a minimum cap it shall be inclusive of the share premium received along with the face value of the share only when it is received by the companies upon the issue of the shares to the Non-resident investor. Amount paid by the transferee during post-issue transfer of share beyond the issue price of the share cannot be taken into account while calculating minimum cap requirement. See A.P. (DIR Series) Circular No. 137, Dated June 28, 2012.

FDI help the indigenous companies to obtain their full potential by channelizing foreign capital thereby lowering costs and also by procuring better and sophisticated technologies for them.

BOX 2 FDI in Layman Terms

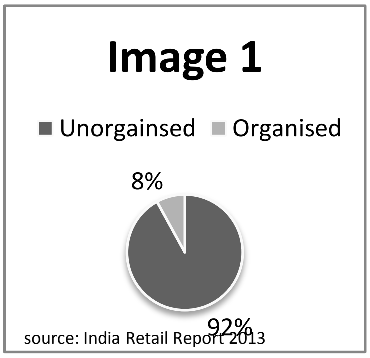
The general concept of FDI encapsulates the idea of flow of funds from a larger pool of money within one economy into another pool in another economy with the intention to yield profit out of the money so invested. FDI is sector specific in nature, that is to say, that the fund channelized through the FDI route is diverted to a specific sector be it manufacturing, mineral excavation, agriculture, food processing or even retail. The fund invested brings with it technology, expertise, skill, novel business models and structural changes in the socio-cultural avenues.

FDI in India is executed envisioning inflow of investment, generation of revenue and employment, enhancement of technology and services pertaining to the retail sector. In 1997, FDI through Government route was allowed in cash and carry retailing.

I. <u>FDI in MBRT: Meaning and implications:</u>

Paul Etgart, a former director of the retail giant Tesco warned while addressing Image Fashion Forum in 2005, "*Indian retail business should not be fooled by partnership offers by global retail giants because they want 100% control and eventual ownership....[U]rgeyour government to retain your strict FDI regulationsfor global retail giants are very smart and clever to tackle local cultural and political obstacles. India must beware.*"[15]India's retail sector is considered as one of the most luring sector of the whole economy at the same time it has been a sensitive sector that affects almost all the sections of the society and economy alike. Retail sector in India comprises of

a) Organised[16]; and
b) Unorganised[17]. (see Image 1)

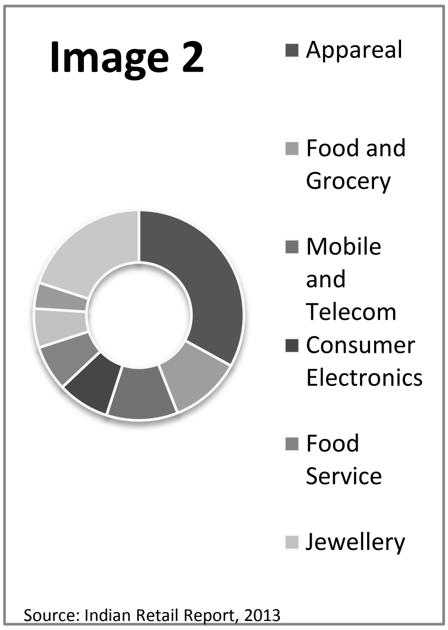


The policy on FDI in retail sector in India is clearly divided into four distinct types:

a) Cash and Carry Wholesale Trading[18];
b) E-commerce[19];
c) Single Brand Retail Trading[20]; and
d) Multi brand retail trading[21].

Among the large hue and cry over the issue of FDI in retailing sector, the policy on FDI in MBRT was approved and accordingly was enacted by issuing the Circular No 1 of 2013 and later the provisions of the FDI in MBRT was amended by the Press Note 5 of the 2013 series. The amended FDI norm for MBRT via Press Note 5 creates a minimum investment limit of US$100 mnfor the investor and that at least 50% of

[15]The Hindu, 'Develop retail sector, India told', (Mumbai, 21 January 2005).
[16] Organised sector comprises of the traders who possess legal permissions and licences to retail and are registered with VAT/ sales tax.
[17] Unorganised sector comprises of local *kirana*, general or family shops registered under Shops and Establishment Act. Unorganised sector also incorporates informal sectorthat includes small grocery or vegetable shops run from a room of a house or *paan/beedi* kiosks, wayside vendors or hand carts etc.
[18] Cash and carry is the sale made to retailers, industrial, commercial institutional and professional businesses or to wholesalers. It is approved via an automatic route and with 100% cap limit.
[19] FDI in e-commerce is on B2B model and not B2C model. It is made through automatic route with a cap limit of 100%.
[20] Single brand retail trading primarily means wherein product of a single brand is sold, that such product is sold internationally under the same brand, these products need to be branded during manufacturing. It is made through Government route subjected to 100% cap limit.
[21]Multi brand retail trading means, where many items are sold under a single roof.



whatever amount of investment so made,[22] shall be diverted to the 'back-end infrastructure', within 3 years. Here 'back-end infrastructure' would mean to include investment made towards manufacturing, processing, distribution, design improvement, quality control, logistics, storage, warehousing, packaging, agriculture market produce infrastructure. However, 'back-end infrastructure' would exclude all front end units. FDI in MBRT shall be dependent upon the business needs of the sector.[23] The Press Note further states, that at least 30% of the manufactured products in the procurement shall be supplied from the Indian Micro, Small and Medium Enterprises[24] (MSMEs).[25] It also provides the retail sales outlets shall be set in cities with a population of more than 10 lakhs or any other cities as per the discretion of the respective State Governments. The sales area may also cover 10 kms radius around the municipal/ urban settlements.[26] Another significant aspect of the FDI in MBRT is that the Government reserves with itself the right of first procurement of the agricultural produce. And also the discretion is left with the state to allow retailing to the Foreign Investors. Like FDI in any other sector, FDI in MBRT attracts certain pros and cons too. Advantages of FDI in MBRT include:

- Enhancement in the merchandising and inventory management;
- Provision of technology to improve productivity;
- Allow integrated supply-chain management to lower down prices of products, better customer services and product quality;
- Promotion of local suppliers and enhancing quality and reliability of products so supplied by them, increase employment opportunities and competition in the market;
- The joint ventures would ease the capital constraints on the organised retailers and overall it would lead to modernization of the sector.

The FDI in MBRT would directly affect the organised sector especially because such FDI would become functional by means of a JV. Hence, direct effect of the FDI will become visible only on 8% of the total retail market and its suppliers (Image 2.).

On the flip side though, it has been argued by many that FDI in MBRT might lead to wiping off of the petty retailers and MSMEs, it may also lead to the competition distortionary policies resorted by the big retailers wiping out the competition posed by the petty mom and pops shops. Those opposing FDI in MBRT, also fear thatit could also result in employment losses to many with the closing down of the retail shops, however with scanty evidence. Moreover, political lobbying and relapse of '*permit raj*' is among other concerns. Most importantly, with the ongoing charges over Walmart of bribery, concern is raised regarding the repetition of similar situation in India.[27]

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[22] That is hypothetically, if there is a venture of US$100 bn then the permitted FDI cap is of 51% i.e. US$ 51bn can be channelized; 50% of this US$ 51bn i.e. US$24.5 bn needs to be directed towards back-end infrastructure.

[23] Press Note 5 of 2013 series, amendment to paragraph 6.2.16.5(iii) of the Circular No1 of 2013

[24] Those MSMEs who total investment of or below US$ 2 Mn. The amendment clarifies that despite the MSME worth may exceed $2 mn still they shall be continued to be termed as MSMEs for the purposes of MBRT.

[25] Press Note 5 of 2013 series, amendment to paragraph 6.2.16.5(iv) of the Circular No1 of 2013

[26] Press Note 5 of 2013 series, amendment to paragraph 6.2.16.5(vi) of the Circular No1 of 2013

[27] Economic Times, 'Walmart's India fallout started with Allegations of Bribery in Mexico' http://articles.economictimes.indiatimes.com/2013-07-25/news/40795626_1_bharti-walmart-fcpa-violation-walmart-mexico accessed on February 19th, 2014; also read Janik Radon et al., 'the Walmart Corruption Scandal: Watershed Moment for Mexico?' Huffington Post, http://www.huffingtonpost.com/jenik-radon-esq/the-walmart-corruption-scandal_b_2389635.html (March 3rd, 2012) accessed on February 19th, 2014.

Despite of the speculations over the ill effects of the FDI in MBRT, there is no denial in the fact that the FDI is a much needed requirement for the complete change of the retail sector that would make it more functional and pro-competitive in nature.

3. FDI IN MULTI BRAND RETAIL AND SOCIAL IMPLICATIONS

FDI in MBRT would profoundly affect the social balance of the country, be it the retailers, farmers, MSMEs and consumers paradigm shifting changes are envisaged. These changes and implications shall be gauged into under separate heads.

I. IMPACT ON AGRICULTURISTS AND AGRICULTURE

India is primarily an agrarian country that has second largest arable land in the world. India produces around 250 mn tonnes of food grains in a year despite of the grand data of production, around 250 mn people go to bed hungry each day. This is primarily due to lack of backend infrastructure to support production in the country. The SaumitraChaudhari Committee estimated that India requires cold storage of 61.3 tonnes capacity while presently it accommodates a capacity of around 29 mn. The Centre extends grant-in-aid to states to construct cold chain storage units but has kept the sealing limit as Rs. 10 cr.[28]The budget kept for the infrastructure and the food spoilage as well as requirement capacity pointed by Chaudhari committee reflects a dismal situation of agricultural produce and the sector *per se* in India. One may even wonder that how can India (on itsown) manage construction and support of cold chain infrastructure with a fiscal deficit of estimated 4.6% in FY 2013-14.[29]

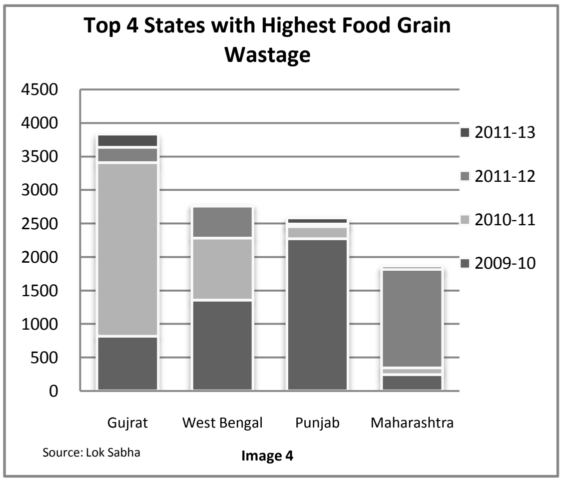

Image 4

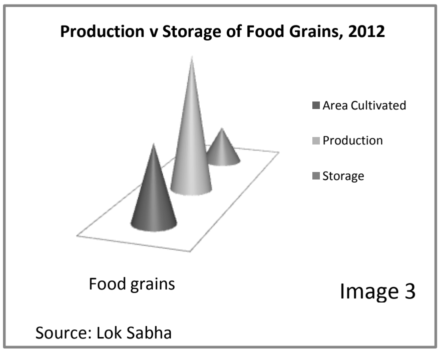

Image 3

FDI in MBRT would have three pronged effect on the agriculturist, i.e., as producers, consumers and also as petty retailers. There is no denying in the fact that the agriculture scenario is detrimental and sensitive in India. On one hand a large portion of the demography is dependent on the sector while there is not much done by the Government in terms of research and development and providing quality warehousing structure since the first Green Revolution[30].

The FDI in MBRT as a policy provides for directing 51% of the FDI into the "backend infrastructure" creating a much needed skeleton for the agro-based retailing in India. Allowing FDI in MBRT, when coupled with FDI in Agriculture[31] provides a fertile ground for the foreign investors to invest and usher in not just monetary investment for the farmers but better R&D facilities, technology transfer along with sophisticated supply chain units such as cold storage and warehouses and modern logistics into the sector.

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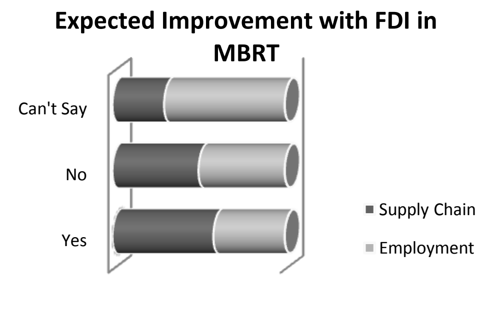
[28] DHNS, 'India Wastes Rs. 44,000 cr worth Food Every Year', Deccan Herald (New Delhi), August 23rd, 2014 http://www.deccanherald.com/content/352942/india-wastes-rs-44000-cr.html accessed on February 24th, 2014.

[29] AsitRanjanMisra, 'Interim Budget: P.Chidambaram Manages to Cap Fiscal deficit at 4.6%', Live Mint, (New Delhi), February 17th, 2014 http://www.livemint.com/Politics/3EV4D93YTR17RkKHIgif9K/Interim-budget-Chidambaram-says-FY14-GDP-growth-to-be-49.html accessed on February 24th, 2014.

[30] A movement including huge research and development coupled with technology transfer initiated in 1968 in India. Leading to usage of better irrigation facilities, High yielding variety of seeds, fertilizers etc., thereby increasing the per hectare production of food-grains and hence making India surplus in terms of grains, vegetables and fruits.

[31] Press Statement for FDI in Agriculture released dated August 13th, 2013 allows 100% FDI in the sector under controlled conditioned. The press statement specified that the FDI policy in MBRT provides for 50% of the first tranche of US$100 mn shall be invested in 'back-end infrastructure'.

In turn, the investors can get access to the untapped retail market of the country, while the consumers can benefit in terms of quality, price and variety. It's a win-win situation for all.



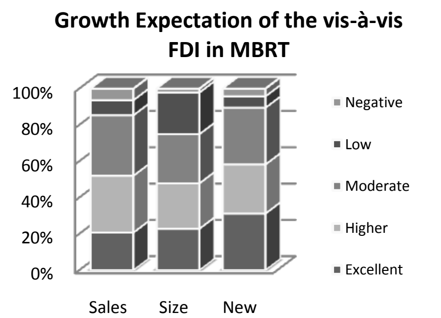
Source: CII Survey (The Impact of FDI in Retail on SME Sector, 2012)

Image 5

The FDI in MBRT when viewed in light of the FDI in Agriculture reveals that when the former is seen as an extension of the latter, then not just the agriculturist but also agro based industries and food processing sector would also flourish. The fact that area would be allocated for the FDI funded retailing outlets decrease the threat to the farmers as '*petty retailer*'. The retailing activity done by a farmer in any way is very miniscule and is concentrated in or near the area of their settlement such as a village or a hamlet. Therefore, the presence of the FDI funded retail store would not affect the farmer as retailer. As a consumer, of warehousing facilities and logistics would facilitate them while the investment channelized towards R&D and better HYV seeds and fertilizers and assurance of a ready market for their produce would act as an incentive to the farmers as a producer.

II. <u>IMPACT ON MSMEs AND FMCGs</u>

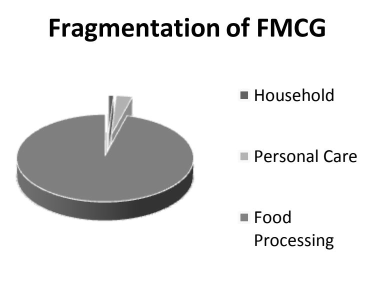
Micro, Small and Medium Enterprises (herein after referred to as "MSMEs") are considered as the key instrument for the purposes of equitable economic development. In India, MSMEs are all the more significant owing to their role in the nation's development through high contribution to domestic production, significant export earnings, low investment, operational flexibility, mobility of location, low intensive imports, capacities to appropriate indigenous technology, import substitution, contribution towards defence production, technology oriented industries, generating competition in domestic and export markets and creation of new entrepreneurs by providing knowledge and training.[32]The MSMEs in India, is infested with an unstructured and loosely regulated under the Micro, Small and Medium Enterprises development Act, 2006. The Act is silent on the functioning of the MSMEs, the supply chain mechanism to be utilised and the output regulation of the MSMEs. Therefore it stands imperative to device a mechanism that would facilitate the operation, supply chain management of the MSMEs along with regulation of quality of products manufactured by the same.



Source: CII Survey (The Impact of FDI in Retail on SME sector, 2012)

Image 6

With respect to the speculation that allowing FDI in MBRT would lead to eventual destruction of the indigenous industries, the Press Note 5 of 2013 series, clarifies that the 30% of inputs of the FDI funded retail stores shall be channelized from the MSMEs that have a total investment of not more than US$2 Mn[33]. However, if the said MSME grows in size and surpasses the monetary limit then also they will be considered for the purposes of the FDI in MBRT. For the purposes of interpretation the Press note 5 clarifies that sourcing from agricultural cooperatives and farmer cooperatives shall be considered as MSME transaction.



Source: AFSIL

Image 7

[32] CAIT, Impact of FDI in Retail on Micro, Small and Medium Enterprises of India (New Delhi, CAIT publications, New Delhi, 2011) http://www.cait.in/e-book/Impact%20of%20FDI%20in%20Retail%20on%20Micro,%20Small%20and%20Medium%20Enterprises%20of%20India.pdf accessed on February 26th, 2014.

[33] Valuation shall be exclusive of depreciation costs.

In a survey conducted by the CII, it was found that most of the SMEs were of the opinion that the FDI in MBRT would translate a bigger gain to them. Around 2/3rd of the SMEs across the country opined that the entry of multinational retailers is an opportunity to increase sales, quality, size of business and capacity addition, generate new orders and thereby lead to branding of their products and creation of employment. They agreed that influx of foreign companies in retail business would directly affect business mechanism and supply chain management.[34]

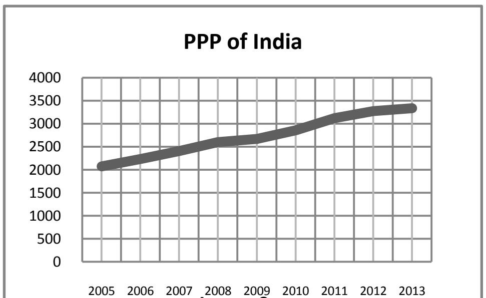
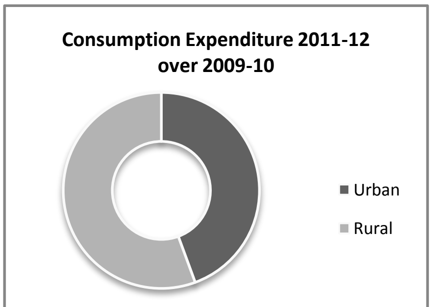


Image 9

Another significant part adjacent to the MSMEs is the FMCG section of the retail sector. The Fast Moving Consumer Goods or FMCGs account for nearly 2.5% of India's GDP. While just food products and personal care products account for 2/3rd of the sector's revenue.

India is considered as one of biggest producer of FMCGs and the sector is fourth largest in size vis-à-vis the Indian economy. The market size of the section is expected to grow from US$ 30 bn to US$ 74 bn in 2018. Growing awareness, easier access and changing lifestyle have been the key drivers for the proliferation of the sector. Rural demand is set to rise with the rise in incomes and greater awareness of brands. The FMCG section in India is divided into household, personal care and food processing products. This sector is dominated by players such as Dabur India, Hindustan Unilever, ITC, Marico etc. Despite of the good picture of the FMCG section of retail sector, coupled with the fact that India is one of biggest producer of FMCG products, but the country's export accounts for a small proportion of the overall output. This is primarily due to the quality of the products so produced and the lacuna prevalent in the supply chain management thereby the FMCGs have limited or no access in the untapped markets in the country. The requirement at this point of time for the section is in terms of requirement of investment. With 200 mn people expected to shift to processed and packed food, Indian FMCG sector needs around US$ 30 bn for investment in food processing industry alone. This investment can usher in by way of FDI in MBRT.



Source: Crisil
Image 8

The temperament and significance of FDI in MBRT over FMCGs can be understood by the fact that as soon as the policy was declared, defensive FMCG stocks declined on profit booking at the stock exchanges, as investors shifted their attention to high beta stocks. Hindustan Unilever, Dabur India, Marico and Nestle dropped by 0.27% to 2.45%. On the other hand, Reliance India Limited witnessed a hike of 3.91%, due to its presence in the retail industry by way of its subsidiary Reliance Retail.[35]

III. IMPACT OVER CONSUMER BEHAVIOUR

Justice R.M. Lodha, while upholding FDI in MBRT, said in a recent judgement, that, "*Consumer is the king and if that is the philosophy working behind the policy then what is wrong with it.*"[36]The high influx of FDI in India emanates from the fact that the India exhibits a high purchasing power parity[37] which in turn reflects the purchasing power[38] of the people at large. Influx of MBRT would mean exploring this purchasing power of the consumers making them more empowered in terms of preference and bargaining power[39]. The theory of consumer choice relates to preference to consumption expenditures, this relation between the preference and the consumption expenditure reflects in turn the consumer demand. Here preference are the desires by each individual for consumption of goods

[34] CII, 'Impact of FDI in Retail on SME Sector', (Survey Report, 2012) http://cii.in/WebCMS/Upload/IMPACTOFFDIINRETAILONSMESECTORSurvey.pdf accessed on February 26th, 2014.
[35] India Infoline, 'FMCG, Pharma stocks Lose Ground', IIFL www.indiainfoline.com/Markets/News/FMCG-pharma-stocks-lose-ground/4515015120 accessed on February 26th, 2014.
[36] *ManoharLal Sharma v. Union of India and Another*, 2013 STPL(web) 399 SC)
[37] Purchasing power parity enables the estimation of what the exchange rate between the two currencies would have to be in order for the exchange to be at par with the purchasing power of the two country's currencies.
[38] Purchasing power means the number of goods that a unit of currency can purchase.
[39] Bargaining power is the relative ability of the parties to exert influence of each other.

and services that translates into choices which is dependent on the income for the purchase of the goods coupled with the consumer's time to define the consumption activities. In a nutshell, the inflow of FDI in MBRT would in increase substitutability of goods for the consumers creating more options in terms of choice and preference within the wide spectrum of purchasing power of the consumers.

One of the greatest concerns that most of the people raise against FDI is related to predatory pricing. It is anticipated that the foreign funded retailers would resort to competition distortionary policies and therefore would manipulate the market so that the competition in the market is adversely affected and that would have a direct implication over the consumers.[40] However, evidence for such claims is unconvincing. Evidence, on the contrary suggest that the inflow of FDI in MBRT would curb the malpractices of the retail stores especially with respect to the distortion of prices for certain goods and commodities such as selling the goods at a higher price than the MRP. Thus, giving the customers the benefits of a competitive market by restricting anti-competitive conduct.

With reference to social implications, the most significant impact of FDI in MBRT is on the consumer behaviour and purchasing pattern. It is to be noted here that each consumer has a distinct buying habit which may or may not coincide with buying behaviour pattern. Behaviour pattern primarily means the design of behaviour of a large number of customers.[41]The buying habit or behaviour are not stationary in nature but are dynamic, despite the fact that certain variables of this buying habit may resist change. Customer buying pattern can be grouped on account of certain variables such as:

1. Place of purchase;
2. Items purchased;
3. Time and frequency of purchase;
4. Method of purchase; and
5. Response to sales promotion device.[42]

Customer behaviour with influx of FDI in MBRT would get deeply affected by the factors 1, 2 and 5 which would in turn result in factors 3 and 4, as stated above. FDI funded retail store with their modern marketing mechanics would lure in the higher middle class Indians with greater purchasing power. There is no doubt that Indian economy is at the juncture of transformation both in terms of economy as well as social structure. The common man with less purchasing power and more tendencies to save has now assumed the role of spending more on luxury and attaining elite shopping experience. Common man today does not just want to buy goods and services but want to have a shopping experience too, the influx of FDI in MBRT would definitely support this.

Consumers have already witnessed a sea-change in the shopping and purchasing power experience with the domestic orgainised retailers such as Big Bazar, Reliance Retail etcnow with the influx of foreign retailers into the market the shopping experience of the consumers will multiply not just in terms of choice but also in terms of wider spectrum of price of commodities.

IV. FDI IN MBRT v. FDI IN E-COMMERCE

There exists a difference between buying a product and shopping a product. Buying a product implies procuring a commodity in lieu of a consideration while shopping suggests an experience which incorporates not just purchase of a product but also providing services and choices so that the consumer makes an informed decision.[43] Physical retailers allow shopping as well as buying opportunity to their cliental while through e-commerce; consumers can have shopping experience only. E-commerce is simply put marriage of technology and retailing, thereby, has distinct and different requirements than retailing *per se*.

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[40] This aspect shall be dealt in detail under the Legal implications.
[41] William Applebaum, 'Studying Customs Behaviour in Retail Stores', TJM http://www.ecu.edu/cs-cas/anth/nuevosouth/upload/studyingcustomerbehaviorinretailstores-090623023217-phpapp01-slideshare.pdf accessed on February 26th, 2014.
[42] Ibid.
[43] Ibid.

The DIPP announced its intention of opening FDI in e-commerce through its discussion paper in January, 2014. The Discussion paper invited comments upon the initiative so made by the DIPP and requested the industry and NGOs related to consumer protection and benefit to suggest the cap limit of the said FDI. The DIPP suggested a cap of either 51% (as in case of MBRT) or 100% (as in case of SBRT).[44]

E-commerce like retail works on two business formats; it can be either B2B[45] or B2C[46]. At present, India allows 100% FDI under the automatic route in B2B commercial operations. The distinctiveness of e-commerce transaction becomes apparent from the fact that such transactions attract not just the FDI policy of the country but also must be in synchronisation with the Information technology Act, 2000, Consumer Protection Act, 1986, Contract Act, 1872, Indian Penal Code, and also involves banking laws applicable on such transactions[47].[48]It is pertinent to note, that, unlike MBRT e-commerce is not geographically bound.

The influx of foreign retailers in e-commerce sector will bring with them the inventory based model of business, which yet is not widely practiced in India. In India marketplace model of business is widely practised. Inventory based model means that the retailer has complete control over the product, therefore can exercise greater visibility into the stock level, know the physical location of the product and control the pick, pack and shipping process which in turn means that the process minimises the risk of accepting orders only to later realise non-availability of the same, optimizing dispatch time and to increase accuracy and respond effectively to customer inquiries about shipping status. The disadvantage of the model, however, is that since movement of the product is in complete control, hence the companies' compromise capital efficiency because they buy product from vendors up front that is to say that they tie up capital in inventory.[49] On the other hand, theMarketplace model entails post purchase experience to the customers such as fulfilment and customer service.[50]It is now a known fact that marketplace model has its own flaws that can be dealt with only by inventory led model.[51]

Marketplace model of ecommerce would have not fundamentally impaired the functioning of the influx of the MBRT in India. India has exhibited a consumption based pattern coupled with an increase in income of the people that has fostered the organised retail sector.[52]Marketplace model based ecommerce has successfully co-existed with the retail sector in India. However, the shift from marketplace to inventory model would hamper the retail sector in terms of loss of consumers owing to the geographical boundations and would also act as impediment in procuring the products from MSMEs since the MSMEs would be unable to supply products in adequate amount to the FDI funded retailers.[53]

When compared to FDI in MBRT, FDI in e-commerce would impair the spirit of the former owing to its nature and would therefore allow commercial presence beyond geographical bounds. Owing to the complexity and dexterity of the ecommerce business models, the consumers will gain higher bargaining power.[54]

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[44] DIPP, 'Discussion Paper on E-commerce in India', Discussion Paper, dated January 7th, 2014 http://dipp.nic.in/English/Discuss_paper/Discussion_paper_ecommerce_07012014.pdf accessed on February 5th, 2014

[45] Business to Business operation model allows transaction between two businesses only. For instance, transaction between an e-commerce portal (Business 1) and a retailer or a wholesaler (Business 2).

[46] Business to Consumer, as the name suggests, is the operation model that allows a direct transaction between the e-commerce portal and the consumer.

[47] Especially in case of payment portals, where the portals need to take permission from the RBI with respect to enable web based transactions.

[48] Supra Note 44.

[49]BejulSomaia, "The Inventory is Marketplace Model Debate", www.vccircle.com/blog/2013/04/22/inventory-vs-marketplace-model-debate accessed on April 3rd, 2014.

[50] Ibid.

[51] Next Big What, "Inventory based ecommerce model is flawed: KunalBahl, Founder, Snapdeal", www.nextbigwhat.com/inventory-based-ecommerce-model-is-flawed-kunal-bahl-founder-snapdeal-297/ accessed on April 3rd, 2014.

[52]FICCI and PWC, "The Indian Kaleidoscope Emerging Trends in Retail" http://www.pwc.in/en_IN/in/assets/pdfs/industries/retail-and-consumer/retail-report-300812.pdf accessed on April 4th, 2014.

[53]Piyush Kumar Sinha, "Development of Modern Retail in India: It's Impact on Distribution and Procurement Networks and Changing Consumption Pattern", Working Paper No. 2012-12-04, Indian Institute of Management, Ahmedabad.

[54] FE Bureau, 'Opening up e-commerce against spirit of FDI in Multi-Brand Retail', Financial Express (New Delhi) January 7th, 2014.

Some have advised that the FDI in ecommerce must be allowed with a cap of 49% and like FDI in MBRT it must be geographically bound.[55] But the question raised in regard of such suggestions is how to geographically restrict internet operations and whether or not such restriction would be against the National Treatment objective as enunciated under the WTO Agreements.

The most significant question that comes to mind is whether the introduction of the FDI in e-commerce into the country is correct action at the present point of time, bearing in mind that the Government has assented to the 51% FDI in MBRT. The move of allowing FDI in e-commerce would impair the very purpose of enticing foreign investors into the retail sector of the country. The move would go ahead and discourage the investors to invest in a sector that is duly divided and where they have the disadvantage of creating infrastructure and follow stringent regulations as and when compared to the FDI in e-commerce.

The RBI has of late announced the Report of Technical Committee in mobile banking operations of the banks which read with the DIPP discussion paper sounds like a prelude to the FDI in e-commerce.[56] There is no doubt that FDI in e-commerce must be opened by India, but the question is whether this is the right time? Whether preference must be first extended to FDI in MBRT to proliferate and let the small retailers, traders, MSMEs and consumers adapt to the present change and then slowly and gradually introduce FDI in e-commerce?

V. ROLE OF GOVERNMENT AND POLICY UNCERTAINITY

The role played by the central government with respect to the FDI policy vis-à-vis the policies to transform the agriculture and commercial infrastructure has been significant and worth analysing. The agriculture sector is cover under the State list under Schedule VII the Constitution of India. It is the work of the State Government to provide adequate assistance to the agriculturist to facilitate the production of the produce and also to provide adequate infrastructure such as cold storage, warehousing and logistics to store and allow finer movement of supply chain. The APMC Act has constituted Committees at State and District level to aid the farmers and to create a platform for the farmers to sell their produce. However as pointed out earlier, this model has led to the proliferation of middlemen that extract from the farmers and the consumers alike. This is a clear failure of Government policy. It is also pointed out that the Government has failed to provide adequate storage and logistic support to the agrarian and people at large which has resulted in high wastage of food by spoilage and thus resulted in inflation of edible commodities.

It has been many times pointed out that the basic problem of India is wastage and food spoilage which occurs in the five parts of the food processing chain: agricultural production, postharvest handling and storage, processing, distribution and consumption. It has also been pointed out that in India nearly 40% of food losses occur during postharvest and processing levels.[57] Due to lack o0f efficient cold storage facilities, one-third of the perishable goods goes to waste.[58] The FCI had publically raised concerns regarding the lack of warehousing

BOX 3 FDI in MBRT and the China Story

In China, FDI in MBRT has led to an exponential growth of small outlets from 1.9 mn to over 2.5 mn since the liberalisation of the sector in 1992, this has doubled the employment in both wholesale and retail. Moreover, in China financial services business is not allowed without a local partner and 67% is owned by a Chinese partner. This rule in China is respectfully followed by foreign investors in the country. China by allowing FDI in MBRT has given a wide variety of choices to its consumers and has also fostered modern retail infrastructure in the country.

Source: Kaanan Gupta, FDI in Multi-Brand Retailing: Lessons from China, CCS Working Paper No. 258 (2012)

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[55] Id.
[56] RBI released the 'Report of the Technical Committee on Mobile Banking' http://www.rbi.org.in/scripts/PublicationReportDetails.aspx?UrlPage=&ID=760 accessed on February 11th, 2014.
[57]Cederburg, Christelet. Al., "*Global Food Losses and Food Waste*", FAO, 20 April 2013
[58] "*Barriers in Indian Food Supply Chain Management*", MBA Skool Youjoomla.com

facilities in India.[59] Bearing in mind the shortage of warehousing infrastructure in India, the Government introduced a scheme called Private Entrepreneur Guarantee Scheme (hereinafter referred to as PEG) in 2008. The scheme involved invitation to the bidders for construction and maintenance of the warehouses. However, the Government failed to attract any investors through the PEG scheme and the deteriorated condition of the supply-chain continues.Since the FDI policy in MBRT allows 51% of the investment to be channelized into 'backend infrastructure' questions the intent of shifting State responsibility to the Foreign Investors of providing quality storage and logistics facilities.

However, the treatment with which the Government has dealt the FDIs is very dismal. Walmart entered into India by way of a JV with Bharti thereby forming the "Best Price" stores which ran on the B2B model. However, the fact that now Walmart has quit from India and Tesco has planned to entered the country raises many questions especially whether the FDIs are 'fair-weather friends' like FIIs? The answer can be found in the Government policies. The Government attitude towards the FDIs is extractive in nature in first place while on the other hand the Government in reluctant to strongly effectuate the FDI policy with respect to MBRTs this is possibly because of lack of political will.

The Investors have also understood the pulse of the Government policies and the lacuna present in the implementation of these policies, especially after the Delhi and Rajasthan government's withdrawal of FDI approval in MBRT[60]. No doubt, they are now seeking assurance from the Government to secure the investment so made by them. On one hand is the Government that has capped the FDI inflow inthe retail sector in line with China[61] while on the other hand there are foreign investors who want assurance of the government to safeguard the invested amount.[62]

VI. IMPACT OVER FOOD SECURITY ISSUES IN INDIA

Right to Food is an aspect of basic human rights, that ensures the right of the people to feed themselves with dignity, implying thereby sufficient food and ensuring dietary requirements to everyone. With introduction of Food Security Bill in the Parliament and the passing of the Act sparked off the debate on assuring food to the large Indian population. In the middle of cost and worth debate that surrounds the Food Security in India, it is to be understood that human capital is one of the most important resources of a country. Certain other facts that need to be considered are:

1. Hunger is number 1 cause of death in India;
2. There are 820 mn chronically hungry people in India, out of which 1/3rd stay in India;
3. About 20 cr Indian sleep hungry every night;
4. India has 212 mn undernourished people; and
5. Over 7000 Indians die of hunger every day.[63]

Bearing the above data it becomes obvious that India on one hand is turning into a huge economy with constant and growing GDP while its citizen are not just affected by hunger but also by malnutrition problems.

FDI in MBRT coupled with FDI in Agriculture would facilitate the government to assure this precious right to the citizens. FDI in MBRT would allow reduction in wastage of food items which would result in the creating a surplus that could be utilised to ensure food to all. The Food Security Act too needs to be amended to disallow stamp

[59] Martin Murray, "*No Food Shortages, Just Warehouse Shortages*", http://logistics.about.com/b/2012/05/15/no-food-shortages-just-warehouse-shortages.htm accessed on April 10th, 2014

[60] ET Bureau, 'AAP Government writes to DIPP, Withdraws Permission to FDI funded Retail Stores', The Economic Times (New Delhi) January 14th, 2014.

[61] China has FDI cap of 100% but mandates a JV with indigenous player in the same sector that own 67% of the JV ensuring control. Also see DeepshikhaSikarwar, 'Finance Minister P Chidambaram sure of big Foreign Retail Entry this Year', The Economic Times (Washington) October 12th, 2013.

[62] PTI, 'Walmart, Tesco seek assurance on Non-reversal of FDI Policy', The Economic Times (New Delhi) June 20th, 2014.

[63] Sources: UN World Food Programme; WHO Global database on Child Growth and Malnourishment, 2006; National Family Health Survey, 2005 found on http://www.bhookh.com/hunger_facts.php accessed on February 15th, 2014.

system.[64] Moreover, FDI in MBRT would create job opportunities which in longer run would affect the problem of employment that in turn would decrease malnourishment problem in India.

It is suggested that while allowing FDI in MBRT, the JV so formed shall be subjected to CSR norms under the Companies Act, 2013 mandating supporting or creation of organisations such as 'AkshayaPatra'[65] to feed the hungry, a miniscule price for the FDIs to operate in India. Akshyapatra and like NGOs that work towards elimination of classroom hunger are channels through which mid-day meals are provided to the children can be targeted to operate CSR functions of the JVs so formed. The NGO has the objective to eliminate classroom hunger, increase school enrolment, address malnutrition and also empower women through employment.

Dr. Sen stated that FDI is good or bad depends upon the kind of investment it is tethered with. Proper channelization of FDI in MBRT can have long lasting effects on the society ensuring food for all and at the same time generate employment assuring work for all thereby facilitating food security in India.

4. FDI POLICY IN MULTI BRAND RETAIL: LEGAL IMPLICATIONS

Law acts as a shock absorber that reduces impact of any bump that may come in the way of progress while at the same time it checks the efficacy and implication of a policy and retards acceleration of any adverse effect such introduction of policy may emanate. Influx of investment from abroad has brought in many speculations, however, it is important that we may observe the FDI policy and its repercussion in legal terms to ensure that the policy is if not 'glitch free'is at least less infested with lacuna that may have more long term benefit to the economy and less adverse effects.

The rationale with which FDI in MBRT is introduced in India can be traced in the WTO Agreement i.e., General Agreement on Trade in Services (herein after referred to as "GATS"). Two most significant commitments under GATS are National Treatment and Market Access. With reference to FDI in MBRT, market access means the ability of a foreign investor to enter the investment arena in India and the limitations that are subjected upon it. For instance, FDI in MBRT is allowed once the Government has notified the same. On the other hand national treatment implies that a foreign and a domestic retailer shall be treated at par. being a signatory to the GATS (that includes the wholesale and retailing services) had to open up retail sector to foreign participation.

With the wake of the FDI in MBRT, the RBI issued Notification dated January 9th, 2014 entitled "Foreign Direct Investment – Pricing Guidelines for FDI Instruments with Optionality Clauses"[66]. [The pre-emptive rights of call and put options are common in context of JVs and shareholder agreements, however, it possess as a grey area. Pursuant to Notification[67] dated October 3rd, 2013, the Securities Exchange Board of India permitted inclusion of the Right of First Refusal, Drag and Tag right and Call and Put options in the Article of Association. Subsequent to it the RBI drew the Notification allowing for shares and convertible debentures to have optionality clause, however, such optionalities cannot involve an assured price exit. The RBI maintained that the exit price when it comes to listed equity with such optionality is subjected to market price. But with reference to unlisted equity with optionality the exit price has to be at an Return On Equity (hereinafter ROE) based price. Therefore, the price linked to the return on equity or a price which is more than the required margin put in there in that agreement for a return on equity. This implies that when a foreign Investor invests in an Indian company if the equity is unlisted the foreign investor invests at a Discounted Cash Flow[68] based calculation or investment price and it is this investment price which will act as the 'floor'. Which means that exit would have to be such that there is an optimality involved at an ROE linked price.[69] With respect to the listed equity it is good news especially when it comes to compulsory convertible Debenture shares or compulsory

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[64] In long run the stamp system will meet the same fate as the PDS system which eventually created a plethora of middlemen who corrupted the PDS. It is recommended that instead of abolishing the PDS system, the same must be consolidated and brought directly under the Chief Minister of State and subjected to the Lokpal.

[65] AkshayaPatra Foundation is a Mid-day meal scheme organisation.

[66] RBI Notification on 'Foreign Direct Investment – Pricing Guidelines for FDI Instruments with Optionality Clauses', http://www.rbi.org.in/scripts/NotificationUser.aspx?Id=8682&Mode=0 .

[67] http://www.sebi.gov.in/cms/sebi_data/attachdocs/1380791858733.pdf

[68] Discounted Cash Flow or DCF is a method of assessing investments taking into account the expected accumulation of interest.

[69] The Notification by RBI provides that the exit price for preference shares or debentures can be done as per international pricing methodology.

convertible preference shares but the Notification adds to confusion regarding unlisted equity and needs more clarity from the RBI.[70]

Another speculation that the FDI in MBRT has brought is with respect to the extension of national treatment and the rising competition concerns among the domestic players. FDI in any form has pro-competitive benefits provided such investment is channelisedincreasing the consumer and competitor efficacy. Any action that may lead to competition distortion needs to come within the ambit of Section 3 or/and section 4 of the Competition Act, 2002. Section 3 speaks of Anti-competitive Agreement while Section 4 deals with abuse of dominant position. On one hand anti-competitive agreement also involves assessment of any policy of the Government that may lead to either horizontal or vertical agreement before its implementation and on the other abuse of dominance is used against entities once they are operational. In context of FDI in MBRT, the anti-competitive speculations are made with reference to Section 3, under the head of predatory pricing. The practice of predatory pricing implies that the Retail stores or Supermarkets would sell commodities or products at a cheaper rate so as to lure consumers destroying competition. But one must bear in mind two things while working on the hypothesis of predatory pricing. Firstly, before functioning of the FDI funded MBRTs all doubts relating to predatory pricing are nothing but speculation. Secondly, while weighing appreciable adverse effect under section 3, Section 19(3) needs to be read to determine the effect of the 'anti-competitive agreement' vis-à-vis its pro-competitive effects. The inflow of FDI in MBRT would attract accrual of benefits to the consumers, improvement in production, distribution of goods or provisions of services and promotion of technical, scientific and economic development by means of production, distribution of goods or provision of services. The introduction of the modern logistics, supply chain mechanism and enhanced back end infrastructure would result in the lesser price for the consumer, creation of broader platform for the MSMEs and agrarians; enhanced services and supply chain would result in creating competitive environment in the retail sector. This would create a dynamic and scientific structuring of the retail sector.

A suggestion in this regard, however, can be made that to strengthen the domestic retailers it is important that their infrastructure and operational activities must be regulated which in turn means providing them with loans to renovate the operations at a concessional rate for a specified period of time so that they can be strengthened to compete with the FDI funded retailers.

Lastly, FDI in MBRT along with other FDIs has again sparked the issues pertaining to Investor-State dispute. The FDI in MBRT is tad different especially since this has always been a grey area under International investment dispute resolution mechanism. It is known that every sovereign nation has the right to regulate and foreign investment so entering the country. This sovereign right however, is subjected to international regulation and treaties that the nations develop among themselves. The most significant umbrella in context of international economics is extended by World Trade Organisation, which mandates its members to adopt standards at the domestic levels in accordance with its respective agreements. Regarding investment the international regulatory framework which India is party to is the Trade Related Investment Measures (TRIMS) Agreement and mainly the BIPAs and BITs. The BITs are often perceived as the ticket to entry for the foreign investors. If a BIT has a national treatment provision then the two BIT signing countries cannot adopt a national regulation that favours domestic investor over a foreign investor. In light of this statement many have argued that the FDI policy in MBRT is a violation of BIT signed by India with many other countries. There are many examples in investment treaty arbitration wherein the cancellation or revocation of licences or permits by the host state has triggered a BIT dispute between foreign investor and the host state. For instance, in *Churchill Mining v. Indonesia*[71], a foreign investor challenged the cancellation of four mining licences by Indonesia. In *Genin v Estonia*[72], the dispute arose when The Central Bank of Estonia revoked the operating licences. This position becomes all the more pertinent in the light of present refusal of already approved FDI sanctions in Delhi and Rajasthan.[73]It is well understood that a "*large majority of India's BIT contain all the assurance of protection of*

[70] However, the notification is silent on unlisted equity.
[71]Churchill Mining PLC v. Republic of Indonesia, ICSID Case No.ARB/12/14.
[72]Alex Genin, Eastern Credit Limited, INC. & A.S. Baltoil v. Republic of Estonia, ICSID Case No.ARB/99/2.
[73] Supra Note 52.

investment to foreign investors with scant exceptions, reservations and carve out provisions"[74], this very principle was recently upheld in the case of *White Industries v. India*[75], wherein India was fined since it violated the BITs provision that allowed the Investor to enter the country.

5. FDI POLICY AND CENTRE – STATE RELATIONS

The FDI policy in MBRT clarifies that the policy is merely enabling in nature and the State Governments or Union territories are free to use their discretionary powers with respect of the policy. It can be therefore be interpreted that the FDI funded retail stores can be opened in States that have agreed or may agree in future as per the respective State or UT laws.[76]This enabling provision has opened a Pandora's Box with respect to Centre-State relations.

The CII[77], in its submission towards the discussion paper of the DIPP on FDI in MBRT, raised concerns with respect to the state intervention. They further raised the issue that giving the States power to rescind would deter investment and defeat the purpose of liberalisation. The CII stated that they were against the provision of state intervention for the purposes of the FDI in MBRT. They firmly maintained that the current regulatory framework was capable enough to deal with the consumer and employee interests both at state and central level. Rather, the CII suggested that insteadof increasing procedural and regulatory approvals and licences it would be more effective to streamline the current regulatory regime.[78]

The Centre while creating the enabling policy for FDI in MBRT understood the implication of the same and the plain reading of the policy may suggest that by giving the states with the power to approve the FDI has either played safe or ambitious. Granting the States power to approve, however, had certain other reasons too. Primarily it needs to be understood that the agricultural produce reaches the market via the APMC, which is basically run by a State Board and is therefore a State subject. The functioning of a MBRT is integrated in nature, which incorporates within its ambit various factors related to manufacturing, production, packaging, land rental, electricity consumption, public health, taxation etc. most of these are subject to the State List[79], however, only in case of movement of goods between the States does the Union list gets attracted. Since the interest of states were greatly affected by the approval of the FDI policy that the Centre decided that it must be the States to approve FDI funding in their respective retail sector. That being said, one need to appreciate the impact such delegation of power may lead to. The first impact would be terms of differences in centre and state relations, vis-à-vis to the approval of the FDI. Secondly, impact would be upon the Investors who would intent to specifically enter a particular state but owing to the complexity of approval may not enter the country at all. The third and the most crucial impact would be on the States inter se since that would lead to not just imbalance development but also would adversely affect their relations.

A major blow to the FDI in MBRT policy occurred with the recent stand taken by the Delhi Government and the Rajasthan Government thereby leading to a fix between Centre and State regarding the Centre State FDI Policy on MBRT.[80] The Delhi Government's stand on the refusal to make FDI in MBRT operational has also impeded the ambitious Amritsar Delhi Kolkata Industrial Corridor (ADKIC).

The rescinding of the approval of FDI in MBRT is also significant since it raises question on states with respect to their right to rescind a policy which the preceding Government had approved. Post the State Governments' rescinding

[74]PrabhashRanjan, 'Foreign Direct Investment in Multi Brand Retail Trading and India's Bilateral Investment Treaties', (2013) 5(1) Trade L.& Dev., 198.
[75] UNCITRAL, Final Award, 30 November 2011.
[76]Circular No 1 (2013) paragraph 6.2.16.5(viii).
[77]Confederation of Indian Industries.
[78] As proposed by CII comments on the DIPP discussion paper on FDI in Multi Brand Retail Tradinghttp://cii.in/WebCMS/Upload/Annexure%20II-%20CII%20Perspective%20on%20FDI%20(2).pdf accessed on February 4th, 2014.
[79] State list of Schedule VII of the Constitution incorporates issues such as: Public health; Agriculture; right over land; fisheries; trade and commerce within the State; production; supply and distribution of goods; markets; taxation on lands and buildings; entry of goods into the local area for consumption/ use/sale therein, use of electricity and excise on the goods manufactured or produced in the State.
[80] Supra Note 52.

the FDI, the DIPP[81] and the Ministry of Commerce and Industry clarified that the approval of the FDI policy is one-way in approach and therefore the States cannot rescind the same.

There is no doubt that retail is a state subject, however, FDI is not. With the withdrawal of approval by the States another fix had come regarding the amendment of the FEMA which is already before the Parliament for amendment.The amendment would result in addition of the list of states approving the FDI in MBRT and legalising the FDI in MBRT in *toto.* Now with the rescinding of approval another amendment will required tobe made thereby again changing the list of States approving the policy.[82] This is not just cumbersome and time consuming but also has a deterrent effect over the investors who are now sceptical about the temperament of the Indian policies and are doubtful in investing in a country that changes its attitude about a policy so frequently. Another question that follows is that whether the policy on FDI will be changed with every change in Government?

Meanwhile, the FDI policy and FEMA[83] amendments are still before the RajyaSabha, therefore, the FDI in MBRT does not enjoy a legal sanction as yet. The CAIT[84] in a press release stated that the RBI as per section 6(3)(b) of FEMA read with section 47 of the Act can make regulations and rules that may restrict, regulate or prohibit "transfer or issue of any security by a person resident outside India"[85]. The rules and regulations made by RBI to carry out the regulatory functions established by the Act shall be put before the Parliament as soon as it is made by the RBI within 30 days while Parliament is in session either in one or two or more successive sessions.[86]While the Government has passed the FEMA amendment in RajyaSabha it has not gone through the voting on the amendments proposed by the member SitaramYechury (member CPI(M)). As per the provision of the Act, if any MP raises a question, the matter has to be discussed within 60 sittings or two sessions. The FEMA amendment was passed in the Monsoon Session of the Parliament;however, the Winter Session wasn't ended *sine die*[87]. Therefore, as and when the Parliament would meet, it shall be an extension of the Winter Session and if the amendment is not passed then it will lapse. However, with the General Election hovering around the session would automatically lapse owing to the change in Government.

Answering the rescinding of approvals by the states, the Ministry of Commerce and Industry clarifies that the approval mechanism extended to the states towards FDI in MBRT is "one way" in approach, i.e., the states have the power to approve but do not have the power to rescind such as approval made. The power is so curtailed by the Centre so that the investor confidence is maintained and that the FDI so entering the country is not threatened by speculation, which would in turn affect the amount of FDI and number of Investors investing in the country.The policy for FDI in MBRT simply places the approval of the FDI in MBRT into the discretion of the States. The policy is silent about the exit option exercised by the states after they have approved the FDI scheme. The one way approach is sound from business perspective of the investors but one must bear in mind that India is a democratic State and that the will of the people is supreme. Therefore, if the will of the people indicate a shift in State's discretion over the FDI policy then such will must be respected.

Interestingly, even if the Centre disallows the states rescinding the approval so given by them previously, the states can still refuse to give licences under the Shops and Commercial Establishment Act of the respective States for setting up the FDI funded retail outlets. The Centre does not want to backtrack on their approvals since such moves by states of approving and rescinding the FDI in MBRT would create speculation among the investors making India a less attractive in terms of investment.

Relations between the States *inter se* and Regional Imbalance

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[81] Department of Industrial Policy and Promotion

[82]NayanimaBasu, 'Can Yes to FDI become a No?', Business Standard (New Delhi, February 3, 2014) http://www.business-standard.com/article/economy-policy/can-yes-to-fdi-become-a-no-114020200269_1.html> accessed on February 20, 2014.

[83]Foreign Exchange Management Act, 1999.

[84]Confederation of All India Traders.

[85] Section 6(3)(b), Foreign Exchange Management Act, 1999.

[86]Section 48, Foreign Exchange Management Act, 1999. Also see CAIT, 'Reserve Bank's authority to Amend FEMA Act to Permit retail FDI Questioned', Press release, dated November 9th, 2012 http://www.cait.in/Press%20Release%20August%20to%20September/Press%20Release%2009-11-2012.pdf> accessed on February 20th, 2014.

[87]Meaning that the session was ended without fixing a date for reconvening.

Inter-state relations and regional imbalance is another avenue that is deeply affected by the FDI in MBRT. The fact that approval of investment into MBRT is vested onto the States and the Investors so invested are mandated to procure 30% of their inputs from the local MSMEs has created a complicated situation. If one state has opened its retail sector to FDI and the JV in which the FDI is directed sources its inputs, manufactured goods, agricultural produce from another state, this would lead to a complex situation not just in matters of taxation but also for the fact that one state would be benefit in lieu of the other state, thereby adversely affecting *inter-se* relations among the states. This would further create regional imbalance, especially since

a) *One state would be profiting on expense of other:*
Where one state does not approve the FDI policy but has a large number of MSMEs while another state that has approved the policy has a huge market but less number of MSMEs, the problem would be that the Foreign retailers would procure goods from the State that has not approved of the FDI to cater the needs of the State that has approved of the FDI. This would provide revenue from the retailers to the State that has not approved the policy, which would be a wrongful gain made to the State on the cost of the State that has approved the FDI in MBRT.

b) *States would be growing asymmetrically creating out flux and influx of population leading to uneven pressure on land:*
In India, we anyways face unequal pressure on land. When the states are given power to approve FDI into their territories then the states that have allowed FDI would face higher employment generation which would lure in the population of states which have either low employment or else have not approved FDI in MBRT. This in turn would create a vortex of population movement that would in turn affect the pressure on land.

c) *It would lead to competition distortionary policies between the states:*
The states that have not allowed the FDI policy may resort to competition distortionary policy so that the States that have allowed the same may not be benefitted by the policy. One of the examples can be in case of state which has high purchasing power and has approved FDI in MBRT may fall victim to the competition distortionary policies of the state that may have high agricultural output but has not approved the policy.

Nonetheless, the policy-framers should have been more pragmatic in dealing with the states, especially bearing in mind that though the states have retail under the state list yet the aspect of FDI is a union matter and the policy must have clarified the "one way approach" in the beginning so as to remove any speculation from the minds of the states, investors and public at large. Moreover, the policy framers at Centre and state level must bear in mind that FDI in MBRT must not be used as a political card, but must be envisioned as a means of developing the sector by influx of investment thereby accelerating the pace of job creation.[88]"*The government should reconsider the decision and ensure that there is a good regulatory regime that is a good regulatory regime that can protect the small retailers. There is no reason why the consumer should be denied better quality products at lower prices.*"[89]

However, it is to be understood that India is a democracy, and the benefit and will of the people is the prime concern of the country. When the people have voted for a particular party that have disapproved of a certain policy in its manifesto then the resultant government must be allowed to rescind the approval that was previously been made by the government. It must be borne in mind that the will of the people must be taken as supreme as and when compared to the interest of the foreign investors. Therefore, the policy must be interpreted to give the states power to approve or rescind the FDI in MBRT.

6. FDI IN RETAIL: A WAY TOWARDS INNOVATION IN RETAIL SECTOR

The FDI policy in MBRT has triggered yet another question, whether the policy is a step towards an innovation in the retail sector?

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[88]SrikantaTripathy, 'State a Divided House over Raje's Decision to roll back FDI in Retail', Times of India (Jaipur) February 4th, 2014.
[89]Ibid. Quoting Pradeep S. Mehta.

FDI in retail, be it in SBRT or MBRT, is no doubt a progressive step towards the retail sector which might usher in some significant changes in the sector. The first change to be observed would be in terms of the level of competition in the market, which would be consequential to the FDI entry. The increase in the level of competition would elevate the level of quality of product and service which in turn would affect the whole shopping experience of the consumers. There is a lot of room for both the Investors as well as the retailers to learn from each other's experiences. The foreign retailers can learn to provide tailored treatment and experience to the consumers (especially because temperament of the Indian consumers is way different from that of the consumers in their domestic markets) while the indigenous retailers can learn to provide high quality products to the consumers at no extra cost. This was not possible with the advent of the domestic multi brand retailers because of the capital constraints in first place and also owing to the fact that the reach of the domestic players is restrictive in nature.

FDI in MBRT would create a systematic regulation of the market which would in turn enhance the functioning of the sector making it more structured and efficient. This is can be done by means of a creation of an independent Regulator to monitor the functioning of the retail sector[90] and also by bringing significant changes in the functioning of the respective State APMC. APMC needs to be amended since now the Commission is leaving more ground for formation and maintenance of middlemen that exploit the farmers and agrarian rather acting as their fiduciary.

7. RETAIL REGULATOR: THE CARROT AND THE STICK SITUATION

It is obvious that the retail sector and the regulations governing the same in India need to undergo a sea change. The retail sector in India is largely unregulated especially in terms of the humungous unorganised and informal sector (Image 1).The only regulation that governs the sector is the respective State laws under the Shops and Establishment Act, which does not have enough teeth to curb the ill effects prevalent in the sector. The MSMED Act, 2006 though provides for a skeletal structure for the formation and protection of the MSMEs, yet it lacks teeth to curb malpractices committed by the MSMEs. A strong regulatory mechanism is often suggested with respect to the retail sector that on one hand would stringent with quality and malpractices but at the same time would not coax business and therefore is flexible in nature. However, a question hence arises as to whether such regulatory mechanism is beneficial or not for the purposes of the sector? Whether creation of such a Regulator would add unnecessary and unwanted burden over the sector?

Business especially in case of retail must not be tightly gripped with laws and regulations since that would hamper the spontaneity with which a business is conducted and thus leading to lesser profits and more complications. This is probably one of the reasons that have not fostered the concept of a tight regulator in the retail sector. Creating a regulator and a set of strict regulation would retard the pace of growth of retail sector leading to a loss of business and time. Another factor is that creation of a Regulator would make the retail sector less elastic, the sector primarily thrives on the idea of this elasticity with which it operates making it susceptible to growth and change. Thirdly, a regulator governing retail sector if given quasi-judicial powers may bring turf war with other regulators.

However, a regulator should create a 'single window' for procuring all clearances for the purposes of establishing and maintaining a retail establishment. Such a window would organise the retail sector, thereby, generating greater revenue for the economy through sales tax and VAT. Also, creation of a regulator would lead to a positive differential treatment among the players in the market in line with the idea 'equality among equals'. A regulator would facilitate the market and thereby benefit the consumer, as well as the players by ensuring healthy competition, quality products and services to name some benefits. The government has already created certain parameters based in which the entry into the market will be allowed, therefore, concerns are often raised as to the enforceability of the norms and the missing monitoring mechanism.[91]

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[90] As proposed by CUTS comments on the DIPP discussion paper on FDI in Multi Brand Retail Tradinghttp://cuts-international.org/CUTS_Comments_on_the_DIPP_Paper_on_%20FDI_in_Multi-Brand_Retail_Trading.pdf accessed on February 4th, 2014.

[91] SuparnaKarmakar, 'Do we Need a Retail Regulator', Business Standard (December 2nd, 2011).

Hence, it stands imperative that an independent regulator must be formed to ensure that the 'single window policy' be maintained in the sector which is equipped enough to tackle with the monitoring and regulatory mechanism required in the sector. What is required therefore is a legislation that is symbiotic in nature and makes the regulation of the retail sector compatible with the modern times and at the same time does not retard the pace of the sector in general.

8. SUGGESTIONS

"*Whether the FDI is a good thing or a bad thing depends on what kind of investment is tethered*"

- Dr.AmartyaSen[92]

The FDI policy of India in terms of MBRT is a loose ended one. Especially since the policy speaks of creating an enabling provision for the FDI in MBRT and leaves to the State to decide whether or not they would allow and enforce the same.

Therefore, in this section, an attempt is made to draft a set of conditionalities, which needs to be fulfilled by the investor before entering into the market and secondly an attempt shall be made to set certain factors that the States may look while approving the FDI in MBRT. The Government has already levied certain regulatory limitations over the foreign investors, for instance:

a) Zoning regulations;
b) Investment norms;
c) Allocating more than half of the investment in the back-end infrastructure;
d) Forbidding branding of the farm produce; and
e) Mandating that 30% of the inputs be sourced from the MSMEs.

Apart from the above, following are the suggestions made with respect to conditionalities and factors to be considered by the State prior to approval.

I. <u>Conditionalities</u>

a) Pre Entry

- Ensure a scientific approach to mandate local procurement dependent upon the economic structure and output of the state. This would ensure and strengthen the position of MSME and consolidate the fact that no harm shall be made to the MSMEs due to the influx of the FDI into the economy and at the same time would foster establishment of more number of MSMEs
- Allowing a small part of the investment into the logistics connecting rural areas and remote rural areas with the nearest warehouse as a part of ensuring 'backend infrastructure'
- Entry allowed only if the Investors agree to function in JV companies for the set period of time after which the foreign players would be allowed to function on their own

b) Post Entry

- Relaxation in terms of taxes to assure FDI inflow, however, not converting India into a tax haven for FDI inflow;
- Allowing FDI through JV structure of business for a reasonable period of time that would ensure that the Indian partners have learnt the mode of business, supply chain methods and distribution mechanism, this will foster creation of more number of domestic retail players.

II. <u>Factors to be Considered by States Prior to Approval</u>

a) Approval subjected to ratio of FDI funded retail stores to the number of metropolitan areas in the state;
b) Approval in a district subject to the population vis-à-vis income distribution;
c) FDI in cash and carry for B2B operation in areas with below population 10 lakh as a qualifier to opening a store in the said area post 3 years of functioning of such establishment in the said area(s).

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[92] Supra Note 57.

9. FOREIGN INVESTMENT, MBRT AND CHANGE IN GOVERNMENT

FDI in MBRT received a serious blow with the Minister of Commerce and Industry declaring that the newly sworn Government would not be allowing FDI in MBRT. The newly constituted Mr. NarendraModiled Government in their election manifesto had already indicated that the government was not in favour of opening the sector to foreign players especially since, in their opinion,such a move would injure the interest of the small and marginal farmers and retailers. The manifesto, however, clarified that the Government would work relentlessly towards strengthening the retail infrastructure, making it more adept with time and also would inculcate policies that would bolster the present supply – chain management of the sector. However, what would be interesting to observe would be the manner in which Mr. Modi would lure in the FDI into the other sector of the country, especially after the present move and the objective ahead to resolve the agrarian crisis in the country. Once the gates to FDI in MBRT would have been opened it would have substantially aided the influx of foreign currency in other sectors as well.

With the present move, however, the Government needs to revive foreign investor interest in India and prove that India is a safe and stable destination for their investments.

10. CONCLUSION

"*Nobody has been able to stop modern and organized retail in the country and there is no evidence to suggest that their presence has threatened the existence of small street corner businesses.*"

- Pradeep S Mehta[93]

FDI policy in India is a sensitive one and there is no denial in the fact that in time it would have a great effect on all the sections of the society alike. The policy is drafted half-heartedly making the implementation a tad difficult for both the investors investing from abroad as well as the indigenous retailers. But one aspect is clear that influx of FDI into the MBRT will surely enhance shopping experience of the consumers not just in terms of competition but quality of products and the variety in terms of choice. The West perceives India as a conservative market reluctant to open its gates to funds already present abroad, therefore, image of India as an investment destination will change immensely owing to the opening of the sector.

India as a country needs to change its outlook towards Western investor, become more amiable and open to funds gushing from abroad. Simultaneously, India needs to be cautious while treading her steps and subject such influx of funds to conditionalities such that the funds stay in the economy for a substantial period of time and at the same time bring a holistic development to the retail sector.

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[93] Pradeep S. Mehta, 'War over Mart', Times of India, February 4th, 2014.

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