GATEWAY HOUSE
INDIAN COUNCIL ON GLOBAL RELATIONS

Devising an Indian policy on sanctions for Pakistan

Ambika Khanna,
Senior Researcher, International Law Studies Programme

PAPER NO. 22 | APRIL 2020

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Printed in India by Airolite Printers.

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List of Abbreviations

1. ADB: Asian Development Bank
2. BIT: Bilateral Investment Treaty
3. CAATSA: Countering America's Adversaries Through Sanctions Act
4. CBU: Completely Built Up
5. DHA: Pakistan's Defense Housing Authority
6. DSB: Dispute Settlement Board
7. EU: European Union
8. FATF: Financial Action Task Force
9. FDI: Foreign Direct Investment
10. FEMA: Foreign Exchange Management Act, 1999
11. GATT: General Agreement on Tariffs and Trade
12. GDP: Gross Domestic Product
13. ICJ: International Court of Justice
14. IMF: International Monetary Fund
15. ISI: Inter-Services Intelligence
16. IPR: Intellectual Property rights
17. JV: Joint Venture
18. MFN: Most Favoured Nation
19. MTCR: Missile Control Technology Regime
20. ODI: Overseas Direct Investment
21. OFAC: Office of Foreign Assets Control
22. OIC: Organisation of Islamic Cooperation
23. PKR: Pakistani Rupee
24. SDN: Specially Designated Nationals and Blocked Persons
25. SWIFT: Society for Worldwide Interbank Financial Telecommunications
26. TAFE: Tractors and Farm Equipment Ltd.
27. UAPA: Unlawful Activities (Prevention) Act, 1967
28. UN: United Nations
29. UNHRC: United Nations Human Rights Council
30. UNSC: United Nations Security Council
31. WTO: World Trade Organisation

Executive Summary

Sanctions have been extensively used by countries as a foreign policy tool, and by multilaterals such as the U.N. It is a means of economic warfare with the objective of coercing change in behaviour of a country, imposing restrictions or signalling power.

India as a country has been sanctioned at least twice by the US and few other countries after its nuclear tests. But it has rarely imposed sanctions on another country. A recent example of India imposing sanctions was when it withdrew the Most Favoured Nation (MFN) status granted to Pakistan after the Pulwama attack in Kashmir. Pakistan too has imposed restrictions on India, such as closing down its airspace, including for Indian VVIPs, a ban on trade with India and discontinuing postal mail, a rare measure that has commercial implications.

However, Pakistan has rarely been sanctioned, despite its having been under global scrutiny for decades particularly for supporting terror financing and harbouring terrorists including those sanctioned by the UN Security Council. The country has been placed on the precarious greylist by the Financial Action Task Force, the inter-governmental global money laundering and terrorist financing watchdog. It is expected to comply with measures that counter money laundering, terrorist financing, and proliferation financing, but has still not been blacklisted despite several warnings. The country has powerful patrons like China, and till recently, the United States.

Therefore, though Pakistan is a continuous threat to India's national security, foreign policy and economy, it has escaped being sanctioned. In the wake of the attack in Pulwama in February 2019, there are pressures on India to toughen its sanctions regime and consider imposing sanctions on Pakistan.

This paper analyses the feasibility of India imposing sanctions on Pakistan. The paper studies the increased entrenchment of the military's business interests and investments in the Pakistani economy, and how sanctions can impact them. It delves into India's current legal framework and compares the regulatory process on sanctions followed by other countries. It explores the loopholes in the extant law and gives recommendations on establishing a strong legal framework on sanctions.

More broadly, the paper also analyses the efficacy of sanctions and their impact on both, the sanctioned and the sanctioning country. This is especially critical as there are no international norms that govern unilateral sanctions. The paper suggest ways in which India can impose sanctions by controlling its own stakeholders including individuals and entities.

Finally, using India's own experience of being subjected to sanctions and the experience of other countries, this paper recommends a multi-pronged approach to sanctioning a country, rather than imposing sanctions in part or in silos. The multi-pronged strategy includes a significant role for the diplomatic community, in addition to seeking support from other nations.

1. Introduction

For the last three decades, Pakistan has, through its government agencies, the Inter-Services Intelligence (ISI), and its military wing, targeted India through terrorist activities, harbouring terrorists and supporting terrorist funding from its territory. It has largely been seen as India's problem. However, in the last year, Pakistan has been at the centre of global and multilateral scrutiny. Specifically:

a. The G20's global terror financing watchdog, the Financial Action Task Force (FATF), has placed Pakistan on its grey list[1] for adopting inadequate measures against terrorist financing and money laundering. In February 2020, the FATF gave Pakistan time until June 2020 to act on its promises to take stronger action before placing it on the organisation's blacklist. Blacklisting will lead to a block on funding from multilaterals like the International Monetary Fund (IMF) and World Bank, and capital flows from foreign businesses. This will cripple its already indebted economy.

b. On 1 May 2019, the United Nations Security Council (UNSC) 1267 Sanctions Committee designated Pakistani resident, Masood Azhar (chief of Jaish-e-Muhammed, a terror group based in Pakistan), as a terrorist, obligating Pakistan to take legal action against him under Article 25 of the UN Charter,for terror-related crimes committed, including the attacks in India: the Indian Parliament, 2001; Pathankot, 2016; Uri, 2016; and Pulwama, 2019.

c. Terrorist organisations such as Al-Qaeda and Taliban, with terror bases in Pakistan, have been designated by the UNSC under its Sanctions Resolution 1267, thus entailing targeted assets freeze, travel ban and arms embargo.

The February 2019 attack in Pulwama, Kashmir, drew military and economic retaliation by India, including a counter-attack at Balakot, withdrawal of the Most Favoured Nation (MFN) status granted to Pakistan, and imposition of 200% customs duties on products originating in, and exported from Pakistan.

A house, damaged during a gunfight between militants and security forces in the Mir Mohalla area of Tral in south Kashmir's Pulwama distrcit, on 5 March 2019. Image credit: Shutterstock

Both countries have sanctioned each other. Since India's 5 August 2019 revocation of special status granted to Kashmir under Article 370 and Article 35A of the Constitution of India, Pakistan has imposed restrictions on India, such as closing down its airspace, including for Indian VVIPs, imposing a ban on trade[2] with India and discontinuing postal mail, a rare measure that has commercial implications. Pakistan also has sanctioned Bollywood and Indian news channels.

Sanctions are used often by the West – especially by the U.S. But India has rarely used them to put pressure on other countries or foreign entities. A recent and atypical example is its restriction on imports of palm oil from Malaysia after that country's Prime Minister made unsolicited comments on India's Citizenship Amendment Act.

With Pakistan posing a threat to India's national security, foreign policy and economy, pressures are increasing for India to toughen its sanctions regime. Harish Salve, India's legal representative at the International Court of Justice (ICJ), recently mentioned using sanctions against Pakistan in the Kulbhushan Jadhav case *(India v. Pakistan[3])*. He stated that India is willing to explore the imposition of sanctions against Pakistan under the UNSC if Pakistan does not comply with the final ICJ judgement in the matter.

In response, India needs to adopt a government-wide approach to consider imposition of sanctions on Pakistan. If it decides to proceed, India needs to adopt a comprehensive legal framework that allows for time-efficient sanction decisions and orders. The U.S. provides an example. It has a structured legal framework, starting with an enabling legislation that permits a designated authority to order imposition of sanctions in defined circumstances. The designated authority then has the power to issue executive orders, targeting identified countries, sectors, entities or individuals.

This paper analyses the potential of India imposing sanctions on Pakistan, bearing in mind the impact on India itself.

2. Types of Sanctions

There is no globally accepted definition of sanctions. Sanctions are a form of economic warfare and statecraft, framed to force a change in behaviour of another state, constrain certain activities or send a signal of power or resolve.[4] Sanctions are often enforced by countries to fulfil their foreign policy strategy. But sanctions are a double-edged sword. The crux of sanctions is self-denial; the sanctioning country denies its own entities or individuals from accessing the sanctioned country's market.

The table below summarises the different levels of severity of sanctions that countries and multilaterals have issued, based on the nature of sanction (targeted or comprehensive), its scope and impact (extent of socio-economic impact and geographical territory):

Table 1: Summary of the different levels of severity of sanctions

Level 1: Low	• India's withdrawal of MFN status it granted to Pakistan • Pakistan's closing of its airspace to India • Pakistan's suspension of trade with India • U.S. sanctions on Pakistan for nuclear proliferation • U.S. sanctions on China for proliferation of Pakistan's nuclear programme
Level 2: Intermediate	• U.S. sanctions on Venezuela • EU sanctions on Russia • U.S. sanctions on Cuba • U.S. sanctions on member countries of the International Criminal Court, an international court at The Hague, for investigating actions of U.S. troops in foreign states**
Level 3: High	• U.S. secondary sanctions on Iran, North Korea and Russia • U.S. sanctions on Chinese technology companies* • U.S. laws on export control, amounting to sanctions • India's sanctions on import of palm oil from Malaysia • Sanctions against India and Pakistan for nuclear proliferation

Source: Gateway House Research

** The embargo on federal spending on Huawei and Hikvision[5] equipment was included in the National Defense Authorization Act.*
*** Sanction imposed under Section 212 of the US' Immigration and Nationality Act.*

Sanctions can be categorised in several different ways, including:

a. They can be **multilateral** or **unilateral.** Multilateral sanctions are imposed by global multilateral institutions, such as the UNSC and General Agreement on Tariffs and Trade (GATT)/World Trade Organisation (WTO), and other organisations such as the European Union, Association of South East Asian Nations or Organisation of Islamic Cooperation (OIC). Unilateral sanctions are imposed by one country on another country, foreign entities or individuals; U.S. Executive Orders, issued pursuant to the Countering America's Adversaries Through Sanctions Act (CAATSA) on Iran, Russia, and North Korea, are examples of unilateral sanctions.

b. They can be **primary** or **secondary.** Primary sanctions prohibit persons or entities in the sanctioning country from engaging with persons or entities in sanctioned country; for instance, UNSC Resolution 1737[6] of 2006 imposed sanctions on Iran for proliferation of nuclear activities. Secondary sanctions, on the other hand, prohibit third countries or their persons or entities from engaging with persons or entities from sanctioned countries; the most effective secondary sanction is CAATSA (applicable to Iran, Russia and North Korea).

c. They can also be **sectoral.** Traditionally, typical target sectors have been economic/financial, the military, travel and diplomatic. To these, another should be added: data and technology.

2.1 Data and Technology: A New Arena for Sanctions

Image credit: Shutterstock

Data and technology deserve special note because they haven't been considered a prime focus of sanctions. In recent years, though, they have become prolific parts of daily existence, including military operations and business. They provide cross-border access to markets and investment opportunities; in fact, one of the primary aims of commercial cross-border technology transfers is to gain access to foreign markets.

Technology sanctions have been in use since the 1970s by the Nuclear Suppliers Group and Missile Control Technology Regime (MTCR). The U.S. has repeatedly imposed sanctions on Pakistan to prevent nuclear technology transfer to Iran, North Korea and Libya, and on China for actively aiding the development of Pakistan's nuclear programme. In 1992, the US sanctioned Pakistan and China for missile technology transfers in violation of MTCR rules; the sanction included a two-year ban on export licenses for any MTCR-controlled items and on U.S. government contracts with Pakistan and China for any MTCR-controlled items. India too was sanctioned by the U.S. in 1998 for its test of a nuclear weapon (the sanctions are no more in effect).

Technology sanctions have moved beyond just defence technology to cyber and data technologies. The Office of Foreign Assets Control (OFAC), the primary sanctions body of the U.S. government, has created an exclusive category of Cyber Sanctions, focusing on specific harms (including compromise to critical infrastructure and massive loss of sensitive information such as trade secrets)[7] caused by significant malicious cyber-enabled activities. A recent example of technology sanctions is the bar imposed by the U.S. Department of Commerce, following the President's executive order[8], on U.S. firms from selling technology to Huawei, a Chinese entity, without government approval.

As of October 2019, eight Chinese technology companies have been sanctioned under the U.S. National Defense Authorization Act and included on the Entity List by the U.S. from trading. Inclusion in this Entity List[9] means that these entities will be subject to specific export license requirements.

China, with one of the world's largest consumer markets, has leveraged its economic strength to gain access to foreign technology. Chinese foreign investment laws require foreign business to transfer technology in order to gain entry into its market.[10] This is of particular concern to foreign countries because most Chinese companies are state-controlled and China uses the foreign technology to infringe on foreign investors' intellectual property rights (IPR). This issue is also at the centre of the on-going U.S.-China trade war. In order to curtail the intrusion by China, in 2018, the U.S. enacted the Export Control Reform Act, tightening export controls on emerging and foundational technologies to protect its technological advancement.

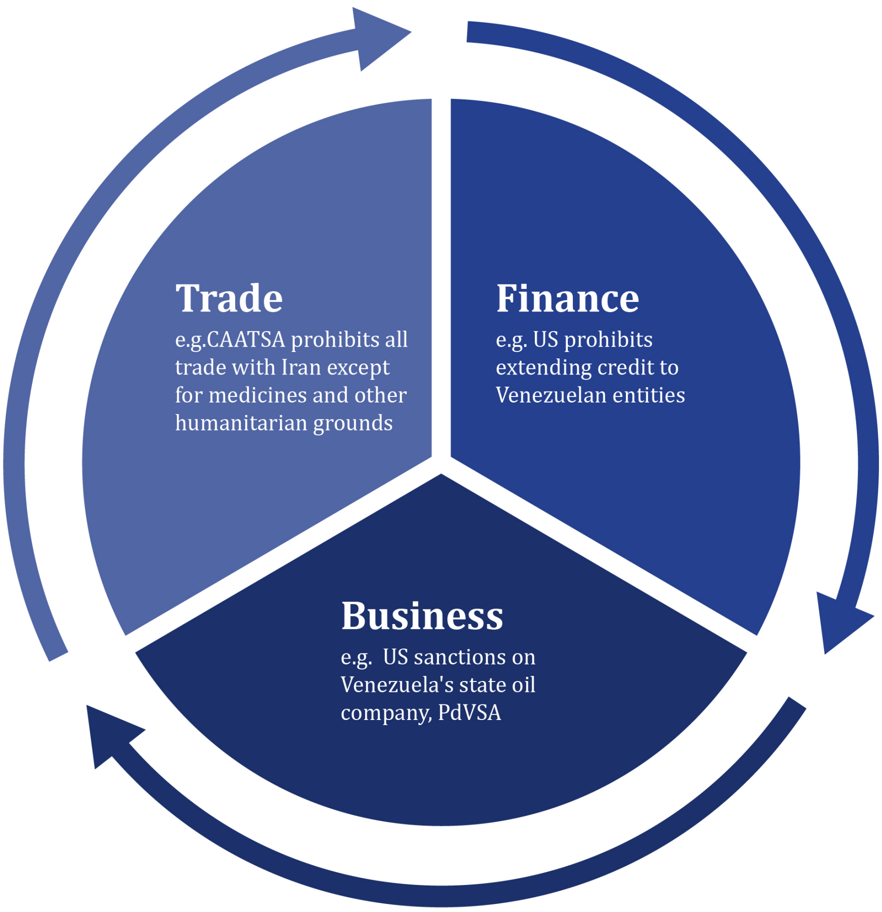
For the rest of this paper, we will limit our focus to economic and financial sanctions, referred to as economic sanctions hereafter. Economic sanctions, the most popular of sanctions, can be sub-divided as follows:

- **Trade sanctions** take the form of non-tariff barriers, embargoes on trading, imposition of tariffs. For example, CAATSA prohibits all trade with Iran except for medicines and other humanitarian goods.

- **Financial sanctions** include prohibiting the transfer of funds to a sanctioned country or entity, freezing the assets of government, corporate entities or individuals. For example, credit sanctions in Venezuela.

- **Business sanctions** can target a specific company, conglomerate or sector. An important component of business sanctions is technology sanctions, explained in this chapter. Sanctions targeting specific Venezuelan banks are an example.

Types of Economic Sanctions



Source: Gateway House Research

The above sub-classification is not exclusive, as one type of economic sanction may coincide with another.

3. The Status of Sanctions under International Law

Multilateral sanctions imposed by the UNSC and the WTO have the force of law. The Security Council applies sanctions to support peaceful transitions, deter non-constitutional changes, constrain terrorism, protect human rights and promote non-proliferation.[11] Articles 25 and 41 of the UN Charter are key provisions used for the effective implementation of sanctions; they mandate member states to implement the UNSC sanctions domestically and to execute all decisions of the UN. Article 103 further creates a binding effect by providing that UN sanctions supersede provisions of international agreements. In the event of a conflict between an India-U.S. bilateral investment treaty (BIT) and a UNSC sanctions resolution, for example, the latter would override the investment treaty. Several judicial cases such as *Libyan Arab Jamahiriya v. United Kingdom*[12] have recognised and upheld the primacy of the UNSC.

UNSC sanctions are strengthened by the subsequent imposition of unilateral sanctions by member states. For example, the EU imposed sanctions on terrorist groups such as the Al-Qaeda and Taliban after the UNSC Resolutions 1267 and 1373.

However, UNSC sanctions have constraints:

- The UN charter regulates and governs the relationships between the UN and its member states but not the relationship between individual states i.e. bilateral relationships.
- Member states do not always abide by UNSC sanctions, and the UN has limited ability to ensure implementation.
- UNSC sanctions do not create a direct obligation on companies and individuals; the legal obligation arises only when a state domestically enforces them.

At the WTO, the Dispute Settlement Body (DSB) authorises a party to a dispute to impose sanctions. When the U.S. alleged that EU subsidies granted to Airbus, an aerospace European corporation, were hurting the U.S. economy,the DSB allowed the U.S. to impose $7.5 billion in tariffs on EU goods (such as European wine and cheese) exported to the US.[13] This judgement was unusual because it allowed the imposition of counter-measures on a sector different from the one in which the claim was made.

In contrast to multilateral sanctions, the legal sanctity of unilateral sanctions is unclear, since they often apply to entities or individuals outside the sanctioning country's domestic jurisdiction. In particular, unilateral secondary sanctions (where sanctions are indirectly imposed on third countries) conflict with international law, which prohibits states from interfering in the internal affairs of other states. In the case of *US v. Nicaragua*[14], the ICJ held that *"the principle of non-intervention involves the right of every sovereign state to conduct its affairs without outside interference; though examples of trespass against this principle are not infrequent, the*

Court considers that it is part and parcel of customary international law." The ICJ upheld this non-intervention principle again in *DRC v. Uganda.*[15] In addition, the Declaration on the Inadmissibility of Intervention and Interference in the Domestic Affairs of States, adopted by the UN General Assembly in 1965,[16] prohibits a state from intervening, directly or indirectly, in the internal or external affairs of another state. These international principles weaken the legal standing of unilateral secondary sanctions.

The UN, at its General Assembly, the UN Human Rights Council (UNHRC) and through other resolutions, has repeatedly observed that unilateral sanctions violate international law.[17] In India, the Ministry of External Affairs (MEA) has stated that unilateral sanctions are inconsistent with international law, diluting the legitimacy of the UNSC sanctions regime.[18] However, India has complied with the unilateral sanctions imposed by the U.S. on Iran, after the U.S. in May 2019 withdrew the waiver it had granted to it.

International treaties, such as Article 21 of the GATT, Article 20 of the U.S.-Iran Treaty of Amity 1955, and U.S. Model BIT, contain national security exceptions that allow parties to impose sanction measures that would otherwise defy these treaties' provisions. This shows that countries have leeway to introduce sanctions that may affect issues addressed by the treaties – for example, trade.

The lack of global norms on unilateral sanctions makes them more vulnerable to challenge than multilateral sanctions. Unfortunately, there is very limited jurisprudence on this. Examples of situations where unilateral sanctions have been challenged or countered under law have been captured in **Annexure 1.**

Thus, unilateral secondary sanctions are extra-territorial in nature. For example, if India imposes sanctions on American businesses operating in the U.S., with no relation to India, for doing business with Pakistan entities, it will be considered to be outside India's jurisdiction, and hence, not in consonance with international law.

4. Efficacy of Sanctions

The effectiveness of sanctions has been a popular topic of debate for several decades given the difficulty in assessing their impact. For the purpose of this paper, effectiveness refers to the operation of the sanctions regime as intended by the imposing body or government.

Multilateral sanctions are more effective than unilateral ones since they bring unified international pressure. Still, some unilateral sanctions regimes work, and some do not. Unilateral sanctions such as the CAATSA, are working, even though they may not conform with international law. Iran's economy has been pushed into severe recession since the re-imposition of U.S. sanctions, with its currency declining significantly. This is primarily because of the control that the U.S. extends over international financial markets and trading systems, supplemented by its powerful influence with other countries. This shows that countries need to have economic heft they can leverage when they impose unilateral sanctions.

Businesses are inclined to adhere to unilateral sanctions for fear of adverse commercial consequences. In September 2019, after the U.S. imposed sanctions on Venezuela, U.S.-based Mastercard suspended services to two Venezuelan banks,[19] severely hurting the latter's operations. Not abiding with a sanctions regime can have severe consequences for businesses. For example, UniCredit SpA (a bank) was fined $1.3 billion for violating U.S. sanctions against Iran. Fifteen European banks have together paid more than $19.5 billion for violating U.S. sanctions against various countries, with the largest being an $8.97-billion penalty paid by BNP Paribas SA in 2014.[20] Recently, the U.S. also imposed sanctions on an Indian group, the Mehdi Group, for rendering maintenance services to ships that hold Iranian oil: as a consequence, it is now a designated entity on the Specially Designated Nationals And Blocked Persons (SDN) List.[21]

Countries should bear in mind that overusing sanctions can have negative effects on themselves. In particular, sanctions can:

- **promote innovation** by sanctioned countries, which must look for domestic resources to fulfil the gap that sanctions create. For example, when the U.S. stopped technology transfers to China, China pushed its own companies to fill the void. This can nullify the intended impact of sanctions by reducing dependency between countries;

- **reduce investment** in sanctioning countries. Sanctions deter foreign investors from entering sanctioning countries for fear of regulatory uncertainty. Sanctions impair cross-border mergers and acquisitions (M&As). In May 2019, Stanley Black & Decker Inc., in the process of acquiring a Chinese company, Jiangsu Guoqiang Tools Co. (GQ), imposed a condition on the latter to stop exporting to Iran;[22]

- **weaken global stability by raising prices of products and services.** For example, when the U.S. sanctioned Iran and companies procuring oil from Iran, the resulting rise in oil prices roiled the oil market. Similarly, U.S. sanctions on United Co RUSAL PLC, based in Russia, one of the world's largest aluminium producers, adversely affected the price of aluminium in global markets;

- **invite counter measures:** The U.S. has indicated that it will impose trade sanctions on France if it introduces a tax on digital services, even though that would harm multi-billion-dollar U.S. companies operating in France, including those like Google and Facebook;

- **create new opposing alliances:** Pakistan has promised Malaysia it will fill the void left because of India's move to ban palm oil imports from Malaysia in January 2020;

- **promote rival currencies and payment systems:** India had adopted a rupee account payment system as an alternative to the dollar payment system to avoid U.S. secondary sanctions. France is working on building an alternative payment system to avoid dealing with dollars. India-Russia-China are exploring an alternative to the SWIFT system. North Korea has studied the possibility of using cryptocurrencies to evade sanctions;

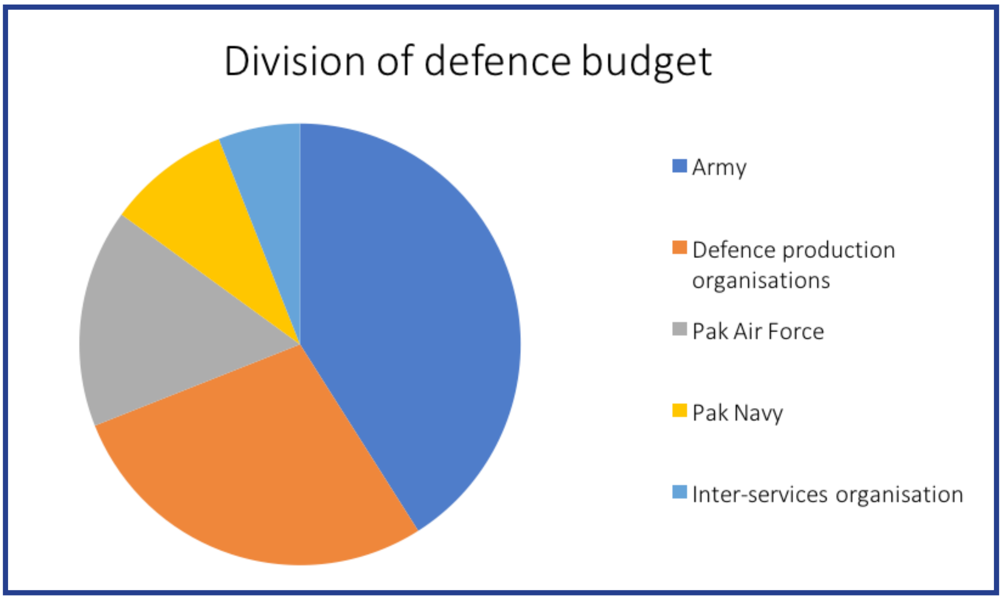
- **weaken a country's position on unilateral sanctions:** India has taken a stand globally against unilateral sanctions. But if it adopts legislation to impose unilateral sanctions on Pakistan, it will open itself to arguments it should accept unilateral sanction regimes imposed by other nations.

All these risks suggest that sanctions can come with a high cost for the countries that impose them in addition to the countries that are targeted. They also suggest that unilateral sanctions are likely to have an impact only when the sanctioning country has, at the least, moderate control over the relevant market of the sanctioned country.

5. Pakistan's Economy

Pakistan may be in a weak position to withstand sanctions, but it is attempting to insulate itself from outside pressure. Its economy is in doldrums due to high military spending, low revenues, lack of focus on development, increasing debt, and poor law and order enforcement. Pakistan's economy was estimated to grow by 3.3% in 2019 and 2.8% in 2020, with inflation rates expected to be around 12% in 2020.[23] Private consumption growth decelerated from 6.8% in FY-18 to 4.1% in FY-19 while investment contracted 8.9%. Deficits and the recent measures taken to address them have reduced development spending and increasing debts.

Over the last decade, Pakistan's military expenditures as a share of its GDP have increased from 3.4% in 2010 to 4% in 2018, higher than the average share of military spending by most countries. The country is the 20th biggest military spender in the world.[24] In contradiction to recent public announcements by its government, Pakistan has increased its military budget (including defence affairs and services, defence production, military pension and development) in 2019-2020 to PKR 1,481,779 million.



Source: Siddiqa-Agha, 2001 p.83

The budget for external debt in 2019-2020[25] has almost tripled in comparison to the last one, constituting a large part of the total budget. In spite of the FATF albatross around its neck, Pakistan's allocation for foreign economic aid has gone up 36% in comparison to 2018-2019. A specific allocation for ADB programme loans has seen a 300% increase.[26]

The table below provides a snapshot of Pakistan's increasing reliance on external aid.

Table 2: Pakistan's increasing reliance on external aid

Particulars	Budget 2018-2019 (in PKR million)	Budget 2019-2020 (in PKR million)
Saudi Arabia (Short-term) Loan	0	480,000
China SAFE Deposits	0 (actual: 275,000)	0
Budgetary Support from Friendly Countries	0	750,000
IMF Loan for Budgetary Support	0	357,450

Source: Finance Department, Government of Pakistan

Additionally, as the table shows, there is a huge difference in the budgeted and actual amount of funds provided by China SAFE deposit (loans by China's State Administration of Foreign Exchange to Pakistan). Pakistan's budget reflects that it seeks to reduce dependency on countries other than China. It has allocated funds to establish 10 design and technology labs and train Pakistani engineers in China with the objective of achieving self-reliance in areas critical to the development of Pakistan, where negligible capabilities exist. The government has committed itself to achieve self-sufficiency in defence production.[27]

Specifically on the trade front, Pakistan, like other developing countries, has been focusing on import substitution, reducing its dependence on imports, and simultaneously strengthening its export competitiveness.[28] For example, imports in the textile sector, including raw cotton, have fallen 12% over the last two years.[29] Imports of dry fruits, rubber tyres, power-generating machinery and Completely Built Up (CBU) motor cars also have declined.[30]
The table below summarises trade between India and Pakistan:

Table 3: Trade between India and Pakistan

Particulars	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
EXPORT	1,857.18	2,171.17	1,821.87	1,924.28	2,066.56
India's Total Exports	310,338.48	262,291.09	275,852.43	303,526.16	330,078.09
%Share	0.60	0.83	0.66	0.63	0.63
IMPORT	497.31	441.03	454.49	488.56	494.87
India's Total Imports	448,033.41	381,007.76	384,357.03	465,580.99	514,078.42
%Share	0.11	0.12	0.12	0.10	0.10
TOTAL TRADE	**2,354.49**	**2,612.20**	**2,276.36**	**2,412.83**	**2,561.44**
%Growth		10.95	-12.86	6.00	6.16
India's Total Trade	758,371.89	643,298.84	660,209.46	769,107.15	844,156.51
%Share	0.31	0.41	0.34	0.31	0.30

Source: Department of Commerce, Government of India; Figures in US$

India's formal exports to Pakistan include textiles and chemicals.[31] Trade between the two countries has been at a standstill since 9 August 2019, after India abrogated the special status granted to Jammu and Kashmir. Given the low volume of trade, India's role in Pakistan's economy is minimal and vice-versa. However, informal trade between India and Pakistan continues to thrive, with exports from India valued at over $4 billion.[32] The main goods involved in the informal trade are jewellery, textiles, and electronics.[33] This entrepot trade is routed through countries such as Dubai.

The largest chunk of Foreign Direct Investment (FDI) in Pakistan comes from China, whose inflow increased 45 times from 2007 to 2016,[34] and increased 94% (year over year) for July – December 2019.[35] Investments from China account for 50% of the total investments in Pakistan, reflecting an effort by Pakistan to secure itself against future economic sanctions. Investments by countries other than China, including the U.S., have dropped significantly in the last 10 years, with a 25.5% decrease in 2018, from 2017 levels.

5.1 Military's Entrenchment in Pakistan's Economy

Nevertheless, there are potential targets for sanctions in Pakistan.

For one thing, the Pakistani military is not just a fighting force, but an economic landlord, with huge business interests and negligible public accountability. This is unlike most other economies, where the military's role primarily focuses on national security and securing the territorial borders. Pakistan's Milbus,[36] short for the vast military-business empire, dominates sectors such as cement, fertilisers, food, pharmaceuticals, textiles and oil and gas. It is run by four parent entities, each of which is associated with different commands of the military: the Fauji Foundation, Shaheen Foundation, Bahria Foundation and Army Welfare Trust. Pakistan's military business as of 2017 was valued at $20 billion.[37] The following explains the degree of entrenchment of Milbus in Pakistan's economy:

- As per a 2019 report issued by the Pakistan Stock Exchange, Fauji Fertilisers, a subsidiary of Fauji Foundation, has the highest valuation amongst the listed companies on the Pakistan Stock Exchange.[38,39] It has been amongst the top 25 best performing companies on the Karachi Stock Exchange for 14 years.

- Fauji Foods, a subsidiary of Fauji Foundation, holds a large market share in the foods industry.

- Askari Bank, a subsidiary of Army Welfare Trust, reflected a profit of PKR 2 billion for the quarter ended March 2019[40] and has an AA+ rating by the Pakistan Credit Rating Agency (PACRA).[41]

Oct 2019, Pakistan, Fauji Corn Flakes by Fauji Foundation
Image credit: Shutterstock

- Askari General Insurance Co. Ltd., a subsidiary of the Army Welfare Trust, showed a profit of PKR 296 million in 2018[42] and has an AA rating by the Japan Credit Rating Agency.[43]

- Fauji Cements, a subsidiary of Fauji Foundation, is one of the largest companies in Pakistan's cement industry.

Apart from the above-mentioned four parent entities, Pakistan's Defense Housing Authority (DHA), with serving and retired military officers on its executive and governing board, runs a vast real estate empire across Pakistan. Amongst its many projects, DHA Lahore has entered into a joint venture with a leading Malaysia real estate developer, Bandar Raya Developments Berhad, for development of a township in Pakistan.[44] Pakistan's Supreme Court has, in the past, questioned the accountability of the state government over the DHA given that state funds are used to further its activities.

The beneficiaries of the profits of Milbus are the military and its serving and former officer cadre. This is explicitly mentioned in the objective statement of most Milbus companies. Due to such deep vested interests, the Pakistani public and economy continue to suffer.

Foreign businesses operating in Pakistan prefer working with the Milbus given the state's support. A few known key examples are:

- Exxon Mobil is in partnership with Army Welfare Trust.[45]
- Fauji Fertilizers Company, a leading company in Pakistan, is the outcome of a joint venture

(JV) with a Danish company, Haldor Topsoe.[46] Both companies, in a consortium with a Tanzanian company, are scheduled to build a multibillion-dollar fertilizer plant in Tanzania.
- The first overseas direct investment by Fauji Foundation was in 2008 – a 50:50 JV with a Moroccan government entity to form Pakistan MarocPhosphore SA.[47]
- Shaheen Aerotraders, a subsidiary of Shaheen Foundation, has opened an office in UAE.

Thus, driving the economic policy of Pakistan, Pakistan's military is the deep state, over and above the government machinery in Pakistan. Therefore, sanctioning Pakistan's military-economic complex would have a direct impact on the Pakistani government without causing unacceptable harm to its people.

6. India-Pakistan Treaties

India and Pakistan have not entered into many trade or commerce-related treaties, given their volatile relationship. The key agreements that govern relations between them are the Lahore Declaration 1999[48] and Simla Agreement 1972.[49] Both agreements set out the understanding and obligation of India and Pakistan to abide by the UN Charter. A strict interpretation of the two agreements suggests that India would be in breach of its commitments under them should it decide to sanction Pakistan unilaterally, However, the UN Charter does not contain a provision that explicitly prohibits coercive economic measures.

Very few Indian companies have made inroads into Pakistan. A few examples include:

- Dabur India Ltd. set up a subsidiary, Asian Consumer Care Pakistan (Pvt.) Ltd[50] in Pakistan in 2006. For FY 2019, it made a profit of PKR 10 crores[51];
- Tractors and Farm Equipment Ltd. (TAFE) India operates in Pakistan through the Pakistani company, Millat Tractors Ltd. Additionally; Millat Tractors is also an export base for Massey Ferguson's exports to Africa. TAFE India and Massey Ferguson have a 58-year old partnership;
- Raymond, a premium Indian fabric shop, set up shop in Pakistan in 2013.

7. India's Legal Framework on Sanctions

To sanction Pakistan, India will need to adopt a comprehensive regulatory framework on sanctions. Unlike the U.S., which has multiple laws that address sanctioning, India has one primary law, the Unlawful Activities (Prevention) Act, 1967 (UAPA) read with the Unlawful Activities (Prevention) Rules, 1968. The National Investigation Agency Act, 2008 is a supplementary legislation. Both these were amended recently and serve as platforms under which India has sanctioned unlawful entities, terrorist organisations, and individuals. A recent example involves four individuals – Dawood Ibrahim, Hafiz Saeed, Zakir-ur-Rahman Lakhvi, and Masood Azhar – who were designated as terrorists under the UAPA. India has also used the UAPA to implement UNSC sanctions resolutions.[52]

Following are some key sanction-related provisions under the UAPA:

Table 4: Key sanction-related provisions under the UAPA

Sanctions imposed on	Kind of sanction/ restriction/ embargo	Penalty	Authority
Unlawful association as defined under UAPA	Prohibit use of funds by the unlawful association – money, securities, credit	Maximum of three years' imprisonment + fine + recovery amount	Central government
	Notify place (house, vessel, tent) used by them	NA	Central government
	Prohibit movable articles used by them	Maximum one year imprisonment + fine	District Magistrate
	Bar on entering notified place	Maximum one year imprisonment + fine	District Magistrate
	Search and detain individual entering or seeking entry into notified place	NA	Police officer, authorised by central government
	Bar on membership or taking part in meetings or contributing or receiving or soliciting contribution	Maximum of two years' imprisonment + fine	By the Act itself
	Bar on person aiding objectives of association and in possession of firearms, explosive etc. and commits an act resulting in loss of life/ grievous injury/ damage to property	In case of death of a person: death or life imprisonment + fine In other situations, five years to life imprisonment + fine	By the Act itself
	Bar on assisting unlawful activity of an association	Maximum of seven years' imprisonment + fine	By the Act itself
Person – unlawful activity	Bar on person taking part in or committing; or advocating, abetting or advising the commission of an unlawful activity	Maximum of seven years' imprisonment + fine	By the Act itself
Terrorist act as defined under UAPA	Bar on committing terrorist act	In case of death of a person: death or life imprisonment + fine In other situations, five years to life imprisonment + fine	By the Act itself
	Bar on raising funds, directly or indirectly, for terrorist act	Five years to life imprisonment + fine	By the Act itself

Source: Gateway House Research

Other notable provisions of the UAPA are:

a. *Application:* Applies to offences committed beyond India. A person outside India shall be held liable for punishment for offences of which he is found guilty in India;

b. *Authority:* The central government is the designated authority for enforcing the law. The Counter Terrorism and Counter Radicalization Division under the Ministry of Home Affairs plays this role.[53]

c. *Tribunal:* Established on a case-by-case basis by the central government. A declaration of a terrorist or unlawful entity under the UAPA has to be confirmed by a Tribunal. This Tribunal is not a permanent establishment.

d. *Additional powers of the central government (List of nodal officers has been released by MHA):*
   - Freeze, seize or attach funds and other economic resources
   - Prohibit persons from making funds available to the designated individuals/ entities
   - Prevent entry into or transit through India

How the UAPA is different from other sanction regimes across the world:
(Annexure 2 provides the regulatory process used by different countries for imposing sanctions)

a. It follows the principles of natural justice – *audi alterem partem* – for example, under Section 4(2) of UAPA.

b. The powers of civil courts as in India's Code of Civil Procedure, are vested in the Tribunal such as for summons, evidence, witnesses.

c. It ignores the importance of intent and/or knowledge, prior to imposing liability or penalty (this is the norm across criminal laws in the world).

d. It does not hold the country itself accountable; accountability is limited to entities or individuals;

e. The power to sanction is with the central government – not with the Prime Minister's Office.

f. The imposition of banning or penalising under this Act does not need to be only an exception – as clearly stated in other laws – such as national security, war etc.

g. It limits the scope to terrorism, unlike other regimes, such as the UK, in its base legislation on Sanctions Law 2018 and Germany in its Law on Sanctions.

8. Way Forward: Sanctions that India can Impose on Pakistan

The following are a few recommendations for how India's current legal framework (the UAPA) should be shaped to serve as the lead legislation for issuing/ imposing unilateral sanctions:

a. Use the term "sanction," not declaration, and name the schedules a "Designated List," on the lines of the SDN List in the U.S. Terminology is important symbolically.

b. Designate a panel of officials from the Ministry of Home Affairs (MHA), Ministry of External Affairs (MEA), Ministry of Commerce. and National Security Council Secretariat (NSCS) to be the decision-making body. This is important to ensure the independence of the designated authority and for well-reasoned decision-making – from arms control to export control to tariff imposition.

c. Currently, the tribunal is formed on a need basis, consisting of only one sitting High Court judge, who is appointed by the central government. The appointments to the tribunal should be carried out in an unbiased manner, possibly by a Supreme Court panel.

d. Provisions regarding the reasons for sanctions such as national security, public order, and safety, should be included in the UAPA. This could be done by expanding the definition of 'unlawful activity'.

e. Set out a clear outline of the details of sanctions – what is being prohibited or restricted, on the lines of Section 235 of CAATSA.[54]

A critical question that merits serious deliberation is whether the trial process delineated under the UAPA should be eliminated in line with other sanction regimes across the world.

If India decides to impose sanctions on Pakistan, it is important that it adopt a whole-of-government approach so that all government departments – including the National Security Council, Ministry of Home Affairs, Ministry of Defence, Ministry of External Affairs, Ministry of Commerce, Ministry of Textiles, and Ministry of Electronics and Information Technology – come together to ensure that the measures are well-phased and targeted. Sanctions will not work in silos. India will have to create a comprehensive strategy, of which sanctions will be a part. Sanctions cannot replace existing measures to resolve conflict; they have to be part of the overall strategy, along with diplomacy and law enforcement. The effectiveness of sanctions will depend on diplomatic channels and adoption of similar informal means to impose sanctions.

India can explore different options to sanction Pakistan based on its ability to implement the sanctions.

8.1. Immediate

- Sanction Dabur India for investing in Pakistan. Pressure it to withdraw from Pakistan.

- Sanction TAFE, an Indian company, for partnering with Massey Fergusson, which is selling in Pakistan through Millat Tractors Ltd. Pressure it not to engage with any entity doing business in Pakistan.

- Sanction consulting firms such as KPMG, which service Milbus (by auditing for Fauji Foods, for instance) for doing business in India.

- Sanction its citizens or residents for featuring in advertisements that are projected in Pakistan. For example, Kareena Kapoor in Pakistan's Dabur advertisements.

- Amend export laws to control re-export. For example, when Sri Lanka imports electronic chips from India, it should not be allowed to re-export them to Pakistan. The U.S. has successfully enforced similar control on re-export of certain commodities under the Export Control Act.

- Sanction Indian subsidiaries of foreign companies in sectors such as e-commerce, retail, pharma, financial services, and energy (for example, Amazon, P&G, Nestle, Pepsi, Coca-Cola, Total, Colgate) from selling Pakistani or Pakistan-origin goods in India.

- Impose sanctions on Indian companies that do any business with any other entity or individual controlled or influenced by any Milbus entity. India's primary reasoning for imposing sanctions on Indian associate, subsidiary, or sister concerns of foreign entities should be that they contribute to the generation of profits of Milbus, which, in turn, uses its funds to sponsor terrorist activities and terror financing. This can be done by requiring due diligence by Indian companies before they partner with another entity. In law, this can be made a compliance measure under the Companies Act 2013.

8.2. Short-term

- Sanction Oppo, a Chinese company with significant market share in India, from setting up a manufacturing plant in Pakistan.

- Sanction Exxon Mobil's business in India until it withdraws its JV with Pakistan. Exxon has a large business interest in India.

- Further impose blanket bans on FDI and Overseas Direct Investment (ODI) to Pakistan under the Foreign Exchange Management Act (FEMA) and related regulations.

- Mandate Indian companies to make a mandatory prior disclosure under the Companies Act, 2013 when an investment is proposed to be made in or with a Pakistan entity. Penalise non-disclosure.

8.3. Long-term

- Impose blanket embargoes on Indian companies that indirectly or directly make any investment or enter into a trading activity, formal or informal, with Pakistan.

With its focus on Neighbourhood First, Act East, multipolarity and regionalism, India is nurturing its friendships and can leverage this to create a network of influence that will support the implementation of an Indian sanctions regime against Pakistan.

It is important to ensure that sanctions imposed, multilaterally or unilaterally, are in line with international humanitarian law. In the UN charter, Article 55(c) read with Article 56 clearly states the importance of following human-rights law. It is important to protect the economic, social and cultural rights of the affected sanctioned population. For this purpose, a monitoring and an evaluation process must be developed.

9. Conclusion

Sanctions are now being seen as a counter-attack to actions by other countries and non-state actors alike, legal or otherwise, that are harmful to a country. But using them creates a sense of being on a constant war footing, in contradiction to the global principles of harmony, inclusion, and development. Overuse of sanctions erodes international norms as well as multilateralism in favour of unilateralism. This suggests that before India proceeds with sanctions, it needs a strong framework to ensure that it will deliberate carefully, act wisely and design policies that will be effective.

Annexure 1

Examples: Challenge to Unilateral Sanctions

- *Iran v. USA:* In July 2018, Iran challenged the U.S. unilateral sanctions regime before the ICJ. The ICJ ordered the U.S. to list sanctions that affect imports of humanitarian goods and products and services linked to the safety of civil aviation.

- *Nicaragua v. USA:* U.S. sanctions on Nicaragua in 1985 were imposed under the International Emergency Economic Powers Act which allows the U.S. president to declare a national emergency to deal with an unusual and extraordinary threat to the national security, foreign policy, or economy of the United States. Nicaragua challenged the embargo before the ICJ.

- The Court of Justice of the EU (CJEU) was asked, on a reference from the English High Court, to rule on the compatibility of the EU sanctions on Russia with the 1994 EU-Russia partnership agreement. The CJEU held that the sanctions in question were not incompatible with that agreement, relying on an exception in Article 99(1)(d) of the EU-Russia partnership agreement, which permits a party to take measures that it considers necessary for the protection of its essential security interests, particularly *"in time of war or serious international tension constituting threat of war or in order to carry out obligations it has accepted for the purpose of maintaining peace and international security"*.

- Oleg Deripaska, a Russian billionaire, sued the U.S. Treasury over the Russia sanctions in the U.S. federal court, after he and some of his companies were sanctioned for supporting the Kremlin. In January 2019, the Treasury Department lifted sanctions on three Deripaska-connected companies.[55]

- Russia and Ukraine: The WTO Ruling of 5 April 2019 upholds Russia's ban on transit of Ukrainian goods through its territory on grounds of national security. Russia had counter-claimed under Article 21 of the GATT, which provides for exceptions, including imposition of embargoes in time of war or other emergency in international relations. [This is the first time that the WTO has ruled for a country under Article 21 of GATT.]

- U.S-Venezuela: Venezuela initiated a request for consultation[56] with the U.S. at the WTO on 28 December 2018. After the U.S.' refusal, Venezuela submitted a request for establishment of a panel on 14 March 2019

Annexure 2

Regulatory Process in Countries for Sanctions

US	Germany	UK	Australia
Base Legislation such as the International Emergency Economic Powers Act, 1977	Primary legislation is the Foreign Trade and Payments Act, 2013	Base legislation such as the Sanctions and Anti-Money Laundering Act, 2018	Base legislation such as the Autonomous Sanctions Act 2010
Executive Order Specific legislation such as CAATSA	Specific order	Specific order/ legislation such as Landsbanki Freezing Order 2008, Iran Sanctions Act	Specific legislation/ order by DFAT, Ministry of Foreign Affairs

Source: Gateway House Research

In the U.S., as seen above, the primary base legislation is the International Emergency Economic Powers Act, 1977, which gives specific power to the executive to impose sanctions. The specific legislations set out the situation in which sanctions can be imposed, the subject of sanctions, and the kind of restrictions, time period etc. Examples include the CAATSA and Venezuela Defense of Human Rights and Civil Rights Act of 2014. It is pertinent to note that sanction legislations such as the Venezuela Act of 2014 impose sanctions on U.S.-governed or -situated assets but the reason for imposing these sanctions could be completely disconnected from the U.S., such as human rights violation in the territory of Venezuela.

The UK has rarely taken the route of unilateral sanctions. It is expected that the Sanctions and Anti-Money Laundering Act, 2018, which received Royal Assent in May 2018, will be implemented. This legislation enables the UK to comply with international sanctions and impose unilateral sanctions. It clearly sets out the situations in which sanctions will be imposed: UN sanctions, international obligation, international peace and security, prevention of terrorism, human rights violations etc. Different departments are allocated the mandate to deal with sanctions depending on its type: the Department of International Trade deals with trade sanctions, the Office of Financial Sanctions Implementation is under the Home Ministry; the Treasury deals with finance sanctions, and the Home Office deals with immigration sanctions.

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