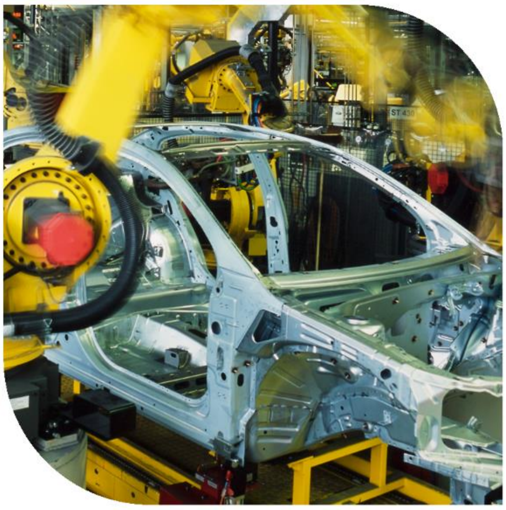
POSITION PAPER

2020 EDITION



POSITION PAPER 2020

Disclaimer

This Position Paper is a collective expression of the views of the members of the EBG Federation and its knowledge partners on key aspects of the business environment in India that affect the development of India-EU business relationships.

The views expressed in each chapter are generally in conformity with the views of EBG Federation. Information in this Position Paper is therefore intended for general guidance only. The views and recommendations put forward in this Position Paper are proposed only to stimulate discussions and offer suggestions to make Indian business environment more competitive. Whilst efforts have been made to ensure that the information contained in this Position Paper is accurate to the best of our knowledge, EBG Federation and its Knowledge Partners namely Deloitte Touche Tohmatsu India LLP, EY, Grant Thornton, JMP Advisors, KPMG in India, OPPI, PwC and TMF-Group does not assume any liability or responsibility for the outcome of any decision taken by any reader on the basis of this position paper.

The exchange rates for the purpose of conversion are based on the exchange rates prevalent in the period of October 2020.

ACKNOWLEDGEMENTS

CONTRIBUTIONS – Position Paper 2020

EBG acknowledges the support provided by Deloitte to edit and design this report for publication.

Introduction contributed by TMF-Group

Shagun Kumar, Anugraha Mundra and Kunal Gaur

Sector Papers contributed by Deloitte Touche Tohmatsu India LLP

- Chemicals & Petrochemicals – Karishma R Phatarphekar and Payal Palejwala
- FMCG – Sumeet Hemkar, Sahil Gupta and Kunal Arora
- ICT – Manoj Kumar and Thirumalesh BN
- Oil & Gas – Gokul Chaudhri, Anuj Agarwal and Tushar Aggarwal
- Power – Gokul Chaudhri, Anuj Agarwal, Gaurav Barchha and Mansi Kakkar

Sector Paper contributed by EY

- Automotive – Rajnish Gupta and Shrey Bhardwaj
- Agrochemicals – Devinder Chawla and Jiwanjot Singh
- Retail – Gaurav Karnik and Rounak Chawla
- Railway – Nikhil Mittal, Nitin A Navali, Kanchibhotla K Sravya and Rajaji Meshram

Sector Paper contributed by Grant Thornton

- Alcoholic Baverages – Prashant Mehra

Sector Paper contributed by JMP Advisors

- Banking – Jairaj Purandare

Sector Paper contributed by OPPI

- Pharmaceuticals – KG Ananthkrishnan and Nitika Garg

Sector Paper contributed by PwC

- Defence – Rajat Chowdhary and Capt Vishal Kanwar (Retd)

Sector Paper contributed by TMF-Group

- Financial Services – Anugraha Mundra and Kunal Gaur

Sector Paper contributed by The Indo Italian Chamber of Commerce and Industry (IICCI)

- Infrastructure – Cesare Saccani

Our very special thanks to all the Sector Committee chairs/co-chairs and members for their valuable time and inputs.

SPONSOR PARTNERS 2020

Our very special thanks to all our sponsor partners for making the EBG Position Paper release event a success.

Gold

Silver

Aria Hotels & Consultancy Services Pvt. Ltd

Corporate

EBG FEDERATION

An introduction to EBG Federation in India

Founded as the European Business Group (EBG) in 1997 as a joint initiative of the European Commission and the European Business Community in India, EBG has come to be recognised by the Indian Government and the European Commission as the industry advocacy group representing the interest of European companies and Indo-European Joint Ventures in India. EBG Federation was established on 11 March 2015 as a Section 8 company under the Companies Act, 2013 to ensure long-term stability and broaden its sphere of activities offering support and advocacy for European businesses in India.

EBG Federation is supported by the Delegation of the European Union to India and works towards promoting, propagating, and safeguarding European business interests in India. The EU Ambassador is our Patron.

Currently EBG Federation has Chapters in Delhi, Mumbai, and Bengaluru with approximately 170 companies as Members.

The primary objective of EBG Federation is to actively support growth in India-EU trade relations, and become the most relevant advocacy group for European business in India and ensure that the needs of European business are well presented to policy and decision makers.

Every year the EBG publishes a ‘Position Paper’ which highlights the group’s views on policy issues. The EBG Federation Position Paper is a collective expression of the views of the members of the EBG Federation and supported by knowledge partners on key aspects of the business environment in India such as Ease of Doing Business. The EBG Position Paper proposes key policy reforms that will be conducive to the growth of business and what we believe are in the realm of possibility for the Indian government to put in place.

The 2020 edition of the EBG Position Paper covers the following key sectors: Agrochemicals, Alcoholic Beverages, Automotive, Aviation, Banking, Chemicals & Petrochemicals, Defence, Energy – (Oil & Gas, Power), Financial Services, FMCG, Healthcare, ICT, Infrastructure, Logistics, Pharmaceuticals, Railway, Retail, and Telecommunications.

Message from Ms. Rekha Khanna
Chairperson, EBG Federation

Every aspect of life has been challenged globally in 2020 – including family health, business, environment, education, essentially normal life. We have had to learn to live with a new normal, discovering innovative, focused ways to continue to function, to replace the value of personal interaction with virtual, to not just survive, but thrive. Nothing has been left unscathed by COVID-19 - with the loss of lives, loss of livelihood, and struggle for survival becoming a harsh reality. However, effective action is being taken, new strategies delivered and forward momentum gradually returning. On behalf of the EBG Federation we express our humble gratitude to all members of the healthcare community that have put patient care first, even while putting their own lives at risk, to the people that continue to drive initiatives and to the people of this great country, that sustain their belief in our future, working for a better tomorrow. Thank you to each and every one!

In view of the pandemic, EBG Federation decided to postpone the launch of its prestigious Position Paper. Aligning with the times and recognising the value of the meaningful impact of the Position Paper, we have decided on a virtual launch. The EBG Position Paper presents real achievements and real issues that need to be addressed urgently to encourage a positive business environment. The original papers were prepared in the beginning of the year. With the changes taking place around us we recognised the need to take a fresh look at business reality and what it will really take to sustain business growth in difficult times. Each Sector Committee has carried out in-depth reviews to define crucial issues and actions ensuring that the perspective presented is current.

It is an honour and great pleasure to express my sincere gratitude to our Sector Committee Chairpersons, Co-Chairpersons, Members and colleagues on EBG Federation's Councils for their active support and actions. EBG has been able to sustain and build on its clear vision to be the most effective voice of European business in India through multiple impactful, virtual meetings, with key policy and decision makers ensuring that our members' issues/needs are well understood. The dialogue has been kept vibrant and interactive. This outcome driven agenda will motivate all our actions moving forward, ensuring that EBG Federation continues to deliver sustained value for its Members and support to the economy.

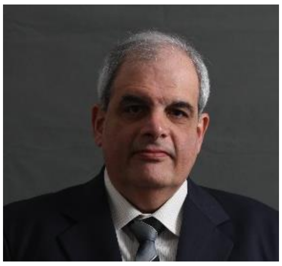
The 18th edition of the EBG Federation Position Paper highlights the breadth and depth of EBG membership and European business presence in India. It effectively showcases the crucial role that European companies play, their requirements, the path to enhance their contribution even further. The Position Paper plays a critical role, providing an effective platform for presenting our contribution and issues, generating vital discussion and laying the ground work for future action.

We believe that the new environment raises an even greater need for EBG Federation to play an increasingly pivotal role in the dialogue between European business, the authorities in India and all vested stakeholders to further develop this vibrant partnership for the benefit of all. The Position Paper is a unique expression of what is and what can be to sustain the strong link between India and the European Union as favoured business and trade partners.

We look forward to continuing meaningful dialogue and your contribution in making business growth a reality that benefits all.

Thank you and sincere regards.

Message from Mr. Kersi Hilloo
Chairman, EBG Federation, Mumbai Chapter



Once again, I am delighted to present the 18th Edition of the EBG Federation Position Paper 2020 amidst the Coronavirus pandemic which has brought to the fore the importance of digital technologies in addressing almost every aspect of the economy. India responded promptly to contain COVID-19 and the scale of response has been unprecedented.

Every year, this policy document gets more comprehensive supporting and strengthening the rapid growing relationship between the EU and India. With EU being India's largest trading and investment partner and after the recent 15th EU-India Summit, the commitment to further strengthen this partnership was reaffirmed.

India is amongst the world's fastest-growing large economies and is an important player in global economic governance with a sizable and dynamic market. Trade in goods and services between the EU and India have increased over the last decade.

There is vast potential for both the EU and India to strengthen trade, economic and investment relations. Global awareness and collaboration between the EU and India are important to drive sustainable transformation taking forward the EU-India Strategic partnership which can play a significant role in post-COVID economic reconstruction.

The primary focus in EBG Federation continues to be on 'advocacy' and strengthening the ties between India and EU companies through the Annual Position Paper which is the key instrument in the development and growth of the dedicated sectors.

Message from Mr. Raman Sidhu, FCA
CEO, EBG Federation

India, Europe and the world have in 2020, been struck by the unprecedented COVID-19 pandemic, which apart from adversely inflicting human peace, welfare, and lives, has also battered the economic theories and tools which had so far underpinned the world's economic edifice. This has left us all with legitimate apprehensions in carrying on with our normal day-to-day activities. However, responsibilities remain and tasks we must carry on and endeavour to achieve a favourable solution to our day-to-day lives. I remain an eternal optimist.

The onset of the COVID-19 pandemic brought about a delay in the launch and release of our prestigious EBG Annual Position paper in end April 2020. We then decided to have this release event delayed to 2020 year-end and more importantly before the 2021 India budget. I have great pleasure, on behalf of all our members, the EU fraternity, sector committees and technical partners in the release of our EBG Position Paper, 2020. This Position Paper encompasses the views of our practitioners in over 19 sectors of business on the current state of play, along with their views on how the government of the day can perhaps bring about further ease of doing business in all these sectors.

EBG Federation organises regular interactions with the central and select state governments. Given the current extraordinary circumstances prevalent in the aftermath of the COVID-19 pandemic, we have been organising webinars with very senior government functionaries, for our members to understand and respond, through an interactive dialogue, to the challenges posed by COVID-19 and how the government intends dealing with these. In the past, we have been addressed by various central ministers, state chief ministers, state deputy chief ministers, and other dignitaries.

This position paper clearly showcases how EU and EFTA countries and their corporates can continue to further play enhance their crucial role in India, as the biggest trading partners. EBG is committed to continue playing an important role in the India and Europe business dialogue. I express my gratitude to all our sector committee members, technical partners, and sponsors, our patron, the EU Ambassador, his team and the EEG for their supportive role in ensuring the successful completion and release of this Position Paper, 2020.

This paper showcases practical advice from our practitioner members on the further steps the Government of India and state government can take, and which are within the realm of doability to further ease doing business in India and to attract enhanced FDI into the country.

With my best wishes to all for the festive seasons.

Message from Sanjeev Varma
Chairman, EBG Federation, Bengaluru Chapter

As the chair of EBG Federation Bengaluru Chapter, it is a pleasure and honour to contribute to the Indo-European community through EBG Federation. EBG Federation Bengaluru has contributed to the ICT and Innovation paper this year, which would not have been possible without inputs from our knowledge Partners, Deloitte Touche Tohmatsu India LLP. This has been a complete team effort where representatives from various European companies came together to contribute their ideas to make it a success. This year's ICT and Innovation position paper provides insights into the IT & ITeS industry landscape, recent macro-economic developments and covers some industry issues and suggestions.

Building a common platform for European companies to come together, share ideas and network would be EBG Federation Bengaluru Chapter's priority. I look forward to the active participation and support from existing members of EBG and hope to on-board new members who share a common agenda.

Message from Rajeev Gupta
Managing Director, RDI & Sr. Advisor, EBG Federation

I have been talking about the building of a new India and my conviction of a new order being built.

No one though could see or imagine a crisis of this magnitude. Who could have ever imagined that a single calamity could bring the entire world to a halt? Who could have thought that the largest and strongest of nations, corporations, and the entire world could be brought to their knees? What one has witnessed in 2020 is like a story from some another planet. No war, no financial meltdown nor any natural calamity could have done what a single virus has done to the whole world.

However, the way India has handled the situation is quite remarkable and yet again shows India as decisive, strong and self-reliant country and as an emerging Global Power.

All world leaders, economists, financial and business wizards of this century have only thought about growth and its management in the last 100 odd years. For the first time, to my mind, we are sitting at a 15%+ reduction in world GDP. We are also looking at changed consumer behaviour, maybe changed priorities, and hence the altered spending and consumption patterns for a lot of goods and services. We are also looking at changes in Global Trade and Supply Chains. In such a situation, where one is not even aware of all the variables, where does one start, what does one do?

Businesses, governments worldwide and all others will have to Re-think, Re-align, and Re-assess. These are times when one needs real thinkers and philosophers. People who can go beyond transactional wisdom and really crystal gaze into the future and imagine what the 'New Normal' will be. Whether globalisation or localisation will be the flavour of the day? Will the uptake of technology leapfrog and will this lead to different world order? What will be the Future of Work, Education, Healthcare, Manufacturing, Supply-Chain, etc.? What policies will help in facilitating the changed world order? This is a time of immense turmoil but an opportunity for all those who can think afresh and collaborate to adopt the changes.

We at EBG Federation have been getting different stakeholders together and have done 45 webinars, till this article goes into print, to help share thoughts and ideas with some of the largest businesses of the world, the Indian government and representatives of all EU countries in India, so that while taking care of national interests we can help pave the way for the future, by leveraging the strengths available globally.

These position papers, which are a result of a series of intensive brainstorming sessions involving hundreds of man-hours of some of the best brains available in the business world, in the nineteen key sectors and representing the who's who of European businesses, is yet another attempt to draw the attention of stake holders in general, and policy makers, in particular, to the contributions made by European players in the growth journey of India and the possible corrective actions required in the policies to facilitate higher growth and participation in the future.

We are confident that a continued and closer engagement between the two sides would go a long way in creating a win-win for all and help India and Europe work together for taking a global leadership position as the world order changes and takes a new shape.

We look forward to a vibrant future and enhanced support and collaboration of stakeholders to ring in new opportunities.

Message from H.E. Mr. Ugo Astuto
Ambassador of the European Union to India

India's rapid economic growth over the last decade has made the country the fifth-largest economy by nominal GDP and the third-largest by purchasing power parity, globally. India's 1.3 billion population, its vibrant entrepreneurial traditions and growing middle class make it an attractive destination for trade and investment. On its side, the EU 27 Member States form a single market of 450 million citizens and more than 20 million businesses, making it the world's largest economy.

The EU and India enjoy a dynamic and balanced trade relationship in terms of both goods and services, with India currently enjoying a slight trade surplus. In 2019, the total value of EU-India trade in goods stood at €80 billion, accounting for 11.1% of India's overall trade in goods. The bilateral trade in services has also seen a steady increase, reaching €29.56 billion in 2018. The EU is also a leading investor in India, with an investment stock valued at €61 billion (April 2000-March 2020), and a major destination for Indian foreign investment. The EU27 in fact accounted for 22% of total FDI inflows into India in FY2019-20.

In short, there is enormous potential for both sides. Against this background, at the EU-India Summit, last July, leaders reiterated their determination to reinforce trade, investment, and economic relations.

In such a promising context, the European Business Group Federation (EBG) has an important role to play in advocating and advancing EU-wide business interests in India. Organised in different sector committees, EBG Federation has acquired an in-depth knowledge of the Indian business environment, thus making it a key voice in deepening EU-India economic cooperation. This Position Paper reflects the commitment of EBG Federation to take to a new level the EU-India business partnership.

The Indian market presents a host of major business opportunities. However, EU companies, particularly SMEs, can also face challenges when operating in such a vast and complex environment. Challenges related to difficulties in accessing the market, import duties, non-tariff barriers, the specificities of the intellectual property regime, the lack of familiarity with the regulatory regimes, including country-specific standards and procurement rules.

The EBG Federation provides a robust framework for European businesses, including SMEs, to come together and have an informed dialogue on these challenges.

In this spirit, I am sure that the recent establishment of the European Economic Group (EEG), which brings together the EBG Federation as well as the bilateral Chambers of the EU Member States, will also prove seminal.

A stronger, more coordinated approach in addressing common issues and proposing solutions through a single European business voice will undoubtedly help in unleashing the full potential of EU-India trade and investment relations

Let me therefore congratulate the EBG Federation for its work and express my continued support for the EBG Federation and the EEG.

Message from H.E. Brigitte Öppinger-Walchshofer
Ambassador of Austria to India

On behalf of the Austrian Embassy, New Delhi, I would like to express my warmest congratulations on the occasion of this year's publication of the EBG Federation's Position Paper, 2020.

Over the years, Indo–Austrian business relations have grown from strength to strength. Bilateral trade went up to almost €2 billion in 2019, with Austria importing goods worth €1,023 billion from India, and India importing Austrian goods worth €923 million, leaving a small trade surplus in favour of India. Austrian direct investment almost doubled over the past five years from €393 million in 2015 to €754 million in 2019, whereas Indian investment in Austria stood at €333 million in 2019. These steadily rising figures show the ever increasing importance of India as a trading and investment partner for Austria, with still a lot of untapped potential.

However, this upward trend stopped abruptly in 2020, a year that has proven to be challenging all around the globe, both in terms of human suffering as well sssas economic loss, which often go hand in hand. India imposed one of the strictest lockdowns in the world that went a long way in tackling the health hazard. Likewise, Austria had to go into crisis-mode for several months. However, after weeks of lockdown to curb the tide of the pandemic, Austria has the situation firmly under control and almost all businesses have been able to start trading again, while observing appropriate safety measures. Leading the international field with a state-aid package of more than €50 billion, the Austrian government has opted for a package of support mechanisms to mitigate the economic consequences of the pandemic for companies and for employment. The point of all these relief efforts has always been to enable the economy to bounce back quickly; however, the export industry will only be able to get back on its feet with a greater degree of trust based on intensive global cooperation than ever before, with fairness, openness, and partnership at the top of the agenda. But also, the Indian economy is gaining momentum, thanks to the relentless efforts of the Indian government and the entrepreneurial spirit of its population.

One of the most recent success stories in these times of crisis is of international technology group, ANDRITZ, which received a contract to supply the electro-mechanical equipment for the Kutehr hydroelectric plant (240 MW) located on River Ravi in Chamba, Himachal Pradesh. The plant will generate approximately 955 GWh of electric power, thus supplying clean and renewable energy to around 4.6 million households.

As another sign of trust in the Indian economy, the local subsidiary of Getzner has agreed to head the newly founded Railway Chapter of the EBG Federation, which is currently working on a strategy paper. Austria is a "railway country" with a long tradition and expertise, which is also reflected in multitudes of Austrian companies in this sector in India.

These are just two of the most recent examples of more than 150 Austrian branch enterprises and joint ventures in India, which typically operate in high-end market niches. In addition to its bilateral agenda, Austria also focuses on the joint development of the European Union's multilateral economic relations with India.

Once again, the present Position Paper, as a collective expression on India's business environment, is a valuable tool to foster international trade relations. Austrian companies know that they can rely on the EBG Federation and therefore extend support to the annual Position Paper, 2020.

Message from H.E. Mr. François Delhaye
Ambassador of the Kingdom of Belgium to India

As 2020 draws near to its conclusion, we can already say that it has been a difficult and highly unusual year. The outbreak of COVID-19 brought about a crisis of global proportions unlike any other we have faced in recent history. The European Union (EU) and Europe, like the rest of the world, were obligated to largely shift their focus away from existing priorities to tackling the crisis at hand. At this point, it's still too early to draw conclusions about the ultimate impact the pandemic will have on European and global trade.

When we analyse the bilateral trade relations between Belgium and India in 2019, we can see that there has been a decline. Unsurprisingly, this persisted in the first half of 2020. This can largely be contributed to a decline in trade in the diamond sector which has historically been dominating trade relations between both countries. Nevertheless, it is important to note that, despite these recent trends, Belgium has maintained its position in the top 5 of EU importers and exporters of goods from and to India. The economic ties between both nations have remained strong and they provide a solid foundation for further enhancement.

Looking back at the beginning of this year, we must also mention another major change for the EU with the decision of the United Kingdom to leave the Union. It is still difficult to predict what the impact of "Brexit" will be, but the consequences will undoubtedly be far-reaching. Belgium, as a founding member of the EU, remains convinced that the EU must, for the benefit and well-being of its citizens, continue on its path of further European cooperation and integration.

Faced with such challenges, it is easy to forget that every cloud has a silver lining. I would therefore, also like to highlight some positive takeaways from these unusual times.

First of all, it had long become obvious that we must aim for more sustainable and reliable trade practices and structures. Never has this been clearer than during the current global health crisis. We can seize the momentum this crisis has created to accelerate our transition to a more sustainable future, which is the only way forward. I am convinced that close cooperation and a strong partnership between the EU and India can be central to this transition.

Building on the first point, I would like to mention the 15^{th} EU-India Summit as another positive takeaway. Even though the summit was held virtually, it did not hamper the further deepening and strengthening of relations between both partners. On the contrary, this summit has shown that there clearly is a willingness to further enhance this partnership in support of sustainable modernisation and to boost cooperation.

The issue of Brexit, the impact of COVID-19, crisis and changing geopolitical realities, can also push both Belgium and India to look beyond diamonds in their bilateral trade. There is an acknowledgement between both countries for the need of diversification of their trade flows. Promising sectors include pharmaceuticals, textiles, biotechnology, ICT, ports, dredging, construction, railways, electronics, food processing, chemicals, renewable energy and clean tech. These promising sectors offer ample potential to curb the current trend of declining trade relations and pivot it to usher in renewed growth.

Last but not least, I would like to thank the European Business Group Federation (EBG) for its continued commitment to offer support and collective representation to European businesses in India, as well as its effort to actively support growth in Indo-European relations.

Message from H.E. Ms. Eleonora Dimitrova
Ambassador of Bulgaria to India

India is a natural partner of EU in Asia as they are the world's largest democracies and two of the world's biggest economies. At the same time EU/Bulgaria and India share the same values as freedom, equality, tolerance and the rule of law.

Bulgaria, member of EU since 2007, regards India, which is a large manufacturer and a growing overseas investor, as a strategic partner in Asia. Bulgaria's potential as part of the vast EU market and India's outstanding economic achievements create favorable conditions for strengthening our economic relations.

My country has all the key elements needed to make business and investment projects successful: financial and macroeconomic stability, favorable tax regime, highly-skilled professionals, as well as the lowest operational costs in the EU.

For the past several years Bulgaria's GDP growth rates have remained above the EU average. Bulgaria applies some of the lowest taxes in the EU, including 10% corporate tax and 0% corporate tax for investments in municipalities with unemployment rate higher than the country's average.

The Embassy of Bulgaria in India fully supports the bilateral trade and investment relations between India and EU/Bulgaria. In this regard I would like to welcome the EBG Position Paper, 2020 as a commendable and well-anticipated act of good will to facilitate even more, the economic relations between EU and India. In the complex and fast-changing world of contemporary business and the economic challenges all over the world due to COVID-19, I feel this is really the need of the hour.

Message from H.E. Mr. Agis Loizou
High Commissioner of the Republic of Cyprus to India

I am pleased to sincerely felicitate the EBG Federation for the release of the 2020 edition of its Position Paper, which reflects the Federation's commitment and hard work in further strengthening the interests of EU businesses in India.

In addition to being a very useful reference tool to understand and identify the challenges faced by the EU businesses in India, the Position Paper enables the business community to be acquainted with the solutions to that end.

I would like to particularly commend the various sectoral committees of the Federation, which contribute to a great extent towards bringing together the businessmen of the same industry for the purposes of sharing information and addressing the challenges they face.

Cyprus and India historically enjoy very close bilateral relations as well as cooperation in various international fora. As for the economic ties, both Cyprus and India are keen to work together to further enhance them to their mutual benefits. Imports and exports from/to India increased substantially in the year 2019, as compared to the previous year. In terms of investment, Cyprus stands as the eighth-largest source of FDI in India.

Given that India has been an important partner for the EU, and the fact that Europe continues to be a desired destination for the Indian business community, both sides positively look forward to further engage in reinforcing their wide-ranging relations, even when the coronavirus pandemic poses big challenges to this end.

Message from H.E. Mr. Milan Hovorka
Ambassador Extraordinary and Plenipotentiary of the Czech Republic to India

The 2020 coronavirus pandemic brought about an unprecedented challenge in every sense: human, social, and economic. Our collective struggle to protect health and lives has hit the global economy and resulted in a slowdown of economic performance, loss of jobs, and significantly reduced trade flows. One could conclude with resentment and apprehension that it looks as if what we have been building for so many years has the tendency to crumble.

However, this crisis, like any other, is not just about the threats. It is also about the opportunities. It is about our capacity to adjust, do things differently, and conduct business in a more environment-friendly manner. From this perspective, I have no doubt that we will overcome even this difficult moment of our history and emerge substantially strengthened and more resilient to meet various challenges in the future.

The Embassy of the Czech Republic in Delhi has not given up even a moment. On the contrary, it has the ambition to be a part of the cooperative actions to resume the economic recovery by increasing awareness of existing trade and investment opportunities, organizing plenty of networking events, and bringing people together, even virtually.

In its efforts, the Embassy is proud to be able to tie-up with various partners representing both government and non-government sectors to make the common vision of strengthening relations between the European Union, of which the Czech Republic is a proud member, and India, a reality.

The European Business Group Federation is such a great partner, and has proven its qualities in these trying times by repeatedly and tirelessly raising its voice in favour of building even stronger bridges between the European Union and India and reminding us all that international partnerships and cooperation are more important in today's globalised but increasingly vulnerable world than ever.

The EBG Federation has been instrumental in organising a number of interactions with ministers and high-ranking officials to help European partners understand better what the Indian authorities both, at the central and states levels, are doing to contain the pandemic, and to explore possibilities of working together. It has been equally active in creating various platforms to promote positive business and personal ties between European and Indian corporates. I can't but mention also the EBG Federation's commitment to free and rules-based trade and investment relations and its endeavors to find a way of dealing with difficulties faced by European companies present in the Indian market or willing to explore its potential.

Finally, I would like to express my gratitude to the entire team of the EBG Federation and all others who have contributed for producing yet another excellent document. I trust that the 2020 EBG Federation Position Paper will help generate better understanding of what Europeans and Indians could and should do together.

Message from H.E. Mr. Freddy Svane
Ambassador of Denmark to India

On behalf of the embassy of Denmark, I would like to record my appreciation for the work done by the EBG Federation in compiling the 2020 position paper. This document provides valuable information on all the sectors in which European companies are involved in India. It also provides a useful guide to some of their challenges and therefore forms a basis for constructive engagement between European businesses and the Government of India. Finally, the document provides a comprehensive guide to, and promotion of, the very extensive partnership that now exists between India and European business interests.

In the year following my arrival in September 2019 for my second term as Danish ambassador to India, I have been amazed at the changes that have taken place in the Indian economy since the end of my first term in 2015.

Through extensive structural reforms, India has climbed from 142 to 63 in the World Bank ease of doing business index. This increase of 79 places is an extraordinary achievement.

Today there are more than 100 Danish companies present in India. Between them, they employ over 200,000 people directly and provide livelihoods for many many more. This means that, outside Denmark itself, India is home to one of the largest numbers of people employed by Danish companies. These companies are involved in a wide range of activities. All of these are active partners to India's development programmes and include new and renewable energy, water and the environment, logistics solutions, health, ICT, fashion, not to mention, of course probably the best beer in the world.

In contrast to my first tenure, when I now engage with Danish companies, I see a significant change in the way they face the challenges that any industry must address. There is a strong proactive approach from the Government of India to tackle such issues, and to further ease the conditions for foreign-owned companies in India.

Denmark has been an enthusiastic partner of India since independence. We have supported India's development in many ways. In particular, the spearheading of the white revolution in the 1960s and 70s which made India a milk surplus country for the first time. Today, we are together focused upon creating a greener tomorrow.

Denmark is building a green strategic partnership with India. Denmark will work along with India to address climate change through the reduction of CO2 emissions, while at the same time meet the challenges of accelerating urbanisation. This means, balancing the need for infrastructural improvements with smart and sustainable energy solutions, through the development of a sustainable environmental policy. This cannot be done without the active involvement of industry and I am therefore very pleased to see how deeply involved Danish companies in India are in the green transformation. Danish solutions in the wind, bio energy and water, and logistics industries are in high demand and I am positive that they will contribute significantly to the successful achievement of our joint objectives in this area.

A robust engagement between the government and industry is essential for the successful development of policy initiatives and the successful implementation thereof. The EBG Federation is a vital medium for facilitation of the dialogue between government and industry. I applaud the work that EBG Federation does in this regard. I encourage leaders on both sides of the discussion to bend their every effort to enhancing this process. Without it, we will not secure the competitive high ground that is so essential to the development of India's economy.

With so many European and Danish companies now active in India, it is vital that we continuously address the framework conditions for doing business in this extraordinary country. Without this activity, in which as I say the EBG Federation must play a leading role, especially now in this COVID-19 affected world, we will not be able to further advance from last year's improvements. Nor will we be able to attract the FDI and create the employment needed for India to exploit its demographic advantages to drive economic growth.

The rest of this year and I dare say, next year too, will be overshadowed by the huge economic damage wrought by the pandemic. In such a world, economic cooperation must be the watchword. EBG Federation must play a central role in the facilitation of such cooperation. Without it, the support that Europe and European companies wish to give to their Indian partners in driving a green economic recovery will be diminished. On the other hand, if it can be provided, then I feel very confident that the collaboration that will ensue will enable India to swiftly regain the requisite economic momentum and positive development.

I commend the activities of the EBG Federation and the position paper as a constructive basis for economic cooperation and ultimate success.

Message from H.E. Ms. Katrin Kivi
Ambassador of Estonia to India

As one of the world's large economies and the largest, free-internet market, India is naturally of growing interest to the Estonian business community. Our bilateral trade has been dominated by trade in paper pulp and mineral oils, machinery, and appliances. However, in recent years, digital services and smart solutions have gained importance. This trend has been brought about by the wide use of smartphones in India and the global digital transformation. We see growing interest in doing business in the fields of cyber security, biotechnology, education technology, e-health, e-governance, smart city solutions, and other sectors of the new economy.

The COVID-19 pandemic that hit us all in 2020 has accelerated the movement towards digital tools and services around the world. These solutions have allowed people to cope with restrictions on movement and gathering in times of crisis, and provided platforms for communication and exchange of information. Thanks to the digital solutions, we can conveniently continue learning, consult our doctors, and share sensitive data securely without leaving our homes. The shift to digital has allowed greater efficiency, benefited the environment, and it continues to save our time. Digitalisation has been Estonia's focus for more than two decades and for our businesses, offers a tremendous opportunity to collaborate, as the digital life becomes the norm across the globe.

Estonia, as a country with a small public service, highly appreciates the support from the EBG Federation in India. As a proud member of the EU, we are glad that all the Member States are represented in India so that we can share experiences and learn from each other.

I would like to thank the EBG Federation for their overall support for the Embassy and Estonian businesses. We have shared excellent cooperation with the EBG Federation also during the difficult times that 2020 has brought along by taking part in online events organised by EBG Federation and receiving EBG Federation at ours.

The annually released EBG Federation Position Paper has served as a comprehensive and practical guide that has provided great insights to our teams at the Embassy and in the capital, and to our companies.

I would like to express my sincere gratitude to the EBG Federation and congratulate them on the release of the 2020 edition of the Position Paper.

Message from H.E. Ms. Ritva Koukku-Ronde
Ambassador of Finland to India

European companies operating in and to India have this year, faced a situation, which is new and unchartered due to COVID-19. As a part of the European Business Family, also the industries, enterprises, and entrepreneurs from Finland have been in a similar position with their European counterparts, where first, the pandemic itself, followed by strict lockdown and restrictions and eventually a severe economic downturn have led to a serious disruption on demand, supply, manufacturing, and logistics.

We are still battling the disease as a national and global priority; however, countries all over the world are simultaneously searching for ways to support their companies, revive their economies, and update their policies towards more competitive and yet more resilient standing in the New Normal. As a part of the extensive stimulus packages for example within the EU and its Member States, we have witnessed a wide consensus towards the Cleaner and Greener World utilising this additional financial support for developing new technologies and solutions. Unfortunately, the crisis also led to increased protectionism and trade barriers in various markets.

Luckily, with the help and support from the Indian administration – both Centre and states – we have managed to sort out most of the issues our companies have been facing during the recent months. Cooperation among the EU Members, with the European Commission and External Action Service, and with other like-minded partners, have also proved to be beneficial and effective, while resolving any of the challenges affecting our businesses. Industry associations such as Finland Chamber of Commerce in India (FINCHAM India) and other bilateral chambers, European Business Group Federation (EBG), and informal platforms such as the European Economic Group (EEG) have been equally efficient in their advocacy work and drive to ensure that the interest of the European companies in India are well looked after and taken forward for the policy makers.

Key elements in facilitating sustainable trade and investment cooperation and enhancing economic growth are trust, predictability, and a stable business environment. In this regard, an Investment Protection Treaty between EU and India would be an important element. Furthermore, constant and constructive dialogue bilaterally, between EU and India and within multilateral platforms, especially at the WTO.

At the EU-India Summit mid-July, a High-Level Dialogue was established to deal with Trade and Investment, as well as economy and industry-related topics. This type of dialogue can – if fully utilised – eventually also facilitate the way towards achieving an ambitious and comprehensive EU-India Free Trade and Investment Protection Agreement. Finland is committed and keen on developing trade and investment and commercial and industry cooperation with India based on mutual interests, shared principles and views on sustainability and responsibility. This includes joint and multilateral approach, bilateral relations, and industry- and company-specific actions. While general trade liberalisation and removal of trade barriers with enhanced investment protection are always at the core of our policy work in India, we are also focusing on technology and innovation, skills and education and science, and aiming towards ambitious and binding climate and environmental targets.

With that in mind, there is an enormous potential for increased Finland-India and the EU-India collaboration. EBG Federation has been one the key facilitators of that interaction here in India, and with the support from us all, can remain so also in the future!

Message from H.E. Walter J. Lindner
Ambassador of Germany to India

Dear readers,

The year 2020 has certainly not been a walk in the park: with what will probably be known as the biggest global pandemic of the 21st century, countries big and small are struggling to save lives and livelihoods – Germany and India are no exception here. While the search for a cure in the form of a vaccine is still on, governments are ropewalking to keep the rising number of cases in check, while at the same time allowing for economic activities to resume. The COVID-19 crisis has already changed the nature of our business relations; webinars and virtual conferences are replacing business trips and meetings in a time when international air travel is still heavily restricted.

But the crisis has also shown us the stability of long-term partnerships and trade relations; many German and other European companies in India have offered help to their local communities, by building hospital infrastructure, supplying protective equipment, and nutrition packages. They have gradually retrieved their production levels despite sometimes challenging supply situations. They are now hoping for resuming consumer demand and are building more resilient supply chains. Their commitment and contributions to EU-India trade relations cannot be valued highly enough.

Despite the ongoing crisis and severe economic consequences, which can already be felt in some parts of the world, the trade relations between Europe and India are still strong: Ahead of China and the United States, the EU is India's largest trading partner with trade amounting to €125 billion. The EU's share in foreign investment inflows to India more than doubled from 8% to 18% in the last decade, making the EU the first foreign investor in India. All of these signs give us hope that as strong trading partners, EU and India will be able to weather the economic storm. However, we should not forget that some bumps in the road still remain: both sides would profit from a renewed effort to find an agreement on investment protection and free trade rules, giving investors and businesses the stable regulatory framework and legal certainty which is now needed more than ever.

This is where the long-term commitment to EU-India trade relations, which lies at the heart of the EBG's activities, plays a key role. Their engagement with Indian policymakers, creating visibility for European business interests and promoting mutually beneficial arrangements will ensure a thriving partnership between EU and India, also in the future. I congratulate the EBG Federation for issuing its 22nd Annual Position Paper and wish the EBG Federation and its members all the success for the years to come.

Message from H.E. Mr. Gyula Pethő
Ambassador of Hungary to India

On behalf of the Embassy of Hungary, I would like to congratulate EBG Federation on the release of the 2020 edition of the EBG Federation Position Paper. As in every year, this important document showcases how the largest democracy, India, can join hands with Europe. In the recent years, India has emerged as the next global powerhouse, and now is at the forefront of global growth in ever-changing international trends, even ahead of China. Equally, our region, the Central European countries – amongst them Hungary - are the engines of Europe, contributing to a large extent to the growth of the old continent. We are aware that India is increasingly focusing on Central Europe as Indian companies realise that this is a very cost-effective way to enter the EU market.

2019 has been an eventful year for India. The government renewed its mandate in the elections, their commitment may be the key of the renewed economic growth that can be supported by Hungarian know-how. As a result of the government's efforts, India has made significant progress to change the business environment. The "Make in India" initiative and the programme of strengthening the Indian SMEs provides opportunities for our companies to take part in the success story of India.

Hungary has a lot to offer for the challenges India faces in the upcoming decade. The needs of the burgeoning population of the cities, the aspirations of the new emerging middle class, the imperative of new job opportunities, the alarmingly high level of pollution in the big cities, and the challenges of water supply - all call for immediate solutions Hungary can readily offer. Hungary has a very long history of frugal engineering, of leveraging a highly skilled workforce and - most importantly - of innovation in many fields (engineering, water management, renewable energy, smart cities, agriculture, food processing, etc.).

India and Hungary have had a long history of cooperation. Many large Indian corporates have a strong presence in Hungary. Tata Consultancy Services, for example, has a large delivery centre in Budapest, employing close to 2500 associates and serving their clients in 29 languages. The latest years' additions are Apollo Tyres' first greenfield investment outside of India and the Sumi Motherson group is planning to build now their sixth brand new factory in a row in Hungary. Indian companies are constantly looking for business opportunities and expanding their portfolio in Hungary, so we have ongoing new investments, like UFLEX and SRF. Likewise, some Hungarian companies have also gained foothold in India, for example the pharmaceutical producer Gedeon Richter, which has a factory in Vapi, Gujarat, in cooperation with an excellent local partner, and Logipix that supplies innovative video surveillance solutions for security and logistics for airports and public spaces.

I would like to thank EBG Federation again for its efforts in fostering European-Indian business relations and congratulate them on playing their important role in improving the Indian business landscape. It is a very important task to collect opinions from our European companies and channel their views and comments to the appropriate Indian parties. The position paper is a great contribution to articulate European views about the Indian business climate.

Message from H.E. Mr. Gudmundur Arni Stefansson
Ambassador of Iceland to India

The economic engagement between Iceland and India continue to expand adding new areas of cooperation. President Ram Nath Kovind's visit to Iceland in September 2019 with a business delegation has added more impetus to the growing politico-economic relations between the two nations.

In a recent visit to India to deliver a lecture on the Arctic at the Indian Council of World Affairs, Mr. Olafur Ragnar Grimsson, Former President of Iceland and Chairman of Arctic Circle highlighted the importance of India's engagement in the changing Arctic. India is one of the Observer States in the Arctic Council and a more active participation from India would benefit the Arctic region and the world.

The Indo Icelandic Business Association (IIBA) has been actively collaborating with the Embassy in facilitating and promoting cultural, trade, and investment between the two nations. Membership to the Association are opened to individuals and business houses that are interested in furthering trade and investment between Iceland and India.

Iceland has been leading the Global Gender Equality Index of the World Economic Forum for over a decade now and this is one important area that Iceland can share its experience and expertise with India. The business communities of the two nations have already initiated cooperation in this area with the visit of FICCI-FLO delegation to Iceland in 2015. A MoU between FICCI-FLO and the Association of Women Business Leaders in Iceland (FKA) was signed during the visit. This was followed by the Women Economic Forum conference organised by Indian based All Ladies League (ALL) in Iceland. These connections can lead to more cooperation in the future. The Gender Equality Studies and Training Programme of the UNESCO that is hosted in Reykjavík by the Government of Iceland is open to participation of professionals from all over the world, including India.

A broad-based Free Trade Agreement is being negotiated between India and the European Free Trade Association (EFTA) of which, Iceland is a member. The trade agreement, when concluded, will serve as a catalyst for increased bilateral trade and investment between Iceland and India.

I wish to congratulate the European Business Group Federation (EBG) on the forthcoming release of its EBG Federation Position Paper, 2020. We are appreciative of the important role that EBG Federation plays in building bridges between European and Indian businesses.

Message from H.E. Brendan Ward
Ambassador of Ireland to India

In recent years, trade and investment links between the European Union and India have seen steady growth. The COVID-19 crisis has had an impact, as it has on every sector of international economic activity. However, it can reasonably be expected that the global rebound will see further and faster growth in our economic links.

The work of the EBG Federation in facilitating and promoting this growth will be more important than ever. The Position Paper provides very useful information on relevant industrial sectors as well as other information of value to the business community.

At the government level, the stalling of economic activity this year makes it very clear that a comprehensive Free Trade Agreement between India and the European Union would be in both our interests. The EU is eager to conclude such an agreement and hopes that this enthusiasm will be shared by India as the economy here returns to the path of rapid growth.

Ireland has been an economic partner of India for many years with very substantial growth occurring in the past five years. Ireland has seen increases in our national trade in recent years, both in goods and in the very important services sector. The total volume of trade in goods and services was approaching $5 billion in 2019. Naturally this year will see a drop, but we are confident that 2020 will see a revival and further expansion. In 2020 we shall also be opening Ireland House, Mumbai. This location will house the Consulate General of Ireland; the Trade Agency, Enterprise Ireland, and our Investment Agency, IDA Ireland. It will be a one-stop shop for individuals and companies wishing to do business with Ireland. It is also a strong symbol of our confidence in the future of the Indian economy right in the heart of India’s business capital.

We are confident that in the years ahead, we shall have the support of the EBG Federation in all our efforts and we look forward to further useful research efforts and publications.

Message from H.E. MR Vincenzo de Luca
Ambassador of Italy to India

I would like to congratulate the EBG Federation on the release of the 2020 edition of its noteworthy and iconic position paper, a very useful tool that for over 20 years has been providing the local European business community with an in-depth, multi-sectorial analysis of the challenges and opportunities of establishing a business in India; providing key-insights to EU entrepreneurs wishing to explore or further consolidate their presence on a complex, yet very promising and rewarding market.

Notwithstanding the current global uncertainty stemming from the COVID-19 pandemic, which has caused a physiological contraction of the economic activity, the Indian growth story remains a success. Over the last decade, India has been growing at a fast pace, becoming the third-largest economy by GDP (PPP) and the third-largest start-up ecosystem in the world. With an average age of 29, its 1.3 billion population is the second largest in the world after China (with the overtake due in 2024) and represents an immense and largely untapped market, characterised by an emerging “aspirational” middle class - often tech-savvy, “connected” and informed about the latest global trends, thanks to the pervasive mobile internet, and by a skilled and relatively low-cost workforce.

For these reasons, echoing the Italian Minister of Foreign Affairs, Luigi Di Maio, who, during the first High Level Dialogue on Economic Relations, recently invited Italian investors to “bet on India”, I too, am encouraging on every occasion, Italian companies to come to India and explore its immense potential. The suggestion for them is to focus in particular on those key priority areas, such as energy transition, green economy, and sustainable infrastructure that not only are pivotal for the Italian government but are also at the core of the EU-India cooperation.

This invitation has certainly not fallen on deaf hears and has been hugely welcomed. In the period 2016-2019, Indo-Italian bilateral trade increased by a whopping 21.90%. Over 600 Italian companies are already present in India, employing over 52,000 people. These figures are encouraging, and I am sure that they are going to further increase in the coming years, thanks to the positive momentum of bilateral relations marked by the multiplication of political visits at the highest level.

It is in the interest of the Italian industry to look at India because of the emerging need of diversifying our export destinations and partially restructuring global value chains. Such a need is shared by the European business community as a whole. That is why it is all the more important for European companies in India to come together, act together, and speak with one voice. And that is why it is even more commendable for EBG Federation to put together this important position paper and to continue to play a crucial advocacy role vis-a’-vis Indian regulators to overcome the remaining difficulties impeding the European business to deploy its full potential in India. Together the EU business in India can do a lot!

Message from H.E. Mr. Artis Bērtulis
Ambassador of Latvia to India

I'm privileged to support the hard work carried out by the EBG Federation, including the tremendous efforts invested in publishing the annual Position Paper, which gives a valuable overview of the important developments across key sectors in India, and reaches out with recommendations for continuous successful cooperation between European and Indian businesses. The activities by the EBG Federation and its Position Paper is also a tangible example of nourishing the EU-India economic partnership, reaffirmed at the 15th EU-India summit in July 2020.

This year the world is facing many challenges that accompany the pandemic. At the same time, I am confident that theses pivotal times give an opportunity for Europe and India to create a fresh blueprint for further expanding and fortifying the partnership and provide for new breakthroughs in trade, business, scientific research, and sustainable development. Let me single out my appreciation for activities undertaken by the Indian government during these challenging times, including important reforms to open up many sectors for private business participation, support to MSMEs and the start-up ecosystem, furthering the ease of doing the business, and stressing the importance of R&D.

The EU-India Roadmap to 2025, adopted during the summit, gives a promising framework also for Latvia and India to work together in various fields for the common good. Latvia and India enjoy stable trade and economic relations. However, there is a lot of untapped potential. Latvia wishes to create knowledge partnerships with India and its representatives from the industry, science, and research. Our scientists and innovators can jointly look for new age technology solutions to various complex situations. From a sectoral perspective, let me particularly highlight the ICT, higher education, transport and logistics, space, high benefit tourism, as well as the film industry, where the Latvian and Indian entrepreneurs could consider various forms of cooperation for mutual benefit and strategic positioning.

Message from H.E. Mr. Julius Pranevičius
Ambassador of the Republic of Lithuania to India

Lithuania-India relations in recent years were gaining new momentum through high-level and business visits, and I may not be more excited to work towards building more bridges between our countries. Historical visit of India's Vice President Venkaiah Naidu to Lithuania marked an important milestone in our bilateral relationship. It was also a strong impetus to further enhance meaningful modern cooperation between Lithuania and India.

Nowadays, when our lives are ruled by globalisation, companies are not restricting themselves geographically and are keen to develop their business in new markets. Despite the distance between our regions, India is a close partner for Europe in all senses. Geographic proximity becomes less and less important determinant of economic cooperation. This especially could be seen in COVID-19 times, when global pandemics hit every aspect of daily life. While in the beginning nations were struggling to contain the pandemics and its impact on economies, after more than 6 months since it all began, companies and businesses are now finding solutions on how to adapt to the situation, do business virtually, and implement changes to current practices.

We currently observe the growing mutual interest in cooperation in Life Sciences – delegations from Lithuania took part in major biotechnology forums in India in 2019 and Indian companies were very interested in a robust and growing life science industry in Lithuania. While the important international forums had to be postponed due to the pandemic, disruptions in supply chains and new reality also gave an impetus for both countries to explore each other's markets for broader cooperation in this area.

Lithuania's economic recovery after coronavirus crisis is believed to be very rapid. Lithuania took the opportunity to use the crisis and change the DNA of Lithuanian economy. Digitisation and reorientation of industry, attraction of new investment, retraining of the employed in high value-added areas, biotechnology, medical services, deployment of renewable energy sources are just few proposed measures to recover from pandemics and increase development overall. Current changes in global economy actually brings significant potential to Lithuania, India, Europe, and their economic cooperation.

In this context, I take this opportunity to congratulate the EBG Federation on taking this initiative to prepare the Position Paper for the year 2020, an important document, addressing the challenges and highlighting opportunities of trade and cooperation between Europe and India, especially in these challenging times.

Message from H.E. Mr. Jean Claude Kugener
Ambassador of the Grand Duchy of Luxembourg to India

It is my great honour to be contributing again to the foreword of this year's position paper, which illustrates the efforts made by the EBG Federation in bringing the EU and India closer in an ever-growing number of partnerships and sectors.

Luxembourg as a founding member of the European Union (EU) has always been a strong believer in tying deep and strong relations with India, especially in the areas of trade and investments. The economic relations between the EU and India are extremely diverse, which I can also attest from the Luxembourgish point of view with a few updates since last year.

Allow me to mention but a few examples: Luxembourg has increased its FDI to India and become the 15th biggest contributor in FDI overall this year. The Luxembourg Stock Exchange (LuxSE), whose "Luxembourg Green Exchange" (LGX) is issuing more than 50% of all Green Bonds worldwide, is considering to work more extensively with its Indian partners since the CEO and Deputy CEO's participation in this year's edition of the "Raisina Dialogue". Ceratizit, the Luxembourgish company specialised in producing hard-metal cutting materials, has opened a new factory extension in Bengaluru, which will optimise its production processes and house the machinery required by the group as it moves to make India its production hub for South and Southeast Asia. ArcelorMittal, the world's largest steel producer, which is headquartered in Luxembourg, acquired Essar Steel and is bringing new investments to India's steel sector. During the 4th India Water Impact Summit in December 2019, Boson Energy became one of the five selected companies from the EU, which exchanged a Technology Collaboration Agreement with the Centre for Ganga River Basin Management and Studies (cGanga) of the IIT Kanpur. Earlier this year, Luxembourg-based Kleos dispatched four of its Scouting Mission nanosatellites to Chennai in preparation of the launch aboard the upcoming Polar Satellite Vehicle C49 mission, which will be conducted by ISRO from the Satish Dhawan Space Centre.

I am also looking forward to the results of the "EU Excellence in India" concept, which will leverage in time. The programme brings together business champions, including the Luxembourg companies Paul Wurth and Ceratizit, present in India since more than two decades, and will enable greater bilateral collaboration between Indian and European companies that implement sustainability and climate actions.

In this context, I would like to warmly thank the EGB Federation for its contributions in promoting these exchanges with our Indian partners, for finding win-win solutions and ultimately in adding value for the European companies and their Indian counterparts.

Message from H.E. Mr. Reuben Gauci
High Commissioner of Malta to India

As the new High Commissioner of Malta in New Delhi, India, I have to admit that I arrived in difficult times for the world at large, with the COVID-19 crisis raging on. Upon landing in India, in September 2020, I felt hopeful that things would get better soon and that India's power of optimism will inspire the world. I am determined that COVID-19 should not be allowed to stand in the way of relations between Malta and India. Prior to the COVID-19 crisis, relations between Malta and India were gaining new heights. Despite the difference in size, the economies of both Malta and India were expanding rapidly.

I can attest that COVID-19 has not stopped the interest of the Maltese and Indian people in each other, who would eagerly continue to visit one another and plan new and exciting projects ahead, the moment this pandemic subsides. In saying so, I am hopeful that the globally renowned Indian pharmaceutical production lines will be producing COVID-19 vaccine in large quantities, once the immunisation drug is finalised, and in doing so India will be a major dynamic in saving our planet from the pandemic.

I truly believe that the world will be better after this pandemic ends, and that it will become a place where economies will thrive for the benefit of all. Countries, like Malta and India, will continue to expand on their business relations for the good of their people.

I acclaim the European Business Group Federation in their tireless efforts in promoting European businesses in India. I also commend the EBG Position Paper 2020 and its goals.

Message from H.E. Marten van den Berg
Ambassador of the Netherlands to India

The world economy encounters the largest shock since the economic crisis of 1929. Specifically, emerging and developing economies have been hit hard by the COVID-19 crisis. Faced with an unprecedented contraction of GDP and a grim outlook for the coming years, governments focus on battling the pandemic, providing social and economic safety for the vulnerable part of the population, and creating a sound foundation for economic recovery. Globally de-globalisation tendencies seem to gain traction, inhibiting the risk for a continued contraction of global economic output.

India has been hit hard by the COVID-19 crisis and needs the support of their international trading partners to maintain the supply chains as much as possible. Foreign direct investment is needed for it provides technology and employment. No matter the dire situation caused by COVID-19, the crisis has created opportunities to fast track a reform agenda to make the Indian economy more sustainable, more crisis-resilient, and as such better positioned in the global economy.

The Netherlands are, worldwide, the second-largest foreign investor, in India it is number four. We are among the top 15 partners of India in terms of trade volume. The interest for India among Dutch companies is increasing, and rightfully so. India with its large consumer market and economic potential provides substantial opportunities for Dutch innovation and technologies. The Netherlands is keen to intensify its business relations with India to emerge as the country's hub for doing business with Europe. As much as 20% of all Indian exports to the European continent go through the Netherlands – making us the 'gateway to Europe'.

India and Netherlands have strong bilateral economic ties in the field of sustainable agriculture, health, water solutions, life sciences, start-up ecosystem, maritime, and port development. Multiple bilateral agreements have been signed in the last two years. Through its diplomatic representations in New Delhi, Mumbai, and Bengaluru, and its trade offices in Ahmedabad and Hyderabad, and Honorary Consuls in Lucknow, Kolkata, and Chennai, the Netherlands is fully committed to continue the bilateral and European economic relations and work on the recovery of our economies. The Embassy of the Netherlands would like to congratulate the European Business Group Federation (EBG) for its commitment in furthering EU-India economic relations and our mutual efforts to overcome the economic dire period caused by the pandemic.

I am sure the Position Paper for 2020 will be of great value in policy making, as well as the promotion of business interests of the European Union in India. India is one of the most important partners for European companies. The EBG Federation plays a key role in this, with this Position Paper as a useful instrument to highlight business opportunities and shared interests.

Message from H.E. Prof. Adam Burakowski
Ambassador of the Republic of Poland to India

It is my personal honor to take this opportunity to express my appreciation for the work carried out by the European Business Group Federation (EBG) in facilitating greater bilateral economic cooperation between the European Union and India, and in its release of the EBG Federation Position Paper, 2020. I wish to congratulate the European Business Group Federation (EBG) on its efforts in supporting European companies in India and its commitment to strengthen business ties between them and their Indian counterparts.

Poland is a longstanding partner of India for more than 65 years with considerable importance on the economic and political level.

The commitment to further consolidate our economic cooperation with India can also be highlighted by the growing participation of Polish companies in trade fairs, conferences, exhibitions, and other fora across India.

However, challenges remain. A lack of clarity on policies regarding Indian sectors, market entry strategies, foreign direct investments, and regulations stand as a barrier to increasing Polish trade and investments with India. There are a lot of challenges that should be addressed, commonly, protection of natural environment and climate change, social and economic tensions or instable political frameworks. However common approach to the challenges will be an impact for fighting them.

In the year 2020, but also in future, the EBG Federation will have the opportunity to play an even more important role in strengthening EU business support in India, by providing business support to EU-India policy and India Member States dialogues. A single EU business voice to address common issues across sectors and member states will be an input to address the challenges mentioned above.

It is my personal honor to express my full support to the EBG Federation and its 2020 edition of the Position Paper.

Message from H.E. Carlos Pereira Marques
Ambassador of Portugal to India

On the occasion of the launch of EBG Federation 2020 Position Paper, I would like to emphasise and praise, once more, its valuable contribution, along the years, to the strengthening of economic and investment ties between Europe and India.

The launching of this important document occurs at a crucial moment for the India-EU relations, when, after a very successful and auspicious virtual annual summit in July, there are hopes that the negotiations for a comprehensive Free Trade Agreement and an Investment Protection Agreement may restart soon.

Portugal is of the view that, not only for economical, but also political reasons, the conclusion of such agreements is of the utmost importance at this stage, and in its capacity of President of the EU Council for the first semester of 2021, will attach the best attention to this priority, helping to establish new bridges between India and Europe.

It was under the Portuguese EU Presidency in 2000, that took place in Lisbon, the first EU-India summit ever, and it will be again during a Portuguese Presidency that an Informal Meeting of Leaders of India and the EU will occur for the first time ever, this time in Oporto, in May next year.

Portugal is proud to host this historical meeting and believes it will help to take the relationship of India with the EU to a very new level, opening the road to a trusted and deeper collaboration.

Congratulations, EBG Federation, on your most relevant work!

Message from H.E. Radu Octavian DOBRE
Ambassador of Romania to India

I would like to congratulate the European Business Group (EBG) Federation for the excellent work in supporting and encouraging the European companies to settle and expending their business on Indian market. India is set to become the third-largest economy in the world by 2025, so the business opportunities are huge and diverse.

European companies including Romanian businessmen understood that India will be the next economic superpower, so they have set new goals in prioritising their business expansion and investments into the Indian market.

I do believe that EBG Federation can contribute to support those initiatives of European companies by facilitating a better understanding of the Indian market and encouraging them to take initiatives, even if that means being out of their comfort zone.

EBG Federation is involved already in different projects and objectives, which support European businesses in India, and I am sure that in the coming years we will see an increase of the EU partnership in India, on multiple levels.

For now the world is facing a difficult and challenging situation in the context of COVID-19, but during crises some big opportunities rise, so we need to be prepared and vigilant to seize the occasion.

In 2019, bilateral relations between Romania and India have been enhanced by several initiatives of Indian companies to increase their presence in Romania by boosting their business and placing new investments. Romania has an extensive partnership with India, which gives us the base to build upon our similarities and complementarities to achieve better developments and greater success for our people.

I will not refer to the past months when all countries faced difficulties due to the measures taken to restraint the spread of coronavirus, because I think it is not relevant. After these challenging times, I believe in the V-shape of recovery of economy, especially for the Indian economy and the EBG can play a good role from a national perspective, as well as in focusing on key issues for EU - Indian collaboration.

EBG is doing a tremendous job in releasing yearly the “EBG Federation Position Paper,” which provides excellent information on important sectors in India and gives guidance to Indian authorities for improving the business environment, which could attract more foreign companies in this market.

Message from H.E. Ivan Lančarič
Ambassador of the Slovak Republic to India

It is my great pleasure and honour to once again congratulate EBG Federation on the release of its Position Paper, 2020. This publication does not only represent common business-related interests of EU Member States in India, but also compiles all important information on relevant industries and other economic indicators that serve as a compass in our further endeavours.

Unfortunately, many of our efforts have been negatively affected by the current coronavirus pandemic that has not only claimed many lives, but altered the international trade and economic relations as well. Countries all around the world are facing depression and we are still far from the end of the pandemic.

Regarding our pre-corona activities, I am proud to mention that the Slovak Republic participated with the largest and highly representative business mission to the IN-EU29 Business Forum in November 2019, headed by the State Secretaries from the Ministry of Foreign and European Affairs and Ministry of Economy. Other than that, we organised several more events aimed at connecting relevant business entities of our countries. In this regard, I´m particularly pleased by the fact that our export to India has doubled in the past two years.

In the beginning of 2019, we launched a campaign to promote Slovakia as a tourist destination and subsequently, in 2020, organised a highly-successful event „1 Lakh reasons to visit Slovakia", that attracted the attention of more than 100 Indian travel agencies.

Even though our efforts are being temporarily hampered by the global pandemic, I believe that once the situation improves, we will double down on our efforts to further develop mutually beneficial economic relations with India.

However, I´m convinced that only a broad, ambitious and comprehensive Free Trade Agreement, as well as an Agreement on Protection of Investments, will enable us to fully exploit the export potential of our economies.

I am using this opportunity to express my support and encouragement to the EBG Federation team in all of their activities that promote EU-India economic partnership.

Message from H.E. Dr. Marjan Cencen
Ambassador of the Republic Slovenia to India

As a relatively new member to the Diplomatic Society in New Delhi, but not new to India, I'm glad to learn about the important work of the EBG Federation. Its annual publishing of the Position Paper contributes to a better understanding of developments in India and helps identify opportunities of closer cooperation between India and EU and the Republic of Slovenia as its member.

EU partners with India in many fields, and India is amongst the main EU trade partners. I was pleased to notice that besides strengthening trade and investments, other elements of economic cooperation, such as renewable energy, technologies, and sustainable development and climate change technologies are gaining importance. It is good to see that we both understand the importance of these elements in our joint efforts to support stronger cooperation amongst our economies and people.

Slovenia and India are long-time partners and likeminded friends that have managed to keep stable relations at official, as well as people-to-people level, despite many geopolitical changes during the last few decades. Our political relations are strong and were given a new momentum with the visit of President Ram Nath Kovind in September 2019. The implementation of the signed programmes and MoUs during the visit will also add to the strengthening of our economic cooperation.

Strong momentum of enhanced economic cooperation is also reflected in substantial increase in bilateral trade of goods in 2019. More Slovenian companies are interested in investing in India, and there were some concrete inquiries by Indian companies to open their base in Slovenia.

The increased interest was also confirmed by the number of signed memorandums and programmes during the Indian president's visit. We are pleased that by giving a green light to launch of Indian Ganga Knowledge Centre, the signed memorandums between two Slovenian companies and Indian Institute of Technology, Kanpur, are very close to fruition. The two companies will be participating in the Clean Ganga Project and thus making a difference on the ground. In addition, the interest of cooperation between start-up companies of both countries is expressed in the field of electric car development. New opportunities for cooperation are also present in the automotive industry, renewable energies, and other green technologies.

Research and other work carried out by EBG Federation represents an important source for official and business representatives in enhancing their knowledge about business environment in India. With better knowledge and understanding, we are also better equipped to contribute to further increase economic and trade relations. I look forward to our future cooperation and wish you success in your endeavours.

Message from H.E. Mr. José Ramón Barañano
Ambassador of Spain to India

On behalf of the Embassy of Spain, I am delighted to congratulate the European Business Group Federation (EBG) for its work in strengthening bilateral economic relations between India and the EU, as well as for supporting European companies and their Indian counterparts. The release of the Position Paper gives a broad overview of the Indian business climate and reflects the need to continue working to make European and Indian companies work closely. There is room for improvement in sectors of interest for both sides such as water, urban development, climate change, and renewable energy.

We have good examples of collaboration between both countries. In this context, synergies regarding development and trade objectives are mutually exploited towards the best possible results.

Trade flows between Spain and India in 2019 exceeded 5.5 billion euros, 4.3% more than 2018, following the growing trend of the previous four years and placing Spain as the seventh-largest trading partner of India within the European Union. This data reinforces the importance of bringing a Bilateral Trade and Investment Agreement (BTIA) or a Free Trade Agreement (FTA) between Indian and the European Union, which will create an optimum business environment that responds to both sides' interests.

Currently, we are facing tough times worldwide but we will definitely overcome them. In this scenario of uncertainty, the European Union has to reinforce its role as a major player in the international arena.

Message from H.E. Klas Molin
Ambassador of Sweden to India

When I was first asked to contribute to the EBG Federation Position Paper, 2020 in late February this year, it was impossible to imagine the extent to which the current pandemic would alter the world where we work, live, and do business. The disease poses severe threats to lives and livelihoods in Sweden, Europe, India, and globally. Our thoughts are with the victims of COVID-19, those who lost a loved one, and those who suffer most from the depression that the global economy is currently undergoing.

Yet, it is in situations like these that the close relations we have built over the years prove their strength and value. Sweden and India have had a frequent exchange of high-level visits, a recent example being the State visit to India by Their Majesties King Carl XVI Gustaf and Queen Silvia of Sweden at the invitation of President Ram Nath Kovind in December 2019. During the pandemic, these exchanges have transformed into a stream of phone calls and virtual meetings between our governments, trying to solve problems for companies and citizens alike. Our active bilateral Innovation Partnership for a Sustainable Future now provides a firm foundation for our countries to propel solutions to common and global challenges, in areas such as health, digitalisation, and climate change.

Swedish companies have been present in India for as long as 120 years. Today, more than 200 Swedish companies employ about 200,000 people directly and more than 2.2 million indirectly in India. They are active in a wide range of sectors all over the country. Their long-term strategies in India have not been affected by the pandemic. Instead, Sweden and Swedish companies remain committed to India, and, despite the tragedy of the pandemic, we also see this crisis as an opportunity to partner in the transition to a greener, healthier, and more sustainable society. In short, jointly build back a better world.

However, continued trade, business, and private investment are key to leveraging the full potential for Indo-European and Indo-Swedish cooperation in ensuring a strong and green recovery after the pandemic. This, in turn, requires continued efforts to ensure a conducive business environment in India. Through its EBG Federation Position Paper, the EBG Federation and its members have played an important role safeguarding the interests of, and solving challenges facing Swedish and European companies in India. On behalf of the Embassy of Sweden, I would like to congratulate and thank EBG Federation for preparing the 2020 edition. This particular year, the document might just prove more valuable than ever.

Message from H.E. Dr. Ralf Heckner
Ambassador of Switzerland to India

At the outset, I wish to congratulate the EBG Federation for the publication of the 2020 edition of its Position Paper.

I arrived in New Delhi in early September and am glad to have presented my credentials to the Hon'ble President of the Republic of India in October 2020. I strive to invest all my energies and creativity into further fostering and broadening our bilateral relationship. To strengthen economic cooperation and trade between Switzerland and India is a priority.

India is one of Switzerland's most important trade and investment partners. There are more than 300 Swiss companies operating through a branch office, a subsidiary, or a joint venture in India. According to Swiss foreign trade statistics, Swiss exports to India in 2019 amounted to almost US$20 billion, while imports from India in 2019 amounted to slightly more than US$2.3 billion. Per FDI data compiled by the Indian Ministry of Commerce and Industry for the period April 2000 to March 2020, Switzerland is the 12th largest investor in India with investments of over US$4.8 billion. On the other hand, India is Switzerland's third-largest trading partner in Asia.

COVID-19 has highlighted the interdependence and the complementarity of the Swiss and Indian economies. The official Swiss network in India has been extremely active in supporting Swiss companies to find solutions to the problems they encountered during the lockdown, especially those related to supply-chain issues. The Swiss team has been in close contact with Indian central and state authorities to resolve company issues and find suitable and working solutions.

The work of the EBG Federation in favour of European businesses in India complements the activities of embassies. The numerous informative and useful webinars connect European businesses with Indian high-level representatives on a regular basis. And the EBG Position Paper, the flagship publication of the EBG Federation, is again making an important point, which is that Europe is one of India's most important economic partners.

I welcome the successful launch of this year's Position Paper and once again convey my warmest congratulations to the EBG Federation.

Message from Mr. Gokul Chaudhri
Partner – Deloitte Touche Tohmatsu India LLP

The India-EU ties date back to several decades with India being amongst the first nations to forge bilateral economic and diplomatic associations with the European Union, then known as European Economic Community. The partnership stood reinforced at the beginning of the 21st century, as India and EU became 'Strategic Partners' and agreed on a Joint Action Plan in 2005 (updated in 2008). Since India's engagement with the EU has substantially intensified and now spans over 30 dialogue mechanisms, covering foreign policy and security issues, trade and investment and sustainable development amongst others. The European Investment Bank (EIB), that has EU member states as its shareholders, has invested €2.5 billion in infrastructure, renewable energy and climate projects in India creating almost 6 million job opportunities. India, on the other hand, continues to remain a hugely attractive investment destination for EU investors, and is the ninth-largest trade partner for the EU. Besides, the existing EU-India Clean Energy and Climate Partnership, the establishment of a formal India-EU climate change dialogue, along with enhanced EU support to the International Solar Alliance (ISA) and cooperation in the International Renewable Energy Agency, offers impetus to India in achieving its ambitious goal of 175GW of renewable energy by 2022.

There is no gainsaying that while the two sides have come far in this continued evolution of their bilateral relationship, the engagement continues to hold out increased potential. In addition to bilateral engagement, India and EU continue to engage on various multilateral platforms like G20, OECD, WTO and UN on issues ranging from climate change to tax policy framework. Amid slowing global growth, mounting trade wars and increasing economic protectionism, India and the EU remain strongly committed to effective multilateralism with United Nations (UN) and WTO at its core.

The government's unprecedented focus on scaling up infrastructure capabilities, growing thrust on industrialisation and indigenisation, and creating employment through R&D and technological advancements hold out tremendous potential for European businesses at large. In fact, interest already evinced by EU businesses in government's flagship programmes – Make in India, Skill India and Digital India is quite encouraging and poises India as one of the next manufacturing hubs for European manufacturers like automobiles and others. Successful negotiation of Bilateral Trade and Investment Agreement (BTIA) or Free Trade Agreement (FTA) would go a long way in achieving this objective. At the ground level, there has been a paradigm shift in approach towards governance as government has unveiled multiple reforms aimed towards improving business climate in India. In the World Bank's rankings on 'ease of doing business', India has been ranked at 63 in 2020 from 139 rank in 2010 among 190 countries assessed by the World Bank. India's leap in 'ease of doing business' ranking is significant and the government is consistently endeavouring in this direction to improve it further. Successful journey of the comprehensive GST regime and overarching efforts of the government to simplify tax legislations and modernise tax administration are important cogs in this wheel of change. Recent enactment of the taxpayer's charter, introduction of faceless audit/appeal, deferrals in statutory tax compliances owing to the COVID-19 pandemic, expeditious issuance of tax refunds are some of the promising measures introduced by the government in this respect.

Both EU and India share interest in further strengthening their political, economic and defence cooperation not only on a robust bilateral agenda, but also on regional and global issues of shared concern and for reforming the multilateral system. Recently, in July 2020, the leaders[1] held the 15th European Union (EU) – India Summit where 'EU-India Strategic Partnership: A Roadmap to 2025' was endorsed as a common roadmap to guide joint action and cooperation over the next five years. The said roadmap deals with key challenges like climate change, environment, global governance, trade and investment, etc. The leaders also discussed prospects for global collaboration and sustained funding for developing, deploying and accessibility of effective diagnostics, treatments and vaccines, in particular linked to the COVID-19 outbreak.

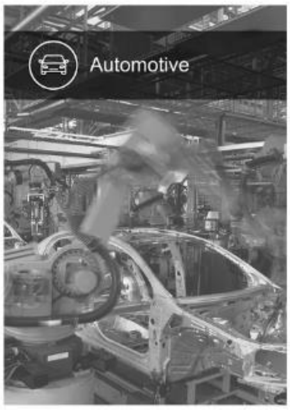
---

[1] India was represented by Prime Minister Mr. Narendra Modi; while the EU was represented by Mr. Charles Michel, President of the European Council, and Ms. Ursula von der Leyen, President of the European Commission.

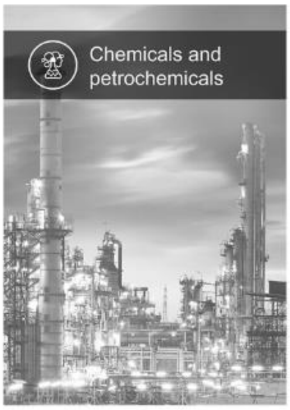
Against this rapidly evolving geo-economic landscape, EBG Federation India, has played a commendable role in facilitating trade and investment flows as well as emerging as a credible voice of EU businesses in bringing forth concerns and recommendations of businesses for deliberation by the Indian policy makers. The EBG Federation Position Papers for many years have been instrumental in shaping policy discussions across industries and successfully enhancing the dialogue on ways to deal with impediments for cross-border trade and investments.

We at Deloitte would like to congratulate the EBG Federation on the 2020 edition of this annual publication and extend our gratitude and pleasure in partnering with them on this significant initiative.


Agrochemicals

Alcoholic beverages

Automotive

Aviation

Banking

Chemicals and
petrochemicals

Defence

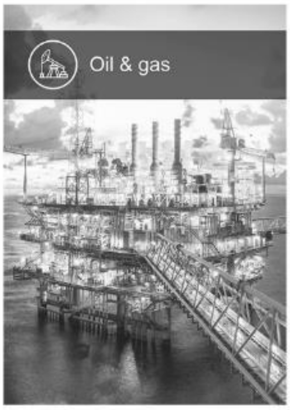
Financial services

FMCG

Healthcare

ICT

Infrastructure

Logistics

Oil & gas

Pharmaceuticals

Power

Railway commitee

Retail

Telecom

CONTENTS

INTRODUCTION

The year 2020 has presented the world with unprecedented challenges and opportunities, as were not captured by any business continuity plans or foreseen by economists, global businesses or Governments. While the disruption caused by the COVID-19 pandemic is still very much a reality, all stakeholders are adjusting to this 'new normal' and preparing to both survive and grow with a new set of rules. India is no different and while there are contrary views on whether the infection curve has flattened or continues to grow, there certainly is unanimity that India is at a tipping point to come out stronger in terms of its economic impact on the global arena. This opportunity certainly comes with its set of challenges and must do's which will be discussed further in this position paper.

The Indian economy was on a growth trajectory when measured by GDP for the past few years however it had started to face headwinds in 2019-20 as the GDP slowed down to 4.2% in the last quarter of 2020 on account of a wide array of factors such as slowing demand, increasing stress on financial sector, etc. As the government was looking to plug these issues the world was struck with COVID-19, the worst pandemic in history of mankind. On 24 March 2020, Prime Minister Narendra Modi chose a bold move and imposed a nationwide lockdown that remained in effect until 31 May 2020. The abrupt nationwide lockdown imposed across India was the biggest and most stringent in the world, forcing 1.3 billion Indians to stay indoors. But unlike other countries (such as Germany, Italy and Thailand), while the lockdown in India did slow down the spread to some extent, the spread continued to impact the country and its citizens, as also the economy. Infection cases kept on increasing despite India being in lockdown and India as on today is the second largest impacted country with respect of virus infected population.

The lockdown also had a very devastating impact on the already slowing economy. As per official data released by the Ministry of Statistics and Programme Implementation, the Indian economy contracted by 23.9% in April-June quarter of this fiscal year. This is the worst decline ever recorded since India started compiling GDP statistics on a quarterly basis in 1996.

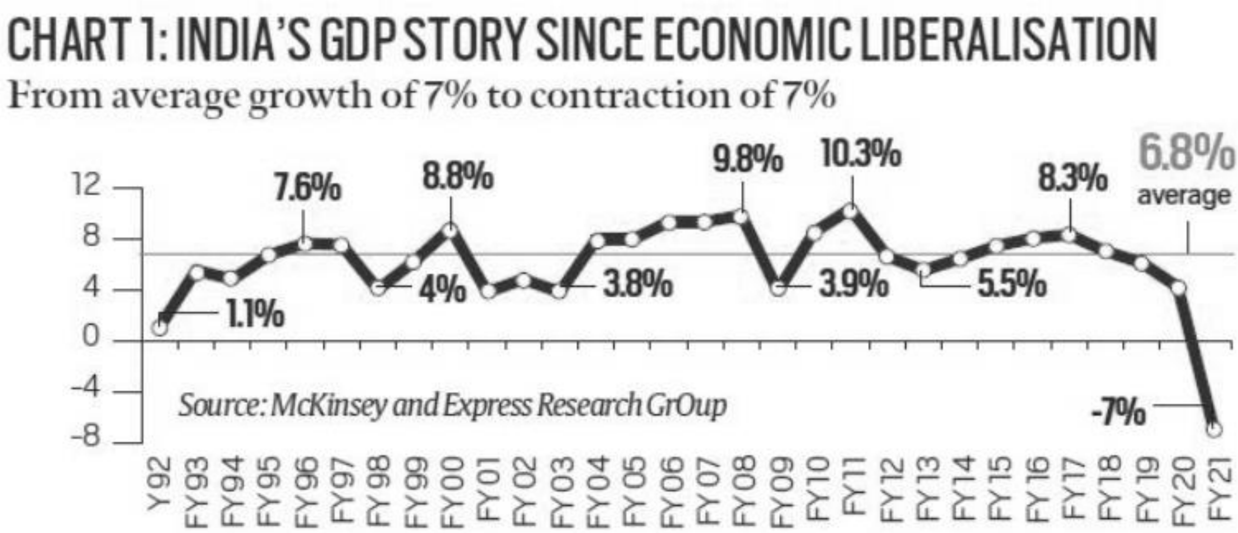
As per IMF estimate, the pandemic, even if swiftly controlled, could shrink per capita GDP across 170 nations by at least 3%. It could result in drastic drop in industrial production, uncertainty over the supply chain, large scale unemployment and even drop in agricultural production etc. The scenario looks very grey with the resultant impact on the demand and supply scenario.

To bounce back from such a situation, India needs to strengthen building blocks of the economy as well as that of society. The Hon'ble Prime Minister of India has made a clarion call to utilise this challenging time not as a national crisis, but as an opportunity for economic revival, to promote 'Make in India' initiatives and become self-reliant. Government will have to be agile and bold in developing a recovery strategy which should not shy away from higher public spending and an expansionary fiscal policy that will boost the aggregate demand for goods and services, which in turn would restore output and create employment.

1. INDIA: WORLD'S LARGEST DEMOCRACY AND OPPORTUNITY OF STRONG ECONOMIC REVIVAL

India which is a home to nearly a fifth of the world's population with almost 65% below the age of 35 has the demographic advantage and a successful track record to draw on to stage a bounce back. Over the past three decades, this country has been one of 18 outperforming emerging economies to achieve robust and consistent high growth. Pro-growth reforms lifted productivity and helped the country weather shocks and cycles. Since 2005, more than 270 million people have escaped extreme poverty. Real GDP growth has averaged 6.8% annually since 1992, and it has been inclusive; economic prosperity has brought significant improvement in living standards.

Fig 1. GDP growth rates (y-o-y, per cent)



1.1 Government measures to revive the economy and early green shoots[1]

In June 2020, country entered the unlocking phase and witnessed some green shoots of kick start in the economy. Payments on Unified Payments Interface (UPI) hit an all-time high of 1.34 billion in terms of volume with transactions worth nearly INR2.62 lakh crore (US$37.17 billion). Also, as on 17 July 2020, total kharif crops were sown on 691.86 lakh hectares against 570.86 lakh hectares during the corresponding period last year, an increase of 21.20% in area coverage compared to last year in the country.

Government of India introduced Pradhan Mantri Garib Kalyan Yojana to provide immediate cash support to the needy. More than 42 crore poor people have so far received financial assistance of INR65,454 crore (US$9.29 billion) under the scheme. The estimated cost of distribution of food grains (rice and wheat) and pulses under Pradhan Mantri Garib Kalyan Anna Yojana, now extended till the end of November 2020, is INR1,48,938 crore (US$21.13 billion). Since 1 July 2020, a total of 19.32 LMT food grains have been lifted by various States and Union Territories (UTs) under Pradhan Mantri Garib Kalyan Anna Yojana 2.

In May 2020, Government, adding to its past measures and that of RBI (Reserve Bank of India), announced a consolidated stimulus package of INR20 lakh crore (US$283.73 billion). The stimulus package was pivoted on "Aatma Nirbhar Bharat", where Micro, Small and Medium Enterprises (MSMEs) received a huge financial package in terms of collateral free debt, guarantee for subordinate debt through Funds-of-Funds, and interest subvention scheme. Besides, the definition of MSME was changed to remove hindrance against their investment and expansion. Other components of the package included three landmark ordinances related to Essential Commodities Act, Farmers' Empowerment and Protection, and Promotion and Facilitation of Agricultural Produce to encourage people to invest in creating infrastructure and storage for agricultural produce, enable barrier-free trade in agriculture, and empower farmers to engage with various stakeholders.

Government also introduced Pradhan Mantri Garib Kalyan Rojgar Abhiyaan, a rural infrastructure and employment generation scheme, for the benefit of returnee migrants. These green shoots have started to create a conducive policy environment to grow further and nudge the economy early on the path of economic recovery and growth.

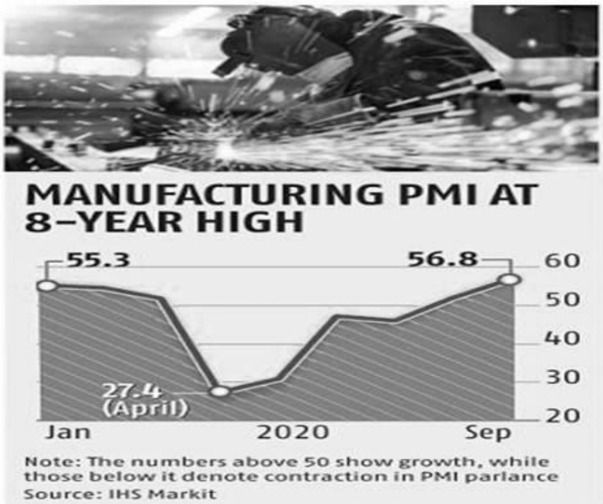
The recent high frequency indicators suggest that economic activity has started to normalise to the pre-COVID levels during the last three months which corresponds to the second quarter of the financial year.

For starters, the PMI (Purchasing Managers' Index) came in at 56.8%, goods and services tax (GST) collections were up 4% on a year-on-year basis to INR95,480 crore while E-way bills were at 50.2 million until 28 September, which happens to be the highest figure since March 2020. Moreover, Indian Railway freight was up 15.33% on a year-on-year basis; 29 million sought work under MNREGS (Mahatma Gandhi National Rural Employment Guarantee Scheme), which was lowest since May and power demand was up by 4.8%. Automobile manufacturers showed significant signs of recovery as they dispatched 13% more vehicles to dealers in September as compared to the same period last year. India's biggest carmaker Maruti Suzuki India posted its highest monthly sales in two years in September, as an end to a nationwide lockdown prompted dealerships to stock up ahead of a festive season.


VEHICLE SALES ACCELERATE

Company	Units sold in Sept 2020	YoY chg (%)
Maruti Suzuki	160,442	30.8
Hyundai	59,913	3.8
M&M	79,306	-1.3
Bajaj Auto	441,306	10.0
TVS Motor	327,692	14.0
Hero MotoCorp	715,718	16.9
Toyota Kirloskar	8,116	-20.45
Kia Motors	18,676	147.20
Honda2Wheelers	526,865	8.48

Source: Companies

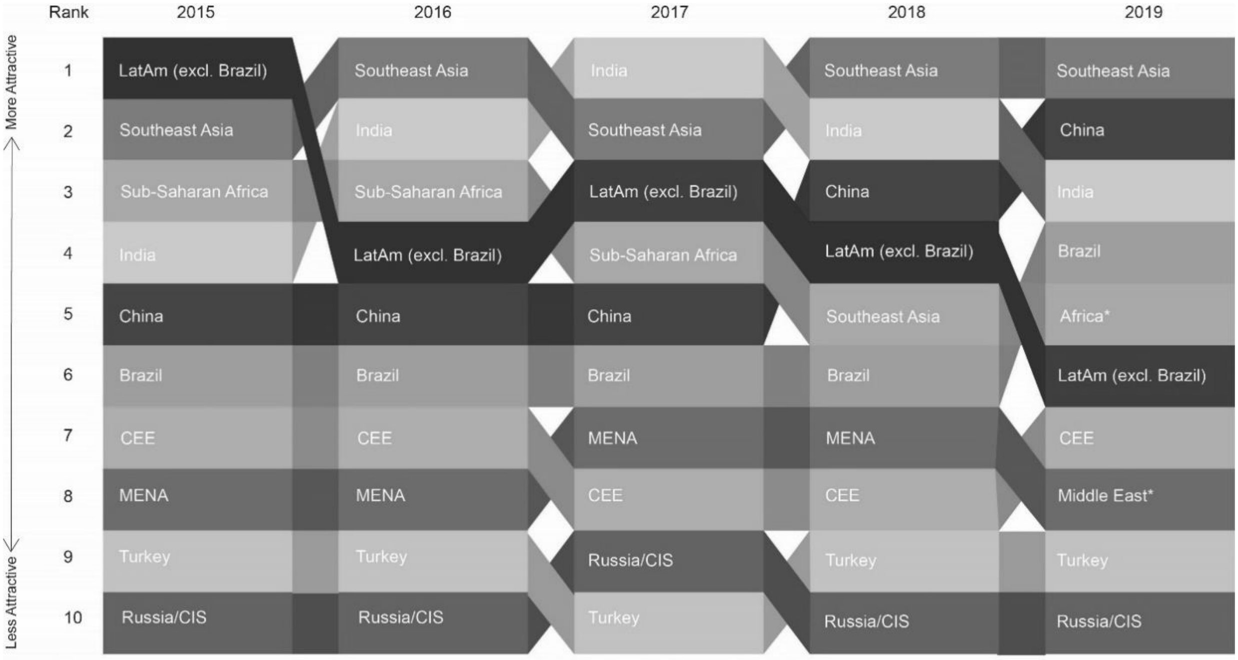


1.2 India Continues to Attract High Levels of Foreign Direct Investment[2]

Apart from being a critical driver of economic growth, Foreign Direct Investment (FDI) has been a major non-debt financial resource for the economic development of India. Foreign companies invest in India to take advantage of inter alia relatively lower wages, talent availability, domestic consumption, age demographics, special investment privileges, improving infrastructure and easier business environment. For a country where foreign investment is being made, it also means achieving technical know-how and generating employment. Indian Government’s favourable policy regime and robust business environment has ensured that foreign capital keeps flowing into the country. The Government has taken many initiatives in recent years such as relaxing FDI norms across sectors such as defence, PSU oil refineries, telecom, power exchanges, and stock exchanges, among others.

According to Department for Promotion of Industry and Internal Trade (DPIIT), FDI equity inflow in India stood at US$469.99 billion during April 2000 and March 2020, indicating that Government's effort to improve ease of doing business and relaxing FDI norms has yield results. FDI equity inflow in India stood at US$49.97 billion in 2019-20. Data for 2019-20 indicates that service sector attracted the highest FDI equity inflow of US$7.85 billion, followed by computer software and hardware at US$7.67 billion, telecommunications sector at US$4.44 billion, and trading at US$4.57 billion.

During 2019-20, India received the maximum FDI equity inflow from Singapore (US$14.67 billion), followed by Mauritius (US$8.24 billion), Netherlands (US$6.50 billion), USA (US$4.22 billion) and Japan (US$3.22 billion). India will continue to be an attractive emerging market for global partners (GP) investment for the coming 12 months as per a recent market attractiveness survey conducted by Emerging Market Private Equity Association (EMPEA). Annual FDI inflow in the country is expected to rise to US$75 billion over the next five years as per the report by UBS.[3]



*Africa included in survey as 'Sub-Saharan Africa' and Middle East included in survey as 'MENA' prior to 2019.

1.3 Continuing Focus on Ease of Doing Business

India continued its upward movement trend in 2020 as well with gain of 14 position to reach at 63rd rank among the 190 countries. The country has successfully improved its position from 142nd in 2014 to 63rd in 2020 which makes it one of the best performers in World Bank Doing Business Index in last 5 years. The World Bank listed starting a business, dealing with construction permits, trading across borders and resolving insolvency as major areas of improvements.

World Bank noted that India's Make in India campaign focussed on attracting foreign direct Investment, boosting the private sector (manufacturing in particular), and enhanced the country's overall competitiveness. The Government had set a goal of joining Top 50 economies in Ease of doing Business index by 2020 and accordingly made significant efforts to improve on all of the parameters measured by Index with particular focus on paying taxes, trading across borders and resolving insolvency.

While COVID-19 was likely to slow the pace of reforms temporarily, the Government has used the opportunity to show agility by simplifying legislation in area of labour laws, digital governance and faceless online interaction with tax authorities. India mainly needs to focus on starting business, registering property, paying taxes and enforcing contracts to further boost its chances of making into Top 50 countries on World Bank DB index.

Source: Compilation from World Bank 'Doing business report' – 2020

The Government continued its Labour reforms agenda with introduction and passage of 3 new Labour Law codes i.e. The Occupational Safety, Health and Working Conditions Code, 2020, the Industrial Relations Code, 2020, Code on Social Security, 2020 which are in addition to Code on Wages, passed by parliament in 2019. The reforms in Labour sector has been a long standing demand from Industry and investor community alike and current regime has consistently acknowledged it as a necessary element for improving ease of doing business. The four new codes subsume 44 central labour legislations and proposes to create a labour compliance framework that is based on "one labour return, one license, and one registration". The Government believes these codes will prove to be game changers for Indian Industry and help move India within Top 10 positions in World Bank's Ease of doing business rankings.

1.4 Way Forward

India has emerged as the fastest growing major economy in the world and is expected to be one of the top three economic powers of the world over the next 10-15 years, backed by its strong democracy and partnerships. India's gross domestic product (GDP) is expected to reach US$6 trillion by FY2027 and achieve upper-middle income status on the back of digitisation, globalisation, favourable demographics, and reforms. The current slowdown in economy is going to present major challenges in short term but as most economic analysts have expressed that since India's fundamentals remain intact so India's economic recovery should be relatively rapid post pandemic. India is poised to become the third-largest consumer market behind only the US and China; and consumer spending in India is expected to grow from US$1.5 trillion at present to nearly US$6 trillion by 2030, a World Economic Forum report.

The pandemic has impacted the economies world over without exception and India is no different. The major challenges staring at Indian economy caused by pandemic necessitated lockdown are weak demand, unemployment and rising inflation. The Government continues to respond robustly to the challenges with historically high stimulus economic packages since April 2020. The economic experts differ on form and shape that economic recovery may take however most seem to agree that full recovery should take at least a year. It is also being suggested that economic recovery will not be uniform across sectors i.e. while some sectors likely to do well such as technology sector, pharma industry as evidenced in the valuations on the traded stock markets, while others such as tourism, airlines, food and beverage may take longer time on road to recovery.

2. RECENT POLICY MEASURES

2.1 E- Invoicing introductions: Goods and Services Tax

As a major step towards e-governance, Government has rolled out E-Invoicing starting from October 2020. Currently, businesses generate invoices through various software and the details of these invoices are manually uploaded in the **GSTR-1 return**. The invoice information is thereafter reflected in GSTR-2A for the recipients for viewing only. On the other hand, the consignor or transporters generate e-way bill again by importing the invoices in excel or JSON manually.

Considering the above, the GST Council in its council meeting, had decided to implement a system of e-invoicing, which will be applicable to specified categories of persons.

E-invoicing or electronic invoicing is a system to generate an electronic document containing transaction information between a buyer and a seller. The Invoice Registration Portal (IRP) gives an identification number to these electronic invoices. The Invoice Reference Number (IRN) generated by IRP will be used to transfer all the invoice information to the GST portal and the e-way bill portal.

The GST e-invoicing system will be implemented from October 2020 for those taxpayers whose turnover is INR500 crore or more. Earlier, it was planned to implement e-invoicing for businesses with turnover of INR100 crore or more in a year.[4]

The GST collections plummeted during the year as economic activities slowed down because of lockdown necessitated by COVID-19 pandemic. The GST collection for Feb 2020 was INR1 trillion which fell to INR0.91 trillion in June 2020 and as of August is INR0.86 trillion. September 2020 staged a recovery with collections at INR0.95 trillion and showing a modest 4% year on year growth.

2.2 Aatma Nirbhar Bharat Abhiyan

The COVID-19 pandemic has posed a severe threat to the economy of the country. To overcome these testing times, Government has come up with Aatma Nirbhar Bharat Abhiyan that promotes the local economy. A special and comprehensive economic package of INR20 lakh crore that accounts for 10% of India's GDP, has been announced to bring the economy back on track. The Government further announced structural reforms across various sectors to pave the way for Aatma Nirbhar Bharat Abhiyan. The package supports MSMEs, farmers and migrant workers, agricultural and allied sectors. It also aims at policy reforms to fast track investment to pave way towards Aatma Nirbhar Bharat, Policy reforms in coal sector, mineral sector, defence production, private participation in space activities, world class airports through PPP, enhancement of Ease of Doing Business through IBC related measures, health reforms and initiatives to increase investment in public health and to prepare the nation for future pandemics, technology driven education with equity post COVID, Public Sector Enterprise Policy for a Self-Reliant India etc.[5]

2.3 Scheme for Promotion of Manufacturing of Electronic Components and Semiconductors (SPECS)

The Scheme was notified vide Gazette Notification No.CG-DL-E-01042020-218992 dated 1 April 2020 will help offset the disability for domestic manufacturing of electronic components and semiconductors in order to strengthen the electronics manufacturing ecosystem in the country.

The scheme will provide financial incentive of 25% on capital expenditure for the identified list of electronic goods that comprise downstream value chain of electronic products, i.e., electronic components, semiconductor/display fabrication units, ATMP units, specialised sub-assemblies and capital goods for manufacture of aforesaid goods, all of which involve high value-added manufacturing. The Scheme will be applicable to investments in new units and expansion of capacity/modernisation and diversification of existing units. Application under the Scheme can be made by any entity registered in India.

The capital expenditure will be total of expenditure in plant, machinery, equipment, associated utilities and technology, including for Research & Development (R&D).

The Scheme is open for applications initially for 3 years from the date of its notification. Incentives under the Scheme will be applicable from the date of acknowledgment of the application. The incentives will be available for investment made within 5 years from the date of acknowledgement of application.

The Scheme will be implemented through a nodal agency which will act as Project Management Agency (PMA) and be responsible for providing secretarial, managerial and implementation support and carrying out other responsibilities as assigned by Ministry of Electronics and Information Technology from time to time.[6]

2.4 Modified Electronics Manufacturing Clusters (EMC 2.0) Scheme

To offset the disabilities faced by industries for quality infrastructure and to develop a robust electronics manufacturing ecosystem in the country to make India an Electronics Manufacturing Hub; Modified Electronics Manufacturing Clusters (EMC 2.0) Scheme has been notified vide Gazette Notification No.CG-DL-E-01042020-218991 dated 1 April 2020 with the objective to address the disabilities, by providing support for creation of world class infrastructure along with common facilities and amenities, including Ready Built Factory (RBF) sheds /-Plug and Play facilities for attracting major global electronics manufacturers along with their supply chain to set up units in the country.

This Scheme will fortify the linkage between domestic and international market by strengthening supply chain responsiveness, consolidation of suppliers, decreased time-to-market, lower logistics costs, etc.

The EMC 2.0 Scheme provides financial assistance for setting up of both EMC projects and Common Facility Centres (CFCs) across the country. The Scheme is open for receipt of applications for a period of 3 years from the date of notification. Further period of 5 years is available for disbursement of funds to the approved projects.

An application shall be made by Project Implementing Agency (PIA) which can be State Government or State Implementing Agency (SIA) or Central Public Sector Unit (CPSU) or State Public Sector Unit (SPSU) or Industrial Corridor Development Corporation (ICDC) such as DMICDC, etc.
All the applications received under the EMC 2.0 Scheme through Project Management Agency (PMA) will be considered by Project Review Committee (PRC) for giving its recommendations to the PMA for according approval-rejection of the projects.[7]

2.5 Production Linked Incentive Scheme (PLI) for Large Scale Electronics Manufacturing

Production Linked Incentive Scheme (PLI) for Large Scale Electronics Manufacturing notified vide Gazette Notification No.CG-DL-E-01042020-218990 dated 1 April 2020 offers a production linked incentive to boost domestic manufacturing and attract large investments in mobile phone manufacturing and specified electronic components, including Assembly, Testing, Marking and Packaging (ATMP) units. The Scheme would tremendously boost the electronics manufacturing landscape and establish India at the global level in electronics sector.

The scheme shall extend an incentive of 4% to 6% on incremental sales (over base year) of goods manufactured in India and covered under target segments, to eligible companies, for a period of five (5) years subsequent to the base year as defined.

The Scheme is open for applications for a period of 4 months initially which may be extended. Support under the Scheme shall be provided for a period of five (5) years subsequent to the base year.

2.6 Key Policy measures as response to COVID-19[8]

The Government has been introducing various measures as policy interventions and economic stimulus to mitigate the adverse economic impact of COVID-19. Some of the prominent ones are listed below:

- Establishments which employ upto 100 employees and if 90% of whom earn up to INR15,000 per month, the government will pay the employee provident fund contribution both of the employer and the employee (12% each) for March 2020 to May 2020. This support is extended for another 3 months i.e. June to August 2020.
- CRR of all banks to be reduced by 100 basis points to 3% beginning 28 March, for 1 year. This will release liquidity of INR1,37,000 crore across the banking system.
- Reduction of policy repo rate by 75 basis points (from current 5.15% to 4.40%).
- Liquidity coverage ratio for banks reduced from 100% to 80% likely to release liquidity.

- Relief for MSMEs with measures such as INR3 Lakh crore (US$39 billion) collateral free loan with 100% credit guarantee, new definition of MSMEs – investment limit revised upwards; additional criteria of turnover introduced.
- Relief for NBFCs with measures such as INR30k crore (US$3.9 billion) liquidity infusion for NBFCs/HFCs/MFIs and INR45k crore (US$5.9 billion) partial credit guarantee scheme for NBFCs.
- Insolvency and Bankruptcy Code (IBC): Threshold of default under section 4 of the IBC has been increased from INR100,000 to INR10 million with the intention to prevent triggering of insolvency proceedings against MSMEs. Further Loans for COVID-19 excluded from definition of default.
- Decriminalisation of certain defaults under the Companies Act 2013 and simplification of mechanism to deal with defaults
- Companies permitted to list securities directly in foreign jurisdiction

2.7 Schemes for Pharmaceuticals Manufacturing

The Indian pharmaceutical industry is the 3rd largest in the world by volume. However, despite this achievement, we are highly dependent on imports of basic raw materials, viz., bulk drugs that are used to produce medicines. The Government of India is committed to ensuring the delivery of affordable healthcare in the country as well as ensuring that there is a steady supply of critical drugs. This has resulted in the launch of Production Linked Incentive Scheme (PLI) for APIs, KSMs and DIs as well as the Scheme for Promotion of Bulk Drug Parks. These schemes have been constructed to incentivise large-scale manufacturing of critical bulk drugs and to build the required infrastructure for developing manufacturing clusters for across India. This aligns with the Government's mission for self-reliance (aatma nirbharta).[9]

2.8 Schemes for Promotion of Medical Devices Manufacturing

The Indian Government has identified the medical devices as a priority sector for the flagship 'Make in India' program and is committed to strengthen the manufacturing ecosystem. India is the fourth largest medical devices market in Asia. Currently, the Indian market has high reliance on imports but in recent times the exports have seen a surge. 'Atma Nirbhar' Bharat mission is providing an impetus to India's vision of becoming a global manufacturing hub for medical devices. Recent initiatives for instance, the Production Linked Incentive Scheme (PLI) and Promotion of Medical Devices Parks Scheme, are a testimony to this. These schemes have been cogently constructed to incentivise large-scale manufacturing and to build required infrastructure for developing manufacturing clusters within India.[10]

3. INDIA-EU TRADE AND INVESTMENT RELATIONS[11]

The 15th Summit between India and the European Union (EU) was held in a virtual format on 15 July 2020. The Summit laid foundations for a deeper and more strategic cooperation between the European Union and India in times to come. Both the EU and India have agreed to deepen cooperation in areas like climate change, maritime security, digital economy, connectivity, research and innovation, water and climate action and civil nuclear cooperation.

According to Prime Minister, Shri Narendra Modi, 'Atmanirbhar Bharat' would be open to the world economies and it will integrate domestic production in India to global supply chains. According to the Indian Ambassador to EU, H.E. Mr. Santosh Jha, "*India-EU Summit has provided a significant boost and a stronger direction to the strategic partnership between the two regions. The outcomes highlight the multi-dimensional nature of their relationship and underline that these relations are not just consequential to the destiny of the respective citizens but also a pivotal factor in shaping the global future as well.*"[12]

President of the European Council Charles Michel remarked after the meeting that *"Today we focused on 3 important topics: COVID-19 and rebuilding our economic prosperity, our EU-India bilateral relationship and regional and security issues. As power dynamics shift across the globe, the EU wants to play a stronger role in the region and as a global actor. Today's substantive dialogue with India will reinforce these strategic goals. The EU and India are bonding together to fight COVID-19* *and I welcome India's role in tackling the virus, both at the regional and global level. And their contribution to the research and manufacturing of a vaccine, which should be available to all. We will cooperate to strengthen our health systems and ensure the WHO is effective".*

In a press release dated 15 July 2020, president of European Commission, the President of the European Council and Prime Minister of India sets out the EU's vision for a strategy to strengthen cooperation and the partnership with India.

The leaders agreed to further develop their trade and investment relations to unleash their full potential particularly in the context of post-COVID-19 economic recovery and support sustainable growth and jobs on both sides. They reaffirmed their commitment to work towards balanced, ambitious and mutually-beneficial trade and investment agreements, opening markets and creating a level playing field on both sides. They also agreed to establish a regular high-level dialogue at ministerial level to provide guidance to the bilateral trade and investment relations and to address multilateral issues of mutual interest.

The 15th Summit also opened a new chapter in EU - India Strategic Partnership with the adoption of India-EU Strategic Partnership: A Roadmap to 2025" as a common roadmap to guide joint action and further strengthen the India-EU Strategic Partnership over the next five years. It also welcomed the signing of the Euratom-India Agreement on research and development cooperation in the peaceful uses of nuclear energy and adopted a Joint Declaration on Resource Efficiency and Circular Economy.

The joint communication will strengthen the EU-India Strategic Partnership by focusing on sustainable modernisation and on common responses to global and regional issues. It is meant to serve for the next decade as a coherent platform to advance key EU interests, improving the way the EU approaches India. The Joint Communication seeks to maximise the opportunities in terms of trade, investment, people-to-people exchanges, foreign policy and security, and global governance, particularly through synergies and coherence in actions by the EU and its Member States.

- Seize the full potential of the EU-India strategic partnership.
- Build a strong partnership for sustainable modernisation, to benefit both sides.
- Join forces with India to consolidate the rules-based global order, based on multilateralism with the UN and the WTO at its core.
- Develop a shared approach at the multilateral level to address global challenges and increase coordination.
- Convene regular meetings to forge mutual understanding and discuss human rights issues – including women's rights and empowerment and child right.

3.1 India and EU: Trade and Investment Trends[13]

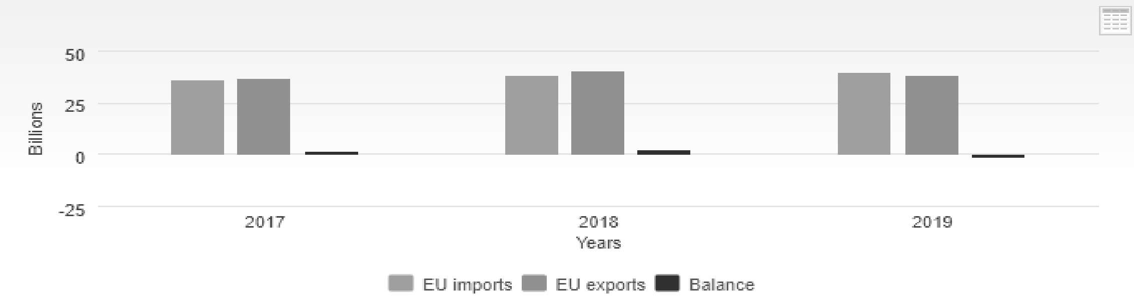
The European Union and India have upgraded their long-standing relationship to a strategic partnership acknowledging their common goals and principles. Nowadays, in a challenging international environment, the EU and India share the same values of democracy, human rights, and fundamental freedoms and support the rules-based global order centred on multilateralism. Both India and EU have taken several measures in order to boost and improve the scope of bilateral trade and investments. India remains a key trade partner on multiple fronts. Following is a key snapshot:

- The EU is India's largest trading partner, accounting for €80 billion worth of trade in goods in 2018 or 11.1% of total Indian trade, ahead of China (10.7%) and on par with USA
- The EU is the second largest destination for Indian exports (almost 14% of the total)
- India is the EU's 10th largest trading partner, accounting for 1.9% of EU's total trade in goods in 2019, well behind the USA (15.2%) and China (13.8%)
- Trade in goods between the EU and India increased by 72% in the last decade
- Trade in services between the EU and India increased from €23 billion in 2010 to €29 billion in 2016. India is now the 4th

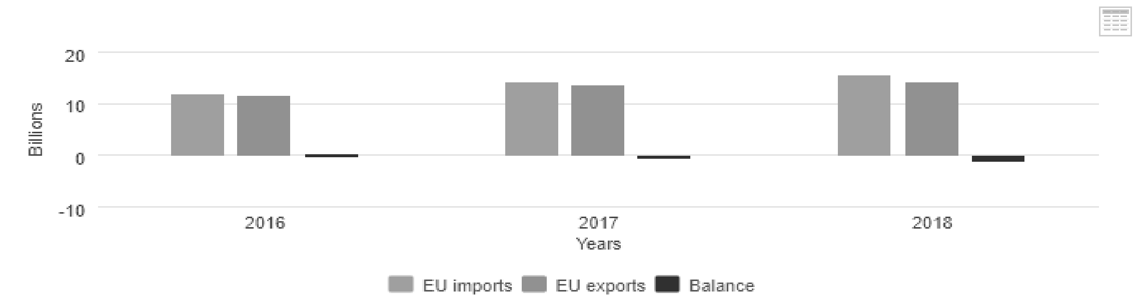
largest service exporter to the EU and the 6th largest destination for EU services exports

- The EU's share in foreign investment inflows to India more than doubled from 8% to 18% in the last decade, making the EU the first foreign investor in India
- EU foreign direct investment stocks in India amounted to €68 billion in 2018, which is significant but way below EU foreign investment stocks in China (€175 billion)
- Some 6,000 EU companies are present in India, providing directly 1.7 million jobs and indirectly 5 million jobs in a broad range of sectors
- Indian companies invested over €50 billion in Europe since 2000

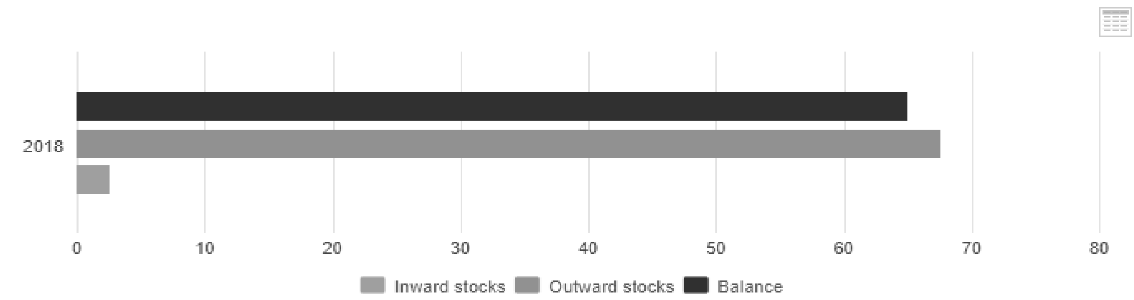
EU-India: Trade in goods



EU-India: Trade in services



EU-India: Foreign direct investment



CONCLUSION

Indo-EU trade and investment relations have seen significant changes and has been defined by deepening integration over the past decade. After the recent summit, the joint statement issued stated that both sides reaffirmed their commitment to work towards a balanced, ambitious and mutually beneficial trade and investment agreements, opening markets and creating a level playing field on both sides. The issue of trade is of vital importance to the relationship as the EU is India's largest trade partner, even after Brexit. The European Union is also the largest source for foreign investment to India, at over $91 billion.[14]

EU president Charles Michel also flagged this area as one, which needs to be upgraded. "The EU is India's largest trade and investment partner. But India represents only about 2% of EU external trade. This is clearly an area that offers impressive potential for significant future growth. We agreed to enhance conditions for traders and investors," he said at a press briefing in Brussels.

The EU and India completed 58 years of diplomatic relations in 2020. Between EU and India, regular and effective political and business dialogue has helped reach a balanced and forward looking relation. EU and India already play an important role in each other's development. India's international reach and relevance will continue to grow, and therefore its importance to the EU, in line with the development of its economy and its diplomatic and defence capabilities. Likewise, India seeks improved market access and harmonisation of barriers to movement across Europe.

With India rising on the ranks ease of doing business and government promoting measures to simplify doing business in India, both EU and India see a great opportunity to take the relationship at next levels.

ENDNOTE

1. https://www.mckinsey.com/in/our-insights/indias-turning-point-an-economic-agenda-to-spur-growth-and-jobs
2. www.ibef.org
3. https://www.empea.org/app/uploads/2019/05/2019-lp-survey-final-web.pdf
4. https://taxguru.in/goods-and-service-tax/e-invoicing-gst-regime.html
5. https://blog.mygov.in/major-announcements-and-policy-reforms-under-aatma-nirbhar-bharat-abhiyan
6. https://www.meity.gov.in/esdm/SPECS
7. https://www.meity.gov.in/esdm/emc2.0
8. https://home.kpmg/xx/en/home/insights/2020/04/india-government-and-institution-measures-in-response-to-covid.html
9. https://www.investindia.gov.in/schemes-for-pharmaceuticals-manufacturing
10. https://www.investindia.gov.in/schemes-for-medical-devices-manufacturing
11. https://www.consilium.europa.eu/en/press/press-releases/2020/07/15/joint-statement-15th-eu-india-summit-15-july-2020
12. https://diplomatist.com/2020/08/25/future-of-india-eu-relations/
13. http://ec.europa.eu: EU India Trade relations
14. https://thewire.in/diplomacy/india-eu-summit-trade-talks

Agrochemicals

Acknowledgements: K S Thyagarajan – Chairman,
Agrochemicals Sector Committee & its Members
Knowledge Partner: Devinder Chawla and Jiwanjot Singh – EY

INDIAN AGRICULTURE SECTOR AND ROLE OF AGROCHEMICALS IN DOUBLING FARMERS' INCOME

Agriculture, with its allied sectors, is the largest livelihood provider in the Indian economy, providing livelihood to more than 54% of India's population. It contributes ~17.4% to India's GDP.[1]India is the second-largest agricultural producer, right behind China and has the second-largest agricultural land holdings (157 million hectares) in the world. India is also amongst the leading exporters of agricultural products globally. The total agricultural exports from India have grown at a CAGR of 14.6% during FY2010-2019 to reach approx. US$38.5 billion in FY2019.[2] In FY2019, total food grain production in India was recorded at 281.4 million tons.[3]

The Indian Government is committed to double the income of farmers by 2022, for which, the government has increased the budgetary allocation of Agriculture and Farmer Welfare Ministry in the 2020-2021 Interim budget to US$19 billion from US$18.4 billion in Union budget 2019-20.[4] Under the 16-point strategy[5] laid down to boost agriculture and farmers welfare, the government has been taking several measures including:

1. Launch of Krishi Udan scheme to help farmers in transporting agriculture products to boost agriculture exports in both international and domestic routes.
2. Increase in agriculture credit target from US$160 billion to US$200 billion to provide financial help to farmers.
3. Allotment of US$37.2 billion for agriculture and irrigation for FY2021.
4. Expansion of NABARD scheme to further strengthen the credit facility for farmers
5. Investments in warehousing and logistics and technology to prevent post-harvest crop losses such as Kisan Rail for perishable goods.
6. Focus on rural areas by allocating US$16 billion for Rural Development and Panchayti Raj.
7. Integration of National Agricultural Markets and e-platforms (e-NAM) with financing of negotiable warehousing receipts.
8. Target of fish production to 20 million tons by 2022-23.
9. Focus on dairy sector and set a target to double the milk processing capacity to 108 tons by 2025.
10. Focus on irrigation as government proposes measures to improve situation in 100 water-stressed districts.
11. Government proposed new scheme "one product for one district" to focus on the district level for horticulture.
12. Government to focus on Zero Budget farming
13. Farm markets to be liberalised
14. To promote balanced use of fertilisers in the farm lands
15. Government to handhold farmers to liberalise agriculture markets
16. Farmers to be provided with funds for setting up standalone solar pumps.

Overall, the focus is not limited to increasing productivity but also reducing the costs of cultivation to increase the net income of farmers.

However, agriculture sector still suffers from the following major challenges impeding its growth[6]: 1) Poor weather updates and high dependency on monsoon for irrigation purpose; about 52% of India's total land under agriculture is still unirrigated.[7] 2) Soil degradation is another area of challenge, as around 36.7% of total arable and non-arable land surface in India suffers from various forms of degradations. India's yield per hectare is 3 tons/ha compared to the global average of 4 tons/ha, primarily due to poor soil health management 3) Low penetration of agrochemicals (per capita consumption of pesticides is 0.3 kg/ha in India as compared to 13 kg/ha in China and 11.9 kg/ha in Japan) 4) Lack of appropriate crop rotation due to small farm size 5) Low levels of mechanisation 6) Illiteracy amongst farmers and consumers.

Furthermore, post-harvest losses cost farmers US$12.3 billion ever year due to poor storage and transportation facilities. Approximately 40% of total fruits and vegetables produced remain unsold due to poor storage and logistic infrastructure. The Union Budget 2019-2020 and 2018-19 had a higher focus on rural income and flow to agriculture with significant increase in agriculture credit, crop insurance, and promotion of food processing infrastructure, agro exports, irrigation, and credit facilities to related sectors such as animal husbandry, fisheries, and aquaculture.[8]

Recent initiatives by the Indian government to support the agriculture sector[9]

The Indian Government has taken various measures to achieve improvement in farm productivity and protect the small and marginal farmers from the vagaries of the weather. Some major steps include:

1. **Soil Health Cards:** Soil Health Card (SHC) scheme was launched by the Government of India in 2015. Soil Health Cards, which are issued every two years, provides every farmer

soil nutrient status of his land and advise them accordingly on the dosage of fertilisers and essential soil amendments that should be maintained for good soil health[10]. Since its launch, Soil Health Cards have been distributed to nearly 107.4 million farmers in the first cycle from 2015-17 and in the second cycle from 2017-19 it has been distributed to 114.5 million farmers.[11]

2. **PM Kisan Samman Nidhi (PMKISAN):** Under the scheme, vulnerable farmers, who own up to 2 hectares of land, will get direct income support of US$80 per annum. The income support will be transferred directly to the account of the beneficiary farmer in three equal instalments of US$26.6 each. To implement the scheme, around US$8 billion will be borne by the government to target 140 million farmers.[12]

3. **Kisan Credit Cards**: The Government proposed Kisan Credit Cards scheme in the Union budget 2018-19, to provide short-term credit support for animal husbandry, fisheries, and aquaculture farmers to help them meet their working capital needs and double their income by 2022.

4. **National e-Governance Plan (NeGP)** aims to digitalise government records to provide easy access to farmers over the internet. Services include, touch screen kiosks, agri-clinics, mass media, Kisan Call Centres, etc. The Department of Agriculture and Cooperation has developed 80 portals, applications, and websites for farmers. The portals include SEEDNET, DACNET, AGMARKNET (prices and arrivals in Mandis), RKVY (Rashtriya Krishi Vikas Yojana), ATMA, NHM (National Horticulture Mission), INTRADAC, NFSM (National Food Security Mission) and APY (Acreage, Productivity and Yield).[13]

5. **Crop insurance scheme:** In the Union Budget 2020-21, the outlay for Pradhan Mantri Fasal Bima Yojana (PMFBY) has been increased to US$2.8 billion, up from the budgeted US$1.9 billion in 2019-20. The coverage of the scheme has been increased to 50% of gross cropped area (GCA) in 2019-20.[14] This is expected to increase the risk appetite of farmers and lead to more spending on agri-inputs, fueling the growth of the sector.

6. **Minimum Support Prices** (MSP) for all unannounced Rabi crops to be hiked from 50% to 109% for year 2020-21. This will benefit the farmers by increasing the average incremental income.[15]

7. **Formation and promotion of Farmer Producer Organizations (FPOs):** On 19 February 2020, the Cabinet Committee on Economic Affairs gave its approval for 10,000 FPOs to be formed in a five-year period from 2019-20 to 2023-24 to ensure economies of scale for farmers. Support to each FPO will be continued for five years from its year of inception. This will benefit small and marginal farmers who do not have the economic strength to apply production technology, services, and marketing including value addition. Through the formation of FPOs, farmers will have better collective strength for better access to quality input, technology, credit, and better marketing access through economies of scale for better realisation of income.[16]

8. **Food processing:** The government has increased the allocation of Ministry of Food Processing from US$160 million in 2019-20 to US$164 million in 2020-21[17] and proposed to set up state-of-the-art testing facilities in all 42 mega food parks.

9. **M-Kisan** is a mobile-based agriculture advisory tool that connects local farmer with subject-matter experts via SMS facility in the local language. It also provides regular weather updates, pest and disease alerts, and real-time market price information to its users.[18]

10. **National Agriculture Market (eNAM)** is a pan-India electronic trading portal for agriculture commodities. It links the existing APMC (Agricultural Produce Market Committee) mandis to create a unified national market.[19] Keeping pace with the government's 'Digital India' push, 415 more 'mandis' will be added to the e-NAM platforms. Per eNAM data, so far, about 585 APMC markets in 16 states and 2 Union Territories (UTs) have been integrated to the e-NAM platform. More than 16.5 million farmers and 127,000 traders have registered at the portal. The trade on its portal has already reached US$12.1 billion.[20]

11. **Village storage scheme:** Government has announced the launch of village storage scheme for women, which will be run by Self-Help Groups (SHGs). The aim of the scheme is to provide holding capacity for farmers in villages.[21]

12. **Krishi Udan:** Ministry of civil aviation will launch the scheme for domestic and international routes to provide transportation solutions for perishable agri-products such as milk and fruits, helping farmers to reduce the wastage of products due to poor logistic infrastructure.[22]

13. **Kisan rail:** In the Budget 2020-21, the government announced the launch of Kisan Rail under a public-private partnership as part of its programme to boost farm income. It will be

helpful in developing a national cold supply chain for perishable goods such as meat, fish, and fruits.[23]

Future farming trends:
Indian agriculture has been witnessing growth, both in terms of value and volume, primarily driven by productivity improvement because of digitisation and favourable government policies. There are various trends that are shaping the future of Indian agriculture:

1. **Emergence of digital agriculture/farming:** Digital farming, which combines sensors, software, and precision machines, is still in its infancy but almost all large players are developing digital offerings or buying into assets. The focus is on technologies for an automated or remotely controlled climate, insect and disease monitoring, and treatment. In January 2019, for example a Brazilian company, Santos Lab, partnered with the Israel Aerospace Industries (IAI) to provide unique drone and advanced analytics solutions for precision agriculture application.[24]

   a. **Usage of unmanned drones**: Drones in agriculture can prove beneficial in improving the efficiency of agriculture. Drones are an alternative to a lack of skilled human resources and other heavy machines and tools, as well as economical to manage farming. There are several kinds of drones, including Crop Spraying Drones, NVDI Drones, Seeding Drones, and Surveillance Drones based on the purpose in agriculture. These drones are fully automated and can help in improving productivity. In 2019, the government released its Drone 2.0 policy, which focuses on Beyond Visual Line of Sight (BVLOS) operations of drones, thereby giving a major boost to its usage[25]. Further, the government is using drones to combat the recent locusts attack on crops of mustard, castor, cumin, and wheat spread over millions of acres in the states of Rajasthan and Gujarat.[26]

   b. **Application of blockchain technology**: With blockchain technology, all information related to the entire cycle of agricultural events can be fed onto blockchain to enable transparent and trusted source of information for the farmers. Farmers can get instant data related to the seed quality, soil moisture, climate and environment-related data, payments, demand and sale price, etc. all on one platform. Blockchain will also help in establishing a direct link between farmers and consumers/retailers enabling farmers to get the real price for their produce.[27] The Indian government's blockchain platform, ELEVEN01, KHETINEXT, a mobile-based agricultural solutions provider is experimenting with the use of blockchain technology to increase productivity and higher income for farmers in partnership with The International Crops Research Institute for the Semi-Arid Tropics (ICRISAT).[28]

   c. **Using AI/machine learning in the agricultural value chain**: In collaboration with the International Crop Research Institute for the Semi-Arid Tropics (ICRISAT), Microsoft has developed an AI-Sowing App powered by Cortana Intelligence Suite including Machine Learning and Power BI. The app sends sowing advisories through text messages to participating farmers on the optimal date to sow, without the need for any capital expenditure on the part of the farmers.[29] There has been a surge in the number of agri-tech start-ups that help farmers increase productivity using advanced IoT and machine learning technologies. In May 2018, NITI Aayog signed an agreement with IBM to develop a model for crop-yield predictions using AI so that farmers can be provided real-time advisories in some states.[30] NITI Aayog has developed a new national strategy for Artificial Intelligence in India which will focus on economic growth and social inclusion. To improve the crop sector, government will use technologies such as AI, remote sensing imageries, and modelling tools to reduce the time lag for settling of claims of the farmers under the Pradhan Mantri Fasal Bima Yojana (PMFBY).[31]

   d. **Data-driven decision making**: The Indian farm ministry is planning to develop a price-forecast model based on the supply and demand of crops primarily to provide market intelligence to farmers ahead of rabi harvests (winter crops) in 2019. With the help of this model and its data, growers can also select highly remunerative crops for sowing, thereby realising better price for their produce.[32] Data will continue to drive farming which could change usage, distribution, and manufacturing of inputs required in the Indian agriculture sector. Companies are increasingly trying to integrate satellite, weather, and IoT analytics with the agriculture sector to increase food security and insurance for farmers.[33]

2. **Emergence of Ag-Biological products/ Integrated Pest Management (IPM):** Integrated Pest Management (IPM) is a sustainable approach to pest management that combines biological, mechanical, physical, and chemical methods. It is an ecological approach and strives to significantly reduce the use of pesticides while maintaining acceptable levels of pest population. New products such as biological pesticides and seed treatment chemicals are being introduced, which require a small volume of chemicals for treatment as compared to normal crop protection chemicals. Department of Agriculture, Co-Operation & Farmers Welfare (DAC&FW) implement a scheme "Strengthening and Modernisation of Pest Management Approach in India" to promote Integrated Pest Management. Some of the benefits of IPM include safe quality produce and improved crop profitability owing to optimum pest control measures and appropriate use of crop protection solutions, fall in the intensity of pest infestations and reduced potential for problems of pest resistance or resurgence.

3. **Integrated farming systems**: The government is promoting the adoption of Integrated Farming Systems (IFS) by states, a holistic farming practice meant for all-round sustainable development of agriculture with animal husbandry, fishery, dairy, and other occupations related to core agricultural practices. The adoption will increase productivity by 2-3 times, create additional employment, save 40-60% resources, and ensure 100% household nutritional security. The government is promoting the Indian Council of Agricultural Research's (ICAR) model on integrated farming system across the country via agri-science centres to help small and marginal farmers tide over problems associated with climate change. ICAR has developed 45 integrated farming systems by including 15 agro-climatic zones.[34]

4. **Promotion of zero budget natural farming**: Under zero budget natural farming, neither fertiliser nor pesticide is used and only 10% of water is to be used for irrigation as compared to traditional farming technique. Farmers use only local seeds and produce their own seeds. Niti Aayog is pushing state to adopt the technique to combat the side effects of chemicals and fertilisers in crops.[35] However, many views on this concept have been expressed by various stakeholders.

Indian agriculture and its allied sub-sectors:

Indian agriculture industry has various allied sub-sectors, major ones being seeds, fertilisers and agrochemicals.

Indian seeds market was valued at US$4.1 billion in 2018 and is expected to reach US$9.1 billion by 2024.[36] Globally, India is the fifth-largest seeds market measured in value terms. In 2016, India ranked 16th globally in terms of fruit and vegetable seeds export. During 2018-19, total seeds exports from India was approximately US$110 million with top countries such as Netherland, USA, Pakistan and Bangladesh.[37] BASF has become the vegetable seeds leader in India after the acquisition of Bayer's global vegetable seeds business, mainly operating under the brand Nunhems®.[38]

The **Indian fertiliser industry** was estimated to be around US$71.8 billion in 2018 and expected to reach US$147.6 billion by 2024, growing at a CAGR of 12.3% during 2019-24.[39] The mandatory "Neem Coating" of urea has helped in increasing the farmer's income by increasing the productivity with less usage of urea.[40] GoI is planning to provide customised fertilisers to farmers based on the quality of soil to promote site-specific nutrient management and achieve maximum fertiliser use efficiency and cost reduction.[41] "Make in India" campaign is also encouraging the domestic fertiliser industry by reviving sick fertiliser plants.

INDIAN AGROCHEMICAL INDUSTRY

1. INTRODUCTION

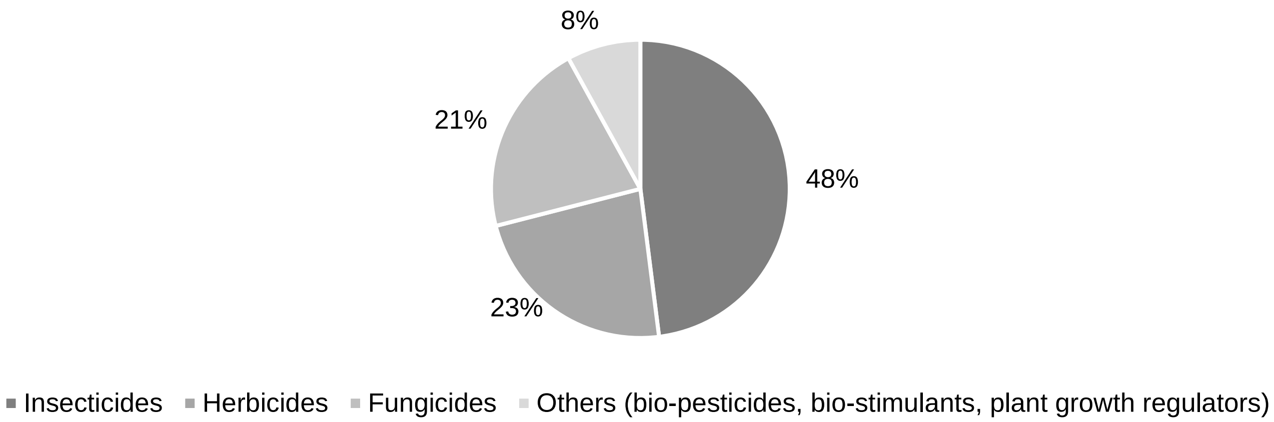
Market description

1.1. India is the fourth-largest producer of agrochemicals globally, after US, Japan, and China. The Indian Agrochemicals market was expected to reach US$5 billion in FY2019 with exports contributing more than 50% share. Indian Agrochemical market has a stable growth with potential of growth in exports.[42] The total installed capacity of the agrochemical industry in India is expected to reach 493,700 tons in 2020. Global agrochemical industry has witnessed a wave of consolidation in the last few years. The industry is now dominated by four major players capturing 65% market share. ChemChina has the highest market share of 22% followed by Bayer CropScience and Monsanto with 20% share.[43] This consolidation in the global industry is impacting the Indian players as well, in terms of competitive positioning and market expansion.[44]

1.2. Around 20-25% of crop production in India is lost due to insects, weeds and diseases, with total value of crops lost annually is estimated at US$12 billion.[45] While the global average consumption of pesticides is 3 kg/ha, India is consuming only 0.3 kg/ha. Furthermore, the area treated with crop protection products is only 35% indicating, untapped potential for pesticide usage in crop cultivation.[46]

1.3. The Indian Agrochemicals market is dominated by Insecticides. Herbicides is the fastest-growing segment.

Figure 1: Split of Indian Agrochemicals market – 2019[47]

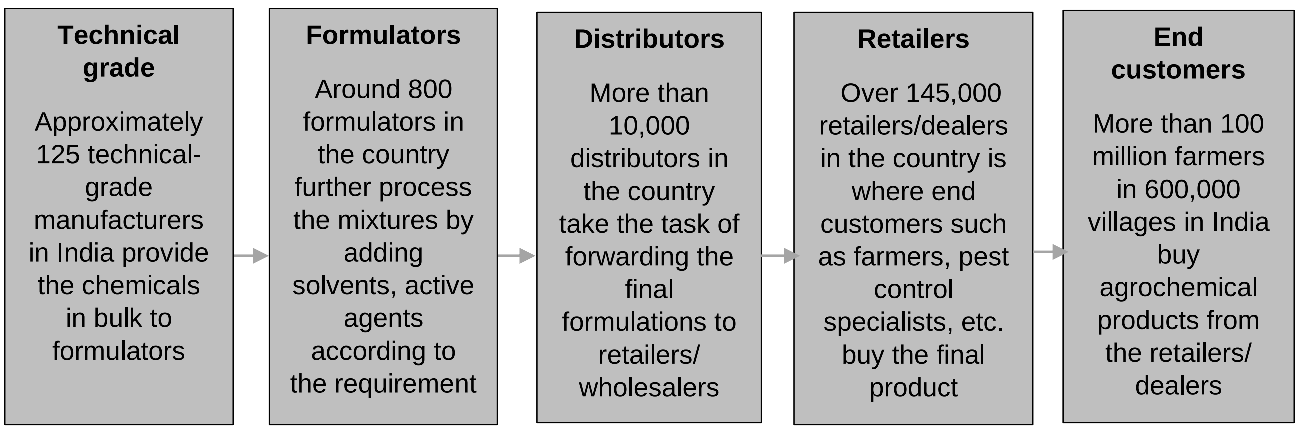


1.4. Reducing labour availability and rising wage rates are growth drivers for herbicides with rice, wheat, sugarcane, and soybean being the major application areas. However, the sale of herbicides is seasonal. Fungicides are mostly used for fruits, vegetables, and rice. The key growth drivers for fungicides include a shift in agriculture from cash crops to fruits and vegetables. Bio-pesticides including bio-stimulants offer significant growth opportunities due to increasing concerns of safety and toxicity of pesticide residues, stringent regulations, and government support.

1.5. Agrochemicals going off-patent – An opportunity for Indian generic players

During the period 2017-2022, patents of 26 pesticides are expected to expire which include 13 herbicides, 4 insecticides, 8 fungicides and 1 safener[49]. Indian generic agrochemical manufacturers can capitalise on this opportunity. They should also look to increase the export of these generics to further penetrate the global market. To lay a strong export foundation, Indian Agrochemical manufacturers could strengthen their marketing network by partnering with local players in the foreign markets. The Indian Agrochemical manufacturers could also explore collaborations, merger and acquisitions to expand their worldwide reach. The gradual shift to generic crop protection chemicals and products going off-patent are likely to open up attractive growth avenues for the Indian agrochemical industry. The government has set a target of US$60 billion by 2022 for agricultural exports by the agriculture export policy.[50]

Figure 2: Agrochemicals distribution network in India[48]



Recent Developments

1.6. "Make in India" initiative

"Make in India" is an Indian Government initiative to encourage companies to manufacture their products in India. The initiative is aimed at enhancing the ease of doing business in India and is expected to attract foreign capital. India's ease of doing business ranking jumped from 77 in 2019 to 63 in 2020[51]. Government could also consider extending support in terms of incentives/tax benefits to agrochemicals, as given to fertilisers and seeds, as all of them facilitate the agriculture sector. While the government's thrust is rightly on "Make in India", keeping in mind the market dynamics of supply and demand and farmers' needs, the government should allow adequate import of the quality technical grade material too to meet requirements. To attain the goals of the initiative, the government should expedite the policy implementation process so that the benefits accrue to the players in a timely fashion. Conversion of technical material to formulation also generates considerable employment locally and hence, should be encouraged as part of the "Make in India" campaign.

1.7. India as a global manufacturing hub

In the wake of tightening environmental norms in China, global players manufacturing in China are facing increased losses due to plant shutdowns and increasing input prices. This has led to these global players looking out for alternative locations, viz. India as a manufacturing hub. This will in turn bring increased FDI to India in the form of capital and more importantly advanced technical know-how; leading to greater production and greater exports. In addition, India has a large pool of qualified and skilled chemical engineers which constitute the backbone in this technology-oriented segment. The government has recognised the immense potential and is focussing efforts on developing R&D capabilities, technical skill training, infrastructure reforms, etc. to support the endeavour to create India as a global manufacturing hub for Agrochemicals. The government should encourage agrochemical companies to mandatorily adopt Good Manufacturing Practice (GMP).

1.8. Impact of GST implementation

Under the new GST regime, agrochemicals are now taxed at 18% while chemical fertilisers are taxed at 5%. In the pre-GST era, agrochemicals attracted an excise duty of 12.5% and VAT of 5% for intra-state sales or CST of 2% for inter-state sales. As a result, there has not been any significant impact on taxes payable. The petroleum sector, the largest source of feedstock for the chemical industry, is out of GST. Hence, the raw material will continue to have the cascading effect of indirect taxes.[52]

1.9. Foreign collaboration

In November 2019, the National Institute of Agricultural Extension Management and the German Agriculture Academy signed an agreement for collaboration in agriculture technical and professional training.[53] In February 2019, India signed an MoU with Ukraine for cooperation in agriculture and food industry.[54] Australia's Western Sydney University forged a partnership with the Indian Council of Agricultural Research (ICAR) and 13 state agricultural universities to invest AUD5 million to leverage new research and developments, which is expected to double farmers' income by 2022.[55]

India also signed multiple MoUs towards trade cooperation in the agricultural space with Netherlands, the second-largest exporter of agricultural products in the world, after US, and known for its smart logistics, storage, and packaging technologies that keep food fresh longer.[56] United Arab Emirates and Saudi Arabia are planning to make India as a base for food security and invest in both organic and food processing industries.[57] India also signed an MoU with Lebanon and Egypt aimed at boosting agriculture production as well as productivity by getting access to best practices and the global market.[58] India and Israel agreed to jointly develop new crop varieties and share post-harvest technologies, following the success of the 10-year-old Indo-Israeli Agriculture Project (IIAP).[59]

EU has also been collaborating with India on extensive EU legislation on pesticides, MRLs, etc. in different forums. The German Agribusiness Alliance (GAA) and Agriculture Skill Council of India (ASCI) signed a MoU with the objective of jointly developing the establishment of 'Indo-German Centers of Excellence in Agriculture', a platform for practical skill development in Agriculture in India.[60] In 2019, EU reduced maximum residues level for Tricyclazole to 0.01 parts per million (ppm) from 1 ppm for all crops effective 1 January 2018, resulting in a 60% decline in Basmati rice exports to the EU. The government has asked Basmati exporters to adhere to the norms for exporting rice to the EU.

The Indian Government signed a Memorandum of Understanding (MoU) with many African nations to boost Agricultural trade and technology transfer agreements. Notably on the same lines the Indian government has also proposed an agreement with South Africa.[61] In addition, the government has allowed 100% FDI under the automatic route in the agriculture and allied sectors industry.

Some leading European companies in India in the agrochemical sector are BASF, Syngenta, Bayer CropScience, and Rabo Equity Advisors. Further, there are a few more major agrochemicals companies from Europe that are active in the Indian agrochemicals market.

2. KEY ISSUES AND RECOMMENDATIONS

2.1. Issue/Objective: Focus on Exports:

India is the fourth-largest producer of agrochemicals worldwide after the US, Japan, and China, and is the 13th largest exporter of pesticides globally. Brazil, the US, France, and Japan are the top importers of Indian agrochemical products.[62] Agrochemical exports from India have increased from 253,000 tons in FY2014 to 461,000 tons in FY2019 with a CAGR of 12.8% during this period.[63]

Recommendations for government:

Currently there is slightly over 50% share of exports in India's agrochemical production. CRAMs business opportunity, competitive manufacturing cost, and scarcity of supply from China amid anti-pollution measures taken by the Chinese Environmental Protection Agency and the ongoing impact of COVID-19 in China could further help India become an alternative source (other than China) for supply of agrochemicals globally. To realise this, the government needs to increase its focus on making policies favourable for exporters. The Government of India has already taken various initiatives to boost exports. For instance, Post Export EPCG duty credit scrip scheme, Market access initiative (MAI) scheme and freight assistance to exporters. These schemes are helpful for exporters to increase the exports.[64]

However, the government needs to reduce the delays in environmental clearance and other regulatory approvals to further propel agrochemical sector exports.[65]

2.2. Issue/objective: Regulatory hurdles:

Stringent environmental regulations requiring time-consuming registration procedures increase the cost of developing new products and simultaneously delay the introduction of new products in the market. Further, the registration of a product in India for the first time u/s 9(3) of the Insecticides Act, 1968 is very tedious, requiring the company to do field trials, lab tests, undertaking product stewardship and risk management for the product. This generally takes 4-5 years of time. On the other hand, the process u/s 9(4), registering the product as "Me too" in India usually takes less than 1-1.5 years as data guidelines have been relaxed. This discourages research-based companies from introducing new products in the market.[66]

Recommendations for Government:

Process of registration by Central Insecticide Board (CIB) and Registration committee (RC), the regulatory body under the Ministry of Agriculture, needs to be streamlined in a way that so that the period for getting a new registration is minimised while meeting safety-related requirements. The guidelines need to be clearly defined by the CIB experts to avoid interpretation challenges, which lead to confusion, thereby adding to the complexities for agrochemical companies. Fast-track approvals and clearances should be provided by regulatory bodies to encourage companies to introduce new green chemistry products. It is encouraging to note that the 'regulators' have adopted "crop grouping" and to encourage label extensions and thereby facilitate a proper product stewardship, are facilitating safe food production. India should implement Organisation for Economic Co-operation and Development (OECD) requirements in letter and spirit and encourage data generation under Good Laboratory Practice (GLP). Peer review on toxicological data should be adopted by India similar to the pattern adopted by OECD member countries. Industry players should form consensus to initiate a dialogue with the government over rules and regulations with the support of industry associations.

2.3. Issue/objective: Focus on green chemistry and incentivise agrochemical manufacturing:

Recommendations for government:

Green chemistry and sustainable agriculture are inherently intertwined. Government should focus on bringing green chemistry to the farms, which is safe to the environment and also to human beings with characteristics of less persistence in soil, water, and plants. Minor change in formulations with replacement of safer intermediates both synthetic and natural should be permitted with ease. Biological products including Bio-pesticides, bio-stimulants, and safer green chemistry molecules should be given priority for introduction. Companies should also invest in R&D activities to develop new green routes of chemical synthesis. Further, the State and Central Government should encourage the setting up of domestic agrochemical industries through incentives and tax holidays/exemptions etc. to complement the Indian Government's "Make in India" initiative. Going forward, the government needs to continue to provide infrastructural support to the industry to develop effective marketing and distribution solutions. The applicable GST too should be reduced from the current 18% to 5%.

2.4. Issue/objective: Early implementation of new Pesticides Management Bill, 2018: The new draft Pesticides Management bill has been cleared by the cabinet and it is awaiting the parliamentary approval. The bill introduces right to compensation for farmers if the pesticide fails to provide the expected performance and strict punishment for manufacturing spurious products.[67]

Recommendations for government:

The government should now approve this bill as soon as possible to streamline the pesticide industry and to ensure greater transparency in the regulation of the Indian pesticide industry**.** Furthermore, data protection for a minimum of five years must be included in the Pesticide Management Bill to encourage innovations.

2.5. Issue/objective: To extend data protection for innovators in the Indian pesticide industry:

The global agrochemical research-based companies have to wait for 9-10 years and pass more than 100 safety tests to bring a new molecule into the market with a cost of minimum US$250 million.[68]

Recommendations for government:

The key concerns of pesticide manufacturers are time-bound grant of licences, grant of registration for new pesticides molecules, accreditation of private laboratories to function as Central Pesticide Laboratories (CPL), elaborate procedure for withdrawal of pesticide samples and making punishments more stringent for misbranded, sub-standard, and spurious pesticides.[69] To safeguard the rights of innovating companies, the government needs to bring in data protection as practiced globally so that companies follow certain guidelines or procedures vis-à-vis cost incurred by the original registrant per the existing global practice.[70]

2.6. Issue/objective: Low investment in R&D:

The industry is facing a serious challenge due to increasing R&D costs. There has been lack of data protection for innovators developing new molecules. This prevents companies from investing in R&D activities and they tend to focus more on the generic products, which require low investments. Indian companies spend roughly between 1% and 2% of their revenue in R&D compared with the global MNCs, which invest about 8%–10% of their revenue.

Recommendations for the government:

Government needs to encourage R&D activities to facilitate new innovations in the Indian market. The industry players should also invest in R&D activities to develop new and green routes of chemical synthesis. New innovations or developments should be recognised, and companies should be incentivised for the same. Additionally, the government must provide a conducive business environment for the agrochemical companies to set up R&D labs in India. Government should encourage labs to adopt Good Laboratory Practice (GLP).[71]

2.7. Issue/objective: Low awareness among farmers:

Only 25%–30% of Indian farmers are aware of agrochemical products and their usage, and there is a lack of reading of labels by farmers.[72] Per capita consumption of pesticides in India is only 0.3 (kg/ha) as compared to 13 (kg/Ha) for China and 11.9(kg/Ha) for Japan due to lack of awareness among farmers for the cost benefit ratio for use of pesticides.[73] Hence, product stewardship is of paramount importance.

Recommendations for the government:

The Indian Government has made it mandatory for dealers setting up insecticide/pesticide shops to possess a graduate degree in agriculture science or biochemistry or biotechnology or life science or graduation with either chemistry or botany or zoology so that farmers are educated about the usage of agrochemicals.[74]

Government should ensue it is implemented in letter and spirit. Extension services help farmers and other rural population to gain access to knowledge, information, and technologies. Government should enhance extension activities to increase awareness among farmers for safe and right use of agrochemicals. Extension services rendered by the private sector should be incentivised. Further, the government should collaborate with private companies in spreading awareness and educating the farmers about the appropriate use of pesticides by organising awareness camps/industry conferences more frequently.

2.8. Issue/objective: Presence of counterfeit/spurious products:

In India, 10%-15% of pesticides sold are spurious per industry sources. It is estimated that the size of the counterfeit pesticide market is around US$270-330 million.[75] Use of non-genuine products leads to loss of revenue to farmers, agrochemical companies, and the government.

Recommendations for the government:

It is noteworthy that the government is adopting standardised label/leaflets along with a QR code for traceability. This will help in curbing the sale spurious products to the farmers. The companies should also invest in technology to help end-users distinguish and validate the authenticity of the original products. Further, Bio-stimulants need to be encouraged but brought under regulation to discipline the market. Hence, the government is considering the regulations to govern the bio-stimulants market.

2.9. Issue/objective: Negative perception linked to the Agrochemical industry:

There has been an increase in the number of cases breaching MRLs in India mainly because of indiscriminate use of pesticides by farmers; this has affected exports of rice, fruits, and vegetables to many countries in the Middle East, the EU, and the US. There have been several reports surfacing online that link increased cancer risk to pesticides such as glyphosate.[76]

Recommendations for the government:

Industry players need to take up the primary onus of enhancing the image of the Agrochemical industry by creating the right kind of perceptions through public awareness. Support from the government will also be vital in this regard by showcasing the importance of the industry in various public forums. Adequate awareness regarding the new MRLs should be spread by the Food Safety and Standards Authority of India (FSSAI) to bring down the number of cases of breaching of MRLs. This adherence will boost the export of agricultural commodities. The industry is already actively taking up with few NGOs/governments on publications related to cancer, backing them with scientific evidence.

2.10. Issue/objective: Health, Safety, Security and Environment (HSSE) implementation

Recommendations for the government:

The government and public bodies must incentivise agrochemicals units to adhere to safety requirements and abide by global standards, especially related to Good Manufacturing Practices. HSSE guidelines framed by the competent authority in the government should be implemented at the earliest.

CONCLUSION

The Indian government is investing in various farmer welfare schemes and creating more avenues that will help in achieving its aim to double the income of farmers by 2022, such as a 16-point agenda that has been declared in the Union Budget 2020-21. The government should deploy sustainable long-term productivity improvement measures to get out of the vicious cycle of loan waivers.

India has the potential to become an export hub for contract manufacturing and custom synthesis in agrochemical manufacturing. There are significant growth opportunities owing to India's low-cost manufacturing base, under-penetration of pesticide uses in domestic market, key products going-off patent globally, plant shutdowns in China, the recent impact of COVID-19 on supply, especially from China, huge export potential and growth in herbicides and fungicides sub-sectors especially.

In the coming years, the agrochemical industry should focus on developing new processes and products with sustainability as the core principle. This requires developing a collaborative platform in which the academia, government and regulatory bodies, farmers associations, manufacturers, industry associations and farmers come together to promote safe and judicious usage of pesticides.

On the other hand, there are many challenges, which need to be addressed to give a fillip to this sector, the most critical ones are the regulatory reforms to be pursued by the government, infrastructural investments, incentivising R&D, ensuring data protection to innovators, and educating the most important stakeholder—“the farmer” about the proper usage of agrochemicals.

In the light of the growth drivers of the Indian Agrochemicals industry, the government’s push to the sector and the need for bolstering digital capabilities. Indian players are well poised to reap the benefits of the growth pockets within the market. The future is bright for Indian Agrochemicals industry, as a facilitator of the Indian Agriculture and of Indian economy. The Agrochemicals sector can certainly help the Government in achieving its aim of doubling farmers’ income by 2022.

ENDNOTE

1. Source: Indian Agrochemical Industry: Role of Agrochemicals in Sustainable Farming, FICCI, July 2019
2. Source: Agriculture and Allied industries report, Indian Brand Equity Foundation (IBEF), November 2019
3. Source: Indian Agrochemical Industry: Role of Agrochemicals in Sustainable Farming, FICCI, July 2019
4. Source: Union Budget 2020-21 Analysis, PRS Legislative Research, accessed on 4 March 2020
5. Source: Budget 2020, Govt unveils 16-point action plan to revive agricultural sector, Business Today, 1 February 2020
6. Source: Indian Agrochemical Industry: Role of Agrochemicals in Sustainable Farming, FICCI, July 2019
7. Source: Quartz India, 29 January 2018
8. Source: Budget 2020, Govt unveils 16-point action plan to revive agricultural sector, Business Today, 1 February 2020
9. Source: Union Budget 2018-19 and Philip capital, 1 February 2018
10. Source: Krishi Jagran, 03 December 2018
11. Source: Soil Health card website, accessed in March 2020
12. Source: Business Standard, 1 February 2020
13. Source: Press Information Bureau, Government of India, accessed on 2 March 2020
14. Source: BusinessLine, 11 February 2020
15. Source: Business Today, 23 October 2019
16. Source: Press Information Bureau, Government of India, 19 February 2020
17. Source: OpenBudgetsIndia, Union Budget (2020-21), accessed in March 2020
18. Source: mKisan website, Government of India, accessed in March 2020
19. Source: Union Budget 2018-19 and Philip capital, 1 February 2018
20. Source: Economic times, 22 January 2020
21. Source: MoneyControl, 1 February 2020
22. Source: CNBC News, Budget 2020, 1 February 2020
23. Source: CNBC News, Budget 2020, 1 February 2020
24. Source: Global Agriculture Drones and Robots Market, BIS Research, accessed on 1 March 2020
25. Source: Geospatial world, 21 January 2019
26. Source: Factor Daily, 04 July 2018 and Krishi Jagran, 26 October 2018
27. Source: Medium, 06 June 2018
28. Source: DowntoEarth, 28 May 2019
29. Source: The News Minute, 21 January 2019
30. Source: The Hindustan Times, 13 May 2018
31. Source: AnalyticsIndiaMag, 27 December 2019
32. Source: Cogencis website, 31 January 2019
33. Source: Social story, 30 May 2017
34. Source: Business Standard, 28 February 2018
35. Source: Indian Express, 22 February 2019
36. Source: imarc press release, accessed on 1 March 2020
37. Source: APEDA, agriXchange, accessed on 1 March 2020
38. Nunhems website, accessed in April 2019
39. Source: imarc website, accessed on 25 February 2020
40. Source: Press Information Bureau, Government of India, Ministry of Chemicals and Fertilizers, 24 March 2017
41. Source: Times of India, 27 June 2018
42. Source: A report on Indian Agrochemical industry, FICCI, July 2019
43. Source: Deutsche Bank report, accessed on 25 February 2020
44. Source: Deutsche Bank report, accessed on 25 February 2020
45. Source: Indian Agrochemical Industry: Role of Agrochemicals in Sustainable Farming, FICCI, July 2019
46. Source: Care Rating report, May 2017
47. Source: Industry estimates
48. Source: Indian Agrochemical Industry: Role of Agrochemicals in Sustainable Farming, FICCI, July 2019
49. Source: Doubling Farmers' Income: Role of Crop Protection Chemicals & Solutions, FICCI, July 2018
50. Source: Indian Agrochemical Industry: Role of Agrochemicals in Sustainable Farming, FICCI, July 2019

51. Source: India Today, 24 October 2019
52. Source: Money control, 28 August 2017 and LiveMint, 30 June 2017
53. Source: Business Standard, 1 November 2019
54. Source: PMINIDA, News, 6 February 2019
55. Source: Economic Times, 08 December 2018
56. Source: Inc42, 09 January 2019
57. Source: Economic Times, 13 January 2019
58. Source: Krishi Jagran, 11 October 2018
59. Source: Livemint, 12 January 2018
60. Source: National skill Development Corporation – Agriculture skill council of India (ASCI), 5 October 2015
61. Source: The Hindu, 5 July 2016 and Economic Times, 23 September 2016
62. Source: Chemical Industry analyst coverage, Thomson Reuters, Morgan Stanley 2018
63. Source: Indian Agrochemical Industry: Role of Agrochemicals in Sustainable Farming, FICCI, July 2019
64. Source: The Economic Times, 12 August 2019
65. Source: Business Standard, 2 October 2018
66. Source: MoM, 371 RC, held on 16 December 2016
67. Source: Business Standard, 24 February 2018
68. Source: A report on Indian Agrochemical industry, FICCI, November 2015
69. Source: Crop Life India, 18 September 2017
70. Source: Business Standard, February 2018
71. Source: BASF News release, 3 March 2017
72. Source: A report on Indian Agrochemical industry, FICCI, November 2015
73. Source: Indian Agrochemical Industry: Role of Agrochemicals in Sustainable Farming, FICCI, July 2019
74. Source: Press Information Bureau, Government of India, November 2015
75. Source: Industry sources
76. Source: The Economic Times, 17 February 2020

NOTE

Alcoholic beverages

Acknowledgements: Sunil Duggal
(Pernod Ricard) – Chairman,
Alcoholic Beverages Sector Committee & its Members

EXECUTIVE SUMMARY

With the NDA Government coming back to power with a thumping majority and Prime Minister Modi at the helm of affairs it was quiet natural that there would be a second wave of reforms in the offing to make India vibrant, dynamic and stronger with the overall objective of achieving a higher growth rate and placing India in the top league of Nations. With a stable Government at the Federal level it was evident that Modi 2.0 would usher in several new initiatives to make Indian Economy far more resilient and competitive with greater bilateral cooperation between the friendly Nations viz. EU, US, UK, Australia and so on. The thrust would continue in further liberalisation of the Indian economy, Atmanirbhar Bharat, Ease of doing business, Health, Education, use of superior technology, bridging the digital gap, greater integration with the global supply chain and greater cooperation between the States and the Centre.

The year 2019 saw Indian alcoholic beverage business gaining some of its lost grounds due to robust growth of the Indian economy, however rising prices of raw materials and multiplicity of taxes has taken the sheen out of it. Increasing taxes and duties along with multiple regulatory challenges are key features of this sector which still remains to be addressed.

Despite of above challenges, India still maintained its dominant position as one of the fastest growing alcoholic beverage market globally. Rapid urbanisation, growing middle class population with rising spending power, and demand for premium products are some of the drivers behind the increase in consumption of alcohol in India.

With the onset of COVID-19 pandemic, like other sectors, alcoholic beverage sector too faced a major setback. With the State sponsored lockdown, which was absolutely necessary at that point in time, had a significant impact on the economy. Most of the economic activities came to a grinding halt along with manufacturing and sale of alcoholic beverage products for almost two months. Even after the lockdown was withdrawn in a phased manner since May 2020, the economy is marred with significant drop in GDP growth due to low economic activity, job losses, complete closure of tourism and hospitality sector, suspension of air travel and hence duty free business. It’s a long haul for the alcoholic beverage sector to reach its pre-COVID-19 stage.

Today liquor companies continue to suffer with State imposed additional COVID-19 cess besides high incidence of import tariff, ever increasing State levies such as excise duties and fees, low pricing flexibility and delay in payments are common in most of the States. Rising taxation without price rise have led to drop in margins in most of the markets. Increasing pressure on cost of inputs, additional burden of GST on inputs, delay in decision making by the Corporations/States are some of the inherent challenges of the alcoholic beverage Industry in India.

States reliance on revenue from alcohol continues unabated. With the introduction of GST, resources left under the direct control of the States is restricted alcohol and Petro products. With the growing dependence on revenue from alcohol, States continue to raise its share of revenue by increasing tax and levies without compensating the manufacturers by giving price rises. Such high prices are expected to fuel counterfeits posing high health risk to consumers, rising incidence of illicit liquor, etc.

The loss of sale during lockdown lead to a significant drop in Excise and VAT revenue for the States leading to increase in taxes in most of the States on the alcoholic beverage products which lead to further drop in sale of alcoholic beverage products. Many State while realising the drop in sale rolled back the COVID-19 cess but many States continue to do so.

Another interesting feature of the Indian alcoholic beverage Industry is the story of **“premiumisation”**. More and more consumers used to look for premium alcohol within the category. With rising aspiration and increasing disposable income, consumers were upgrading towards premium ones in the country, within IMFL or to international brands. In order to meet the aspiration of discerning consumers companies in India were introducing premium products which they feel would drive the growth in the next decade. Various companies over the last couple of years have introduced several premium brands to get a share in the premium category which are significantly adding to their bottom line. More and more people in the urban areas were looking for premium products and were willing to pay for it. However, the pandemic has completely watered down the dreams of the brought a

The revenue from the alcoholic beverage segment forms a large chunk of revenue for most of the States to carry out development activities. Apart from Bihar, Gujarat, Mizoram and Manipur, where liquor is prohibited, revenue from alcoholic beverage industry is a major contributor to state exchequer – with over INR190,000 crores revenue for the year 2017-18 from Excise duty and VAT and it is expected that the revenue for the alcohol would surpass INR 2,20,000 crore for the year 2018-19. It is estimated that alcoholic beverage Industry would provide employment to more than 2.5 million people directly and indirectly.

The alcoholic beverage industry – as a substantial revenue contributor to State exchequer and a provider of employment to millions – awaits fair treatment to be accorded to the industry by resolving some of the key issues by accepting the recommendations made by the industry.

INTRODUCTION

India is one of the key markets for the global alcoholic beverage industry, consistently occupying a spot amongst the leading countries.

The total consumption of wines and spirits (9 litres branded) in India during 2019[1] are as follows:

i. Imported wines volume remains primarily flat at 0.5M, out of total 2.8M cases for wine in 2019
ii. Of the Total 345 million cases of Spirits market; Whisky accounted for 220 million cases followed by Brandy for nearly 73million cases, Rum 42million Cases, Vodka 8million cases, GIN accounting for 2million cases;
iii. Only 1.7 million cases of spirits (whisky, gin, vodka, rum, brandy, etc.) were imported into India in 2019.
iv. Of the total spirits imported into India in 2019, imported Whiskey (BIO) accounted for only 1.2 million cases.
v. Out of the above 220 million cases, Bottled in India (BII) Scotch whisky is about 3.3 million cases, made with the help of bulk imports of whisky.;

The marginal increase in consumption of spirits and wines in 2019 as compared to 2018 (337 million cases spirits market) could be attributed to factors such as continued levy of high taxes and duties – both at Central and State levels, States raising taxes, additional levy, etc.

The marginal increase in consumption of spirits and wines in 2018 as compared to 2017 (315 million cases spirits market) could be attributed to factors such as continued levy of high taxes and duties – both at Central and State levels, States raising taxes, additional levy, etc.

In addition to high incidence of import duty imposed at the central level for imported products, alcoholic beverages are also subject to varying rates of excise duty, and value added tax or sales tax at the state level. Accordingly, the total incidence of tax (including import duty and local taxes) on products imported into India varies from 300% to 500%.

The challenge for 'Made in India' as well as imported products gets compounded due to following factors:

i. GST – Alcohol being kept outside the ambit of GST.
ii. Taxation on Extra Neutral Alcohol kept open by GST Council leading to uncertainties.
iii. States unwillingness to offer price increases in spite of:
    a. increased production costs by much as 33%
    b. increase in excise duties and Imposition of COVID-19 Cess
iv. Levy of GST on inputs and services

Furthermore, the producers are forced to bear the brunt as they cannot pass on the increased costs to the consumers leading to shrinking margins, reduced consumption and consequently fall in revenue for the States.

The Indian alcohol industry is significantly different from markets in other large countries. The market architecture varies from one State to another in terms of taxation, regulation, legalisation, production and promotion. It is like operating in 36 different countries (29 States and 7 Union Territories). The tax structure in two neighbouring States is typically different, resulting in a strong incentive for unauthorised interstate movement of alcoholic beverages. Even the legal drinking age varies from one State to another.

Distribution and logistics are under developed in most Indian states. More and more States are opting for State owned corporations which are managed in a better way. The model varies from part/fully owned by the state government and part/fully owned by private enterprises. Distribution in the southern States like Tamil Nadu, Telangana, Andhra Pradesh and Kerala are fully owned and managed by the State government run corporations.

Any form of advertising of alcoholic beverage products is strictly 'prohibited', thereby making brand visibility and/or introduction of new products extremely difficult. This has led to the emergence of brand extensions.

Star rated hotels, stand-alone restaurants and duty-free shops (travel retail) have traditionally been the key channels of sale for international alcoholic beverages. Star-rated hotels and stand-alone restaurants can spend only up to 3% (reduced from 10%) of their annual foreign exchange earnings to purchase capital goods and duty-free alcoholic beverages. Travel retail continues to be a channel for international brands sales in India and increase in international travel has boosted such sales. However, the high incidence of customs duty on imported alcoholic beverages limits the potential of increased availability and not least depriving potential consumers with an opportunity to upgrade to choicest wines and spirits.

1 KEY ISSUES AND RECOMMENDATIONS

1.1 Reduction of Basic Customs Duty (BCD) on alcoholic beverages

The biggest impediment for the development of the imported alcoholic beverages market in India (other than beer made from malt at 100%) remains the high incidence of Basic Customs Duty (BCD) pegged at 150%, before the application of state levies and duties. This is very high by international standards when compared to China (5%), Brazil (20%) and the average G20 countries duty of 30%.

According to an analysis, the gradual reduction of China's tariff from 65% to 5% between 2000 and 2007, while maintaining domestic taxes at relatively low levels by regional standards, led to a massive increase in legal spirits imports (from US$30 million to roughly US$500 million), thereby also vastly increasing revenue collection (from US$30 million to US$265 million, counting tariff + special consumption tax + VAT). Regarding Cognac imports only, government revenues soared by 785% between 2000 and 2007. The revenues went up by nearly 1500% as regards wine imports.

In India, the high incidence of basic customs duty coupled with state duties/taxes acts as a major bottleneck for premiumisation and the growth of the imported alcoholic beverages. Products becoming excessively expensive beyond the reach of majority of Indian consumers renders them non-saleable. The high level of duties and taxes also leads to a flourishing grey market resulting in a loss of revenue for both the central and state governments. Moreover, there is also a high influx of counterfeit products in the market, which undermines brand equity, deceives consumers and poses a high health risk for consumers.

The size of the imported alcoholic beverage segment as compared to domestic production is currently negligible. (1% of the total consumption of legitimate commercial alcohol is imported).

RECOMMENDATION:

There is a need to rationalise the import tariff in a phased manner from 150% to 75% and ultimately to 30% over a period of 2-3 years. However, to protect of the domestic alcoholic beverage industry, an appropriate threshold limit has to be determined in consultation with the stakeholders.

1.2 Clarity on taxation Extra Neutral Alcohol (ENA)/Grain Neutral Spirits (GNS)

Extra Neutral Alcohol (ENA)/Grain Neutral Spirit (GNS) is the principal raw material for the production of India Made Foreign Liquors (IMFL). While alcohol for human consumption is outside the purview of Goods and Service Tax (GST) per The Constitution, however there is a lack of clarity on the taxation of ENA/GNS. Prior to the introduction of GST, ENA/GNS was under VAT regime with NIL Central Excise duty. Post GST Industry expected that it would continue under VAT but there is a lack of consensus between the States and the Federal Government and the matter is pending with the GST Council. The decision to maintain Status Quo taken at the 20th GST Council meeting held on 5 August 2017 still continues leading to an uncertainty regarding taxation of ENA/GST. Despite of Industry paying up VAT on ENA/GNS, GST Officials keeps chasing us to pay up GST on ENA/GNS ignoring the decision of the GST Council.

RECOMMENDATION:

We humbly request the GST Council to take up the matter and decide once for all whether ENA/GNS is under GST or VAT and bring in the required clarity and certainty. And since the industry is paying VAT on ENA/GNS from 1 July 2017, the applicability of GST on ENA/GNS, if any, should be prospective and commensurate with the rate prior to GST considering the fact that final product is outside GST.

1.3 Establishment of a National Alcohol Regulatory body

There is a need to bring greater transparency in operating environment of the alcohol industry; a greater degree of transparency will curb corrupt practices, which in turn shall lead to plug the leakage of the official revenue that should effectively flow to the country's exchequer. Studies have revealed that the unrecorded alcohol generates tax equivalent revenue which is almost 50% of the official tax revenue.

The industry is a large consumer of the agriculture produce and hence linked to the agriculture sector at the backend. The industry supports tourism in the country. It contributes revenues in excess of INR200, 000 crores and an estimated 2.5 million jobs directly and indirectly put together.

Per the Constitution of India, alcohol is a state subject; it falls under entry 8 and 51 of the List II of seventh Schedule of the Constitution of India:

Entry 8. Intoxicating liquors, that is to say, the production, manufacture, possession, transport, purchase and sale of intoxicating liquors;

Entry 51. Duties of Excise on the following goods manufactured or produced in the State and countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India:—

a) alcoholic liquors for human consumption;

b) opium, Indian hemp and other narcotic drugs and narcotics,

c) but not including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph

d) of this entry.

Presently, the State Governments control grants of licenses to manufacture, regulate prices both MRPs and ex-distillery prices, distribution of alcohol and in some States even retailing of alcohol, at times by creating state monopolies. Despite stringent controls put forward by the State government, there are challenges in terms of counterfeit, illicit liquor which leads to revenue loss and risk to precious lives.

The Central Government should set up a National Alcohol Regulatory body to control and regulate manufacturing of alcohol along the lines similar to the Central Electricity Regulatory Commission.

Key benefits arising out of the proposed establishment:

- By enforcing transparent ways of doing business - plugging revenue leaks and curbing/eliminating corrupt practices. It will address revenue leakages by providing documentary audit trail which will increase government tax collection, reduce black money generation and corruption, curb unreported/undeclared sales, reducing illicit and spurious alcohol thereby curbing incidence of deaths from consumption of counterfeit products.
- The State governments will retain its control on the revenue generated from possession, transport, purchase and sale of alcohol through state Excise laws.

RECOMMENDATION:

A National Alcohol Regulatory body should set up by the Central Government to control and regulate manufacturing of alcohol along with following suggestions on carving primary role of the Authority.

- The regulatory body WILL NOT interfere with state level taxes and levies but only play an advisory role.
- The regulatory body shall – in consultation with the States – formulate a Model Excise Policy, which can be implemented by all States to maintain uniformity across the country, thereby bringing ‘Ease of Doing Business’ within this industry.
- The regulatory body shall regulate route to market channels in States to ensure state monopolies or state created monopolies for distribution of alcohol which encourage corrupt practices are obviated.
- The regulatory body shall regulate manufacturing capacity in the country to ensure there is no mismatch between supply and demand for alcohol.
- The regulatory body shall ensure that regulatory environment pertaining to the value chain in States’ domain are uniform across all states.
- The regulatory body shall, in consultation with the State Governments, prescribe prices on advisory basis to ensure healthy competition between the states.
- It will prescribe norms for number of retail outlets/100,000 consumers to ensure supply of sufficient alcohol thereby discouraging supply of spurious/illicit alcohol.
- The regulatory body shall also promote responsible retailing and consumption of alcohol by creating special purpose vehicle to promote responsible retailing and consumption where both government and the industry will contribute resources.

1.4 State level issues

1.4.1 State Excise cycle and regulatory requirement under Central Acts:

Labels should be registered with State Excise department before commencement of business in respective States. It is an annual requirement and varies across States beginning with the financial year and gets over by early July. Labels once approved by the State Excise department on payment of fees can only be revised after paying additional fees. The Industry also complies with specific labelling requirements mandated by Central Authorities like Food Safety & Standards Authority of India (FSSAI) under FSS Act as well as The Legal Metrology Act (Department of Consumer Affairs).

The requirement under the various state excise legislation and the Central legislations are almost similar in nature except difference in the size of the alphabets/numerals etc. Frequent changes in the labelling requirement creates disruptions in business and most importantly huge financial implications on businesses. This year with the introduction of Alcobev Standard by FSSAI and mandatory labelling requirements lead to a situation where most of the States agreed to the guidelines suggested by FSSAI under the Central Act. This is a welcome move and tend to move towards uniform labelling regime.

RECOMMENDATION:

1. Changes in labelling or other requirement under the Central Acts should follow the excise cycle which begins from 1 April, barring a few States. Compliance would enhance substantially if changes required follows the excise cycle.
2. Labelling requirements under the Central Acts should not lead to repetition and avoid confusion.
3. Move towards simplified uniform labelling requirement combining both FSSAI and State Excise labelling requirement;
4. States should aim at announcing their annual Excise Policy, possibly beginning April each year.

1.4.2 Ease of doing business:

The reform that started with the coming into power of the NDA Government in 2014 picked up pace in successive years. This resulted in India moving up the ladder to 63rd position out of 190 nations in the World Bank ease of doing business survey 2019, from 77th in the previous year. This is a significant achievement. This has been possible due to multiple reforms in economic laws and simplifying the processes involved in it.

The journey that started in 2014 gathered momentum and consultation between the Centre and States intensified leading to a much deeper reforms in the coming days. With thrust on Atmanirbhar Bharat and the integration with the global supply chain we are expected to see a plethora of reforms in the days to come.

The reforms initiated has led to cut down on number of processes and practices adopted earlier to run and operate business. This exercise has significantly improved India’s position in the World Bank ranking on Ease of doing business conducted each year by World Bank.

Fortunately, this year too alcoholic beverage sector got covered under BRAP 2019 undertaken by DPIIT. Inclusion of alcoholic beverage sector under the BRAP 2019 would see a vast change in the way State Excise department functions. Regular monitoring of operational activities like timely issuance of permits/registration of brands, labels/Renewal of Distillery license etc. would be monitored jointly by teams from DPIIT and the State Government agency. The inclusion of some of the State Excise issues within BRAP would lead to significant improvement in the way alcoholic beverage trade is conducted.

With the onset of covid-19 and the announcement of country wide lockdown many States moved to online registration of labels and their renewals once the lockdown was withdrawn. That gave a huge amount of confidence to the Excise department and the Industry members that digitisation is possible and could run successfully in State Excise.

With the initial breakthrough, Industry looks for further reforms in the State Excise regulation with better use of technology, faster decision making, cutting red-tapeism which will enable member companies to remain competitive, and operate in a compliant manner.

RECOMMENDATION:

1. To remove unwanted License conditions which acts as a barrier for smoother and simpler operations of the manufacturer;
2. Free flow of finished goods and raw materials with faster approvals;
3. The current annual registration process should be replaced by longer duration approvals, say for 3-5 years, on annual payment of fees by the brand owners;
4. Renewal of labels should be automatic on payment of fees in case there is no change in labels as compared to previous year.

5. Companies shall furnish an undertaking stating no changes in labels and pay the annual fees online and labels should get automatically registered for the next Excise Cycle/Year so that companies could start business from day one.
6. Better use of technology to improve upon monitoring, tracking movement of goods and enforcement;
7. And finally faster decision making at the State Excise which has been a major bottleneck.

To sum up, the year 2019 has been an incredible year for the Indian alcoholic beverage Industry. Industry could bounce back and regain its lost glory despite of many hurdles faced by it. The contribution of alcoholic beverage Industry improved significantly, provided employment, and have tried to improve the image of alcoholic beverage Industry by being ethical and compliant. It has also taken up several projects to educate consumers to behave responsibly. The introduction of new alcoholic beverage standard by the Food Safety Authority in line with global standards makes Indian alcoholic beverage industry at par with the global ones. India being one of the largest-growing alcoholic beverage market, more and more premium international brands came to test the Indian market. That offered unique opportunity to the Indian consumers to experience all premium brands albeit at a higher price point. That boils down to the factor that high incidence of tariff and local taxes hinders the growth of premium alcoholic beverage products. Gradual reduction of tariff, reform in Excise laws and rationalisation of state taxes and levies would provide the required impetus to maintain the growth story. That will ensure sustained investment in developing markets and new products which will further propel the growth of premiumisation and building premium brands.

However, with the onset of COVID-19 in early 2020 followed by complete lockdown for most of 2020, the gains made by the alcoholic beverage business in 2019 has been completely washed out. With hospitality, tourism and aviation sector closed, economic conditions substantially down with loss of employment and the impact of Covid-19 still continuing in many States it will take months before the alcoholic beverage sector could see a turnaround.

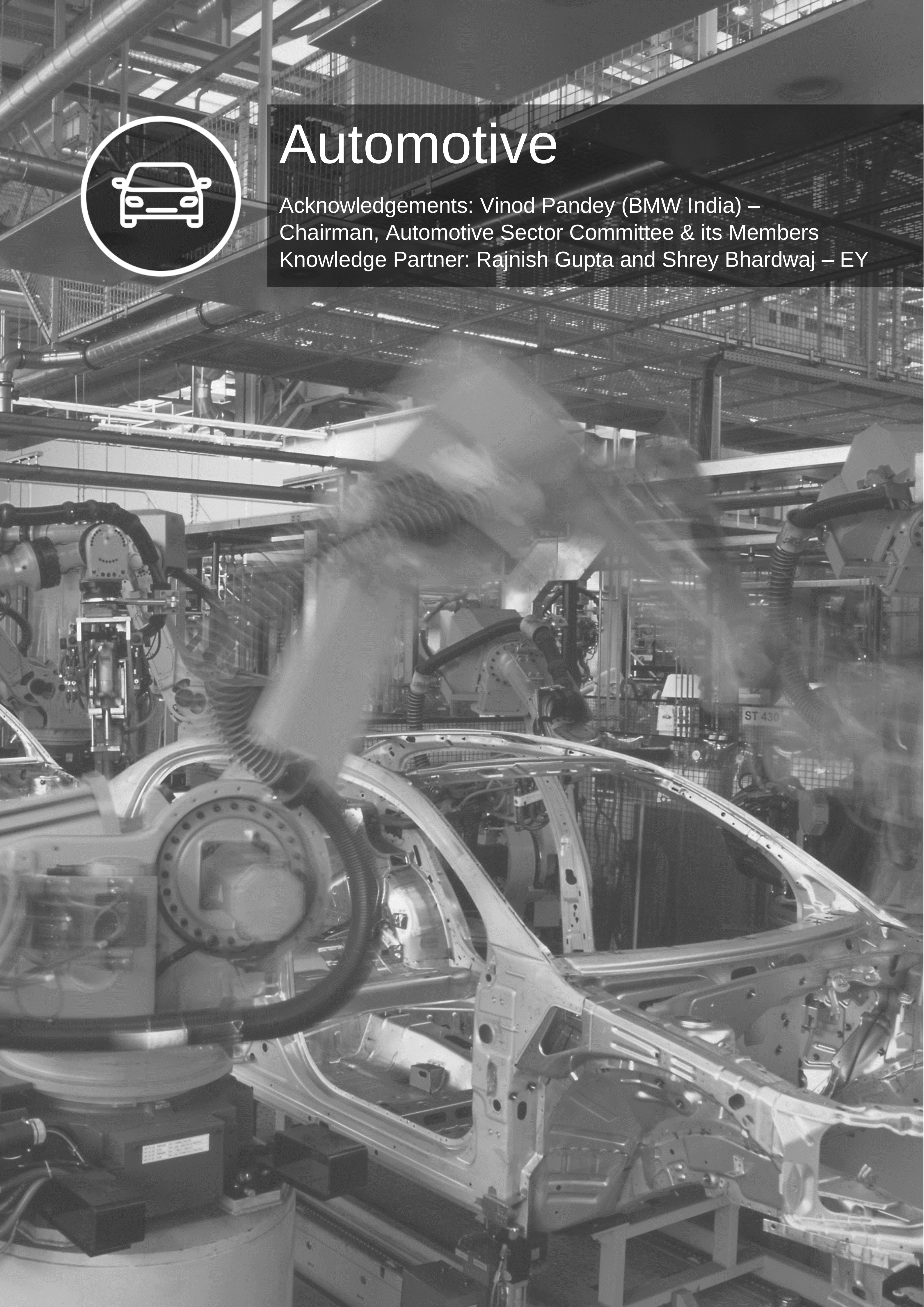
ENDNOTE

1. Source: IWSR 2019

NOTE

Automotive

Acknowledgements: Vinod Pandey (BMW India) – Chairman, Automotive Sector Committee & its Members
Knowledge Partner: Rajnish Gupta and Shrey Bhardwaj – EY



EXECUTIVE SUMMARY

The automotive industry is one of the key drivers of India's economic growth and a major participant of the global automotive value chain. The automotive industry is one of the pillars of the Indian economy and contributes ~7% to the nation's GDP. In FY2020, the industry manufactured 26.4 million vehicles, of which 4.8 million were exported.[1] In 2017, India overtook Germany to become the fourth-largest automobile market in the world.[2] The sector witnessed FDI inflow of US$22.4 billion during April 2000–June 2019, accounting 5.1% of the total FDI inflows during the period.[3] India's auto sales, which used be fifth-largest till FY2019, has slid back to levels of almost a decade ago due to a combination of factors including an over dose of regulations, a slowing economy, liquidity issues, and the COVID-19 pandemic.[4]

COVID-19 has hit India at a time when both the Indian economy and the automotive industry were hoping for a recovery. The pandemic is expected to have an overall revenue impact of at least US$1.5–US$2.0 billion per month across the automotive industry.[5] Passenger vehicle sales plunged 78% YOY during the first quarter of FY2021,[6] impacted by the nationwide lockdown implemented to prevent the spread of the virus. As the market opens, further decline in passenger vehicle demand is expected, as consumers are likely to delay their discretionary spends. The supply chain is expected to adapt quickly, however extended supply chain visibility at tier 2/3 level is the biggest risk mitigation factor that vehicle companies will need to address.

The Government of India has been supportive of the automotive sector as it has been a critical enabler in driving manufacturing volumes and excellence through a multi-pronged policy framework. The government has listed out a series of possible measures such as scrappage incentive scheme and reduction in the goods and service tax (GST) rate to revive the auto sector. A planned and concentrated response will be required from the industry, government, and regulators to ensure a V-shaped recovery of the automotive industry.[7]

The EBG Federation recommends a few points for attention across the three levers of technology, taxation, and trade to truly realise the immense potential of Indian automotive industry.

- Create an equitable taxation structure for the large vehicle segments by having uniform rate for the automotive industry. This will enable greater manufacturing competitiveness and help India compete on the global stage. The taxation structure needs to be clearly delinked from the vehicle length and engine capacity.
- Significant reduction in the import duty on vehicles with volumes capped at 5000 units/annum. Reduced import duties will provide impetus to new model introduction, leading to growth of domestic market and facilitating manufacturing in the medium to long term.
- Provide exemption from Quality Control Orders (QCOs) and import restrictions to European OEMs having established local manufacturing operations with annual sales volume of less than 25000.
- Long-term EV policy framework of at least seven years, that allows for continuity and attracts desired investments required for EV deployment. The focus should be to drive localisation of key EV components by incentivising local manufacturing.
- Establish High Level Dialogue on Trade and Investment with EU and also revive Broad-based Trade and Investment Agreement (BTIA)
- Collaborate with EU on working out modalities, framework conditions for developing connected mobility eco-system.
- Policies adopted to promote clean energy should not stigmatise diesel fuel. The government should adopt measures that bring parity between BSVI petrol and diesel vehicles.

The European OEMs have made significant investments in the country and have established themselves as trusted partners in driving the nation's growth agenda. They are willing to continue contributing by introducing well-researched automotive technologies, products and systems, however, would need an enabling framework. We look forward to early implementation of the recommendations proposed in this Position Paper.

AUTOMOTIVE INDUSTRY

1. BACKGROUND

1.1. Significance of the Indian automobile industry

The automobile industry is one of the largest and fastest growing sectors of the Indian economy and constitutes 7.2% of the GDP and 49% of the manufacturing GDP. The industry provides employment to around 37 million people directly and indirectly and contributes to 15% of total GST collection amounting to INR1.5 trillion[8]. The industry is regarded as a 'Sunrise Sector' under Make in India and is instrumental in shaping the country's economy. India is the world's largest tractor, two-wheeler and three-wheeler manufacturer and the fourth-largest passenger vehicle manufacturer. Despite its large size and current slowdown, the auto industry has significant growth potential owing to the country's low passenger vehicle penetration. Vehicle penetration is estimated at 28 passenger cars per 1,000 people in 2019 and expected to reach 72 vehicles per 1000 people by 2025, clearly establishing a strong upside potential.[9]

India's GDP contracted by 23.9% during the first quarter of FY2021 due to the nationwide lockdown imposed by the central government on March 25 to curb the spread of COVID-19 pandemic. The country's real GDP is expected to contract 10.9% in FY2021 with a decline of 12%-15% expected in second quarter (July-September) and 5%-10% in following quarter (October-December).[10] The government needs to bring impactful reforms with due diligence, which can yield immediate results to stimulate demand and resolve liquidity crunch. In addition, the automobile industry will need expansion of the domestic consumption base, high value manufacturing competitiveness and technological capabilities to achieve its target of 12% GDP contribution by 2026.

Automotive sales and production witnessed a year-on-year decline of ~18% and ~15% respectively in FY2020 mainly due to weak consumer sentiments, liquidity crunch and increased vehicles prices due to regulatory changes. Automotive sales and production declined by ~75% and ~79% respectively during the first quarter of FY2021 vis-à-vis the corresponding period in the previous year[11]. India exported 4.8m vehicles globally in FY2020. During this period, two-wheelers accounted for ~74% of Indian vehicle exports, followed by passenger vehicles (14%)[12]. Passenger vehicles exports increased by 0.2% (year on year) during the period as OEM's focused on exports to offset subdued domestic sales.[13] Vehicle exports could play a significant role in India's future manufacturing growth in the coming years on back of increasing manufacturing prowess. The government is also working towards signing favourable trade agreements, which would allow Indian auto companies to increase export in Europe.[14]

1.2. European Investments

- European players continue to make significant investments in India throughout the automotive value chain – from manufacturing components to sales and after-sales services.
- Leading original equipment manufacturers (OEMs) such as BMW, Daimler, Fiat, Piaggio, Renault, Volvo, and VW Group have invested over INR300 billion in the country so far. They have significantly contributed in terms of world-class manufacturing facilities, R&D, training and employment, and provided greater choices to the Indian consumer.
- Leading component suppliers such as Bosch, Continental, Durr, Magnetti Marelli and Michelin have played a pivotal role by bringing in latest technology and improve product performance.
- The share of European vehicles sales in India is estimated at approximately 5% in both Passenger Vehicle (PV) segment and the Commercial Vehicle (CV) segment during FY2020. The market share is expected to increase owing to increasing consumer preference for premium and technologically advanced products, both in the PV and CV segments[15].

1.3. Government Initiatives

The government's Automotive Mission Plan (AMP) 2016–26 envisions the industry to grow around four times by FY2026, reaching a value of US$260-300 billion[16]. Under the plan the government envisions overall automotive sales to cross 60 million units and a base case scenario of 9.4 million passenger vehicle unit sales by FY2026. However, the passenger vehicle sales contracted to 2.8 million units in FY2020, and further collapsed by ~80% y-o-y during the first quarter of FY2021 due to the COVID-19 pandemic. The recovery of PV and 2W sales to FY2019 peak numbers is expected to take place only by FY2023, if the present situation prevails and no measures are taken by government and industry players to revive demand.[17]

E-mobility has emerged as a top priority in the government's transportation strategy. From August 2019, the government reduced the GST rate on electric vehicles to 5%. In February 2019, the Government of India announced the FAME-II scheme with a fund allocation of INR100 billion (US$ 1.39 billion) for FY2020-22. It aims to provide impetus to the adoption of EVs and PHEVs by way of offering an upfront incentive on the purchase of vehicle and establishing necessary charging infrastructure.

Under FAME II, the government has levied stringent eligibility criteria basis vehicle end-use, vehicle price cap, localisation and product features, which would restrict the incentives for majority of the OEMs. Unlike FAME-I, FAME II does not benefit the private owned vehicles except for the two-wheelers. The government also announced a road map under the phased manufacturing programme (PMP), entailing phased increase of basic custom duty on EVs, its inputs, parts and assemblies to promote indigenous development. Also, as per the guidelines released by DHI in April 2019, OEMs will have to indigenise a significant portion of components to avail the FAME II incentives. DHI listed EV's assembly and components used across vehicle categories and charted the associated deadlines (during 2019 to 2021) as the effective timelines for indigenisation.

We understand that the government has a legitimate objective in terms of providing incentives for locally manufactured products, however, indigenisation requires volumes, which may take time depending on the consumer acceptance and demand for EVs. The government may, therefore, consider a longer duration for targeting indigenisation and focus on market creation in the initial few years. We believe that these restrictions will not only impede technology transfer, but also slow down the pace of development and adoption of EVs.[18]

In addition to EVs, The government has taken other initiatives of assistance to the automobile industry:

- The Ministry of Road Transport & Highway relaxed homologation norms for OEM imports of up to 2,500 units of CBUs or CKDs of PVs or motorcycles, and up to 500 units of other categories annually, irrespective of their price and engine capacity. We consider this as a positive step for automakers as they can now experiment with multiple models to explore market acceptance, especially for niche/ non-existent models, and alternative drive train variants without being concerned about the homologation cost and time spent on certification. Successful experiments can then be adapted for localisation.[19]
- We strongly support the government's decision of leapfrogging to BS VI emission standard from April 2020 and on the timely roll out of BSVI fuel to support this transition. However, it is imperative that the government should put measures in place to bring parity between BSVI petrol and diesel vehicles.
- EBG Federation commends the government's efforts at adopting higher crash/safety standards.

2. FUTURE OF MOBILITY IS DRIVING DISRUPTION

The global automobile industry is undergoing a significant transformation with the emergence of new mobility ecosystem. The automobile industry is likely to witness significant changes in the next five years on the back of digitisation, increasing automation and new business models. Accelerating technological disruptions together with changes in consumer choices and preference can result in an industry structure that may be very different from the current one.

In the near term, the future of mobility is likely to be impacted by:

- Electric vehicles,
- Shared mobility, and
- Connected vehicles.

Future direction of mobility provides unique challenges to the industry. If India wishes to become an industry leader, it needs to facilitate investments in new technologies while also deepening expertise in the existing technologies to improve efficiency and reduce emissions. It is therefore important for India to frame and evaluate policy choices (GST rates, EV policy, etc.) that incentivise innovation and adoption of advanced technologies. Additionally, there is need for a free and open market that through competitive pressure would further drive innovation leading to larger benefits to consumers. In this context, it is imperative to remove technical barriers to auto imports.

3. INTERVENTIONS FOR REALISING POTENTIAL

Realising the true potential of Indian auto industry and making it globally competitive will require concerted efforts of all stakeholders. There is an urgent need to focus on specific policy interventions across the **technology, taxation, and trade levers** to enable Indian automotive industry to position itself as a global leader.

3.1. Technology

- The auto industry is undergoing significant disruptions on the back of technological advancements. Besides increasing technological maturity (autonomous, connected) and emergence of sharing economy, the need for environmental protection has been a key driver in the Indian perspective. In this context, the need for reduced vehicular pollution is creating a push for greater electrification and consequent charging infrastructure, alternative fuels and policy initiative on CO_2 emission standards.
- India ranked No.1 in terms of road fatalities across countries according to the World Road Statistics, with over 1,50,000 fatalities in 2018[20]. The situation is compounded by ever increasing road congestion, impacting productivity and subsequently driving erosion of economic value creation.

3.1.1. BS VI Transition:

EBG Federation shares concern for rising pollution in Indian cities, however, disagrees with the approach of singling out diesel vehicles as the key contributor. EURO VI advanced clean diesel technology has emissions almost on par with petrol.

Recommendations:

a. EBG Federation highly appreciates the government's efforts in ensuring the pan-India availability of BS VI fuel within the committed timelines to ensure smooth transition.

b. We recommend the government to adopt measures that brings parity between BSVI petrol and diesel vehicles given the inherent benefits of diesel vehicles especially in the context of India.

3.1.2. Electric Mobility

- Over the past 7-8 years, there has been a lot of deliberation and action initiated around promoting EVs, given the environmental benefits. However, despite the focus, penetration of electric vehicles continues to be low. Range anxiety, high cost of batteries, unavailability of compelling EV models, inadequate charging infrastructure and lack of long-term policy roadmap on incentives have been some of the reasons for the limited uptake of electric vehicles in India.
- The National Electric Mobility Mission Plan and schemes such as FAME are positive initiatives and convey the government's intent to promote EVs. FAME II scheme commits an outlay of INR100 billion over a period of three years to boost electric mobility in India. However, it levies stringent eligibility criteria which excludes majority of EV OEMs to qualify for incentives. At this stage of market development, it may not be desirable to link incentives with localisation as the OEs and the component suppliers are not yet ready to manufacture vehicles or components for the current low volume. In the absence of minimum demand for EVs, the government's push for manufacturing of EVs in India may not be immediately realised.
- Further, the incentives apply to vehicles used for public transport or those registered for commercial purposes in 3W, 4W and bus segments, and only 2Ws are covered in privately owned category. Also, FAME II incentives, with an upward ceiling of INR1.5 million for 4Ws, is not relevant for the premium vehicles. Furthermore, with an implementation plan for only three years, it lacks clarity on the financial support that would be available on a long-term basis.

Recommendations:

a. EBG Federation recommends that the government adopt a long-term EV policy framework **(at least seven years)** to provide confidence for long term investments. As instance, will the 5% GST rate on EVs be maintained for an extended period of time for OEMs to plan significant investments on the back of a low GST rate?

b. EBG Federation understands that the government's decision of increasing import custom duty on electric vehicles and components is in line with its phased manufacturing programme (PMP) to promote indigenous development. However, we recommend the government to extend timeline of meeting indigenisation targets as domestic manufacturing will need to be underpinned by minimum volumes. The government may consider implementing the PMP after the industry achieves a certain minimum EV volumes or penetration.

c. EBG Federation welcomes the government's move to include plug-in hybrids under the FAME II scheme. Initial market creation is a pre-requisite for faster electric mobility adoption. EBG Federation recommends that the policy framework should also cover privately registered and premium vehicles to enable the mass uptake. EBG Federation appreciates the government decision to reduce GST rate on EVs to 5% and strongly recommends reducing the GST rate of PHEVs to 18%[21]. PHEVs offer an excellent channel towards transition to battery electric vehicles. Range anxiety is an impediment to uptake of EVs and the sooner the policy makers recognise this and take measures to address the issue, their chances of making EVs a success will increase manifold.

d. The planned outlay of INR10 billion towards the charging infrastructure is a welcome move, however the government should ensure they are in line with international standards. EBG Federation recommends that India should go the global way, by bringing about a definite set of charging standards and following it up with concrete policies. EBG Federation recommends adoption of the CCS charging standards for DC Fast Charger (>100 volts).

3.1.3. Connected Mobility

- The global automotive industry is making significant efforts to focus on connected mobility to bring safety and reliable transport to all mobility consumers. It is important to shape the future from a technical perspective as a vehicle manufacturer, establish enabling regulatory framework and infrastructure. Despite India being the fourth-largest PV manufacturer, India is still not a leading country from a technology perspective.
- Vehicle-to-vehicle and vehicle-to-infrastructure communication is key to developing intelligent transportation systems. Connected and autonomous vehicles can allow for fundamentally new use cases for vehicles and more efficient use of infrastructure.
- European vehicle manufacturers can offer advanced safety features in the products such as driver assistance, anti-collision and lane departure warning; however, they are not able to do so due to lack of requisite frequency licensing.
- Data privacy implications for connected vehicles are significant. The data collected by the cars will not only be commercially valuable but also contain extremely sensitive information about individuals.
- EBG Federation can play a critical role in introducing and adaptation of new technologies such as the lane departures, radar, and lidar in the Indian auto industry. These new advanced technology solutions can significantly improve safety quotient of urban mobility if implemented consistently.

Recommendations:

a. EBG Federation recommends that the Government of India work together with the EU on working out modalities and framework conditions for developing connected mobility eco-system.

b. Roll out of 5G network with fast and steady network across India to explore full potential of connected mobility and autonomous vehicles.

c. De-licensing of frequency bands is important to introduce advanced product safety features.

d. Data safety, security, and privacy would be the critical factors. Therefore, the Government of India would need to come out with clearly defined regulations for data handling and management, in alignment with European laws.

e. EBG Federation recommends the government to support research on autonomous driving through R&D incentives and testing infrastructure. It can partner with European automotive industry.

3.2. Taxation

A favourable taxation policy can provide a major fillip to the automotive industry. EBG recommends transparent, consistent and stable tax and regulatory regime as pre-requisite to drive growth. Companies need a level playing field and long-term clarity to plan their business strategy and investments.

3.2.1. GST on Passenger Vehicles

- EBG Federation expected GST regime to address the tax rate anomaly existing between small and large vehicles. Since, GST rates are on ad valorem basis, therefore, the customer will anyway pay higher taxes on ex-showroom price of large/premium vehicles, which is higher than that for small cars.
- Currently, premium vehicles in India attract the top GST slab of 28% and an additional cess of 20% on sedans and 22% on SUVs, taking the total tax incidence to 48% and 50% respectively.

Recommendations:

a. EBG Federation is disappointed with additional cess on large/premium cars. Premium car manufacturers bring in products with latest innovative technology, highest safety and emission standards, contribute to high skill development, and provide employment opportunities. Therefore, demerit categorisation of these products is equivalent to penalising innovation. Removal of additional cess can also provide an excellent opportunity to export such premium products to the global markets in future.

b. EBG Federation acknowledges the government's concern on revenue collection. However, EBG Federation suggests a phased approach:

  - Difference between GST rate for small cars (length<4m) and large/ premium cars (length>4m) should be reduced to 10% by capping compensation cess at 10%. Review of proposed two-rate tax structure after two years to evaluate the possibility of converging to a single rate.
  - Standard GST rate of 18% for two-wheelers
  - Currently, the GST rate of 18% has been administered on a select few auto components, which comprise merely ~30% of the overall auto component production, while others are taxed at much higher 28%. We believe a standard 18% rate for auto components is critical, especially when the auto component industry is expected to undergo large transitions due to the government's push on e-mobility.

c. We strongly recommend single rate for the automotive industry, capped at 28%. The taxation structure needs to be clearly delinked from the length of the car and should solely be meant to incentivise safer and greener cars. The government should further consider bringing down GST rates on vehicles to offset the impact on demand arising from higher prices of BS-VI compliant vehicles. Prices of BS-VI compliant commercial vehicles and passenger vehicles can go up by 8%-10% and 3%-7% respectively.[22]

3.3. Trade

- Passenger vehicle exports need strong attention from the government to continue increasing focus of global manufacturers in positioning India as an export hub, especially to markets without local manufacturing capabilities.
- There is a mismatch between the Indian capability and needs of the global markets. Globally, small car is estimated to account for 15%-20% of the overall passenger vehicles produced[23]. However, share of small car production in India is much higher at around 55% in FY2020.[24]
- EBG Federation sees it as a positive development that India export portfolio has started to diversify with the share of small cars produced shrinking to 55% during FY2020 as compared to around 69% in FY2010.[25] However, the pace of change is slow and there is lack of capabilities and investments directed towards increasing capacity to manufacture medium to large size vehicles. It is challenging for automakers to manufacture and realise volumes for medium & large vehicles, given the construct of the government's automobile policy.

Recommendations:

- EBG Federation emphasises the urgent need for government support in creating an equitable domestic duty structure in the large vehicle segments to enable greater manufacturing competitiveness and volumes and help India compete on the global stage.

3.3.1. Import/ Custom duty

- Most European carmakers imports parts and completely knocked down (CKD) kits to India and assemble locally to maximise domestic value addition. Higher import duties on components sourced from Europe vis-à-vis import duty from FTA countries such as Japan, ASEAN and South Korea, places European manufacturers at a significant competitive disadvantage.
- The premium vehicle penetration remains very low in India. The premium car manufacturers bring in products with latest innovative technology, highest safety and emission standards. Though there has been a shift in consumer preference to more sophisticated, durable and reliable vehicles, higher tax incidence remains a major deterrent.
  - High duty on import of fully built passenger cars into India: Most completely built units (CBUs) of new cars are charged at basic customs duty of 100% for cars with FOB value > US$40,000 or engine capacity > 3.0L for petrol engines or > 2.5L for diesel engines[26].
  - European manufacturers are constrained by economies of scale and quality considerations and hence not able to develop the supplier ecosystem to expand localisation beyond a point.

Recommendations:

a) As import duty in India on imported vehicles is among the highest globally, EBG Federation strongly recommends a significant reduction. Reduced import duties will provide impetus to new model introduction, leading to growth of domestic market. This will facilitate expansion of manufacturing activity in the mid to long term.

b) The EBG Federation welcomes the move of homologation relaxation. It will save extra time and investments and will also help assess the market acceptance of new models for the future local investment or assembly at a reduced cost. We urge the government to increase the limit to 5000 and reduce the import duties on these vehicles. This will help test marketing of new products and a successful market acceptance could pave way for localisation in the future, also bringing in technological advancements.

c) In the past, the government of India incentivised the imports of premium motorcycles by reducing the import duties by 50%. Something similar could be considered for high-end cars to help the consumers drive better quality of cars.

d) EBG Federation recommends an **offsetting mechanism to the government to a fixed percentage of total vehicles manufactured in India to be imported under the reduced duty structure thus promoting local manufacturing.**
   - Number of CBU vehicles for import at a concessional rate to be limited to 10% of the volumes produced locally in a financial year.
   - Applicable concessional basic customs duty: 15%
   - Import volume cap: 5000 units in a financial year

3.3.2. Withdrawal of export incentive schemes:

India lost the export incentive case filed by the US at the WTO, ruling that some of India's export subsidy programmes violates provisions of the WTO**.** The implementation of the WTO ruling will be led to the withdrawal of popular export incentive schemes, such as the Merchandise Export from India Scheme (MEIS) from January 2021. The government has announced new globally compliant export incentive schemes as replacement.[27]

- The government has announced fresh schemes to boost exports. The existing Merchandise Export from India Scheme (MEIS) has been replaced by a new scheme - Remission of Duties or Taxes on Export Product (RoDTEP) effective January 2021. RoDTEP is expected to adequately incentivise exporters.[28]
- The insurance cover under the Export Credit Insurance Scheme has also been

enhanced, providing flexibility to banks in giving loans to exporters.

- The government has also taken measures to ensure effective monitoring of export financing by the commerce department and a fully automated electronic refund route will be set-up for input tax credit in GST to help exporters.

Recommendation:

- EBG Federation recommends that the government implement these expeditiously.

3.3.3. Quality Control Orders (QCO)/Import restrictions: Government has recently issued a series of notifications concerning automotive components such as QCO for safety glass, draft QCO for wheel rims, replacement brake lining assemblies and drum brake linings that require mandatory ISI marking under a license from the Bureau of Indian Standards (BIS). Tyre import has also been moved from the “free” to “restricted” category. The government’s intent is to ensure high-quality imports and drive localisation; however these licensing requirements have a major disruptive effect on the entire automotive supply chain.

- The order has critical business impact as these components are required a) for local vehicle production in India; b) fitted on CBU vehicle; c) for the purpose of spare parts and d) for testing and certification. These components are specific to models and cannot be manufactured locally due to very low volume.
- Given the limited volume, carrying out BIS certification, audit, marking, and compliance activities for components produced in multiple overseas plants is a huge challenge and financial burden due to development of special tooling, production management systems, audit & compliance requirements for conformity of production etc. Especially in the light of ongoing COVID-19 crisis, companies are under severe economic strain. Overseas audits are not being conducted due to international travel restrictions. In the absence of alternative solutions, EU companies producing in India could face severe supply issues leading to production disruption, resulting in significant financial implications.
- The quality of imported components follows stringent European regulations and also complies with the local requirements of Central Motor Vehicle Regulations. Therefore, there is no health and safety risk associated with these products that the government intends to curb through QCO for sub-standard imports.
- Since the entry into force of tyre restriction, imports of tyres into India from the EU have decreased by more than 50%, with considerable losses for **EU tyre manufacturers.** To-date, the measure has not been notified to the World Trade Organisation (WTO), nor have guidelines been issued to clarify the process of obtaining license. It is also pertinent to highlight that due to low volumes of specific tyre varieties required for the domestic market, local production is not cost effective.
- These notifications go against the ethos of "Ease of Doing Business" especially for companies who are supporting government's initiative of "Make in India".

Recommendation:

- EBG Federation recommends exemption of OEMs with local manufacturing operations and annual volume of less than 25000 units from QCOs
- For the OEMs with more than 25000 units annually, QCO should:
    - Exempt completely built unit vehicles
    - Exempt components (capped at 5000 units annually for each part number) required for local production, aftersales operations, testing and homologation
    - Extend implementation timeline for QCO Safety Glass to 01 October 2021 given the current COVID-19 challenges and travel restrictions
- Import of Tyres to be moved back to “Free” category for OEMs and established Tyre manufacturers
- Provide sufficient time for implementation (~18 months) of any new future licensing/ QC requirements. It is also important to provide transparency about the applicable administrative procedures for obtaining the relevant certification.

3.3.4. Establish High Level Dialogue (HLD) on Trade and Investment: The EU automotive industry is heavily invested in India and is committed to growing its footprint in India on a sustainable basis. EU industry would, therefore, welcome an early establishment of the HLD on trade and investment, agreed at the recent EU-India Summit. EU industry hopes that a dialogue at ministerial level could provide political steer and guidance to resolve some of the longstanding issues and seize the opportunities available to further strengthen this relationship.

3.3.5. Revive India-EU BTIA: India EU Broad based Trade and Investment Agreement (BTIA) has been under discussion since 2007. An ambitious and balanced BTIA can contribute to major expansion of trade and investments between India and EU. EBG Federation believes that India-EU BTIA would be in mutual interest of both the trading partners for the following reasons**:**

- FDI and trade are complementary to each other. Deepening of the trade relations will significantly drive higher levels of investment from EU to India
- EU-India BTIA could help India become an integral part of the supply chain of European corporations
- EU automotive industry is very keen to see EU-India BTIA becoming reality, which would give the automotive sector on both sides much needed push in terms of trade, technology and job creation.

Recommendations:

- EBG Federation considers the inclusion of automotive sector in a future trade agreement to be a must and stands for a pragmatic compromise of tariff reductions and relaxation of non-tariff restrictions. Differentiation between premium and volume products is a possible pathway that can address the Government of India's concern of adverse impact on the local automotive industry.
- Such a trade agreement could include a considerable reduction of tariffs as the first step with the introduction of review clause that would link further tariff reductions to the achievement of certain criteria by India within a clearly defined period.

4. FOCUSED POLICY INITIATIVES

Policy support can have significant impact on issues concerning pollution and road safety.

4.1. Vehicle Scrappage Policy

- According to the National Green Tribunal (NGT), there will be over 21 million ‘end of life vehicles’ by 2025 and about 9 million vehicles will be due for scrapping by next year, of which, 75% are two-wheelers. In India, more than 1.2 million commercial vehicles are more than 15 years old and an effective scrappage policy will have the potential to support the sector by boosting replacement sales equivalent to 36% of annual sales.[29]
- The government is closing in on finalising the vehicle scrappage policy. This would boost demand for automobiles and reduce vehicular pollution. The policy would help India reduce the import of metals such as copper and aluminum, which can be extracted from scrap.
- The road ministry issued draft guidelines in October 2019 to set-up vehicle scrapping centers in the country to promote a legally backed dismantling and scrapping industry.
- The policy is also expected to disincentivise older vehicles by introducing measures such as more frequent pollution checks, higher re-registration charges and stringent fines for not carrying required documents to deter the use of vehicles more than 15 years old. However, the Central Government is unlikely to provide any direct scrapping incentive but is expected to encourage State Governments and OEMs to provide sops against scrapping certificates.

Recommendations:

a. The government should consider offering scrapping incentives initially to stimulate higher demand. Incentives could come from the savings that the government can make from reduced oil imports.

b. EBG Federation recommends a “Fleet Modernisation”/“Scrapping” programme by providing liberal one-time incentive for vehicles more than fifteen years old.

   i) Financial incentive of 50% reduction in applicable taxes (including road tax) for buying new vehicles

   ii) Higher incentive to promote green mobility- the incentive can be increased to 75% reduction in applicable taxes for buying battery electric vehicles.

c. The EBG Federation welcomes Road Transport and Highway Ministry's intent to set-up vehicle scrapping centers to promote legally backed dismantling. However, we urge the government to cover dimensions such as end-of-life for vehicles based on kms travelled, mileage or years in the final draft. Also, financial incentives should be tradable against a certificate of destruction.

d. EBG Federation recommends that OEMs and their dealers should not be entrusted with the sole responsibility of collection and scrappage of vehicles. The OEMs and the dealers can provide technical guidance to independent private recycling centers. For example, in Germany, vehicle scrappage is handled through certified and independent dismantling centers that handle scrap vehicles.

CONCLUSION

In FY2020, sales fell across vehicle segments and the COVID-19 outbreak has cast a long shadow over the much-anticipated mild recovery in the Indian economy in FY2021. There are challenges both on the supply as well as demand side, due to plant shutdowns and lower consumer demand. Moreover, the recent Quality Control Orders/ and notifications on Import restrictions will result in significant business disruptions leading to potential existential crisis for European automotive players with low volumes. We recommend a planned and concerted response, both immediate and medium to long term to ensure steady recovery. Apart from the action taken by the industry, the support from government and regulators will remain key to catalyse this revival. Strategic policy interventions by the government to enable a vibrant automotive ecosystem is the need of the hour. European companies are committed to contribute to local value addition by introducing advanced sustainable technologies, products and systems. Collaboration between European players and the Indian government could be mutually rewarding.

ENDNOTE

1. SIAM Flash Report March 2020
2. "India is expected to be the world's third-largest automotive market in terms of volume by 2026," *Invest India*, https://www.investindia.gov.in/sector/automobile, accessed 7th September 2020
3. FDI Statistics, Department for Promotion of Industry and International Trade
4. "Covid-19 impact: Govt looking at GST rate cut for automobile sector," *Business Standard*, https://www.business-standard.com/article/economy-policy/government-assures-auto-industry-leaders-of-incentives-and-support-120090401571_1.html, accessed 7th September 2020
5. "Opinion: COVID-19 impact on Indian automotive industry- Taking action in troubled times," *Economic Times,* https://auto.economictimes.indiatimes.com/news/industry/opinion-covid-19-impact-on-indian-automotive-industry-taking-action-in-troubled-times/74944847, accessed 7th September 2020
6. SIAM Flash report June 2020
7. "Covid-19 impact: Govt looking at GST rate cut for automobile sector," *Business Standard*, https://www.business-standard.com/article/economy-policy/government-assures-auto-industry-leaders-of-incentives-and-support-120090401571_1.html, accessed 7th September 2020
8. "Parliamentary panel suggests lower GST rate for auto sector," *Economic Times,* https://economictimes.indiatimes.com/industry/auto/auto-news/parliamentary-panel-suggests-lower-gst-rate-for-auto-sector/articleshow/74465017.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst, accessed 7th September 2020
9. "Automobile- India becomes the world's 4th largest vehicle market," *InvestIndia*, https://www.investindia.gov.in/sector/automobile, accessed 7th September 2020
10. "Economy Likely To Contract 10.9% In 2020-21, Says SBI Report," NDTV India, https://www.ndtv.com/business/india-gdp-data-news-state-bank-of-india-sbi-lowers-2020-21-gdp-forecast-to-10-9-per-cent-from-6-8-2289687, accessed 7th September 2020
11. SIAM Flash report June 2020
12. SIAM Flash report March 2020
13. Passenger vehicle exports increase 5.89% in Apr-Dec; Hyundai leads with 1.45 lakh units." *Business Today,* https://www.businesstoday.in/sectors/auto/passenger-vehicle-exports-increase-5-89-percent-apr-dec-hyundai-leads-with-1-45-lakh-units/story/394129.html , accessed 7th September 2020
14. "Covid-19 impact: Govt looking at GST rate cut for automobile sector," *Business Standard*, https://www.business-standard.com/article/economy-policy/government-assures-auto-industry-leaders-of-incentives-and-support-120090401571_1.html, accessed 7th September 2020
15. SIAM Flash report March 2019
16. "Automotive Mission Plan 2016-26 unveiled: Here are the key highlights," *ET Auto*, https://auto.economictimes.indiatimes.com/news/industry/automotive-mission-plan-2016-26-unveiled-here-are-the-key-highlights/48772090, accessed 7th September 2020
17. "Opinion: 9 indicators that the woods are still dark and deep," Economic Times, https://auto.economictimes.indiatimes.com/news/industry/opinion-9-indicators-that-the-woods-are-still-dark-and-deep/77645752, accessed 7th September 2020
18. "Subsidy ends for ~95% of electric scooters", *Crisil*, https://www.crisil.com/content/dam/crisil/our-analysis/views-and-commentaries/impact-note/2019/apr/crisil-research-impact-note-unplugged-subsidy-ends-for-~95percent-of-electric-scooters.pdf, accessed 7th September 2020;
   "Govt Lists Out EV Components To Be Produced Locally For Claiming FAME II Benefits," *Inc2,* https://inc42.com/buzz/govt-lists-ev-components-produced-locally-fame-ii/, accessed 7th September 2020
   "Automobile Industry in India," *IBEF*, https://www.ibef.org/industry/india-automobiles.aspx, accessed 7th September 2020
19. "Indian Government To Ease Import Regulations For Premium Cars, Motorcycles And EVs," *NDTV,* https://auto.ndtv.com/news/indian-Government-to-ease-import-regulations-for-premium-cars-motorcycles-and-evs-1864005, accessed 7th September 2020

20. "Road accidents claimed over 1.5 lakh lives in 2018, over-speeding major killer," The Economic Times, https://economictimes.indiatimes.com/news/politics-and-nation/road-accidents-claimed-over-1-5-lakh-lives-in-2018-over-speeding-major-killer/articleshow/72127418.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst , accessed 7th September 2020
21. "Tax boost for EVs, GST slashed to 5% from 12%," *The Economic Times,* https://economictimes.indiatimes.com/news/economy/policy/gst-on-evs-slashed-to-5-from-12/articleshow/70407309.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst , accessed 7th September 2020
22. "GST rate cut remains auto companies' top demand ahead of Budget," *The New Indian Express,* https://www.newindianexpress.com/business/2020/jan/17/gst-rate-cut-remains-auto-cos-top-demand-ahead-of-budget-2090730.html, accessed 7th September 2020
23. "Global Light Vehicle production forecasts, Q12019 edition" *LMC Automotive*, accessed 7th September 2020
24. SIAM Flash Report March 2020
25. "India takes center stage as vehicle exports grow," *Business Line,* http://www.thehindubusinessline.com/specials/auto-focus/india-takes-centrestage-as-vehicle-exports-grow/article9669143.ece, accessed 7th September 2020
26. Vehicle Taxes, Society of Indian Automobile Manufacturers.
27. "Govt caps key export benefit to Rs 2 crore per exporter till December" *Economic Times*, https://economictimes.indiatimes.com/news/economy/foreign-trade/govt-caps-key-export-benefit-to-rs-2-crore-per-exporter-till-december/articleshow/77876889.cms, accessed 25h September 2020
28. "Switch to new export scheme in January," *The Telegraph*, https://www.telegraphindia.com/business/switch-to-new-export-scheme-in-january/cid/1704970, accessed 7th September 2020
29. "Scrappage policy: No direct sops for junking old cars," *The Economic Timesl,* https://economictimes.indiatimes.com/industry/auto/auto-news/no-direct-sops-for-junking-old-cars/articleshow/72340728.cms?from=mdr, accessed 7th September 2020

NOTE

Aviation

Knowledge Partner: Davinder Sandhu (Independent Advisor)

1. EXECUTIVE SUMMARY

India is the third-largest domestic aviation market and seventh-largest aviation market in the world, with 207 million passengers (to, from and within India) in FY2019. It is expected to become the third-largest aviation market by 2024.

There has been a sustained road map of policy and regulatory reform in the civil aviation sector that has included government support for greater private sector involvement.

The last year has seen significant changes in the sector that promise to continue the opening up of greater opportunities for both growth in volume of passengers, as well as continued investment in civil aviation infrastructure.

2. IMPORTANT DEVELOPMENTS

Thrust on private participation in airport development

There has been a renewed thrust on private participation in airport development under PPP mode. AAI has undertaken transactions for six brownfield airports at Ahmedabad, Lucknow, Jaipur, Guwahati, Thiruvanathapuram, and Mangaluru with the selection of a new entrant, Adani Group. GMR airports has won concessions to develop and operate airports at Bhogapuram and Nagpur. The transaction process for a new airport near Delhi at Jewar has been concluded.

The government has now announced 100 new airports by 2024. This is in line with the government's commitment to promote domestic travel and include those areas which haven't been connected so far, and is a part of the National Infrastructure Plan.

Aviation Turbine Fuel may be brought under GST regime

The airline industry is facing short-term headwinds and pressures on margins. One of the key challenges for airline industry is that the landed price of Air Turbine Fuel (ATF) for domestic flights in India is one of the highest in the world. ATF remains outside the scope of the Goods and Services Tax (GST) which is an anomaly. In many states, the local taxes on ATF are in the range of 25-30%. This is besides federal taxes.

It is now being actively considered that ATF may be included in the indirect tax regime.

The jet fuel's inclusion in GST would allow airlines to take input tax credit on the GST paid, thus bringing down the effective cost. One can imagine the surge in demand if the government decides to bring ATF under Goods and Service Tax (GST) and provides input credit on the taxes paid thereon.

Maintenance, Repair and Overhaul – reforms provide welcome reprieve

The landmark NCAP 2016 removed many procedural hurdles faced by the Maintenance, Repair, and Overhaul (MRO) industry and have been duly welcomed by them.

In a welcome development, the Goods and Services Tax (GST) council has slashed the tax rate on aircraft maintenance, repair and overhaul (MRO) services from 18% to 5%, with full input tax credit, from 1 April 2020. The notification also changes the place of supply for B2B MRO services to the location of recipient. This change is likely to assist in setting up of MRO services in India. Domestic MRO will also get protection due to 5% tax paid under section 3(7) of the Customs Tariff Act, 1975 on most imported goods (sent abroad for repairs) as this tax is not available as credit.

Drones – the next big revolution in aviation

In August 2018, the government released Drone Regulations 1.0 which became effective from 1 December 2018. On 13 January 2020, the Ministry had issued a public notice to drone operators directing them to voluntarily register their drones on the Digital Sky platform by January 31 to avoid penal action.

This came after the Directorate General of Civil Aviation (DGCA) issued the Civil Aviation Requirements (CAR), Section 3 - Air Transport Series X, Part I Issue 1, which was released on August 27, 2018. The CAR regulates the use of drones in the Indian Airspace and these regulations provide a process for obtaining Unique Identification Number (UIN), Unmanned Aircraft Operator Permit (UAOP) and other operational requirements, including identification of civil drones and drone operators. The Ministry of Civil Aviation (MOCA) has registered 19,553 Unmanned Aerial Vehicles (UAV) or drones since it made it mandatory for operators to register.

After the launch of the DigitalSky Platform under Civil Aviation Regulations (CAR) 1.0 with effect from 1 December 2018, a basic framework for regulations has been established. The focus now has been on addressing challenging frontier issues such as Beyond Visual Line of Sight (BVLOS) and Autonomous Operations. Ministry of Civil Aviation had constituted a task-force on the recommendation for CAR 2.0 and have circulated a draft policy for stakeholder consultations.

Recommendations for the purpose of CAR 2.0 may include:

(a) **BVLOS Operations:** Expansion of operational airspace for UAS operating beyond the visual line of sight and above the current limit of 400 ft.

(b) **Autonomous Operations:** Use of algorithms for piloting may be permitted, but only if adequate safety, security and privacy principles are demonstrated in the design of operations.

(c) **Drone Corridor:** A segregated airspace defined by the appropriate authorities in consultation with the airspace designers to keep commercial UAS operations out of the non-segregated airspace in which manned aircrafts operate.

(d) **UAS Traffic Management:** A UAS Traffic Management should be responsible for managing UAS induced traffic, especially in the Drone Corridor.

(e) **Pilot Training:** Improved and advance pilot training methods should be introduced to meet the professional requirements under CAR 2.0.

(f) **Droneports:** Designated areas dedicated to facilitate take-off and landing of the UAS.

(g) **Payload/cargo:** Commercial UAS operations will foster various new forms of air freight capabilities.

(h) **Make in India:** 100% FDI in UAS and RPAS-based commercial civil aviation services would provide a boost to the make in India initiative in this industry.

These represent exciting possibilities of drone use in health, agriculture, and general logistics. In a country like India, this opens vast possibilities of investments and partnerships in the entire drone industry landscape.

CONCLUSION

During the year, there have been path breaking developments in the Civil Aviation sector in India. These have addresses policy, taxes, and other reforms to continue robust growth in the sector, and to welcome and aid new investments in continuing to expand both volumes as well as the infrastructure assets.

European countries can continue to see India as a preferred partner in the sector. The growth is continuing, and it has still virgin markets to explore.

NOTE

Banking

Acknowledgements: Peter Born (Commerzbank AG) – Chairperson, Banking Sector Committee & its Members
Knowledge Partner: Jairaj Purandare – JMP Advisors

EXECUTIVE SUMMARY

The banking sector in India has been witnessing phenomenal changes since liberalisation of the economy and over the years, some of the largest banks in the world have set up their presence in India. The European banks operating in India supplement the strong economic partnership between India and Europe and support the business interests of Europe in India.

While acknowledging the efforts of the Indian Government to bring in reforms for the banking sector, EBG Federation would request that efforts may be directed towards addressing certain issues which still remain unresolved. In order to facilitate the Government's efforts in addressing the issues faced by European banks in India, EBG Federation has set out below the key regulatory and tax concerns of the European banks operating in India.

Regulatory/commercial considerations

This year, EBG Federation proposes to identity and focus on the following issues:

1. Aligning the minimum capital requirements of Basel III for Common Equity Tier-1 with RBI requirements.
2. Deferring the implementation of the Large Exposures Framework with regard to interbank exposures
3. Dealing with the issue of expiring international investment agreements that India has executed with European countries.
4. Reworking the priority sector norms to align them with the overall status granted to foreign bank branches operating in India regardless of number of branches and scale of operations.
5. Acknowledging the role of custodians in facilitating foreign portfolio investments, the rights, duties and obligations cast on the custodians and freeing them from the risk or exposure to tax attributable to the foreign portfolio investors, recognising that regulations should capture the risk of loss of revenue rather than placing it on the custodian who is only a facilitator.
6. Applicability of RBI's Discussion Paper on Governance to Branches of Foreign Banks

Key tax considerations

The tax issues are summarised in detail in the paper. Some of these issues have been a challenge for foreign banks in India for a few years now and EBG Federation would urge a speedy resolution to these if found appropriate in the context of the overall policy framework of the Government.

1. BACKGROUND

Based on the announcements made by the Indian Finance Minister in the Union Budget 2020-21 on 1 February 2020, EBG Federation believes that this Government attaches much importance to the banking and financial services sector in India. While several reforms have been announced for banks in the past few years, EBG Federation believes that it is necessary to continually refine the policies to improve the banking business. To achieve this goal, EBG Federation is pleased to present this paper which discusses the key regulatory and tax issues which could act as a roadblock for the European banks operating in India.

2. GENERIC INDUSTRY ISSUES

2.1 Key regulatory issues

- Storage of payment systems' data and cross border data transfers
- Inconsistency in minimum capital requirements vis-à-vis Basel norms
- Large Exposures Framework
- 24 X 7 Market access
- International investment treaties
- Enhancing limit of bank credit to NBFCs for on-lending eligible for Priority Sector Lending (PSL)
- Netting bills
- Priority sector lending requirements
- Applicability of RBI Discussion Paper on Governance in Branches of Foreign Banks

2.2 Key tax issues

- Rationalisation and parity of tax rates between foreign and domestic companies
- Tax issues for custodian banks relating to Foreign Portfolio Investors
- Availability of concessional tax rate of 5% on interest income arising to Foreign Portfolio Investment
- Taxation of dividend in the hands of FPIs
- Exclusion of financial services industry from the ambit of Equalisation Levy applicable on E-commerce Supply or Services w.e.f. 1 April 2020
- Issues relating to applicability of indirect transfer provisions per section 9 of the Act to FPIs:
- Levy of differential Securities Transaction Tax on FPIs in lieu of Capital Gains tax on Listed Securities
- Tax regime for India-based fund managers
- Interest paid by Indian branch of a foreign bank to its head office/overseas group offices
- Deduction for provision for non-performing assets in the books of foreign banks
- Non-applicability of withholding tax provisions on interest payments made to foreign banks
- Tax issues in connection with conversion of Indian branches of foreign banks into subsidiaries
- TDS on cash withdrawals:
- Exclusion of Banks from the applicability of Section 269SU
- GST on foreign bank charges
- Tax deducted at source (GST TDS)

3. KEY ISSUES AND RECOMMENDATIONS

3.1 Key Regulatory Issues

3.1.1 Storage of payment systems' data and cross-border data transfers

Background:

In recent years, there has been a considerable growth in the payments ecosystem in the country. However, all payments system providers do not store the payments data in India. Therefore, RBI issued a circular no. RBI/2017-18/153 on 6 April 2018 requiring all the payment system providers to store the entire data relating to payments systems operated by them only in India. As per the said circular, this data should include the end to end transaction details/information collected/ carried/ processes as part of the message/payment instruction. Further, for the foreign leg of the transaction, the data, if any, can be stored in the foreign country, if required. Thereafter, based on the clarification issued by the Indian Banks Association (IBA) pursuant to its meeting with the RBI, all banks operating in India are required to adhere to the guidelines laid down by RBI. Therefore, all foreign banks including European banks which provide payment services in India will be required to comply with the data storage requirements specified by the RBI. Further, those European banks which use the services of third parties for payment services such as credit cards, internet banking, mobile payments, and payment gateways will need to ensure that the third-party service providers comply with the abovementioned RBI guidelines.

In addition, sections 40 and 41 of the Personal Data Protection Bill, 2018 (PDPB) outline restrictions and requirements around the location and transfer of personal and sensitive personal data.

On perusal of the PDPB as well as the RBI circular on local storage of payments systems data, it follows that copies or originals of certain categories of data, as applicable, are required to be maintained by European banks only on servers physically located within India.

Issues:

Data localisation may result in significant costs and unintended consequences, like loss of time and resources in setting up new data centres, modifying the network architecture or using local cloud vendors. From the perspective that India is home to various outsourcing offices, it may not be logistically and legally possible for overseas entities to locate data within India due to logistic and legal impediments.

Data localisation undermines the effectiveness of a financial institution's international risk monitoring programme. For example, compliance with anti-money laundering laws and sanctions requires a comprehensive and holistic approach, whereby quantification of risk encompasses a customer's entire relationship across a financial institution in a location agnostic manner. Aggregation of data on a client's activity across borders allows a holistic assessment of the said client's global activity for better informed decision making, whereas creation of national silos of information prevents the seamlessness of such programmes, while, at the same time, negatively impacting seamlessness of user experience.

Recommendation:

EBG Federation recommends that PDPB should permit transfers of all kinds of data, without the proposed limitations on categories of sensitive or critical personal data. The movement and storage of data across national borders is essential to providing cross-jurisdictional and core products and services to customers. It is also fundamental to manage risks across affiliates and borders, and comply with financial regulatory requirements across jurisdictions (including those related to Know-Your-Customer and anti-money laundering laws).

3.1.2 Inconsistency in minimum Capital Requirements vis-à-vis Basel norms

Background:

The Basel Committee on Banking Supervision (BCBS) issued a comprehensive reform package entitled 'Basel III: A global regulatory framework for more resilient banks and banking systems' in December 2010, with the objective to improve the banking sector's ability to absorb shocks arising from financial and economic stress, whatever the source, thus reducing the risk of spill-over from the financial sector to the real economy. BCBS specifies the minimum capital requirements and its components which includes Common Equity Tier (CET), Capital Conservation Buffer and Total Capital Ratio. The Basel III reforms also introduced a new capital charge for the risk of loss due to the deterioration in the creditworthiness of the counterparty to a derivatives transaction or a Securities Financing Transaction (SFT). This potential mark-to-market loss is known as Credit Value Adjustment (CVA) risk. It captures changes in counterparty credit spreads and other market risk factors.

Issue:

1. According to BCBS, the minimum CET 1 to risk weighted assets ratio required is 4.5%. However, according to RBI, minimum CET 1 required is 5.5%. While all the other capital requirements (Capital Conservation Buffer, Countercyclical Buffer, GSIB's additional capital) are synchronised with BCBS Norms, minimum CET alone has been a divergent. As RBI strives to be consistent with global practices, this divergence has not been

capital efficient. For an exposure with similar characteristics, the capital set aside in India will be higher compared to other Basel compliant countries.

2. Currently, the CVA charge is computed on the exposures of the foreign bank branches to their Head Office. This results in branches providing additional capital for change in credit spreads of the parent entity which is counter intuitive. In fact, a deterioration in the parent rating would be a Debit Value Adjustment (DVA) for the branch.

Recommendation:

EBG Federation recommends the following:

1. Allow Indian branches of foreign banks to exclude the exposures to the parent for the purpose of computing CVA capital charge.
2. The RBI requirement regarding CET 1 should be fully aligned with the Basel III capital requirement. Accordingly, the banks operating in India, including foreign banks should be required to meet the CET 1 at 4.5% only. This will help all the banks to operate on par with their global peers.

3.1.3 Large Exposures Framework

Background:

In order to align the exposure norms for Indian banks with the BCBS standards, the RBI has laid down certain guidelines on the Large Exposures Framework (LEF) on 1 December 2016, which was subsequently revised on 3 June 2019. The said guidelines are aimed at tightening the norms pertaining to concentration risks of banks, especially in relation to large borrowers, by setting prudential limits on large exposures to a single borrower or a closely related group of borrowers. The said guidelines have come into effect from 1 April 2019.

Issues:

1. Derivatives Exposures: The existing regulatory methodology for computing exposures on the over-the-counter (OTC) derivatives (and any other instrument with counterparty credit risk) using the Current Exposure Method (CEM) as prescribed by the RBI has shortcomings. CEM does not take into account the benefits of portfolio diversification, hedging and other risk mitigation techniques. Using CEM alongside an advanced framework such as LEF may cause unintended consequences for banks resulting in banks having to limit their exposures because of overestimation of counterparty risk using the existing methodology as opposed to the intent of the LEF guidelines. The single/group counterparty limits per the LEF may therefore be too restrictive, as far as the off-balance sheet market traded exposures are concerned and are not conducive to the overall development of a liquid OTC derivatives market with adequate depth. This in turn will hinder banks' ability to manage/hedge their risks efficiently. **The current exemption of the Non-centrally cleared derivatives exposures from the purview of exposure limits expires on 1 April 2021**. If the bank has to liquidate its positions when the existing exemption expires, this may adversely impact the market stability.

2. Head office Exposures: Per the LEF circular issued by RBI, "….for Indian branches of foreign G-SIBs, exposure limit on a G-SIB, including their head office, will be 20% of eligible capital base and exposure limit on any other bank (i.e., not G-SIB) will be 25% of eligible capital base. Similarly, for Indian branches of foreign non-GSIBs, exposure limit on a non-GSIB, including their head office, will be 25% of eligible capital base and exposure limit on a G-SIB will be 20% of eligible capital base…." Thus, the revised LEF circular has brought Head Office/Branches exposure within the purview which were exempted from single/group borrower limits earlier. This severely restricts the ability of the branches of the foreign banks in India to hedge/mitigate their risks with their parent entity. The branches of these foreign Banks rely on their parent entities for more efficient pricing which in turn improves the efficiency of the local market.

   The exposure of a foreign bank's branch in India to its Head Office (HO)/branches is currently within the scope of the LEF guidelines. This restricts the ability of a foreign bank's branch to hedge the risks with its parent thereby impacting the overall efficiency of the market.

   The current exemption on the non-centrally cleared derivatives exposures from the purview of LEF would end on 1 April 2021. The existing regulatory methodology (Current Exposure Method) for computing counterparty exposures on derivatives has shortcomings. It does not take into account the benefits of portfolio diversification, hedging and other risk mitigation techniques. Using CEM alongside an advanced framework such as LEF may cause unintended consequences for banks resulting in banks having to limit their exposures due to overestimation of counterparty risk using the existing methodology as opposed to the intent of the LEF guidelines.

3. Netting and Margining: The existing regulations do not permit netting while computing the counterparty credit risk exposures. Additionally, many banks have Global Credit Support Annexed (CSA) to manage the margining and collateral more efficiently with other interbank counterparties. The collateral exchanged under these Global CSAs are not allowed to be considered for the purpose of computing the counterparty exposures in India.

4. Under the normal FPI quota, not more than 30% of an FPI portfolio (government securities/state development loans (SDL)/corporate bonds) can be in bonds maturing in less than 1 year (increased from 20% recently). This regulation reduces flexibility for an FPI to hold bonds till maturity, because the portfolio needs to be continuously balanced to ensure that this restriction is adhered to. Although there is an exemption of this rule under the VRR route, it entails a minimum lock-in period for investments.

Recommendation:

EBG Federation recommends the following:

1. To extend the exemption of the Non-centrally cleared Derivatives exposure from the scope of LEF till the implementation of Basel III recommended methodology for computing counterparty credit risk (SA-CCR) along with netting and margining.
2. Exclude back to back derivatives exposures to head office from scope of LEF altogether to enable foreign Bank's branches in India to offer hedging solutions to the local market participants, or
3. Include only net MTM for calculation of exposures to HO rather than positive MTM + PFE. Computation of capital charge needs to incorporate a forward looking element in the form of PFE given the medium term nature of such planning. However, for computing the current exposure to a counterparty under LEF, only net MTM as on the date of computation should be taken to reflect the outstanding exposure.
4. Exclude the Exposures to HO/Branches of HO from the purview of the LEF to enable foreign Bank's branches in India to offer hedging solutions to the local market participants and also to manage its local onshore risk efficiently.
5. To provide greater flexibility to FPIs by expanding the FPI quota for investment in bonds maturing in less than year, which is currently at 30% of the FPI portfolio.
6. To exempt the exposures of Foreign Bank Branches in India to their Head Office and other Branches from the exposure limits under LEF.

3.1.4 24 X 7 Market access

Background:

The RBI issued Master Direction dated 7 January 2020 on ‘Risk Management and Inter-bank Dealings’ which permits AD Cat-I banks to voluntarily undertake user and inter-bank transactions beyond onshore market hours’ with a view to enable banks with foreign branches and subsidiaries to undertake foreign exchange transactions with persons resident outside India.

Issue:

These guidelines only enable overseas branches and subsidiaries of Indian banks to execute foreign exchange transactions with non-resident customers.

Recommendation:

EBG Federation wishes to recommend that the said guidelines should also be extended to branches and subsidiaries of foreign banks operating in India. EBG Federation submits that allowing overseas branches and subsidiaries of foreign banks to offer these products, will go a long way in promoting the onshore forex markets to non-residents which is a key driver for this initiative given the physical presence and client access of such foreign banks. We earnestly believe that in the absence of participation from affiliates of foreign banks operating in India, the onshore market may not achieve the desired depth, liquidity and consistent pricing outside India daylight hours. These are key requirements to make the onshore market a viable option for foreigners seeking to hedge their exposures.

3.1.5 International Investment Agreements

Background:

International investment agreements (IIAs) ensure investors compliance with internationally agreed standards of protection. From the point of view of the countries of origin of the investors such IIAs are important corner stones to support the internationalisation of their industries. Therefore, EBG Federation member countries have linked certain support schemes linked to foreign direct investments to the existence of such IIAs. Likewise, the country that receives these investments generally benefits economically, socially, as well as politically making them aspirational for all signatories of an IIAs.

Issues:

Bilateral IIAs between India and certain EBG Federation Member states have either ended or are about to end in due course. With this EBG Federation foresees a hampering of the investment appetite of European investors into India. Likewise, certain promotional schemes for foreign direct investors linked to the existence of IIAs will not be available to investors, making investments into India less attractive.

Recommendation:

To ensure that banks can continue supporting financing foreign direct investments into India, EBG Federation recommends to accelerate renegotiations or an extension of the IIAs.

3.1.6 Enhancing limit of bank credit to NBFCs for on-lending eligible for Priority Sector Lending (PSL)

Background:

In August 2019, Reserve Bank of India provided that credit to Non-banking finance companies (NBFCs)/ Housing Finance Companies (HFCs) other than Micro Finance Institutions (MFIs) for on-lending towards agriculture, micro and small enterprises and housing sector will be eligible for classification under PSL up to a limit of 5% of the individual bank's total PSL on an ongoing basis. This move was undertaken in order to encourage banks to lend to NBFCs, which were undergoing a liquidity crunch. This worked really well and banks used this opportunity to deliver credit to NBFCs.

Recommendation:

It is recommended that instead of 5% this limits gets increased to 10% with a flexibility between NBFCs/HFCs separately on a sustainable basis. This should increase bank funding to the NBFCs/HFCs which significantly support PSL and reach to those customers which bank is not able to reach with given constraints.

3.1.7 Netting bills

Background:

As per the Discussion Paper on Margin Requirements for non-centrally cleared derivatives issued in 2016, the RBI has stated that the methodology applied to compute margin requirements should be able to capture any loss caused by default of a counterparty with a high degree of confidence. It is further stated in the said paper that due to lack of legal unambiguity on reckoning exposures based on net basis, the requirement of variation and initial margins have to be applied on a contract by contract basis. Portfolio margining models can be used only when RBI specifically permits computation of margins on a portfolio basis.

Issue:

A primary concern of market participants in this regard is the inconsistent netting treatment under the insolvency proceedings to which nationalised banks (such as the State Bank of India) are subject, and those insolvency proceedings to which other domestic companies are subject.

Recommendation:

Requiring margin on a gross (and not net) basis would result in significantly higher costs, would be operationally cumbersome and would also be out of step with global moves towards incentivising bilateral margining of non-centrally cleared derivatives. It is therefore recommended that it is essential to ensure greater consistency in the application of netting in India and aligning the margin requirements with global standards in fulfilment of its G20 commitments. The collateralisation of transactions on a gross basis in light of an assessment that netting is not "unambiguously clear", would only compound counterparty credit exposure.

We understand that the Ministry of Finance, Government of India, intends to achieve a positive netting status for India. This will enable net regulatory capital requirements, promote India as a financial center and encourage increased foreign investments.

The current uncleared margin rules with respect to initial margin and variation margin require multiple cash flows. Additionally, it may result into excess exposure computation. Incorrect exposure number will impact capital adequacy and Risk Weighted Assets. Legal clarity on netting will result in the exposure and margin numbers being aligned resulting in a more accurate exposure picture. We request that the swift passage of the Netting Bill be encouraged by RBI and that uncleared margin rules should not be implemented until the Netting Bill is adopted, so that the two are aligned.

3.1.9 Priority sector lending requirements

PSL Targets	PSL norms before July 2012	Revised PSL norms issued in July 2012 (banks with 20 or more branches)	Revised PSL norms issued in July 2012 (banks with less than 20 branches)	**Revised PSL norms issued in March 2018 (banks with 20 or more branches)**	**Revised PSL norms issued in March 2018 (banks with less than 20 branches)**
Overall PSL targets	32%	40%	32%	40%	40%
Agricultural lending	Nil	18%[1]	Nil	18% (8% Sub-target for small and marginal farmers)	Nil
Micro and small enterprises (MSE)	10%	Nil	Nil	7.5% sub-target for lending to micro enterprises	Nil
Export credit	12%	Nil	Nil	Nil	Nil
Weaker sections of society	Nil	10%	Nil	10%	Nil

Background:

The Reserve Bank of India (RBI) revised the Priority Sector Lending (PSL) norms applicable to commercial banks operating in India in July 2012. The revised PSL norms place foreign banks with 20 or more branches in India at par with Indian banks. Such foreign banks were granted the flexibility to achieve these norms within a five-year period to end on 31 March 2018. Foreign banks with less than 20 branches were permitted to retain their original PSL obligations, with no sub-limits within the overall PSL norms.

The PSL guidelines were further modified on 23 April 2015 by RBI (final PSL guidelines). The table below provides the changing scenario of PSL norms for foreign banks in India over the recent past:

Recommendations:

EBG Federation seeks to address the issue from three perspectives:

- In terms of the capabilities and global experience of EBG Federation constituents in areas where we believe we add value to the Indian economy.
- Areas which we lack both global and domestic expertise which we believe we should be exempted from.
- Areas which require minor regulatory changes to increase the flow of credit to needy segments of the economy.

EBG Federation makes the following recommendations:

(i) EBG Federation recognises the need for the approach adopted by the RBI and agrees that banks present in India should all in one way or another participate in reaching RBI's objectives. However, different banks have different expertise and capabilities. Accordingly, while all banks should be required to fulfil PSL targets, EBG Federation recommends that the choice of achieving priority sector should be left to the banks discretion, with such discretion being exercised within a wider range of RBI approved PSL target segments.

(ii) **Widen the definition of priority sector eligible categories**

The Government of India's de-recognition of general exports as Priority Sector Lending (PSL) eligible has limited avenues for foreign banks to fulfil their obligations.

EBG Federation respectfully requests to review the current imperative priorities of the economy against the extant priority sector guidelines. EBG Federation recommends that the components of priority sector for the purpose of achieving PSL targets should be widened to include:

a. **Infrastructure/ Renewable sector lending:** As per the PSL guidelines, Bank loans up to a limit of INR 15 crore to borrowers for purposes like solar-based power generators, biomass-based power generators, wind mills, micro-hydel plants and for non-conventional energy-based public utilities Viz. Street lighting systems, and remote village electrification are considered as PSL. Given the importance of the Renewable Energy sector and the fact that it is not viable to run a project in this sector with INR 15 crore, EBG Federation recommends an increase in the limits from INR 15 crore to INR 150 crore.

b. The scope of PSL activities should be expanded to cover higher exposure to sectors such as service, warehousing, energy and higher education which are already existing PSL areas.

c. Indirect lending to the agricultural sector, MSE advances, lending to weaker sections of the society without any specific sub-targets (for foreign banks with 20 + branches), and finally,

(iii) The framework for **PSLCs be widened to include RBI regulated NBFCs and micro finance institutions.** These would lead to a deepening of the market place and true price discovery.

(iv) **A new PSLC category:** PSLC exports should be introduced to assist smaller banks with less than 20 branches meet the 40 percent criteria. This allows larger banks to continue to originate export credit despite the reduced emphasis and allows foreign banks with less than 20 branches access to a market trading platform for meeting their obligations under 'exports'.

(v) **Sub-target in small and marginal farmers lending & Non Corporate farmers lending targets**

A sub-target of 8% of adjusted net bank credit (ANBC) for lending to small and marginal formers and to ensure that the overall lending to non-corporate farmers does not fall below the system-wide average of the last three years' achievement. All efforts should be maintained to reach the level of 13.5% direct lending to the beneficiaries who earlier constituted the direct agriculture sector. The applicable system wide average figure as applicable to domestic banks and made applicable for foreign banks with 20 branches and above from FY2019-20, for computing achievement under priority sector lending will be notified every year. For FY2019-20, the applicable system wide average figure is 12.11% has been imposed for foreign banks with more than 20 branches. Foreign banks, including those with 20 or more branches, should be exempt from this sub target of lending to small and marginal farmers. Agriculture is a new target segment and given the lack of expertise, geographic reach and credit experience, it has been extremely difficult for foreign banks to direct 18% of their entire lending to this sector. Foreign banks have no experience either in India or globally in lending directly to small and marginal farmers. We recommend that foreign banks including those with 20 or more branches be exempted from this mandatory lending to small and marginal farmers and non-corporate farmer targets.

EBG Federation would like to bring to your attention that while PSL targets have been harmonised for foreign banks (20 or more branches) with domestic schedule banks, the enablers to reach out to the target segment as provided to domestic schedule banks like are missing:

1. Domestic banks can appoint NBFCs as Business Correspondent.
2. Domestic banks do not have distance criteria restrictions for BCs.
3. Interest subvention scheme

(vi) **Targets for Micro, Small and Medium Enterprises (MSMEs)**

MSMEs typically operate in industrial clusters. Such clusters are usually at non metro centres. Accessing these centres is difficult for foreign banks. Hence, we recommend the sub-target for lending to micro enterprises should not be imposed on foreign banks, including foreign banks with 20 plus branches.

(vii) **Market structures: On-lending, securitisation and assignments**

Over a period of time, RBI has deemed on-lending to NBFCs involved in lending to the priority sector segments as being ineligible for PSL purposes which lately it has been reintroduced with caps. EBG Federation believes that reintroduction of credit enhancement in assignment transactions can significantly boost flow of credit. A control mechanism to check PSL contribution and KYC policy adherence could be defined for this purpose. Separately, it is EBG Federation's view that the interest rate cap should be delinked from the base rate of the investing/purchasing bank to provide a level playing field for all banks. It is EBG Federation's recommendation that the interest rate cap regulation should be withdrawn and free market risk-based pricing should be permitted.

Credit Enhancement for securitised transactions should be ring fenced and out of the liquidator's purview or NIL TDS on deposits in the name of Trust for such transactions,

(viii) Based on the data published by RBI[2] overall weaker section achievement at banking system level has never crossed 10% since 1991. Data for March 2015 indicates that only PSU banks achieve their weaker section targets (marginally above the target of 10%). Private sector banks, which also use business correspondents extensively, have averaged at around 6% on weaker section achievement. Average achievement for foreign banks with 20 or more branches for Weaker Section is at 0.9% of ANBC. Further, most of weaker section asset book at the banking industry level is done by lending to Small/Marginal farmers which requires deep rural penetration and such network is not accessible to foreign banks.

Hence to achieve weaker section numbers foreign banks with 20 or more branches are required to buy Small & Marginal Farmer PSLCs, resulting in indirect loading of SF/MF targets as well. Since the banking system at an aggregate level does not have surplus in weaker section category, the availability of these PSLCs is currently less (with high cost) and there is no certainty of their continued availability.

In view of the above factors, achieving weaker section through self-origination or PSLCs is unlikely to be sustainable for foreign banks having 20 or more branches).

(ix) **Qualify activities undertaken by banks for CSR activities** Specific to certain areas such as financial literacy and promoting financial inclusion as PSL, or alternately permit a set-off against the ANBC numbers which define the overall OSL targets.

(x) Adapt the Inter-Bank Participation Certificate (IBPC) Scheme to **permit full participation benefits** for both originator and investor.

(xi) Foreign banks to be allowed to maintain Agricultural PSL numbers on year end basis as against the quarterly average requirement.

(xii) Banks to be allowed to generate PSL assets through Fintech platforms;

Banks to be lending to Fintechs who will be sourcing PSL eligible loans (MSME, Agriculture) through their platforms, this category will be similar to Direct lending to Micro Finance Institutions.

3.1.10 RBI Discussion Paper on Governance in Commercial Banks

Background:

RBI has put out a Discussion Paper aiming for higher aspirational standards in governance for entities engaged in financial intermediation in India.

Issues:

The RBI Discussion paper stipulates a requirement for banks including Foreign Banks operating under Branch Model (FBOBM) to have a Board of Directors with Independent Directors, a Memorandum & Articles of Association, and to conduct Annual General meeting of shareholders.

Foreign Banks operating under Branch Model (FBOBM) have a different legal and governance structure from Foreign Banks operating under Wholly Owned Subsidiary Model (FBOSM) and private/public sector banks. An FBOBM is not a locally incorporated entity, does not have a share capital and operates through the Tier I and Tier II capital requirements of RBI, with the entire capital funded by the respective head offices. There is no requirement under Indian laws, including under the Companies Act, 2013 or the Banking Regulation Act, 1949, for a branch of a foreign bank to constitute a 'board of directors'. Moreover, shareholders are based in geographies where the parent entity is listed, and it would be challenging to have shareholder meetings as specified in the Paper.

Further, Corporate Governance is a continued focus at foreign banks where the bank / bank holding company is incorporated per the prevailing rules in the home country, starting with the Board of Directors (Board) at the global level. The respective Boards seeks to manage its legal entities, subsidiaries and branches with oversight and controls appropriate for their respective business activities. In order to provide appropriate standards for legal entity governance, the respective Boards of foreign banks have put in place Governance Policies and Standards, which are also reviewed periodically by the home country regulators. Further, FBOBM has governance, oversight and control from their controlling office/Head Office.

Recommendations:

EBG Federation requests an exemption from the requirement of a "Board of Directors" and conduct of shareholder meetings like AGM for an FBOBM.

We also request the paper to take cognisance of the equivalent governance standards set out in the Global Governance Policies and standards of the foreign banks / bank holding companies, while allowing flexibility to FBOBM to continue with these equivalent standards.

We believe that such a distinct treatment for FBOBM is possible, considering that a similar approach is proposed for public sector banks in the Draft Paper, wherein in case of inconsistency between the provisions of the Discussion Paper with the specific statutes applicable to them or in case the major shareholder (i.e., Government of India) retains its instruction, the latter is deemed to prevail.

It would be relevant to highlight that these requirements are not prevalent in other prominent countries which adopt a similar foreign branch model, like Hong Kong, Singapore, Japan, Thailand, Vietnam, Malaysia, Taiwan, Australia, China, Ireland, Luxembourg, Germany etc. We would also like to draw attention to EU regulations whereby EU branch of non-EU banks are subject to the EU countries requirements (based on the EBA guidelines) where the branch is located but taking into account internal governance arrangements that the branch does not have a management body but persons responsible for directing the business.

3.2 KEY TAX ISSUES

3.2.1 Rationalisation and parity of tax rates between foreign and domestic companies

Background:

Most of the foreign banks in India are set-up in the form of branches which are duly regulated by the RBI and are considered as foreign companies in India per the provisions of the IT Act. Accordingly, the income earned by such branches from their banking operations carried out in India is considered to be in the nature of business income and accordingly, the profits from such business are taxed at the base rate of 40% plus surcharge and health and education cess, as applicable (i.e., maximum rate of 43.68%). In September 2019, a new optional tax regime was introduced for domestic companies. Under this optional regime, the rate of tax for domestic companies is reduced from 30% to 22%, resulting in a maximum tax rate of 25.17% for such companies, subject to certain conditions. Domestic companies which opt this regime will also not be subject to the provisions of Minimum Alternate Tax (MAT).

Further, earlier, the Indian branches of foreign banks were not subject to the payment of Dividend Distribution Tax (DDT) on their distributed profits, while subsidiaries were charged DDT at an effective rate of 21.17% on their distributed profits, which narrowed the gap between the headline tax rates for foreign companies and domestic companies. However, Budget 2020-21 has abolished DDT payable by domestic companies and tax dividends in the hands of the recipient.

Issue:

The reduction in the corporate tax rate for domestic companies coupled with the abolition of DDT creates a significant disparity between the tax rates applicable to foreign companies and to domestic companies (43.68% vis-a-vis 25.17%), specifically when the manner of computation of profits for domestic companies and non-residents operating in India under a branch route is ordinarily identical except for certain restrictions imposed on branches of foreign banks (e.g., deduction for HO expenses, etc.). Globally, the general practice is to have a tax rate parity across all kinds of companies within the same industry. Examples are all BRIC countries except India and a majority of OECD countries (UK, Japan, etc.) as well as important financial centres like Hong Kong & Singapore.

Recommendation:

While abolishing DDT is a positive step, it is recommended that the corporate tax rates for branches of foreign companies be reduced to bring them at par with domestic companies. Foreign banks operate in India as a branch due to regulatory and commercial reasons and a reduction in corporate tax rate for such branches will provide a level playing field as compared to branches of domestic banks and encourage investment by foreign entities that are keen to invest in India through a branch route.

3.2.2 Tax issues for custodian banks relating to Foreign Portfolio Investors

Background:

Foreign banks operating in India facilitate foreign investment by Foreign Portfolio Investments (FPIs) by acting as custodians (cash and securities) for the FPIs investing in India. Prior to the introduction of the Securities and Exchange Board of India (SEBI) FPI Regulations, 2014, the role of the custodian entailed provision of custodial services (such as maintaining accounts of securities, undertaking activities as a domestic depository, collecting the benefits or rights accruing to the client in respect of securities, keeping the client informed of the actions taken, and maintaining and reconciling records) With the introduction of the SEBI FPI Regulations, 2014 and thereafter, SEBI FPI Regulations, 2019, custodians are now notified Designated Depository Participants (DDP) with more responsibilities (such as granting registration to FPIs, surrender of registration, monitoring/clubbing of investment limits and other related responsibilities).

On one hand, while the local custodians are treated as extensions of SEBI and expected to administer the registration process for FPIs, on the other hand, their operations as a custodian expose them to tax challenges. Further, an amendment has been made in the Finance Act, 2020 in the definition of the term “person responsible for paying tax”. In the case of a non-resident, any person authorised by the non-resident or the agent of such non-resident in India will be considered as the person responsible for paying tax. The term “agent” has been defined as a person from or through whom the non-resident is directly or indirectly in receipt of any income. As a result, the local custodians are concerned that they may be considered as “agents” of FPIs and consequently, be exposed to the risk of non-payment/short payment of tax in India by the FPIs.

Given that the FPIs are directly taxpayers in India, there is complete KYC per Indian regulations to be applied to such FPIs and the larger role of a DDP, it is important to release the custodians of the tax risks associated with discharging the custody function. This is important, especially given that the income that a DDP earns form activity of an FPI is very small, relative to the potential tax exposure of the FPI that can devolve onto the DDP.

Issues:

There is an exposure under the Indian tax law that such entities could be held to be representative assessees of their non-resident clients [which will include their FPI clients]. As representative assessees, such entities could be held to be responsible for discharging any shortfall in tax payments due by their clients. Such entities are merely service providers and the fees that they may earn from providing services to their non-resident clients have no linkage with the possible tax exposure of their clients. Hence, if these entities are required to discharge the tax liability of their clients, it could result in a substantial tax burden;

Recommendation:

Banking and broking services providers should not be held to be responsible for the tax liability of their non-resident clients. Such entities have no ability to determine the possible tax liability of their clients, and as such are in no position to exercise any diligence in this regard beyond placing reliance on undertakings provided by their clients and/or advice received from tax consultants. Under the circumstances, it is EBG's recommendation that a specific clarification should be provided so that banking and broking service providers are not held as representative assessees of their clients. EBG Federation further recommends that a separate carve out be made for DDPs in respect of their FPIs from treatment as 'agents/representative assessees'.

3.2.3 Availability of concessional tax rate of 5% on interest income arising to Foreign Portfolio Investors

Background:

The FPI route has become a popular mechanism for undertaking foreign investment as it allows foreign entities to acquire listed securities on Indian stock exchange and to subscribe to non-convertible debentures. The list of instruments in which FPIs can invest is provided in the Para 20(1) of the SEBI (Foreign Portfolio Investors) Regulations, 2019.

SEBI, in the newly notified regulations, has diluted the list of permissible securities in which a FPI can make investment, which, inter-alia includes the following:

- Shares, debentures and warrants issued by a body corporate, listed or to be listed on a recognised stock exchange in India;
- Units of schemes launched by mutual funds under Chapter V, VI-A and VI-B of the SEBI (Mutual Fund) Regulations, 1996;
- Units of schemes floated by a Collective Investment Scheme in accordance with the SEBI (Collective Investment Schemes) Regulations, 1999;
- Any debt securities or other instruments as permitted by the Reserve Bank of India for foreign portfolio investors to invest in from time to time.

With a view to encourage greater off-shore investment in the debt market by FPIs, the concessional tax regime provided in Section 115AD of the Income-tax Act, 1961 (the IT Act) and consequential lower rate of tax deducted at source (TDS) at 5% per section 194LD of the IT Act on the interest earnings from Rupee Denominated Bond (RDB) and Government Securities (G-Sec) have been implemented from June 2013 onward.

The Finance Act, 2020 has extended the concessional withholding tax rate of 5% on interest payable in respect of the investment made in municipal debt securities. Further, the sunset period for the concessional withholding tax regime is extended from 30 June 2020 to 30 June 2023.

The above mentioned concessional tax regime on selected investment instruments is favourable as compared to most of the tax treaties signed by India.

Issue:

Non-commensurate expansion of tax-friendly measures which is explained as follows:

1. On one hand, the Government of India is offering various investment avenues by allowing FPI investment in various instrument whereas on the other hand, concessional tax regime related to interest income, implemented from June 2013 onward, has not ballooned in the same proportions.
2. Interest earned on securities is taxable at 20% except interest on RDB, G-Sec and municipal debt securities and therefore concessional TDS rate at 5% is not available to various other debt instruments wherein FPIs invest.
3. Moreover, per Notification No. 56/2013 dated 29 July 2013 issued by the CBDT in this regard, the concessional tax rate is available only if the rate of interest on RDB is within 500 basis points of applicable base rate of SBI. Considering this condition, it is uncertain if the concessional tax rate of 5% would be applicable for debentures, discounted securities, etc.
4. The higher rate of TDS of 20% on interest income on various other debt instruments like pass through certificate (PTC), unlisted Non-Convertible Debenture, etc. acts as a deterrent for FPIs as against the concessional TDS rate on selected instruments.

Recommendation:

To remove above anomaly in the development in FPI regulation and corresponding applicable tax law, EBG Federation recommends that the scope of concessional taxability of interest income and corresponding TDS of 5% should be expanded to cover all interest earnings by FPIs on all the other permissible debt securities instruments and discounted instruments.

3.2.4. Taxation of dividend in the hands of FPIs

Background:

The Finance Act, 2020 abolished DDT, re-introducing the classical system of dividend taxation with effect from 1 April 2020. Dividend income was exempt upto 31 March 2020 in the hands of the shareholder under section 10(34) of the Act subject to the Indian company paying DDT at the rate of 20.56%. With effect from 1 April 2020, dividends are taxable in the hands of the recipient.

This shall impact FPIs which are specifically governed by the provisions of section 115AD of the Act. As per the existing provisions of section 115AD of the Act, income [other than dividends referred to in section 115-O of the Act] received by FPIs in respect of securities is chargeable to tax at the rate of 20% (plus applicable surcharge and health and education cess).

The Finance Act has further, excluded the reference of section 115-O of the Act from section 115AD. With this amendment, dividend income is now taxable in the hands of the FPIs at the rate of 20% (plus applicable surcharge and health and education cess).

Additionally, it is to be noted that currently, section 196D of the Act creates an obligation to withhold tax at the rate of 20% on the person responsible for making payment of income on securities referred to in section 115AD(1) of the Act (except for interest income under section 194LD) to a FPI, at the time of credit or payment, whichever is earlier.

Issues:

i. Rate of tax on dividend

It is relevant to note that most countries around the world tax domestic corporate dividends at lower rates considering that such profits are already taxed once at the level of the dividend paying company. Accordingly, to align the tax rates in India with other countries, there is a need to amend the provisions of section 115AD of the Act for taxing the dividend income at a rate lower than 20% (say 10%).

Currently, there are provisions under the Act (such as section 194LC or section 194LD) which provide a concessional rate of taxation in respect of certain interest incomes where the recipients of income are non-resident investors. Accordingly, to make the Indian capital markets competitive with the global markets, it is recommended that dividend income be taxed at a rate lower than 20%.

ii. Rate of withholding tax on dividend

Per section 90(2) of the Act, where the tax treaty provides a lower rate of taxation, the same shall prevail over higher rates prescribed under the Act. Accordingly, if withholding on dividend income is mandated at higher rate of 20% under section 196D of the Act (and not at the rates in force), it would amount to withholding of taxes at higher amount than the final tax liability, owing to a lower rate of tax under the tax treaty. Such withholding of tax which is higher than the final tax liability is unwarranted and against the principle of taxation. This may not be intended by the legislature.

Recommendation:

i. It is recommended to provide concessional rate of tax 10% for taxing dividend income received by FPIs under the provisions of section 115AD of the Act.

   Further, while the tax payer can claim refund of higher taxes withheld, it may result in undue hardships and practical difficulties such as cash flow management issues.

ii. In order to curb the above difficulties, it is recommended to amend the provisions of section 196D(1) of the Act to enable withholding at “rates in force” in place of “20%” in line with the provisions of section 195 of the Act to enable application of the lower rate, if any, per the tax treaty, wherever applicable, and avoid unnecessary hardship to FPIs.

   Further, it is also recommended to amend the definition of ‘rates in force’ per section 2(37A)(iii) of the Act to include a reference to section 196D of the Act.

3.2.5. Exclusion of financial services industry from the ambit of Equalisation Levy applicable on E-commerce Supply or Services w.e.f. 1 April 2020

Background:

Finance Act 2020 (FA 2020) has expanded the scope of Equalisation Levy (EL) to introduce a 2% levy on consideration received/ receivable by Non-Resident (NR) E-commerce Operators (EOP) for providing or facilitating Ecommerce Supply or Services (ESS) to certain specified persons. The EL on ESS is applicable w.e.f. 1 April 2020. In this regard, an amendment to Chapter VIII of the Finance Act 2016 (FA 2016) has been enacted.

Issues:

The existing provisions of EL on ESS do not provide for any industry or sector specific exclusion from EL. The said provisions are very wide and have been worded in a way that could have undesired consequences, especially for certain sectors. One such sector is financial services. Given the manner of operation of financial services entities in India and given the fact that in almost all cases, the said entities are required to be both regulated by an appropriate authority and also to have a presence in India in order to operate in India, EL on ESS should not apply to the financial services industry.

There is a need to carve out financial services industry such as banks, non-banking financial companies, primary dealers, asset management companies, insurance and re-insurance companies, broker dealers and their back-office entities from the applicability of EL on ESS. This exclusion is especially relevant for financial organisations that have access to customers in different jurisdictions i.e., multinational financial institutions across banking, asset management, insurance, etc.

The efficacy of global measures such as the ongoing work under Pillar 1 under Action 1 of the Base Erosion and Profit Shifting (BEPS) recommendations of the OECD and which provides a framework for addressing the concerns of the digital economy is highly dependent on a uniform approach being adopted by each member country. Any unilateral measure is not only inconsistent with the global agenda but is also likely to result in undesirable multiple taxation of the same income without any tax credit or an effective opportunity of eliminating such multi taxation.

There are various factors which distinguish the functioning of the financial services industry from the other sectors and hence, there is a need for a specific carve out from the scope of EL on ESS. We have summarised a few key factors below:

Financial sector players are highly regulated by various financial sector regulators. The regulators oversee the functioning of the financial services industry, clientele, sources of earning income, movement of funds within/ outside India, accounting and reporting requirements, etc. Thus, there is already an added layer of regulatory supervision on their service offerings and income generated in India.

Given the nature of services rendered by the financial services sector players, they are typically structured as subsidiaries or locally recognised branches of foreign players. Where a customer of a particular jurisdiction is onboarded, the regulations require the initial relationship to be through a local entity i.e., either a subsidiary or a local branch. Thus, even where the services are rendered digitally, the relationship continues to be with the local entity resulting in profits of these service offerings being taxed in the local jurisdiction.

Even for providing digital services, customers can be onboarded only after carrying out necessary due diligence, Know Your Customer (KYC) checks, Anti-Money Laundering checks, etc. Thus, due to already existing extensive tax reporting obligations, the income from such services is appropriately recognised and taxes are discharged on a timely basis in the jurisdiction of the customers.

In respect of institutional businesses, inter-branch activities and inter-company transaction agreements are very common in the industry. They are extensively undertaken to ensure that the financial risks are centralised, the operations are conducted basis the global brand and quality requirements by the branches/ subsidiaries across jurisdiction. These services are duly compensated within the group due to regulatory and taxation requirements of each jurisdiction.

A large portion of the digital services rendered by offshore financial services entities are rendered to their Indian Group companies. These are subject to GST (under the reverse charge mechanism) and in many cases even withholding tax. A charge of EL will further increase the cost of rendering services from India. Further, given that only fifty% credit is available for GST for banking entities, this is a significant cost increase.

It may be appreciated that tax on digital services is a matter of global debate at various forums. Various consultations were made by the financial services industry across jurisdictions which were duly considered by the governments, thereby providing exclusions to financial services industry from Digital Service Tax (DST). An exclusion has been provided by countries such as the UK, France, Italy, Spain, and New Zealand to financial services industry from the levy of DST.

In light of the above, it is imperative to have a specific exclusion from the provisions of EL on ESS for the financial services industry without which there will be a significant impact on the financial services sector.

Recommendation:

EBG Federation recommends that banks, non-banking financial companies, primary dealers, insurance and reinsurance companies, broker dealers, asset management companies and their back-offices in India be exempt from the EL given the reasons enumerated above.

3.2.6. Issues relating to applicability of indirect transfer provisions per section 9 of the Act to FPIs:

Background:

Finance Act, 2012 inserted certain clarificatory amendments in section 9 of the Act. The amendments, inter-alia, included insertion of Explanation 5 to section 9(1)(i) of the Act to state that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India.

Further, the Finance Act, 2017 introduced a proviso to Explanation 5 to section 9(1)(i) of the Act to state that Explanation 5 shall not apply to any asset or capital asset, being investment held by a non-resident, directly or indirectly in a FPI registered as Category I or Category II under the 2014 Regulations.

The SEBI has recently notified the 2019 Regulations. These regulations have come into force with effect from 23 September 2019 and would supersede the 2014 Regulations.

One of the key changes in the 2019 Regulations is re-categorisation of the FPIs. The 2014 Regulations provided for registration of FPIs under three categories. The 2019 Regulations has reduced the number of FPI Categories from three to two.

As per the 2019 Regulations, Category II shall include all other FPIs not eligible to be included in Category I FPI such as:

a. Appropriately regulated funds not eligible as Category I FPI;

b. Endowments and foundations;

c. Charitable organisations;

d. Corporate bodies;

e. Family offices;

f. Individuals;

g. Appropriately regulated entities investing on behalf of the client per the prescribed conditions; and

h. Unregulated funds in the form of limited liability partnership and trust.

Given the above changes in categorisation of FPIs, the Finance Act, 2020 has inserted a third proviso to Explanation 5 to section 9(1)(i) of the Act providing relief from applicability of indirect transfer provisions to only Category I FPIs under the 2019 Regulations. Additionally, grandfathering is provided from indirect transfer provisions to non-resident investors holding an asset in the erstwhile Category-I and Category-II FPIs (under the 2014 Regulations) upto the date of repeal of the old Regulations i.e., until 22 September 2019.

While the provision of grandfathering to existing non-resident investors is a welcome move, FPIs re-categorised as Category II FPIs under the 2019 Regulations would now be subject to indirect transfer tax provisions in India even though they are regulated by the SEBI.

Issues:

The re-categorisation of FPIs by SEBI has, inter-alia, impacted those FPIs which will now be treated as Category II FPIs as against Category I FPIs in the erstwhile regime e.g., regulated funds which are not from/ whose investment manager is not from FATF countries will be classified as Category II FPI under the SEBI 2019 Regulations vis-à-vis Category I FPI under the SEBI 2014 Regulations. Thus, even though the FPI is a regulated entity in the home jurisdiction, merely as it is/ its investment manager is not from a FATF country, the FPI is considered to be Category II FPI under the 2019 Regulations. It is relevant to note that such FPIs though treated as Category II FPIs, are subject to KYC requirements applicable to Category I FPIs.

Recommendation:

Given the above, based on SEBI 2019 Regulations, exemption from indirect transfer provisions should also be provided to FPIs which are registered under Category II [per SEBI 2019 Regulations].

3.2.7. Levy of differential Securities Transaction Tax on FPIs in lieu of Capital Gains tax on Listed Securities

Background:

In order to make the Indian capital markets more attractive to invite foreign investment and create a vibrant Indian economy, the need for predictable tax treatment in transactions on the stock exchanges is of paramount importance and common around the world. Capital markets require a higher degree of tax certainty as compared to other industries given that millions of capital market transactions are effected every day involving multiple market participants (funds, fund managers, financial institutions, custodians, brokers, etc.).

FPIs are foreign investors that invest in Indian listed securities and derivatives pursuant to and within the scope of the guidelines provided by the SEBI. FPIs are regulated by SEBI and the scope of investments is limited to portfolio investments. SEBI rules prevent Indian nationals from using FPIs, thus prohibiting any round tripping. Private equity/mergers and acquisitions types of transaction fall out of the permitted investment scope of FPIs.

Many of the Funds are public market funds, and tax certainty is absolutely essential for the Funds and the Fund Managers to make their decisions since they need to compute Net Asset Value (NAV) of the units on a daily basis taking into account the income tax applicable on the transaction. Similarly, cross border investors in the Funds, who enter and exit a Fund at varying times at varying prices, also need to compute the NAV of their shares/ units (both realised and unrealised under financial accounting principles), taking into account the tax applicable to the transactions.

Lack of ability to determine an accurate NAV (as a result of tax uncertainty) impedes decision making for the Fund Managers as well as the investors in the Funds. Thus, it is imperative that there is complete clarity on the taxation of the investments.

Further, many FPIs such as banks and financial institutions issue Offshore Derivative Instruments to Funds in accordance with the regulations set forth by SEBI. As such, the Funds are able to gain economic exposure to the Indian market without having to deal with the significant operational difficulties of transacting directly and also obtain leverage. The FPIs, in turn, hedge their exposure under the ODIs via various means, including transacting in the reference Indian securities. The potential applicability of the General Anti-Avoidance Rule (GAAR and uncertainty in their application in the context of cross border transactions where tax treaty relief is sought, and imposition of Capital Gains Tax (CGT) on their hedging transactions will pose significant challenges to these FPIs, and they will not be in a position to practically manage or retain the (uncertain) tax risk in the Indian securities.

Current Indian tax framework for FPIs in India in respect of capital gains and issues arising therefrom.

There exists a concessional income-tax framework for FPIs in India. However, the capital gains tax regime in India is complex compared to other global markets and there are various aspects of the tax system which, as outlined below, make investing into India more onerous relative to other markets.

a) Complex CGT regime under the Act

- Different tax rates and period of holding (to qualify as long-term) for different types of securities i.e., equity shares, mutual fund units, debt securities, futures, etc.
- Computation of capital gains following First-In-First-Out method
- FPIs are required to track transactions resulting into dividend stripping/ bonus stripping to determine capital loss, if any, not allowable
- Restrictions on set-off of capital losses under specific situations
- Requirement to pay quarterly estimated taxes and file detailed annual tax forms and be subjected to scrutiny audit
- Refund of excess taxes paid can take years to obtain (long after the investors in the Fund has changed from when the tax was incurred).

b) Uncertainty relating to GAAR and the Multilateral Instrument (MLI)

GAAR is applicable in India with effect from 1 April 2017. GAAR has the power to override DTAAs. FPIs have been investing in India availing the benefits of the applicable DTAA. Currently, there is no clarity on how GAAR will apply to FPIs availing of DTAA benefits. While India’s DTAA with Mauritius and Singapore have been amended to remove CGT exemption on shares, the respective DTAAs continue to provide benefits for gains on non-share investments (e.g.,, bonds, listed derivatives, etc.) and India has DTAAs with a number of other countries that provide for CGT exemption on shares.

The potential for GAAR to be invoked to override the provisions of a DTAA and impose CGT, interest, and penalties of up to 200% causes significant uncertainty for FPIs causing barriers to investment and negatively impacting the ease of doing business in India. While many countries have some form of GAAR, it has not been an issue for FPIs in other countries, since these countries do not impose CGT on listed securities transactions. Given the unique features of the listed securities market and the tremendous volumes of transactions completed on a daily basis, GAAR together with CGT is ill suited. Further, the MLI which is an outcome of BEPS Action Plan 15 of the OECD intends to offer solutions for governments of various countries to plug loopholes in international tax treaties by transposing results from the BEPS project into bilateral tax treaties worldwide. India is a signatory to the MLI and for approximately 23 DTAAs entered into by India with various countries (i.e.,, Australia, France, Japan, Luxembourg, Netherlands, Singapore, UK, etc.), the MLI is effective from 1 April 2020. Currently, there is no guidance on the manner in which MLI will be applied. Given the lack of clarity on the manner in which anti-abuse provisions (i.e.,, GAAR and MLI) would be applicable to FPIs, a further layer of uncertainty and complexity is added for FPIs in investing in India.

c) High cost of trading

In India, the cost of trading includes several levies like brokerage, service tax, stamp duty, Securities Transaction Tax (STT), SEBI turnover fees, exchange transaction fees and custody fees. These costs, coupled with high tax administrative and compliance costs, result in the overall cost moving upwards. In fact, India is the eighth-most expensive out of 46 countries in levying market charges (both tax and non-tax) globally. The addition of capital gains tax on this would change the result further.

d) Repatriation of Funds & Secondary Tax Liability of Custodians

FPIs need to repatriate the proceeds from the disposal of their investments on a frequent basis, with many requiring daily repatriations. As with other markets, they do not leave idle proceeds in a foreign currency when they should be redeploying it to other investments and managing their foreign exchange risk.

Coupled with this is the obligation that Indian custodians face to set aside taxes when they permit repatriation of funds to FPIs and the potential risk of being treated as representative assesses. They will require provision of tax certification from a certified accounting firm prior to allowing repatriation of funds and will deduct and remit to the government an amount for taxes on gains. This is problematic in (i) hindering the free flow of funds in and out of India, and (ii) FPIs will need to go through the long and difficult tax refund process at the end of the tax year when the total taxes deducted from/paid by the FPIs exceed the actual tax is owed (e.g., subsequent losses can offset earlier gains). When the FPIs obtain a refund years later, the investors in the Funds would have changed.

e) Double Taxation

Imposition of CGT on FPIs can result in double taxation to foreign investors due to the fact that the FPIs will be subject to Indian CGT on their investments in the Indian securities, and then the investors in the FPIs (i.e.,, the investors in the funds) can be taxed again in their home countries when they receive distributions. Further, foreign tax credits (i.e., CGT paid by FPIs to be used as credits to off-set taxes on the investors in the investor's home country) are often not available or difficult to obtain in practice. This is due to (i) the nature of the way investments are typically made (i.e., investments via Funds), and (ii) complex foreign tax credit regimes.

f) While India permits foreign tax credits to offset Indian income taxes, credit is not available where the Indian resident makes the investment via a fund that invests in foreign securities. This is because the foreign CGT would be assessed on the fund and not directly on the Indian investor in the fund.

International practice on taxation of capital gains on portfolio investments by FPIs

Globally, most countries do not impose CGT on listed security transactions of foreign investors on their portfolio investments. In fact, no G20 country imposes capital gains tax on portfolio investment. These include countries such as Australia, China, Hong Kong, Indonesia, Japan, South Korea, Malaysia, New Zealand, Philippines, Singapore and Taiwan in the Asia Pacific region, Austria, Belgium, Cyprus, Denmark, France, Finland, Greece, Germany, Hungary, Ireland, Italy, Luxembourg, Norway, Netherlands and Poland in Europe and Brazil, Canada, Chile, Colombia, Peru and the U.S.

Countries in Asia that impose capital gains tax are limited. To raise revenue, many countries have adopted a transaction-based tax, such as STT or stamp tax on listed securities transactions. These types of taxes are simpler and easier to administer. They achieve the twin goals of raising revenue and providing tax certainty and efficient functioning of the capital markets. Countries generally do not impose both transaction taxes and CGT. For instance, countries like China, Hong Kong, Indonesia, South Korea, Malaysia, Philippines Singapore, Taiwan in the Asia Pacific region, Bulgaria, Cyprus, Greece, Ireland, UK in Europe and Brazil, Chile, Colombia, Peru have either STT or stamp tax.

Globally, India is one of the very few countries that imposes CGT on foreign portfolio investments in listed securities, and even rarer amongst countries that impose both CGT and STT, placing them with countries such as Pakistan and Bangladesh (Pakistan and Bangladesh impose both CGT and STT on FPIs).

Taxes and other levies in India vis-à-vis other countries are higher by about 22%-27% thereby reducing the net proceeds to be received by investors.

Recommendation:

In view of the above and in line with the international tax practice, EBG Federation recommends that FPIs be exempted from

CGT. This is also in line with the recommendation of the Expert Committee on GAAR headed by Dr. Parthasarathi Shome.

If warranted, however, a differentiated STT rate between domestic investors and FPIs can also be considered in lieu of the CGT i.e., a higher STT be levied on FPIs vis a vis domestic taxpayers and an exemption be granted for CGT levied under the Act on income earned by FPIs in the Indian capital market. We note that many countries impose CGT on domestic taxpayers while exempting FPIs (even without imposing a differentiated STT or no transaction taxes at all) and hence, this differentiation is not out of the ordinary (e.g., Australia, China, Japan, Korea, Taiwan, Brazil, etc.).

Without prejudice to the above, EBG Federation recommends that capital gains arising on transfer of shares of companies forming part of the S&P BSE 500 index of the Bombay Stock Exchange should be exempt from tax in the hands of FPIs.

Benefits of utilising STT in Lieu of CGT

The imposition of higher STT in lieu of CGT on FPIs dramatically improves the ease of doing business in India and should:

- Provide tax certainty, predictability, and ease of operation so critical to FPIs
- Lead to a smooth, cost effective and efficient tax collection mechanism
- Create a level playing field for all FPIs investing from any jurisdiction
- Reduce litigation for FPIs
- Free up the resources of the Revenue due to simplification resulting in ease of administration, and allow tax officials to focus on other important areas
- Increase investment flows and liquidity into the Indian capital markets
- Allow corporate India to raise equity resources at higher valuations, lowering funding costs, and improving the Indian economy
- Increase tax revenues

We believe the elimination of the complexity and uncertainty of CGT on FPIs will result in significant increase in STT revenue. This is not just due to an increase in the STT rate. Rather, it will be due to significant increase in investments into and trading in the Indian capital markets. The change will increase the ease of doing business in India, increase the investment and trading from existing FPIs, and encourage new FPIs that have previously been hesitant to invest in the Indian capital markets.

3.2.8 Tax regime for India-based fund managers

Background:

In certain cases, the presence of Fund managers in India may be considered as constituting a Permanent Establishment (PE) for the offshore funds managed by such Fund managers. This may create an additional exposure for the offshore fund and may increase its tax liability in India. Thus, to encourage fund managers to shift their base to India and to alleviate their concerns regarding additional tax consequences as result of this shift, the Finance Act, 2015 had clarified that management of an eligible offshore fund by an eligible fund manager in India shall not create a business connection for the eligible offshore fund in India, subject to certain conditions. The said conditions are onerous for the fund managers and while some of the conditions have been relaxed in the past few years, this was not sufficient impetus for the fund managers to move their base to India.

Issue:

Of the conditions notified in order to be outside the purview of creating a business connection, several are impractical and onerous to comply with. Some examples are requirement of members of the fund not being connected persons, limit on direct or indirect participation interest of the members in the fund, etc.

Recommendation:

It is recommended that the conditions notified, in order to be outside the scope of creating a business connection should be simplified. Further, the India-based fund managers should not be viewed as having a business connection or constituting a PE of the offshore fund in India as long as the offshore fund conducts all its activities in accordance with the applicable regulations of the home country and if the offshore fund adequately compensates the India-based fund manager on an arm's length basis.

3.2.9 Interest paid by the Indian branch of a foreign bank to its head office/overseas group offices

Background:

The Finance Act, 2015 amended the provisions of the Indian tax law to tax the interest that is paid by the Indian branch of a foreign bank to its head office/overseas group office, by treating the Indian bank branch (on the one hand) and its head office/overseas group office (on the other hand) as separate and independent entities.

Issue:

If the interest payments by an Indian branch of a foreign bank to its head office/overseas branch offices are taxed, it is likely to have an adverse impact on foreign banks in India. Foreign banks may pay tax in India at the rate of 40% (plus surcharge and education cess) on the interest that they earn from their Indian branch office, unless they get relief under a tax treaty.

Recommendation:

It is recommended that this amendment be withdrawn with retrospective effect.

3.2.10 Deduction for provision for NPAs in the books of foreign banks

Background:

The Indian tax law provides for deduction of provision for bad and doubtful debts of an amount not exceeding 8.5% of total income computed before claiming deduction under Chapter VIA of the IT Act in the case of Indian banks.

Issue:

In case of foreign banks, the deduction for provision for bad and doubtful debts is available only up to 5% of the total income. The argument put forth for differential rates is that Indian banks are subject to PSL norms (such as lending to the agriculture and education sectors). However, it may be pointed out that foreign banks having 20 or more branches in India are subject to similar PSL norms as Indian banks. Further, foreign banks are already subject to a higher tax rate. Therefore, this is a case of discrimination against foreign banks.

Recommendation:

It is suggested that foreign banks be brought at par with Indian banks and allowed a deduction of provision for NPAs at 8.5% instead of the existing 5%.

3.2.11 Non-applicability of withholding tax provisions on interest payments made to foreign banks

Background:

Currently, a person responsible for making interest payments to an Indian bank is not required to withhold tax on such payments.

Issue:

No such exemption is available with respect to interest payments made to foreign banks. Therefore, foreign banks are required to apply to the Revenue authorities for a NIL withholding tax certificate on an annual basis, which increases their administrative burden.

Recommendation:

It is recommended that an exemption from tax withholding be provided on interest payments made to foreign banks in order to reduce the administrative burden and provide a level playing field.

3.2.12 Tax issues in connection with conversion of Indian branches of foreign banks into wholly owned subsidiaries

Background:

Pursuant to the RBI providing authorisation for conversion of Indian branches of foreign banks into Wholly Owned Subsidiaries (WOS), the Finance Act, 2012 has introduced an exemption from tax on capital gains arising on the conversion of a branch of a foreign bank into a WOS, provided the conversion is in accordance with the scheme framed by RBI in this regard.

A notification dated 6 December 2018 was issued by CBDT to provide much needed clarity on issues connected with conversion such as eligibility for set off of carry forward losses, treatment of unabsorbed depreciation, and tax credits of the branch.

Issues:

There are several issues linked with the conversion of a branch into a WOS which are still required to be clarified such as levy of GST on conversion of branch to a WOS, deduction for various conversion related expenses, non-applicability of MAT and Transfer Pricing related provisions, extension of the tax neutrality to different modes of conversion, clarification on dual residency.

Recommendation:

EBG Federation recommends the following:

i. Specific clarification to be incorporated in the notification or the IT Act that the conditions specified in the notification to be made applicable 'only at the time of conversion' and there will not be any claw back or withdrawal of the capital gains exemption under section 115JG of the IT Act, at a later stage.

Notwithstanding the above, in case conditions relating to claw back of the exemption are to be applied post conversion, then it should be clarified that the conditions will not be applicable to the following events:

- dilution (mandatory or otherwise) pursuant to the RBI guidelines /approval; or
- fresh issuance of shares by the subsidiary; or
- mandatory restructuring (due to home country regulations); or
- internal re-organisation.

ii. An appropriate amendment in the IT Act is required to extend the tax neutrality to conversion through any mode such as amalgamation, slump sale, and demerger, or any other mode of conversion as may be approved by RBI.

iii. Specific clarification to be incorporated that the Minimum Alternate Tax (MAT) under section 115JB will not be applicable in respect of gains, if any, in the books of account of branch on account of such conversion. Suitable amendments are required to be made in sections 115JB and 115JG.

iv. Specific deduction for all conversion related expenditures that may be incurred by the foreign bank under sections 35A, 35AB and 35D of the IT Act;

v. Specific clarification that deduction of expenses under sections 40(a)(i), 40(a)(ia) and 43B of the IT Act which are incurred by the branch but taxes on which are paid by the subsidiary or the expenses are paid by the subsidiary, as the case may be, should be allowed to the subsidiary.

vi. Specific clarification to be incorporated that the transfer pricing provisions under section 92 of the IT Act are not applicable on such conversion and that an APA entered into by the branch should continue to be applicable to the subsidiary for the balance period of APA.

vii. Specific clarification is required for giving eligibility for exemptions/relief on conversion in case of integration of group entities in India and that the shareholder of the subsidiary company can be the parent company or the holding company of the parent entity or any other entity, under the scheme of conversion approved by RBI.

viii. Specific clarification is required to provide that the conversion will be governed by the conditions under the final notification and excluded from purview of definition of amalgamation under section 2(1B). Appropriate amendments will be required to be made in the sections 2(1B) and 115JG.

ix. In anticipation of the dual licensing i.e., presence through both branch and subsidiary mode, a specific clarification is required that the tax neutrality and relief for conversion would be applicable to dual presence structures under a scheme approved by RBI.

x. While carry forward of provisions for bad and doubtful debts has been considered in the final notification, a specific provision is required so that benefit of write-off by subsidiary out of provisions created by the branch will be available to the subsidiary in accordance with the provisions of section 36(1)(vii).

xi. Specific clarification is required that the pre-condition under section 36(2) that "the debt should represent money lent in the ordinary course of business by the taxpayer for purposes of claim of write-off" is not applicable to subsidiary created on conversion with respect to provisions created by the branch and subsequently written off by the subsidiary.

xii. Specific clarification is required to exclude reference to 'direct or indirect benefit or consideration' as it has varied interpretation and risk of potential litigation.

xiii. Specific clarification is required to exclude the conversion from purview of obtaining No Objection Certificate (NOC) under section 281 for transfer of assets from branch to subsidiary on conversion.

xiv. Specific clarification to be provided with respect to withholding tax exemption under section 195(3) to be extended for a limited period of a year post conversion to provide a reasonable timeframe to lay down appropriate systems and processes in place.

xv. Appropriate modifications be carried out in the tax systems to ensure smooth rollover from branch to subsidiary and timely tax compliances with increased focus on technology driven tax administration.

xvi. Certainty that GST will not be levied on the conversion of an Indian branch of a foreign bank to a WOS.

3.2.13. TDS on cash withdrawals

Background

The Finance Act, 2019 introduced section 194N in order to provide for deduction of tax on cash withdrawals to discourage cash transactions and move towards less cash economy with effect from 1 September 2019. As per the said provisions, TDS was applicable at 2% [20%, if no Permanent Account number (PAN)] on cash withdrawals exceeding INR 1 crore. In compliance with section 194N, banks/other specified entities have been deducting TDS on cash withdrawal exceeding INR 1 crore and reporting in the TDS return on a quarterly basis.

An amendment to this section was introduced by the Finance Act, 2020 and is effective from 1 July 2020. This amendment was not a part of the original Finance Bill, 2020 presented on 1 Feb 2020 and was incorporated by way of an amendment to the Finance Bill in March 2020. As per the said amendment, where the person withdrawing cash has failed to file its return of income for all the three financial years preceding the financial year in which the cash withdrawal is made and the due date for filing the returns for the said years has already passed, TDS will apply at an increased base rate of 5% and on a lower threshold of INR 20 lac.

Issues and recommendations:

a. The amendments to the Finance Bill, 2020 were presented in the Parliament on 23 March 2020. Immediately thereafter, a nationwide lockdown was enforced with effect from 25 March 2020 due to the COVID-19 situation. Other than customer-facing branch staff, most other employees of the banks have been working from home. In view of this, practically, it has been difficult for the technical teams to work on system amendments to implement such a change effective from 1 July 2020. In view of this, we request you to grant the banks additional time of at least six months to effectively implement this amendment. Hence, a request is being made to defer the implementation of the revised provision till at least 1 January 2021.

b. Prescribe a standard template of declaration-

   As per the revised provision, the tax rates on cash withdrawals would vary depending on the status of tax return filing for the 3 immediately preceding previous years for which the due date of filing return under Section 139(1) of the Act has not expired. However, there is no guidance as to how banks/other specified entities would get access to such information, since it is not a mandatory requirement for customers to submit the said information to banks.

   Further, it may be appreciated that, different categories of taxpayers, such as individuals, partnership firms, and companies have different due dates for filing the return of income starting from 31 July till 30 November depending upon whether the provisions of Tax audit under Section 44AB of the Act are applicable to them and whether they are required file an Accountants Report in Form 3CEB for international transactions. Therefore, banks would be required to maintain an elaborate tracking of cash withdrawal transactions before and after such due dates during the financial year. This would put a significant pressure on the systems of banks.

   In view of the above, EBG Federation recommends the following amendments:

   - Standard declaration - Considering the practical difficulties involved, the Government may prescribe a standard statutory declaration to be provided by customers to their banks on an annual basis about their income tax return filing status. This would simplify the trigger event and the threshold for withholding tax on cash withdrawals for banks making it easier for them to configure the amendments in the systems.

- Years for which information to be provided: Instead of three immediately preceding previous years, the Government may consider obtaining the return filing data for three immediately preceding assessment years ended. This would ensure that customers would have an opportunity to file their returns and furnish the declarations to banks as on the first day of the financial year. For example, assessment year 2019-20 would end on 31 March 2020. Hence, as on 1 April 2020, the customer would be able to file declaration with the bank for three immediately preceding assessment years ended, i.e., AY 2019-20, AY 2018-19 and AY 2017-18. If the tax policy is meant to give a higher threshold only for taxpayers filing their returns on or before the due date, the same may be accordingly prescribed in the text of the declaration.

- Clarification in respect of tax exempt entities and newly set up entities - There are certain entities (e.g., foreign embassies) which are exempt from filing tax returns in India. However, based on the provisions of the section, non-furnishing of tax returns will attract lower threshold and higher rate of TDS for cash withdrawals done by such entities, which certainly does not seem to be the intention of the law. Further, new entities who are in business for less than three years or who are in the first year of operations, will also face the hardship of being subject to higher rate of tax and lower threshold limit in the event they have not been in a position to comply with the condition of furnishing their return of income for last three years. Hence, a circular/notification clarifying that the provisions of Section 194N should not be applicable or would be applicable only for completed assessment years to such entities should be issued.

- Clarification on the base amount on which tax is to be deducted – The erstwhile provisions of Section 194N required banks to deduct an amount equal to two% of sum exceeding INR 1 crore. However, in the amended section, the requirement is to deduct tax at source on "such sum". This may be interpreted to mean that the tax is required deducted on the entire sum as opposed to cash withdrawal exceeding the prescribed threshold of INR 1 crore or INR 20 lac, as the case may be. Based on the reading of the section along with applicable first proviso, it may not be the intention of the tax policy to change the base of deduction of tax to entire amount of cash withdrawal as compared to the amount exceeding the threshold limit. Hence, EBG Federation recommends that it should be explicitly clarified that tax would continue to deducted only on the amount exceeding the applicable threshold.

3.2.14. Exclusion of Banks from the applicability of Section 269SU

Background:

In order to promote a 'less cash' economy, a new section 269SU was introduced by Finance Act, 2019 to provide that every person carrying on business shall provide the facility for accepting payment through prescribed electronic modes in addition to other electronic modes of payment being provided by businesses with turnover exceeding INR 50 crore during the immediately preceding financial year. Failure to provide the prescribed modes will entail levy of penalty under the newly introduced section 271DB.

In this regard, in addition to any other existing mode of electronic modes of payment, with effect from 1 January 2020, the following electronic modes are notified:

- Debit card powered by RuPay;
- Unified Payments Interface (UPI) (BHIM-UPI); and
- Unified Payments Interface Quick Response Code (UPI QR Code) (BHIM-UPI QR Code)

Any charge including the Merchant Discount Rate (MDR) shall not be applicable on or after 1 January 2020 on payment made through above prescribed electronic modes. The prescribed modes are applicable immediately from 1 January 2020. However, penalty of INR 5,000 per day for non-implication of the aforesaid prescribed modes will only be applicable from 1 February 2020. Hence, effectively the aforesaid modes should be available effective 1 February 2020. In addition to the modes prescribed by the CBDT, the existing electronic modes of payments (i.e., NEFT, RTGS etc.) continue to be valid.

Further, the CBDT has recently clarified that the provisions of section 269SU of the Act shall not apply to specified persons who only have B2B transactions and at least 95% of aggregate of all amounts received by such persons during a year (including sales / turnover / gross receipts) are by any mode other than cash.

Issues:

The dispensation provided by CBDT is only for entities having B2B transactions and not for B2C transactions. Almost all banks have retail clients and hence, the relaxation provided by CBDT will not be of any help to the banks.

Further, the Finance Minister in the Budget Speech 2019 stated the following:

"to promote digital payments further, I propose to take a slew of measures. … . Further, there are low-cost digital modes of payments such as BHIM, UPI, UPI-QR Code, Aadhar Pay, certain Debit cards, NEFT, and RTGS, which can be used to promote less cash economy. I, therefore, propose that the business establishments with annual turnover more than INR 50 crore shall offer such low cost digital modes of payment to their customers and no charges or Merchant Discount Rate shall be imposed on customers as well as merchants. RBI and banks will absorb these costs from the savings that will accrue to them on account of handling less cash economy as people move to these digital modes of payment." Thus, it is clear that RBI and banks will act as a mere facilitator of payment transactions through digital modes and hence, logically, these provisions should not be made applicable to banks.

With business spread across length and breadth of country and with very large number of branches, POS machine has to be installed, QR code to be enabled for every branch and configuring accounting aspect in CBS system.

Recommendation:

Banks should be specifically exempted from the applicability of the provisions of section 269SU.

3.2.15 GST on foreign bank charges

Background:

The Goods and Services Tax (GST) authorities have taken a position that the overseas correspondent bank charges are part of the overall services rendered by the bank in India. Accordingly, the banks in India are the recipient of the services provided by the overseas banks and therefore, are liable to pay GST under the reverse charge mechanism

On the other hand, the banking industry has taken a position that the customer (and not the bank in India) is the recipient of service of the overseas bank's services for the following reasons:

- There is no specific written contact between Indian bank and overseas correspondent bank(s)
- The transaction commences at the behest of the customer who instructs the bank in India to collect / remit the amounts in its favour from the overseas correspondent bank(s).
- Bank charges are not a cost of operation for the bank in India and the same are born by the customer

Further, the Central Board of Indirect Tax and Customs (CBIC) has published Frequently Asked Questions (FAQs) for the financial services sector, covering banks, Non-banking financial companies (NBFC's) and insurance companies on June 3, 2018. As per the said FAQs it has been clarified that in the present situation, there are <u>two supplies</u> namely, one from the bank in India to the importer/exporter and one from the overseas correspondent banks to the bank in India. Hence, the liability to discharge GST on such supplies will be required to be determined accordingly.

Issues:

Determination of recipient of service with respect to charges levied by the overseas correspondent banks to the bank in India

Recommendation:

For the first supply, (i.e., the bank in India to the exporter/ importer), the bank in India would be paying GST on the fee / commission income for the services provided to the customer.

For the second supply, the bank in India would communicate the total charges deducted as overseas correspondent bank charges to the customer. Thus, the recipient (the customer) should pay IGST on the overseas bank's charges, under the reverse charge mechanism.

The bank in India, should **not be** paying GST on correspondent bank charges for the following reasons:

- The bank in India is only acting as a liaison between the Indian exporter / importer and the foreign bank.
- The remittance is collected by the bank in India on behalf of its Indian customer.
- The bank in India is not the service recipient of the services rendered by overseas correspondent bank(s) in this transaction structure.

3.2.16 Tax deducted at source (GST TDS)

Background:

The Central Government, on the recommendation of the GST Council, had issued a notification No 61/2018- Central Tax, dated November 5, 2018 stating that the provisions of GST TDS would not be applicable if the services are provided from one public sector undertaking bank to another public sector undertaking bank.

Issues:

The benefit of this exemption is not extended when the payments are made by a public sector undertaking bank to a foreign / private bank.

Recommendation:

The benefit of this exemption should also be extended when the payment is received from a public sector undertaking bank by a foreign / private bank for the following reasons:

- Indian and foreign banks, render services to numerous persons specified u/s. 51 of the CGST Act and Notification No. 50 / 2018 dated 13 September 2018.
- The specified persons i.e., the recipients, would now be required to deduct tax at source under provisions of Section 51 and 20(x) and deposit the same into the Government Treasury.
- It is submitted that the business of all banks including is highly regulated and subjected to strict supervision of the RBI.
- The transactions effected by the foreign banks are duly reported in the GST Network along with the returns in Form GSTR-1.
- The books of account of the foreign banks would also be subjected to audit by a Chartered Accountant / Cost Accountant under provisions of Section 35(5) read with 44(2) of the CGST Act.

From the above, it would be evident that there exists a strong trail of transactions effected by the foreign banks and also the primary objective of the Government in introducing the said provision was to stop evasion in the unorganised sector and provide for tracking. Hence, bank to bank transactions should be excluded for deducting GST TDS i.e., when the payments are remitted by the public sector undertaking banks to foreign banks.

CONCLUSION

EBG Federation believes that despite the current COVID-19 pandemic, the Indian economy is on the path of recovery and will soon progress on its growth trajectory. Banks and financial institutions will certainly have a key role in facilitating the growth of the economy. EBG Federation looks forward to contributing actively in this process and is of the view that its recommendations as set out above, if implemented, will act as a catalyst in deepening the range of financial products and services available to customers in India. It will also improve the access to cost effective financial services, thereby enhancing the competitiveness of Indian businesses, and in furthering the objectives of the government and the RBI of extending the reach of financial services across the economy.

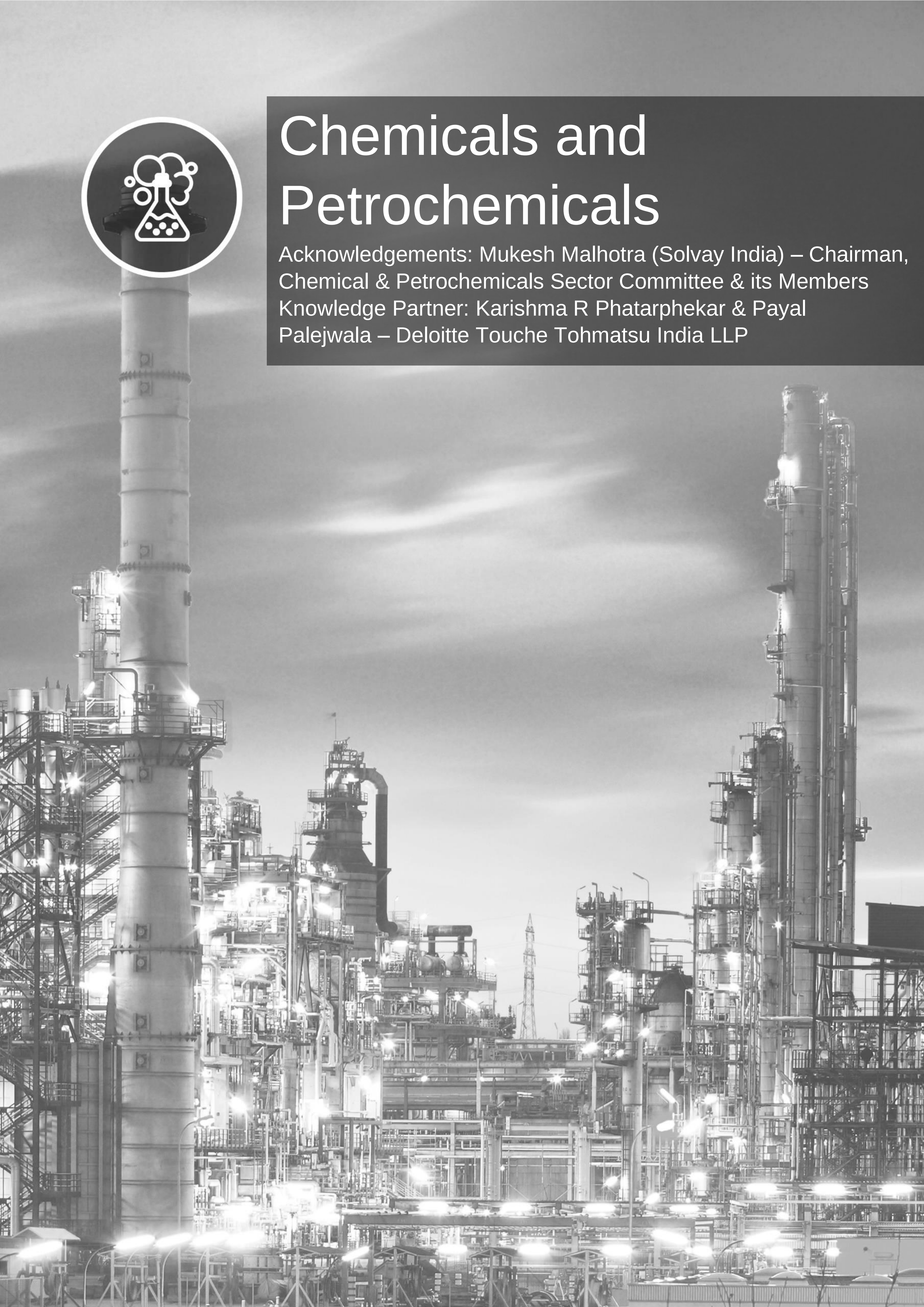
ENDNOTE

1. Within this, not more than 25 percent should relate to indirect lending.
2. Report of the Internal Working Group to Revisit the Existing Priority Sector Lending Guidelines `2 March 2015); and Database on Indian Economy – https://dbie.rbi.orgsssss.in

NOTE

Chemicals and Petrochemicals

Acknowledgements: Mukesh Malhotra (Solvay India) – Chairman, Chemical & Petrochemicals Sector Committee & its Members
Knowledge Partner: Karishma R Phatarphekar & Payal Palejwala – Deloitte Touche Tohmatsu India LLP



EXECUTIVE SUMMARY

Global chemicals market is expected to grow at 5.5% per annum to reach a market size of US$5.7 trillion (~5.3 trillion Euros) by 2020. The global chemicals market is expected to keep growing as a result of increased urbanisation and growing markets in developing countries such as India, Turkey and Thailand. Countries with a mature market such as China, Australia and Germany are also expected to see accelerated growth as they switch to higher value specialty and pharmaceutical chemicals.

The Indian chemicals market accounts for nearly 3% of the global chemicals industry and has potential to reach US$226 million by FY2020 growing at a Compounded Annual Growth Rate (CAGR) of about 9% and in an optimistic scenario, US$248 billion at a CAGR of 11%. The industry contributes about 2.11% of India's Gross Domestic Product (GDP). Some of the key growth drivers for Indian chemical industry are large population, huge domestic dependence on agriculture and strong exports, cost competitive manufacturing.

Government initiatives such as 'Make in India' is encouraging companies to manufacture their products in India. This initiative reflects the attitudinal shift in India towards investors from a permit issuing authority to true business partner. The Make in India initiative is expected to boost several end user industries and thereby increasing domestic demand for high quality chemical products. The government has taken certain initiatives to encourage Indian chemicals manufacturing industry such as rationalisation of duty structure for feedstock, improvement of infrastructure and focus on skill development. The government is also contemplating setting up of 'Reverse Special Economic Zones (SEZs)' in Mozambique, Iran and Myanmar in order to facilitate import of cheap feedstock available in overseas markets.

Indian chemicals Industry should focus more on Sustainability in chemical conversions. Efficient process engineering and latest developments in catalysis to be adopted in chemical plants through support from global companies. The government should focus on promoting compostable plastics which undergo degradation by biological processes and do not leave visible toxic residues.

The chemicals & petrochemicals industry continues to face conventional challenges such as inadequate availability of intermediates & feedstock, location & infrastructure, taxes & duties, uncompetitive domestic demand, R&D, fragmented capacities, skill development and health and safety norms. Government's focus on the above key priority areas can pave way for development and success of chemicals & petrochemicals industry. This would also serve as an ideal 'Make in India' opportunity and create considerable employment opportunities, direct and indirect, for our growing workforce. The Chemicals and Petrochemicals sector needs to enhance its public image by creating positive perception through public awareness. Support from the government is needed for this by showcasing the importance of the industry at various public forums.

A collaborative effort by the government and stakeholders to expand capacities and reduce dependency on imports is required to unlock the potential of the Indian chemicals industry.

1. INTRODUCTION

Market Description

1.1 Chemical Industry in India is highly diversified, covering more than 80,000 commercial products. It is broadly classified into basic chemicals, specialty chemicals and agrochemicals. India's proximity to the Middle East, the world's source of petrochemical feedstock, make for economies of scale.

1.2 India is a strong global dye supplier, accounting for approximately 16% of the world production of dyestuff and dye intermediates. Chemicals industry in India has been de-licensed except for few hazardous chemicals. Upcoming petroleum, chemicals, and petrochemical investment regions (PCPIRs) and Plastic Parks will provide state-of-the-art infrastructure for chemicals and petrochemical sector.

1.3 Total production of major chemicals and petrochemicals stood at 27,858 MT during 2018-19, a growth of 4.18% over 2017-18. Alkali chemicals had the largest share in the chemical industry in India with approximately 69% share in the total production. Production of polymers accounts for around 61% of the total production of basic major petrochemicals.[1]

1.4 Indian chemical industry employs more than 2 million people and is projected to reach US$304 billion by 2025. Demand of chemical products is expected to grow at approximately 9% p.a. over the next 5 years.[2]

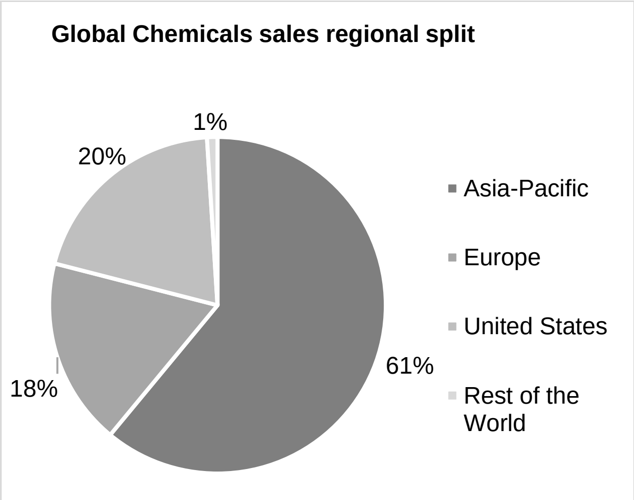
1.5 The Indian Chemicals and Petrochemicals industry is an integral constituent of India's commercial landscape in India providing key raw materials and intermediates, which are utilised by a host of downstream manufacturing companies across sectors.[3] India is the sixth-largest producer of chemicals worldwide and the third-largest producer in Asia (after China and Japan) in terms of output. The industry contributes about 1.20% of the nation's Gross Value Added.[2]

1.6 The global chemicals market was valued at US$4.3 trillion (~4 trillion Euros) in 2015 and is expected to grow at 5.5% per annum till 2020 to reach a market size of US$5.7 trillion (~5.3 trillion Euros).[4] The Indian chemicals market accounts for nearly 3.40%[2] of the global chemicals industry, and is estimated at US$147 billion in FY2015[4] and US$139 billion in FY2016.[3] The industry has the potential to reach US$226 billion by FY2020 growing at a Compounded Annual Growth Rate (CAGR) of about 9% and in an optimistic scenario, US$248 billion at a CAGR of 11%.[4]

1.7 Commodity chemicals is the largest segment of the global chemicals market, accounting for 51.3% of the market's total value. The commodity chemicals segment is expected to be the markets most lucrative in 2017, with total revenues of US $2.21 trillion (Euro 1.96 trillion), equivalent to 51.3% of the market's overall value.[5] The specialty chemicals constitute 22% of total chemicals and petrochemicals market in India. As of FY2018, the total market size is around US$35 billion. The demand for speciality chemicals is expected to grow at 12% CAGR from FY2019-2022.[6]

1.8 The global chemicals market is expected to keep growing as a result of increased urbanisation and growing markets in developing countries such as India, Turkey and Thailand. Asia's large and growing middle class demands better crop yields, more consumer goods and electronics, and improved water treatment, all of which involve the design of advanced, cost-efficient chemical systems. Countries with a mature market such as China, Australia and Germany are also expected to see accelerated growth as they switch to higher value specialty and pharmaceutical chemicals.

1.9 The below chart shows global chemical sales regional split[7]:



1.10 The industry produces a wide range of chemical products. The key segments of the Indian Chemicals and Petrochemicals industry can be grouped into the following –

Fine & Specialty chemicals**:** This downstream segment comprises technology intensive chemical plants that use basic chemicals as feedstock and are characterised by high value and low volume products. These operations require highly trained skill sets and heavy orientation to research and development (R&D) targeting specific consumer end user industries.

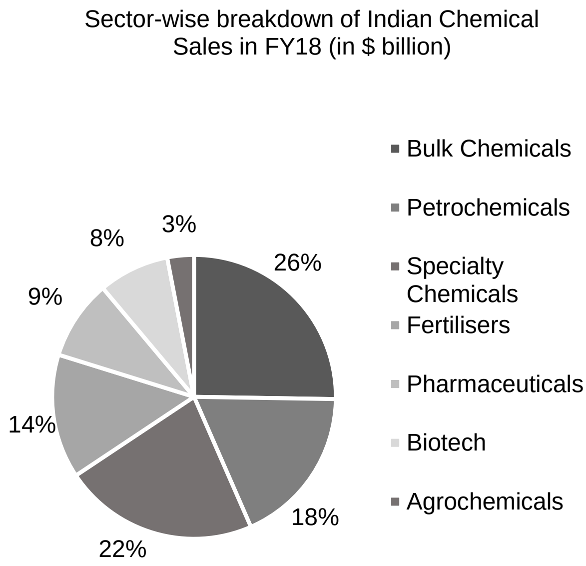
Bulk chemicals**:** This is the conventional, mature and commoditised segment with differentiation on the basis of economies of scale, access to cheap feedstock volumes and to markets. Such chemicals are manufactured on a large scale and act as inputs to the downstream industries. Bulk chemicals include basic organic and inorganic chemicals.

Petrochemicals**:** These are chemicals derived from petroleum and natural gas. Petrochemicals play a vital role in the economy by facilitating growth of various end user sectors including agriculture, infrastructure, healthcare, textiles and consumer durables. The major segments of petrochemicals are basic petrochemicals and end-product petrochemicals.

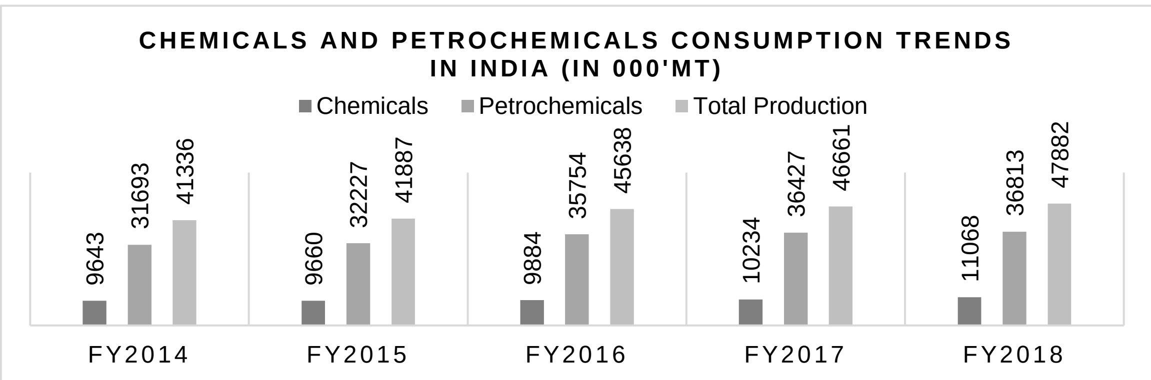
Agrochemicals: These are chemicals meant for protecting agricultural crops against insects and pests, and include insecticides, fungicides and herbicides. India is the fourth-largest producer of agrochemicals after the United States, Japan and China.[8]

In terms of market share, bulk chemicals form the largest segment followed by petrochemicals and specialty chemicals. Detailed breakdown of Indian chemical sales during FY2018 are presented below[9].

Chemical intermediates – which is between Bulk and Specialty Chemicals - is an important sub-segment in the Chemical industry and hence need to be separately mentioned.



1.11 Over last year, India's petrochemicals export scenario has considerably improved due to doubling of Ethylene capacity by Reliance Industries. This has not only mitigated import substitutions but helped India to become net exporter of Ethylene. Exports of Benzene and Paraxylene has also substantially grown last year. Production has witnessed 3.7% CAGR between FY2014 and FY2018.[10]



Source – Department of Chemicals and Petrochemicals

Production of Petrochemicals have marginally increased by 1.1% over last year and chemicals have grown by 8%. Production growth in chemicals are mainly driven by products of Chlore-Alkali Industry (Caustic Soda, Soda Ash and Liquid Chlori).

Growth Drivers[11]

1.12 India is steadily moving up the ranks as a global economic power and a business magnet for investment. Key drivers for success in the chemical sector include proximity to strong growth markets, greater ease in doing business, and the continued development of petroleum, chemicals and petrochemical investment regions (PCPIRs). Backed by one of the strongest GDP growth rates in the world, the future looks bright for the Indian chemical industry. India is currently outpacing China as the world's fastest-rising major economy. The country is the sixth-largest economy by nominal GDP and the third-largest by purchasing power parity (PPP). India is also on track to becoming the world's third-largest economy by the next decade and the second-largest by 2050. The key drivers that have led to the growth of the industry are:

- **Robust demand**

  Large population base coupled with strong export demand has provided prominent opportunities in Indian chemical industry. The market for crop protection chemicals in India is expected to reach US$7.5 billion by 2019. This growth in demand is based on a rapidly growing population and a decrease in per capita availability of arable land, both of which result in a greater need to increase agricultural yield.

- **Policy support**

  The government has taken up a favorable initiative of setting up of Petroleum, Chemicals and Petrochemicals Investment Regions (PCPIRs), plastic parks, Central Institute of Plastics Engineering and Technology (CIPET), Centre of Excellence (CoE), Chemicals promotion and development scheme (CPDS). PCPIRs are investment regions for petroleum, chemicals and petrochemicals along with associated services. Four such PCPIRs have already been approved. Plastic parks will facilitate state of the art technology development as well as a conducive ecosystem to produce specialised plastic products. Upcoming PCPIRs and Plastic parks will provide state-of-the-art infrastructure for Chemicals and Petrochemicals sector.

- **Chemicals manufacturing hub**

  There is a global shift towards Asia as the world's chemicals manufacturing hub. Manufacturers in the Asian region enjoy low people costs, relatively relaxed environmental norms and government subsidies. The economies of scale, cheaper people cost, availability of cost effective raw material sources have supported the growth story by keeping the costs low. Closure of plants in countries such as EU and China owing to increasing environmental concerns has opened doors for Indian manufactures to invest further in specialty chemicals. The ongoing trade war between USA and China has the potential to boost India's chemical industry.

- **New focus segments**

  There is a focus on new segments such as specialty and knowledge chemicals. The specialty chemicals market has witnessed a growth of 14% in the last five years.

- **Cost competitive manufacturing**

  Investments in capacity building and R&D in the industry have not happened at par with the general economic growth in the country over the last few decades. As a result India has never been a serious player in the global market and could not take advantage of the global economic slowdown the way China did. However, recent development in policies has boosted in investment in research and development which has contributed growth of the chemical industry. Additive manufacturing (also known as 3D printing) uses information from the digital realm to create a physical product, encapsulating the IT/OT transition, potentially helping chemicals companies save costs during the R&D process. Low people cost, cost effective raw material sources, world-class engineering, skilled manpower has helped in keeping the manufacturing cost low.

Future outlook [12]

The bulk chemicals market has seen a subdued growth due to challenges in feedstock availability and is expected to grow at nearly 5% per annum over the next five years. Petrochemicals market is expected to grow at a rate of around 9% to reach US$44 billion by FY2020, on the back of increased polymer demand. The specialty chemicals market is expected to continue growing at around 13% per annum to reach a market size of US$52 billion by FY2020. The agrochemicals market is expected to grow at 7.5% per annum in next five years to reach US$6.3 billion by FY2020, the growth being primarily driven by increased planned expenditure and government focus on raising agricultural productivity.

1.13 *Export potential and Investment regime for Indian chemical products*

The industry is well recognised globally for high quality products on a low manufacturing cost base. Globally, India ranks 14th in exports and eighth in imports of chemicals (excluding pharmaceuticals products).[13] While India remains a net importer of chemicals and petrochemicals, the share of these exports has increased to 10.6% of the total national exports during FY2016.[14] Further, exports during the first six months of FY2017 (i.e., April to September, 2016) increased by 2.86%, compared to exports during the same period in FY2016.[15]

India is a predominant exporter of agrochemicals to the US, Europe and Africa. Indian dyestuffs are also well received internationally, accounting for about 16% of the world production of dyestuff and dye intermediaries, particularly reactive acid and direct dyes.[9]

1.14 The manufacture of most chemical products is de-licensed (with only certain items being covered under the compulsory licensing list because of their hazardous nature) and entrepreneurs need to submit only the Industrial Entrepreneurs Memorandum to the Department of Industrial Policy & Promotion (DIPP) to start chemical manufacturing. There are no quantitative or other restrictions on the import of chemicals except on a few chemicals which are covered under the obligations of international conventions.

1.15 In the Chemicals and Petrochemicals industry, 100% foreign direct investment (FDI) is permissible under the automatic route, subject to certain exceptions. FDI in the sector witnessed inflows amounting to US$2.2 billion during the two year period from April 2014 to March 2016, as compared to US$1.08 billion during the period April 2012 to March 2014 (an increase in FDI inflows by around 107%). The sector attracted inflows amounting to US$532.48 million during April to September 2016.[9]

1.16 Increasing urbanisation (at CAGR of nearly 2.1%[16]), government focus on affordable housing and rising per capita disposable income (estimated at around US$1,768 during FY2017 - an increase of 9.9% from FY2016[17]) is expected to fuel consumption and result in a strong growth outlook for several key end user industries such as construction, automotive, electronics, etc. This will positively impact growth in the industry, which is expected to surge at 9-11% over the next five years.[18]

Recent Investments in Indian Chemical and Petrochemical Sector

Indian Chemical Sector attracted FDI investment of US$1.3 billion in FY2018 which is about 3% of the total FDI inflow. Both Indian and overseas companies are investing in either greenfield or brownfield projects in this industry. Petrochemical upstream sector is highly capital intensive and linked to the availability of crude as feedstock. Hence National Oil Companies (PSUs) are major investors in this sector. Among the private sectors, Reliance is the largest investor in both greenfield and brownfield projects.

It is worthwhile to note that Indian Chemical Companies have started focusing on global markets for investments. Recently, largest Agrochemical company in India, United Phosphorous Ltd. announced the acquisition of Arysta Lifescience for about US$4.2 billion. With this acquisition UPL will not only get access to Arysta's global market but will also improve its penetration in Indian Agrochemical market. Possibility of moving certain products to low cost manufacturing base locations will give the possible boost to India.[19]

European Investment in India

European chemical players are looking at Asian markets as the next growth phase due to the high consumption base. Some of the European chemical companies present in India are:

1. BASF
2. Solvay
3. Syngenta

In addition to the above, about nine other European companies are active in this sector and are doing business in India.

Non-tariff barriers

To prosper, the chemical industry needs an enabling legal framework, and free access to global markets, which means the removal of tariff and non-tariff barriers. Currently however, the chemical industry still faces costly tariffs, unclear rules of origin, discrepancies between national legislations, multiple standards, limited protection of trade secrets, and trade defense measures.

With globalisation and the WTO under pressure, bilateral Trade Agreements (TAs) are becoming increasingly important for global markets access. However, bilateral TAs are insufficient, because they address only part of the needs of the chemical industry and are difficult to negotiate.[20]

The current covid-19 crisis could not have come at a worse time given that many countries are resorting to policies which are protectionist in nature. As tariff rates on multiple products have been reduced globally pursuant to the establishment of WTO, many countries often resort to Non-Tariff Barriers (NTB) to protect domestic manufacturers and safeguard national interests.[21]

Recently, India is considering a proposal to levy 15% COVID-19 tax on all chemical and petrochemical imports from 1 May 2020 to 31 March 2021 to protect the domestic industry. Per the proposal, the provisional duty would also be applicable on all preferential imports under India's various free trade agreements (FTA), and would cover organic chemicals, inorganic chemicals, plastics, rubber, man-made filaments and man-made staple fibres. The 15% tax would be in addition to the lowest tariff called applied most favoured nation (MFN) duty in trade parlance.[22] Moreover, anti-dumping investigations are underway on more than 100 Chinese products being imported by India.[23]

The commerce and industry ministry is already working on a plan to substitute imports under the Atmanirbhar Bharat Abhiyan and is looking to correct duty structures, including any duty discrepancies with countries that India has FTAs with. Incentives to promote local production and export competitiveness such as export incentives parity with China and duty-free import of plant and machinery could also be offered for the chemical and petrochemicals sector[24]

Given the rise in protectionist measures specifically the NTBs, it is important to ensure that the gains from the last 25 years on mutual recognition and convergence of regulatory standards are not done away with. Specifically, for developing countries like India, it is in their interest to support a holistic global effort in this regard to ensure that NTBs do not become a hindrance in their growth and specifically of SMEs.[25]

BIS Standards

Department of Chemicals & Petrochemicals, Ministry of Chemicals & Fertilisers, Government of India has announced the proposals for mandatory BIS certification for various chemicals and fertilisers which include around 72 chemical and petrochemical. These would allow domestic and international businesses to acquire licenses until they can produce, develop, or utilise the substances impacted.

The requirements include numerous specific chemicals and other common polymers, including polyethylene, polypropylene, polyvinyl chloride, and polyurethane. Products marked for certification shall meet with the respective Bureau of Indian Standards (BIS) requirements. The credential introduces another tier to corporate procedures that need to be surmounted for market entry.[26]

According to BIS requirements, foreign companies exporting to India need to register with the BIS to ensure their imports meet agreed standards. Such companies would also need to undergo checks by the BIS, which would include visits to the respective plants.

These new bureaucratic steps would lengthen the time taken to register and import to the country. However, the full impact of the regulation remains unclear.[27]

2. GENERIC INDUSTRY CHALLENGES

2.1 **Feedstock**: Continuous availability of reliable and competitive feedstock is a key challenge to the growth of the Indian chemical industry. The primary building blocks such as ethylene, propylene and butenes (relevant for specialty chemicals products) are mostly consumed captively for commodity products (such as polyethylene, polypropylene, etc.) and hence are not accessible in the merchant market. In the absence of domestic feedstock, India remains heavily reliant on import of feedstock, which is not a sustainable growth model.

Also, the rising global crude oil prices has adversely affected the availability of feedstock at competitive prices. Crude oil is a major cost driver in the petrochemical industry, as many of the key chemical building blocks (for example, aromatics, ethylene, and propylene) used for industry's products are directly produced from oil or its derivatives (for instance, naphtha and liquefied petroleum gas). Thus, volatility in oil prices has a direct impact on prices of feedstock, and consequently on the manufacturing cost of chemicals.

2.2 **Location and Infrastructure**: The major Indian chemical industry has been set up along the west coast in Gujarat, while the highest demand of chemicals is in southern and eastern India. This gives rise to logistical transportation costs, thus increasing the overall cost of chemicals.[28] Lack of adequate infrastructure facilities including transportation facilities (such as roads, ports, railway, pipeline networks, etc.) pose a challenge for domestic manufacturers in procuring raw materials at a cost competitive price. This leads to a rise in the manufacturing cost and, creates bottlenecks in growth and continuity of operations. Intermittent power supply also has an adverse effect on the energy intensive chemical industry.

2.3 **Duties:** Inverted duty tax structures affect the competitiveness of the industry. The government has attempted to rectify this through several proposals in the Finance Bill 2017 by reducing customs duty on o-xylene, 2-Ethyl Anthraquinone, Medium Quality Terephthalic Acid (MTA), Qualified Terephthalic Acid (QTA), Vinyl Polyethylene Glycol for use in manufacture of Poly Carboxylate Ether and Clay 2 Powder (Alumax) for use in ceramic substrate for catalytic convertors.

However, compliance procedures and mechanisms for levy and refunds of cess and duties are quite onerous under present regime. It is expected that while deciding the tax rates under GST, the government would avoid any credit accumulations on account of inverted duty structure. Further, in case there is credit accumulation on account of inverted duty structures, the model GST law provides for a refund of accumulated credit. The government should ensure that such refunds are granted expeditiously to the taxpayers so as to avoid blockage of working capital.

2.4 **Uncompetitive domestic market:** India has signed Free Trade Agreements (FTAs) with various countries agreeing to levy negligible import duty on various chemicals. Further, certain chemicals are placed in the Open General License of imports. These have resulted in increased imports of various chemicals, intermediaries and end products from low cost manufacturing hubs like China. Consequently, the domestic industry is rendered uncompetitive, especially the small and medium players, lacking economies of scale and cost efficiency.

2.5 **Fragmented capacities**: Typically, fragmented and dispersed units are not in a position to enjoy economies of scale and face capital constraints due to sub optimal capacities, which impedes their growth options and further impacts the competitiveness across the value chain.

2.6 **Investment in R&D**: More resources and finances need to be invested on the R&D front. The lack of incentives for R&D has hampered the much needed investments in the segment.

2.7 **Skill development**: There has been a dearth of talented manpower in the industry. Individuals entering the industry and institutions providing the training/degrees lack orientation to practical skill sets. The industry has an additional human resource requirement of 1.72 million by 2022.[29] Together with the government, the industry needs to take measures to attract, recruit and retain the right talent.

2.8 **Health and Safety norms**: Players in the chemicals and petrochemicals industry have often been lax in adopting established and proven health, safety, security and environment norms. This further impacts public perception linked to the sector and works negatively in terms of attracting requisite talent to work in the industry and results in higher risk of industrial accidents.

3. KEY ISSUES & RECOMMENDATIONS

Issue/Objective: Developing India as a global hub in specialty chemicals and fulfilling the domestic demand

3.1 **Issue:** Feedstock availability

Recommendations:

The government policies should focus on ensuring availability of competitive feedstock with relevant brownfield infrastructure to the industry. This is critical for domestic and international companies to invest in India. Some of these concerns are sought to be addressed in the draft National Chemical Policy. However, the delay in finalisation of the same has impacted the industry.

The government should consider implementing the following recommendations:

1. Investments should be encouraged in areas where sustained feedstock supply is available.
2. Cluster approach should be followed to rationalise efforts in feedstock allocation with anchor units setup at PCPIRs
3. Government to government contracts should be encouraged for locking in international feedstock supply.
4. Setting up of global scale plants for manufacture of base chemicals.
5. Grant of incentives to manufacturers for using bio-based /non-fossil fuel-based raw materials.

The industry should also explore alternate feedstock options such as olefins, coal-based feedstock, pet coke, shale gas etc. Shale gas is an untapped resource in India and exploration of domestic shale gas can help in meeting India's growing energy demand. The chemical companies may also consider setting up gas cracker plants, or investing in upcoming plants and securing off-take agreements in resource rich nations to secure cheap feedstock.

3.2 **Issue**: Inadequate infrastructure

Recommendations:

Domestic manufacturers face difficulties in procurement of raw materials at cost competitive prices due to poor infrastructure facilities at ports, railway depots and poor pipeline connectivity. Further, intermittent power supply adversely affects the energy intensive chemical industry.

While there has been an increased focus towards infrastructure development, given the significant inadequacies, it will require time to overcome the shortfalls. Focused infrastructure development for the industry has been attempted through the setting up of clusters such as PCPIRs and in capacity building of existing identified chemical clusters across India (largely Gujarat and Maharashtra). It is imperative that enabling frameworks are developed for effective infrastructure creation in the PCPIRs and chemical clusters by providing specialised infrastructure required for the industry to facilitate co-location of players across the value chain i.e., - feedstock suppliers and downstream players. This could be done by creating a network of specialised and high pressure pipelines and cryogenic storage containers etc. Similarly, centralised effluent treatment units and air separation units in such clusters would help small players.

The supporting logistics infrastructure for the industry, namely construction of quality logistics and transportation facilities such as roads, railways, ports and terminals handling chemicals and petrochemicals along with the requisite port-based logistics infrastructure, will be critical to ensure overall development. Concerted efforts should be continued by the government and private industry to close out the infrastructure gaps. The government may consider the Public Private Partnership (PPP) model for building necessary infrastructure, especially roads and ports. India signed the historic deal with Iran and Afghanistan in May, 2016 for development and operation of the Chabahar port in Iran, to establish a link from the Gujarat coast to the energy rich Central Asia. This would provide an impetus to the supply of feedstock as well as access to international markets. Per the terms of the agreement, India has to extend credit of US$150 million for development of Phase one of the Chabahar port. However, the credit has not been disbursed yet by the Export-Import Bank of India, which is awaiting completion of an application from the Port and Maritime Organisation of Iran.[30]

3.3 **Issue:** Inadequate availability of intermediates

One of the key concerns facing the Indian chemical industry today is the growing import dependence of key petrochemical intermediates - acrylic acid, propylene oxide, polyols, phenol, styrene, vinyl chloride, acetic acid, vinyl acetate, methyl methacrylate etc. While the upstream refining and basic petrochemicals [propylene, ethylene] industry has grown rapidly in the last decade, and the downstream specialty chemicals industry also continues to deliver robust growth, petrochemical intermediates are proving to be a vital missing link for sustainable growth of the Indian chemical industry, with trade statistics showing an import dependency of close to 50%. As demand for specialty chemicals grows, driven by growth in end-user industries such as construction, mining, consumer goods etc. this import dependency will only become more acute, hampering downstream industries. It is imperative that the country focuses on building manufacturing infrastructure for petrochemical intermediates.

Recommendations:

The technology to manufacture petrochemical intermediates is available with a select group of global chemical companies including BASF and forging successful partnerships has proven to be a challenge thus far. However, we believe the government can play a key role in facilitating this process by concerted action in the following priority areas:

1. Creating an integrated petrochemical intermediates master plan for India which would match feedstock availability with downstream and end-use demand for critical value chains
2. Encouraging or mandating producers of petrochemical building blocks (propylene, ethylene) to make specified volumes available for petrochemical intermediates. Thus far, more than 90% of the propylene and ethylene produced in India goes for manufacturing of bulk plastics, leaving only modest volumes available for higher value added petrochemical intermediates.
3. Supporting investment in petrochemical intermediates by re-examining duty structures across the value chain.
4. Establishing petrochemical intermediate clusters as frontrunners in the national campaign to improve the ease of doing business, by accelerating the simplification of key procedures such as land acquisition or environmental clearances

The challenges of making this aspiration a reality are not unique to India. Other major chemical-producing economies such as China, the European Union and Singapore have faced and resolved similar challenges. Hence, effective action on the above priority areas can pave the way for development of a successful petrochemicals intermediates industry. This would also serve as an ideal ‘Make in India’ opportunity and create considerable employment opportunities, direct and indirect, for our growing workforce.

3.4 **Issue:** Alignment of taxes and duties

Recommendations:

Rationalisation of taxes is of paramount importance in this sector. Inverted duty structures should be suitably rectified to bring players at par with global players and enhance competitiveness of output from India. While fixing GST rates for taxing goods and services, the government should ensure that should be no abnormalities on account of tax rates or inverted duty structure. Further, the government should also ensure that there is no additional cost on account of natural gas (which is a key input for chemical and petrochemical industry) being out of GST.

India has entered into FTAs with various countries for reducing customs duty on import of chemical products. The government should follow a balanced approach while entering into FTAs and review them regularly, so that industry players from signatory countries are mutually benefited.

The European Union has also expressed its will to move forward in the negotiations for having a FTA, or Bilateral Trade and

Investment Agreement (BTIA) with India at the earliest. The government should endeavour to favourably conclude dialogue on such agreements.[31]

3.5 **Issue**: Dispersed and uneconomical capacities

Recommendations:

The primary objective should be to set up state-of-the-art units with economies of scale so that they are competitive. Units with smaller capacities should be consolidated or ideally upgraded. The consolidation and relocation, if any, should take place in a manner that will shift downstream capacities closer to the anchor plants so that logistics become cost efficient and units are located in proximity to supporting infrastructure. The government could consider incentives to encourage such consolidation.

It is important to address is the efficiency of some of these operating units. Technology selection and selection of key performance consumables is based on age-old procedure of tendering evaluations. This entire system needs to be overhauled to a more value-driven approach.

3.6 **Issue**: Ease of doing business

Recommendations:

In a welcome initiative, the government introduced SWIFT (Single Window Interface for Facilitating Trade), enabling importers /exporters to file a common integrated declaration in place of various forms filed across agencies. Various other customs related compliances were eased out to promote ease of doing business.

The government should further expedite the simplification of procedural and compliance matters by consolidating /streamlining the myriad acts and rules pertaining to the chemicals and petrochemicals industry. The Central Government should also regularly interact and engage with the State Governments for effective implementation of the initiatives.

3.7 **Issue**: Investments in R&D

Recommendations:

It is imperative to look to strengthen connect between Industry and Academia. The pedagogy & infrastructure should be adapted to make it more relevant to present era of industry needs. Academic Research in India to be made more relevant for businesses and interface between Academia and Industry to be more broad based.

It is imperative that R&D spend be increased so that new materials, products and technologies are developed in line with the objectives to position India as a global specialty chemicals hub. The government should also incentivise R&D spend by way of tax breaks, soft loans, subsidies, etc. The R&D spend by Indian companies has been limited and needs to be increased to 3-5% of revenues. International collaborations with multinational chemical giants can provide an impetus in these efforts. The government can also facilitate indigenous R&D under a PPP model.

The draft National Chemical Policy proposes to set up a National Chemical Development Centre to promote R&D.[32] The National Chemical Laboratory, a constituent laboratory of Council of Scientific and Industrial Research (CSIR), had earlier set up a NCL Innovation Park to support growth and expansion plans of research and knowledge-based business entities. Further, BASF has setup an Innovation Campus in Navi Mumbai, India in March, 2017 with an investment of approximately Euro 50 million and would employ upto 300 scientists. This will research and innovate on a wide range of specialty chemicals covering areas such as personal and home care, process development, crop protection, etc.[33] BASF has also inaugurated a new mobile emission catalysts site in Chennai, India on March 2, 2017 which will help the industry meet stringent emissions regulations including the proposed Bharat Stage VI (Euro 6) norms.[34]

Effective implementation of the IPR framework to protect innovators and facilitate monetisation of new materials and discoveries is also needed. In this regard, the government had released the National IPR policy in May 2016, with an objective to sustain entrepreneurship, stimulate innovation and provide further impetus to the ‘Make in India’ initiative. However, the policy has received mixed reactions from the industry and experts on its ability to meet the stated objectives. The industry’s concerns regarding lack of data protection remain unaddressed, impacting the development of the chemicals industry (Agrochemicals in particular).

3.8 **Issue**: Human resource development

Recommendations:

India has a large manpower pool. In order to create the pool of skill sets required by the industry, investments should be made in technical training infrastructure. It is also critical to attract talent into the chemicals and petrochemicals industry. The training agenda can be developed jointly as a public-private collaboration. The government is also focused on setting up skill development councils or centres as a medium to execute training plans. As an illustration, under the draft national chemical policy, the government has plans to set up Chemical Engineering Education Centres within leading universities and institutes.

The Ministry of Skill Development & Entrepreneurship had entered into three Memorandum of Understandings (MOUs) with the Ministry of Chemicals and Fertilisers to collaborate and collectively address the human resource requirement.[35] The government had also sanctioned additional 10 centres under the Central Institute of Plastics Engineering and Technology (CIPET) in different parts of the country. However, during FY2016, only five new centres were set-up. In April 2016, the government has approved setting up of 11 new CIPETs including an Advanced Polymer Design and Development Research Laboratory of CIPET.[36]

3.9 **Issue:** Health, Safety, Security and Environment (HSSE)

Recommendations:

Safety management is one of the critical requirements within the sector to prevent disruption of operations and endangering of human lives, There have been initiatives to improve safety through setting up of systems and processes such as the Chemical Plant Safety and Security Rating System which aims to encourage the attainment of zero accidents and to incentivise the units to achieve best safety operational measures. Chemicals and petrochemicals industry players must specifically invest and maintain best practices on HSSE. The government and public bodies must also incentivise units to adhere to safety requirements and abide by global standards. The government plans to setup a National Chemical Safety Centre and the National Bureau of Corrosion Control in the proposed national chemical policy to regulate and prevent corrosion.[37]

Strictness and honesty in enforcement of Environmental standards is the key for success in Chemical industry to enhance its public image.

3.10 **Issue**: Negative perceptions and image linked to the Chemicals & Petrochemicals industry

Recommendations:

The Chemicals and Petrochemicals sector needs to enhance its public image by creating positive perception through public awareness. Support from the government is needed for this by showcasing the importance of the industry at various public forums. These efforts will also serve well in attracting skilled technical talent to the industry. This is vital for long term growth as well as in conveying the importance of the industry within the national commercial landscape. A roadmap in this direction needs to be put in place.

4. COVID-19[38]

4.1 Potential long-term impact on chemical companies

Large chemical and petrochemical companies are responding by cutting capital and operational expenditures, which will filter down to suppliers and oilfield services companies. This suggests:

- Inefficient and highly leveraged companies may face a liquidity crisis, with some being forced out of business.
- US shale producers will be particularly under strain if the supply glut and depressed prices continue.
- Some of the larger, healthier companies may alter or accelerate their plans to diversify into other energy segments. Prompting a change in business model.
- In the wake of lay-offs and furloughs, companies may face a shortage of skilled labor when the market rebounds.

4.2 Steps to consider:

Chemical and Petrochemical leaders will be defined by what they do along the three dimensions of managing crisis: respond, recover and thrive. Some of key next steps include:

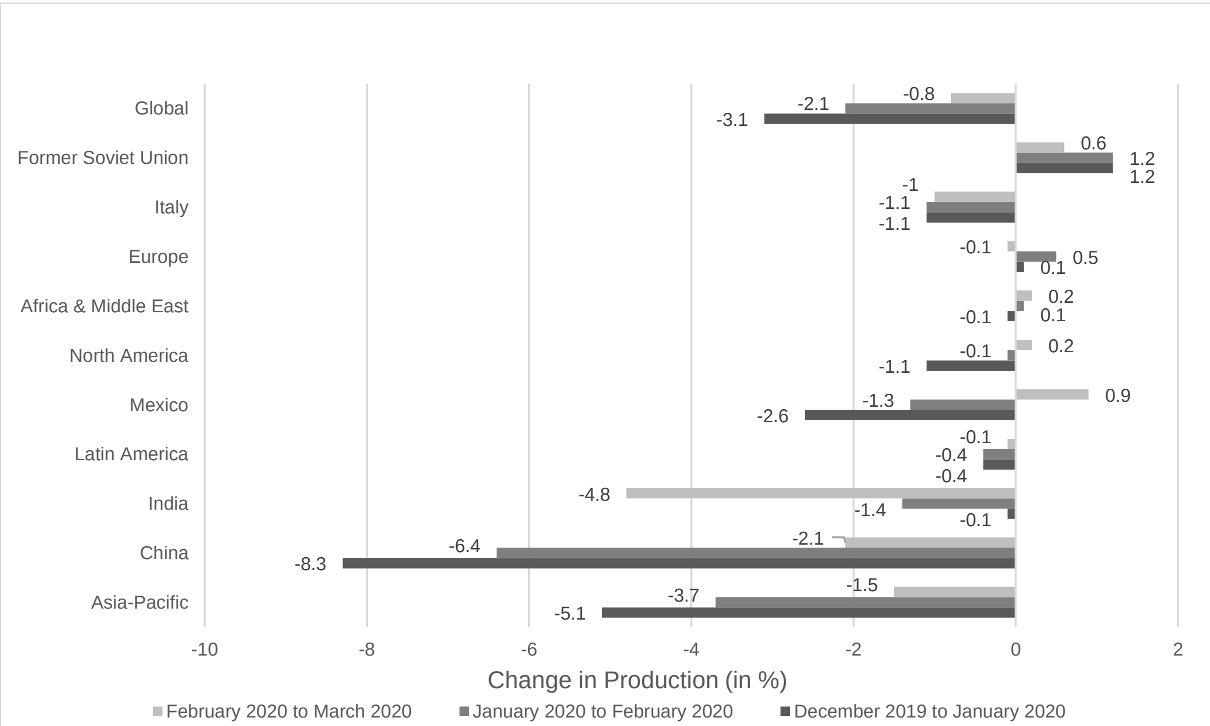
- Assess whether the company has the financing to continue, balancing the trade-off between immediate needs and what has been promised to the market in terms of return, dividends, share, buy-backs, etc.
- Consider if the crisis can be used as a catalyst to rethink how work is done, such as accelerating adoption of digital capabilities
- Determine what future of work will look like and align talent strategies for new environment

4.3 Regional analysis of global chemical industry: Impact due to Covid-19 Pandemic[39]

Based on chemical type, the industry is segmented into petrochemicals, basic inorganic, polymers, specialty chemicals, consumer chemicals, and others. Due to the downfall in crude oil prices, the market of petrochemical is expected to be most affected. Based on geography, the global chemical industry is classified into four key regions, including North America, Europe, Asia-Pacific, and Rest of the World. Asia-Pacific is anticipated to be highly affected by the spread of the COVID-19 due to the effect of the pandemic in China, Japan, and India. China is a major country in terms of the chemical industry. Per the CEFIC Chemdata International, in 2018, chemical sales in China reached around US$1.32 trillion. According to the International Council of Chemical Associations (ICCA), China is the eighth-largest chemical importing nation and the twelfth-largest chemical exporting nation across the globe. After China, the US is anticipated to get majorly impacted by the spread of COVID- 19.

The major companies operating in the Chemical industry being affected due to coronavirus outbreak include BASF SE, DowDuPont, China Petroleum & Chemical Corp., SABIC, Mitsubishi Chemical Corp., Wanhua Chemical Corp., Chevron Phillips Chemical, Evonik Industries, Jianshi Yuantong Bioengineering Co., Ltd., PPG Industries, The Linde Group, and others. Looking towards the alerting situation many chemical companies have halted their production facilities across the globe. Some other companies which are still working are operating at only 40-60% efficiency.

Percent change in chemical production due to COVID-19 worldwide between December 2019 and March 2020, by region[40]



5. The new reality beyond COVID-19[41]

The sheer impact of COVID-19 and associated disruptions has immediately directed the attention of virtually every chemical player on aspects essential to the sustainability of the business: cash, liquidity, and strength of the balance sheet. Many organisations have set up a dedicated crisis and liquidity teams to ensure adequate managerial attention.

Looking beyond these, there are a few emerging observations that likely will have a more prolonged impact on the industry:

5.1 **Traditional growth product-markets segments are not necessarily growing anymore** (e.g., aviation or automotive). This implies product and grade shifts (following, e.g., a demand shift from PP to LDPE), re-allocation of volume on markets and channels, and adjustments to go-to-market strategies. Chemical players will have to 'sharpen' their ability to sense demand and adapt rapidly to changing patterns. Developing more sophisticated demand models, supported by digital tools, will be necessary as well as adopting more agile and technically advanced sales and operations planning capabilities with a significant focus on scenario testing and optimisation.

5.2 **In a more competitive world, access to market will be increasingly important**. Development of strong marketing and sales organisations, with global reach, close to key clients and leveraging the full suite of marketing excellence levers (including more sophisticated pricing models) will be essential to winning volumes and margins. Digital will also be critical, by providing tools to optimise pricing and access to clients, particularly at times of social distancing (e.g., digital/remote inbound/outbound marketing, centralised sales, etc.). Models are still relying heavily on third parties, and traders will inevitably be challenged.

5.3 **Cost and operational excellence is a key 'license to operate'** – with an imminent further consolidation in the industry. This is not new to the industry, especially for European players who went through drastic cost reductions to stay afloat in the 2009–2011 period. What is new is that players with historical feedstock advantage (including Middle East producers) will activate all cushions, reaching to all possible reservoirs of cost optimisation and workforce productivity. An option to consider is to consolidate, especially if there is a good portfolio fit as with the Sipchem/Sahara merger initiated in 2019. We will see more such moves in the region. Digital, again, can provide additional tools to optimise operations and supply chain, among others.

5.4 **For companies with a strong balance sheet, this could be a unique moment to carry-out M&A at record low prices.** Companies with such characteristics should set-up ad-hoc M&A teams to look at opportunities very quickly – the window of opportunity will last months, not years.

5.5 **Agility in running the business, with better digital tools for information circulation, scenario modeling, and decision support are becoming critical.** Speed is becoming even more essential in capturing opportunities offered by a fast-changing market environment. COVID-19 has demonstrated the relevance and importance of digital ways of working. It is vital to go beyond that, introducing advanced analytics and digital tools for scenario modeling, digital control towers for decision making support, and digitalising further commercial interactions in the channels

CONCLUSION

The Indian Chemicals and Petrochemicals industry holds huge potential as the strong growth outlook of end user industries is expected to fuel the demand for chemical products. The industry offers several opportunities for both domestic and international chemical players. Some of the opportunities on which India can leverage are listed down below:

- India's advantage for investments are almost unparalleled, it will become one of the largest consuming economies offering very large captive market for the companies.
- It is the youngest nation with a large workforce and low cost of manufacturing. Besides, it has a strategic location that provides access to both west and east.
- With very low per capita consumption, Indian chemical industry provides a large head room to grow. It is fragmented
- End use industries such as automobiles, electronics, packaging, infrastructure etc. are on a growth path providing sustainable growth for years to come.

- Indian democratic environment and stable government focused at providing business friendly environment and infrastructure[42]

The government should focus on addressing industry concerns regarding infrastructure, feedstock supply, transfer of technology and competitiveness of the domestic market on priority. A collaborative effort by the government and stakeholders to expand capacities and reduce dependency on imports is required to unlock the potential of the Indian chemicals industry. The European chemical players can consider fresh collaborations, investment /merger and acquisition opportunities to advantage from the strong industry outlook.

ENDNOTE

1. https://www.investindia.gov.in/sector/chemicals
2. https://www.investindia.gov.in/sector/chemicals
3. Chemicals & Petrochemicals sector – Achievements Report dated January 18, 2017, Department of Industrial Policy & Promotion (DIPP), Ministry of Commerce & Industry
4. Handbook on Indian Chemical Industry – September 2016, FICCI
5. MarketLine Industry Profiles-Global Chemicals-December 2017
6. https://www.investindia.gov.in/sector/chemicals
7. http://www.indiachem.in/brochure/Presentation%20by%20Shi%20P.%20Raghvendra%20Rao.pdf
8. Chemicals and Petrochemicals Statistics at a glance 2016, Ministry of Chemicals & Fertilizers
9. http://www.indiachem.in/brochure/Presentation%20by%20Shi%20P.%20Raghvendra%20Rao.pdf
10. http://ficci.in/spdocument/23036/Knowledge%20paper-India%20Chem%202018-ficci.pdf
11. https://www.hdfcsec.com/hsl.docs//Sector%20Update_Chemical%20Industry_Aug%202019-20190829131231924043.pdf
12. Handbook on Indian Chemical Industry – September 2016, FICCI
13. Handbook on Indian Chemical Industry – September 2016, FICCI
14. Chemicals and Petrochemicals Statistics at a glance 2016, Ministry of Chemicals & Fertilizers
15. Chemicals & Petrochemicals sector – Achievements Report dated January 18, 2017, Department of Industrial Policy & Promotion (DIPP), Ministry of Commerce & Industry
16. Source: Article in The Hindu dated February 26, 2016 (http://www.thehindu.com/features/homes-and-gardens/indias-challenge-of-disordered-urbanisation/article8285145.ece)
17. Advance Estimates of National Income, 2016-17, Ministry of Statistics & Programme Implementation
18. Handbook on Indian Chemical Industry – September 2016, FICCI
19. http://ficci.in/spdocument/20441/Knowledge-Paper-chem.pdf
20. https://www.gpca.org.ae/2019/07/03/unlocking-the-potential-of-the-chemical-industry-through-a-global-sector-agreement/
21. https://www.financialexpress.com/industry/sme/cafe-sme/msme-logi-non-tariff-barriers-what-government-should-do-to-ensure-msmes-remain-competitive-globally/1782873/
22. https://economictimes.indiatimes.com/news/economy/foreign-trade/petrochem-chemical-imports-likely-to-face-15-covid-tax/articleshow/75834553.cms?from=mdr
23. https://www.icis.com/explore/resources/news/2020/07/16/10530588/india-bent-on-seeking-alternative-to-china-for-petrochemical-imports
24. https://economictimes.indiatimes.com/news/economy/foreign-trade/petrochem-chemical-imports-likely-to-face-15-covid-tax/articleshow/75834553.cms?from=mdr
25. https://www.financialexpress.com/industry/sme/cafe-sme/msme-logi-non-tariff-barriers-what-government-should-do-to-ensure-msmes-remain-competitive-globally/1782873/
26. https://globalomega.com/quality-control-orders-for-mandatory-bis-certification-of-various-chemicals-and-fertilizers-by-department-of-chemicals-petrochemicals/
27. https://www.argusmedia.com/en/news/1888482-india-may-impose-bis-rules-on-more-petchem-imports
28. https://www.exportersindia.com/blog/opportunities-and-challenges-for-the-indian-chemical-industry.htm

29. Press release dated March 9, 2016 by the Ministry of Skill Development and Entrepreneurship
30. Source: Article in Livemint dated February 27, 2017 (http://www.livemint.com/Politics/lIhUckmnYMrTCBlBxPaDTO/Indias-Chabahar-port-plan-runs-into-Iran-loan-application-h.html)
31. Source: Article in the Business Line – The Hindu dated February 20, 2017 (http://www.thehindubusinessline.com/economy/policy/as-fta-hangs-fire-eu-wants-india-to-extend-investment-pacts/article9552228.ece)
32. Speech of the Union Minister of Chemicals and Fertilizers, Mr Ananth Kumar, at 'Indian Chemical Industry: Challenges & opportunities'; organised by The Associated Chambers of Commerce and Industry of India (ASSOCHAM) on December 4, 2015
33. BASF News Release dated March 3, 2017 (https://www.basf.com/en/company/news-and-media/news-releases/2017/03/p-17-149.html)
34. BASF News Release dated March 2, 2017 (https://www.basf.com/en/company/news-and-media/news-releases/2017/03/p-17-144.html)
35. Press release by Ministry of Skill Development & Entrepreneurship dated July 9, 2015
36. Chemicals & Petrochemicals sector – Achievements Report dated January 18, 2017, Department of Industrial Policy & Promotion (DIPP), Ministry of Commerce & Industry
37. Speech of the Union Minister of Chemicals and Fertilizers, Mr Ananth Kumar, at 'Indian Chemical Industry: Challenges & opportunities'; organised by The Associated Chambers of Commerce and Industry of India (ASSOCHAM) on December 4, 2015
38. https://www2.deloitte.com/global/en/pages/about-deloitte/articles/covid-19/covid-19-s-impact-on-oil--gas--and-chemical-organizations.html
39. https://www.prnewswire.com/news-releases/global-chemical-industry-and-the-impact-of-covid-19-regional-analysis-and-key-player-profiles-301045312.html
40. https://www.statista.com/statistics/1103403/global-chemical-output-change-due-to-covid-19-by-region/
41. https://www.gpca.org.ae/2020/06/24/covid-19s-impact-on-the-petrochemical-industry/
42. http://ficci.in/spdocument/20441/Knowledge-Paper-chem.pdf

NOTE

Defence

Acknowledgements: Ola Rignell (SAAB India) – Chairman, Defence Sector Committee & its Members
Knowledge Partner: Rajat Chowdhary, Capt Vishal Kanwar (Retd) – PwC

1. EXECUTIVE SUMMARY

Self-reliance and indigenisation in defence are important for both strategic and economic reasons. Besides delivering products to meet current and future operational requirements at the lowest total cost, the procurement programmes shall also provide the necessary industrial capability to produce, maintain, and further develop the system over its entire service life. Additionally, these programmes shall support development of self-reliant capabilities in Aerospace & Defence to help reduce dependency on imports. This requires the application of incentives and stringent requirements to ensure the OEM´s ability and willingness to share and transfer required technologies and capabilities, as well as to assure timely deliveries, quality and performance. To meet these purposes, the policy framework for defence procurement needs to be conducive and provide pre-requisites to bring the best value for money to the nation.

The current Indian procurement policy, DPP2016, through the Strategic Partnership (SP) Policy for major defence platforms has a strong focus on maximising indigenous content. However, there are several issues in the SP Policy which may not make the SP programmes the most efficient way to ensure self-reliance. Some of the key issues are:

- While the SP Policy does not allow OEMs to hold the controlling share of the JV/SPV formed with the Indian SP, OEMs need to take joint and several responsibilities in critical areas including quality, deliveries and the success of the transfer programme.
- The SP for each platform will ultimately be selected on basis of price competition. To win the bid, SPs may naturally seek to choose the lowest bidding OEM which would force them to choose the cheapest compliant bid even if that is at odds with the objectives of achieving a high quality of ToT and a partnership model for the long term.
- In a situation where multiple SPs will seek price discovery before deciding which OEM to partner, there may be potential leakage of the OEMs' price and sensitive technical information.
- Although the SP policy identifies ToT and indigenisation as key criteria for shortlisting OEMs, however, such criteria are ultimately based on an upfront assessment of something that may not practically be evaluated until some point in the future.

The evaluation methodology within the DPP currently places the emphasis on selection of equipment acceptable after meeting minimum technical criteria, and the lowest price (L1). Applying this methodology for the supply of technologically complex equipment that will be in service for decades, may not support selection of the optimal solution. Currently, there are no provisions for qualitative procedures that secure a truly holistic evaluation of the full product performance, complete capability transfer and total cost to acquire, operate, support and upgrade. To ensure that the above objectives and self-reliance stated within the preamble of the DPP are achieved, there is a need to re-engineer these aspects and methodologies within the current procurement policy framework. Following are some of the key recommendations to strengthen India's defence preparedness and build a credible defence industrial base:

- The government should consider all important cost parameters related to procurement and ownership, including costs for operations and support, of the entire equipment/system over its full service life for L1-based selection. The Life Cycle Cost (LCC) should be the most important criteria for selection of the vendor.
- For the procurement of highly technical products, e.g., fighters, the government should adopt the use of Best Value method, which gives weightage to LCC, technical capability of the indigenisation strategy. Adoption of the Best Value method would provide due importance to the upgradability, operation availability, transfer of technologies and will yield better value for money.
- The government should bring more flexibility in the offset policy by allowing group companies or subsidiaries of foreign OEMs to discharge offset obligations on the behalf of OEMs.

- The government should expand the list of eligible services for discharge of offset obligations, and include assembly, integration and testing services; setting up testing infrastructure; undertaking skill development projects in India. In addition to the avenues for discharge of offset obligations mentioned, some additional avenues for discharge of offset obligations such as investment in specified projects along with mode of discharge should also be considered.
- The government should allow a more flexible approach that permits global OEMs to define offset amounts to be allocated to each IOP over the course of the programme, instead of committing fixed dollar/percentage amounts to IOPs at the time of offset proposal submission.

2. INDIAN DEFENCE OVERVIEW

The government has been driving the Make in India programme, wherein defence is one of the key focus sectors. However, there are several policy and procedural issues that constrain, on one hand, the domestic and foreign companies and OEMs from setting up domestic supply chains, and on the other, the government from getting the "biggest bang from its buck" to achieve its objective of indigenisation and import substitution.

The Stockholm International Peace Research Institute (SIPRI) has reported that India has overtaken France to be the world's fourth-largest[1] military spender in 2018. The report stated India's defence spending rose by 3.1 per cent to USD 66.5 billion. Top three in the list include United States, China and Saudi followed by India and France. However, India imports about 60% of its defence equipment procured under capital expenditure head. The country is ranked second in terms of arms import behind Saudi Arabia for the period of 2015-19 as per SIPRI data. India has a long way to go to become self-reliant in defence production. Nevertheless, increase in defence export comes as a sigh of relief, which doubled to USD 1.5 billion[2] in 2018-19 from USD 0.6 billion in 2017-18. In order to improve India's competitiveness in the international defence market, the government plans to foster the participation from private and public sector players to encourage integration of new technologies and innovations.

2.1 Defence Budget Analysis

The government has allocated about USD 45.8 billion[3] (INR 3,23,053 crores) as defence budget (excluding defence pensions and civil works). The defence budget for 2020-21 has seen a marginal increase of 5.8% over the last year and accounts for 10.6% of the total budget allocation. The defence budget is less than 1.5 % of the GDP which seems to be insufficient considering the evolving security situation in India and its neighbourhood. Considering that the revised estimates exceeded budget estimates by 6.7%, this year's budget allocations seem to be inadequate that are just 2.1% more than the revised estimates. We are pleased to see additional capital allocations for Naval Utility Helicopters (NUH) programme. An increase in capital expenditure by 3.0% over the revised estimates seems to be less and inadequate for the initiatives for modernisation by the Indian armed forces. Our view on some of the key implications of the budget are as follows:

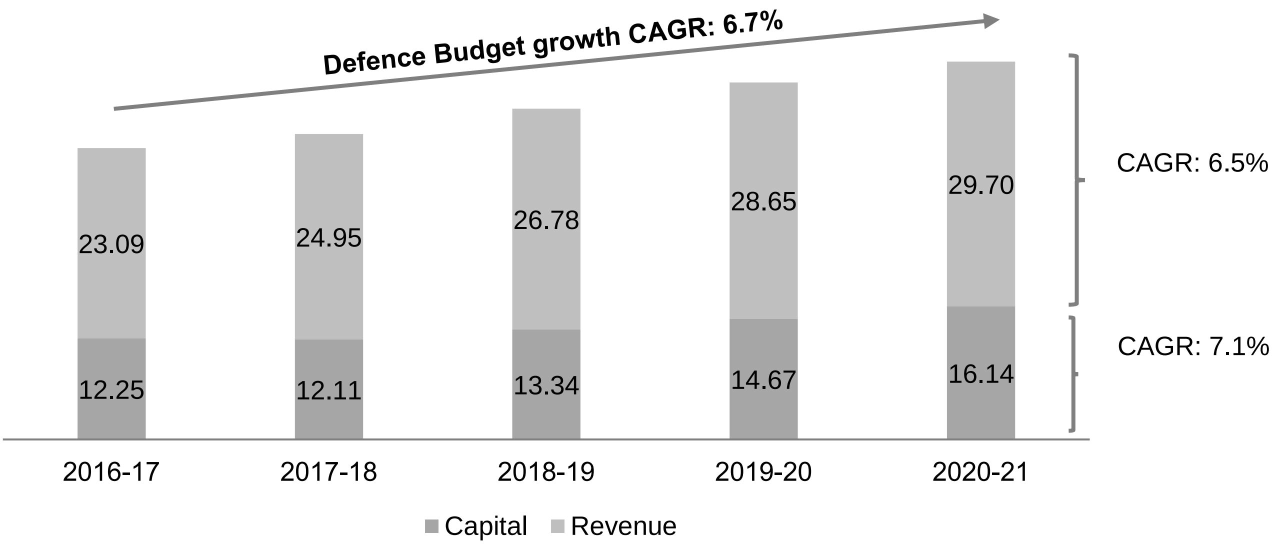
- India should allocate at least 2.5 % of GDP for Defence procurements
- Increased capital allocation for the Indian Air Force (IAF) is mainly for the purchase of aircraft from France's Dassault Aviation.
- Increase in R&D expenditure allocation to boost indigenous defence manufacturing.
- Promotion of the Make-in-India initiative would assist in the developing and nurturing of intrinsic defence production capability but needs to be done in a way that attract foreign OEM:s to invest in India.
- Slight increase in modernisation budget to impact the forces and will leave them with very little scope for modernisation and procurement of new weapon systems.

Key statistics of defence budgets, 2019-20 and 2020-21

	2019-20 (Budget Estimate)	2019-20 (Revised Estimate)	2020-21 (Budget Estimate)
Defence Budget (USD in billions)	43.32	44.88	45.84
Growth of Defence Budget (%)	5.0%		2.1%
Revenue Expenditure (USD in billions)	28.65	29.21	29.70
Growth of Revenue Expenditure (%)	3.2%		1.7%
Share of Revenue Expenditure in Defence Budget (%)	66.1%	65.1%	64.8%
Capital Expenditure (USD in billions)	14.67	15.67	16.14
Growth of Capital Expenditure (%)	8.6%		3.0%
Share of Capital Expenditure in Defence Budget (%)	33.9%	34.9%	35.2%

1. *Growth rate in comparison to Actuals for 2018-19*
2. *Growth rate in comparison to Revised Estimates for 2019-20*
3. *Figures in US$ billion*

Indian defence budget over the last five years (figures in USD billion)



Highlights of the defence budget 2020

- A less than adequate budget allocation has been announced for the defence sector
- Revised estimates indicated that the capital budget for 2019-20 has been completely exhausted and would exceed the budgetary estimates by a margin of 6.7%, which should have been considered for the allocations for 2020-21.
- The total defence budget allocation has increased by 5.8% as compared to 2019-20 budget estimates. **However, the increase over the revised estimates of 2019-20 is marginal at 2.1%.**

- The growth in capital budget estimates is 10.0% and that of revenue budget estimates is 3.7% whereas growth of capital and revenue budget allocations over the revised estimates are 1.7% and 3.0% respectively.
- The capital outlay for the Air Force for 2020-21 is the highest among the three forces at INR 43,282 crore and 38.1% of the total capital budget. Of the total capex allocation, nearly two-thirds or USD 3.82 billion (INR 26,910 crore) would go into buying and upgrading aircraft and aero engines.
- The capital outlay for the Indian Army is at USD 4.6 billion (INR 32,392 crore), of which USD 3.66 billion (INR 25,799 crore) has been allocated for the procurement of aircraft, vehicles and equipment.
- The capital outlay for Indian Navy is USD 3.79 billion (INR 26,688 crore), significant portion (USD 1.8 billion, i.e. INR 12,746 crore) of which will be spent to enhance its naval fleet (warships and submarines).
- Capital allocation towards Research and Development (R&D) has marginally been increased by 0.5% to USD 1.49 billion (INR 10,533 crore). However, the revised estimates of USD 1.24 billion (INR 8,724 crore) indicate that R&D spend was 17% under-utilised as compared to the budgetary allocation of USD 1.49 billion (INR 10,484 crore) for 2019-20, which is not a good sign for the vision of self-reliance in the sector.
- The defence allocation in 2020-21 stands at 10.6% of the total Union Budget of USD431.33 billion (INR 30.4 lakh crore) as compared to 11.0% in 2019-20; Though, it was likely to reduce in the expectation of a stimulus package to stabilise the economy, the overall share of the defence budget in the total union budget has been continuously falling over the years.
- Budget for Navy's Naval Maritime Reconnaissance Helicopters (NMRH) programme has remained unutilised in the current year and thus reallocated for the next year. An additional USD 317.82 million (INR 2,240 crore) has been allocated for Naval Utility Helicopters (NUH) programme.
- Increased capital allocation for Indian Air Force to cater for purchase of aircraft from Hindustan Aeronautics Ltd. and France's Dassault Aviation.
- There is a substantial increase in defence pensions budget by 13.6% over revised estimates and 19.4% over budgeted estimates with allocation of USD 18.99 billion (INR 133,825 crore).
- Over the last five years, the defence budget has grown at 6.7% (CAGR) - revenue budget grew at 6.5% and capital budget at 7.1% CAGR.

3. KEY ISSUES AND RECOMMENDATIONS

While many issues have already been addressed, there are some outstanding issues especially on some aspects of policy and taxation that need to be addressed by the government to better achieve the goal of indigenisation.

3.1. Strategic Partnership (SP) Model

- The SP model was promulgated with an aim to enable participation of private Indian firms in partnership with global defence majors to create a defence manufacturing ecosystem under 'Make-in-India'.
- The Strategic Partner (SP), which will be an Indian company owned and controlled by resident Indian citizens, would be awarded the contract for major defence platforms. The SPs will tie-up with the OEM through a Special Purpose Vehicle (SPV) or JV where the SP should have the majority ownership and control.
- List of segments under SP model include fighter aircraft, helicopters, submarines and armoured fighting vehicles (AFV)/ main battle tanks (MBT).

3.1.1 Issues with ownership and control

- Under SP model, the Indian entities are responsible for response to the RFP, negotiation, contract and delivery, without any true experience in major platform development, production and maintenance. A SPV or JV formed between the SP and the OEM must have ownership and control with resident Indian citizens.

- OEMs on the other hand, cannot hold the controlling share of the SPV/JV. Nevertheless, the OEM has to take joint and several responsibilities in the critical areas of the platform without having a majority stake in the SPV/JV. OEMs must take such responsibility even though they are neither the respondents, nor the contract holders.

3.1.2 Issues with SPs engaging with multiple OEMs

- In the current L1 system, the price remains confidential until the point of decision, allowing effectively each OEM to give his best offer in good faith. However, in the SP route, in a situation where multiple SPs will seek price discovery before deciding which OEM to partner, there may be potential leakage of the OEMs' price and sensitive technical information.

3.1.3 Issues on Indigenisation and ToT in SP Model

- As the SP will ultimately be selected on basis of price competition, they may naturally seek to choose the lowest bidding OEM. This in effect may force them to choose the cheapest compliant bid which could be at odds with the objectives of achieving a high quality of ToT and design and an evolutionary partnership model for the long term.
- It is difficult to objectively evaluate the real success of ToT until after the execution of the project. This may be many years in the future, motivating the OEMs to put something on paper that seems most attractive to win the competition, irrespective of the real feasibility.
- Although the SP policy identifies ToT and indigenisation as key criteria for shortlisting OEMs, however, such criteria are ultimately based on an upfront assessment of something that may not practically be evaluated until some point in the future.

3.1.4 Issue with IP and design transfer:

- It would render the project more attractive for an OEM if the design remains within a JV/SPV in which the OEM has a long-term interest. The OEM will be attracted by a long-term design partnership allowing it to maintain some control of and benefit from the future development and use of the design.

3.1.5 Recommendations on Strategic Partnership Model

- The limitations in the SP policy concerning foreign ownership, control and contract award to majority Indian owned SP should be altered to allow the OEM to be the contract holder as well as to retain control of the SPV in order to warrant success.
- For platforms under the SP model, OEMs should be allowed to have at least 51% control of the JVs with SP. Such ownership will encourage OEMs to hand over core technology as it can retain control on the technology transferred and the IP. If the OEM has no future control of the IP/ToT that is handed over, then it may be reluctant to really hand over core technology. 51% control of OEMs in such a JV would make a difference.
- Indian ownership and control of the SPV may be considered when the SPV´s self-reliant capabilities are established. Once the products as per the original contract are delivered and the requirements are fulfilled, the OEM may consider giving the Indian partner a majority shareholding. This will significantly help achieve the overall aim of the SP Policy of progressively building indigenous capabilities in the private sector to design, develop and manufacture complex weapon systems for future needs.
- In case of indigenisation, it would be better to stipulate the ToT and indigenisation as necessary and run the incentive retroactively. For ToT, any incentive could be paid only the once the ToT is meaningfully absorbed and the authorities are confident that the additional ToT is real. If the required level of indigenisation is exceeded a bonus payment could be made, but only once the performance is proven. This would incentivise performance in the project and discourage "ambitious" claims in a bid to win the competition.

3.2 Offset Regime

3.2.1 Issues in current offset policy

- DPP 2013 and 16 are much more flexible than earlier versions: they allow a larger number of avenues for discharging offsets and allow multipliers. However, these provisions are not retrospective. Since many ongoing contracts are under the highly restrictive DPP 2008, there are numerous challenges in discharging offset obligations and claiming credits.

- Due to the limited timeframe provided to fulfil offset obligations, global OEMs have found lesser reasons to invest in more sustainable, advanced and long-term engineering and manufacturing projects within India.

- Though flexibility to change IOPs has been retrospectively allowed, it is still time consuming for OEMs to get approval for change of the IOP (it can take up to six months), in case an IOP is unable to fulfil its commitment. It becomes even more difficult if the new IOP proposed was not on the list of IOPs originally approved. This process leads to greater compliance cost and creates a difficult execution environment for discharge of offset contracts. OEMs feel that they should have more flexibility to change IOPs.

- The offset credit mechanism for banking of offset claims is currently not time bound and highly inefficient and non-transparent. There are very few banking proposals that have been approved.

- Currently, only tier-1 sub-vendors on the main platform are permitted to discharge offsets to the extent of their workshare (by value) on behalf of the prime vendor, thereby restricting its scope. Tier-2 and tier-3 sub-vendors are currently not permitted to discharge the offset obligations on behalf of OEMs.

- Group companies, sister concerns, and subsidiaries are not permitted to discharge offset obligations on behalf of the OEM without their being the part of the supply chain of the main platform/equipment being bought.

- Due to the limited timeframe provided to fulfil offset obligations, global OEMs have little incentive to invest in more sustainable, advanced and long-term engineering and manufacturing projects within India.

- The offset policy is complex and requires further simplification in the implementation stage as the documents to be submitted to MoD are voluminous, without any scope of e-filing.

- Qualified aerospace-grade raw material suppliers are not currently established in India due to the limited size of the market. Aerospace-grade raw materials could represent up to 60%of the cost of complex aerospace products, and under the current policy this value would be excluded from the offset credit value for manufacture of such products. The current “Value addition” principle incentivises OEMs to source low technology commodities in India rather than higher complexity items having greater import content. To avoid losing offset credit due to import of aerospace-grade materials for large, complex aerospace systems and platforms, OEMs are compelled to focus on placing only ‘low value-low complexity’ work for which raw material sources are available in India.

- OEMs have been facing challenges in Transfer of Technology (ToT) to DRDO on account of lack of laid down methodology for valuation of such ToT. Technology transfer or technology acquisition (TA) to DRDO are permissible methods for discharge of offsets. However, OEMs face challenges on two counts:
  - Many OEMs have found it difficult to reach an agreed position with DRDO on value of technology (IPR) proposed to be transferred, primarily due to absence of established methodology for valuation of technology.
  - Such TA by DRDO is restricted to only 30% of value of offsets to be discharged. However, the actual value of technology proposed to be transferred far exceeds the 30% threshold and any excess value due to this activity cannot be banked under the current provisions.

- There is a scope that ToT be evaluated by a recognised third party for offset proposal.

3.2.2 Recommendations on offset policy

- Group companies/fully owned subsidiaries should be allowed to discharge offsets within the same proposal. A single OEM might have several subsidiaries/ entities – asking each entity to maintain a separate offset bank, or submit offset proposals that are independent of each other, will lead to short-term and tactical rather than long-term, strategic partnerships with Indian companies. An OEM could have multiple departments that could work with an Indian partner – but disallowing group companies from participating in the offset contract means that the OEM is disincentivised from growing the partnership with the Indian company.
- For OEMs to look at Indian partnerships in a strategic rather than transactional manner; Indian partner companies/foreign tier 2 or tier 3 companies should be allowed to discharge offset obligations on behalf of the vendor. The vendor can then enter multi-project, long-term relationships for manufacturing in India, and. This will help Indian Offset Partners (IOPs) grow faster. The vendor can also encourage international tier 1/tier 2 sub-vendors and other partner companies to do the same, leading to more technology partnerships.
- Tier-1 suppliers should be allowed to discharge offset obligations on behalf of the foreign OEM for all offset contracts and they should be permitted to discharge offset beyond the extent of their work share. Tier-1 suppliers play an important part in the Aerospace & Defence industry, supplying anywhere from 50-80% of the cost of the final product, and they also own the IP for technology in areas such as aircraft engines, avionics, landing gear, hydraulic actuators, machining, and sheet metal components. For India to develop an ecosystem of aerospace capabilities, it is crucial for Indian companies to get opportunities in areas that Tier-1s are active. If global Tier-1s can discharge obligations without any workshare cap, the scale of manufacturing activity would significantly increase.
- Defence Offset Management Wing (DOMW) should be better empowered to take quick decisions.
- The period of offset discharge has been fixed at the period of supply of the main equipment plus two years as per the DPP. OEMs believe that it should be determined on basis the mutual negotiations between MoD and OEM considering various factors such as contract type, period of implementation, time taken for IOP to build capabilities and meet quality requirements.
- Flexibility in performance period will enable a more transparent and controlled programme management by the OEM offset obligor. Hence, a further extension in the period of performance will encourage more complex collaboration in defence manufacturing and development.
- Instead of committing fixed dollar/percentage amounts to IOPs at the time of offset proposal submission, a more flexible approach that permits global OEMs to define offset amounts to be allocated to each IOP over the course of the programme may be adopted. This continuous feedback model will enable greater and more robust IOP engagement and will better benefit India’s industry across large, medium, and small-scale enterprise.
- The offset credit mechanism for banking of offset claims should be time bound and efficient and there should be a prescribed time limit for the DOMW for replying to questions.
- The MoD should expand the list of eligible services for discharge of offset obligations, to include assembly, integration and testing services; setting up testing infrastructure; undertaking skill development projects in India.
- There is a need to create a skilled workforce for advanced manufacturing, in India. Allowing skill development for discharging offset obligation may help in creating a skill base in the Indian industry.
- In addition to the avenues for discharge of offset obligations mentioned, some

additional avenues such as investment in specified projects may be included.

- In terms of value addition, a more pragmatic, market-based approach would be to include the imported raw material value in the offset credit amount in cases where raw material is not available locally. This would incentivise sourcing of higher complexity work packages, thus increasing aerospace manufacturing volumes, and creating the conditions for raw material suppliers to invest in facilities in India.
- Alternatively, India should establish thresholds for value addition, similar to global practices, above which the OEM would receive full offset credit in the amount of the total invoice value, e.g.,, greater than 40% India value addition would result in offset credit amounting to 100% of the invoice value.
- Another variation of this can be to include raw materials that are not currently available in India for value-add calculation. Eventually, as the OEMs develop India sources for such raw materials, give them a 3x multiplier for raw material value.
- A well-defined valuation methodology based on global standards may be laid down in the DPP for the cases involving TA to DRDO. Moreover, in case the value of technology proposed to be transferred exceeds the offset requirement, any excess value should be permitted to be banked.
- Approved banked credits up to the date of contract signature should be allowed to be used towards discharge of offset obligation even though such credits were not part of initial offset proposal.
- Valuation of ToT to Industry - Offset credit for ToT to industry is only 10% of buy back value. Therefore, presently only low-level technology is generally given to industry via the offset route. Policy of offset credit for ToT to industry should be similar to technology acquisition by DRDO. An independent body should evaluate the ToT and offset credit given for full value with multipliers.
- Based on the valuation offset credit should be awarded over and above the credits linked to buy back
    - For ToTs, higher value may be provided by know-why ToT rather than know-how ToT
    - In addition to the offset credits for ToT value, it can also be included as a criterion for award of the main bid

3.3 Export, imports & licensing

3.3.1 Revision of list of defence items requiring Industrial License

The Ministry for Commerce and Industry released two revised and independent lists of defence items requiring an industry licence under the Industries (Development and Regulation) Act, 1951, and under the Arms Act, 1959. Annexure I pertains to defence aircraft, warships of all kind and allied items of defence equipment, which are covered under the Industries (Development and Regulation) Act, 1951. Annexure II covers tanks and other armoured fighting vehicles and arms and ammunitions and allied items of defence equipment, which are covered under the Arms Act, 1959. The list of defence items requiring industrial licences has been pruned by removing the requirement of licensing for 'parts and components of the equipment', which is expected to facilitate the entry of small and medium enterprises (SMEs). This move will also help foreign original equipment manufacturers (OEMs) looking to build the supply chain under the Strategic Partnership (SP) model. FDI policy in defence sector is applicable to the manufacturing units that are planning to produce items that require industrial license. As components and subcomponents have been removed from the licensing list, the foreign companies can now set up 100% subsidiary in India or formulate a joint venture with majority control.

3.3.2 Issue with Open General Export License (OGEL) scheme

The Government notified the Open General Export License (OGEL) scheme on October 2019. Thereafter MoD suggested that for intra-company transfer, companies should apply for OGEL. However, the online OGEL system is still not in place and though the companies are being advised to apply offline under OGEL category, the applications are not processed in the absence of online system. Companies are then advised to apply via normal SCOMET application route, but approval time is reset resulting in substantial delays. This delay impacts global programmes and undermines India's reputation towards Ease of Doing business.

3.3.3 Issue with imports for skill development

The Government of India places significant focus on skill development. There is also a tacit understanding that ToT requires skill upgradation. However, there are no fiscal benefits for such initiatives particularly towards import of components for this purpose. There is no duty exemption either towards imports for the purpose of skill development. Skill development entities such as sector skill council and/or NSDC are hopeful that case-by-case exemptions can be sought but lack of precedence and clarity on timelines involved results in reluctance to rollout skill development programmes.

3.4 FDI

3.4.1 Current FDI Policy

As per the policy, foreign investment up to 49% is permitted in the defence sector through automatic route, and beyond that limit through government route on case to case basis, wherever it is likely to result in access to modern and state-of-art technology.

3.4.2 Impact of revised list of defence items requiring industrial licences (IL)

The list of defence items requiring (ILs) were pruned by removing the licensing requirement for 'parts and components of equipment'. The current FDI policy is applicable to those segments/products in the defence sector which require industrial license under the Industries (Development & Regulation) Act, 1951. This essentially leads to the understanding that for manufacturing parts and components, the FDI cap of 49% under automatic route would not apply. Thus, foreign players may own up to 100% stake under the automatic route.

3.4.3 Recommendations

- For segments/products subject to industrial license under the Industries (Development & Regulation) Act 1951, FDI in defence of up to 74% under automatic route should be permitted unconditionally.
- Additionally, the criteria for approving 100% FDI should be made quantitative and measurable. Foreign OEMs in the proceedings for transfer of technology involving intellectual property (for example, high-tech jet engine systems), find the 49% cap inadequate.

3.5 Indigenisation and ToT

3.5.1 Indigenous content vs indigenous capability

- The DPP mandates a certain minimum requirement of Indigenous Content (IC) for each procurement category. The current IC requirement refers to how much of the relative cost (in percentage terms) of the product is produced in country. Since it requires transfer of manufacturing of equipment of an already developed product, it is inefficient not just for the OEM but also for the local industry. A high IC does not necessarily mean that capabilities are transferred. For e.g., – if a fuel pump has 40% IC, it does not imply that the capability to develop and produce a fuel pump exists indigenously.
- The cost-based IC approach for production transfer leads to build-to-print license manufacturing. License manufacture may eventually result in a high IC percentage along with viable business for the local manufacturer in the short-term. The level of actual capabilities acquired and captured such as the know- how and know-why that can be used for future programmes are negligible. Therefore; there is a need to reassess this definition of cost-based IC. To ensure self-reliance to develop, produce and upgrade, there is a need to focus on achieving high indigenous capability.
- Indigenous capability content ensures securing long-term independence by build-up of self-reliant capabilities. Capabilities include the prerequisites to excel in engineering in terms of know-how, know-why, processes, methods, tools and technologies. This approach to true ToT/capabilities will result in long-lasting benefits.
- To achieve higher self-reliance and indigenisation there is a need to promote indigenous capability over indigenous content in R&D as well as in production. This transfer of capability that includes ToT, transfer of design, production, and support should be given due ratings and weightage (I1). The

rating procedures should allow for qualitative evaluation and each key parameter should have different weight reflecting its level of importance.

- Besides assessing the best transfer of industrial capabilities offered (I1), the foremost objective of a defence procurement procedure is to identify the alternative that brings the most to strengthening national security. For e.g., in case of fighter procurement; air power is derived from a combination of self-reliant operational capabilities at lowest total life cycle cost.

3.5.2 Evaluation methodology for better ToT and indigenous capability

True L1 – Life cycle cost evaluation

The current 'L1' process does not consider all important cost parameters related to acquisition and ownership of the entire system over its full-service life, which also must include support, operation and preferably projected upgrade cost. An asset may be cheaper to procure but costlier to operate and maintain i.e. The Life Cycle Cost (LCC) is the most important criteria to evaluate and must form a key part of the L1 based down select. The use of LCC requires a model that is able to correctly identify all the cost elements and properly estimate all the cash outflows throughout the life of the asset. Moreover, an incomplete model may not only produce incorrect estimation but also distort fair play among the bidders. A detailed approach towards calculating true LCC must be developed that also includes a PBL approach to L1 determination of LCC.

3.5.3 Technical/Operational Capabilities Evaluation (T1)

Additionally, for India to get cutting-edge technology systems, fair weightage should be given to parameters that reflect the true operational performance of the system. Presently within the policy framework, only objectively quantifiable technical performance figures are considered. If a specific equipment or product meets a bare minimum threshold, it qualifies as compliant. There are no additional weighted criteria assigned towards improved performance over this threshold. Further, there is no way to evaluate important factors that reflect the ability for self-reliant sustained operational relevance in the long term, such as upgradeability, operational availability and effectiveness.

For procurement of highly technical products there should be a system performance-based evaluation and a weighted approach to reward requirements that exceed minimum thresholds. Rather than assessing certain point performances, a more effective way is to evaluate the capabilities and effectiveness of the total system starting with an assessment of the Concept of Operations (CONOPS). From the CONOPS, various types of mission scenarios that reflect both the present and future operational environment and threats should then be used for evaluation purposes.

3.5.4 A holistic weighted approach

- Defence technologies need long term investments and are therefore prone to high obsolescence and low economies of scale. Local industry should therefore have the capability to constantly upgrade and evolve with changing future technologies. The Defence Policy objective of self-reliance will not be achieved without having a well thought out indigenous capability development (I1) strategy, so that the Indian industry is assured of access to capabilities for upgrade and continuous development of modern defence technologies and platforms.
- This will only be possible when modern technology is transferred in the truest sense to the local industry in a way that will truly import capability, sustainability, knowledge and skills within design, in-service support and production.
- For the procurement of highly technical products such as fighter aircraft, the use of Best Value method i.e. T1L1I1 assessment, in addition to a weighted mechanism that gives due importance to upgradability, operation availability, transfer of capabilities and technologies will always yield better value for money.
- A methodology to comprehensively evaluate and select platforms based on quantitative methods of best value for money through an L1/T1/I1 approach is the need of the hour. This approach will lead to self-reliance and indigenous capability development in the real sense.

3.6 Taxation Regime

3.6.1 Issues

The Indian tax regime is complicated. While finalising bids, OEMs need to consider multiple taxes likely to be applicable through the supply chain such as custom duty, GST etc. Such taxes are not entirely creditable or capable of being passed on to MoD, leading to higher bid prices due to cascading effect and distortions in bid pricing due to tax reasons.

Direct tax

- Royalties/fees for technical services earned by non-residents from notified defence projects entered with the government of India for security of India are exempt from tax in India. Notification is required to be obtained from the government in this regard. Similar defence contracts entered with the DPSUs acting on behalf of MoD/Government of India are not specifically captured in the provision.
- Notification in the official gazette for aforesaid exemption is presently a time-consuming process.
- Further, at times the foreign company may receive income which could be other than royalties or fees for technical services e.g., income from onshore supplies in connection with EPC contract involving both offshore and onshore elements, which as per the current provisions, may not eligible for tax exemption.
- Foreign defence entities desirous of establishing a presence in India generally set up a liaison office for identifying opportunities, developing relationships with potential customers and providing administrative support. Indian revenue authorities have been quite aggressive in alleging/assessing such liaisons and support offices as permanent establishments (PEs) of non-resident OEMs/contractors in India. This has often led to frivolous tax demands and more frequent long-drawn tax disputes.
- The Income-tax Act, 1961 provides for a deduction on any expenditure of a capital nature incurred wholly and exclusively for the purposes of any specified business carried on during the year. The Act also provides for 100% deduction of profits and gains to the persons engaged in the eligible business. The licensed manufacture and production of defence and aerospace equipment and parts thereof are not specifically included in specified business.

Indirect Tax

- The government is working towards the immediate requirement in the defence sector towards modernisation and upgradation. For this purpose, import of defence equipment that are not being manufactured in India are being exempted from the Customs Duty. Also, such exemption has been extended to imports made by defence public sector undertakings and other public sector undertakings.
- GST does not apply on MRO services undertaken outside India. Taxing of MRO services in India has resulted in increased cost for Indian private companies
- Petroleum products (including ATF) have been kept outside the ambit of GST. ATF in India is 55-60% costlier than the Gulf and Asian region.

3.6.2 Recommendations

Direct tax

- Clarity is to be provided on the availability of tax exemption on royalties/fees for technical services contracts by non-residents (foreign OEMs) with DPSUs. In order to promote domestic manufacturing, such exemptions may also be extended to private companies as well.
- Procedural delays in providing such tax exemptions may be looked into
- It is recommended that the provision of section 10(6C) be suitably amended to extend the exemption to other incomes which the foreign company may derive from the project in connection with security of India.
- Necessary guidelines should be issued to reduce tax litigation in cases where a PE of the non-resident has been alleged. This shall ensure certainty in tax outcome, thereby encouraging investment.

- In order to encourage the 'Make in India' initiative and investments in the defence sector, it is recommended to extend capital expenditure deduction provided under section 35AD or provide profit linked deduction/tax holidays from eligible business of manufacture and production of defence and aerospace equipment and parts thereof.

Indirect tax

- To improve cost competitiveness, GST exemption should be extended to MRO services undertaken in India.
- The cascading effect of ATF taxes have brought ruin to the A&D sector. To achieve cost efficiency ATF should be brought under the GST regime with a uniform rate across India.

ENDNOTE

1. SIPRI https://www.sipri.org/research/armament-and-disarzmament/arms-and-military-expenditure/military-expenditure
2. Centre for Land Warfare Studies https://www.claws.in/static/India%E2%80%99s-Defence-Exports.pdf
3. Average exchange rate of first 10 months of 2019-20 considered for currency conversion: (US$1.0=INR 70.48)

Financial Services

Acknowledgements: Sarpreet Benipal (Home Credit) – Chairman, Financial Services Sector Committee & its Members
Knowledge Partner: Anugraha Mundra and Kunal Gaur – TMF-Group

EXECUTIVE SUMMARY

The world over, non-banking financial entities complement the mainstream banking system in the process of financial intermediation. The shadow banking sector in India primarily includes Non-Banking Financial Companies (NBFCs) and collective investment vehicles such as money market funds, fixed income funds, real estate funds, and securitisation-based credit intermediation like securitisation vehicles and structured finance vehicles. Mutual Funds, Alternative Investment Funds and Insurance companies also mobilise huge sums of money and support the investment flow of funds. India's financial system saw a huge turmoil for last two years especially due to non-performing assets (NPAs)/Stressed Assets of the Public-Sector Banks and the Liquidity Crisis of the NBFCs. The transition of credit intermediation from the banking sector to the non-banking sector though welcome, calls for increased monitoring and prudential regulation.

The efficiency and competitiveness of the banking sector is likely to increase with entry of differentiated banks, posing some transitional challenges to the universal banks. The mutual funds market is expanding beyond the top 15 cities. Various initiatives by regulators to develop the corporate bond markets seem to be bearing fruit as reflected in increased issuance and turnover in the secondary market. Concerns arising from frauds and cyber-attacks remain elevated with the recent global ransomware attacks. Various responses by the regulators in this regard include setting up of an Inter-disciplinary Standing Committee on Cyber Security by the Reserve Bank of India (RBI).

The government seems to be committed to its target of increasing the inclusion of every household in the financial system so that the masses can get all the legitimate benefits arising out of the growth of the country and in turn, the funds mobilised from the people could also be brought in the formal channel thereby giving the economy of the country an extra thrust to lead the path of growth.

The onset of the pandemic in India and resultant lockdown starting March 2020 has severally impacted the whole economic activity and NBFC sector, which was already struggling to overcome the liquidity, and the NPA crisis has been presented with newer unprecedented challenges. The Indian government has though timely responded with scores of measures to boost liquidity but it's still early days to fully evaluate the depth of its adverse impact. The sector at the same time also holds the key for economic revival by making credit available to length and breadth of country to boost MSME investments and consumer demand.

The advancements whether in the form of digitisation or regulations result in expectations by European companies for further improvement by the Government of India to strengthen the financial sector. The EBG Federation, through this paper and on behalf of European companies have highlighted issues and suggested recommendations so that the real issues are discussed and addressed in the right forum.

While the government initiatives are helping to move towards globalisation and creation of opportunities for becoming a developed nation with focus on investment in infrastructure growth, education and health care schemes, finance, tax and governance reforms promoting digital economy with incentives and rewards; it is imperative that the issues and recommendations are mentioned in this paper are also discussed appropriately for an inclusive growth.

1. INTRODUCTION

India's financial sector comprises commercial banks, insurance companies, non-banking financial companies, co-operatives, pension funds, mutual funds, other smaller financial entities and payment banks being latest entrant to vibrant arena. NBFCs have done a remarkable work on many fronts including but not limited to financial inclusion, coverage of geographical areas otherwise unviable for commercial banks to operate, extending formal credit to India's medium and small enterprises, which is crucial for India's economic development.

India along with other large emerging global economies were already witnessing declining economic growth for past few years even before the COVID-19 pandemic drastically affected all world economies without any exception. India is projected to be amongst the worst-hit economies globally wherein all major rating agencies and banks estimate that the Indian economy is likely to contract in double digits in the range of 11-12%, which is supported by First Quarter (April-June) GDP decline by 23.9%. At this time it, is a common belief that recovery post pandemic will not be v-shaped owing to large-scale reduction in consumption and investments.

The slowdown in global and domestic growth impulses in the recent past impinged on credit demand. The asset quality, capital adequacy and profitability of scheduled commercial banks improved after a long period of stress, although challenges emerged from other areas like non-banking financial companies and co-operative banks. The COVID-19 impact of already stressed sector is likely to worsen going forward the issues such as resolution of stressed assets, weak corporate governance, and frauds that need to be addressed to reaffirm a robust financial sector that minimises systemic risks.

Domestically too, the weakening of growth impulses and subdued credit off-take are playing out, with sporadic credit default events and incidents of frauds exacerbating the reluctance to lend. This is starkly evident in the slowdown of flow of resources, both from banks and non-banks to the commercial sector in the first half of 2019-20. In turn, this waning of confidence is weighing on overall economic activity. This is worrisome as it is taking hold at a time when the recent improvements in asset quality and profitability of the banking sector are at a nascent stage and capital ratios of public sector banks (PSBs) are shored up due to recapitalisation by the government. Notwithstanding the enhanced resolutions through the Insolvency and Bankruptcy Code (IBC), the overhang of NPAs remains. The health of the banking sector hinges around a turnaround in macroeconomic conditions, which may now be prolonged in view of pandemic.

Although the balance sheet size of the NBFCs constitutes 18.6% of SCBs, it has emerged as an important pillar of the Indian financial system. The sector, which had witnessed a robust expansion in 2017-18, experienced headwinds in 2018-19 and 2019- 20 (up to September) as market sentiments turned negative post-IL&FS event and recent defaults by some companies. The Reserve Bank and the government have taken several measures to restore stability in the NBFC space. The Reserve Bank took measures to augment systemic liquidity, buttress standards of asset-liability management framework, ease flow of funds by relaxing ECB guidelines and strengthen governance and risk-management structures. The government provided additional support through the partial credit guarantee scheme, encouraging PSBs to acquire high-rated pooled assets of NBFCs. Furthermore, the Finance Bill 2019 through amendments in the RBI Act, 1934 conferred powers on the Reserve Bank to bolster governance of NBFCs. These measures are geared toward allaying investors' apprehensions and aiding NBFCs in performing their role better. Going forward, the Reserve bank will continue to maintain constant vigil over NBFCs and take necessary steps to ensure overall financial stability.[1]

The economic growth slowdown even before COVID-19 economic impacts, of past 3-4 years had major adverse impact on NBFCs sector, which manifested in form of asset liability mismatches, liquidity crisis and widespread defaults in debt service by NBFCs. A large part of portfolio of NBFCs consist of small and medium business owners who experienced significant decline is demand as well as profitability of their products over the last few years owing to general economic slowdown along with disruptions such as demonetisation, GST, technological changes, competition from other developing countries and newer business models. This has contributed to rise in non-performing assets in books of majority of NBFCs. Further NBFCs having large exposer towards infrastructure and real estate sector have witnessed highest stress in their loan books as evidenced by the growing level of non-performing assets (NPAs).

The sector is also facing major liquidity crisis, while the prominent NBFCs with good ratings are better placed to deal with the current challenges, the smaller ones have been impacted the most in their ability to run business because of the liquidity crunch. Securitisation of assets has emerged as important source of viable fund-raising owing to difficulties being faced in raising funds from other sources. The rise of NPAs in books adversely affects the credit ratings, which in turn further impair the ability to raise funds as cost of funds goes up for such NBFCs.

Government of India along with the Reserve Bank of India has recognised the issue being faced by NBFCs and have responded with number of measures to alleviate the situation and boost lending to NBFC, some prominent among these are priority sector classification, extending partial credit guarantees, Easing of risk-weightage norms for banks, partial credit guarantee, co-origination model, securitisation and credit guarantee fund trust for MSME.

NBFCs are also facing competition from FinTech firms, which continue to capture market share with their high tech and low-cost operating models and by setting new standards when it comes to customer experience. The FinTech start-ups have seen a tremendous growth over the last 5 years with approximately 1,800 FinTechs founded in the period mainly to fulfil the unmet needs of the underserved retail segment. The size of FinTech transactions is estimated to reach US$137.8 billion by 2023 with a CAGR of 20%.[2]

FinTechs are successfully deploying data analytics, blockchain, machine learning and AI to deliver much better customer experience through new-age underwriting models, seamless partner integration and real-time loan decisions.

1.1 Market Description

1.1.1 Non-banking financial companies (NBFCs) refers to financial intermediaries, which offer various services that include equipment leasing, hire purchase, loans, investments and chit fund activities. These entities play a vital role in offering credit to the unorganised sector and to the small borrowers at the local level. NBFCs can be classified on the basis of a) their asset/liability structures; b) their systemic importance; and c) the activities they undertake. In terms of liability structures, NBFCs are subdivided into deposit-taking NBFCs (NBFCs-D) - which accept and hold public deposits - and non-deposit taking NBFCs (NBFCs-ND) - which rely on markets and banks to raise money. Among NBFCs-ND, those with an asset size of INR500 crore or more are classified as non-deposit taking systemically important NBFCs (NBFCs-ND-SI). At the end of September 2019, there were 82 NBFCs-D and 274 NBFCs- ND-SI as compared to 88 and 263, respectively at the end of March 2019.[3]

1.1.2 The future looks promising for the life insurance industry with several changes in regulatory framework, which will lead to further change in the way the industry conducts its business and engages with its customers. There are 24 life insurance and 33 non-life insurance companies in the Indian market who compete on price and services to attract customers, whereas, there are two reinsurance companies. The industry has been spurred by product innovation and vibrant distribution channels, coupled with targeted publicity and promotional campaigns by insurers. The market share of private sector companies in the non-life insurance market rose from 15% in FY2004 to 56% in FY2021 (till April 2020). In life insurance segment, private players had a market share of 31.3% in new business in FY2020.The government has approved an ordinance to increase Foreign Direct Investment (FDI) limit in the Insurance sector from 26% to 49%, which would further help attract investment in the sector. Per Union Budget 2019-20, 100% FDI was permitted for insurance intermediaries.

The Gross premium collected by life insurance companies in India increased from INR2.56 trillion (US$39.7 billion) in FY2012 to INR7.31 trillion (US$94.7 billion) in FY2020. During FY2012–FY2020, premium from new business of life insurance companies in India increased at a 15% CAGR to reach INR2.13 trillion (US$37 billion) in FY2020.[4]

The domestic insurance industry appears to be very vibrant. The government's policy of insuring the uninsured has gradually pushed insurance penetration in the country and proliferation of insurance schemes. India with 3.71% penetration rate in 2018 in the insurance sector offers greater penetration potential when compared to global average of 6.2%.

1.1.3 Mutual fund (MF) industry in India is maturing with broad-basing of investors and increasing geographical spread. MFs in India have become major players in the equity and corporate bond markets and are also providing crucial liquidity support to the money market. Consequently, their influence on price movements in equity and debt markets as also domestic liquidity conditions has increased over time. While the penetration of the MF industry in India, as measured by the Assets under Management (AUM)/GDP ratio, is still low compared with the global average, favourable demographics, a history of high savings propensity and regulatory reforms brighten the outlook for the industry. The AUM of the Indian MF Industry has grown from INR7.67 trillion as on 28 February 2010 to INR27.23 trillion as on 29 February 2020 more than 3½ fold increase in a span of 10 years.[5]

MFs appear to have emerged as a preferred investment avenue for individuals as well as corporates. While the flow of resources to banks generally declined during the period 2013-18, the flow of resources to small savings schemes registered modest increase. In comparison, the flow of resources to MFs and insurance companies registered a significant increase during the period. During the period 2013- 2018, the CAGR of bank deposits and small savings were 11% and 6%, respectively, which was much lower than CAGR of AUM of MFs (25%).[6] AMFI data shows that the MF industry had added, on average, 9.55 lakh SIP accounts each month during FY2019-2020, with an average SIP size of about INR2,850 per account. In the current financial year (2019-2020), the total inflows through SIPs stood at INR82,929 crore. [5]

1.2 Recent Developments

1.2.1 **NBCF Liquidity Crisis:** Based on the risks of few NBFC defaults, Banks and Mutual funds slowed down on further lending to NBFCs and recalled money, which led to asset liability mismatch of NBFCs and further added to liquidity crisis. On the other hand, when the interest rates were rising, margins of NBFCs came under pressure and raising capital became tough. Anticipating further risks, Banks and Mutual funds started cutting exposure to NBFCs since April 2018 in the wake of the huge bad loans, which led to a drop in their exposure to the sector. This also created a ripple effect in capital markets as all NBFCs including Housing Finance Companies started feeling the heat from investors. This also raised questions on few NBFCs having exposure to real estate and developers as the risk of default increased.

1.2.2 **Exposure to Sensitive Sectors**: Capital market, real estate and commodities have been categorised as sensitive sectors by the Reserve Bank as prices of these assets are prone to fluctuations that may pose a risk to financial stability. By the end of March 2019, the capital market exposure of NBFCs had decreased compared to March 2018, even as real estate exposure edged down. As a result, an overall decrease in sensitive sector exposure was registered

1.2.3 **NBFC Registration Cancellation:** As per the regulatory guidelines, only those NBFCs with a minimum net owned fund (NOF) of INR2 crore are allowed to operate. As a result, 2018-19 saw a record number of cancellations of registration. The number of NBFCs registered with the Reserve Bank declined from 9,856 at the end of March 2019 to 9,642 at the end of September 2019[7].

1.2.4 **AIFI**: The Reserve Bank regulates and supervises four all India financial institutions (AIFIs), viz., Export Import Bank of India (EXIM Bank), National Bank for Agriculture and Rural Development (NABARD), Small Industries Development Bank of India (SIDBI) and the National Housing Bank (NHB). Consequent to the Reserve Bank's divestment of its entire shareholding in NHB on 19 March 2019, it has become an entirely government-owned institution.

1.2.5 **Strengthening the NBFC Sector:** To strengthen the liquidity framework for NBFCs, a liquidity coverage ratio (LCR) has been introduced for all deposit-taking NBFCs (NBFCs-D) and non-deposit taking NBFCs (NBFCs-ND) with an asset size of INR5,000 crore and above. This measure—covering almost 87% of the total NBFC sector by asset size—will be implemented along a glide path spanning over four years, commencing from December 2020. The complex business structure of the core investment companies (CICs)—which were at the heart of the recent NBFC sector challenges, is under review.

1.2.6 **Prudential Framework**: During 2018-19, the Reserve Bank introduced a prudential framework for resolution of stressed assets, which aimed at ring-fencing and protecting the banking sector from the build-up of non-performing assets. The macro prudential framework was further aligned to the best international practices, while monetary policy responded to the emerging macroeconomic developments. The Reserve Bank improved governance and reporting practices of banks. Concerted efforts were undertaken to strengthen the liquidity and regulatory framework governing non-banking financial companies and also to remove the regulatory arbitrage, while catalysing liquidity flows to the sector. Modernisation of payment and settlement systems was a concomitant pursuit.

1.2.7 **Policy Measures for NBFC Sector**

- The Finance Bill 2019 through amendments in the RBI Act, 1934 conferred powers on the Reserve Bank to strengthen governance of NBFCs so as to protect depositors'/creditors' interest and secure financial stability. The amendments empowered the Reserve Bank to remove the directors of NBFCs; supersede their board and appoint administrators to improve governance and protect the interests of depositors and creditors; impose penalties in case of non-compliance with various requirements; and to resolve an NBFC by amalgamation, reconstruction or splitting an NBFC into different units or institutions.
- Reverse bank of India has set out various developmental and regulatory policies that directly address the stress in financial conditions caused by COVID-19. They consist of expanding liquidity in the system, reinforcing monetary transmission so that bank credit flows on easier terms, easing financial stress by relaxing repayment pressures and improving access to working capital and improving the functioning of markets. Repo rate, reverse repo rate, CRR and minimum balance of CRR has been reduced. Further 6-month moratorium has been provided on payment on instalments of Term Loan outstanding has been provided for.
- RBI announces second set of measures to preserve financial stability and help put money in the hands of the needy and disadvantaged. These measures aimed at maintaining adequate liquidity in the system and its constituents in the face of COVID-19 related dislocations, facilitate and incentivise bank credit flows, ease financial stress, and enable the normal functioning of markets. States and UTs allowed to borrow more to manage COVID-19. Reverse Repo rate reduced from 4.0% to 3.75%
- As part of COVID-19 Economic package for NBFC sector government introduced two schemes of credit guarantee. First Scheme is special liquidity facility of INR 30,000 crores wherein investments made in investment grade debt securities of NBFC, HFC, and MFI is fully guaranteed by government. The second scheme involves INR 45000 crores partial guarantee scheme to help the lower rated small NBFCs and MFIs.
- A Working Group constituted by the Reserve Bank to review regulatory and supervisory framework for Core Investment Companies has submitted report and recommended that the number of layers of CICs in a group should be restricted to two along with measures to strengthen the governance practice by constituting board level committees, appointing independent directors and a Group Risk Management Committee.
- End-use restrictions relating to external commercial borrowings were relaxed with eligible borrowers allowed to raise ECBs from recognised lenders (except foreign branches/overseas subsidiaries of Indian banks) of (i) a minimum average maturity period of 10 years for working capital purposes, general corporate purposes and repayment of rupee loans availed domestically for

purposes of on-lending (other than capital expenditure) by NBFCs. (ii) a minimum average maturity period of 7 years for repayment of rupee loans availed domestically for capital expenditure.

- Banks were allowed to provide partial credit enhancement (PCE) to bonds issued by NBFCs-ND-SI registered with the Reserve Bank and HFCs registered with National Housing Bank, provided the tenor of the bonds is not less than three years, proceeds from such bonds shall only be utilised for refinancing existing debt of the NBFCs-ND-SI/HFCs.
- To encourage NBFCs to securitise/assign their eligible assets, the Reserve Bank has relaxed the minimum holding period (MHP) requirement till 31 December 2019 for originating NBFCs in respect of loans of original maturity above 5 years, subject to certain conditions.
- All scheduled commercial banks (excluding Regional Rural Banks and Small Finance Banks) were allowed to co-originate loans with NBFCs-ND-SI for the creation of eligible priority sector assets, facilitating sharing of risks and rewards.
- Asset Finance Companies, Loan Companies, and Investment Companies were merged into a new category called NBFC- Investment and Credit Company (NBFC-ICC), reducing the complexities arising from multiple categories and also providing the NBFCs greater flexibility in their operations.
- Large NBFCs, with asset size of more than INR5000 crore were required to appoint a functionally independent Chief Risk Officer (CRO) with clearly specified role and responsibilities, with involvement in the process of identification, measurement and mitigation of risks.
- The Government of India has rolled out the scheme to provide a one-time partial credit guarantee for the first loss up to 10% to public sector banks (PSBs) for purchase of high-rated pooled assets amounting to INR1 lakh crore from financially sound NBFCs/HFCs.
- Co-origination of priority sector loans by banks and NBFCs: The Reserve Bank in September 2018 announced guidelines for co-origination of priority sector loans by banks and NBFCs with a view to enhancing flow of funds to the sector at competitive rates. As per the norms issued by the RBI for all scheduled commercial banks (excluding Regional Rural Banks and Small Finance Banks) and Non-Banking Financial Companies - Non-Deposit taking- Systemically Important (NBFC-ND-SIs), the sharing of risks and rewards between these entities should be in a manner that enables appropriate alignment of respective business objectives, per their mutual agreement. The co-origination arrangement should entail joint contribution of credit by both lenders at the facility level. NBFC-MFIs and mid-sized NBFCs focusing on the MSME segment are expected to be the key beneficiaries given their focus on customer segments, which qualify for priority sector classification.[8]

2 KEY TRENDS IN FINANCIAL SERVICES

NBFCs have been complementing banks as financial intermediaries by leveraging on their efficient and nimble operations and tailor-made products for niche areas. The need to strengthen their regulation and supervision has come to the fore in view of their rapid expansion in recent years. The Reserve Bank has been striving to harmonies regulatory requirements of various classes of NBFCs while putting in place specific policy measures for particular classes of NBFCs such as core investment companies and legacy NBFCs as needed.

2.1 Government-owned NBFCs

In 2017-18, the Reserve Bank aligned the regulatory requirements of government owned NBFCs with those of privately owned NBFCs. Government-owned NBFCs will have to adhere to all regulations on income recognition, provisioning norms, corporate governance, and conduct of business regulations, deposit directions and reserve funds by 31 March 2019. Asset classification norms have to be complied by 31 March 2020 and capital adequacy, leverage, exposure norms and statutory provisions are to be phased in progressively by 31 March 2022[9].

2.2 Core Investment Companies (CIC)

Core investment companies registered as NBFCs primarily invest in group companies and do not carry out any other NBFC activity. They are required to invest up to 90% of their net assets in equity shares, preference shares, bonds, debentures, debt or loans of group companies, while equity investments in group companies must constitute at least 60% of net assets. To promote infrastructure development through investment in Infrastructure Investment Trusts (InvITs), core investment companies registered with the Reserve Bank as NBFCs were allowed to act as sponsors to InvIT issuances and to reckon holdings of InvIT units as part of the sub-limit of 60% for equity investments in group companies. Exposures of core investment companies to InvITs are limited to their holdings as sponsors[10].

2.3 Consumer Protection – Ombudsman Scheme

The banking ombudsman scheme is a cost-free apex mechanism for expeditious resolution of complaints of bank consumers. On similar lines, the ombudsman scheme for NBFCs was launched by the Reserve Bank under Section 45L of the Reserve Bank of India Act, 1934 with effect from 23 February 2018. To begin with, it has been operationalised for all deposit-taking NBFCs (NBFCs-D). Offices of the NBFC Ombudsman have started functioning from Chennai, Kolkata, Mumbai and New Delhi. Additionally, as the digital mode of financial transactions is gaining traction in the country, a dedicated ombudsman scheme for digital transactions would be implemented going forward[11].

The Ombudsman Scheme for NBFCs-D was extended to eligible NBFCs-ND, with an asset size of INR100 crore or above with customer interface.

2.4 Emergence of new-age digital lenders

The emergence of new-age digital lenders has further intensified the competition for NBFCs in the market. Primarily called FinTech companies, these digital lenders are attempting to gain a share of the lucrative opportunity in the Indian lending market through their mastery of data and technology. These start-ups conduct off-balance sheet and on-balance sheet lending, powered by innovative processes to deliver a captivating customer experience, quick turnaround time, reduced fees and increased transparency.

2.5 Embrace a new attitude to winning over the customer

'Customer is king' has never been truer than it is today. With lenders incorporating technology advances to penetrate underserved markets and differentiate in mature markets, customer expectations have evolved. The proliferation of new entrants with differentiated business models to serve customers is also increasing pressure on existing, incumbent NBFCs to increase customer focus. Customers now demand seamless, personalised, 24X7 interaction across multiple touch-points, customised to their needs. This will require NBFCs to embrace techniques to derive customer insight, such as customer personas and journey maps, enhance their understanding of customer behaviour and subsequently drive-up meaningful outcome.

Winning the customer experience race will require much more than just technology; it also mandates a new attitude to winning the customer. The world over, financial services are experiencing a moment of disruption. Multiple smaller players are working on specific problems in the life insurance value chain — from customer on-boarding and financial planning to customer servicing. These are driving the incumbents to change their conventional way of thinking. These challengers have seen benefit in collaborating with the incumbents rather than trying to upend the business.

2.6 Know Your Customer – Moving from segmentation to micro-segmentation

Personalisation of content has become ever important, especially in a time when customers are bombarded with a plethora of emails and SMS. Statistics show that more than 91% of people unsubscribe to email communications, 44% of direct emails go unopened and 60% opt out of mobile notifications[12]. The primary cause of this remains a glut of unrelated and irrelevant messages, which turn off the customer's interest. When flooded with choice, customers focus only on those products or services that are most relevant to them. NBFCs must adopt a micro-segmentation approach in finding smaller sets of people to whom a specific product, service or a feature of a product could be vital. By incorporating marketing analytics, NBFCs can rapidly, dynamically, at massive scale, mine huge amounts of data, encompassing customer transactions, demographics and interactions as well as with data from external sources. In addition to identifying lucrative micro-segments and probability of purchase, NBFCs will be able to communicate effectively with customers and price loan products better to minimize customer drop-outs. Over time, such tools will also help NBFCs capitalise on opportunities for up-sell, cross-sell and re-sell, thereby, boosting the customer lifetime value.

2.7 Union Budget of India 2020[13]

The Union Budget for 2020 was presented to the parliament on 1 February 2020. The Budget aimed to promote start-ups, benefits to the middle-class tax payers to place money in the hands of people, push to attract foreign capital. Few key features of the Budget were:

Personal Tax

Optional new tax regime for individuals and HUF

- The Budget has proposed a new tax regime with effect from AY 2021-2022. It is optional for taxpayers and provides lower tax rates.

  The Income-tax slab rates applicable under the new tax regime would be:

Slab Rates	Slab Rates
Up to INR 2,50,000	Nil
INR 2,50,001 to INR 5,00,000	5%
INR 5,00,001 to INR 7,50,000	10%
INR 7,50,001 to INR 10,00,000	15%
INR 10,00,001 to INR 12,50,000	20%
INR 12,50,001 to INR 15,00,000	25%
Above 15,00,000	30%

- Surcharge and education cess would apply per existing rates.

Determination of residential status for certain categories of individuals

- A citizen of India would be deemed to be a resident of India in any financial year, if such individual is not liable to tax in any other country.
- Amendment proposed by the budget provides for such an individual to be resident in India in either of the two scenarios –
  - (i) the individual’s stay in India during the financial year is 182 days or more; or
  - (ii) the individual’s stay in India is 120 days or more in the current financial year and 365 days or more in the preceding 4 financial years.
- A resident in India would be considered as not ordinarily resident if the individual has been a non-resident in India in 7 out of 10 preceding financial years.

Corporate Taxation:

Dividend Distribution Tax

- Currently, companies are required to pay DDT on the dividend declared/distributed/paid to shareholders at the rate of 15% plus applicable surcharge and cess.
- The Budget now proposes to abolish DDT for dividends declared, distributed or paid on or after 1 April 2020.Consequently, dividends will be subjected to tax in the hands of the shareholders in all cases.
- It is also proposed that interest expenditure be allowed as deduction from dividend income, subject to a cap of 20% of such income.
- The Budget also proposes to eliminate the cascading tax effect in case of inter-corporate dividends by providing a deduction in respect of dividends received by a domestic company to the extent such dividend is distributed.
- Such deduction shall be allowed only if the dividend is distributed by the company at least one month prior to due date of filing of return of income.

Tax Audit limit

- It has been increased from INR1 crore to 5 crores provided the taxpayer has received all the amounts including amount received for sales, turnover or gross receipts in cash, which does not exceed 5% of the total amount and all payments including payments incurred for expenditure in cash does not exceed 5% of the total amount.

Due date for compliances

- Effective AY 2020-2021, it is proposed that the tax audit report be filed one month prior to the due date for filing income tax return.
- Consequential amendments are proposed for reports and certificates for claiming various tax exemptions and deductions.
- The due date for furnishing Accountant's Report in Form No. 3CEB is proposed to be changed from 30 November to 31 October.

Start-ups

- It is proposed to increase the turnover cap for eligible start-ups claiming tax holiday from INR-25 crore to INR 100 crore.
- The window for claiming tax holiday is proposed to be expanded to three consecutive years in a block of 10 years from the current block of seven years.

Business Connection

- In a major expansion of the definition of 'business connection', the Budget proposes to include, within its ambit, the income attributable to the following activities from AY 2021-2022:
    - Advertisements targeted at residents or through an Indian IP address
    - Sale of data collected from a resident or through an Indian IP address
    - Sale of goods/services from data collected from residents or through an Indian IP address.
- It is also proposed to include within the definition of 'Significant Economic Presence', systematic solicitation of business whether from digital means, effective from AY 2022-2023.

International tax proposals

- Currently, royalties exclude any amount paid for sale, distribution or exhibitions of cinematography films. It is now proposed to include such amounts within the purview of royalties.
- Under the existing provisions, fund managers of eligible investment funds (EIFs) do not constitute 'business connection' in India for the EIF. This is subject to conditions, which include a cap of 5% investment by residents in the particular EIF. This condition is proposed to be relaxed, whereby the investment by the fund manager during the first three years not exceeding INR 25 crore shall not be counted for the 5% cap. Further, it is proposed that the minimum fund corpus shall be achieved within a period of 12 months instead of the existing 6 months.
- The Budget proposes to exempt Category I FPIs from the applicability of indirect transfer provisions.
- In alignment with Article 6 of the multilateral instruments (MLI), the budget proposes to deny treaty benefits to all arrangements created for the purpose of tax evasion and avoidance.

Transfer pricing

Income attribution to the permanent establishment (PE) in India

- Under the current regime, it was not clearly provided whether the Advance Pricing Agreement (APA) provisions apply to determine income attributable to PE in India. Further, Safe Harbor Rules (SHR) were not available in such cases.
- From AY 2020-2021, it is proposed that taxpayers can opt for SHR to determine the income attributable to a PE in India (detailed rules are expected to be notified separately).
- It has also been clarified that APA provisions shall also apply to determine income attributable to a PE, in cases of APAs entered into, on or after 1 April 2020.

Goods & Service Tax

- New simplified returns and e-invoicing will be implemented from 1 April 2020.
- There will be an additional window for un-availed transitional input tax credit (ITC) for taxpayers.
- Refunds process has been simplified and fully automated.

- Aadhaar-based verification is being introduced to weed out dummy/non-existent taxpayers.
- There will be an exercise on revisiting the GST rate structure and other tax buoyancy measures.

Custom Law

- Health Cess at the rate of 5% will be levied as duty of customs on import of specified medical equipment.
- Additional measures will be implemented to curb misuse of Free Trade Agreements (FTAs) and Rules of Origin will be revisited.
- Additional safeguard measures on imports will be implemented to protect the domestic industry.
- Electronic credit ledger has been introduced for making duty payment by way of direct duty credit for export and other benefits.
- There has been an upward revision of duty rates across sectors to provide a level playing field for domestic players.

Summary

The Budget has a lot of positive announcements that should give a boost to the economy. rationalising the personal tax regime, lowering individual tax rates, abolishing dividend distribution tax, providing impetus to start-ups, strengthening bond markets and creating an enabling environment for foreign investors and sovereign wealth funds are steps in the right direction.

3. ISSUES & RECOMMENDATIONS

NBFC remains a critical sector and for it to play an important role in development of the economy and it to work as alternative to mainstream banking the following issues will need to be resolved

Streamline Road blocks for efficient operation	Level playing fields with Bank
• Fund raising avenues and prudential ceilings for exposure of banks.	• Participation in priority sector lending
• Refinance mechanism for NBFC	• Emergency Credit Line Guarantee Scheme (ECLGS)
• IND AS Norms	• PCG 2.0 tenure
• Remove barriers to issue credit cards.	• One Time restricting Norms
• Simplification of KYC requirements especially for small ticket loans and micro finance.	• Equivalent treatment in current tax regime
• Consistent regulatory environment to make compliance cost effective	• Limited or need-based participation in the payment and settlement system
• Credit rating	• Exemption for NBFCs from the restrictions imposed on opening of current accounts by banks

3.1 Fund raising avenues and prudential ceilings for exposure of banks to NBFCs

NBFC's raise around 70 percent of their resources from bank borrowings and debentures. With the increased turmoil in the financial markets and investor confidence low on this sector raising money through debentures have become costlier. NBFCs face a higher cost of borrowings, which is eventually passed on to their borrowers in the form of higher interest on loans. It increases delinquencies and reduces profit margin, which affects their credit rating with the banks in turn. It becomes a vicious circle as with a low credit rating, cost of funds goes up further.

Under the "Large Exposures Framework (LEF)" circular issued in June 2019, bank exposures to a single NBFC is restricted to 15 percent of their available eligible capital base, while general single counterparty exposure limit is 20 percent, which can be extended to 25 percent by banks' Boards under exceptional circumstances.[14]

The government has understood to some extent the issue and on its part taking steps to increase liquidity in the NBFC sector, which was hit after default by IL&FS Group.

- It increased loan exposure limit of banks to a single NBFC (excluding gold loan companies) from 15% to 20% of its capital base in September 2019[15].
- The government amended the Companies (Share Capital and Debentures) Rules by removing Debenture Redemption Reserve (DRR) requirement for NBFCs.
- End use restrictions relating to external commercial borrowings were relaxed for eligible borrowers.

While government has been actively working towards resolving liquidity issues of NBFC's EBG Federation recommends

- given the strong reliance of NBFC's on the banks for meeting their funding requirements government to further relax ceiling imposed on banks to provide finance to them.
- RBI should grant systematically Important Non-deposit taking NBFCs (Asset Size 500 Cr or above) deposit taking licenses upon their request and appropriate credentials underscoring their systemic importance in providing credit to geographies and customers where traditional banks still can't reach. This will also reduce their dependency on bank for source of funds and lower the cost of funds, thus enabling NBFC's to provide loans at a competitive rate.
- government should work together with the industry to strengthen and develop bond markets further thus opening an alternative long-term source of funds for NBFC's. Masala bonds, new products like covered bonds could be explored in a healthy bond market providing a reliable long-term cost-efficient fund source.

These measures would encourage the objective of financial inclusion, help mitigate liquidity crisis and bring stability to the NBFC sector, particularly those that catering to the mass market.

3.2 Refinance Mechanism for NBFCs:

The regulatory regime for NBFCs has evolved to a stage where the regulation relating to the assets side of our balance sheet have been harmonised with that for banks. However, on the liability side, NBFCs continue to depend largely on banks. One single default by an NBFC created such a negative sentiment that banks suddenly became very apprehensive and reluctant to lend. This created a liquidity crunch for the sector, which in turn had a multiplier effect on important sectors like automobiles, MSMEs and Consumer goods. Therefore, the need of the hour is to develop funding sources outside the banking system. For this, a refinancing mechanism on the lines of National Housing Bank (which refinances Housing Finance Companies) is the desired solution. Further, MUDRA can play an important role in refinancing a large number of Small and Medium NBFCs.

3.3 IND AS norms:

NBFCs have been mandated to follow IND AS norms on provisioning for credit losses and these provisions are much higher than RBI norms. RBI guidelines on provisioning for restructured accounts require additional provisioning of 10%. IND AS norms require provisioning to be done for credit losses on historical average and own experience of respective lenders and therefore, all accounts are adequately provided for. We, therefore, recommend that the additional provisioning requirement may be dropped for restructured accounts for NBFCs.

3.4 One-time restructuring norms:

Currently guidelines on onetime restructuring prescribe the customer account to be in 0- 30 bucket as on the date but exclude standard accounts in 31-90 bucket. Given that the micro & small enterprises have uneven cash flows and even prior to COVID-19, were having viability issues, we seek your consideration of this scheme for all the standard accounts in 0-90 bucket so that the wider spectrum of customers can benefit from it.

3.5 Emergency Credit Line Guarantee Scheme (ECLGS):

NBFCs raise funding from the banks by assigning the receivables from the existing loan contracts and these loans are then transferred to the banks while servicing is continued to be done by the NBFCs which have originated the loans. Banks don't have reach to these customers and under the current guidelines, NBFCs can't provide loans to these customers and banks are unable to provide. We, therefore, request that NBFCs be permitted to provide loans under ECLGS to its own customers whose contracts have been assigned by it for the purpose of raising funding resources from the banks.

3.6 PCG 2.0 tenure:

The guarantee under PCG 2.0 @ 20% is limited to 18 months and as a result, banks are giving loans to NBFCs repayable entirely in 18 months whereas NBFCs are giving loans to their customers for 36-48 months. It also results in ALM mismatch for the NBFCs creating liquidity stress. We, therefore, suggest increasing the tenure of guarantee under PCG 2.0 to 36 months to encourage the banks to lend for 36 months.

3.7 Exemption for NBFCs from the restrictions imposed on opening of current accounts by banks: NBFCs and HFCs have various current accounts with banks-based on the bank of the customer for which they have NACH/ECS mandates. Such banks may or may not have CC/OD facility extended to such NBFC/HFC. Pursuant to the Circular, these current accounts will need to be closed. The requirement to route all transactions through CC/OD Account would mean that all amounts collected from its borrowers and all loan amounts disbursed have to be routed through the CC/OD account. This change will make tracking of business-wise collections and disbursals difficult for financial institutions.

3.8 Credit Rating: Should not be an "Eligibility" Criteria for funding: All the measures announced to date have a minimum prescribed credit rating as an eligibility criterion. Any NBFC, which does not have the minimum prescribed rating is "not eligible" to take benefit. Credit rating is just a view, which is the norm globally. However, when it comes to funding of NBFCs, it is unfortunate that credit rating is used as an eligibility criterion

3.9 Barriers to issue of credit cards by NBFCs

Lobby Group Payments Council of India (PCI) has recommended the Reserve Bank of India's (RBI) Committee on Deepening of Digital Payments (CDDP) to permit non-banking financial companies (NBFCs) to issue physical or digital credit cards. This suggestion was made with the intention to speed up the growth of the digital payment's ecosystem in the country.

The credit card is one of the most important tools to develop India's digital payments and hence PCI council is betting big on the credit card issuance framework by NBFCs. According to RBI's statistics although the credit bureau has over 400 million customer records while about 40 million credit cards have been issued so far, the market for credit card growth remains untapped.

Clearly, the credit cards market is significantly under-penetrated and one of the key reasons is the constrained universe of issuers that currently only comprises of banks (on automatic route). NBFCs are practically constrained from the credit card market on account of high access barriers, both for the issuance of "general" credit cards and co-branded cards such as having net owned funds worth INR 100 crore, other restrictions etc. Furthermore, they are altogether foreclosed from issuing variants of other cards like charge cards, debit cards, and stored value cards.

In recent years, NBFCs have performed exceedingly well with respect to credit deployment. By leveraging technology, they have augmented their distribution powers to serve otherwise under-supplied segments thereby facilitating government's agenda of digitisation. Through this initiative, NBFCs will be able to tap differentiated segment of prospective credit seekers who are new to the credit market thereby bring more and more people under formal economy.

Given the strong government focus on digitisation and financial inclusion, EBG Federation recommends entry barriers for NBFCs to enter this segment be softened.

3.10 Simplification of KYC requirements especially for small ticket loans and micro finance

In COVID-19 situation, online instant and paperless KYC should be allowed for NBFC and additionally NBFCs should be allowed to rely upon the KYC checks carried out by the customers' bank: Since almost all NBFC customers have bank accounts (and since their KYC would have been done by the bank while opening the account)

- Getting details and evidence of such bank account and maintaining the record of such account should be made sufficient compliance of the KYC requirements under the PMLA Act.
- In the longer run, development of a KYC repository (similar to the NSDL acting on behalf of mutual funds) could be developed for banks and NBFCs to rely upon for KYC checks.
- Current laws and regulations require same amount of effort for performing due diligence and KYC on the customers irrespective of ticket size of the loan. While the EBG Federation fully supports the intent of the government in ensuring maximum transparency in the eco-system, however, for NBFIs, which are in retail lending space especially in low ticket loans, this is quite onerous as a lot of their customers are from low income group (and may not even have PAN cards), which in effect supports the financial inclusion agenda of the government by including the underserved sections of the society. Further, unlike high ticket mortgage loans which entail a longer loan processing time and multiple verifications, for small ticket loans, a quicker processing time helps these organisations to keep their costs low and enable them to pass the benefit to the customers.

3.11 Consistent regulatory environment to make compliance cost effective

The regulatory regime for NBFCs is lighter and different in many respects from that for the banks. The steady increase in bank credit to NBFCs over recent years means that risks are being transferred from the more lightly regulated NBFC sector to the banking sector in India. RBI's given the defaults in the industry has been trying to introduce various measures to regulate NBFC's. Frequent and numerous changes lead to an ambiguous regulatory environment and discourages NBFCs to innovate. Further, certain initiatives although taken with the right objective, like Central KYC (CKYC) have not had the desired impact and has led to the increased cost of compliance, which ultimately leads to the increased cost of lending. The government is further setting up rules for data protection, which is an important move but it should also take into consideration practical difficulties and business impact to strike a correct balance between protection of rights and business hindrances. Certain recommendation on Personal Data Protection Bill, 2019 are as follows:

- <u>Reasonable time for implementation of the Bill:</u> Proper planning with adequate timelines for implementation of the PDP Bill shall yield desired results preventing contraventions by various data fiduciaries. It is recommended to provide for a comprehensive timeline relation to compliance of each provision under this Bill.
- <u>Tax holiday to financial institutions</u> for putting in place the infrastructure in compliance with the Bill.
- <u>Treatment of data obtained by an organisation from external sources for processing the loan:</u> It is recommended to allow the data fiduciary to have access to the data of the data principal from the external sources and that the data fiduciaries shall be made responsible for the loss caused to the data processors.
- <u>Restriction on cross border processing (in particular, storing) of sensitive personal data outside India shall be removed</u> : It is recommended that the prohibition on processing (in particular, storing) of sensitive personal data outside India shall be removed and

proper guidelines shall be issued by the regulator with regards to audit and alternatively, an inspection of such data so that such data can be managed by data fiduciary even over cloud space, which shall be available at manageable cost and reduced operational risk.

EBG Federation further recommends the regulatory environment should be consistent and its compliance cost-effective to ensure viability of business.

3.12 Participation in Priority Sector Lending (PSL)

India's approach to financial inclusion has been multi-pronged. One of its major corner-stones is the presence of stipulations on "priority sector lending" by the commercial banks. For this purpose, priority sector includes the following categories, viz., agriculture; micro, small and medium enterprises; export credit; education; housing; social infrastructure; renewable energy; and others (like weaker section of the community). Indian commercial banks are required to lend 40% of their credit to the priority sector.

Priority sector credit accelerated in 2018-19, largely driven by a recovery in credit to agriculture and housing. Pradhan Mantri Awas Yojana (PMAY), coupled with the Reserve Bank's June 2018 initiative to expand the eligibility of housing loan limits for priority sector lending enabled a sharp jump in housing loan growth from 0.7% in 2017-18 to 24.9% in 2018-19[16].

On 13 August 2019 the Reserve Bank allowed bank credit to registered NBFCs (other than micro finance institutions (MFIs)) for on lending to agriculture and micro and small enterprises (MSEs) to be treated as priority sector lending, subject to certain restrictions. Only fresh loans sanctioned by NBFCs can be classified as priority sector lending by the banks. On-lending by NBFCs for term-lending component under agriculture will be allowed up to INR10 lakhs per borrower and up to INR20 lakhs per borrower to micro and small enterprises. EBG Federation recommends to greater inclusion of NBFC's in lending to priority sectors.

An important development during 2016-17 was the operationalisation of the Priority Sector Lending Certificates (PSLCs) scheme in April 2016.The Reserve Bank has provided a platform to enable trading in PSLCs through its core banking solution (CBS) portal (e-Kuber). The total trading volume of the Priority Sector Lending Certificates (PSLC) platform introduced above to allow market mechanism to drive priority sector lending by leveraging the comparative strength of different banks – grew by 78% in 2019. [7]

EBG Federation strongly recommends including NBFCs in this initiative if they get inexpensive funds from the banks to pass on the benefit to lowest end of the spectrum. This will not only aid the banks in meeting their targets but also can help reach out to such low end of the borrower pyramid and manage the risk associated with such direct lending.

3.13 Issues arising from present corporate income-tax regime

3.13.1 Tax deduction for provisions for bad and doubtful debts

Under the existing provisions u/s 36(1)(viia) in the I.T. Act, a provision for bad and doubtful debts made by banks and FIs is allowed as a deduction to the extent of 7.5% from the gross total income. Alternatively, such banks and FIs have been given an option to claim a deduction in respect of any provision made for assets classified by the RBI as doubtful assets or loss assets to the extent of 10% of such assets. The Budget 2017-18 in a welcome move extended this benefit to NBFCs as well, however, the limit was capped at 5%, which needs to be looked into.

3.13.2 Treatment of Special Reserves under section 115JB of the Income-tax Act

NBFCs are statutorily required to transfer certain amount towards special reserve, debenture redemption reserve, create provision towards Non- Performing Assets (NPAs), diminution in the value of investments, etc., in accordance with the directions issued by RBI. However, the amount transferred towards these statutory reserves and provisions are required to be added back to the profits per profit and loss account, as part of the adjustments required under Section 115JB of the Act. This translates into a higher tax being paid by NBFCs even though they are mandatorily required to create reserves/ provisions per the RBI directions. Thus, there is a case for the government to consider allowing NBFCs to claim deduction towards creation of such reserves/ provisions under Section 115JB of the Act.

3.13.3 Relaxation under section 194A of the Income-tax Act

Section 194A of the Income Tax Act provides for deduction of tax at source (“TDS”) at the rate of 10% on payment of interest (excluding interest on securities) to a resident. Sub-section 3 of Sec. 194A provides for non-applicability of Sec. 194A in some cases, which include banking companies to, which Banking Regulation Act applies. However, such exemption has not been extended to NBFCs.

Since NBFCs are supplementing the banks and these entities are also regulated by the Reserve Bank of India, EBG Federation recommends that these NBFCs should be treated at par with banks and the benefit of ‘Nil TDS’ should be extended to them as well.

3.13.4 Thin capitalisation rules under Section 94B of the I.T. Act may impede NBFC operations

Section 94B, which was introduced from April-17 states that where an Indian company, or a permanent establishment of a foreign company in India, being the borrower, incurs any expenditure by way of interest or of similar nature exceeding one crore rupees, which is deductible in computing income chargeable under the head "Profits and gains of business or profession" in respect of any debt issued by a non-resident, being an associated enterprise of such borrower, the interest shall not be deductible in computation of income under the said head to the extent that it arises from excess interest, as specified in sub-section (2).

The amendment was brought in the light of cross-border transaction where the profit is shifted to a lower tax jurisdiction, and the money is remitted in the form of a loan. The interests on the loans are then claimed as an expense and thereby, lowering the company’s tax burden. However, as the status stands today, banks and insurance companies have been exempted from the provisions of this section but NBFCs haven’t been included in the exemption list. This places NFBC’s at a disadvantageous position and the hardship results in restricting the growth of NBFC’s especially who are in initial years of their business or not able to get funding from local banks at reasonable rate of interest due to any reason.

While the government has taken steps to bring parity between banks and NBFCs on the regulatory aspects, EBG Federation strongly recommends that NBFCs be also included in exemption list to create a level playing field.

3.14 Limited or need-based participation in the Payment and Settlement System.

The government has been strongly driving e payments and there has been strong growth in these. RBI has played a pivotal role in facilitating e-payments by making it compulsory for banks to route high value transactions through Real Time Gross Settlement (RTGS) and by introducing NEFT (National Electronic Funds Transfer) and NECS (National Electronic Clearing Services), which has encouraged individuals and businesses to switch to electronic payments. The Reserve Bank of India (RBI), under powers from the Payment and Settlement Systems Act, 2007, has endeavoured to ensure that India has ‘state-of-the-art’ payment and settlement systems that are not just safe and secure, but are also efficient, fast and affordable.

RBI can make the settlement process more inclusive and broader in approach can look to include NBFC’s in settlement process because of the nature of activities done by NBFCs, NBFCs extensively use payment and settlement system to carry out various transactions. It will ensure a level playing field if NBFCs can participate in the payment system on a limited basis to facilitate payment of at least their own customers.

CONCLUSION

The COVID-19 pandemic has presented Financial Sector especially NBFC sector with mammoth challenge of survival, sustain and growth. The government has been very nimble is recognising the challenges and responded swiftly with various support measures but lot more needs to be done to make sure that sector sail through these uncertain times as its crucial for whole Indian economic Engine. Although the balance sheet size of the NBFCs constitutes 18.6% of SCBs, it has emerged as an important pillar of the Indian financial system. The sector, which had witnessed a robust expansion in 2017-18, experienced headwinds in 2018-19 and 2019- 20 (up to September) as market sentiments turned negative post-IL&FS event and recent defaults by some companies. The Reserve Bank and the government have taken several measures to restore stability in the NBFC space NBFCs have been complementing banks as financial intermediaries by leveraging on their efficient and nimble operations and tailor-made products for niche areas. Rising customer expectations and the proliferation of digital business models have accelerated the need for existing NBFC incumbents to transform their operations, while forcing new NBFC entrants to rethink their entry strategy. With recent events increasing the scrutiny on NBFCs and their operations, it is imperative for players to build robust risk and governance models as they grow their businesses.

The role of NBFC's in facilitating inclusive growth has been recognised by all and an important building block in the building India's dream of US$5 trillion economy dream. NBFC's beside government support should look at ways at leveraging technology to optimise operating costs and provide new offering to tap new markets, these will help them give impetus and rise from the current scenario.

GLOSSARY OF TERMS

AUM	:	Assets Under Management
EBG	:	The European Business Group
EU	:	European Union
FDI	:	Foreign Direct Investment
FIs	:	Financial Institutions
FPIs	:	Foreign Portfolio Investors
FS	:	Financial Services
GST	:	The Goods & Services Tax
HFCs	:	Housing Finance Companies
HNWIs	:	High Net Worth Individuals
IBC	:	The Insolvency and Bankruptcy Code, 2016
ICAI	:	The Institute of Chartered Accountants of India
IMPS	:	Immediate Payment Service
IPOs	:	Initial Public Offer
KYC	:	Know Your Customer
MAT	:	Minimum Alternative Tax
MFs	:	Mutual Funds
MNCs	:	Multinational companies
MSME	:	Micro Small and Medium Enterprise
NBFC AFC	:	NBFC Asset Financing Companies
NBFC IFC	:	NBFC Infrastructure Finance Companies
NBFCs	:	Non-Banking Financial Companies
NBFCs D	:	Deposit taking NBFCs
NBFCs ND	:	Non- Deposit taking NBFCs
NBFC-MFIs	:	NBFC – Micro Finance Institutions
NBFC-P2P	:	NBFC – Peer to Peer Lending Platform
NPAs	:	Non-performing Assets
NSE	:	National Stock Exchange
P2P	:	Peer to Peer
RBI	:	The Reserve Bank of India
RERA	:	The Real Estate (Regulation and Development) Act, 2016
SEBI	:	The Securities Exchange Board of India
UIDAI	:	The Unique Identification Authority of India
UNCTAD	:	The United Nations Conference on Trade and Development
UPI	:	Unified Payments Interface

ENDNOTE

1. Report on Trend and Progress of Banking in India 2018-19 – Reserve Bank of India
2. Emerging technologies disrupting the financial sector – Assocham May 2019
3. Report on Trend and Progress of Banking in India 2018-19 – Reserve Bank of India
4. India brand equity foundation - https://www.ibef.org/industry/insurance-sector-india.aspx
5. Association of Mutual Funds of India - https://www.amfiindia.com/indian-mutual
6. Mutual Funds performance evaluation in India - http://www.journalcra.com/sites/default/files/issue-pdf/34098.pdf
7. Report on Trend and Progress of Banking in India 2018-19 – Reserve Bank of India
8. RBI/FIDD/2020-21/72 Master Directions FIDD.CO.Plan.BC.5/04.09.01/2020-21 – Reserve Bank of India
9. Report on Trend and Progress of Banking in India 2017-18 - www.rbi.org.in
10. Report on Trend and Progress of Banking in India 2017-18 - www.rbi.org.in
11. Report on Trend and Progress of Banking in India 2018-19 - www.rbi.org.in
12. Guidelines for messaging consumers, kahuna.com, September 2018
13. Government of India - Finance Bill 2020 - https://www.indiabudget.gov.in/doc/Finance_Bill.pdf
14. DBR.No.BP.BC.43/21.01.003/2018-19 dated June 03, 2019 on “Large Exposures Framework (LEF) issued by RBI
15. BI/2019-20/60 DBR.No.BP.BC.18/21.01.003/2019-20 dated 12 September 2019 issued by RBI
16. Report on trend and progress of banking in India -2018 -19 issued by RBI June 2019

FMCG

Acknowledgements: Dev Bajpai, Chairman & Suchana Mukherjee (Hindustan Unilever), FMCG Sector Committee & its Members
Knowledge Partner: Sumeet Hemkar, Sahil Gupta and Kunal Arora – Deloitte Touche Tohmatsu India LLP

EXECUTIVE SUMMARY

This paper analyses the opportunities and challenges in the Fast Moving Consumer Goods (FMCG) sector, one of the largest sectors of the Indian economy. The sector is broadly divided in the following categories – foods and beverages, health care, and household and personal care products. The urban and rural segmentation of revenues in the sector is at 55% and 45% respectively.

The sector is expected to grow at a compounded annual growth rate (CAGR) of 25.44%, with an anticipated turnover of US$103.7 billion (€91.16 billion) by FY2021. With the advent of COVID-19 in FY2021, sales volumes are down by 24.4% year-on-year in quarter 1 of FY2021 as compared to a fall of 7.7% in quarter 4 of FY2020. However, the sector is expected to recover in FY2021, anticipating an increase in rural demand.

Growing awareness, easier access, and changing lifestyles are key drivers of growth for the consumer market, with the policies of the Government of India providing time to time impetus. Some such policy measures include relaxation of licensing rules, approval of 51% and 100% foreign direct investment (FDI) in multi-brand retail and single-brand retail respectively, focus on physical, social and digital infrastructure announced under the Union Budget 2020, and numerous draft regulations/amendments to existing regulations. These measures are driving growth in packaged food, dairy products and food processing segments.

The economic parameters have been significantly impacted by the outbreak of COVID-19. While governments across the globe including in India have taken significant steps, the lockdowns and social distancing mandates have negatively impacted consumption trends. Essentials (staples, packaged food, home and hygiene products) have been less impacted, while economic concerns have reduced spending on discretionary goods like confectionary and appliances. Social distancing has accelerated adoption of e-commerce and consumers continue to embrace digital platforms for a variety of needs. The ability of companies in FMCG sector to digitalise fast and optimise the use of data analytics and improve customer experience would create the big differentiators in the industry.

Besides the opportunities, the paper also discusses the challenges faced by players in the sector and ideates on recommendations to resolve such challenges. Such challenges, inter alia are the newly introduced/amended legislations such as Consumer Protection Act, 2019, under which advertising is sought to be regulated by the government draft e-commerce policy, parallel imports and counterfeits, availability of fake/IPR infringing products, issues in the goods and services tax (GST) regime such as lack of sufficient budgetary support for units located in specific states in comparison to the erstwhile indirect tax law, lack of clarity about formulating modalities for passing on the benefits of reduced rates and input tax credit to consumers even when the manufacturer has passed on all the benefit of the above to the value chain and, through the value chain, to the consumers. The paper also discusses some unique tax and regulatory changes impacting the sector.

In the above backdrop, the paper concludes that if the issues discussed in the paper are resolved, the FMCG sector should chart a strong growth trajectory over the next five years.

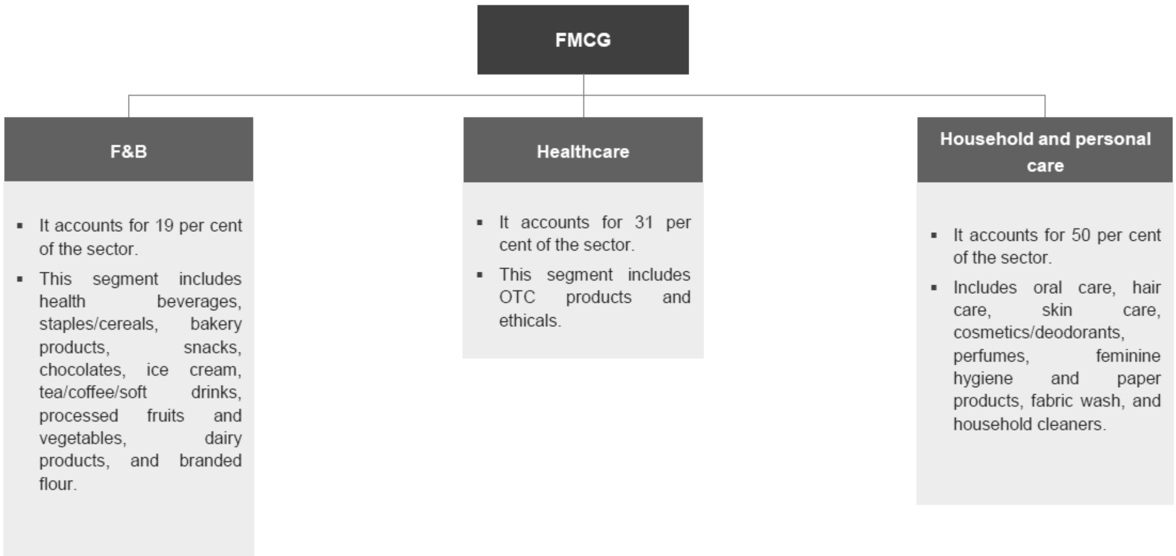
1. INTRODUCTION

Market Description

The FMCG sector is the fourth-largest sector in the Indian economy, generating revenues that is expected to touch US$103.7 billion (€91.16 billion) by FY2021. The sector is expected to post a CAGR of 25.44% in revenues.

Despite certain inherent challenges, the Indian retail landscape continues to remain dynamic. India's twin growth engines i.e., economic liberalisation and demographic profile, set it apart from other nations and present a convincing business case for global retailers seeking to enter the market. Indeed, it is expected that India would be the third-largest consumption economy in the world by 2025.

The FMCG sector can be broadly segmented as follows:



Source: India Brand Equity Foundation, August 2020

Notes: OTC is over the counter products; ethical are a range of pharma products.

Within the sector, household and personal care segment is the leader with almost 50% of the overall market, while healthcare at 31% and food & beverages at 19% come next in the market share. Growing awareness, easier access, and changing lifestyles have been the key growth drivers for the sector.

The market reach of the FMCG sector has been growing significantly both in urban and rural India. While the urban segment is the larger contributor with around 55% of total revenues, the rural segment is rapidly catching up and currently contributes around 45% of total revenues. The size of the rural segment is expected to cross US$220 billion (€193.40 billion) by 2025. Notably, FMCG products account for close to 50% of total rural spending. It is expected that the rate of growth of rural segment is between 1.5 and 1.7 times above the rate of the urban segment.

2. INDUSTRY TRENDS AND MARKET OUTLOOK

The FMCG sector has grown at an annual average of about 11% over the last decade. However, the overall sector growth has shown a decline as can been seen from the latest trends. The sector has seen a fall in sales volumes during FY2020 and in quarter 1 of FY2021. This is particularly because of economic uncertainty due to COVID-19 and heightened volatility in crude and currency. The beauty and personal care category have been the worst hit with growth falling to low single digits in 2019 due to a fall in consumption of discretionary spend-driven products such as skincare, haircare, etc. However, this segment is now leading the growth in the sector since June 2020 as demand starts to pick up after COVID-19 induced lockdowns start getting relaxed and normal activity resumes.

Another factor contributing to degrowth is the high volatility in crude and currency. Crude is the main raw material and any fluctuation in its prices directly hits the middle line of the sector. Other non-crude raw materials such as palm oil or palm fatty oils have seen import restrictions which drove up the domestic inflation.

However, industry analysts estimate a recovery in FY2021 to 11-12% from the lows of 8-9% in FY2020. This expected recovery is being attributed to growth in agriculture GDP.

While the growth in traditional FMCG revenues declined in 2019, sales on e-commerce platforms have helped stabilise the sector's growth, thanks to deep discounts and attractive consumer schemes offered by online retailers. E-commerce portals are expected to play a key role for companies trying to enter the hinterlands. The internet has contributed in a big way, facilitating cheaper and more convenient means to increase the reach of a business. Internet users in India are likely to grow to 850 million by 2025. Presently, India is the second-largest online market, with over 560 million internet users, ranked only behind China. The online sales of FMCG products is approximately US$1.2 billion (€1.05 billion), which contributes to 2% of the total FMCG sales. This percentage is expected to grow to 5% by 2022. Digital influence is relevant for both mass and premium brands. Magnitude and shape of digital influence varies significantly based on 'intent' of consumption and 'degree' of category penetration. Interestingly, market leaders in offline are not necessarily the leaders in the digital space and vice versa.

3. MARKET OPPORTUNITIES

3.1 Policy and Regulatory Framework

- Industrial license is not required for almost all food and agro-processing industries, barring certain items such as beer, potable alcohol and wines, cane sugar, and hydrogenated animal fats and oils as well as items reserved for exclusive manufacture in the small-scale sector.
- The Government of India recognises food processing and agro industries as priority sectors (for lending purposes). It also provides subsidies and incentives to cold storage chains to enable optimal utilisation of food produce in India by minimising wastages. In her speech while presenting the Union Budget 2020, the Finance Minister (FM) laid down 16 action points to improve agriculture, irrigation and rural development, setting aside an amount of INR 2,830 billion (€33.58 billion). There is increased attention expected to outlay on infrastructure and on building a data driven economy. Implementing these steps should positively impact the growth of the FMCG sector by contributing to the physical, social and digital infrastructure.
- Food Security Bill would reduce prices of food grains for below poverty line (BPL) households, allowing them to spend resources on other goods and services, including FMCG products. This, along with direct cash transfer subsidies are expected to trigger higher consumption spends, particularly in rural India, which is an important market for most FMCG companies.
- Under the Union Budget 2020-21, an optional alternative tax regime has been introduced for individual taxpayers. Under this alternative tax regime, most tax exemptions and deductions cannot be claimed by an individual taxpayer. Taxpayers can choose to either continue paying taxes according to higher slab rates and claim deductions and exemptions as they exist at present, or switch to the new regime. This is likely to help taxpayers at different income levels optimise their net tax liability, taking into consideration their needs and capacity to invest in scheduled saving and investment instruments and will increase the disposable income available with them.
- The Government of India also approved 51% FDI in multi-brand retail trade, 100% FDI in single-brand retail trade. Recently, the government also relaxed sourcing requirements for single-brand retail trade and issued clarifications in respect of contract manufacturing further enabling investments into the Indian market. These measures will continue to boost the nascent organised retail market in the country.

3.2 Sectorial opportunities in FMCG Industry

Major sectorial opportunities for FMCG sector are highlighted below:

- Packaged food: About 10-12% of output processed is consumed in packaged form, thus highlighting the huge potential for expansion of this industry. The food packaging industry is India's fifth-largest with a current worth of nearly US $40 billion (€35 billion). A survey conducted by the Associated Chambers of Commerce of India (ASSOCHAM) revealed that 82% of the workforce, in some of the key metros, prefers packaged food compared to eating outside food or at road-side eateries. Additionally, hygiene concerns have driven a shift towards packaged products in areas such as paneer, cheese and processed meat and seafood, with a shift towards packaged paneer and ghee. The Indian packaged food market is forecasted to see a strong growth by increasing product availability as a result of manufacturers' new product developments and greater penetration of smaller cities and rural areas. The consumption slowdown appears to have not impacted the packaged food segment like other FMCG segments and sales have remained strong during 2020.

- Dairy products: India is the largest milk producer in the world accounting for 20% of the global market share. Since the consumption is growing, many foreign companies are entering India with a variety of dairy products. However, there is scope for growth for other players as value added products (butter, curd, paneer, ghee, yogurt, etc.) form only 15% to 20% of the total dairy production. Considering the higher purchasing power, higher awareness and preference for tertiary processed milk products coupled with low availability, there is an opportunity to grow the spending in this category. India's demand for milk and milk products is increasing twice as fast as the production of milk. The dairy market in India reached a value of INR10,527 billion (€125.97 billion) in 2019. The market is also witnessing a consumer shift towards healthier products such as ultra-high temperature processing (UHT) milk, probiotic drinks and yoghurts, etc. It is projected that the market will reach a value of INR21,971 billion in 2024, exhibiting a CAGR of around 16% during 2020-25. During her speech while presenting the Union Budget 2020, the FM announced facilitation in doubling of milk processing capacity from 53.5 million MT to 108 million MT by 2025. In February 2020, the Union Cabinet approved allocation of INR44.60 billion (€0.53 billion) to dairy farming to improve the competitiveness and productivity of the dairy industry in India.

- Food processing industry: The Indian food processing industry accounts for 32% of the country's total food market, one of the largest industries in India and is ranked second in terms of total food production, production of horticulture crops and production of fish, aquaculture. India is also ranked first in terms of spice production. By 2024, the food processing industry will potentially attract US$33 billion (€29.18 billion) investments and generate employment for 9 million people. Following measures were announced in the Union Budget 2020 for food processing projects:

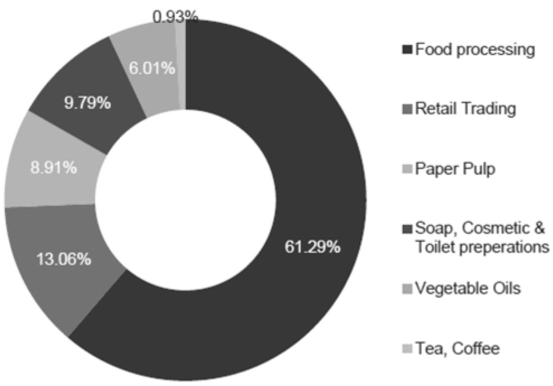
- An exercise to map and geo-tag India's 162 million MT of agri-warehousing, cold storage, reefer van facilities and creation of warehousing in line with Warehouse Development and Regulatory Authority (WDRA) norms.

- Setting up of seamless national cold supply chain for perishables, inclusive of milk, meat and fish through “Kisan Rail” by the Indian Railways - through Public-Private Partnership (PPP) arrangements. There will be refrigerated coaches in Express and Freight trains.

- The government has recognised the importance of start-ups as engines of growth for the economy. Reports forecast that the country's food-tech sector, which is already growing phenomenally, could reach up to US$3.5 billion by 2021 and US$8 billion by 2022. HungerBox, an Indian food tech start-up raised US$12 million (€10.60 million) from Paytm. Curefit, an integrated health and fitness platform raised US$45 million (€39.75 million) from multiple investors. Other such foodtech start-ups which raised funding during 2019 include Biryani by Kilo, Limetray, FreshMenu, Fingerlix, etc.

- The sector witnessed healthy FDI inflows of US$16.28 million during April 2000 – March 2020. Proposals for investment worth US$2.84 million arising from paper pulp, sugar, fermentation, food processing, vegetable oils and vanaspati, soaps, cosmetics and toiletries industries in the FMCG sector were already implemented until December 2019.

Cumulative FDI inflow share – April 2000 to March 2020 (US$ million) is as under:



4. RECENT DEVELOPMENTS

4.1 Consumers have started demanding customised products specifically tailored to their individual tastes and needs. The trend toward mass-customisation of products is expected to intensify further.

4.2 Despite economic slowdown, consumers are willing to spend to buy premium goods at higher prices in the space of convenience, health and wellness.

4.3 Availability of products has become way easier as internet and different channels of sales have made accessibility of desired products to customers more convenient at the required time and place. Online grocery stores and online retail stores like Amazon, Flipkart, Grofers, etc. are making FMCG products more readily available.

4.4 Digital commerce is expected to play a big role in the near future as digitally influenced spend in FMCG is likely to rise to US$45 billion (€39.37 billion). 40 per cent of FMCG consumption to be digitally influenced by 2020. Companies should invest in data driven market and create/shape the digital strategy.

4.5 The volatility in the price of crude and non-crude oils (such as palm oils) in 2019-2020 has left the sector’s cost line largely fluctuating over the year.

4.6 The Consumer Protection Act, 2019 which was enacted on 9 August 2019 to provide for protection of the interests of the consumers and to establish authorities for timely and effective administration and settlement of consumer disputes, has been notified and comes into force from 20 July 2020.

4.7 The government has recently issued draft advertising guidelines for prevention of false or misleading advertisements as well for due diligence to be carried out for endorsements to prevent unfair trade practices and protect consumer’s interest.

4.8 The Central Government has codified the labour laws into 4 Labour Codes – The Code on Wages, The Industrial Relations Code, The Social Security Code and the Occupational Safety, Health and Working Condition Code 2020. All these codes have been notified and their implementation is bound to impact the costs of the FMCG sector.

4.9 Upon receiving industry feedback, the Department of Consumer Affairs has now shared a draft proposal on Decriminalisation of minor offences under Chapter V of The Legal Metrology Act 2009. This amendment seeks to decriminalise minor offences and is in furtherance to the principles of Ease of Doing Business.

4.10 The Taxation Laws (Amendment) Act, 2019 was passed in December 2019 reducing the corporate headline tax rate of existing companies to 22% and to 15% in case of new manufacturing companies, subject to, among other things, the condition that specified tax incentives should not be claimed by the taxpayer company.

4.11 In 2019, the Ministry of Electronics and Information Technology proposed the Personal Data Protection Bill, 2019. This Bill proposes significant responsibilities on the Data Fiduciaries and seeks to establish a Data Protection Authority to ensure adherence to the Rules therein.

4.12 In 2020, the Ministry of Electronics and Information Technology issued a report drafted by committee of experts on Non-

Personal Data Framework which seeks to establish a mechanism towards protection of non-personal data.

5. INDIAN COMPETITIVENESS AND COMPARISON WITH WORLD MARKETS

The following factors can make India a competitive market on the global stage:

5.1 Availability of Raw Materials

Owing to diverse agro-climatic conditions in India, there is a large raw material base suitable for food processing industries. India is the largest producer of spices and cashew and is the second-largest producer of rice, wheat, sugarcane, milk, and fruits and vegetables and one of the largest producers of coconut and livestock. India also produces caustic soda and soda ash, which are required to produce soaps and detergents. The availability of these raw materials gives India the geographical advantage.

5.2 Low-cost Labour Force

Low-cost labour gives India a competitive advantage. India's labour costs consistently rank among the lowest worldwide and are often cited as the country's principal advantage as a manufacturing base. According to the Bureau of Labour Statistics, average labour compensation (including pay, benefits, social insurance, and taxes) in India's organised manufacturing sector has only increased marginally in recent years, from US$0.68 (€0.60) per hour in 1999 to around US$1.50 (€1.33) per hour today. When compared with an average compensation of US$3.00 (€2.65) per hour in China's manufacturing sector (a 20% year-on-year increase fueled by an annual 13% rise in China's minimum wage), India's labour cost advantage places the country in more direct competition with emerging manufacturing jurisdictions such as the Philippines and Vietnam over now-declining China, Thailand, and Malaysia. Many multinational corporations (MNC's) have established their plants in India to outsource for domestic and export markets, because of its wage arbitrage. The impact of Code on Wages Act, 2019 on India's cost advantage remains to be seen.

5.3 Demographic Dividend and Advantage

Demographic dividend: India's abundant labour force is English-speaking, young, skilled, and cost-efficient. The government has initiated Self Employment and Talent Utilisation (SETU) scheme to boost young entrepreneurs. It has invested US$163.73 million (€144.64 million) for this scheme. The government has also launched the Skill India Mission to achieve the vision of 'Skilled India'. It is committed to equipping women with market relevant skills.

Demographic advantage: India is expected to rank amongst the world's top three growth economies and amongst the top three manufacturing destinations by 2020. This is on account of:

- Favourable demographic dividends for the next 2-3 decades. Sustained availability of quality workforce.
- Strong consumerism in the domestic market.
- Strong technical and engineering capabilities backed by top-notch scientific and technical institutes.

5.4 Growing domestic market

As income levels are rising, there is a clear upward trend in the disposable income of people. With the rise in disposable incomes mid-and high-income consumers in urban areas have shifted their purchase trend from essential to premium products. Rapid economic growth provides a large domestic market.

5.5 Infrastructure investment plans

India has seen a rise in investments in infrastructure space both from the government and from international investors. Further, large investments in infrastructure have provided momentum to overall PE/VC investments into India which touched an all-time high where infrastructure recorded US$1.4 billion (€1.24 billion) during October 2019. On lines of 2019, the FM provided an outline of the INR100 trillion National Infrastructure Pipeline (NIP). Union Budget 2020 announced that the Government of India is expected to invest an amount of INR1700 billion (€20.35 billion) in transport infrastructure sector and INR220 billion (€2.63 billion) in power and renewable energy sector. This will help to reduce inefficiencies in the supply chain.

6. KEY ISSUES FACED BY THE INDIAN FMCG INDUSTRY

Some of the key issues and industry recommendations have been listed hereinafter.

6.1 Impact of Government Regulation on Advertisements:

The Consumer Protection Act, 2019 ('The Act') is a welcome step in ensuring a broader, wider and stricter ambit for protecting the consumer interests as well as for establishing authorities for a timely and effective administration and settlement of consumer disputes.

As a progressive move, the Act empowers the establishment of a Central Authority (CA) or the Central Consumer Protection Authority (CCPA) to administer the provisions of the Act and promote, protect, and enforce the rights of consumers.

Focusing on the governance of misleading advertisement, The Act has recommended a framework for adjudication of disputes arising out of misleading advertisements, without providing for a mechanism for such adjudication. This is more concerning where certain adjudications which may require technical expertise have not been considered and addressed in the Act.

In addition to the above, under section 16 of the Act, the District Collector (DC) may on a complaint made to the DC or on a reference made by the CA or a Commissioner of the Regional Office inquire into or investigate complaints on false or misleading advertisements and submit a report to the CA or to the Commissioner of the Regional Office, as the case might be. This may lead to a situation where in the case of an advertiser whose advertisements are telecast across the country, there can be multiple complaints that several DCs across geographies may receive at the same time thus leading to parallel investigations being set into motion.

To address the above issues, the following may be recommended:

- With respect to technical expertise in adjudicating complaint on misleading advertisements, the industry seeks the Ministry to consider a Regulator enforced, Self-Regulation model for advertisement where the efforts of the industry complement those of the CA. Advertising Standards Council of India (ASCI) is such a Self-Regulatory Organisation (SRO) that has been dealing with cases of misleading or false advertising for more than three decades and has a pool of credible experts. Sections 13(3) read with Section 104 (2)(a) of the Act, empowers the CA to appoint experts to assist in the discharge of its functions under the Act. Drawing its powers from these sections, the CA may consider utilising ASCI's expertise as the expert body investigating complaints and giving their findings to the Director General.
- With respect to multiplicity of complaints that may arise out of Section 16, it can be proposed that there should be a mechanism wherein all complaints, irrespective of where they are filed and who receives it, are forwarded to the CA and then, after a preliminary examination, the CA may send it further for investigation either to the Director-General or the Sector Regulator as it may deem fit.

The Ministry of Consumer Affairs has in 2020 released a set of Consumer Protection Rules, to give effect to the Act. Amongst others, **The Central Consumer Protection Authority (Prevention of Misleading Advertisements and Necessary Due Diligence for Endorsement of Advertisements) Guidelines** have been notified to addresses the issue of misleading advertisements and necessary due diligence for endorsement of advertisements**.**

These Guidelines cover a wide range of topics such as puffery, comparative and bait advertising, advertisements targeted at children, expert endorsements, and disclaimers among other topics.

Certain issues and recommendations that need to be highlighted are as follows:

- Definition of Child and advertisements targeted at Children- The definition read with other conditions stipulated in the guidelines are quite restrictive in nature and may cause operational challenges to air/publish advertisements that are otherwise fair and responsible and pose no harm to children.
- The Guidelines tend to restrict advertisements on grounds of accepted

standards of public decency- a term that is both ambiguous and subjective and may not be well articulated at different forums.

- The Guidelines require advertisers to ensure that there is adequate supply of goods or services to meet foreseeable demand generated by such advertisement. The phrase ‘foreseeable demand’ may have several connotations and includes variable factors such as pilot testing, new launch, manufacturing capacities, freight and transportation and so on, thus making it impossible to arrive at a static number that an advertiser can rely on at the time of advertising.
- The proviso to the clause governing ‘Puffery’ is conflicting in nature where it requires evidence to substantiate a puffery, which in ordinary terms is given to understand as an exaggerating claim.
- In furtherance to the recommendation to engage expert bodies like ASCI under the Act, it is pertinent to mention here that, as provided in Clause 15 of the Guidelines, ASCI has the competence and the capability to provide through a separate set of experts, the advertising advice referred to therein to the Endorsers. ASCI can and will at all times ensure that the experts providing advertising advice to Endorsers are separate and distinct from the experts who are called upon to opine on claim substantiation and the adequacy of it which is the subject matter of the complaint against misleading advertisements. ASCI can discharge both the functions and still maintain highest norms of ethics and credibility, which it effectively does even at the present times- where ASCI is concurrently engaged in adjudicating complaints and providing advertising advice.
- A key impediment posed by the Guidelines is with respect to Clauses 16 and 17, where the endorser of any product or service is required to be in use of such product or services so endorsed. Implementation of such a provision seems to be beyond the scope of any advertiser where the endorser may be requested to confirm his belief and use of the product, however there can be no reasonable parameters to judge the preference of the endorser or even to ensure that the endorser is actually using the product.

6.2 Labour Reforms

The government in a progressive move has codified all the 44 labour laws into 4 labour codes. While the Code on Wages has been notified in 2019, the Industrial Relations Code, along with the Social Security Code, and the Occupational Safety, Health and Working Conditions Code have been notified on 29th September 2020. The move taken by the Government of India towards simplification and coding of these laws is a welcome step. While the direction has been paved, the journey ahead requires collaboration and adoption across States.

Some of the key issues and recommendations may be as follows:

- While codification is an attempt to reduce this complexity, the proposed codes fail to bring about significant changes on the ground as the compliance obligations for businesses are not significantly reduced. The essence of codification is an element of consistency- while the Codes rationalise definitions of different terms to a large extent, they are not uniform in all respects. The inconsistent usage of basic concepts like workmen and wage in the code has created further confusion and seems to be one of the reasons why notification of the Central as well as the State rules have not followed close on heels. An expeditious approach towards codification will be critical. Complexity for national players is magnified and a case in point is manner of dealing with Minimum Wages by different States.
- Further, the number and aging of labour cases in India is extremely high. This is clearly a matter of concern for all stakeholders, including judiciary itself. The cases will continue to pile on unless there is a quick judicial reform introduced. The approach taken towards this can be two; one is that of providing dispute redress opportunity at the administrative level, as has been suggested in some of the Labour Codes or by institutionalising an Ombudsman System, with representation of key

stakeholders and two is by decriminalising labour non-compliances and substituting prosecution with compounding for non-repeated non-compliances.

- While the government has invested thoughts on the unorganised workforce and migrants, the need of governance of employment of gig workers, floating workers etc. is important both from employer and employee perspective. This becomes more relevant in the post COVID world that has brought down boundaries across nations and the ability to work on online platforms on projects across the globe is high. It is clearly not a problem of tomorrow; it is a here and now issue. Women constitute 50% of our society however their representation in industry is very low and boosting women representation specially in the manufacturing facilities will play a pivotal role for shaping sustainable talent mix to boost future industrial growth and thus economy. The government must make administrative and legal reforms applicable through centre to all the states/UTs that ease female talent building, sourcing, and deployment in the industry, especially in terms of 3 shift operations (round the clock deployment) for female employees.
- Restrictive and inflexible provisions around working hours, closure etc. are counter -productive to these needs. It is important to revisit the globally recognised labour principles for protection of workmen and creatively carve out win -win solutions for employees and employers. Creation of employment opportunities, especially for local/women/marginalised workforce, needs encouragement through policy incentives and schemes that provide fiscal/non-fiscal support to businesses creating such opportunities.

6.3 The Personal Data Protection Bill, 2019

During her speech while presenting the Union Budget 2020, the Finance Minister made a remark that “Data is the new oil” and went on to describe the way data has changed the way an economy works.

Recently, India has released The Personal Data Protection Bill 2019, which is currently being analysed by a joint parliamentary committee. This Bill seeks to provide for protection of personal data of individuals and create a framework for processing such personal data. The Bill addresses several aspects like consent, purpose limitation, storage limitation and data minimisation while introducing concepts of data fiduciary, data protection authority etc[1]. This Bill is likely to have a significant impact on businesses that use or collect personal data in India, and companies could be fined up to 4% of annual worldwide turnover for non-compliance, and 3-year prison sentences for some violations.

Most FMCG companies handle data of consumers, vendors, employees, shareholders and other stakeholders and therefore, data privacy and data protection are directly linked to the trust, risk and reputation of such companies.

Some of the key issues and recommendations in the Bill are as under:

- A large number of items are required to be informed to the data principal (verbally or through written notice at the time of collection). It is recommended that information required to be notified to the Data Principal must be streamlined so that the most important information stands notified rather than a plethora of information presently requiring notification. This will enable better understanding of why data is being collected and processed and will help in providing an informed consent by the Data Principal.
- Every company has numerous contracts with manufacturers, job work, contractors, distributors, clients, etc. The requirement of taking, recording and storing consents, even in such contractual relationship would only lead to additional and unnecessary cumbersome compliances for the Data Fiduciary and as terms of the data collection and with no real benefit to the Data Principal. It is recommended that a new provision be inserted for a separate independent ground for processing of personal data necessary for performance of contracts/legitimate interest.
- The right to confirmation and access poses significant problems to a Data Fiduciary in implementation. A Data Fiduciary may be working with multiple

data processors and listing all these third-party processors to the Data Principal in one place would be impractical as well as confusing as many of these processors may not be relevant/familiar to the consumer and also pose an increased risk of leakage of trade secrets. It is recommended that this requirement is deleted.

- A Data Fiduciary is obligated to keep the data updated by proactively enquiring from each Data Principal whether the data is accurate, which imposes unnecessary cumbersome compliances. It is recommended that the obligation for provision of accurate/updated data be shifted from data fiduciary to the Data Principal.
- A Significant Data Fiduciary should be so classified basis the sensitivity of the personal data processed and risk of Harm likely to result by virtue of such processing and not by turnover of the enterprise or volume of data collected and processed.
- Several provisions of the Bill refer to regulations to be framed to give effect to the law. Industry should be consulted whilst these draft regulations are being framed.

6.4 Non-personal Data Governance Framework

The Expert Committee constituted by the Ministry of Electronics and Information Technology to study various issues relating to non-personal data submitted its report in July 2020. The Committee observed that non-personal data (NPD) should be regulated to: (i) enable a data sharing framework to tap the economic, social, and public value of such data, and (ii) address concerns of harm arising from the use of such data.

Some key issues and recommendations in relation to the report are as under:

- There are conflicting regulatory roles and overarching definitions- compliance to which can become burdensome for industries.
- There is a need to provide clearer explanations of the differences between the types of NPD. More specifically, it needs to deal with overlaps between the definitions of Community NPD and Private NPD (to the extent collected by Private efforts and investment). This is pertinent to resolve as not doing so would mean unfair recommendations in the framework.
- The Committee has recommended that Private NPD may also include such data in a global dataset that pertains to non-Indians and which is collected in foreign jurisdictions, other than India. Given the requirement for mandatory sharing of metadata by Data Businesses, this recommendation would be seen as overreach of the regulations and the Authority. Global datasets which do not concern Indians should be excluded from the scope of the future regulatory framework.
- A community has been defined as any group of people that are bound by common interests and purposes, and involved in social and/or economic interactions and can be a geographic community, a community by life, livelihood, economic interactions or other social interests and objectives, and/or an entirely virtual community. Given the wide definition of a community, and therefore Community Data, there is a need to sharpen the definition and role of the Data Trustee and the boundaries within which it can perform its role.
- Data Business: With the threshold (quantitatively or qualitatively) for being classified as a Data Business, yet to be defined, there is ambiguity on how the threshold will be understood by individual sector regulators. While some may choose very high thresholds, thereby including only a few of the largest entities, some regulators may keep low qualitative or quantitative thresholds. This could mean many small or medium-sized businesses may be declared as Data Business. Given the onerous and costly compliance requirements mentioned in the report for a Data Business, this would be extremely burdensome on a large number of Indian businesses.
- In the recent past, 4 new Authorities have been proposed for the regulation of the technology sector - the proposed Non-Personal Data Authority (NPDA), the Data Protection

Authority (DPA), the E-Commerce Regulator, and the Central Consumer Protection Authority. This should be reconsidered as it would result in jurisdictional overlaps and might adversely affect the quality of regulation due to costly, slow and, potentially, contradictory oversight.

6.5 Impact of Plastic Waste Management Rules 2016

India is by no means the world's largest plastic polluter, but poor waste management systems make its problem worse than other countries (another reason recycling and collection is ineffective). India produces 26,000 MT of plastic trash daily, which ends up in landfills or on the streets and eventually, spills over into waterways.

Key Issues:

i. National framework on Extended Producer Responsibility:

- PWMR mandates that producers and brand owners operating in more than two states, need to get registered with Central Pollution Control board (CPCB) whereas others can get registered with the State/UT Pollution Control Board (SPCB).
- User industries having pan India operations are accordingly registered with CPCB, who provide yearly EPR collection and escalation targets at a national level to them. The said EPR targets are to be realised by the registered brand owners/producers at a national level from any of the states on the basis of geography, brand and substrate neutrality. As a result, the CPCB registered brand owners/producers are not supposed to register with each SPCB or make EPR plans state wise.
- However, various states/UTs have been setting their own EPR collection targets at a state/UT level, in variance to the central guidelines issued by CPCB. Furthermore, they have been insisting on obtaining SPCB registrations in spite of the fact that multi state operators have to register themselves centrally with CPCB.
- The government (i.e., Ministry of Environment, Forest and Climate Change) released a draft Unified EPR Framework on 23 June, 2020. The involvement of the entire value chain and the ULBs has been reiterated. The concept of Brand & Geography neutrality finds a strong support in the framework as does the need of a National Certification System & Governance. The framework emphasises on the need to have a circular economy, minimised trade barriers & low compliance cost as well as inclusion of waste pickers in waste management mainstream as key to a sustainable framework. MLP as a substrate has been identified for higher EPR obligations.

ii. Need for a single definition of Single Use Plastic (SUP):

- SUP is a big part of this problem — globally, 40% of plastic is used for SUP. The Indian government has time and again announced its commitment to eliminate SUP by 2022. The biggest issue faced by the industry is the ambiguity in the definition of SUP.
- In order to streamline the action plan against SUP across India, the Central Ministry of Environment, Forests and Climate Change (MoEFCC) has issued Standard Guidelines on SUP, vide its letter 172/2001/HSMD dated 6 September 2019 giving adequate illustrations of what may be considered as SUP in general parlance i.e., single use throwaway plastics. An indicative list of items has been provided for consideration by State/UT authorities to phase out plastic carry bags, plastic cutlery, thermocol, plastic flags etc. The guidelines made specific reference to the Multi-layered packaging and PET/PETE bottles as an exception since there is no sustainable alternatives and the user industry is obligated to undertake onerous Extended

Producers Responsibility (EPR) for the allied waste collection and processing, as defined under Plastic Waste Management Rules 2016 (“PWMR”). MoEFCC under Swachh Bharat Mission has issued similar advisory to all states on 11.09.2019 on implementation of phase out of SUP/packaging mentioned in the guideline.

- However, states/UTs (for e.g. Tamil Nadu, Chandigarh, Andaman and Nicobar) have been making their own guidelines and regulations around what constitutes SUP/restricted packaging and thus eligible for ban and/or phase out, and the same is in non-conformance to the MoEFCC/Central guidelines and definition of SUP. Furthermore, said ill-informed bans are being mandatorily enforced on manufacturing producers and brand owners.

Following are some of the key recommendations:

- MLP being the most efficient way of packaging, the focus needs to be on deploying practical solutions of segregation and disposal of plastic waste rather than a complete ban or phasing of MLP packaging as proposed. In all developed jurisdictions of Europe and in the USA, there is no ban prescribed for MLP packaging. Instead, the focus is on efficient ways of disposal through the principle of EPR.
- Nationwide implementation of the Unified EPR Framework as against a state level program on EPR.
- Higher EPR obligations should be imposed on substrates that are non-recyclable without any cross subsidisation across substrate types.
- Usage of recyclable plastics (which can be transformed into a new product or raw material for producing new products) or biodegradable/compostable plastics shall attract 50% lower EPR obligation.
- Incentivisation of Post-Consumer Resin (PCR) usage, Refuse Derived Fuel (RDF) usage, EOL Treatment methodology promoting circular economy, mechanism for making the framework mandatory & not optional at the state level.
- Defining the scope and timelines for activating the National Digital platform & creation of an inter-departmental forum to coordinate actions on PWM and SWM rules.
- Creation of an inter-ministerial (MoEFCC, Ministry of Chemicals & Fertilisers, Ministry of Petroleum & Natural Gas, Ministry of Food Processing Industries, Ministry of Health & Family Welfare Ministry of Drinking Water & Sanitation, Ministry of Housing & Urban Affairs) forum to coordinate actions on PWM.
- Develop common central guidance on Single Use Plastic (‘SUP’): Aim behind issuance of central guidelines on SUP was to ensure congruence of uniform efforts and harmony amongst plastic notifications issued by different states and UTs. However, including plastic packaging types within the scope of various state/UT bans, which otherwise are not part of central guidelines of banned or restricted packaging, would mean defeating the entire purpose of issuing the central guidelines in the first place. It would completely be in non-conformance to the spirit of the centrally published guidelines so far. The effect of state/UT notification is on entities which have operations in multiple states. As a result, divergent state specific regulations have the potential of posing regulatory risk to business continuity of industries, leading to disharmony, inconsistency and ambiguity in addressing plastic waste.

6.6 Legal Metrology Act, 2009 and Legal Metrology (Packaged Commodities) Rules, 2011 (the PC Rules)

The Legal Metrology Act, 2009 was enacted to standardise weights and measures in trade and commerce and to keep up with the advancement in science and technology. The Ministry of Consumer Affairs, Food and Public Distribution (MCFPD), amended the PC Rules vide notification dated 1 March 2018 by allowing manufacturers/packers/ importers for putting stickers/tags/online printing, etc. up to 30, 2018 for making the mandatory declarations required under the Legal Metrology (Packaged Commodities) Rules, 2011.

The issues and recommendations under the Legal Metrology Act/Rules can be listed as follows:

- Rule 5 of the PC Rules specifies the standard quantity for specified commodities provided in the Second Schedule. With the rise in competition, innovation and consumer demand, it is recommended to either scrap such a schedule or to expand the scope of the schedule to include a wider range of standard quantities. This is more relevant during these unprecedented times of Covid19, where providing greater flexibility to consumers by permitting more pack sizes will be in consumer interest. It will give more options to the consumers especially to those who buy to consume on a daily basis rather than stock.
- Value based packaging under the PC Rules provides an exemption from adhering to a standard quantity if the value of the product is INR10 or less. However, with an increase in the Consumer Price Index over the preceding years, it is highly recommended that the upper limit for value-based packaging be increased from INR10 to at least INR20.
- Rule 18 (2A) of the Packages Commodity Rules- While the industry agrees that the intention behind this Rule is to curb restrictive and/or unfair trade practices of charging different retail prices for identical packs, but the literal interpretation of the Rule, however seems to read in a way that curbs a manufacturers' right to have different retail prices (for an identical pack) in different geographic areas. The wording of the current Rule, as it stands, seem to restrict all differential pricing/MRP even if it's justifiable for various reasons and whether or not it's an unfair/restrictive trade practice as the term used in the said Rule is applicable for all the "identical pre-packaged commodity(ies)".
- In July 2020, basis the industry feedback, government has released a consultation proposal for decriminalisation of offences and to review the civil and criminal penalties under Legal and Metrology Act, 2009 in order to consider the suitability for the imposition of criminal liability. While the proposal is a positive move towards decriminalisation, there are still some ambiguities such as:
  - In the proposal, the term "cancellation of license" has been repeatedly used in various sections (Section 25 to Section 47). The Legal Metrology Office, whether at the State or at the Central Government, only issues 'registrations' and the term needs to be changed accordingly.
  - The fines proposed for the second offence are too steep and the proposal seems to have a "one size fits all" approach. It has been submitted that fines need to vary depending on the nature and gravity of violation. The determination of the punishment should also be viewed keeping in mind whether there was a mens-rea involved.
  - Non-compounding of any alleged violation at the department level should not result in the aggrieved party not having any remedy. The rule of law requires application of principles of natural justice and as such, an opportunity should always be given to the aggrieved party. Moreover, the broader proposal is to convert the nature of offence from criminal to civil, but the remedy process (other than appeals under Section 50) seems to be missing.
  - It can be proposed that the Controller of Legal Metrology in the States acts as an Adjudicating Officer whose confirmation/order is required before fines can be

imposed by the Legal Metrology Officer and then, an Appellate Authority is also constituted wherein appeals from the orders of an Adjudicating Officer can be preferred.

6.7 Recent Updates from the GST Perspective in the FMCG Sector

- **Anti-profiteering**
    - A question that arises as a result of rate rationalisation is whether companies in question have adequately passed on the benefit on account of tax reduction to end consumers. This is on account of the Anti-Profiteering provision, introduced as an anti-inflationary mechanism under section 171 of the Central Goods & Services Tax Act, 2017, which mandatorily requires reduction in prices, in case of reduction in output GST rate or an increase in input tax credit. There is however lack of clarity on how to compute the benefit to be passed on to end customers i.e., whether increase in quantity/grammage of products is allowable, in lieu of a specific price reduction.
    - In light of the aforesaid GST rate cuts, there has been a surge in the complaints received by anti-profiteering authorities from customers, regarding companies not passing on adequate benefit of the GST rate cut. Absence of a clear mechanism has led to use of arbitrary methodologies by the anti-profiteering authorities, and consequent prolonged litigations. Thus, pressure has been mounted on companies to constantly re-visit prices with the evolving law, and pass on the benefit of rate reduction or input tax credit expansion to customers.
- **Budgetary Support Assistance:**
    - Another issue that has affected FMCG businesses is the lack of sufficient budgetary support under the GST regime for units located in states like Uttarakhand, Himachal Pradesh, North Eastern States or Jammu & Kashmir. Under the erstwhile regime, several FMCG manufacturing concerns were set up in areas that enjoyed area-based excise duty exemptions. However, under the GST regime, there is no ssuch *ab-initio* tax exemption available. In order to reduce the hardship of such units, budgetary support has been provided by the Department for Promotion of Industry and Internal Trade (DPIIT) to such units in area based exemptions, for residual periods, for which units would have operated under the area based exemption scheme. Such support is being provided by way of refund of GST limited to the share of Central Goods and Service Tax (CGST) and Integrated Goods and Service Tax (IGST) retained, after the devolution of taxes to the states. This only works out to 58% of the CGST amount paid and 29% of the IGST paid by such unit.

Following are some of the key recommendations:

- It is recommended that guidelines are issued by the government at the earliest that clarify the methodology that needs to be adopted by FMCG companies for passing on the benefit to end customers. Specifications around whether pricing check has to be carried out across all intermediaries in the supply chain and whether it needs to be done at a product level would help companies.
- Lack of sufficient budgetary support: Since majority FMCG companies set up shop in excise-free areas, additional budgetary support must be provided to them in order to tide them over.

6.8 Enforcement of trademarks for brand protection against rampant sale of fakes, trademark infringements and look-alikes

Trademark infringement and counterfeiting has become a ubiquitous problem growing at an exponential rate in India even in times of the pandemic, taking undue advantage of the consumer and trade. Counterfeit products are a hazard and against the interest of the consumers, interest of the industry and also the government at large, due to loss of income to the exchequer through unaccounted sales, taxes, etc. of counterfeits. Industry estimates suggest that 30% of all products sold in the FMCG market in India are counterfeit. This is despite strong laws to regulate the infringement of intellectual property (IP) rights.

Following are some recommendations from the industry:

- In light of risks and protection of interests of all the stakeholders, it is important to provide the necessary support and infrastructure to the IP right holders to allow them to effectively fight counterfeit products and people involved.
- Section 115(4) of the Trade Marks Act, 1999 (TMA) mandates that an opinion from the Trademark Registry on the impugned trademark is required before an officer equal to the rank of a deputy superintendent of police takes cognizance and further actions, including search and seizure with respect to offences of applying and selling of goods with false trademarks, i.e., infringement and counterfeiting. This creates an impediment in taking timely actions allowing people ample time to get away. With such a prerequisite for the police, offences under TMA cannot be considered fully cognizable as intended, desired and required by the industry and IP holders. The opinion from the trademark registry as above takes considerable time due to lack of resources and department priorities impeding expedited actions against counterfeiters by the trademark proprietors and the police.
- Trademark proprietors are using the judicial or copyright infringement route to take actions due to extreme delay in procuring such opinion for police actions under trademark law. This is not only increasing the burden of the judiciary but also makes the section in TMA otiose and irrelevant.
- Using the copyright infringement route is also not viable because of the requirement of registration documents though copyright registration is not mandated under the law, by the law enforcement officials. However, it is important to note that as copyright vests on creation and registration is not compulsory, documents of proprietorship are not available with copyright owners, making it difficult for the law enforcements officials to determine the rights and limiting actions against counterfeiters under copyright protection.
- Trademark Rules 2002 have been replaced with Trademark Rules 2017. Applying for well-known trademarks has been made easier by laying down the criteria for deciding whether a mark is a 'well-known' mark or not, such as mark is known and recognised by the relevant section of the public, duration/extent/geographical area of promotion of the mark, whether registration has been made, whether successful enforcement actions have been taken etc. However, certain challenges in terms of no timelines under the Rules for such determination, lack of clarity on process for opposition, exorbitant fee, restrictions on size of digital uploads of evidence may not encourage brand owners to take this route. Brand owners may prefer to get a declaration from the Court rather than opting for this route.

According to the 2020 International IP Index by the US Chamber of Commerce's Global Intellectual Property Centre (GIPC), India's score has improved for the third consecutive year from 36.04% [rank 36 of 50] in 2019 to 38.46% [rank 40 of 53] in 2020. The GIPC has stated that – *"India has made significant progress in protecting intellectual property (IP) but the "job is not yet done"*. Thus, while broader challenges remain, the increase is a result of specific reforms that better align India's IP environment with the international IP system. Challenges in the IP environment in India include, for instance[2], in the biopharmaceutical sector, "Indian policy continued to breach international standards of the protection of innovation and patent rights, revoking patents generally accepted around the world and announcing that other patented medicines are being considered for compulsory licenses." The continued use of compulsory licenses, revocation of patents, and weak legislative and enforcement mechanisms across all IP rights raise serious concerns about India's commitment to promoting innovation.

In summary, while it has become harder to obtain intellectual property rights (IPRs) in India, it continues to be difficult to enforce IPRs. The focus should therefore shift to enforcement of IPRs. It is also suggested that to speed up the adjudication processes, the Central Government should consider fast track courts for IP enforcement cases.

6.9 Parallel Imports and Counterfeits

Parallel import is a scenario where goods are brought in a jurisdiction without the permission of the brand owner (i.e., IP right holder). These goods are not counterfeit goods, but merely unauthorised imports from the brand owner's perspective. On account of the lower costs of the parallel importer (as there are no brand management and advertising costs), the products are available cheaper. The manufacturers, oppose this practice as it eats into their legitimate sales.

Further, owing to the unauthorised imports, there are instances where due to variance in product formulations (different countries may have a different product formulation which is suited best for its consumers), the consumer experience of a brand may be negatively affected. In some industries, the authorised resellers may not be able to provide proper after-sales service or replacement.

Under the Trade Marks Act, 1999 (TMA), infringements of a registered trade mark under Section 29(1) covers imports or exports of goods. Imports of goods under Registered Trademarks require consent of registered proprietor of the trademark before imports. Similar provisions exist under Indian Copyright Act, 1957, Patents Act, 1970 and Designs Act, 2000.

However, Circular No. 13/2012 dated 8, 2012 issued by CBEC (the Circular) on parallel imports, states that parallel imports of branded goods are permitted under the TMA. The circular refers to section 30(3)(b) of the TMA without, in any manner, clarifying or interpreting this provision but merely reproducing it. It concludes that TMA permits parallel imports and on the basis of such conclusion, directs the field formation of the customs authorities across India to follow the circular. There is no clarification, express or implied, provided in the Circular, that "no consent" of the registered proprietor is required before, or at time of importation of branded products. The intent of law cannot be to penalise the domestic infringers and let importers who infringe go free.

Since the issuance of impugned circular, custom authorities at seaports, airports, and inland container depot have stopped examination and inspection of containers that represent carrying imported goods that are freely importable including branded parallel imported goods. This has prompted the traders, importers to import counterfeit goods under the garb of parallel imports and there is a surge in imports sale of counterfeit goods in markets. While the circular seeks to address the parallel imports by issuing directions under the impugned circular, it had the effect of legitimising counterfeit goods. Pending Supreme Court's judgement in the Samsung Electronics case referred above, it cannot be said that India follows international exhaustion of rights. The CBIC circular permitting parallel imports which impinges on the rights of the right holder may therefore be considered premature. In the absence of information sharing of such parallel imports by customs authorities to Right holders, they are unable to verify the same and ascertain if any counterfeits have been shipped along with genuine goods. This has far reaching implications resulting in release of counterfeits that may have been coupled with genuine goods, into the domestic market posing a high risk to the health and safety of consumers and entailing unnecessary hardships on the right holders

Key recommendations:

Basis the present provisions of the TMA, it is suggested that a further clarification be issued by which the above position is suitably reflected and/or impose a reasonable restriction on the importer(s) to declare these parallelly imported goods as 'parallel goods'. It is also urged that customs authorities carry out 100% examination and/or intimate the right IP holders of all parallelly imported goods.

6.10 Draft e-commerce policy with respect to counterfeits, trademark infringements, look-alikes etc.

The menace of counterfeiting through the e-commerce channel has become an area of concern for brand owners. The Department for Promotion of Industry and Internal Trade (DPIIT), Ministry of Commerce and Industry had, in February 2019, issued the Draft National e-commerce Policy for Stakeholder Comments. The draft policy, in a comprehensive manner, covered all aspects of E-commerce Business and issues associated with the same including specific focus on 'Consumer Protection'. Then again in November 2019, the Ministry of Consumer Affairs published draft rules on E-commerce for stakeholder comments.

Some of the recommendations made by on the draft policy are as under:

- Enhanced due Diligence by E-commerce Market Place: The current due diligence process adopted by E-Commerce players is insufficient. Sellers these days provide fake addresses and details, operate with multiple address and multiple GST number to ensure that their real identity is not disclosed. Practices such as duly /periodic verifying documents submitted by the sellers, running checks on the GST numbers submitted by sellers, physical checks like visiting the sellers address etc. should be followed. Technology such as Geo Location Tagging etc. should be used to verify area of operation of sellers. Any lack of due diligence in verification process should result in liability of the E-commerce player.
- Role of E-Commerce Players beyond Intermediary: The common legal defence of E commerce players is that they are only Intermediary under the IT Act and therefore the obligation with respect to the counterfeit products is only limited to take down. The role and responsibility of E-commerce with respect to issue of counterfeiting needs to be clearly defined. In absence of clear jurisprudence of this issue counterfeiters are using e commerce as safe haven for their business.
- Collaboration amongst Industry Players: Sharing of Information of Counterfeiters amongst E-commerce players including creating Common Database of Counterfeiters for all the blacklisted entities who were found to be dealing in counterfeit products on E-commerce platform shall ensure that such non-compliant blacklisted entities are either delisted. It will create deterrent for businesses to engage in this crime. This shall ensure that the problem is arrested at the root and shall also discourage counterfeiters who keep registering themselves on different websites under different names.
- Create deterrent for Counterfeiters: Currently there is no deterrent to the counterfeiters or e-comm players for selling counterfeit products. Introducing penal provisions will place additional responsibility on the marketplace to own up what they sell on their platform thereby conducting proper due diligence and checks of the sellers on their platform. Marketplaces should impose financial disincentives for sellers if found to be selling counterfeit products on their platform. In addition, if a seller is found to be selling counterfeit products, the marketplace should blacklist that seller from selling all products on its platform for a specified period.
- Avoid Multiplicity of Legislations: In 2019, the DPIIT as well as The Ministry of Consumer Affairs have issued the draft E-commerce Policy and the Consumer Protection Guidelines for E-commerce respectively. It is important to highlight that Consumer Protection Guidelines dilutes the position taken in the E- commerce Policy on the issue of counterfeiting. It is submitted that the multiplicity of guidelines and legislations in this area will lead to issues of interpretations and effective enforcement.

6.11 Food Laws – High Fat, Salt and Sugar food items (HFSS)

The Government of India is actively promoting nutrition and wholesome food to tackle the dual burden of malnutrition in the country. On one hand it is tackling undernutrition through programmes such as 'Poshan Abhiyaan' and on the other hand programmes such as the 'Eat Right India' have been launched to combat negative nutritional trends to fight lifestyle diseases. With requests from the civil society organisations, the government has been framing guidelines and regulations to promote the intake of wholesome food and decrease the consumption of high fat, salt and sugar food items (HFSS).

A few issues and recommendations in this area are listed as under:

- In September 2020, the Ministry of Health & Family Welfare has notified The Food Safety and Standards (Safe Food and healthy diets for School Children) Regulations, 2020 to come into effect from 1 July 2021. The regulations mandate that food products high in saturated fat or trans-fat or added sugar or sodium cannot be sold, marketed, advertised or samples in schools or in an area within 50 meters from the school gate in any direction by food companies and others. The 50 meters ban is being opposed by Packaged food manufacturers and Retailers as it is onerous and has multiple operational challenges. Amidst other reasons, in certain cities and big towns, considering the mushrooming of schools, a good part of these places will fall within the 'no sale region' if the 50-metre restriction is implemented. Further, since schools/creches can be opened by anyone and even without any board affiliation (like play schools, crèches), in the future, if schools are opened within 50 metres of an already existing establishment that sells these products, the establishment will have to stop business. This will create a huge acrimonious situation and may give rise to needless litigation. Industry has therefore recommended that the 50-metre restriction in the said regulation be withdrawn.

- The draft Food Safety and Standards (Labelling and Display) Regulations, 2019 which inter alia proposed front of pack labelling for HFSS foods is still under discussion between FSSAI, Industry and the civil society stakeholders. After much opposition and deliberations on the Nutrient thresholds proposed in the draft for HFSS and the manner of declaration, the FSSAI has undertaken a project "Nutrient (Fat, Sugar and Salt) Threshold Study in packaged foods". The study which is being conducted by 'The Nutrition Alchemy' (Label Blind) at the behest of FSSAI involves assessing the current nutritional information (per 100 gm/ml and per serve) of packaged food products across major food and beverage categories and sub-categories defined by FSSAI. A total of 30 companies and 1328 products are being included in the study. Culmination of the study and the resultant proposal from FSSAI will restart the discussion on the issue.

6.12 Drugs and Magic Remedies Act, 1954

The Drugs and Magic Remedies Act, 1954, was intended to prevent gullible or vulnerable members of the public from being exploited through advertisements for drugs or cosmetic products that claim to have magical properties. A draft amendment bill named The Drugs and Magic Remedies (Objectionable Advertisements) (Amendment) Bill, 2020 has been circulated by the Ministry of Health and Family Welfare for suggestions and comments. Amongst other proposals, the Bill seeks to:

- Expand the scope of the DMR Act by increasing the list in the Schedule from 54 to 78 items
- Enhance and quantify the penal provisions under Section 7 of the DMR Act.

Key recommendations:

Many of the proposed additions to the Schedule of DMR Act have been borrowed from Schedule J to the Drugs & Cosmetics Rules, 1945. All ayurvedic products had exempted from the provisions of Schedule J and this proposed amendment to DMR Act tends to take away that exemption by including Schedule J conditions in the Schedule to the DMR Act. What is required is effective implementation of the current DMR Act rather than expanding its scope.

6.13 Drugs and Cosmetics Act and Rules 1940

At present, the manufacturing, import, sale and distribution of cosmetics are covered under the Drugs and Cosmetics Act and there were no separate regulations for cosmetics, allowing such products to often circumvent testing and other regulatory norms, as many other rules meant specifically for pharmaceuticals do not apply on cosmetics (only seven rules relate to cosmetics)

There is substantial scope to grow the Personal Care/Cosmetics market in the country. The per capita consumption of beauty and hygiene products is still very low in our country. One of the ways by which this Industry can optimise its potential is through freeing it from a regulatory overload.

One of issues plaguing the industry is around the substantial delay in seeking manufacturing licenses (due to pre-market approval requirement). Often, for products which are manufactured in more than one States, while one authority grants the license, other(s) raise concerns on the same application, even though both States are implementing the same central rules.

Today's cosmetic market is driven by innovation including new colour pallets, special products targeted to specific skin types and unique formulations considering different needs of consumers. Most cosmetic products have a life span of less than five years and manufacturers reformulate 25% of their products every year keeping consumer needs and trends in mind. They need to improve products constantly in order to stay ahead in a highly competitive market where more choice and greater efficacy is expected by the discerning consumer. In such a dynamic industry, speed to market is of prime importance.

The following can be some of the key recommendations:

- The industry feels that treating drugs and cosmetics at par is unfair and hence recommends that Cosmetics Rules need to be separated from rules for Drugs under the same Act.
- The government should move from a regime of Pre-market Approval to post-market notification. The current rules applicable for cosmetics may be amended to replace product licensing to notification to authorities post launch. We recommend that the government should adopt simple notification of cosmetic products - like in EU and ASEAN - where the system followed is post market notification, as compared to pre-market approval as is in vogue in India.
- Creation of a portal for notification and online submission of information by manufacturers for grant of license may be thought of. Through the Pre-market notification, individual companies may submit all the documents required as per the current rules and regulations for pre-market registrations. This would ensure that the regulators receive all the necessary documents to ensure safety, quality & efficacy of the products while providing the flexibility to the industry to increase the market responsiveness. Prior Intimation of the above should suffice and allow the authorities to evaluate and pick up non-compliant products and take corrective actions.
- The manufacturers will ensure full compliance with disclosure and labelling norms at all times, so that the cosmetic product is not misbranded, and consumer gets full information as per disclosure requirements under provisions applicable to cosmetics. If there is a non-compliance noticed once the product is in market, the same procedure will apply as it applies today. No such instance will go without being dealt with once the sample is picked up.

CONCLUSION

India represents a good opportunity for international retailers in single brand retail, cash and carry, and e-commerce, as the country appears to be bound for recovery and on the cusp of a strong growth phase over next five years. The ongoing COVID-19 pandemic presents unique opportunities and challenges to the FMCG sector. The tipping point for brick and mortar retail continues to be the opening up of FDI norms in multi-brand retail, a move that is not expected in the near-term. The total FDI inflow was over US$318 billion (€285 billion) between 2014 and September 2019 representing nearly 50% of the cumulative FDI in India since April 2000. Further, India's ranking in the World Bank's Ease of doing business 2020 report has moved up 14 places to 63 among 190 nations. The Economic Survey 2020 has pegged India's GDP to grow at approximately 6-6.5%. Increase in the internet penetration and improvement in the physical infrastructure will make India an attractive place for investment, especially when some of the trade related difficulties based by the industry, and as discussed above are alleviated.

ENDNOTE

1. Please refer to sections 3(13), 3(14), 3(20) and 3(37) of the Personal Data Protection Bill, 2019 for the meaning of the terms Data Fiduciary, Data Principal, Harm & Significant Data Fiduciary respectively.
2. http://www.business-standard.com/article/economy-policy/protecting-patents-india-worst-in-world-114012900371_1.html

NOTE

Healthcare

Indranil Mukherjee (B. Braun) – Chairman,
Healthcare Sector Committee, and its Members

EXECUTIVE SUMMARY

India's Gross Domestic Product growth rate contracted by 23.9% for the April 2020 to June 2020 quarter as the coronavirus pandemic took a toll on the country's economy. It is estimated that medical technology industry has suffered a 50-85% drop in revenue across categories in April-June due to the situation. "**Atmanirbhar**" has brought in several opportunities to many sectors, prominent among them being the medical device manufacturing in India. To ensure that all medical devices meet certain standards of quality and efficacy, the Union Health Ministry on 11 February 2020 notified 'all devices (medical equipment, instruments)'used on humans or animals as "drugs" under Section 3 of the Drugs and Cosmetics Act, 1940 with effect from 1 April 2020.

In Union Budget 2020, an additional 5% health cess was levied on the import of large category of medical devices. In March 2020, industry submitted representations to Ministry of Finance, however there is no action on this issue yet. Medical Device Bill has been proposed to regulate Medical Devices in India. The NITI Aayog (Planning Commission) held stake holder consultations with all industry Associations to discuss w.r.t Medical Device Bill. The government is contemplating a separate regulator to regulate Medical devices in the country

In 2019, The HEALTH TECHNOLOGY ASSESSMENT BOARD ACT 2019, has been issued by the Government of India to be it enacted by Parliament in the Seventieth Year of the Republic of India. The bill is very well articulated to encompass the constitution and working of the board. A few dimensions which may benefit the overall impact of the said ACT pertain to more weightage for patient centricity, key opinion leaders, and subject matter experts.

Under initiatives like Make in India, several state governments have taken up the onus of setting up medical device manufacturing parks in their respective states and have got the approval from the Government of India to do so. There would be six medical devices manufacturing clusters in the country in states like Andhra Pradesh, Kerala, Telangana, Tamil Nadu, Maharashtra, and Sikkim. Meanwhile, in view of the situation arising out of the COVID-19 pandemic, an additional allocation of 40 thousand crore rupees has also been made for the Mahatma Gandhi National Rural Employment Guarantee Scheme during this financial year.

The first meeting of NMDPC has been held under the Chairmanship of Secretary, Department of Promotion of Industry and Industrial Trade (DPIIT), to discuss public procurement order. It has been decided NITI Aayog will share a brief legislative view of Draft Biomedical Devices Bill and DCGI will brief on the current regulatory regime under Drugs and Cosmetics Act, 1940, and BIS and QCI to point out the adequacy of current regulatory regimen. Medical devices should be exempted from Legal Metrology (LM) as in the past. All Medical devices comply with the principal Act (D & C Act 1940. Having another parallel Act of LM will complicate the labelling & create confusion.

Annual Report 2017-18 of the "DOP" - Department of Pharmaceuticals laid down in the Parliament, also states that Medical Devices are very different from Drugs. Since the scope of DPCO, 2013 is restricted to "formulations" as defined in Para 2 (1) (i), which means a medicine processed out of or containing in one or more drugs, notified medical devices, can under no circumstances be considered as a medicine, till the circular of NPPA dated 15 February 2015, as it does not fall within the definition of "formulation" and consequently considering it as a Non-Scheduled formation is contrary to DPCO, 2013 and NPPP-2012.

1 MEDICAL DEVICES

1.1 COVID-19 Impact

1.1.1 The unprecedented Economic Impact of COVID-19 Pandemic

India's Gross Domestic Product growth rate contracted by 23.9% for the April 2020 to June 2020 quarter as the coronavirus pandemic took a toll on the country's economy. It is estimated that medical technology industry has suffered a 50-85% drop in revenue across categories in April-June due to the situation.

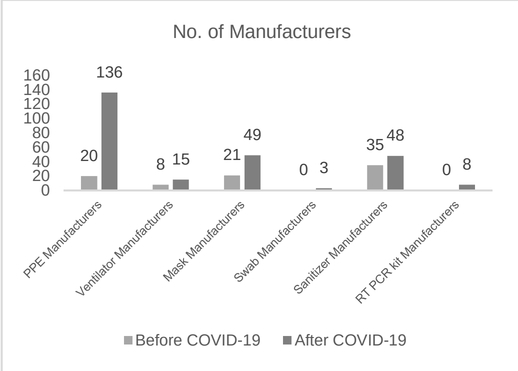
Another significant impact of COVID-19 situation has been on the employment across sectors in India. According to data from the Center for Monitoring Indian Economy (CMIE), India's overall unemployment rate as on 13 August 2020 stood at 7.9% and is expected to settle at a higher level than seen before the COVID-19 induced lockdown. In the medical device sector, the effects of shrinking margins of hospitals can be seen at the channel and service dealership networks, and sub-dealers are already experiencing significant workforce downsizing.

1.1.2 The Road to Economic Reforms to Negate COVID-19 Pandemic Impact

On 12 May 2020, Prime Minister of India made a clarion call for an '**Atmanirbhar Bharat**' - a self-reliant India to rejuvenate the industries. In order to encourage domestic production of critical APIs (Active Pharmaceutical Ingredients)/KSM (Key Starting Material) and medical devices, Union Cabinet on 12 March 2020, has approved a scheme for development of three bulk drugs and four medical devices parks in which Government of India will give incentive to States with a maximum limit of INR1000 Crore per bulk drug park and INR100 Crore per medical device parks.

The COVID lockdown situation and the call by the Indian Prime Minister, Narendra Modi towards becoming more self-reliant or "**Atmanirbhar"** has brought in several opportunities to many sectors, prominent among them being the medical device manufacturing in India. The coronavirus pandemic has spawned a cottage industry in PPEs, hand sanitisers, masks, etc. India is now the second-largest manufacturer of PPEs, after China. **Atmanirbharta**, or self-reliance, is facing a quality challenge in the protective gear market. There has been a flood of complaints about low-quality PPEs, sanitisers, gloves and so on, raising concerns about the impact on India's public health response to COVID-19 and infection control strategies (Figure 1).

Figure 1 Surge in Medical Device Manufacturing after COVID-19



Source:https://www.healthcareradius.in/26566-medtech-sector-inches-towards-self-reliance

1.2 Background and Industry Landscape

India is an important trade partner for the EU and an emerging global economic power. India is the fastest growing large economy, with growth rates of about 7%. The EU was India's largest trading partner, accounting for €92 billion worth of trade in goods in 2018 or 12.9% of total Indian trade, ahead of China (10.9%) and the USA (10.1%). The EU is the leading destination for Indian exports (almost 18% of the total). India is now the fourth-largest service exporter to the EU and the sixth-largest destination for EU services exports. The EU is one of the largest investors in India, with an overall stock of more than €72 billion in investments. India too is emerging as a proactive investor in the EU, with €4.9 billion in 2016. Close to 6,000 EU companies are present in India collectively providing direct employment to 1.2 million workers and indirect employment to 5 million.

Indian healthcare industry is a US$96.7 billion industry and in terms of both employment and revenues, the Indian healthcare industry has grown to one of the biggest sectors in the country and has attracted a lot of foreign players. India contributes significantly to the global pharmaceuticals and vaccines market, however lags behind in the medical device segment. This is because the local manufacturing is largely limited to high volume and low-cost segment of medical consumables. To change the status to promote and develop local manufacturing capability in the low volume and high technology segment, the policies need to relook into fostering the whole ecosystem to develop innovative and high-end R&D in medical device technology in India. Global investments in the medical device sector can help the shift of narrative from '**Make in India**' to '**Make from India**' and spur exports that help to accelerate India's position into the medical device value chain. The Medical Devices industry in India is valued at US$5.2 billion, contributes 4-5% to the US$96.7 billion Indian health care industry.

With about 750 to 800 medical device manufacturers in the country and an average investment of INR170-200 million, industry has an average turnover of INR450-500 million in India. The industry has steadily grown at a CAGR of 15.8% and witnessed a surge from US$2.02 billion in 2009 to US$3.9 billion in 2015 and as it is estimated to achieve the target of US$50 billion by 2025.

The Government of India is planning to increase public health spending to 2.5% of the country's GDP by 2025. The healthcare market in India is set to increase three-fold to INR8.6 trillion (US$133.44 billion) by 2022. The hospital industry in India is forecasted to increase to INR8.6 trillion (US$132.84 billion) by FY2022 from INR4 trillion (US$61.79 billion) in FY2017 at a CAGR of 16-17%. There is a significant scope for enhancing healthcare services considering that healthcare spending as a percentage of Gross Domestic Product (GDP) is rising. The government's expenditure on the health sector has grown to 1.4% in FY2018E from 1.2% in FY2014. The Indian medical devices industry is a diverse space that has been growing at a CAGR of over 7%, this US$5.2 billion segment is projected to reach US$50 billion in the next five years. Diagnostic equipment contributes to the major chunk of the global market share, while in India the biggest contribution comes from the equipment and instruments category (almost 35%).

Recent policy changes by the government have brought some imported medical devices under the price capping. While currently only 24 items including cardiac stents, knee implants and condoms are regulated, inclusion of more devices would allow the National Pharmaceutical Pricing Authority (NPPA) to notify them as drugs, thereby bringing them under the price capping system. NPPA has notified all medical devices as drugs under the provisions of the Drugs Prices Control Order (DPCO-2013) with effect from 1 April 2020 in pursuance of notification dated 11 February 2020. With effect from 1 April 2020, all medical devices shall be regulated by the government as drugs for price monitoring. Therefore, the maximum retail prices (MPRs) of all the medical devices would be monitored by the government under the provisions of Para 20(1) of the DPCO, 2013 to ensure that no manufacturer/importer increases the MRP of a drug more than 10% of MRP during preceding twelve month. As India is on track to becoming a US$100-billion strong bio-economy by 2025, Med. Tech. companies are working together to build a stable network across the country. With more than US$3 billion invested in the sector and the government favouring the medical device industry under the Make in India initiative, the time is right to boost research and development to create some next-generation technologies, including wearable devices indigenously. The global *In-vitro* diagnostics (IVD) market is estimated to reach US$80 Billion in 2024. The Indian IVD market is forecast to grow at a CAGR of 7-8% from 2019 to 2023. In 2018 the total market value was US$2.1 billion. IVD has witnessed several changes and additions in the recent past with a paradigm shift from traditional diagnostics to new generation diagnostic that work at the gene level.

1.3 Issues/Headwinds

1.3.1 Manufacturing, Logistics, Supply-Chain Issues in COVID-19 times

Manufacturing/production in plants suffered due to lack of manpower and location in containment zones with less capacity utilisation. Increased cost of many input and packaging materials. More issues in terms of availability of contractual manpower, issues being faced on loading, unloading of container and trucks. Occasional shortage of trucks and higher freight rates. Inability of employees to commute to/from work in case of sealing of nearby state border. Inability of employees to return from hometowns at end of leave due to non-availability of public transport. Issue of clearance of imported materials at some ports. Suggestion for free movement to be allowed between nearby districts or boarders and restriction on people movement based on COVID-19 status of origin/destination districts and not on the basis of state borders. Frequent changes in policies also had an adverse impact. Companies had to pay huge demurrage charges as there was delay in shipments release from custom office. Waiver for demurrage was available only for brief time period till 03 May 2020.

1.3.2 Medical Devices (Amendment) Rules, 2020

To ensure that all medical devices meet certain standards of quality and efficacy, the Union Health Ministry on 11 February 2020 notified 'all devices (medical equipment, instruments)'used on humans or animals as "drugs" under Section 3 of the Drugs and Cosmetics Act, 1940 with effect from 1 April 2020. The Central Government, after consultation with the Drugs Technical Advisory Board, through a gazette notification dated 11 February 2020, released the Medical Devices (Amendment) Rules, 2020 after amending the previously Medical Devices Rules, 2017, for mandatory registration of medical devices with Central Drugs Standard Control Organisation. The Medical Devices Rules, 2017 was published in the Official Gazette dated the 31 January 2017 and last amended, dated the 11 Feb 2020. The aim is to regulate all medical devices so that they meet certain standards of quality. Besides it will also make medical device companies accountable for quality and safety of their products. Once notified, the manufacture, import and sale of all medical devices will need to be certified by the Central Drugs Standard Control Organisation.

The Medical Device Industry welcomed the notification from the government and highlighted that this step will enhance safety for the Indian patients in the long run. It will also act as a guide for Indian companies to come up with international standards integrate with global regulations enhancing exports, encourage foreign direct investments (FDI's) with standardised guidelines. The move will also encourage ancillary industries to be set up in the country. The Medical Device Expert Advisory Group was created to help CDSCO and MOHFW in rolling out regulations and to create regulatory framework for Medical Devices and these decisions taken at DTAB level in absence of any representation from Industry without explanation of changes and rationale behind it. Industry also sought for clarifications on operational issues like Import License (IL's), definition of importers and manufacturers, Registration certificates (RC's), low-risk high-end and high-risk low-end products which will be coordinated with Drug Controller General of India and the Health Ministry.

The government on the other hand mentioned that definition of Medical Device is included in the Drugs and Cosmetic Act and as such the government have been regulating the same under the provisions of the Act and as such request was from Industry Associations to bring all the Medical Devices under regulation. In this regard the Expert Committee constituted by Government of India in consultation with all stakeholders such as BIS, FICCI, CII, NITI Aayog, DOP etc. came up with "Report on Roadmap of Medical Devices, Ministry of Health & Family Welfare, Government of India" as how to bring the Medical Devices under regulation. The gazette notifications dated 11 February is based on the recommendations given in the Roadmap. The regulations are dynamic in nature and changes per technological developments, requirements.

Regulatory timelines for products notified as medical device Vide S.O. 5980(E) and S.O. 775(E)

In order to regulate Medical Device, per S.O. 5980(E), 3 December 2018 – Four medical devices notified—w.e.f. 1 January 2020, namely- Nebuliser, Blood Pressure Monitoring Devices, Digital Thermometer and Glucometer

Further per S.O. 775(E), 14 February 2019 - Eight medical device notified w.e.f. 1 April 2020, namely – All implantable medical devices, CT Scanning equipment, X-Ray equipment, MRI Equipment, Dialysis machines, Bone marrow cell separators, Defibrillators and PET equipment

Applications for the above-listed impacted products were submitted by companies in FY2019-2020. In some cases, it has been more than a year since these applications were submitted. Later, the CDSCO released notifications regarding extension of the implementation date by a year. All these products applications have been returned with query and have to resubmit these applications few months before this effective date.

For effective implementation, below should be consideration:

1. Definite Timelines for re-submissions **-** The industry is looking forward to CDSCO for definite timelines to resubmit these returned applications**.**
2. No disruption in supply for applicants who have submitted timely applications **-** It is also understood that the some of the applications/endorsements for the said S.O.'s are yet to be reviewed and the industry has an apprehension that there may be challenges in issuing the import licenses in a timely manner before the implementation date.
3. Consideration for India-specific Labelling **-** As these medical devices, which are already marketed in the Indian market, are brought under the regulation for the first time, the India specific labelling will have to be incorporated in the label. These will include the details such as the import license number, which will only be available to applicants once the import licenses are approved and issued by the CDSCO.

Checklist for product approved as Medical Device in country of origin but covered under the definition of drug in the country:

Issue of product classification where product is approved as Medical Device in country of origin but covered under the definition of drug in the country has been acknowledged by CDSCO office. In this regard, your office has also issued office memorandum; dated 15 Nov 2019 to streamline this process that such application would be processed by New Drug/Import Division through SUGAM portal, however documents would be submitted per medical device checklist.

For implementation of same provision, CDAC has been requested in the same office memorandum to make provision for submission of such applications in SUGAM portal. CDAC is yet to make necessary provisions for the application of Drugs, which are treated as Medical devices in the country of origin, so that the importers can file the requisite documents in line with medical device checklist in SUGAM for drugs. This checklist is pending to be created in SUGAM.

1.3.3 Trade Margin Rationalisation (TMR)

Medical devices usually go through several points of sale along the supply chain - from a distributor to a wholesaler to a retailer and a hospital - before they reach a consumer. Each point in supply chain incurs various costs, such as freight, inventory carrying costs, rental, salaries, marketing and sales overheads and service and statutory expenses of compliance.

Trade margin is the difference between Price to Trade (the price at which the manufacturer or marketing company sells the drug to the distributor or stockist) and the maximum retail price (MRP). The government's recognition of trade margin rationalisation for medical devices as a fair and balanced approach to ensure reasonable prices to consumers is a welcome move for the patients as well as the industry. Under the proposed Trade Margin Rationalisation regime, manufacturers would be allowed to offer a limited price margin for the entire trade channel. 'Price to Trade' is an important element in rationalising trade margins and there should be an equitable framework for ascertaining the Price to Trade for both importers and local manufacturers. For the calculations of TMR, Price at the First Point of Sale (distributor) should be used instead of landed cost. Use of landed costs in trade margin calculation does not incentivise efficiency. Landed costs depend on Transfer Price (price at which the devices are transferred internally between the parent company and its subsidiary) and is not comparable with the Price to Distributor, which is the market price.

The approach mentioned below would enable a level-playing field will emerge from this criterion while reducing the MRPs substantially.

As per the DOP report,

$$\text{*Formula to arrive MRP} = \text{Price to Stockist (PTS)} \times \left\{1 + \left(\frac{TM}{100-TM}\right)\right\} + \text{Applicable GST}$$

Where TM = Trade margin not exceeding 30

E.g. If PTS = INR100, then allowable MRP = INR142.28 @ 30% margin

The Prime Minister's office held a consultative meeting with industry Associations of Pharmaceuticals & Medical devices to seek their opinion on TMR. All

the Industry Associations supported the government of India's proposal to implement TMR from Price to trade/Distributors (PTT/PTD). The same could be announced in the next 2-3 months with % between 30 and 65 from PTD. Price to Trade (first point of sale, referred as the 2nd option in NITI's paper on TMR) should be considered for TMR fixation for medical devices. Recommendation to consider the implementation of "Report of the Committee of High Trade Margin in The Sale of Drugs 2015, where by Price to Trade (Price to the Distributor), will be decided by the manufacturer/Importer and GOI will decide on the percentage of Trade Margins
= (MRP- Price to Distributor) x 100/MRP.

1.3.4 Public Procurement Order (PPO)

Public Procurement Order on Medical Devices dated May 2018, calls for certain percentage of local contents: Medical disposables/consumables - 50%, Medical equipment, Surgical instruments- 25%, Implants 40%, Diagnostic Regents 25%. In practice, 85% critical devices of Class C & Class D are imported, with hardly one/two local manufacturers. The guidelines also state that the local content requirements would be increased in a phased manner over the course of three years. Local content will be computed on the basis of the cost of domestic components in the device compared to the total cost of the device.

The guidelines also state that preference will be given to local suppliers in terms of procurement. All local suppliers will be required to furnish a self-certification of use of local content prior to bidding for public contracts.

The possible challenges could be:

- Import Substitution Impractical: Even developed countries depends on import. (China 70 %, Japan 50 %, USA 30 %)

PPO implication in Tertiary/referral hospitals:

- Patients will be denied the benefits of world-class technologies
  - Lowering of eligibility criteria for bidders:
- will lead to poor quality procurement from un-reliable suppliers

Suggestion: A neutral agency should judge the present status of local capacity in each category and define local content.

However, it could be noted that unlike several other sectors, medical devices are comprised of thousands of very varied products in engineering and design complexity. At present, India has got adequate manufacturing capabilities for products like syringes, cannulae, stop cocks, extension lines, blood bags, dressings, hospital furniture, and suction machines, but lacks the desired ecosystem for devices like heart lung machines, pacemakers, complex catheters etc. A uniform 25-50% local content ask, preceding any meaningful scaling up of the missing sophisticated component ecosystem will create a risk of 'garage manufacturing' with low cost low quality knocked-down kits-based assembly. A pro-active policy formulation to regulate medical devices differently than drugs should permit free market dynamics to succeed and keep regulations simple, protecting consumers, and incentivising 'Make in India'.

Furthermore, many of IVD s & Devices need temperature control during its transportation. Under the circumstances to open & repack the products will affect the integrity of the product's quality. It is therefore necessary that products requiring temperature control environment are not included in the list of imported products requiring local content

Industry recommends that compliance to standards (like BIS, ISO, IEC) should not be treated similar to regulatory approvals (CDSCO, USFDA, EU MDD) for the purpose of licensing, procurement etc. This has reference to DOP's recent guideline for public procurement. To ensure quality of devices other than the 23 notified devices, government can ask for USFDA as proof of quality on all devices that come under regulation, and procurement can ask for CDSCO certificate as the only proof of quality of goods.

Ministry of Commerce & Industry launches revised "Public Procurement Order" for Promoting Domestic Manufacturing of Medical Devices.

The Scheme shall be implemented by Dept. of Pharmaceuticals (DOP). DOP will decide on the availability of manufacturers in each category of medical device and can make necessary changes as deemed appropriate. The said policy was launched in 2018 but has not yet been implemented across the country. The current policy is unfavourable to MNC's for some tender values.

1.3.5 Public Procurement Order (PPO) Revision

In 2017, DPIIT issued the PPO for enhancing purchase of local goods. In 2018, it was modified by Department of Pharmaceuticals (DoP), giving local content requirements for the sector. In June 2020, DPIIT has revised the PPO with stringent provisions and severe restrictions for import based supplies and advised the nodal ministries to issue sector specific order. The medical industry has submitted representations to DPIIT & DoP highlighting the industry's concerns and requesting for stakeholder's consultation before finalising the order. DPIIT has suggested industry to work this out with DoP.

Recommendation: Industry recommends significant relaxations in the revised PPO before implementation in medical device sector. In current form, it can lead to severe supply disruptions due to high import dependence in many product categories. Resolution of these issues particularly in clause 3 of revised PPO, is critical for medical device industry. DOP should continue with PPO 1.0.

1.3.6 Price monitoring

As per NPPA, the companies are only allowed to have one-time 10% increase in the celling price of all medical devices including Ortho Implants. However, the additional burden of health cess, increased custom duties, increased freight costs, devaluation of Rupee etc. has made it unviable for the companies to sustain.

Recommendations: In this context, the following actions are suggested to be considered in preparation for the August Price Order.

- Allow a one-time increase by 20% in the ceiling price due to extraordinary financial situation
- Allow the additional basic Customs Duty and Health Cess imposed to be passed on to customers beyond the MRP
- **Allow Bone Cement to be charged per free market trend**: Modify the 25 August 2017 office memo which, instructs orthopaedic companies to provide bone cement free of cost. Permit bone cement to be sold independently, as a free market trade or under TMR model.
- **Provide clarity regarding revision Surgery knee components**: The 16 August price order seeks to control prices on Primary knee implants. A small percentage of patients need to come back for revision surgery for which an additional range of components are needed which are not under price control. However, this point is not clear in the order creating confusion in the market place. A clarification is needed to remove this ambiguity.

1.3.7 Rationalising GST

The National Health Policy 2017 and WHO Essential Diagnostic Policy has placed emphasis on the role of preventive and promotive care components. It specifies health screening as a key lever for both communicable and non-communicable diseases. The government has also been taking all possible efforts to provide affordable medicines and diagnostic tests. Diagnostics services are also an integral part of the services to be offered by the 150,000 Health and Wellness Centres to be operationalised by 2022, under Ayushman Bharat.

Recommendation: It is therefore, requested that GST for diagnostic instruments and reagents may be at a lower rate as the clinical decisions are mainly based on the diagnostic tests using these medical instruments and diagnostic reagents. There is a need to rationalise the GST on Medical Instruments categorised under HSN 9027 from 18% to 12%. While implementing GST, GST Council has adopted Customs Tariff Headings for the purpose of determination of GST rate. Medical Instruments are classified under Chapter 90 on which GST rate for HSN 9018 is 12% whereas GST rate for the instruments falling Chapter 9027 is 18%.

1.3.8 Health Cess

In Union Budget 2020, an additional 5% health cess was levied on the import of large category of medical devices. In March 2020, industry submitted representations to Ministry of Finance, however there is no action on this issue yet.

Recommendation: In case if the Point no. 2 is not considered and companies are not allowed to pass on the cost to the customer. Then we would like to request that considering the multiple challenges faced by the medical device industry in current times, we urge DoP to write to Finance Ministry for roll back of health cess on medical devices.

1.3.9 Augmenting Healthcare Infrastructure to create demand

According to our estimates, for a hospitalisation rate of 7.0% (increase from current rate of 4.2% due to impact of COVID), average occupancy of 80% (assumed to increase from current 70% with increase in hospitalisation) and ALOS of 6 days (assumed to decline from current 7 days), **900,000 additional beds** will be required over the next one decade **assuming 65% AB-PMJAY coverage**. Even assuming I**NR 2.5 million investment per bed** at current value (mix of secondary and tertiary care beds), creating this infrastructure will require an enormous **investment of US$32 billion over the next 10 years**. Hence there is a need for specific focus on financing of healthcare sector. Private players have acted as the bedrock for capacity and capability for the healthcare sector and have been responsible for nearly 70% of healthcare delivery in the country. Considering the limitations government has on public spend on healthcare, to support demand generation in Tier 2, 3 & 4 cities and towns, government must encourage private sector investments and accord '**National Priority'** status to the healthcare sector.

Recommendations: "National Priority" status would make the healthcare sector eligible for priority sector lending akin to the agriculture and the textile sectors, with a comprehensive set of following measures:

- Ensure access to long term financing options (20 years tenor) at competitive rates for setting up new hospitals
- Ensure provision of land free of cost or at highly subsidised rates to set up facilities;
- Higher FSI for hospital buildings, as they are required to be located in central areas;
- Rates for power to be reduced to about 50% of applicable commercial rates;
- Formulate modalities for declaring "**Special Healthcare Zones**" in key geographies with attendant benefits such as earning exemptions for facilities located there, infrastructure support, manufacturing incentives, etc.;
- Incentives for accelerated job creation and training of skilled workforce;
- Extended tax holidays to enable ploughing back of earnings into infrastructure investment

1.3.10 Legal Metrology

As it has been mandated to comply with Legal Metrology labelling requirements, the Med. Tech companies have deliberated various issues with Director Legal Metrology Ministry of Consumer Affairs in context to issues faced by them e.g. labelling, font size, import date etc.

All devices are now regulated under DPCO 2013, they should be exempted from Legal Metrology (Packaged Commodity) Rules, especially clauses around labelling. As per S.O. 648(E) and G.S.R. 102 (E) all medical devices would be registered in CDSCO office and hence would follow labelling regulations per Chapter: VI Labelling of Medical Devices in Medical Devices Rules, 2017. It would be challenging to follow 2 different rules for same product and hence if there could be exemption provided for Medical Devices to follow Legal Metrology Act. Similar exemption in legal metrology has already been provided for Drugs which are covered under Scheduled and Non-Scheduled formulation.

1.3.11 Medical Device Bill

Medical Device Bill has been proposed to regulate Medical Devices in India. The NITI Aayog (Planning Commission) held stake holder consultations with all industry Associations to discuss w.r.t Medical Device Bill. The government is contemplating a separate regulator to regulate Medical devices in the country

1.3.12 NPPA (National Pharmaceutical Pricing Authority)

NPPA has notified all medical devices as drugs under the provisions of the Drugs Prices Control Order (DPCO-2013) with effect from 1 April 2020 in pursuance of notification dated 11 February 2020. With effect from 1 April 2020, all medical devices shall be regulated by the government as drugs for price monitoring. Industry support the need for monitoring the prices of devices, under DPCO 2013 to enhance patient affordability. However Medical devices business is different from drugs and hence we would not be able to implement DPCO 2013 for all Medical Devices. This would be possible to implement in B2C (Business to Customer) however timelines for implementation should be required to aligned with G.S.R. 102 (E); Dated 11 Feb 2020.

This is not possible to implement in hospitals/Institutions sale directly (B2B). This is because of following reasons:

a. Sale of these products is the outcome of negotiations based on accessories, software's, and AMC, CMC and installation expenses. Equipment is considered a depreciable asset for the purchasing organisation and their cost can vary from equipment to equipment depending on various factors like Annual Maintenance Contracts; Add on features opted by the buyer; procurement business models like reagent rental model etc.

b. It has inbuilt provision of self- regulation by the industry and scrutiny of prices by the buyers

c. In tender/bid/public procurement the manufacturer needs to submit a fall clause in the form of affidavit, guaranteeing minimum prices and also manufacturers additionally need to produce order copies of previous sales done to similar kind of hospitals per similar terms and conditions? It's highly recommend that the equipment sold under B2B arrangement should be exempted from DPCO, as it's unrealistic to have an MRP because of above mentioned reasons.

1.3.13 National Medical Devices Promotion Council (NMDPC)

The first meeting of NMDPC has been held under the Chairmanship of Secretary, Department of Promotion of Industry and Industrial Trade (DPIIT), to discuss public procurement order. It has been decided NITI Aayog will share a brief legislative view of Draft Biomedical Devices Bill and DCGI will brief on the current regulatory regime under Drugs and Cosmetics Act, 1940, and BIS and QCI to point out the adequacy of current regulatory regimen. It was also decided that NMDPC will work towards the technology transfer and skill building of the medical device industry.

1.3.13.1 Grey Areas

The amendment to LM Rules are not without grey areas. In our view, the biggest grey area is the use of expression "not for commercial or trade purpose" in the definition of "institutional consumer". In case the sale of pre-packaged goods is to institutional consumer, then LM Rules are not required to be complied with. In case of such sales, the LM Rules require manufacture, importer or packer to label the pre-packaged goods with the declaration - "not for retail sale". The exemption is significant because it reduces the administrative cost of labelling as well as the probability of occurrence of non-compliance, given that there is little to be declared on the label.

1.3.14 Overcharging demand notices to companies

Many Med Tech. companies have received overcharging notices from NPPA directing to pay overcharge amount for increasing prices by more than 10% per annum during 2014 to 2016. Medical devices are different from drugs in respect of nature, mechanism of action, manufacturing, quality control and mode of administration. The impact of these notices may have detrimental impact on the business climate and health economic milieu leading to severe dampening of the Med Tech. company initiatives and inadequate patient outcomes.

1.3.15 Regulation of roadmap of medical devices

Considering that bringing all medical devices into regulatory control, CDSCO increasing their workforce to ensure efficient and transparent regulatory services. As all medical device would be regulated, CDSCO office need more staff to timely review increased number of applications.

1.3.16 Bureau of Indian Standards (BIS)

BIS under the directions of NITI Aayog has been working to develop Indian standards for a list of commonly procured items by MoHFW.

Adopt International Harmonised Standards for Medical Devices

- As per MDR 2017, Medical device shall confirm to BIS. ISO should be followed if no relevant BIS standard is available. Request ministry to accept compliance to International standard wherever ISO/IEC is available

- Bureau of Indian Standards are similar to International standards in technical content.
- Medical device manufacturers/importers comply with ISO/IEC since operations are expanded in different geography of the world & most of countries accept device which are complaint to International Standards.

News reports indicate that the Bureau of Indian Standards (BIS) will have authority to regulate medical devices, which is going to take ease of doing business back to 20 years. Now CDSCO has developed a competency over a period of time and supporting the industry well so that should remain the authority to regulate medical device as it is. Globally, single regulatory authority regulates both drugs and devices under ministry of health e.g. USFDA, Health Canada, PMDA (Japan), TGA (Australia). Quality Control Order (QCO).

Quality Control Orders (QCO) have been issued by DOP for 6 products which will mandate certification of those products by BIS and testing in India. Mere conformation with BIS standards does not prove efficacy and safety of device. Further, BIS standards are mainly duplication of ISO standards. Mandating BIS conformation for products already conforming to ISO standards will be considered as technical barrier to trade. The proposed Quality Control Orders has a limited scope as it does not adequately address all aspects of quality, safety and performance and only covers the product safety standard of medical devices. Conforming to the order would mean increase in compliance cost for companies that are already adhering to essential checklist requirements of CDSCO or US FDA/CE norms as well as for domestic companies looking to export, since products must first conform with BIS standards, then qualify for global ISO/IES standards and then go for CE/US FDA for eligibility for global markets. Guidance documents released by CDSCO provided the list of laboratories where the applicant could go and get performance evaluation done. In this regard industry raised query about the fee charged by medical device testing laboratory, the turnaround time, and if CDSCO would control and monitor these two parameters to avoid financial burden on the industry and delays in the testing process

Certification process by Quality Council of India (QCI) – QCI has developed a parallel certification scheme, in spite of stiff opposition from industry chambers, for quality management system in medical device manufacturing and are in the process of developing an India specific product certification scheme.

Recommendation: Industry recommends continuity of device regulations **under Drugs and Cosmetics (D & C) Act** to ensure predictable regulatory environment for medical devices in future. Regulations must adopt consensus standards (ISO etc.) to demonstrate compliance to the essential principles. BIS must adopt such standards on regular basis and rely upon these consensus standards to increase predictability, streamline premarket review, provide clearer regulatory expectations and facilitate market entry for safe and effective medical devices. Compensation for faulty medical devices

The Govt. provision of compensation in case of injury or death due to any Medical Device found malfunctioning. The industry argues that the compensation for Severe Adverse Events (SAE) should be on a case-to-case basis, compensation should be on the extent of injury, irrespective of the risk-class of medical device. It has been proposed by Govt. that compensation should be the same irrespective of the class of device (this is now set at INR4 Lakhs for non-death case and INR8 Lakhs for death). Both government and Pvt. Clinicians can be appointed in Causality committee. Also, only clinicians from the respective therapy will be in the causality committee having experience in that device. Causality committee will call for compensation only if it is proven beyond doubt that it is the “device only” which caused the adverse event and no other reasons.

1.3.17 Medical Device Act

Govt. is contemplating a new Act for medical devices on the lines of Drugs & Cosmetics Act.

1.3.18 National List of Essential Medical Devices (NLEMD)

An expert committee has been set up by the Government of India and has submitted its report.

Industry urges for separate Medical Device regulations through a new act in accordance with global best practices, which is globally harmonised, specific to medical devices in accordance with the Medical Device Rules 2017. Recommendation was made to notify devices category wise and not as an individual item.

1.3.19 Uniform Code of Pharmaceuticals (UCPMP)

In December 2014, the Department of Pharmaceuticals issued a voluntary uniform code for pharmaceutical marketing practices. Due to industry confusion, the same agency issued a clarification in March of 2015 saying that the code applied to medical devices. The code includes a number of burdensome provisions that would hamper companies' ability to interact with healthcare providers.

It has been proposed by government that codes for both Pharmaceuticals & Medical devices should be merged into a single code. The Department of Pharmaceuticals (DOP) held a consultative meeting with industry Associations of Pharmaceuticals & Medical devices to seek their opinion on UCPMP. The DOP Secretary has stated that the said code will have to be implemented by all the companies after some amendments are made by the government.

In July, Industry associations had meeting with Department of Pharmaceuticals which strongly recommended that there needs to be a separate code for Medical devices as they are completely different from Pharmaceutical products/drugs. DOP secretary agreed to request and directed the Joint secretary in DOP to have a separate meeting with Industry Associations of Medical devices to discuss the same.

1.3.20 Voluntary Registration (VR)

Industry welcome the good initiative of DCGI to regulate each component, accessories etc. under Voluntary Registration to offer a complete package to end-user without any fees. Validity of the same is only **up till Sept 2021**. Industry need is to pool together the huge portfolio (implant) of accessories which are compatible to the main devices which needs time and proper scrutiny.

Adhering to VR present proposal, industry should be allowed to apply the accessories directly under main registered devices with the ISO & FSC and no fees under extended application to have the same IMPORT License no#.

Definition: - Definition of Accessories are to be published

No registration Fees for Accessories: - Accessories or Software are not supposed to have any dedicated dossier therefore, no technical review/assessment is required and always to be treated as an accessory to main device. Therefore, No registration fees must be levied on the industry. It is well justified that Accessories, software are **always to be approved without any Product or site registration fees.**

No VR Reg. No: - # Once Import License application have already been made mandatory to be completed by Sept' 2023 under 4 Risk Class, then no **separate VR no#** is required to print only for few months on the accessories (smallest pack e.g., screw etc.) resulting into huge monetary as well as stationary loss in printing item specific label. Anyway under MDR'2020, **post IL approval the Import License no# is to be printed mandatorily**.

VR to be put on Hold: - Again **on 03 Sept' 2020 another proposal released** by MoH classifying 24 categories under various therapeutic areas covering almost all the accessories referring to previous notification on Voluntary Registration. In that case, to avoid repeat work, MoH to be requested **to hold the specific Voluntary Registration for the time being & can be reinstated post finalisation of their Phase wise manner**. The situation is becoming more confusing because of time to time requirements coming from MoH & DCGI resulting in repetition of work for the industry.

Readiness: - The current portal of CDSCO needs improvement for uploading of documents. Training to industry is desirable. Even industry needs to be ready with the screening considering industry's huge portfolio.

1.3.21 Innovation in Medical Devices

Industry seeks appropriate mechanisms for recognition and reward of innovations including incremental innovations in the medical device sector w.r.t pricing, procurement and regulations. Continuous Improvement & Innovations including incremental innovations are an integral part of the medical device products development and therefore, in order to bring more investments in medical device innovations leading to Make in India. Industry recommends for setting up term of reference for recognition of innovations including incremental innovations.

1.4 Probable Opportunities/Tailwind

1.4.1 Make in India

NITI Aayog, the think tank body of the Government of India, has started working out a roadmap for the promotion of medical equipment manufacturers in the country. The government has also allowed 100% foreign direct investments (FDI) in companies manufacturing medical devices through the automatic route. The Indian government has already chalked out plans intending to remove all roadblocks and offer tailor-made solutions to attract investment to make India a manufacturing hub for medical devices.

Medical device manufacturing comprises of five broad segments, including patient aids like pacemakers and hearing devices, dental products like braces and dentures, MRI and other diagnostic machines, prosthetics like knee implants and artificial joints, and disposal & consumables like needles and syringes.

Under initiatives like Make in India, several state governments have taken up the onus of setting up medical device manufacturing parks in their respective states and have got the approval from the Government of India to do so. There would be six medical devices manufacturing clusters in the country in states like Andhra Pradesh, Kerala, Telangana, Tamil Nadu, Maharashtra, and Sikkim. These clusters would provide a huge boost to domestic manufacturing of high-end medical devices at a lower cost and significantly enhance job creation. Setting up of drug parks and Medical Devices Park will reduce the country's import dependency significantly. In order to encourage domestic production of critical APIs (Active Pharmaceutical Ingredients)/KSM (Key Starting Material) and medical devices, Union Cabinet on 12 March 2020, has approved a scheme for development of three bulk drugs and four medical devices parks in which Government of India will give incentive to States with a maximum limit of 1000 Crore rupees per bulk drug park and 100 crore rupees per medical device parks. Meanwhile, in view of the situation arising out of the COVID-19 pandemic, an additional allocation of 40 thousand crore rupees has also been made for the Mahatma Gandhi National Rural Employment Guarantee Scheme during this financial year.

1.4.2 “New Production Incentive Scheme” for Promoting Domestic Manufacturing of Medical Devices

The scheme was launched by Department of Pharmaceuticals. Implementation of scheme will be carried by a Nodal Agency and a high-powered committee of Secretaries will review the applied proposals of the companies. The company has to invest a minimum of INR180 crores in their plants in India in over 3 years in the targeted segments such as Cancer care, Radiology & Imaging Medical devices implantable electronic devices like Pacemakers, Cochlear implants, etc. and Renal Care medical devices. The Scheme shall provide incentive of 5% on incremental sales of goods manufactured in India covered under target segments. Incentive will be provided by government for a period of 5 years.

1.4.3 Ayushman Bharat Pradhan Mantri Jan Arogya Yojna (AB-PMJAY)

Ayushman Bharat - Pradhan Mantri Jan Arogya Yojana a flagship scheme of Government of India was launched as recommended by the National Health Policy 2017, to achieve the vision of Universal Health Coverage (UHC). This initiative has been designed on the lines as to meet SDG and its underlining commitment, which is "leave no one behind". AB-PMJAY provides health cover up to INR5 lakh per family per annum for secondary and tertiary care hospitalisation to around 10.74 crore poor and vulnerable families (approx. 50 crore individuals) based on the deprivation and occupational criteria per the Socio-Economic Caste Census. Ayushman Bharat is an attempt to move from sectoral and segmented approach of health service delivery to a comprehensive need-based health care service. Ayushman Bharat aims to undertake path breaking interventions to holistically address health (covering prevention, promotion and ambulatory care), at primary, secondary and tertiary level. Ayushman Bharat adopts a continuum of care approach, comprising of two inter-related components, which are -

- Health and Wellness Centers (HWCs)

- Pradhan Mantri Jan Arogya Yojana (PM-JAY)

Key Updates in the year 2019:[i]

- As of September 2019, it was reported that 18,059 hospitals have been empanelled, over 4,406,461 lakh beneficiaries have been admitted and over 10 crore e-cards have been issued.
- Recently, The National Health Authority has issued new revised packages & price list of 1557 procedures that includes cost of medical devices under Ayushman Bharat Part 2. Prices of some old procedures have been reduced while many new have been added.
- The Health Ministry has released INR3,520 crore in last two years to states under the Ayushman Bharat scheme
- Ayushman Bharat scheme covers 50 crore poor and vulnerable people in the country and provides a health assurance cover of INR5 lakh per family per year for secondary and tertiary care for serious and catastrophic illnesses.
- While 21,000 centres are already operational, close to 20,000 are set to be added within the next six months

1.4.4 Health Technology Assessment

The HEALTH TECHNOLOGY ASSESSMENT BOARD ACT 2019 has been issued by the Government of India to be it enacted by Parliament in the Seventieth Year of the Republic of India. The respective chapters and sections/sub-sections appropriately reflect the purpose and the objective of the title. A more vivid representation of amalgamation of professionals in the field of health economics outcomes research/pharmacogenomics practitioners would ensure translation of the therapies into patient outcomes based on the value of the novel and innovative research based drugs and devices, which is the need of the hour for a low and medium income country like India. Pertinent and crystallised comments have been mentioned section-wise below to aid informed clinical and health policy decisions by the board.

The following considerations would help to make the overall HTA process inclusive and participative.

- A working group approach would enable an eclectic mix of practitioners from industry, KOLs and patient group representatives providing crucial inputs at decisive steps of HTA development.
- Practitioners from industry must be involved as they can contribute to the HTA analyses by providing crucial inputs at decisive steps of HTA development.

1.4.5 Capacity Building

- Continuous skill development of regulators for new and changing regulations
- For new hires, a better induction and process training modules should be adopted in partnership with EBG Federation with EU regulators.
- Training programmes should be delivered by EU regulators on upcoming EUMDR to avoid any impact on current registrations.
- Training of BIS on harmonising their standards to International standards & implementation of same for local manufacturers.

1.5 Critical challenges, Needs and urgent requirements for Medical Devices

i. A draft Medical Devices Act, including IVD, has been prepared, but not finalised. It is critical to invite healthcare, Medical devices, Medical equipment's and IVD companies inputs on the final version of the proposed Act followed by adoption and implementation to ensure clarity. Oversight of the Act to be under the domain of the CDSCO (or a similar body) in view of their in depth understanding of the subject.

ii. In India healthcare and more specifically *In-vitro* diagnostics is "out-of-pocket" expense, which means a majority of the population pays for their diagnostic tests. Though the government has launched an excellent programme through the Ayushman Bharat initiative and public sector/some private organisations sponsor healthcare expenses for their employees and family, there is a need to expand coverage under Ayushman Bharat, introduction of affordable national insurance system or a system of reimbursement.

iii. In AB-PMJAY, the present package rates are significantly less than market price and may pose challenges in synchronous and universal implementation of the scheme. Moreover, absence of diagnosis related groups (DRGs) could make introduction of Innovative technology in AB-PMJAY difficult.

iv. If TMR is extended for other categories of devices, will severely hamper- launch of innovative devices. Further, the calculation of the TMR should be calculated from PTT onwards only and not from landing cost.

v. Any attempt to implement the PPO rule will be disruptive to patient treatment and/or will result in procurement of devices with monopolistic cost escalation of the devices.

vi. Medical devices should be exempted from Legal Metrology (LM) as in the past. All Medical devices comply with the principal Act (D & C Act 1940. Having another parallel Act of LM will complicate the labelling & create confusion. Further LM should not disregard the globally acceptable symbols of DOM/DOE. Also inserting information in a particular font size inserting will make the country specific labels too big which may affect sterility & hide information.

vii. The government should withdraw the penalty amount which has been imposed on Med Tech. companies through the overcharge notices. The Annual Report 2017-18 of the "DOP" - Department of Pharmaceuticals laid down in the Parliament, also states that Medical Devices are very different from Drugs. Since the scope of DPCO, 2013 is restricted to "formulations" as defined in Para 2 (1) (i), which means a medicine processed out of or containing in one or more drugs, notified medical devices, can under no circumstances be considered as a medicine, till the circular of NPPA dated 15 February 2015, as it does not fall within the definition of "formulation" and consequently considering it as a Non-Scheduled formation is contrary to DPCO, 2013 and NPPP-2012.

viii. The challenge for the regulation of roadmap of medical devices would be the SUGAM Online Portal as well as document requirement guidelines. Regulating the products class wise would be preferable instead of regulating everything as this may lose visibility on high risk products

ix. The patients need to be compensated on the outcome of the adverse event, caused due to faulty medical device ONLY after the causality is established by an expert group.

x. BIS should continue to work as a body for making standards and should not be tasked to act as a regulator for medical devices. CDSCO should continue to regulate Medical devices.

xi. The inclusion of New Medical devices, diagnostics & equipment's in the New National List of Essential Medicines (NLEM) 2019 which is being prepared by ICMR should be done after taking appropriate inputs from manufacturers/importers of Medical devices, Medical equipment's and IVD companies before the final version of the proposed list is published by Ministry of Health & Family welfare.

xii. The amendments made in the New Drug Price Control Order (DPCO) 2019 which is being prepared by DOP should be done after following appropriate guidelines & inputs from Medical technology companies.

xiii. The country faces a scarcity of trained personnel equipped to operate and interpret newly developed solutions available in the market.

xiv. Taxation and customs duty for Medical devices & diagnostics products are high varying between 5% and 28%, leading to a higher price for life saving tests. This needs to be rationalised and customs duty reduced. Further customs duty on spare parts is even higher and has to be reduced.

xv. While the NEDL list has been developed there is a need to finalise and circulate the list to all healthcare providers in order to ensure efficient implementation

xvi. In order to increase local development and manufacture tax benefits for R & D are essential.

xvii. Awareness and acceptance of the need for quality diagnostics among government, policy makers, Clinicians, hospital administrators and patients is a crucial element of the mix

xviii. There should be clarity regarding legal metrology for medical device. It should be aligned per schedule and non-schedule drugs, and not be applicable for medical devices

xix. For price monitoring, NPPA should exempt equipment's which are in B2B category. It should only be applicable for B2C category product

xx. Provision for checklist of product approved as Medical Device in country of origin but covered under the definition of drug in the country

In conclusion, Medical devices & equipment's along with *In-vitro* Diagnostics are one of the most powerful weapons of defence and offence against disease and better health for all. The time for widespread adoption is now.

We expect to seek a stable policy environment in India, both on the regulatory and pricing front, so that the companies can then focus on "serving patients".

2 *IN VITRO* DIAGNOSTICS

2.1 Background

According to the Medical Device Rules, 2017 besides others granting the import license requires:

A. Clinical performance evaluation **for new in vitro diagnostics medical devices Class B, C and D** which **do not have an Indian predicate device** and are not **registered in one of a GHTF country** (FSC available) and/or **has not been marketed for at least two years** in that country and/or there is evidence or theoretical possibility, on the basis of **existing knowledge, of any difference in the behaviour and performance in Indian population** (please refer to Annex 1 for the decision tree when clinical performance evaluation is required)

B. For importing products

- **Local Batch testing** is required for in vitro diagnostics medical devices s**pecified for 20 disease categories listed in PE guidance document per** the proviso of Clause (h), Paragraph (ii), part II of Fourth Schedule of Medical Devices Rules 2017, where in, it is stated that "In case of in-vitro diagnostic medical devices, performance evaluation report by the manufacturer shall be submitted by the applicant.

This creates hurdles for ease of doing business and launch of cutting-edge technologies for Indian Patients in a timely manner.

2.2 Purpose

Industry wishes to bring state of the art diagnostics solutions to India; an endeavour towards timely availability of assays for the patient and disease management.

The following document summarises industry challenges with regards to current MDR 2017 pertaining to performance evaluation and local testing and give proposals how to ensure safety and performance of Medical Devices-IVDs without requiring local clinical performance evaluation and local testing.

2.3 Definitions according to the Medical Device Rules, 2017:

- **"new *in vitro* diagnostic medical device"** means any medical device used for *in vitro* diagnosis that has not been approved for manufacture for sale or for import by the Central Licensing Authority and is being tested to establish its performance for relevant analyse or other parameter related thereto including details of technology and procedure required.
- **"predicate device"** means a device, first time and first of its kind, approved for manufacture for sale or for import by the Central Licensing Authority and has the similar intended use, material of construction, and design characteristics as the device which is proposed for license in India;

- **“Clinical performance evaluation”** means the systematic performance study of a new *in vitro* diagnostic medical device on a specimen collected from human participants to assess its performance.
- **“performance evaluation”** in relation to *in vitro* diagnostic medical device means any systematic investigation by which data is assessed and analysed to establish or verify performance of the *in vitro* diagnostic medical device for its intended use

2.4 Challenges

2.4.1 Organisation

Clinical Performance Evaluations and local testing of such a wide range of portfolio might cause problems in proper implementation of technology by testing sites which would be difficult to control by the organisations. This would lead to delays.

2.4.2 Samples

2.4.2.1 Availability

The vast portfolio may not have sufficient patient samples at testing sites/hospitals/MDTLs for clinical performance evaluation for each and every test. Getting human tissue samples required for clinical performance evaluation and local testing would be extremely difficult and, in some cases, impossible for Institutions/Hospitals/Labs.

2.4.2.2 Hurdles with Samples

- Selection of samples (random)
- Integrity, stability and control of the samples
- Volume of samples
- Process of sample handling is not always controlled
- Panels are sometimes from processed samples (e.g. Diluted)
- Samples are not always well characterised to understand/explain discrepancies or product deficiencies
- Untrained lab personnel or not enough personnel
- Appropriate storage of products and samples

2.4.3 Costs

For performing the evaluation, Free of Cost materials are to be provided to the labs. There are no set guidelines for sample size criteria and different labs may ask for different kit sizes (number of tests) for evaluation. Performing PE for large number of parameters as covered in Medical Device Rules, 2017, will lead to exponential increase of such Free of Cost materials/tests (multiple Free of Cost reactions for each parameter) putting a financial burden on our organisation in addition to the test license fee, fees to the lab, cost of placing the instrument/analyser at the site which in Lakhs to crores of rupees. All samples of varied disease area might not be available at one single testing centre. If each of the tests is to be evaluated for the performance, individual instruments, costing multiple Lakhs to Crores, will be required to be placed at multiple sites which will increase the cost and lead to financial burden increasing exponentially. The will lead to the situation where viability of introducing an assay will be low or economically viable only at a high cost. The financial considerations may force the organisations either not to introduce the assay or introduce the assay at high cost in turn affecting the disease management decisions for patient population.

2.4.4 Placing Instruments

Most diagnostics instruments can test multiple parameters catering to varied diseases & preventive care thereby optimising the instrument output, best economies of scale and maximising laboratory efficiencies. Placing such large instruments ONLY FOR PERFORMANCE EVALUATIONS/LOCAL TESTING of dedicated parameters which the institutes specialise in would not be meaningful for the institutes (testing centres) nor the Diagnostics service providers (Industry). Placing the instrument itself is a challenging and an uphill task due to multiple reasons:

- Many Labs are autonomous, and they cannot be persuaded for performing the evaluation as the same does not fall under their mandate. Further they are not directly involved in fulfilling such regulatory guidelines. Labs ask to know what is in for them for conducting the PE exercise.

- Even if persuaded, labs ask the organisations like ours to provide a letter from CDSCO addressed directly to the Directors of the institutes for starting any such evaluation which will be scrutinised in-house by the lab administration. It may even go to their ethical committee as the centres might require ethical approvals for using patient samples.
- The Performance Evaluation/Local Testing further warrants placement of the instrument not ordered by the lab and not part of their inventory. A complete set of mechanism is to be established by lab to take such placements. At times, space constraint is a limitation for conducting such PE and most institutes would not allow placing the instrument for just evaluation of parameters. Institutes would prefer to allow instruments for evaluation, if they can use for routine testing also, and not only for purpose of evaluation.
- Given the vast geography, Indian health sector is a tiered set up where the patients are spread across the country. Many of the global set ups work on centralisation for diagnostics testing. This global model has led to evolution of high throughput cutting edge instruments offering multiple parameters on same platform. These platforms are prime importance to private diagnostic chains in the country where the instruments can be viably placed.

2.4.5 Time

As the application of test licenses also requires mentioning the number of kits, it will take months to get the kits on an agreed testing site, commercial viability and sample size leading to the delay in launch of critical state of art cutting edge technologies for better patient outcomes.

2.4.6 Lot Availability

Lots availability at a time on account of Global manufacturing Bottlenecks/Scale Up requirements could be an additional factor leading to delays in product availability for customers.

2.5 Impact on Indian Patient Population

The vast portfolio may not have sufficient patient samples at testing sites/hospitals/MDTLs for clinical performance evaluation for each and every test thereby delaying and probably restricting the accessibility of advanced test for the Indian patient population.

- Health Economic will be affected
- Patient who need the Medical device will be affected
- Delay and probably restricted access of advanced test for the Indian patient population.
- These IVDs might not be available in the Indian market as no samples will be available for conducting PE and the PE cannot be completed.
- Delay in launch of state-of-the-art diagnostics solutions for the Indian populations stemming from difficulty of doing business and high costs of launching a product.
- Higher price for patients
- Cutting Edge Technologies/ Products which are not manufacturer in India will get blocked for the Indian Population. For Example: Tissue Diagnostics Portfolio, EGFR, BRAF & KRAS amongst many other Industry products.

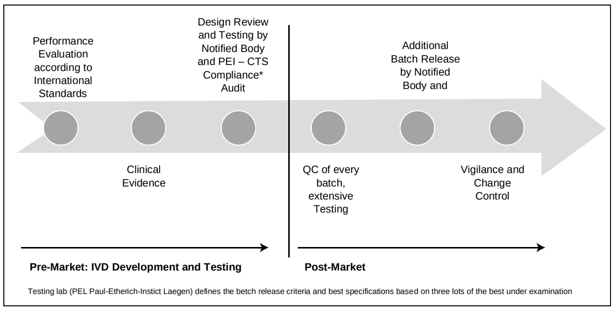
2.6 Points to Consider: Justification for Waiver of Performance Evaluation/Local Batch Testing of IVD Products

2.6.1 Testing and Validation of IVD Medical Devices by the Manufacturer

In order place products into the EU market, Industry has to fulfil the European regulations. The EU regulations states:

The 'manufacturer' or authorised representative, as the legal entity in Europe, must ensure that the device meets the essential requirements specified in the EU regulations and follow the appropriate conformity assessment procedure. The essential requirements assure, the safety, suitability and performance of a medical device as well as to take care of health and required protection of the patient, user or third party. The essential requirements assure, the safety, suitability and performance of a medical device as well as to take care of health and required protection of the patient, user or third party. It is the responsibility of the manufacturer to test and control the product to the highest standard and to maintain its quality per the intended use. Any discrepant testing results must be documented and evaluated as a part of the quality management system, risk assessment and the Post-Market-Surveillance Requirements and data submitted tom the regulatory authorities. Manufacturer ensures that the device meets the essential requirements specified in the Medical Device Rules 2017 and follow the appropriate conformity assessment procedures. Further the Safety and effectiveness of the device are ensured through product, process design, product validation, process and manufacturing controls, finished product testing and Post market surve illance as laid down in these rules.

Referenced below is the example of the route followed in EU for IVDs



- Performance Evaluation according to International Standards
- Clinical Evidence
- Design Review and Testing by Notified Body and PEI – CTS Compliance and Audit
- QC of every batch, extensive Testing by Manufacturer
- Additional Batch Release by Notified Body
- Vigilance and Change Control

2.6.1.1 Performance Evaluation

Performance Evaluations are done according to the international standards. All custom platforms are validated and verified. Analytical/ Performance Evaluation explores all aspects of the assay performance e.g.:

- Precision, including repeatability and reproducibility
- Analytical sensitivity: Limits of blank, detection, quantitation
- Analytical specificity and interference
- Linearity of quantitative and semi-quantitative assays
- Stability of samples, calibrators, controls; real time vs accelerated; on-board vs storage vs opened/prepared samples
- Matrix comparison
- Method comparison Measuring range, reference range
- Software for instrument and algorithm

2.6.1.2 Clinical Performance Evaluation

Clinical evaluation is done according to international standards and clinical evidence is generated. Depending upon the classification, design review and testing is done by the notified body. Notified body further inspects product development and design. Post Marketing includes QC release both in house and by the notified body.

2.6.1.3 External Review and Testing

Depending on the classification design review and testing by notified body is done. Notified body inspects product development and design.

2.6.1.4 Internal QC Testing

During manufacturing extensive QC testing is done

- Product inspection and testing during manufacturing and use to uncover defects
- Procedures used in each assay to assure a test run is valid and results are reliable e.g.:

a. Kit Controls – the negative and positive control provided with the kit; used to validate the test run

b. Quality Control Samples

c. Should be treated in the exact same manner as test samples

2.6.1.5 Post Market Surveillance

Post Market Surveillance (Change Management and vigilance process in place)

2.6.2 Product Risk Classification

Class B Products are defined as **low moderate risk.**

(b) An in vitro diagnostic medical device referred to in clause (a) shall be assigned to Class B, if it is intended to be used to obtain, -

(1) test results that are not for the determination of a medically critical status; or

(2) preliminary test results which require confirmation by appropriate laboratory tests.

Due to the classification low moderate risk of Class B Medical Devices/IVDS, data on clinical performance evaluation may not be necessary, unless scientifically justified and considered necessary depending on the nature of the medical device.

2.6.3 Requirements in other countries

Nearly all regulated countries worldwide such as United States, EU , Japan, Australia, Canada, Singapore, Malaysia, Korea, Taiwan, Vietnam, Thailand, Indonesia, Mexico, Saudi Arabia, etc. do not require local clinical performance evaluation and local Testing of IVDs specified. For the products having GHTF country regulatory approval and FSC requirement of PE in India Is re-inviting the wheel.

2.7 Proposal

- **Waiver of local batch testing for IVDs Waiver of clinical performance evaluation Class B, Class C and Class D products**

Unless scientifically justified and considered necessary depending on the nature of the medical device

- Acceptance of Performance Evaluation and QC testing done by the manufacturer and acceptance of the performance evaluation report and Certificate of Analysis generated by the manufacturer and/or notified bodies/reference labs in the country of origin.
- Acceptance of product approval in GHTF countries who already reviewed and evaluated the performance evaluation and safety of the product.
- Post Registration Evaluation

Authority review

- Review of the analytical performance data, clinical evaluation data and the final analysis and report give a good understanding of reliable results or a good study management
- Ask questions and challenge the manufacturer on their results, if needed
- Ensure an effective Post-Market-Surveillance, Vigilance Reporting System and Change Management System
- Implement an External Quality Control Schemes (EQAS) in your country (supports to increase the lab quality)
- Consider audits of the manufacturing sites

2.8 Benefits

- Patients have early access to new diagnosis of diseases or conditions
- Patients have early access to improved assays
- No extra resources for capacity building
- No extra resources for lab personnel
- More time on on-market potential issues and post market surveillance

2.9 Points for In-Vitro Diagnostics (IVDs) FY-2020

Medical Device Amendment Rules 2020

Background:-*In-vitro* diagnostic market is broadly divided into equipment, analysers reagents, software and services. The service sector is largely unorganised, with a large presence of players located at the regional or city level. IVDs are regulated vide Medical Device Rule 2017 under Drugs and

Cosmetics act 1940. On 11th Feb 2020, Ministry of Health and Family Welfare (MoHFW) issued **Medical Devices (Amendment) Rules 2020 vide** S.O. 648 (E) & G.S.R. 102 (E) for regulating medical devices and IVDs in phased manner. MoHFW has an objective to create a database of all medical devices and IVDs currently manufactured/imported in the country so that safety, quality and performance of non-notified Medical Devices & IVD can be monitored

- **S.O. 648 (E)** - **Expansion of "Medical Devices" definition**: - *All devices including an instrument, apparatus, appliance, implant, material or other article, whether used alone or in combination, including a software or an accessory.*
- **G.S.R. 102 (E) -** *A new Chapter IIIA related to "Registration of certain medical devices" has been inserted in the Medical Devices Rules, 2017*.

Central Drug Standard Control Organisation (CDSCO) on 3rd Sep 2020 issued Risk based Classification for registration of IVD Instruments, Analysers and Softwares under Medical Device Amendment Rules, 2020. Industry has been provided 30 days' time to provide comments.

It is a welcome move for bringing every devices and IVDs under ambit of regulations so that substandard devices and IVDs can be restricted. The list-based approach will also help manufacturers and importers easily classify their Medical Devices/IVDs, by referring to the CDSCO's classification list. ***However, the classification proposed by CDSCO for various categories of IVD analyser, instrument or software does not harmonise with global guidelines /regulations like IMDRF, EU or USA risk class. These guidelines/regulations classify the analysers as risk class A expect for point of care and self-testing products, whereas CDSCO has classified every analyser based on the diagnostic test performed on them.*** The different approach in the risk class of these instruments and need to comply with the higher-class requirements would require manufacturers and importers to submit exhaustive data/document adding unnecessary resource burden and additional time to market products.

Additionally it is to be noted that the proposed classification list by CDSCO does not match with the fundamentals laid down in the form classification rules: Part II Rule 2 sub-rule (v) clause 2 of the MDR 2017, quote-"an instrument intended specifically to be used for an *in vitro* diagnostic procedure should be Class A". Considering the rationale stated above we request CDSCO to reconsider the risk classification of IVD instruments and harmonise it with its own regulatory guidance MDR 2017 and global guidance like IMDRF.

3 Pre-natal Diagnostic Test (PNDT) Act

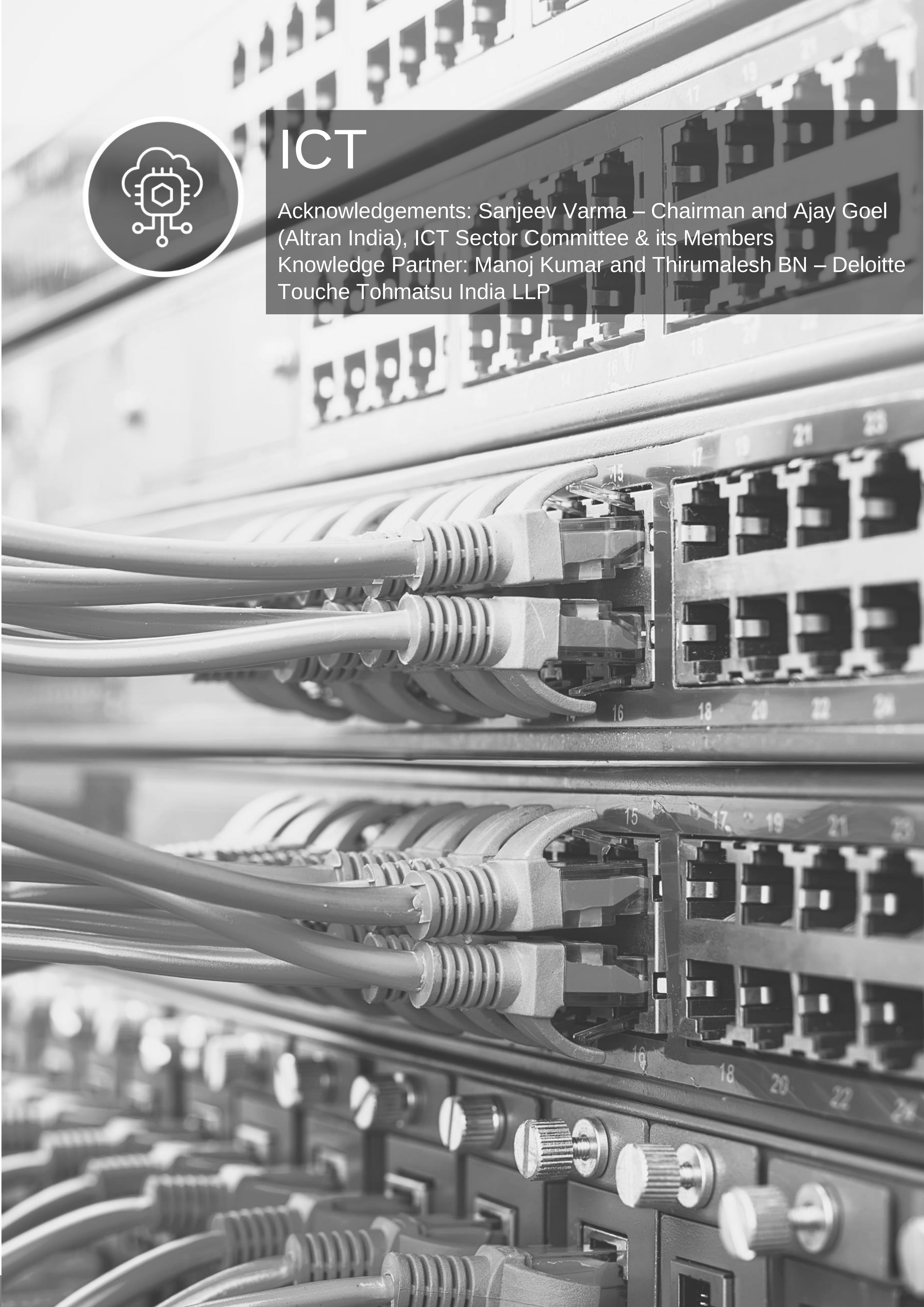
In India Health is a state subject. Hence implementation is at State level whereas Act is enforced by the Central Government. We are facing enormous issues as different states have different implementation rules and business is being hampered due to this. Earlier only Ultrasound was included in this Act but now they have extended it to all Imaging equipment which can detect sex of the foetus like CT & MRI etc.

Our demand to avoid all these state-wise interpretations is to have one ePNDT portal across India. We have made various representations but still no concrete outcome yet.

ENDNOTE

1. https://economictimes.indiatimes.com/industry/healthcare/biotech/healthcare/released-rs-3520-crore-in-last-two-years-to-states-under-ab-pmjay-health-minister/articleshow/73933662.cms?from=mdr

NOTE



ICT

Acknowledgements: Sanjeev Varma – Chairman and Ajay Goel (Altran India), ICT Sector Committee & its Members
Knowledge Partner: Manoj Kumar and Thirumalesh BN – Deloitte Touche Tohmatsu India LLP

EXECUTIVE SUMMARY

Direct tax

The Budget 2020 was expected to bring rationalisation in various areas such as equalisation levy, rationalisation of rate of taxes for small and medium industries (SMEs), etc.

The following areas are required to be addressed:

- Harmonisation of capital gain tax rates for start-
- Rationalisation of TDS mechanism on service charges retained by e-commerce companies.
- Tax credit of equalisation levy (EL) available to a foreign company in home country.
- Clarity on secondment of employees by a foreign company resulting in constitution of permanent establishment (“PE”).
- Benefit of carry forward losses for IT-sector companies.
- Initiation of penalty proceedings under section 271(1)(c)//270A and 271C of the IT Act.
- Amendment to Indirect Transfer Rules.
- Amendment to source rules for business connection
- Amendments to exemption to non-residents from filing of income tax return

Indirect tax

There have been no announcements in the Budget from an indirect tax perspective on account of the following:

- All goods and sales tax (GST) related amendment-making powers are with the GST Council. While there may not have been any changes in the Budget, the GST Council has made several announcements in the last 21 months addressing substantive/legal as well as procedural issues for smooth implementation of GST. The active involvement of the GST Council to iron out issues under GST has been well received and appreciated by the industry. However, there may still be a few areas (at present) that need to be addressed, which include:
- Allow refund of GST paid on capital goods when used in export/zero-rated supplies.
- Employee benefit expenses should be out of GST.
- Issue suitable clarification on requirement to cross charge salary cost of employees at head office to branch offices.
- Mere cost allocation between HO and BO should be treated as supply and input tax credit reversal is not required.
- Upfront IGST exemption for import of capital goods by EOUs/STPIs should be extended without any time limit.

1. INTRODUCTION

Information Technology (IT) and Information Technology Enabled Services (ITeS) including Business Process Management (BPM).[1]

1.1. Market Description

The global sourcing market in India continues to grow at a higher pace compared to the IT–BPM industry. India is the leading sourcing destination across the world, accounting for approximately 55% market share of the US$185–190 billion (€164.07–168.51 billion) global services sourcing business in 2017–18.

Indian IT and ITeS companies have set up over 1,000 global delivery centres in about 80 countries across the world.

India has become the digital capabilities hub of the world with around 75% of global digital talent present in the country. India's IT and ITeS industry grew to US$181 billion (€160.53 billion) in 2018–19.

Exports from the industry increased to US$137 billion (€121.50 billion) in FY2019 while domestic revenues (including hardware) advanced to US$44 billion (€39.02 billion). Spending on IT in India is expected to grow over 9% to reach US$87.1 billion (€77.25 billion) in 2018.

Revenue from digital segment is expected to comprise 38% of the forecasted US$350 billion (€310.42 billion) industry revenue by 2025.

Indian IT's core competencies and strengths have attracted significant investments from major countries. Having proven its capabilities in delivering both onshore and offshore services to global clients, leading Indian IT firms are diversifying their offerings and showcasing leading ideas in blockchain and artificial intelligence to clients using innovation hubs and research and development centres in order to create differentiated offerings and new opportunities.

1.1.1. IT hardware

Demand for electronic products in India is poised for significant growth in the next few years, driven by a strong economic outlook.

The Indian electronics and hardware market grew by 8.6% year-on-year (YoY) to reach US$75 billion (€66.51 billion) in 2015, driven by rising local demand and growing disposable incomes. It is expected to grow at a compound annual growth rate (CAGR) of 13–16% during 2013–18 to reach US$112–130 billion (€99.33–115.29 billion) by 2018.

Though India's electronics and hardware industry is growing at a robust rate, a majority of the demand is met through imports.

Around 50–60% of the demand for electronic products is fulfilled through imports, while nearly 70–80% of the electronic components market is imports dependent. In order to curb imports, the Government of India has identified and treated the electronics sector as a priority under its Make in India programme.

This scheme promotes manufacturing in India to boost job creation and skill enhancement, facilitate investment, foster innovation, protect intellectual property, and build a best-in-class manufacturing infrastructure/landscape in the country. This has resulted in various Indian and global manufacturers announcing their expansion plans.

1.1.2. Telecommunications

India is currently the world's second-largest telecommunications market with a subscriber base of 1.20 billion and has registered strong growth in the past decade and half. The Indian mobile economy is growing rapidly and will contribute substantially to India's gross domestic product (GDP), according to a report prepared by GSM Association (GSMA) in collaboration with the Boston Consulting

Group (BCG). As of January 2019, India has witnessed a 165% growth in app downloads in the past two years.

The liberal and reformist policies of the Government of India have been instrumental, along with strong consumer demand, in the rapid growth in the Indian telecom sector.

The Government of India has enabled easy market access to telecom equipment and a fair and proactive regulatory framework that has ensured availability of telecom services to consumers at affordable prices. The deregulation of foreign direct investment (FDI) norms has made the sector one of the fastest growing and a top five employment opportunity generator in the country. With 560.01 million internet subscribers, as of September 2018, India ranks as the world's second largest market in terms of total internet users. Further, India is also the world's second largest telecommunications market with 1,197.87 million subscribers, as of December 2018 and of importance to note, in 2017 India surpassed the United States of America (USA) to become the second largest market in terms of number of app downloads. The country remained as the world's fastest growing market for Google Play downloads in the second and third quarters of 2018. Over the next five years, rise in mobile-phone penetration and decline in data costs will add 500 million new internet users in India, creating opportunities for new businesses.

1.1.3. R&D and innovation

The research ecosystem in India presents a significant opportunity for multinational corporations across the world due to its intellectual capital available in the country.

Legions of Indian engineers working across the globe highlight the highly trained manpower available at competitive costs. Consequently, several multinational corporations (MNCs) have shifted or are shifting their research and development (R&D) base to India. These R&D bases either develop products to serve the local market or help the parent company overseas deliver new innovative generation of products faster to the markets across the world.

India's engineering R&D (ER&D) globalisation and services market reached US$22.3 billion (€19.77 billion) in 2016 and is set to rise to US$38 billion (€33.70 billion). India accounted for 40% (US$13.4 billion [€11.88 billion]) of the total US$34 billion (€30.15 billion) of globalised engineering and R&D in 2016. India has a total of 25 innovation centres in the country and has been ranked as the top innovation destination in Asia and second in the world for new innovation centres. The country accounts for 27% of Asia's new innovation centres. India moved up to the 60th position in the 10th edition of Global Innovation Index (GII) in 2017 and will likely get into the list of the top 25 nations in the next 10 years.

India ranks second amongst the countries with highest increase in contribution to high-quality scientific research. India-based R&D services companies, which account for almost 22% of the global addressed market, grew much faster at 12.67%.

The market for ER&D companies in India is mainly structured across pure play PES companies such as Cyient, QuEST, eInfochips and the larger IT companies with a PES play such as Wipro, TCS, and HCL. India's ER&D services market is expected to reach US$15–17 billion (€13.30–15.07 billion) by 2020 and

North America continues to be the largest market contributing to 55% of revenues.

With the Government of India's support, the R&D sector in India is all set to witness some robust growth in the coming years. India is also expected to witness strong growth in its agriculture and pharmaceutical sectors as the Indian government is investing large sums to set up dedicated research centres for R&D in these sectors. The Indian IT industry is also expected to add to the development of the R&D sector.

1.2. Recent Developments

The last couple of years have seen invigorated efforts in measures by the Indian government to encourage and promote the ICT sector in the country.

Some of the key initiatives include the following:

1.2.1. National programme on artificial intelligence

In the Interim Budget 2019–20, the Government of India announced plans to launch a national programme on artificial intelligence and setting up of a National Artificial Intelligence Portal. The Finance Minister in his budget speech announced that nine priority areas had been identified.

1.2.2. Digital India

The vision of the Digital India programme is to transform India into a digitally empowered society and knowledge economy. The Digital India programme is centred on three key vision areas, i.e. Digital Infrastructure as a Utility to Every

Citizen, Governance and Services on Demand, and Digital Empowerment of Citizens.

The Finance Minister in his budget speech announced that India is now leading the world in the consumption of mobile data. Monthly consumption of mobile data increased by over 50 times in the last five years. The cost of data and voice calls in India is now possibly the lowest in the world. More than 3 lakh Common Service Centres (CSCs) employing about 12 lakh people, are digitally delivering several services to the citizens. The CSCs are expanding their services and also creating digital infrastructure in the villages, including connectivity, to convert the villages into Digital Villages.

The Government of India will make 1 lakh villages into Digital Villages over the next five years[5]. The Government of India is planning to launch an initiative to bring 'digital boards' as a part of a larger initiative, promising an investment of `90 billion (€1.14 billion) in state-run schools and colleges.

In the Union Budget, 2018–19, the Indian government had allocated `3,073 crore (€391.55 million) for the Digital India programme. As per the Budget implementation report, on 06.12.2018, the Government of India approved the National Mission on Interdisciplinary Cyber-Physical Systems (NMICPS) at a total outlay of `3,660 crore (€466.34 million) for a period of five years[6].

Budget 2020*: There has been also mention of widespread digitisation as fibre to home will link over 1,00,000-gram panchayats during the Financial Year (FY) 2020-21 through BharatNet. The government has allocated INR6,000 crore for this initiative. Besides, the budget has also allocated INR8,000 crore to set up National Mission on Quantum Computing and Technology.*

1.2.3. Start-up India

Start-up India is a flagship initiative of the Government of India, intended to build a strong ecosystem that is conducive for the growth of start-up businesses, to drive sustainable economic growth, and generate large-scale employment opportunities. On 19 February 2019, the Finance Minister announced that to provide relief to and boost investments into start-ups in India, the Indian government has decided to widen the definition of 'start-up' and simplify the process of getting approval for exemption.

The key modifications *inter alia* suggested by the Finance Minister include the following:

- An eligible entity shall now be considered to be a start-up for up to 10 years from the date of incorporation/registration as against the existing duration of seven years.
- An entity will also be considered a start-up if its turnover for any of the financial years since its incorporation or registration does not exceed `100 crore (€12.74 million) as against the existing limit of `25 crore (€3.18 million).
- Consideration received by eligible start-ups for shares issued or proposed to be issued by all investors shall be exempt up to an aggregate limit of INR25 crore (€3.18 million).

1.2.4. Make in India

India's IT & BPM sector can benefit from the policies and infrastructure provided by the Make in India initiative. Under Make in India, mobile and parts manufacturing companies have increased from two to more than 268 providing huge job opportunities. Through this initiative the Centre of Excellence for Internet of Things has been set up in Bengaluru. It has a capacity to incubate 40 start-ups and focuses on building solutions for applications such as agriculture, automobile, telecom, healthcare, and consumer goods. The Indian government's IT/ITeS Sector Skill Council (SSC) is facilitating the expansion of the skilled workforce with the help of National Association of Software and Services Companies (NASSCOM). The Government of India has also been promoting regulatory support to protect intellectual property and strengthen cyber security laws among other things. The key six sectors which are boosting Make in India are the automotive sector, electronics system design and manufacturing, renewable energy, roads and highways, pharmaceuticals, and food processing.

2. ISSUES AND SUGGESTIONS

2.1 Corporate Taxation

2.1.1. Harmonisation of tax rates for start-up and SME companies

Issues

- The provisions of the IT Act do not specifically provide any exemption for taxability of the capital gains earned by the investors of start-up companies.
- The rate of taxation is similar to all other investors and the long-term capital gain (LTCG) is taxed at 20% and the short-term capital gain (STCG) is taxed at the slab rates.
- The investors are interested in deploying funds into new companies and ventures and also the investment made at the earlier stage are subject to higher risk.

Recommendations

- Considering the risk appetite of angel investors investing in early-stage companies, LTCG arising from sale of shares of unlisted companies should be made exempt from tax (similar to erstwhile exemption under section 10(38) of the IT Act and reduction of tax rate of STCG to 15% instead of slab rates of tax applicable on all STCG.
- Eligible investors could also be defined under the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012 of a particular category of investors.
- The above amendment would be critical for encouraging the new investors, leading to creation and growth of new start-up companies.

2.1.2. Rationalisation of TDS mechanism on service charges retained by e-commerce companies

Issues

- In Budget 2020, the TDS on e-commerce operators has been introduced, however there are certain ambiguities which are yet to be addressed and clarified by the Government.
- The applicability of the withholding tax provisions on e-commerce operators outside India is unambiguous. Further, due to existence of equalisation levy (EL) on payments made to non-resident e-commerce operators providing online marketing services and due to lack of clarity on applicability of withholding tax provisions on such non-resident operators has led to ambiguity and double levy of taxes both under withholding provisions and EL.
- In case where multiple e-commerce operators are involved, the requirement to withhold taxes may potentially apply to all such e-commerce operators, resulting in double withholding of tax on same transaction.
- E-commerce operator is defined to mean a person who owns, operates or manages digital or electronic facility or platform for electronic commerce and is responsible for paying to the e-commerce participant. It is not clear from the definition of e-commerce operator that whether it covers an entity that provides payment processing service.
- The threshold for applicability of withholding tax on e-commerce operators is very low
- Clarity on the meaning of term ‘facilitated’ by the e-commerce operators is not available.

Recommendations

- It is recommended to bring in a clarification on applicability of withholding tax provisions on non-resident e-commerce operators and clarification is to be provided that e-commerce operator should be clarified to cover only persons resident in India. The proposed withholding tax rate of 1% on the gross amount received from customers will create significant working capital challenges for e-commerce participants. Hence, it is recommended that taxes should be deducted by e-commerce operator only on the net amount which is remitted to the seller and the rate of withholding tax should be aligned to that under the proposed TCS provision i.e., 0.1%.
- It is recommended that a suitable clarification should be provided that the liability to withhold tax is that of the e-commerce operator making payment to the ultimate person selling goods or providing services to the customers, and not on other e-commerce operators.

- It is recommended the term ‘facilitated’ should be clarified to mean supply of goods or services through the digital or electronic facility or platform of the e-commerce operator, and thus should not include merely an advertisement –which redirects the customer to website of other entity/supplier.
- In view of the Government’s push for digitising payments, ambiguity on withholding tax applicability to payment processors is likely to lead to ambiguity and potential litigation. Hence, it is recommended that the definition of e-commerce operator should be clarified to exclude payment processing entities, since these merely facilitate payments much like a bank, and does not facilitate the sale of goods or provision of services.
- The threshold for applicability of withholding tax on e-commerce operators is to amended and increased appropriately to provide relief to small vendors

2.1.3. Tax credit of EL available to foreign companies in home country

Issues

- In the present scenario, all the IT companies are subject to the deduction of equalisation levy on payment made to the non-residents in relation to specified e-commerce transactions.
- The double taxation avoidance agreements entered by India with the country of residence of such non-residents does not support the claim of such credit against its income tax liability in its home country. The same has been leading to double taxation of the income in the hands of the non-residents on such income.
- Due to equalisation levy, the non-residents might increase the cost of specified services and accordingly the recipient of such services have to bear more cost for the said services.

Recommendations

- It is recommended that the government enters into agreements for credit with other countries for allowance of the EL as credit on such income being taxable in the country of residence.
- The same would contribute to Ease of Doing Business for the recipient foreign company in India.
- By providing credit of EL, the cost of services might also reduce as some service providers increase the cost of services as they are not willing to bear EL and ultimately the cost is borne by the end users

2.1.4. Clarity on constitution of service permanent establishment in India

Issues

- In the current business scenario, all the agreements entered into by an Indian company with a foreign company for secondment of employees is disputed by the income tax authorities stating that the same would constitute PE of the foreign company in India.
- Such litigations are restricting the foreign companies in deploying expatriates in the operations of the Indian company, and also in promotion of business in India through foreign investments.

Recommendations

- The government would require bringing in the clarification stating that where a secondment is purely for the benefit of the Indian company and the complete costs of the assignee is effectively borne by the Indian company, it should not constitute a service PE for the foreign company in India.
- Clarification to be brought in place to the effect that in the aforesaid scenario, reimbursement of the salary cost by the Indian company would not constitute any technical services and shall not be treated as fees for technical services.

2.1.5. Extension of benefit of carry forward of losses under section 72A of the IT Act

Issues

- In the current developing economy, many IT companies are proposing to expand their businesses through mergers with other companies in similar sector.
- However, the IT Act does not provide the benefit of carry forward of losses on mergers under Section 72A of the IT Act for IT service companies.
- The above restriction, does not provide a roadmap for encouraging the investments and mergers in the IT sector.

Recommendations

- The government should extend the benefit of carry forward of losses on mergers under Section 72A of the IT Act for IT sector companies. In order to encourage the growth in the sector, the existing beneficial provision of Section 72A of the IT Act (which are restricted to manufacturing companies (including manufacture of computer software) should be broad based and be extended to all IT services companies.

2.1.6. Initiation of penalty proceedings under section 271 (1)(c), 270A and 271C of the IT Act

Issues

- The income tax authorities are increasingly initiating penalty proceedings mechanically under Section 271(1)(c)//270A of the IT Act in respect of all additions made in the assessment order, irrespective of the favourable orders of the higher judicial forums supporting the contentions of the company.

Recommendations

- Guidelines should be issued advising the field officers that penalty proceedings should be initiated only in rare circumstances involving deliberate suppression of material facts that have a bearing on the assessment proceedings, etc.
- The Taxpayer's Charter which is proposed to be introduced by the government should incorporate conditions for initiation of penalty proceedings in relation to covered matters and also to bring in the restriction for initiation of penalty proceedings based on mere non-acceptance of a claim by the tax officers
- Interpretation issues or tax positions supported by decision of any appeal forum from Income Tax Appellate Tribunal and above should be kept outside the ambit of the penalty proceedings.

2.1.7. Amendments to 'indirect transfer' rules

Issues

- The Finance Act 2017 had introduced provisions to exempt non-residents who, directly or indirectly, hold shares or interest in Category 1 and Category II foreign portfolio investors (FPIs) registered with the SEBI under the SEBI (FPI) Regulations 2014 from applicability of the 'indirect transfer' provisions which is brought in retrospectively from Assessment Year, 2012–13.
- However, there is ambiguity with regard to 'indirect transfer' valuation rules that specify the manner in which fair market value (FMV) of assets of foreign company with underlying assets in India is to be computed.
- The rules also prescribe the information and documentation required to be maintained and furnished to the tax authorities by an Indian entity whose shares are indirectly transferred.
- Concerns that arise are as follows:
    - Conflict with Explanation 6 to section 9(1)(i) of the Act in the context of non-reduction of liabilities in respect of the shares deemed to be situated in India.
    - No clarity in relation to computation of income. Non-availability of definition of 'liabilities' in the rules. Treatment of convertible instruments like preference shares.
    - Availability of Double Taxation Avoidance Agreement (DTAA) benefits.

Recommendations

- Clarity on the term liabilities under the rules by providing specific guidance on whether operating liabilities (like current liabilities), preference share capital will be considered as liabilities in the computation of FMV.
- Clarification on reporting requirements in cases where treaty exemption is applicable.
- Clarity on filing Form 49D is required by the Indian company when there is no income accruing/arising in India on account of the indirect transfer.
- Provide specific exemptions from the indirect transfer rules for intra-group transfers, especially when the merger/amalgamation is between two foreign companies outside India.

2.1.8. Applicability of MAT on dividend income

Issues

- The cascading effect of taxation of dividend is removed under normal provisions under the Act by introduction of section 80M, however the dividend income will now be subject to MAT

Recommendations

- It is recommended to amend section 115JB to exclude dividend income received by a domestic company, if the dividend is paid by such domestic company to its shareholders on or before the due date wherein due date means the date one month prior to date of filing the return of income.

2.1.9. Abolition of buy back tax

Issues

- Levy of buy-back tax on shares bought back in the hands of the Companies

Recommendations

- As per the budget speech it is noted that the system of Dividend Distribution Tax was reintroduced since it was easier to collect tax at a single point and the new system would lead to increase in compliance burden and with the advent of technology and easy tracking system available, there was no justification for DDT. Similarly in case of Buy back tax as well, there is a reduction in rate of return on equity capital and with the advent of technology, tracking system is available and accordingly, it is recommended that buyback tax should be abolished in line with DDT.

2.1.10. Amendments to source rules for business connection

Issues

- In light of the amendment to the business connection rules, sale of goods and services using any data collected from India maybe taxable in India. Accordingly, any sale, made using data even that collected by Liaison Offices ('LO'), Independent agents may become taxable in India under the Act.

Recommendations

- It is recommended that suitable amendment be made to provide exemption from taxability, if sales are made using data collected by LO and Independent agents.
- It is also recommended that limit of INR50 lacs be provided in respect of sales made using such data.

2.1.11. Amendments to exemption to non-residents from filing of income tax return

Issues

- The proposed amendment to section 115A of the Act to provide that the income of a non-resident taxpayer consists only of interest, dividend, royalty or Fees for Technical Service ('FTS') and taxes have been withheld at the rate specified in section 115A of the Act, then non-resident taxpayer is not required to file its return of income of India.
- In case of related party transactions -while an exemption from requirement to file the tax return is provided to non-residents but no such exemption from Indian transfer pricing compliances has been granted. It could have been relaxed for foreign companies especially because the Indian related party (being one of the party to transaction) would anyways be required to undertake this compliance.

Recommendations

- The exemption in relation to obligation to file return of income should be extended to non-residents whose income has been subject to tax withholding under tax treaty, albeit at a lower rate as compared to rate prescribed under section 115A of the Act(as section 195 of the Act itself enables tax withholding at applicable rates under tax treaty).
- An exemption should be provided to the non-residents from Indian transfer pricing compliances if they are exempted to file return in India. Especially for foreign companies because the Indian related party (being the counterparty party to transaction) would anyway be required to undertake this compliance. This will further help to reduce unnecessary compliance burden on non-residents.

2.1.12. Stay from Income Tax Appellate Tribunal (“ITAT”)

Issues

- In the budget 2020, it has been proposed to mandatory minimum payment of 20% of demand for seeking stay before ITAT. In case of a covered matter of earlier years, where the tax authority has already given a judgement in favour of an assessee, paying of 20% of the amount cannot be considered as a natural justice.

Recommendations

- Accordingly, considering a principle of natural justice, it is recommended to exclude the cases of covered matters from the condition of depositing 20% of the amount of tax, interest, fee, penalty, or any other sum payable under the provisions of the Act.
- As per the Instruction No. 1914 dated 21 March 1996 read with Office Memorandum dated 29 February 2016 and dated 31 July 2017, the Assessing Officer has the power to enhance/reduce the payment of 20% of demand wherein an appeal is pending before Commissioner of Income Tax (Appeals). It is recommended that similar provisions should be introduced for stay before ITAT.

2.1.13. Prior filing of tax audit report before filing return of income

Issues

- In the budget 2020, it is proposed that tax audit report under section 44AB to be furnished by the assessees at least one month prior to the due date of filing of return of income to enable pre-filling of returns in case of persons having income from business or profession.
- It may be possible that the certain amount payable as covered under section 43B and TDS on transaction covered section 40(a)(i)//Section 40(a)(ia) is paid/deposited during interim period (after the furnishing of tax audit report but before filing of return of income). The payments made//TDS deposited during the interim period may lead to mismatch between tax audit report and return of income, hence it is possible that an addition may be made in the intimation under section 143(1)(a) causing additional compliance burden on the assessees.

Recommendations

It is recommended that:

- Suitable modification be made under section 143(1)(a) to amend definition of “an incorrect claim apparent from any information in the return” so as to specifically exclude the mismatch arising on account of payment made//TDS deposited during the interim period; or
- Suitable modification be made in return of income so as to allow separate amount of claims under section 43B//40(a)(i)/40(a)(ia) towards payments made//TDS deposited during the interim period.

2.2. GST related

2.2.1. Issues with respect to refund of GST paid on capital goods when used in export/zero rated supplies

Issues

- Refund of GST paid on capital goods where the same is used in export/zero-rated supplies is not available under the GST regime.
- Rule 89(4) of Central Goods & Services Tax Rules, 2017 (CGST Rules) provides for refund of unutilised ITC for zero-rated supply made without payment of taxes. As per the said rule, ITC on inputs and input services is allowed as refund. However, it does not include ITC on capital goods. Thus, a registered person making zero-rated supply cannot apply for refund of ITC paid on capital goods.
- As a result, companies engaged in export i.e. Export Oriented Unites (EOUs), Software Technology Parks of India (STPIs,) etc. cannot utilise the said ITC, resulting in blockage of working capital.

Recommendations

- Capital goods form a large part of investment for businesses and a situation of restricting refunds only to inputs and input services and not to capital goods leads spike in pricing, cash crunch, and blockage of working capital.
- Therefore, it is recommended that refund of input tax credit on capital goods should therefore be permitted by way of an amendment to the provision.
- Where allowing of refunds is seen as difficult in one shot owing to the quantum

involved in case of capital goods, the amended provision may also prescribe a staggered manner of refund to be granted.

2.2.2. Employee benefit expenses should be out of GST

Issues

- There are multiple facilities/services that companies provide for employees which are either subsidised or a pass through in terms of cost. There is no profit earned by companies from making such supplies to employees and are more in the nature of employee benefits which may or may not be included as part of the employee contract.
- In this regard, Schedule I of the CGST Act provides that gifts exceeding `50,000 (€637.08) in a financial year by an employer to an employee shall be treated as a supply of goods or services. It is relevant to note that companies also do not claim credit of tax costs incurred on such facilities/services. Accordingly, the companies should be seen as the end consumer in the supply chain and there should be no further supply to the employee.

Recommendations

- Accordingly, it is recommended that Proviso to Schedule I of the CGST Act be removed as where the no further recovery is being made to the employees, then the company should be treated as the end customer.
- Further, where recoveries are being made from the employees, the same would automatically amount to supply on which GST would be levied appropriately.

2.2.3. Suitable clarification be issued on requirement to cross charge salary cost of employees at head office

Issues

- Karnataka Advance Ruling Authority in the case of M/s Columbia Asia Hospitals Private Limited held that activities undertaken by employees of corporate office to other units qualify as "supply" as per Entry 2 of Schedule I of CGST Act, since employee-employer relationship is applicable only to corporate office and cannot be extended to other units.
- The ruling has also been upheld by Appellate Advance Ruling Authority.
- It may be noted that IT companies having multi state/division operation apportion HO employee salary cost (e.g. CEO, CFO) to respective units/states/division. Since salary cost is not subject to GST, their further apportionment should also not be subjected to GST. Moreover, HO is not providing any services to respective units.
- On the contrary, CBIC recently clarified in FAQs that if HO and branches are distinct persons as specified in Section 25(4) of CGST Act 2017, invoice is required to be issued and GST should also be paid.
- Salary cost is a non-GST cost. If the concept of ‘employer–employee’ relationship and the term ‘distinct person’ is supplied with such far-fetched meanings, the true intent of the law to keep certain transactions outside the ambit of GST and bring within its purview the transactions where there is an actual ‘supply’ fails.

Further, in case where global CXO is appointed as an employee of the Indian entity, then the above interpretation would require dealers to pay GST on reverse charge basis as import of services in respect of the same. All the activities undertaken by the employee is on account of the employment contract.

Recommendation

- It is recommended that a clarification be issued that there would not be any GST on HO salary cost by deeming them as supplies to other units and the FAQs be amended to this extent as under no circumstance can a head office managing countrywide operations be construed as providing any ‘supply’. The entire framework of GST would be incorrectly implemented if this were to be treated as a supply.

2.2.4. GST implications on transactions between Head Office (HO) and Branch Office (BO) located outside India

Issues

- It has been a stated and implemented policy of Government that a nation should not export taxes. It is also a settled legal proposition that a person cannot provide service to one-self or one’s branch.

- Considering that in mind, the Government, vide notification no. 15/2018 – Integrated Tax exempted services provided by HO in India to its BO outside India.
- Purpose of not allowing export of services to own establishment is to restrict export incentive for encashment of credits through fictitious claim of service exports to own branches.
- While intention of above exemption is noble, following issues may arise on account of the said exemption:
  - Insertion of above entry into exemption notification may prompt field formations to issue notices contending that exemption is prospective and for periods prior to 27 July 2018, tax was payable on such services.
  - Insertion of above entry may prompt field formations to consider value of such activities as 'exempt supplies' and require proportionate reversal of ITC under section 17(2)
- As stated above, law prior to 27 July 2018 does not suggest that there is a supply liable to tax when Indian HO carries out activities for foreign branch. The above exemption entry should not result in a situation of presumption of supply and therefore, requirement for reversal of ITC.

Recommendation

- Clarification should be issued to the effect that transactions of mere cost allocation between HO and BO does not involve any element of supply.
- Exemption provided under Entry 10F of the above mentioned notification should be provided retrospectively with effect from 1 July 2017.
- An explanation should be inserted in Rule 42 and 43 of CGST Rules to provide that such HOBO transactions qualifying as "exempt" would not warrant input tax reversal.

2.2.5. Exemption from IGST paid on capital goods by STPIs/EOUs

Issues

- Benefit of upfront IGST exemption on import of capital goods by STPI/EOU was extended till 31 March2020. Post this, option to claim IGST exemption will no longer be available. This would put undue strain on finances of units engaged in 100% exports as these companies have huge investments by way of capital expenditure.
- Not extending upfront exemption to EOU/STPI units, where there is a large representation of MSME would result in significant burden for such units.

Recommendation

- Upfront IGST exemption for import of capital goods should be extended without any time limit. In this regard, Parliamentary Standing Committee Report on Impact of GST on exports dated 19 December 2017 is relevant.
- The benefit should be extended for domestic procurement as well. In absence of this, these units would resort to imports for availing exemption which would be against "Make in India".

2.3. Customs-related Issues

2.3.1. Clarification with respect to concessional Basic Customs Duty (BCD) on telecommunication networking products and request for review of the product list

Issues

- The First Schedule to Customs Tariff Act, 1975 under Chapter 85 prescribes the tariff heads and rates for telecom products. Telecommunication networking equipment are classified under HSN 8517 62. Extract of tariff (as it reads today) is provided below for reference (see tables).

  **Tariff rate increased from 10% to 20% vide Finance Act, 2018*

Tariff item		Description	Standard rate
851762	**--**	Machines for the reception, conversion and transmission or regeneration of voice, images or other data, including switching and routing apparatus:	
85176290	**---**	**Other**	**20%***

Other telecommunication related equipment are classified under:

Tariff item		Description	Standard rate
851769	**--**	**Other:**	
85176990	**---**	**Other**	**20%***

**Tariff rate increased from 10% to 20% vide Notification 74//2018 - Cus dated 11 October 2018*

- Various notifications issued, granting and withdrawing exemptions under Customs Tariff Act has created an ambiguity on appropriate rate of BCD for items falling under 8517 62 90 and HSN 8517 69 90.
- Notification No 57, 2017 – Cus dated 30 June 2017 as amended from time to time prescribes an effective rate of 10% for items falling under 8517 62 90 and 8517 69 90. However, specific items have been excluded from the benefit of the concessional rate and therefore would attract rate of 20%.
- In other words, the effective rate of items falling under 8517 62 90 and HSN 8517 69 90 is as under:

Particulars	Effective rate
Following items, falling under 8517 62 90 and HSN 8517 69 90, not covered by notification* prescribing concessional rate: a) Wrist wearable devices b) Optical transport equipment c) Combination of one or more of Packet Optical Transport Product or Switch (POTP or POTS); d) Optical Transport Network (OTN) products; e) IP Radios; f) Soft switches and Voice over Internet Protocol (VoIP) equipment, namely, VoIP phones, media gateways, gateway controllers and session border controllers; g) Carrier Ethernet Switch, Packet Transport Node (PTN) products, Multiprotocol Label Switching Transport Profile (MPLS-TP) products; h) Multiple Input/Multiple Output (MIMO) and Long Term Evolution (LTE) products	20%
All other items falling under 8517 62 90 and HSN 8517 69 90	10%

(a) Issues which require clarification from CBIC

- The list of items mentioned in the Notification (as shown in the table above) has led to many interpretational issues, specifically because telecom networking products including the following are classified under HSN 8517 62 90:
  - Access points;
  - Network access controllers;
  - Switches
  - Wireless modem support;
  - Firewall appliances;
  - Port serial control gateway;
  - Integrated networking equipment;
  - Fibre channels;
  - Networking equipment and its accessories; etc.
- These items are closely related to the list of items mentioned in the Notification. They in fact make-up the final products and assist in its intended use.

- The exclusion list seems to outline the technical nature of activities performed by the products or intended use and does not necessarily specify the products itself. This has led to a lot of debate and practical difficulties at the time of clearance of goods.
- There is therefore an ambiguity as to what specific products would be liable to a concessional rate of BCD at 10% and those that would be liable at the full tariff rate of 20%.
- Owing to this ambiguity, several companies have been in fact discharging the full rate of 20% under protest.
- Further, there have been instances observed where customs ports have contrary interpretation in relation to applicability of concessional rate for the same product. For example, a particular product would have been cleared at BCD rate of 10% in Port A and at higher BCD rate of 20% in Port B.
- The above issue has been explained by ambiguity faced by the industry in import of Ethernet Switches (Without carrier) and Firewall and network security usually found in the IT environment which would require immediate clarification by way of Circular.

Product	HSN	BCD Rate for product	Interpretation
Ethernet Switch (without Carrier)	8517 62 90 (Classified at par with Carrier Ethernet Switches)	10%	• Ethernet switches are different from Carrier Ethernet Switches (which are classified under 8517 62 90 and attract at 20%). • Ethernet Switches are used within enterprise for their internal information and communication Technology. Further, these are used for establishing Local Area Network (LAN) connection to PC's Laptops, Printers and other IP enabled end points which are part of the single business entity. • On contrary, Carrier Ethernet Switches are used by telecommunications network providers//internet service providers to provide Ethernet services to their customers. • Therefore, Ethernet switches (without carrier) are different from Carrier Ethernet Switches and hence should not be classified under the exclusion part Notification No 57, 2017 – Cus. Consequently, Ethernet Switch (without carrier) would merit a BCD rate of 10% as per said Notification. • Our ask is that Ethernet Switches (Without carrier) should not get classified as Carrier Ethernet Switches falling under item (g) of exclusion list of Entry 20 of Notification 57/2017-Cus
Firewall and network security	8517 62 90 (classified at par with gateway controllers)	10%	• Firewall and network security commonly used in ITA environment have been denied benefit of standard rate of 10% as these are treated to be par with gateway controllers. • It should be noted that firewall and network security are hardware///software appliance the blocks, filters, or restricts and to a degree directs network traffic. These are different from “Gateway

Product	HSN	BCD Rate for product	Interpretation
			controllers" whose primary task is to link two networks. • Firewall and network security, being telecom in nature should be provided benefit of standard rate of 10% as against the current rate of 20% paid by most companies. • Our ask therefore is to clarify that the Firewall and Network Security should not get classified as "Gateway controllers" falling under item (f) of exclusion list of Entry 20 of Notification 57/2017-Cus.

- Therefore, our request with respect to the above products, namely Ethernet Switch (Non-Carrier) and Firewall and network security, is a clarification by way of a circular on applicability of Concession rate for the said products i.e., (a) Ethernet Switches (b) Firewall and Network Security.

57/2017-Cus thus attracting a higher rate of BCD at 20%.

- Most of the ITA products mentioned in the Information Technology Agreement to which Indian is a signatory would attract nil rate of BCD. The list of such

Product	HSN	BCD Rate for product	Interpretation
VoIP Phones	8517 18 10 Telephone sets, including telephones for cellular networks or for other wireless networks	*Nil*	• VoIP Phones or IP Phones without web conferencing and video enabled facilities would be classified under and should attract *nil* rate of BCD in line with ITA. • On the contrary to the above, VoIP phones have been classified under 8517 69 90 in Notification 57/2017-Cus and more specifically been included in the exclusion part thereby providing for higher BCD rate of 20%. • Our ask in relation to VoIP phones is that these should not get classified under 8517 69 90 and a suitable amendment has to be made in the said Notification.

(b) Issues which require amendment in Notification 57/2017-Cus

- In addition to the confusion that the exclusion list has created, it is important to note that several of these items, such as routers, modems etc. are ITA products. However, they have been included in the exclusion part of notification

product in Annexure A and B of the ITA agreement also includes Telecom and IT products classified under 8517.

- Any duty levied on the ITA product would be a violation of the ITA entered in to by India.
- Overall, our request in relation to the above issue is to amend the

Notification 57/2017-Cus to exclude all the ITA products (including VoIP), which would attract a nil rate of tax.

Recommendation

1) **Issue of Clarificatory Circular with respect to Notification 57/2017-Cus:**

- To eliminate ambiguity mentioned in issue (a) above, we request the CBIC to revisit the exclusions in the entry 20 of the Notification and issue an clarification by way of circular which would provide specific list of products falling under HSN 8517 62 90 and 8517 69 90 (i.e., Ethernet Switches and Firewall and Network Security) that would be eligible for concessional rate of 10%.

2) **Amendment to Notification 57/2017-Cus:**

- We request CBIC to amend the notification to remove ITA products from the exclusion part of the entry 20 of the Notification 57/2017-Customs and consequently, such ITA products should merit nil BCD rate.

2.3.2. Requirement for SVB order on import of ITA goods to be done away with

Issues

- ITA (Information Technology Agreement) bound goods enjoys exemption from Basic Customs Duty ('BCD') vide exemption notification 25/2005 and 24/2005 -customs dated 1 March 2005 dated.
- In light of IGST leviable on import transaction being creditable, an SVB order issued under the customs valuation provisions would see no impact on the duty///tax payable by an importer to the exchequer as there would be no BCD payable and entire amount of IGST paid shall be available as credit to the importer.

Recommendation

- Given that there would be no revenue impact (BCD being 0) on ITA goods irrespective of the value adopted, as the credit shall be available to the importer, it is recommended that the requirement for obtaining SVB order in case of ITA goods should be done away with. This would also reduce the burden on the customs authorities and the focus could be on cases where import duties are involved.

2.3.3. Single adjudication authority for SVB matters

Issues

- Circular 5/2016- Customs dated 9 February 2016 provides for procedure for investigations of related party import cases and other cases by Special Valuation Branches.
- Para 9.2 while dealing with final assessment of goods imported from related parties states that "where imports have been cleared through multiple customs locations, the jurisdictional commissioner of the SVB shall, after issue of notice by the proper officers in the said locations, make a proposal addressed to the Commissioner (Customs), CBEC recommending appointment of Common adjudicating authority by the Board for purpose of passing order for finalisation of provisional assessment"
- While the said circular provides for Common adjudication authority for the finalisation of the provisional assessment, practically this has not been fully implemented and the final assessments have been carried by the respective locations.
- Decentralised and multiple adjudications for a SVB holder leads to various hardships such as contrary valuation for the same products imported from same related parties, duplication of efforts etc.

Recommendation

- We request CBIC to issue Circular for mandatory implementation of procedure provided by Para 9.2 of Circular 5/2016-Cus in relation to Common adjudicating authority for imports made in multiple locations.

CONCLUSION

India is an emerging economic powerhouse. It is a growing domestic market and an expanding export hub for information technology and innovation activities.

Therefore, it needs to address the issues articulated above to ensure sustained growth and success in the absence of which it would become extremely challenging to do business. Furthermore, European businesses would face a hard time in doing business and bringing in fresh investments in these sectors into India. Specific plans for each sector need to be made and chinks in the economy need to be ironed out to ensure that India continues to remain a sought-after investment destination and also render Indian ICT exports competitive in the international arena.

NOTE

Infrastructure

Acknowledgements: Mr. Cesare Saccani (President, IICCI) – Chairman, Infrastructure Sector Committee & its Members
Knowledge Partner: The Indo Italian Chamber of Commerce and Industry (IICCI)

EXECUTIVE SUMMARY

- The Indian economy has experienced robust growth in the past decade and is expected to be one of the fastest growing economies in the coming years.
- The Infrastructure sector is a key driver of the Indian economy and is one of the largest receivers of FDI inflows to India.
- Since the last few years, there has been a significant push from the Government, which has been providing financial support (budgetary allocation of US$63 billion for 2019-20) and implementing initiatives to give a boost to the sector.
- Private sector is emerging as a key player across various infrastructure segments, ranging from roads and communications to power and airports. In 2019, infrastructure sector in India witnessed private equity and venture capital investments worth US$14.5 billion.
- The eight core infrastructure industries include coal, crude oil, natural gas, refinery products, fertilisers, steel, cement and electricity saw a cumulative growth of 0.6% in 2020
- The infrastructure requirement by India for a sustainable development is US$780 billion by 2022.
- Highway construction in India increased at a CAGR of 21.44 between FY2016-FY2019. In FY2019, 10,855 km of highways were constructed. The Government of India aims to construct 65,000 km of national highways at a cost of INR5.35 lakh crore (US$741.51 billion) by 2022.
- The innovative hybrid annuity model (HAM), the toll-operate-transfer (TOT) model and the conceptualisation of the Bharatmala programme have helped turn things around while many cash- strapped developers have successfully deleveraged by selling off assets. Meanwhile, technology induction such as the FASTag programme is achieving substantial growth in penetration.
- Bharatmala indicates that the already substantial opportunities in the sector could scale up by another dimension. Given programmes such as Bharatmala, Setu Bharatam, and Char Dham Connectivity and the proposed economic corridors, some INR7 trillion could be absorbed in investments over the next five years.
- The Transport & Logistics segment grew significantly in FY2018, with disruptive technologies such as Cloud-based systems, robotics for various value-added services, IoT and Big Data analytics contributing to its growth. Improved logistics with India's ranking of 44 out of 167 countries in World Bank's Logistics Performance Index (LPI) 2018.
- Maritime sector's fortunes ebb and surge with trade activity. Global trade has been slow for the past several years and that has adversely affected growth. The Indian ports and shipping sector have seen slow growth as a result. While there is hope of a revival in iron ore exports, as well as an increase in the import of crude and related products, the policy emphasis and implementation on developing coastal trade and cruise tourism, and other policy measures to increase capacity and improve efficiencies in the sector.
- Good revenue growth for Indian Railways and Metro rail projects worth over INR500 billion (US$7.7 billion) is underway. The accident record has improved but it still leaves a lot to be desired. Apart from enhanced targets for doubling lines, gauge conversions, etc., major projects like the dedicated freight corridor, the expansions in the Northeast and the planned network of high-speed lines should eventually lead to volume expansions. The Railway Ministry has announced that 151 trains in 109 pairs of routes will be operated by private sectors. The private sector will invest INR30,000 crores.
- With initiatives like 'Housing for All' and 'Smart Cities Mission' the Government of India is working on reducing bottlenecks and impeding growth in the infrastructure sector.
- Hence there are ample opportunities in the sub sectors of infrastructure but a lot is left to desired with several issues that plague the sector:
- Delays and time overrun: projects from railways (77/371); roads (100/607), urban development (19/58) for data available as of November 2018.
- Age old problems persist in clearing bottlenecks such as land acquisition, clearances and approvals along with resolution of disputes and arbitration.
- Projects face inordinate delays due to difficulties in securing project finance, political and social friction, delays in securing environmental clearances, policy ambiguities, poor health of sponsors, and problem of

stressed assets and reluctance of banks in providing credit.

- The Indian contract law is well placed and is capable of resolving all issues in its current form. Rather, the need of the hour is to ensure better implementation of the existing laws with a few amendments and the introduction of standardised contract agreements. These changes will require strong will on part of the government authorities. Better implementation of the current laws with the requisite amendments will help in alleviating most of the problems of the construction industry.
- The collapse of IL&FS set the alarm bells ringing. IL&FS is a major player in the sector as both a developer and financier, and this put many projects at risk. It also led to a sharp spike in bond market yields and led to renewed caution about infrastructure projects on the part of lenders leading to temporary disruptions in raising funds. There has also been a slowdown in tapping overseas sources due to weakness in the rupee.
- However, the sector seems to be on a much firmer footing, given the evolution of successful models and with the BJP returned to power with a strong majority. Hence continuity with the Union Transport minister, road building activity is likely to see a graph of continuous acceleration with ambitious targets set to construct 40 kms per day and complete all current mega road development projects including Delhi-Mumbai economic corridor.
- Lastly, it remains to be seen if Prime Minister in his Modi 2.0 agenda follows through with key campaign promises of US$1.44 trillion to build roads, railways and other infrastructure, a boost to manufacturing as well as get on the long-awaited land reforms.

INTRODUCTION

- India is expected to become 3rd largest construction market globally by 2022.
- Sectors like power transmission, roads & highways and renewable energy will drive the investments in the coming years.
- Development of world class infrastructure will lead to 9-10% growth of Indian economy.
- In the Union Budget 2019-20, the Government of India has given a massive push to the infrastructure sector by allocating US$63 billion for the sector.
- Favourable valuation and earnings outlook make this sector an attractive opportunity.
- Only 24% of the National Highway network in India is four-lane, therefore there is immense scope for improvement.
- The Regional Connectivity Scheme (RCS) gives opportunity for development of airports.
- India's infrastructure development plan by 2022 requires an investment of 780 billion US$, with a focus on:

Sector	Description	Investment (in US$)
Smart Cities	Environmental renewal (greenfield and retrofitting) of 90 Indian cities by 2023	31 billion by 2023
Railways	Introduction of high-speed lines, traffic decongestion, safety, electrification, replacement and upgrading of rolling stock and stations, doubling of 18,000 km of tracks, third and fourth lines and conversion of 5,000 km of tracks into broad gauge	from 8 billion in 2015 to 23 billion allocated for 2019-20
Metro	25 projects approved for a total of 500 km of metro lines	7.7 billion in 2019-20
Highways	10,855 km of highways built in 2019, another 65,000 km by 2022	13 billion allocated for 2019-20
Airports	Vision 2040 to have 200 operational airports as against 106 at present and target of 1 billion passengers by 2040	45 billion
Renewables	175GW by 2022 (100GW solar, 60 GW wind)	125 billion by 2022
Ports	Develop 10 coastal economic regions with 6 new mega ports	15 billion by 2022

Growth Drivers

INVESTMENTS

- Infrastructure sector is one of the largest receivers of FDI inflows to India.
- Construction Development sector and Infrastructure activities sector received FDI inflows amounting to US$25.66 billion and US$16.84 billion, respectively from April 2000 to March 2020.
- In June 2018, the Asian Infrastructure Investment Bank (AIIB) has announced US$200 million investment into the National Investment & Infrastructure Fund (NIIF).
- Japanese investment has played significant role in India's growth story. Japan has pledged investments of around US$35 billion for the period of 2014 -19 to boost India's manufacturing and infrastructure sectors.
- Between January 2018 and January 2019, multilateral agencies granted funds worth $7 billion for various water supply and sewerage projects.
- As of October 2019, the US government's Overseas Private Investment Corporation (OPIC) is planning to invest in India's infrastructure, port and solar energy sectors.
- Increasing impetus to develop infrastructure in the country is attracting the major global players like China Harbour Engineering and Mizuho Financial Group.

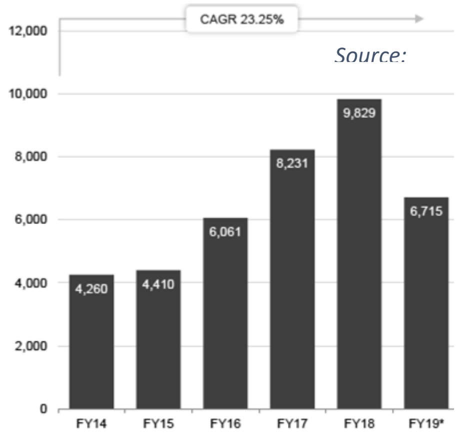
I. TRANSPORT & LOGISTICS

1. Roads and Bridges

   India has

   - 2nd longest road network (5.89 million km) 26 km construction, per day
   - 64.5% of freight traffic and 90% of passengers are transported on the road
   - US$107 billion for construction of 83,000 km of road for the next 5 years
   - Expenditure includes the Bharatmala project, one of the largest highway construction projects in India (US$83.25 billion) as well as Setu Bharatam, Chardham connectivity and economy corridors.
   - US$22 billion will be earmarked for road development in the North East to improve connectivity with Bangladesh, Nepal and Myanmar.
   - The hybrid annuity model (HAM) has become popular because the government ensures that it obtains requisite clearances prior to project award.
   - The toll-operate-transfer (TOT) model is attractive since there is low (or zero) construction risk, relatively stable cash flows, a long concession period and revenue optimisation via O&M on offered stretches.

Highway Construction in India (km)



Issues and areas of concern:

- Age-old problems persist in clearing bottlenecks such as land acquisition, clearances and approvals along with resolution of disputes and arbitration.
- Rising price of raw materials such as sand and aggregates
- Quality of consultancy available, sub-contractor capacity, the quality of independent engineers is not up to the mark
- There is need for earthmoving machinery (excavators, cutters, moles, etc.)

Way Ahead:

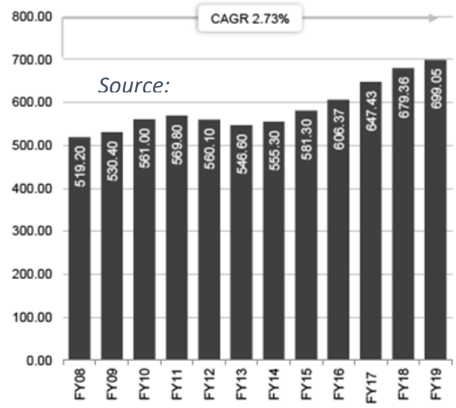
- There is a need for skill development and training in order to better the quality of design and safety consultants available in the sector that can be carried out by accredited certification agencies along with an emphasis on use of certified building and construction materials.
- Proper project preparation and due diligence are the much-needed steps to guarantee that only feasible projects are put on the block.
- At the time of preparing detailed project reports, National Highways Authority of India (NHAI) should allocate land for surplus cut soil to ease the execution process.
- With long term benefits in mind, operational FASTags should be linked to insurance premiums of cars to increase electronic toll collection penetration.

2. Ports

India is

- 16th in world with 7517 km coastline length
- 12 large ports and 205 intermediate and small ports
- 70% by value and 95% of trade by volume is done through maritime transport
- 704.82 million tons cargo traffic in 2020
- Government plans to develop 10 coastal economic regions as part of the Sagarmala project, with six new megaports developed in the country. The areas would be converted into production centres, supported by port modernisation projects, and could cover 300- 500 km of coastline.
- US$15 billion investments planned by the Ministry of Shipping via National Maritime Development Policy

Cargo traffic at major ports (million tonnes)



Issues:

- One of the foremost issues is that major and non-major ports fall under diverse administrations making the coordination between ports problematic.
- Land acquisition and obtaining environmental clearances be challenging for new and/or non-major ports.
- Poor connectivity of major ports with industries by rail or roads being a major challenge, leads to time and cost overruns. Even though the National Highways Authority of India has given a major push to port connectivity, many crucial projects suffer from implementation delays.
- Almost 25% container cargo is transhipped through international transhipment ports due to the lack of infrastructure to handle larger vessels at the Indian ports.
- Barring a few exceptions like JNPT, the dock capacity of most of the ports is considerably low, compared to top global ports.

- Drafts are a key limitation in the country because terminals and ports cannot cater to vessels beyond Panamax (draft over 13 metres) size, which are increasingly ruling global trade.
- Labour issues pose a major challenge in some of the older ports like excess manpower, lack of adequate training, deteriorating manpower quality, opposition to reforms and various anti-competitive practices.
- Erratic accessibility of equipment to handle large volumes, deficient dredging capabilities, outdated navigational aids and IT systems, lack of proper equipment handling training and technical expertise, limited mechanisation, procedural bottlenecks at various ports in the country are some of the challenges faced in this sector.

The Way Ahead:

Immediate attention to infrastructure improvement:

- An efficient internal mode of transportation system is important for the success of ports and shipping sector. Thus, the timely completion of various projects in the logistics chain is critical to meet the heavy traffic.
- Create a traffic capacity of 3,200 million tons.
- De-bottlenecking existing ports and capacity improvement at existing ports
- Dry docks needed to provide repair services.
- Port support services - operational and maintenance services such as pilotage, dredging, refuelling and supply of maritime goods such as barges and dredges
- Exploring partnerships for technology and manpower with advanced maritime countries as maritime sector needs modernisation and upgradation. This may be possible through collaborations and partnerships with successful maritime clusters in the field of ship design, automation and technology along with training and development of manpower.
- Development of maritime clusters: These clusters usher in innovation, create employment opportunities and attract foreign investors. We should nurture such clusters and encourage ancillary industries and more indigenous components. Such clusters are likely to encourage public- private partnerships, which will be a key enabler in attracting new technology, encouraging strategic alliances and enhancing investments.

The sector has many favourable factors for sustainable development, but eventually, it will depend on how the various participants leverage the opportunities available to them to transmute the sector into an engine of growth for the country.

3. Airports

The key twin drivers for construction opportunities in airports are the NABH [NextGen Airports for

Bharat] Nirman initiative and Vision 2040 for the aviation sector.

- India's domestic air passenger traffic is expected to grow at an average compound annual growth rate of 8.5% till 2040, taking the sector close to the target of 1 billion passengers by 2040.
- Based on the projected growth in traffic, India will require capacity augmentation at brownfield airports as well as setting up of new greenfield airports.
- Vision 2040 aims to have 200 operational airports by 2040, compared to just 103 in 2019.
- The Regional Connectivity Scheme contributed to the increase in operational capacity.
- The three key aspects of NABH Nirman are fair and equitable land acquisition, a long-term master plan for airport and regional development and balanced economics for all stakeholders.

Issues:

- Despite a separate policy being in place for greenfield airports, most of them have faced inordinate delays due to land acquisition issues, difficulties in securing project finance, political and social friction, delays in securing environmental clearances, policy ambiguities, etc.

Projected growth in airport infrastructure by 2040

	2018	2040
Operational airports	106 (as of March 8, 2019)	200
International airports	34	70
Cities with 3 operational airports	0	2
Cities with 2 operational airports	0	31
Airports handling over 10 million passengers annually	7	47
Airports handling over 1 million passengers annually	37	84
Land area under airports (acres)	90,000	240,000
Cumulative cost of land acquisition and multimodal connectivity ($ billion)	NA	30-50
Cumulative capex for airport ($ billion)	NA	40-50
Total capex – land plus airport development ($ billion)	NA	70-100
Direct employment at airports – airport, retail and security ('000)	46	80

Source: Vision 2040, Ministry of Civil Aviation

- The public-private partnership (PPP) model has not been quite successful for infrastructure sectors (including airports) due to land acquisition issues, delays in clearances, poor health of sponsors, problem of stressed assets and reluctance of banks in providing credit.

Way Ahead:

- Timely creation of capacity, modification of existing policies and regulatory frameworks in line with changing requirements, and close coordination between the central and state governments are the need of the hour to capitalise on growth opportunities in the airport sector by all stakeholders including construction companies.

4. Railways

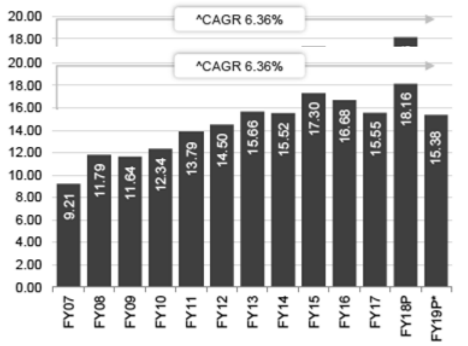
India is

- 4^{th} largest in the world, with length of 1,23,236 km, Indian railway network is the main artery of the country.
- The goal is to triple Indian freight traffic from the current 1.1 billion tons to 3.3 billion by 2030.
- Indian Railways will invest US$545 billion by 2032 to increase capacity
- An investment is also planned to adopt the European Train Control System for the development of the infrastructure complex
- A new "Online Vendor Registration System" was launched by Research Designs & Standards Organisation (Indian Railways) to have transparent digital systems and procedures
- The modernisation of 236 stations, the construction of new terminals, the development of a high-speed network and the construction of 25,000 km of railways by the end of 2020 are expected
- For a number of years now, India has envisioned a high-speed rail (HSR) network. While, initially, the progress was abysmally slow, the government has more recently made rapid strides towards achieving this vision.
- High Speed/Semi High-Speed Connectivity: Mumbai - Ahmedabad, Delhi-Agra and Delhi - Chandigarh: capital expenditure US$30 billion
- Dedicated Freight Corridor (East - 1856 km: from Punjab to Bengal; West - 1504 km UP to Maharashtra)/US$51 billion
- Financial and technical assistance from countries such as Japan, France and

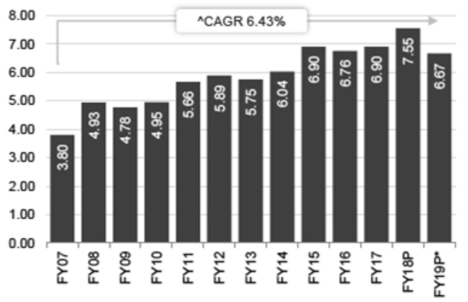
Spain have provided the much-needed push to HSR development in the country.

- Indian Railways (IR) is the country's biggest energy consumer, using about 18.98 billion units (BUs) of power. Energy is the second biggest expenditure item for the organisation, accounting for about 23% of its ordinary working expenses.
- In order to reduce its fuel expenditure, IR has prepared an action plan to run on 100% electricity by 2024 and become a net-zero emission network by 2030. In July 2019, the longest electrified tunnel was built between Cherlopalli and Rapuru stations.

Earnings from freight (in US$ billion)



Passenger earnings (in US$ billion)



Issues

- Age old issues such as land acquisition persist along with local opposition, resettlement and rehabilitation (R&R) of project-affected people, the unwillingness to adopt modern technologies, huge costs of construction continue to adversely impact project implementation.
- Moreover, environmental degradation along the HSR routes, R&R of project-affected people and regionally imbalanced development are perceived to be other potential pitfalls of HSR development in the country.
- Urgent need of Indian Railways to be electric

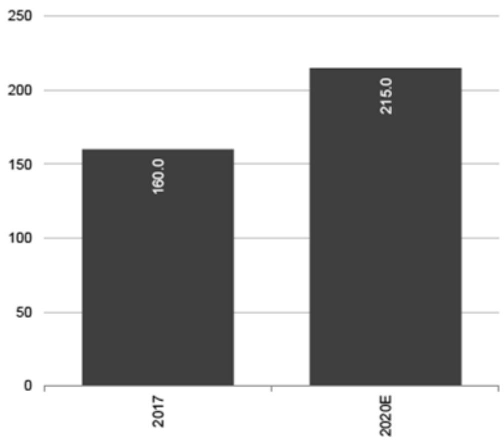
The Way Ahead

- Issues need to be dealt with targeted corrective policy and action should be taken in a time-bound manner to deal and ensure timely and effective implementation of the project.
- The annual electrification targets for 2020-21 and 2021-22 are 10,500 rkm respectively should be adhered too.
- IR's power requirements, even after taking efficiency measures, will triple by 2030 to 49 BUs. To meet its increasing energy requirements, feasibility should be carried out for using alternative fuels such as bio-diesel, compressed natural gas and liquefied natural gas. It will also need to take up more renewable energy projects.
- That said, in the long run, IR will need to invest in the training and capacity building of personnel to implement new initiatives and measures.
- Thus, IR's energy requirements and plans present significant opportunities for power producers, renewable energy developers, technology providers and manufacturers of rolling stock and electrical equipment.

5. Logistics sector

The Indian logistics sector provides livelihood to 22 million-plus people and improving the sector would facilitate a 10% decrease in indirect logistics cost, leading to a growth of 5-8% in exports. It is estimated that the worth of Indian logistics market would be around US$215 billion in next two years compared to about US$160 billion currently. The boom in next couple of years is expected largely due to the implementation of Goods and Service Tax (GST).

Logistics market size (US$ billion)



Leasing activity in the Indian logistics sector reached an all-time high of 33 million sq.ft. in 2019. To cater to this demand, the number of newly-constructed warehousing units should increase by 25% CAGR until 2021. This growth will be seen around the densely populated metros and tier-1 cities and presents an opportunity for both real estate funds as well as developers.

Challenges that beset the Indian logistics industry, the foremost of which is it being largely in the unorganised realm. The other challenges hindering its growth include high cost, underdeveloped material handling infrastructure, fragmented warehousing, presence of multiple regulatory and policy making entities, lack of seamless movement of goods across modes, and poor integration with modern information technology. These challenges, particularly the ones pertaining to procedural complexities, redundant documentations and involvement of several agencies at our ports and borders, severely dent our performance in international trade, resulting into about 70% of the delays.

Need of the hour is to formulate an integrated logistics policy.

The integrated logistics policy could go a long way in streamlining and consolidating multidepartment requirements, besides facilitating corrective action, effective monitoring and prompt grievance redressal. In an integrated manner to achieve the same by harnessing the potential of emerging technologies, bringing in investment, creating human capital, removing bottlenecks, improving intermodal transport mix, automation, single window clearance system, and simplifying procedures.

Along with it, a mechanism needs to be created to measure the sector's performance at regular intervals against the set benchmarks, thus, providing evidences to the policymakers so that a favourable policy environment is created.

II. SMART CITIES

1. Smart Cities

- The "Housing for All" programme aims to build 20 million urban homes and 30 million rural homes by 2022.
- Government investments have led to the approval or construction of 3.9 million homes so far
- City renewal programme and smart solution application
- Environmental regeneration (greenfield and retrofitting) of 100 Indian cities by 2023
- Total cost of projects: US$70 billion
- Impact on the total urban population: 99.486,840

Issues and Way Ahead:

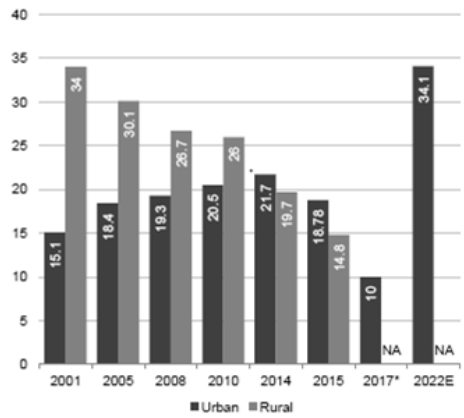
- When the Indian government announced its Smart Cities Mission in June 2015, the move was cheered and seen with scepticism in equal parts.
- On the one hand, the programme was hailed as one that would usher in an “urban renaissance” by promoting sustainable and inclusive urban development and drive economic growth. On the other, there was serious apprehension about India’s readiness to build technology-enhanced infrastructure that would address the structural inequalities and inadequacies in the cities.
- Four years hence while it is difficult to announce a judgement on the success of the mission, it is clear that the programme is still work in progress.
- According to the Ministry of Housing and Urban Affairs, as of December 2018, almost two-thirds of the projects envisaged under the programme have

either not started or are at the tender-issuing stage.

- While projects worth US$30 billion on for 100 smart cities were included in the original proposals, only 1,675 projects worth US$8 billion have been implemented so far.
- Innovative technology-led initiatives are being implemented across cities. Some cities such as Ahmedabad, Hyderabad, Surat, Coimbatore, Bengaluru, Mangaluru, Delhi, Mumbai and Chennai have launched initiatives for the deployment of advanced communications systems, intelligent transit management systems, smart meters, GIS and GPRS for solid waste management, online billing systems, mobile-based complaint redressal systems, etc. Ten cities have commissioned integrated command and control centres (ICCs) to provide a single interface for multiple solutions.
- That said, in a mission of this scale – with 100 cities across states that are diverse in every way – there are bound to be delays and cost escalations. Industry experts contend that globally, it has taken around 15 years to transform cities into smart cities. This explains why, despite the sluggish implementation, the euphoria surrounding smart cities, particularly how these will change the way urban India lives, refuses to die down.

2. Real Estate & Building Construction
    - The urban housing shortage in India is estimated at around 30 million units by 2030 which is being addressed through Pradhan Mantri Awas Yojana (PMAY), Urban, under which more than 15.3 million houses have been sanctioned up to February 2020.
    - Real estate sector in India is expected to reach a market size of US$1 trillion by 2030 from US$120 billion in 2017
    - Increasing share of real state in the GDP would be supported by increasing industrial activity, improving income level and urbanisation.
    - Mumbai and Bengaluru have been rated as the top real investment destination sin Asia.

Urban-rural housing shortage (million)



3. Affordable Housing
    - The inward migration of people from rural and semi-urban areas to urban areas is continually exacerbating the housing shortage situation in cities. The fact that majority of these migrants hail from lower income groups, brings the need for affordable housing into the limelight. The affordable housing sector from its current state – will have a shortage of 33 million houses (urban areas) by 2030, is in no way equipped to cater to the burgeoning demand.
    - The Prime Minister Awas Yojana (PMAY) - Urban, launched in 2015 aims to address the challenge of housing shortage amongst low-income groups in cities and envisages building of 20 million houses by 2022. A rural component has also been added to PMAY, which aimed at building/upgrading 10 million houses by 2019.
    - The private participation narrative in the affordable housing space is also changing favourably. A large number of developers are making inroads into this segment and are finding it lucrative. One of the biggest policy impetus for private developers came through the formulation of a public- private partnership (PPP) policy in September 2017.
    - The next few years until 2022, will be action packed for the affordable housing space. Policy impetus coupled with various affordable housing

schemes by state governments and active private sector participation will result in tailwinds for the sector, making Housing for All a commercially viable opportunity.

- The government has also laid significant emphasis on the adoption of prefabricated and 3D construction technology to boost speedy, safe and sustainable construction.
- Currently, around 125,000 houses in the country are being constructed using prefabrication technology, with several companies using 3D software solutions in order to make precasting and fabrication more efficient. The MoHUA is also exploring the use of 3D construction technologies for building affordable houses in 25 cities in the country.

The Way Ahead

- Given the huge demand-supply gap, the housing segment provides significant market opportunities to all stakeholders in the construction sector in the next four to five years. This is also expected to
- drive the demand for low-cost construction materials and technologies. The technology sub-mission under the PMAY would also facilitate the adoption of modern, innovative and green technologies and building materials for faster and better-quality construction of houses. Another segment which is expected to gain traction is prefabrication technology. This technology is expected to not only reduce construction time but also build more cost-effective houses. Together these initiatives are expected to help make affordable housing a reality and ensure that construction is done in a sustainable manner and at a low cost. Land Reforms - following the re-election of the government -
- Urgent need for land reforms, land initiatives & land pooling
- 3P to 4P approach with people involvement

4. Water

- In India, almost one-third of the current population lives in cities and this will reach half the country's population in just a few decades. India houses about 17% of the world's population and has only 4% of global water resources. With increasing economic activities, population growth and rapid urbanisation are exerting major pressure on water supply, water quality and public health.

Issues:

- India is soon going to be confronted by a serious resource challenge. The available water resources have reduced over the years but the demand has escalated and is projected to overtake the availability very soon.
- Water demand will continue to grow and by the year 2025 it is expected to increase by over 20%, fuelled by industrial requirements which are projected to double from 23.2 trillion litres per annum at present to 47 trillion litres per annum.
- Domestic demand is expected to grow by around 40% from 41 trillion litres per annum to 55 trillion litres per annum while irrigation will require 14% more water – 592 trillion litres per annum up from 517 trillion litres per annum currently.
- The Ministry of Water Resources, River Development and Ganga Rejuvenation predicts that per capita water availability will reduce by 36% by 2025 and by about 60% in 2050 from 2001 levels.
- While agriculture will remain the major water user, the challenges posed on water requirement by growing urbanisation calls for a monumental shift in response from all stakeholders.
- Challenges are poor financial health of ULBs, low level of private sector participation, shortage of skilled manpower, absence of accurate database with ULBs, and heavy dependence on public funds.

The Way Ahead

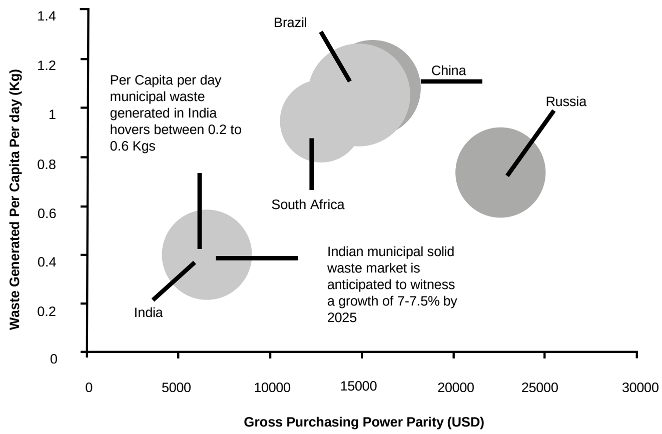
- In an increasingly complex water situation, the country's water utilities need to focus on ways to ensure more efficient water management and the adoption of new technologies for maintaining municipal water supply systems.

- Utilities will ultimately be more sustainable and competitive, which carefully and creatively use their water assets for strategic urban advantage.
- The introduction of the aforementioned measures and initiatives in the water and waste sector has largely been restricted to a few big cities. More recently though, smaller cities too have started adopting these measures to improve civic services.
- Therefore, concerted efforts have to be made to spread awareness about smart technologies and roll out financial support in the form of subsidies. Steps such as 90% rebate on sewer charges for those using decentralised STPs as introduced by DJB can be replicated by other ULBs too for greater uptake. An enabling ecosystem has to be created wherein all the stakeholders collaborate to introduce such world-class technologies.
- The need for Non-revenue Water NRW management in Indian cities is important for the operational and financial health of water utilities. Cities such as Singapore, Manila and Phnom Penh have successfully implemented water loss management programmes to reduce NRW to below 20% levels. Indian water utilities are struggling to provide clean drinking water due to ever- increasing populations, expanding service areas and high levels of water loss.

5. Solid Waste Management

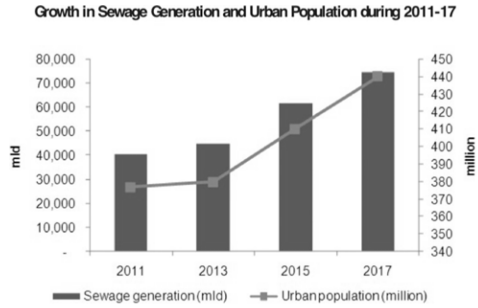
- One of the prerequisites for building a smart city is effective monitoring and management of solid waste.
- Unfortunately, most Indian cities fail to treat waste effectively as the existing solid waste management (SWM) infrastructure is inefficient and inadequate.
- With India flourishing economically, an increase in the purchasing power parity has led to more affordability, accessibility to resource use and a rapid surge in the waste volumes as well.
- Like many developing countries, India too is struggling with the straining waste management systems adversely impacting the ecological health.
- The total waste generation in India presently hovers around 60-65 MTs per annum, of which only 20% is actually treated. Municipal solid waste (MSW) holds a significant chunk, 75% of the total waste generated in the country of which only 25% is scientifically processed. The remaining is either dumped in sanitary landfills or is crudely littered.
- Given the current urbanisation growth levels in India, more population pressures on urban agglomerations is anticipated in coming years and so in the municipal waste generation volumes.
- Considering the current urban trends, it is not at all surprising to mention that the MSW quantum in India can see an increase of double the existing volumes by ten years down the line. Infect, it is projected to hover around 80 MTs by 2030, offering a business case of approximately US$20 Billion.
- According to the Ministry of New and Renewable Energy (MNRE), 175.28MW of power is currently being generated from waste and an additional 163.37MW from biomass gasifiers and 767.51MW from SPV Systems is being generated respectively.

Purchasing Power Parity and Per Capita-Per Day Average Waste Generated in BRICS Nations (In Kgs)



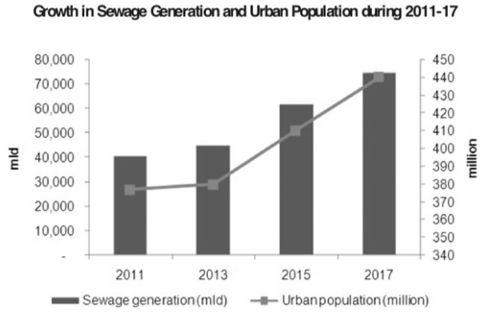
6. Sewage collection

- Increasing municipal and industrial activities has resulted in significant increase in sewage generation in urban areas of the country.
- Between 2011 and 2017, the total



sewage generated by Class I and Class II cities increased from 40,715 million litres per day (mld) in 2011 to 75,020 mld in 2017, recording a CAGR of 10.72%.

- The country's sewage treatment capacity increased from 11,787 mld in



2009 to 26,066.31 mld in 2018 (as of July 2018). About 83% is currently operational.

- In the last couple of years, the government has launched a number of programmes/schemes for augmenting sewage treatment and collection infrastructure in the country. Ongoing schemes like development of 100 Smart Cities, the Atal Mission for Rejuvenation and Urban Transformation of 500 habitations, the Namami Gange Mission and the Swachh Bharat Mission are estimated to entail an investment of over 3 trillion.
- The progress under these schemes has been slow with majority of the projects currently in the bid- ding and planning stage.
- The new Environment (Protection) Rules, 2017 has relaxed the discharge standards for treated wastewater/sewage (for upcoming STPs).
- Given the financial constraints and inefficiencies of ULBs, the case for more PPP in the sector is strong. The Namami Gange programme has awarded two sewage treatment projects for Haridwar and Varanasi under the new Hybrid Annuity Model.
- A number of incentives and policy structures have been promulgated by the municipal agencies as well as state governments to encourage different stakeholders to recycle and reuse wastewater.
- A number of ULBs in India have started to deploy advanced sewage treatment technologies such as sequential batch reactor, moving bed biofilm reactor and moving bed bio-reactor to improve the quality of treated sewage and optimise O&M cost and land requirements.

Key benefits

Through these smart solutions, ULBs can improve their performance by expediting the waste collection process, ensuring real-time monitoring of vehicles and reducing the time that elapses between rerouting vehicles to waste bins by tracking vehicles that are closest to the point of collection. Further, installation of mobile applications for SWM empowers the end beneficiaries as it enables quick complaint and grievance redressal. Also, reliance on intelligent technologies reduces human intervention thereby eliminating the chance of error.

Issues:

- The inefficiency in handling waste stems mainly from the inability of most cities to carry out proper segregation, transportation and storage of waste.
- Moreover, state governments lack expertise in using modern methods of waste treatment and also do not have the required resources for its execution.
- In most cities, collection services are not extended to unauthorised or remote settlements due to their inaccessibility or lack of capacity of inhabitants to pay for these services.

- The existing sewerage infrastructure is most cities is characterised by obsolete and faulty pipeline networks, insufficient treatment capacity, sub-optimal capacity utilisation, etc.
- Poor financial health of urban local bodies (ULBs) is another major issue of concern. ULBs in India are primarily dependent on government funds for implementing sewerage projects. Their own revenues from user charges as well as other local taxes are not even sufficient to recover O&M expenses.
- Further, the lack of a fixed revenue stream is major constraint that limits private sector investments.
- The contracting process for most sewerage projects is considered to be very weak. The project documents are not standardised and leave a lot of room for ambiguity.
- Majority of the ULBs lack up-to-date and accurate data on key sewerage parameters, including generation, treatment, collection efficiency and treatment capacity.
- One of the greatest hurdles to effective treatment of waste is the lack of proper waste disposal methods. Setting aside urban spaces for utilising them as landfill sites is another formidable issue. With increasing urbanisation, the lack of adequate space for dumping of waste has resulted in littering on streets. This has resulted in externalities such as health hazards.
- In addition, despite the introduction of many innovative WtE technologies like pyrolysis and plasma gasification technology for converting waste to energy, their uptake has been slow. It has been seen that ULBs lack expertise as their staff and engineers do not have the requisite training and knowledge. Moreover, these techniques are expensive as compared to conventional methods of incineration or combustion, which make them unattractive.

The Way Ahead

- Integration of smart technologies into waste management practices is the Way Ahead for cities to achieve the zero-discharge status.
- Citizens too need to adopt waste segregation at source and use technologies such as mobile applications to expedite waste management processes.
- Moreover, smart cities that have already launched initiatives must create greater awareness about the successful new methods and technologies to enable greater uptake in other cities.
- Though the initiatives taken by the government are laudable, policy and regulatory gaps still persist.
- The policy framework does not have the necessary clauses for financial penalties for non- compliance of the rules by a ULB. NITI Aayog has suggested exploring the possibility of setting up a central authority – the Waste to Energy Corporation of India (WECI) – for fast-tracking the setting up of WtE plants across smart cities. More such measures are needed for achieving the sustainable SWM goal. Moreover, expertise to at least make the right technology choices, if not develop new technology, is also the need of the hour.

  Source: Indiainfrastructure.com

E. INFRA FINANCE AND ISSUES

At a critical stage, the infrastructure sector in India is faced with insurmountable challenges of acquiring funds for project development and management risking the projects with possible financing defaults. Challenges such as high cost of capital, obstacles in obtaining non-recourse funding and dearth of long- term funding sources are currently haunting the industry. Moreover, the banking sector is under major duress on account of NPAs.

Emerging funding sources are slow to take off: Significant developments have taken place with respect to alternative sources of infrastructure financing - *infrastructure investment trusts (InvITs) proposed in 2013-14, infrastructure debt funds (IDFs) started in 2011-12 and National Investment and Infrastructure Fund (NIIF) activated in 2017 with Master Fund, Fund of Funds (FoF) and Strategic Fund. The NIIF* has currently over US$3 billion of committed capital and has a target of US$6 billion (49% contribution by the government and rest to be raised from foreign and domestic investors)

Most of these funds started out with a lot of enthusiasm, they are yet to make the intended impact. This is primarily attributed to the factors such as lack of enthusiasm among domestic investors to invest in them as well as lack of awareness about their future prospects. Nevertheless, considering the current situation of mounting NPAs with Indian banks, it becomes imperative for these funds to be more effective.

One of the biggest developments in the past 12-15 months was the signing of an MoU between NHAI and the State Bank of India for an unsecured loan worth US$4 billion. The loan will be provided for a period of 10 years with a three-year moratorium on repayments. It is notably the largest one-stroke loan to have been sanctioned to NHAI by any institution.

Meanwhile, the Life Insurance Corporation (LIC) bought bonds worth INR20 billion in the first issuance of NHAI's 30-year bonds in 2018-19. NHAI also has plans to announce a buyback policy. Under the policy, the authority plans to buy back 20 national highway and 19 state highway projects spanning 3,160 km from private players.

In case of financing water and sanitation projects, funding comes from several different sources. Government funds have always been the main source of finance for water supply and sanitation projects in the country. These funds are extended in the form of budgetary support and grants, and through schemes such as the Atal Mission for Rejuvenation and Urban Transformation (AMRUT), the Smart Cities Mission (SCM), the Swachh Bharat Mission (SBM) and the Namami Gange programme. Further, since municipal water supply is a state subject, most of the funding for such projects comes from the state government. Funds to urban local bodies (ULBs) are extended through state transfers and grants-in-aid. In addition, ULBs use their own resources for meeting capital expenditure on urban water and sanitation infrastructure. Water and waste water projects in India also receive sizeable funding from international financing agencies such as the World Bank, the Asian Development Bank and the Japan International Cooperation Agency. These multilateral agencies provide financial support to the sector in the form of concessional/ non-concessional loans, equity investments, grants and loan guarantees. Funds for water and related projects are also provided through financing institutions such as Housing and Urban Development Corporation Limited, India Infrastructure Finance Company Limited and Infrastructure Development Finance Company Limited.

In spite of this, the investment requirements of the water supply and sewerage sector are substantial, and the current level of investment leaves much to be desired. The fundamental problem lies in the lack of attractiveness of the sector due to various issues, owing to which private players have been cautious in investing their funds. The situation is further exacerbated by the poor financial health of ULBs that are still struggling to garner funds for meeting their expenditure requirements.

The time is ripe for the country to tap alternative sources of funding such as infrastructure investment trusts (InvITs), infrastructure debt funds (IDFs) and National Investment and Infrastructure Fund (NIIF). The Economic Survey also stressed the need to fill the infrastructure investment gap by financing from private investment, institutions dedicated for infrastructure financing like National Infrastructure Investment Bank (NIIB) and also global institutions like Asian Infrastructure Investment Bank (AIIB) and New Development Bank (erstwhile BRICS Bank).

Sources:

IBEF, PwC, Hindustan Times, Indian Infrastructure, Economic Survey 19-20, Enincon consulting

NOTE

Logistics

Acknowledgements: Sanjay Tiwari (Maersk Group)
Logistics Sector Committee & its Members

The Government of India published its draft National Logistics Policy in July of this year. The publication of this document is a watershed moment in that it aims to address a lot of issues pertaining to the logistics industry itself as well as the role that the logistics industry plays in enabling manufactured products to reach their ultimate customers in a timely and cost effective manner.

Rather than repeating the extensive list of issues which we have in the past felt need to be addressed when it comes to the transportation and logistics industry, and with that the various modes of transportation and storage, we will comment on a few salient points from the paper.

In its preamble the Government itself states that the logistics industry is characterised by:

- Being at the mercy of a complex regulatory environment with multiple stakeholders holding sway
- Generally a low level of technology adoption
- Unpredictable supply chains resulting in high inventory carrying costs, a cost which is not just born by business but is ultimately paid for by the consumer
- A seemingly fragmented and unorganised sector with a general lack of trust between key participants

This summing of the transportation and logistics industry is a particularly unflattering one. In order to address many if not all issues plaguing the industry the Government proposes to

- Create a modern, efficient and resilient industry
- One that utilises and offers multi-modal capabilities
- Deploys best in class technology
- Help create a vast pool of skilled manpower
- Improve India's overall ranking in the Logistics Performance Index over the next five years
- And finally reduce logistics cost by 5% of GDP, also over the next five years

In order to realise its ambitions the Government has defined five pillars

Five pillars:

1. Integrated logistics services: faster, safer, cheaper.
    - While this ambition is noteworthy our question is what this means in practice. Will it be an end to unnecessary stoppage or handling of cargo in transit?
    - A Master Plan for National Logistics will be drafted.
        - Who will work on this? What are the main components in terms of:
        - Infrastructural objectives
        - Key indicators
            1. Speed
            2. Time
            3. Cost
            4. fulfilment
    - The Government wishes to create an overarching national logistics platform (iLog), which in terms of its intent is a good idea. Again, a few questions arise:
    - What are we benchmarking it against, which countries have been successful with such a national platform?
    - Are we not living in an era of overlapping networks rather than a single overarching network?
    - What role can the private sector play
    - Will this network tap into international networks such as TradeLens which are fast gaining adoption across the globe?
    - Idea of a logistics monitor is good. What KPIs will be fed into it?
    - A national dashboard that indicates that the cost of transporting a particular commodity from a to b has actually come down by x% over time, with the time to transport therefore also assuming to have come down
    - The Government wishes to drive R&D in logistics: is there a plan to in-source best in class expertise from other countries such as The Netherlands?
2. Efficient and multi-modal transport: shift from road to rail and water.
    - What does this imply? Disincentivise certain modes of transportation, make access to others easier, practice 'nudge economics'
    - The Government wishes for India to become a hub of air cswargo. Our question is whether the government realises what eco-system is required to operate cargo aircraft and container vessels? Look to benchmark with Singapore, China, UAE, Netherlands, Germany, Luxembourg. Look at the much more lenient and efficient Customs regulations of these countries

3. Meet logistics needs of core sectors of the economy, the customers of the logistics industry.
    - Our recommendation would be to among others find out where stoppage is occurring. Which parties currently benefit from inefficiencies, e.g. empty trucks that ply certain routes?
    - Driving MSME competitiveness is a good idea. How can the large players such as Maersk help smaller providers to come up and fill out the eco-system?
4. Logistics for international competitiveness (connecting local to global)
    - We believe that it is very praiseworthy to recognise the role that the logistics industry plays in helping Indian exporters reach their international markets. In order for India's logistics industry to become more efficient and competitive we believe that we should define competitiveness better.
        - Make India welcoming for foreign players and carriers. Is India a place for companies to serve only Indian customers or international customers?
        - Can goods come in and out easily? Can containers move around freely?
        - What paperwork is involved to move a container in- or out? Dutch Customs allows pre-declaration of goods before they leave China on an aircraft so that they move through the right channels more quickly. That is a major reason why logistics companies choose The Netherlands as their hub.
        - Trust doesn't just have to flow between players in the industry, it also has to flow from government agencies to industry players and vice versa
        - The streamlining of work with Customs and Partner Government Agencies is an excellent idea, who will run with this?
5. Finally, the government lists Logistics for Emergencies & Disasters, which is truly a broad view of logistics and a very welcome one. This is the human face of logistics. The outbreak of the COVID-19 pandemic and the subsequent lockdown which held the country in its grip would have been impossible to survive were it not for the transportawtion and logistics industry. The men and women working in this industry kept going 24/7 throughout the pandemic, loading aircraft and trucks and rail carriages and vessels, distributing goods from central warehouses to hungry and anxious consumers nationwide. It is very commendable that the Government seeks to strengthen and make explicit the role of the logistics industry in helping to deal with emergencies and disasters.

    We have few questions pertaining to the institutional mechanisms that the Government proposes to put in place.

    1. Who will be in the National Logistics Council?
    2. Who will man the Logistics Sector Co-ordination Committee? How will they plow through the list of action items (see Sunil's list)
    3. Central Advisory Committee for Logistics: who will be in this?
        I. How do we measure progress? If goods are moving from WB to UP or Bihar, how do we measure whether key impediments are being removed?
        II. What dashboard will they have?
    4. National Logistics Forum for engagement with private sector players
    5. The Logistics Division will function as the secretariat for the above bodies. Which Ministry will this come under?

Maritime India Vision 2030

Key Focus Area

Performance Improvement

- **TA-2: Improve performance of ports to world class levels**

a. **Process improvement**
    - Standardisation and simplification of process/documents (port & customs), especially for handling containers across all ports in the country. This should also be completely automated with Standard SoP's
        i. **Flexibility in Customs Process:** Sea Cargo Manifest Transhipment Report (SCMTR): flexibility and exceptions for export transactions required. Proposed 24 hrs cut-off shall be made flexible under special conditions viz perishables, essentials etc, to limit delay of exports and loss to exporters. This will also impact yard capacity of the port.

ii. **Automation of gate process**: Vehicle booking system shall be installed on priority. Process to ensure exit/entry only with full documentation

iii. **Remove duplicate activities**: Gate Process at ports are complex and time consuming. These are required to be optimised to exclude redundant transactions/data exchanges (data already available in the system) at gate. Objective is to limit role of Gate clerk and Gate Supervisor. Hard copy EIR which today enables truck navigations inside the port /yard shall be automated to OTP/SMS based instruction system. Proper security measures are required to ensure protection from IT frauds/ cyber-crimes.

iv. **Information Exchange Process:** Multiple systems operating in isolations (ICEGATE, PCS, SCMTR, TOS, Banks, etc.). Integration of various systems will be essential for seamless data interchange and process efficacy. Information exchange to be automated to reduce paper exchanges between Port, CHA, CFS, Customs, Transporter (Road/Rail), CISF, PGA, Customs, etc. is required.

- Need for monitoring/encouraging process adoption and process efficacy measurement.

b. **Infrastructure required**

- Need for port-specific infrastructure requirement assessment including upgradation/modification/rehabilitation of the existing infrastructure
- Mandatory development of truck parking yards in the proximity of the ports for effective gate automation and truck management system
- Berth mechanism program for each port
- Draft/depth enhancement programme for each port
- Reception facilities for vessels at India ports needs to be upgraded. Provisions for removal of sludge, waste, garbage to be made available
- Encourage modal shift from road to rail by developing multimodal terminals (MMLP/PFTs), rail freight rationalisation and investment in rail infrastructure

c. **Performance Indicators**

- KPI such as QC moves, RTG moves, evacuation process shall be identified based on the capability/capacity of the terminal. It should not be one size fits all approach. For example, twin lift cranes productivity shall not be compared with single lift cranes. Similarly, feeder vessels cannot be compared with mainline vessels
- Productivity norms shall be aligned with the performance obligation in the concession agreement.
- High productivity norms should not result in incremental capex which then result in excess capacity creation
- Terminal operators shall be incentivised to achieve productive norms as this may require additional capex which has not been envisaged
- Provision for review of the productivity norms from time to time considering the traffic pattern (coastal/feeder/mainline vessels), equipment available (RMQC/MHC etc).

d. **Hinterland Connectivity**

- Hinterland connectivity projects shall be identified based on to origin-destination mapping of cargo flow and shall be implemented on priority. E.g Elevated corridor for Chennai port.
- Port wise hinterland connectivity plan is needed with obligation on state government/local authorities to implement in time bound manner

e. **Roadmap to prioritize transformation of major ports into landlord ports**

- PPP in Dredging and other ancillary services

f. **PPP structure should encourage productivity improvements**

- **TA-5: Make Maritime logistics highly cost competitive with end to end services**

a. **Cost Competitiveness of India Ports:**

- Rationalise the VRC
    i. VRC shall be at par with global transhipment hubs
    ii. Reduction of Vessel Related Charges
    iii. Benchmarking study to be undertaken to understand cost elements and structure of VRC at ports like Singapore, Colombo etc.

iv. Cost of major capital projects like dredging etc shall be considered as creation of national assets with complete funding support from the government and such cost shall not be allocated the Port Authorities.

- Light house dues
  i. With advancement of in technology, many of the services are not used currently e.g navigation aids are replaced by GPS, VTMS etc,.
  ii. These shall be rationalised at kept at par with global hubs.
  iii. Standardisation of light house / VTMS dues across all ports (major or non-major)
- Incentives on coastal cargo to be rationalised:
  i. Standard incentives/discounts/subsidies shall be replaced with volume-based incentives.
  ii. Recommendation on replacement of standard incentives /discounts/subsidies for coastal shipping with volume-based discounts to be relooked based on inputs from INSA
  iii. Impediments for costal shipping to be highlighted
- Reduce cost of repositioning empty EXIM containers between the gateway port and the hinterland clusters:
  i. Significant repositioning of empty is happening in hinterland clusters with limited access to IWT & Coastal For example NCR, Punjab, Rajasthan. Current customs law permits repositioning of empty EXIM containers through IWT and Coastal shipping using cabotage cargo to bring the costs down
  ii. Appropriate amendments in the Customs law to permit repositioning of empty EXIM containers using cabotage cargo within the country by all modes of transportation viz road, rail, river and sea. This will reduce the overall EXIM logistics cost by bringing down the empty repositioning costs.
  iii. Permit repositioning of empty EXIM containers using cabotage cargo using all modes of transportation viz road, rail, river and sea
  iv. EXIM containers stay period (without payment of imports duty) to be increased from 6 months to 1 years
- Rail freight charges to be rationalised, especially for movement of empty containers

- **TA-12: Make all Ports and other maritime bodies Health Safety Security and Environment (HSSE) compliant as per global benchmarks**

a. Enhanced Safety at ports

b. Standardise all health and safety processes across all ports

c. To adopt Green Port-Policy to reduce pollution in the port by switching equipment and vehicles on electric or CNG/LNG fuelled

- Need LNG/CNG stations to be available within the port for continuous supply
- Restriction on production of solar power above 1 MW to relaxed for terminal operators and terminal operators shall be allowed to sell the electricity to the gird
- Waste management and disposal facilities (for auctioned cargo) shall be made available. Example compost plant in Cochin. NITI Aayog/IPA are working on implementing STP/ETP at major ports on PPP and this can be included in the scope of PPP operator
- Use of renewable energy shall be expedited. Need to renewable energy usage plan for each port to reduce carbon emission. Example – DPW terminals are working to reduce carbon emission at their terminals by 60% (69.5 Kilo Tonnes) by 2030

Maritime Leadership

- **TA-3: Create new world class ports in India**

a. Transhipment port

- Proper due diligence before ascertaining a preferred location. (shipper as well as shipping line perspective, least cost of creation, measures to encourage shipping lines to tranship at Indian Ports)
- Revisit must have factors for transhipment ports to include – transhipment strategy of majority of liners, Critical cost elements for a shipping line (charter hire, bunker, crew, port costs), all port costs including capex for building a new transhipment terminal or upgrading the existing
- Support from the government to establish world class transhipment port – World class infrastructure (deep draft berths along with channels etc and suitable equipment) and

tariffs comparable with other competing transhipment ports in the region. Measures to encourage shipping line to move to Indian transhipment hubs is required

- Identify transhipment ports considering location, infrastructure (berths & storage area), draft and modern cranes to handled 22,000 TEU vessels
- Subject to market response to the Vizhinjam port (incl. capacity utilisation), explore feasibility of new transhipment hub in Kanyakumari region for future

b. Role of Modern Technology

- Formation of advisory board for port modernisation by the Government of India with representatives from logistics sector to oversee the progress.
- The representatives from the trade bodies to be an office bearer of that trade association. No provision for case to case nomination by the trade association.

c. Maritime Master Plan

- Effectiveness of Maritime India Vision 2030 can be ensured by detailed implementation plan (long term, medium term, short term).
    i. Any new capacity development shall be based on National Maritime Master Plan approved by the competent authority
    ii. Plans of different entities (Major Ports, Central Govt and State Govt) shall be aligned to prevent duplication of the infrastructure facilities
    iii. Clear definition of priorities at national, state, and city level
    iv. Hinterland connectivity plan for each port based on inputs from state government/local authorities, road (MoRTH/NHAI) and railway authorities, IWAI
- This may not be viewed as binding on the state but considered to be directional and shall be aligned to the cargo forecast to ensure that excess capacity is not created, and other assets are not cannibalised
- Develop a plan/roadmap for transhipment port(s) including identification of incentives/initiatives required to upgrade exiting ports

d. Port led industrialisation shall be included and key industrial sub-sectors to be targeted are Semi-Conductors, Medi-Tech (hi-tech medical instruments) and Agri-Chem

- Requirement for attractive land pricing, flexible structure including provision for co-developer/master developer and international marketing capabilities
- Port to develop basis trunk infrastructure and some standard infrastructure for plug & play. For this existing land policy to be amended. Port Land Policy is under revision and draft is expected by next month.
- As an example Jafza model shall be preferred for port led industrialisation.
- Ports to come-up with commodity specific strategy and plug & play infrastructure requirements
- Setting up of separate entity under MoS to look after port led industrialisation

- **TA-11: Become Global Maritime leader through active participation in global maritime activities**

a. Creation of apex maritime body (Global Maritime body): Formation of separate executive organisation preferably through IPA as knowledge centre which would act as 'Face' of Indian maritime sector and represent India as a maritime nation, holistically both at Global and local level international events or conferences.

- Complex maritime ecosystem with many sub-sectors. Efficiency of the marine ecosystem is driven by many external factors such as multi-modalism, digitisation, connectivity, transport technology, regulatory regime etc.
- Given the interdependence with external factors, the proposed apex maritime body shall be established by the Government of India with representatives from different in fields of logistics. This will enhance integration of maritime ecosystem with the overall logistics ecosystem
- The apex maritime body shall have members from private sector/trade association.
- Members of the apex maritime body shall be involved in policy formulating committees of the government

b. Develop country-wise and port-wise collaboration strategies for enhancing cooperation

- areas covered ship operations & management, port logistics, marine finance, maritime law and Technology. Include education & port led industrialisation as the focus area
- Dubai to be include as strategic partner for port led industrialisation (Jafza) and technology (Dubai Trade) by exploring G2G collaborations/MoU

c. Increase Indian registry and controlled tonnage so as to enable India have more negotiating power at global level

- For a more market oriented and competitive platform, benchmarking of existing Indian registry shall be undertaken to understand the proposition offered by ship registries in HK, SIN, Panama, etc
- Fiscal incentives are required to increase Indian registry and controlled tonnage based on inputs from INSA
- **Ease of Doing Business:** Registration process shall be online and application for registry must be approved within 48 hours of submission
    i. Back end processes shall be outsourced to professional organisation and only the final approval to be tasked with the Govt with specific instructions for approvals to be granted in a time-bound manner as stated above. (e.g. Passport application processing by TCS and final approval by MEA)

d. Cooperation with BIMSTEC nations

- Notify ports (e.g. Cochin, Chennai, Tuticorin, Andaman & Nicobar etc) as Regional Transhipment Hubs for BIMSTEC (RTH)
- Support these RTH in attracting cargo by enhancing competitiveness. Example improve infrastructure & cost competitiveness (reduce VRC)
- Incentivise terminal operator at these RTH for handling BIMSTEC cargo. (Not to implement coastal tariffs)
- Ease of doing business among the BIMSTEC nations with "harmonising process"

Capacity Building

- **Thrust Area 7: Integration & enhancement of Indian maritime institutes of global standards**

a. Skill development shall be expanded to cover entire logistics ecosystem and shall not be restricted to maritime

b. Development of skills and human resources (Skills Gap Analysis)

- Jobs in the logistics sector do not look as attractive as jobs in other industries. Also, a lack of awareness is a cause of concern to attract people to this industry. But the demand is increasing.
    i. A Skill Gap Analysis (SGA) is proposed for all identified roles. National Skills Development Corporation (NSDC) to be nodal agency for the same. This should be Biennial exercise and not necessarily a one-time thing.
    ii. Industry specific requirements must be considered by aligning closely with the industry. This will help in addressing the gap of relevant as well as employable skills.
    iii. A special focus to be paid on digital roles as the entire sector is going through a digital transformation and the current manpower lacks it big time.
    iv. Design Vocational Training Courses of short duration (1-2 months) to mid-term duration (3-6 months). These programs can address gaps in job roles which are in the Semi-skilled/Skilled Category and do not require specific education qualification. Some of the Job roles could be Lashing, Picker/Packer. The target audience for this could be youth from tier 2 towns and can be also covered under government employment programs along with industry participation.
    v. A hire & train model is being proposed to address these challenges. Courses in line with the Skill Gap Analysis should be launched with close consultation with corporates in maritime sector.
    vi. Job assurance from the industry is required to attract the talent
    vii. Incentives/allowance per student is required from the government
    viii. Skill development shall be expanded to cover entire logistics ecosystem and shall not be restricted to maritime
    ix. Training of the truck drivers to be prioritised
    x. Incentives from the government to encourage industry participation in skill development

c. Accreditation & Certification from Existing Colleges

- Plethora of institutes offering courses on port Management/Supply Chain Management/Nautical Sciences/Marine Engineering. Apart from the Indian Maritime University, very few of them are accredited and have a standing in the corporate environment

- Improve quality of training institutes, training standards and accreditation/certification. Upgrade courses curriculum (dual degree) and educations standards (faculty) to global best practices. Research based courses by collaborating with global universities and student exchange
- A re-look at entire curriculum is important to make it more relevant and updated.
    i. A course steering committee is proposed with existing faculty, govt. experts and industry captains to be part of the same.
    ii. To increase the popularity of the courses, corporate tie-ups to ensure placements
    iii. Department for International Affairs to be constituted at IMU to facilitate students exchange programs with overseas universities.
    iv. IMU campuses to get global accreditation such as from International Maritime Organisation (IMO) for the offered courses.
    v. Separate accreditation body which will be responsible for accreditation and hence will maintain the quality of institutions
    vi. Extend IMU through satellite campuses in India & some select countries to capture untapped potential
    vii. Campus roadshows/Awareness Campaigns should be arranged

d. Focus on Gender Diversity to the sector

- The industry is male dominated, but there is a huge opportunity for women in the sector, especially since demand for seafarers is increasing
    i. A suitable affirmative action policy should be drafted to facilitate women admission in all courses.
    ii. An awareness campaign to be designed for attracting women to this industry in association with various media platforms
    iii. Corporates should also support this by providing support to diversity agenda while hiring.
    iv. Flexible working environment is the key to this
    v. A robust gender sensitisation program needs to be formed and should be part of every course/initiative being offered.
    vi. Form women networking groups to increase networking and support within the community.

- **Thrust Area 8: Development of Indian shipbuilding, repair recycling industry to world class level**

a. World class capabilities in ship building and repair (including barges, tugboats & other floating crafts) and ship recycling

b. Enhance financing capacity by developing a maritime fund

    - Adequate ship repair & shipping building capacity to be developed on east as well as west coast. Ship broken in east coast was moved in broken condition to west coast for repair
    - Indigenous shipyards are required to provide ship designs, offer cost & time competitiveness.
    - INSA to share the list of 4-5 critical points

- **Thrust Area 13: Enhance India's stature in global shipping and share in seafarer**

a. Promotion of 'Make in India' Barges by making it mandatory for coastal and Inland Water movement to use Barges Made in India by giving 1-2 years lead time before implementation.

    - Make in India initiative should not end up in creation of monopolies or increase cost of vessel/ownership. Today one can get a ship in less than 6 months.
    - There should be monitoring of available capacity within India. Technological advancement shall be encouraged by reducing duty on import

a. Emphasis on mental health of seafarers. Induction of training, health examination and counselling related to mental health pre-boarding of vessel

b. Development of online facility for ISPS/NSPS Audit compliance

    - Recommendations of such audits should not lead to expectation of investing in state of art equipment with no means of return by the terminal operator
    - Need to have similar standards across our coastline. *Today ports in Gujarat which are close to Pakistan don't have CISF and*

major ports continue to pay significant amount for deployment of CISF

c. Traffic separation scheme implementation in all ports
    - Setting up of vessel traffic separation schemes & vessel traffic management system should not be mandatory (as recommended in the report).
    - These should be done on need basis and at same time it should not end up in levying multiple charges onto port users.
    - The marine related charges have to be rationalised and shall not be collected under various heads e.g. VTMS charges, Light house dues

d. Benchmarking of existing Indian registry with ship registries in Hongkong, Singapore, Panama, etc. to understand the proposition offered. Organisation & Operating structure, processes, other KPIs
    - Traffic separation scheme shall not be mandatory as it add to the cost.
    - Benchmarking of existing Indian registry with ship registries in Hongkong, Singapore, Panama, etc. to understand the proposition offered

Multi-Modalism

- **TA-14: Promotion of Inland Waterways Transport**

a. Increasing share of 'inland water cargo' and 'coastal cargo' to enhance demand of ships
    - Actual issues on the ground
    - Terminal package: Terminals at major traffic centres along waterways should be packaged as an "Integrated Terminal Package" on PPP basis. Integrated terminal development by bundling specific set of terminals per PPP player to leverage network benefits.
    - Industrial parks and logistics hubs at such locations should also be integrated to allow the operator to provide end-to-end logistics support.
    - Vessel Fleet licensing: fleet-level licensing across each waterway to ensure scale & quality of operations. Cap number of fleet licenses for initial year.
    - Exclusivity: Given the significant investment and market risk, geographical exclusivity of at least 100 km radius for the private players.
    - Tariffs: Tariff freedom for both CRC and VRC. Amendment in IWAI Act may be required to address current mechanism of tariff notification by IWAI/MOS

- **TA-14: Promotion of Inland Waterways Transport to be applicable on coastal shipping)**

a. MoS is emphasising on (i) developing 22-23 new inland waterways, (ii) enhance trade with neighbouring countries (iii) develop 10 Ro-Ro & 60 Ferry terminals (iv) encouraging PPP, (v) Financing of inland vessels (vi) rationalise tax regime (GST rate, tonnage tax etc) across different mode and (vii) attract cargo from large Indian PSUs

b. Terminal locations shall be identified based on techno-commercial viability. Terminal development shall not be limited to mega terminals. Development of small "built to suit" terminals with low capital costs shall be encouraged. Ensure infrastructure development to not result in high fixed overhead.

c. Government to prioritise development of last & first mile connectivity, ensure data availability (LAD, air draft etc), ensure water depth (LAD) and night navigation facility (river/coastal)

d. Terminal locations shall be identified that can result in time saving, instead of cost saving only. Supply chain delays will erode all transport cost savings (Surat – Bhavnagar)

e. Multimodal terminals development shall be categorised as (i) multimodal with Ro-Ro facility (rail/road) and (ii) Multimodal using cargo handling

f. Holistic terminal (IWT, coastal jetties and port terminals) development policy integrating plans/objectives of the State and the Central Government to prevent cannibalisation and duplication of infrastructure.

g. Dedicated infrastructure for coastal/IWT shall not be developed and existing facilities shall be incentivised to use available capacity. Streamline processes to encourage handling of coastal/IWT /EXIM at one common facility

- **Encourage multi-modal transport system to result in enhancement of rail share**
    - **Infrastructure:** Upgradation plan for non-DFC routes to promote double stacking of ISO containers
    - **Rolling Stock:** Adequate number of wagons and locomotives, especially for bulk shall be maintained to ensure rolling stock availability within 4 hours of requisition
    - **Policy:** Policy of Indian Railways on pricing of containers is required to be rationalised to ensure greater modal share. Today

pricing benefits being passed on are more short term and in fits and bouts

- For seamless modal exchange, regulatory processes, documents and tax regime is required to be standardised
- Cargo origin-destination data (already captured under E-waybill) shall be analysed while planning infrastructure development to ensure optimal utilisation and efficacy,
- Enhance DFC feeder network to leverage maximum benefits of DFC.
- Eastern DFC network between Ludhiana and NCR shall be upgraded for double stack container operations
- Railway shall provide scheduled services based on time-table
- Rail freight to be rationalised, especially over shorter leads/distance to encourage modal shift
- Streamline process to handle EXIM & domestic cargo on one train

Ease of Doing Business

- **TA-4: e-Governance in Maritime Sector for Ease of Doing Business and Paperless Operations**

  a. Digitisation approach:

  - The scope of NLP Marine to be expanded to include other logistics mode.
  - Should be based on a distributed computing paradigm with a cloud-native design strategy. We should not try to "fit" a product to meet the requirements. Being an important intervention, design must be purpose-built from foundational blocks.
  - Promote Standardisation & Harmonisation with all concerned Ministries, and encouraging private sector participation via the "Latch-On" services and foster innovation within the start-up communities
  - One single interface and no manual filling for desirable user experience by creating only. User experience is less-desirable with use of multiple portals (track & trace, clearance, payments, customs, CFS etc).
  - Should be setup as a separate entity with a mandate to execute the vision of the Government (identical to GSTN).
  - To facilitate data exchange, a value exchange system that assigns credit for data contribution and offsets the credit when data is consumed.
  - MOS digitisation initiatives include NLP Marine with latch-on provisions, digitisation of major port processes (1800 process reduced to around 200) and smart ports
  - Mandatory on-boarding of all stakeholders including Ministry of Finance, Ministry of Commerce & Industry, Bank and other Partner Government Agencies (PGA) will be required for end to end seamless solutions
  - Digitisation process of major ports shall be expanded to include all non-major as well as state ports
  - Industry associations shall be involved/consulted while developing the digital platform to integrate the latch-on requirements

- **TA-10: Reforms in all Maritime Acts/Laws/Regulations/Policy**

a. Major Port Authorities Bill, 2020

  - Clarity on tariff fixation

b. PPP Policy

  - Review mechanism in Concession Agreements
  - Treat all Concessionaires equally and at par with regards to dredging, connecting infrastructure, power etc,. Don't discriminate in port support facilities because of timing of concession.
  - Implementation of Arbitration Awards:
    i. Impact on liquidity of BOT operator due to funds locked up in various arbitration awards in their favour against respective Major ports/PSU

    ii. Cabinet Committee on Economic Affairs issued directions to all PSUs to release 75 % of the award amount pending in any appeal against Bank Guarantee

    iii. Government to issue suitable directions to banks for not insisting 100 % margin for issue of such BGs
  - Viability Gap Funding for Bulk Terminals for tackling pollution

c. Revised Model Concession Agreement

  - <u>Actual Project Cost:</u> Concept of total project cost is limited to cost estimates at planning stage. This would result in numerous issues with the lenders and make financing of the project even more difficult. Total project cost shall be amended to actual project cost to include actual cost incurred

- Concession period of maximum of 50 years with the ROFR clause to the existing Concessionaire - Life of a berth is normally 50 years
- Clearances: Authority to ensure clearances from MoEF should be obtained prior to bidding and provide security clearance, if required for contractors
- Supporting Infrastructure: Authority shall ensure availability of supporting project infrastructure before the OCD.
- Usage of Assets: Permission to use the assets handed over as well as facilities created between the Date of Award and COD
- Change in Scope: All Change in Scope provisions shall be based on discussion and mutual agreement between the parties.
- Change in Law: Any additional cost due to change in law shall be met by the Authority
- Performance Standards: Provide performance standards for the Authority along with provision for Liquidated Damages.
- Minimum Guaranteed Traffic: Gradual increase over the period of first 5 years subject to a max 40% of capacity p.a for the remainder of the Concession.
- Level playing field: Authority should ensure dredged draft alongside the berths for similar cargo is same unless such deeper draft is technically not feasible
- Future Ready: In case of need for deeper channels in future, the port may be required to increase the depth at the entrance channel.
- Payments: Penalties for delay in payment to the Authority are very high- 6% (shall be 2%) over and above 10 Year G Sec rate
- Additional Requirement: Additional utilities and land shall be provided at SOR rates as against the proposed 1.2 time the SOR
- Termination: Termination compensation to be rationalised – include 100% debt due payment/actual project cost/200% equity. Compensation payment provision for termination before COD is required. When there is no debt due, the Authorities tend to interpret the compensation payable is Nil.
- Escrow: Escrow account mechanism shall be replaced with rolling bank/performance guarantee.

d. Land Policy

- High lease rentals & escalation – tend to treat Ports like private commercial enterprises rather than service providers

e. Others

- Service Exports from India Scheme (SEIS) to promote the investments in upgradation/setting up ports and logistics assets
- Actual Project Cost: Total project cost shall be amended to actual project cost to include actual cost incurred to enhance attractiveness for lenders
- Termination provision including compensation payment for termination before COD is required enhance market attractiveness
- Review mechanism in Concession Agreements is required to address unforeseen situations (COVID-19) and enhance market attractiveness
- Given the long concession period, provision for enhancing capacity by developing infrastructure (berth length etc.) after reaching certain capacity threshold is required.
- Selection of PPP operator shall be based on commitment on efficiency enhancement and capacity enhancement

Implementation of the Maritime Vision

a. Empowered committee shall be constituted to facilitate implementation of MIV and monitor its progress

b. Need for a professional program management entity for initial 2-3 years to streamline the process, prepare documents, policy and deliver few projects

c. Program management entity shall closely work with JS (SM&PPP) by providing external support/capacity to deliver on MIV recommendations in next 3 years

d. MIV monitoring group with representatives Ministry of Shipping, port trusts, maritime boards, and trade associations include CII and IPPTA shall be formed to monitor the progress and implementation of MIV.

DIGITALISATION:

I. The e-system of transmission of data and documentation must have a robust digital system which should address following legal concerns:

1. Data Protection
2. Data Confidentiality
3. Ensuring robust procedures and policies in restricted access to data, on need to know basis or limited purpose, consensual access to data, restricted authorisation ensuring transmission and dissemination is to intended user and for intended purpose.
4. Ensure best protocols, procedures, systems and protections in place to safeguard the information provided by stakeholders and continue to keep and update such protocols, procedures, systems and protections in place, in order to enforce and maintain the utmost confidentiality and to prevent and protect against unauthorised use,, unlawful processing and against accidental or unlawful destruction, loss or alteration or damage, unauthorised disclosure of or access to of the information provided by stakeholders.
5. Effective and continuous monitoring of the system for identifying loopholes in the system and to eliminate potential unauthorised use, illegal use or breach.
6. Strict demarcation of liability & responsibility, and enforcement of penalty on unauthorised/illegal use or breach of system.
7. Establishment of data protection centres with a quick action time and recovery time in case of any concerns.
8. Established guidelines on use, right to delete, access, transmission and dissemination of data in line with Indian and international laws.

II. On issue of Bill of Lading and other documents:

i. **Electronic Bill of Lading**

The Electronic Bill of Lading replicates the functions of all traditional B/L[1], the transfer of document in an e-form and correlative transfer of title over the goods such transfer operates can be replicated easily electronically and in a safe environment. An eB/L is an electronic record shall have legal and functional equivalence of an original paper B/L. The establishment of title and transfer of delivery to the rightful owner can be achieved electronically using a 'Agreement' between all the parties and technological solution.

An electronic bill of lading (eB/L) is not simply an electronic version of the paper bill of lading. Rather it is a combination of an agreement and technology which can replicate the functions of a traditional paper bill of lading.

Benefits of eB/L are as follows

- Accelerates payment and time to cash due to faster processing
- No paper documents to process and manage
- Reduction in Labor cost and processing time
- Electronic Presentation of trade documents with an eB/L
- Reduction in Letters of Indemnity and Demurrage costs
- Auditability and traceability of electronic documents between all parties
- Can accept presentations outside working hours
- Reduction in errors as no rekeying in of info
- Reduction in frauds and lost Bills of Lading
- Reduction in courier costs, bank charges and manpower
- Positive environmental impact

Service Providers for facilitating eB/L

Considering the legal and technological requirements of implementing eB/L, there is a need of a third party service provider to facilitate the eB/L transaction. These service providers will need to be registered with office of DG Shipping basis the follow qualification criteria

1. Should have a strong technology platform with proof of concept established with successful transactions in India
2. Should have a well drafted 'agreement/Rule Book' acceptable across all legal domains globally to ensure sanctity and enforceability of eB/L in all countries.
3. Should be registered with IPA as a Latch On to the Indian Port Community system
4. Should be using a technology validated and endorsed by the International Group of P&I CLubs

Various Govt Dept of customs and Reserve Bank of India including all Indian Banks will issue necessary circulars internally to address the below listed challenges in implementation of eB/L in India

1. In case of trade financing by way of Letter of Credit/Documentary credit, the seller/shipper has to submit to the bank various documents physically viz original invoice, packing list, shipping bill, certificate of origin, legalisation documents, EIA certificate and several other documents basis the nature of the goods and requirements of the buyer (LOC/Purchase Order etc), the same should be accepted by the bank in electronic format (EDI,XML,PDF)

2. Bill of Lading being a Negotiable Document attracts Stamp Duty in several states in India. So along with defining the eB/L process, the process of payment of stamp Duty for eB/L will need to be established.

3. Circulars or regulations to assist Banks and forex dealers to ensure usage and acceptance of eBL

4. The contents of the Bills of Lading are as provided by Shipper to the Shipping Line as required under terms of the Letter of Credit or the Purchase Order between the parties to Sale Contract. The same should not prevent the issuance and circulation of eB/L which are actually already regulated through the eUCP 600.

5. Since the eB/L is a negotiable document the issuance of the same and subsequent transfer from one stake holder to the other will need to be done with use of encryption key or Digital Signature or both

Recommendations

1. The **IGP&I** approved services providers (providing eB/L Blockchain solution) should be given option to latch on the PCS platform.

2. Govt of India should issue a notification & directive to **Reserve Bank of India including all the Indian banks and Insurance Companies** to accept the electronic mode of Bill of Lading OR transactions done through these IG P&I approved eB/L portals/solution providers which can be latched on with PCS.

3. Once all Shippers, consignees, CHA's and their respective banks are brought under the purview of eB/L experience and later like eDO , the same should be made compulsory across all the transactions through an order from RBI to all foreign exchange dealers in India.

4. Once the above mentioned challenges are clarified & worked upon, CSLA in concurrence with necessary stakeholder(s) can discuss and provide an SOP document on how eB/L can be linked as an end to end solution for stakeholders with each role clearly defined.

5. Since at UN level, 'UNCITRAL Working Groups IV' is in working on eCommerce which covers eB/L and is in process of formulation international laws, convention, standards. India should adopt the recommendations of this UN group.

6. Jurisdiction for disputes on Bill of Lading shall be as per terms and conditions under Bill of Lading. The agreement for electronic bill of lading transmission shall be as agreed between the parties.

ii. **Other documents:**
The other documents which require NOC, approvals, checks, coordination with various departments like Port Health Officer, Customs, Immigration, Ports, terminals and other stakeholders should:

1. Have a common interface and system.

2. Ensure every stakeholder interface is seamlessly connected to another interface.

3. Zero manual intervention is required when any information is already uploaded in any of the stakeholder interface.

4. Digital will mean electronic transmission and not scanning and sending by email.

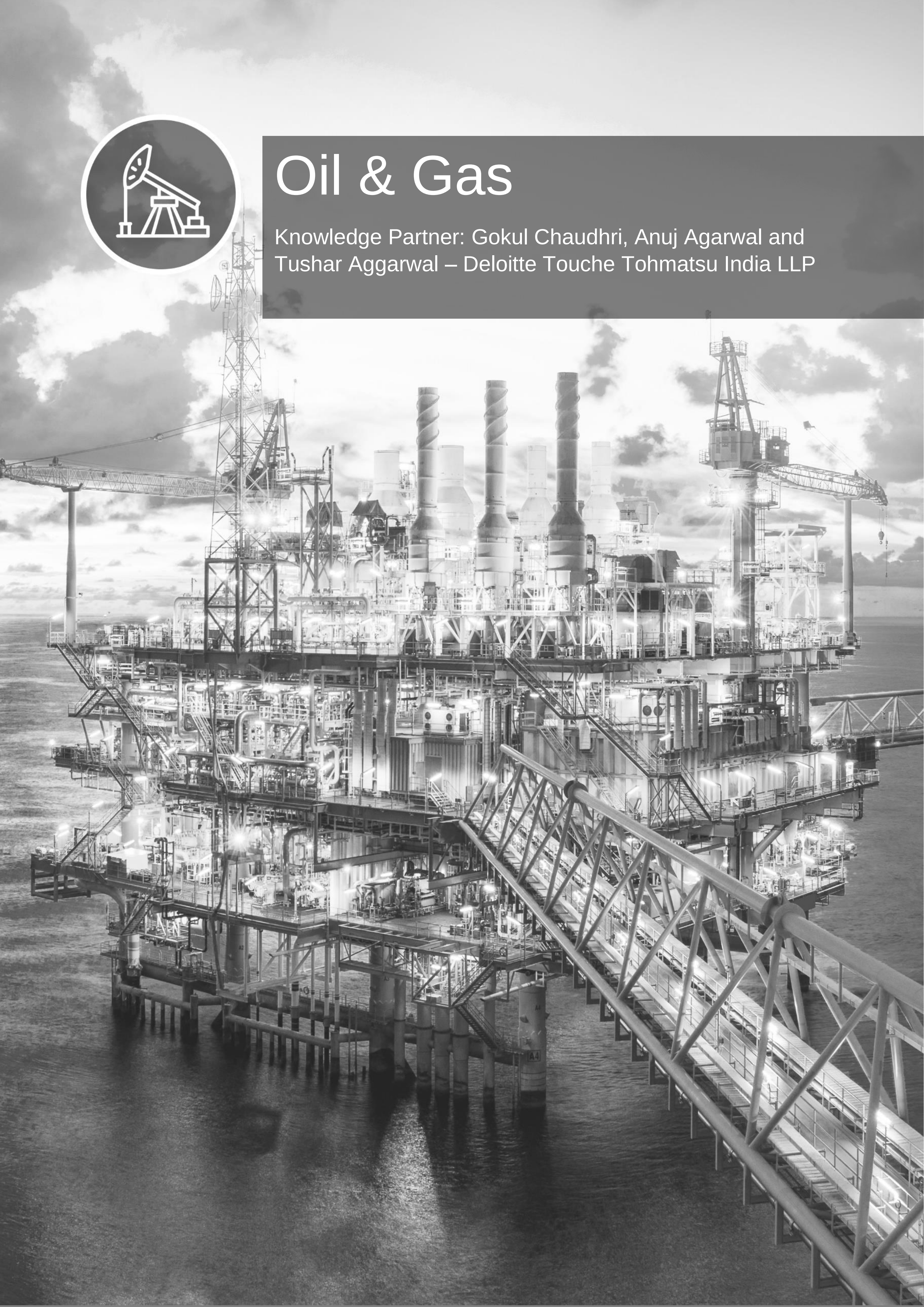
5. Systems or files used should be common or integrated with Shipping Lines transfer/dissemination of data systems.

6. Easy validation of data without duplication.

NOTE

Oil & Gas

Knowledge Partner: Gokul Chaudhri, Anuj Agarwal and Tushar Aggarwal – Deloitte Touche Tohmatsu India LLP



1. INTRODUCTION

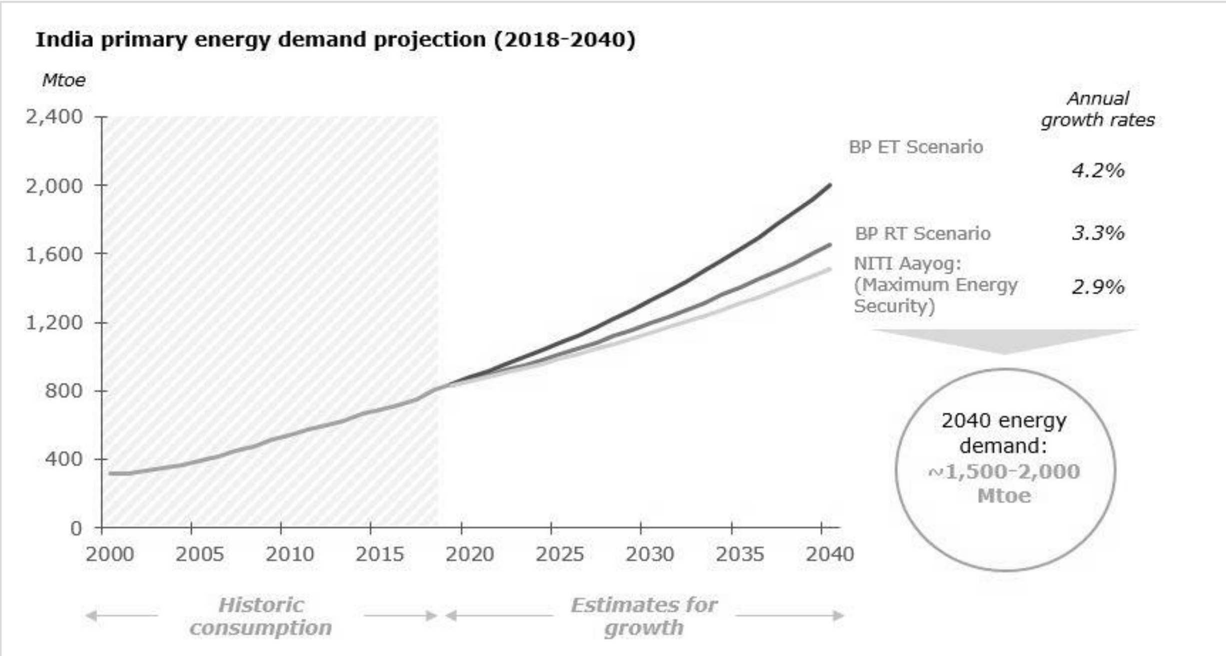
MARKET DESCRIPTION

1.1 With an estimated Gross Domestic Product (GDP) of US$3.2 trillion (~Euro 2.86 trillion) in the year 2019[1], India is the fifth-largest economy in the world ranked by nominal GDP and is likely to become the third-largest economy globally by 2025[2]. The energy sector is crucial for sustaining and further improving the growth momentum of the economy.

1.2 India's energy consumption is projected to grow at 4.2% per annum under Evolving Transition (ET) scenario up to 2040, faster than all major economies of the world.[3]

continue to be met predominantly by fossil fuel sources, i.e., coal and oil, dependence on renewable sources of energy and nuclear power too is expected to increase many folds. Renewable energy consumption will surge driven largely by growth in solar capacity.

The government had set a target of installed renewable energy capacity of 175 Gigawatt (GW) by 2022, comprising 100 GW from solar, 60 GW from wind, 10 GW from biomass and 5 GW from small hydro power. Another target to achieve 450 GW by 2030 has been set by the government.

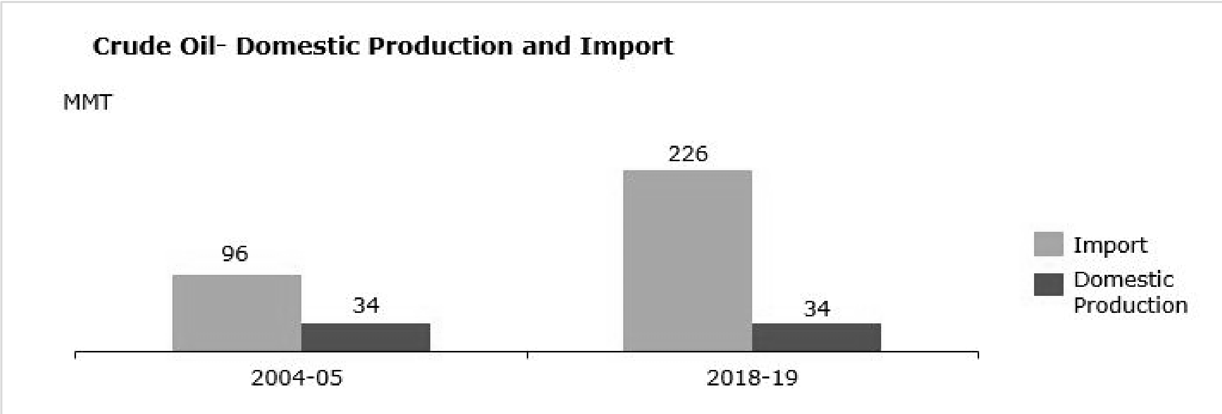


1.3 While India's energy demand increased to 809.2 million tonnes of oil equivalent (Mtoe) in 2018, the per capita consumption of energy is still much lower than the world average due to a large population base. India's share of total global primary energy demand is set to roughly double to ~11% by 2040, underpinned by strong population growth and economic development. The energy demand is expected to reach roughly 1,928 Mtoe by 2040.[4]

1.4 India's primary energy basket is skewed towards fossil fuels, coal being the main source of energy. Though country's energy requirements in the medium to long run shall

1.5 In the primary energy space, Oil and Gas industry is an important pillar and ranks amongst India's eight core industries. This industry is one of the highest contributor to the exchequer, by way of taxes, duties, levies, lease, license fee, royalty, cess and profit petroleum.

1.6 India's crude oil consumption during FY2018-2019 was 260.7 Million Metric Tonnes (MMT)[5], which was met by domestic production to the extent of 34.2 MMT and the balance by imports. India is one of the largest importers of crude oil in the world with imports constituting more than 80% of the total domestic oil consumption.

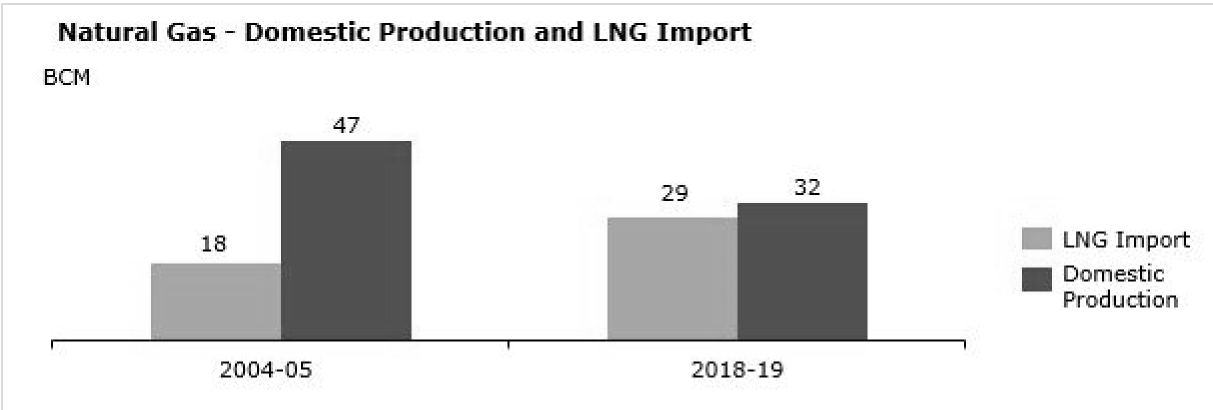


vIndia has stopped importing crude oil from Iran and Venezuela, in light of sanctions imposed on both countries by the United States of America (USA). Earlier, Iran supplied almost 10% of India's needs. India is now diversifying supply sources to cut dependence on oil-rich Middle East. US oil supplies to India have jumped ten-fold with imports rising to 6.2 MMT in FY2018-2019[6]. Indian Oil Corporation Limited (IOCL) signed agreement with Russia's Rosneft for supply of 2 MMT of Russian crude oil[7]. However, India has potential to meet a higher share of demand from domestic production with total crude oil reserves of 594.49 MMT as on 31 March 2018 (provisional).[8]

1.7 India's natural gas consumption including Liquefied Natural Gas (LNG) during FY2018-2019 was 60.8 Billion Cubic Metre (BCM)[9]. Sector wise consumption[10] of natural gas is as follows:

- Fertilisers industry (27.7%)
- Power generation (24.28%)
- City gas distribution (17.1%)
- Others (Steel, Petrochemicals, refinery, etc. (32.8%)

1.8 India increasingly relies on imported LNG and was the fourth-largest LNG importer in 2018, accounting for 7.1% of global imports[11]. The domestic production of natural gas during FY2018-2019 amounted to 32.1 BCM. India has potential to aid growing demand of natural gas of various sectors from domestic production, with total reserves of 1,339.57 BCM of natural gas as on 31 March 2018.[12]



1.9 In FY2018-2019, domestic production of petroleum products increased to 262.4 MMT from 254.3 MMT during FY2017-2018. Further, total domestic consumption of petroleum products increased to 213.2 MMT from 195.6 MMT during FY2017-2018[13].

1.10 While India is a net importer of crude oil, it is a net exporter of petroleum products with High Speed Diesel (HSD) and Motor Spirit contributing a major share to exports. Export of petroleum products was 61.1 MMT during FY2018-2019 and rose from US$35 billion (~Euro 31 billion) in FY2017-18 to US$38.3 billion (~Euro 34.2 billion) in FY2018-19.[14]

1.11 India's economic growth is closely connected to energy demand. The need for oil and gas is projected to grow further, providing vast opportunities for investment. To meet this demand, the government has adopted various policies, such as allowing 100% Foreign Direct Investment (FDI) in many segments of the sector, such as natural gas, petroleum products, pipelines and refineries (except for investment in public sector undertakings). This move, along with various others, has made the oil and gas sector in India a more viable sector to invest. Today, India's oil and gas sector attracts both domestic and foreign investment, as seen by the presence of Indian and foreign companies such as Reliance Industries Ltd (RIL), Essar, BP, Shell and Cairn. The cumulative foreign investment in the petroleum and natural gas sector between April 2000 and March 2019 stood at US$7.02 billion (~Euro 6.18 billion)[15].

DEVELOPMENTS IN THE SECTOR

Recent developments – Policy framework

The Prime Minister (PM) has set a target for reduction of 10% in energy import dependency by 2022.[16] In this regard, the incumbent government has taken several policy as well as administrative measures in order to augment domestic oil and gas production and reduce dependency on imports, for meeting the energy requirements of the country. As a result of the radical policy changes, the government is expecting cumulative investments of ~US$40 billion in the Indian Exploration and Production (E&P) sector in the short term (4 - 5 years)[17].

Key policy developments in the oil and gas space have been discussed below.

1.12 **Hydrocarbon Exploration & Licensing Policy (HELP)**

To stimulate new exploration activity for oil, gas and other hydrocarbons, in March 2016, the Union Cabinet approved a new Hydrocarbon Exploration & Licensing Policy (HELP). As part of this change, the government endeavoured to make a policy shift from the extant Production Sharing Contract (PSC) model, based on Pre-Tax Investment Multiple (PTIM) and cost recovery, to Revenue Sharing Contract (RSC) model for licensing of hydrocarbon acreages. Under the new regime, the government will not be concerned with cost incurred by the explorer, and will instead receive a share of gross revenues from the sale of oil, gas etc. Contracts for hydrocarbon acreages will be based on 'biddable revenue sharing' wherein bidders would quote revenue share in their bids, forming a key parameter for selection of the winning bid. The bidder giving highest net present value of revenue share to the government, as per transparent methodology, would be preferred under such parameter.

Key features of HELP are as follows:

(a) Open Acreage Licensing Policy (OALP) - In OALP, a bidder can also apply to the government seeking exploration of any block, thereby not restricting exploration activity only to blocks put on tender by the government. For this purpose, the investor will submit Expression of Interest (EoI) for contracting the block/s of their choice, which will be subsequently awarded through bi-annual bid rounds.

(b) Uniform licensing system covering exploration and production of all hydrocarbons, i.e. oil, gas, coal bed methane (CBM), etc., under a single license and policy framework.

(c) National Data Repository (NDR) – NDR under the aegis of Directorate General of Hydrocarbons (DGH) provides seamless access to India's E&P/seismic data to investors through digital medium, with a view to harness the potential of India's large basinal area.

(d) Pricing & Marketing freedom for crude oil and natural gas produced under the new contractual and fiscal regime.

(e) Concessional royalty regime for deep water and ultra-deep water areas; no royalty payable for the first 7 years and thereafter, a concessional royalty rate of 5% for deep water areas and 2% for ultra-deep water areas. For shallow water areas, royalty has been reduced from 10% to 7.5%. For onland fields, royalty rate to be 12.5% and 10% for Oil and Gas & CBM blocks respectively.

(f) Petroleum operations or coal bed methane operations undertaken under specified contracts awarded as part HELP or OALP are exempted from the levy of Basic Customs Duty (BCD) and attract concessional Integrated Goods and Services Tax (IGST) rate of 5%.

The Ministry of Petroleum and Natural Gas has signed contracts for seven blocks awarded under OALP-IV on 20 January 2020. The total area awarded is spread over seven onland blocks, covering 18,510 square kilometre (sq. km) and three sedimentary basins. The seven blocks awarded have resource potential of approximately 33 billion barrels of oil and oil equivalent gas. The fifth bid round under OALP, with close to 20,000 sq. km of acreage up for bidding, opened in January 2020 and is likely to close in April 2020. Till January 2020, 81 Petroleum Exploration Licences (PELs) in 94 exploration blocks, covering an area of 136,790 sq. km have been awarded to leading E&P companies under four rounds of OALP[18].

Also, total data uploaded in NDR till 30 November 2019 is 2.30 million line kilometres of 2D Seismic Data, 0.78 million square kilometres of 3D Seismic data and 17,588 exploratory wells.

1.13 Discovered Small Field Policy (DSF Policy)

The government brought out the Discovered Small Field Policy, 2015, to early-monetise the already discovered hydrocarbon fields. Discovered fields are areas that were already discovered but could not be monetised due to various reasons such as isolated locations, small size of reserves, high development costs, technological constraints, fiscal regime, etc.

In May 2016, 67 discovered small fields were clubbed into 46 contract areas and were offered through an open and transparent international competitive bidding process under a new fiscal regime in the DSF Bidding Round 2016 (DSF Policy Bid Round-I). The new fiscal terms included revenue sharing arrangement with the government (instead of cost sharing), marketing and pricing freedom for both oil and gas, moderate royalty structure, waiver of oil cess, etc. Subsequently, the Cabinet Committee on Economic Affairs (CCEA) has approved award of contract in 31 contract areas. It is expected that locked hydrocarbon volume of 40 MMT of oil and 22 BCM of gas will be monetised over a period of 15 years.[19]

DSF Round II was introduced to extend the DSF Policy to identified discovered small fields/un-monetised discoveries for offer. The round included 25 contract areas covering 59 fields discovered oil and gas fields with estimated resources of 190 Oil and Oil Equivalent of Gas[20]. The Empowered Committee of Secretaries (ECS) and Group of Ministers approved the award of 23 contract areas to highest ranked bidders on 1 March 2019 as part of DSF Bid Round – II.[21]

1.14 Creation of strategic crude oil reserves

Creation of strategic crude oil reserves is a significant step towards energy security of India and preventing supply disruptions, considering dependency on oil imports. In Phase I of the program, storage facility of capacity 5.33 MMT at three locations viz. Visakhapatnam, Mangalore and Padur is operation. Under Phase II, the Union Cabinet has provided in principle approval for creation of additional storage facilities of 6.5 MMT of crude oil at Chandikhol in Odisha and Padur in Karnataka with an envisaged investment outlay of INR110 billion (US$1.6 billion). Work on two more facilities at Bikaner in Rajasthan and Rajkot in Gujarat is expected to be initiated soon.

To incentivise establishment of such reserves, the government vide Finance Act, 2016, had provided an income tax exemption to income earned by foreign companies on account of storage of crude oil in a facility in India and sale of crude oil therefrom to any person resident in India, subject to satisfaction of prescribed conditions. Further, Finance Act, 2017 has exempted income arising to foreign companies on sale of leftover stock of crude oil from the strategic petroleum reserves after expiry of the agreement/arrangement, subject to certain conditions. The Finance Act, 2018 further extended this exemption to income arising from sale of leftover stock of crude oil on termination of the agreement/arrangement in accordance with terms mentioned therein. The Finance Act, 2020 (<<*assuming by the time paper is finalised, Finance Bill would have received presidential assent*>>) has exempted income accruing or arising to Indian Strategic Petroleum Reserves Limited (ISPRL), a wholly owned subsidiary of Oil Industry Development Board under the Ministry of Petroleum and Natural Gas, under an arrangement for replenishing crude oil in its storage facility in pursuance of directions of Central government, provided crude oil is replenished within three years from end of financial year in which it was removed for the first time.

The Abu Dhabi National Oil Company (ADNOC) and ISPRL have entered into an agreement for investment by ADNOC of about US$400 million by way of storing crude in the underground rock cavern in Mangalore of capacity 5.86 million barrels (0.81 MMT). The period of storage will be 3 years with an automatic extension of 2+2 years.[22] In addition, ADNOC has agreed to hire underground strategic storage capacity of 1.25 at Padur[23].

ISPRL also signed an agreement with Saudi Aramco to store 4.6 million barrels of oil by leasing a part of the 2.5-million tonnes (MT) Padur storage during PM Narendra Modi's visit to Saudi Arabia[24].

1.15 **Unbundling of GAIL (India) Limited**

GAIL (India) Limited has been instructed by Mr. Dharmendra Pradhan, Minister of Petroleum & Natural Gas and Minister of Steel, to plan to separate its gas marketing and transmission businesses.[25] Through this separation, the government wants to bring greater transparency in price determination, address the concerns of private and other state owned players, and eventually create a gas-trading hub. The government is considering to sell the pipeline business to a strategic investor post 2022[26].

1.16 **City Gas Distribution (CGD)**

A typical CGD network provides piped natural gas to households, commercial establishments and industries, and Compressed Natural Gas (CNG) for vehicles. In addition to being environment friendly, CNG is also usually cheaper than Liquefied Petroleum Gas (LPG), Petrol and Diesel. At present, 91 geographical areas including major cities like New Delhi and Mumbai are operational. As of October 2019, 1838 CNG stations are available catering to the requirement of 3,454,000 CNG vehicles in the country[27].

The government is keen on expanding the CGD network in the country and Petroleum and Natural Gas Regulatory Board (PNGRB) will soon start bidding for 44 Geographical Areas (GAs) under 11th round of CGD[28]. CGD has been granted 'Public Utility Status' by Ministry of Labour and Employment[29]. 86 and 50 GAs have been authorised under the 9th and 10th CGD Bidding rounds respectively[30]. With successful implementation of these CGD networks, it is envisaged that more than 70% of India's population in 229 GAs and 407 districts will have access to natural gas against 19% of population today. Over the next decade, it is estimated that natural gas demand will increase from 24 million metric standard cubic metres per day (MMSCMD) to ~60 MMSCMD[31].

1.17 **Production Enhancement Contracts (PEC)**

In order to raise production from existing mature fields, the government through PEC is encouraging infusion of world-class E&P technologies and practises. India, at present has over 61,851 sq. km of area under nomination fields, which are reaching the maturity stage. The current production from these fields is estimated at 25.6 MMT Oil and 24 BCM[32] gas. Introduction of PEC is envisaged to encourage private and foreign investments in these fields and adoption of best-in class management practises which would aid in improving India's domestic production. Oil and Natural Gas Corporation Limited (ONGC) had invited bids to raise output from its 64 marginal fields. The winning firm will have complete marketing and pricing freedom for their share of incremental production[33].

1.18 **National Policy on Biofuels[34]:** The government has notified National Policy on Biofuels 2018 on 8 June 2018, which is expected to give boost to the biofuel programme of the country. The major features of the Policy are as below:

- Categorisation of biofuels as 'Basic Biofuels' viz. First Generation (1G) bio ethanol & biodiesel and 'Advanced Biofuels' – Second Generation (2G) ethanol, bio-CNG etc. to enable extension of appropriate financial and fiscal incentives under each category.
- Expanding the scope of raw material for ethanol production by allowing use of sugarcane Juice, sugar containing materials like sugar beet, sweet sorghum, starch containing materials like corn, cassava, damaged food grains like wheat, broken rice, rotten potatoes, unfit for human consumption for ethanol production.

- The Policy allows use of surplus food grains for production of ethanol for blending with petrol with the approval of National Biofuel Coordination Committee.
- With a thrust on Advanced Biofuels, the Policy indicates a viability gap funding scheme for 2G ethanol Bio refineries of INR50 billion in 6 years in addition to additional tax incentives, higher purchase price as compared to 1G biofuels.

The government has approved 'Pradhan Mantri JI-VAN (Jaiv Indhan-Vatavaran Anukool Fasal Awashesh Nivaran) Yojana' for providing financial support to Integrated Bio-Ethanol Projects using lignocellulosic biomass & other renewable feedstock, with a total financial outlay of INR19.695 billion for the period FY2018-2019 to FY2023-2024.

Under Sustainable Alternative Towards Affordable Transportation (SATAT) scheme, government has envisaged to establish 5000 Compressed Bio Gas (CBG) plants across the country by 2023. Under this scheme, Oil Public Sector Undertakings will procure CBG from potential entrepreneurs at an assured price.

To encourage Biodiesel produced from Used Cooking Oil (UCO), Oil Marketing Companies will set up UCO processing plants at 200 locations[35].

1.19 **Privatisation of Bharat Petroleum Corporation Limited (BPCL)**

The CCEA, chaired by PM Narendra Modi has accorded 'in-principle' approval for strategic disinvestment of Government of India's shareholding of 53.29% in BPCL along with transfer of management control. EoI for stake sale was issued by the government on 7 March 2020. BPCL has a strong presence in refining, fuel marketing and infrastructure accounting for ~15% share in refining, 26% share in fuel retail, 24% share in retail outlets and 14% share in pipelines[36]. Stake in BPCL offers the buyer access to one of the fastest growing energy markets in the world. The objective of the government is to bring in new management and technology through a strategic investor and increase competition in the downstream sector. Numaligarh Refinery Limited (NRL) will not be a part of the disinvestment.

1.20 **Transportation Fuels Marketing Reforms:**

The CCEA chaired by PM Narendra Modi approved the review of guidelines for granting authorisation to market transportation fuels[37]. This has represented a major policy reform for granting authorisation for marketing fuels since 2002. The government has introduced these reforms to encourage investment from private players, including foreign players, ensure better competition and better services for consumers. The major features of the policy are as below:

- Lower entry barrier: Entities seeking authorisation need to have a minimum net worth of INR2.5 billion vis-à-vis the current requirement of INR20 billion prior investment.
- Non-Oil Companies can invest in the retail sector
- For retail, a minimum 100 retail outlets need to be setup and each outlet should have facilities for at least one new generation alternate fuel (CNG, LNG, electric vehicles, biofuels) within 3 years of operations.
- Authorised entities are required to set up minimum 5% of the total retail outlets in the notified remote areas within 5 years of grant of authorisation.
- Entities seeking authorisation can apply for retail or bulk or both

1.21 **National Gas Grid**

The government has proposed to expand the National Gas Grid to 27,000 kilometre (km) from the present coverage of 16,500 km. The government is constructing 13,500[38] km of natural gas pipeline to supplement the existing transportation infrastructure.

- Pradhan Mantri Urja Ganga Project – The 2,665 km Jagdishpur- Haldia- Bokaro-Dhamra pipeline is being constructed and is estimated to be completed by December 2020. It aims to connect five states in hinterland namely Uttar Pradesh, Bihar, Jharkhand, Odisha and West Bengal.
- Barauni Guwahati pipeline – To extend the gas grid to North East, a 729 km long pipeline is also under construction. It is estimated to be completed by December 2021.
- North East Region Gas Grid – Indradhanush Gas Grid Ltd, a joint

venture by five Oil & Gas public sector companies is developing a gas grid for north-eastern region with total length of 1,656 km pipeline. Cabinet has approved a Viability Gap Funding of 60% of estimated project cost for setting up the gas grid in North East India[39].

- Kochi – Kottanad Bengaluru Mangalore Pipeline – GAIL (India) Limited is constructing 872 km pipeline in Kerala and Tamil Nadu. It is in advanced stage of construction.

1.22 **Other Developments:**

(a) Pradhan Mantri Ujjwala Yojana (PMUY): The government launched PMUY to provide 80 million deposit free LPG connections to poor households in the country. Under this scheme, the government has already achieved a target of providing 80 million LPG connections to adult women of poor households on 7 March 2019, seven months ahead of schedule[40]. Further, government is focussing on providing smaller 5 kilogram cylinders to improve consumption and increase refills by beneficiaries[41].

(b) The government has prepared a project to conduct 2D seismic surveys of all sedimentary basins of India to generate seismic data for initiating E&P activities. As on 30 November 2019, surface coverage of 41,902 Line Kilo Meter (LKM), out of 48,143 LKM has been achieved under National Seismic Programme 2019.

(c) Ministry of Petroleum and Natural Gas has prescribed minimum local content for Petroleum and Natural Gas products under Department of Promotion of Industry and Internal Trade Public Procurement. The policy to provide purchase preference linked with Local Content was extended for a further period of one-year w.e.f. 1 October 2019.

(d) Shell and RIL have given up Panna-Mukta fields which were operated under PSCs for the past 25 years. Shell also exited the CGD business in India after selling its 10% stake in Mahanagar Gas Limited for INR7.7 billion.

(e) With effect from April 1, 2020, BS-VI standards will be implemented in the entire country requiring supply of fuels containing 10 parts per million (ppm) of sulphur.

(f) The government notified ‘Reforms in Exploration and Licensing Policy, for enhancing domestic exploration and production of oil and gas’ on February 28, 2019, with the objective to intensify exploration activities, attract foreign and domestic investment and enhance domestic production. The policy reform focus on four major areas - increasing exploration activities in unexpected areas, marketing and pricing freedom has been granted for those new gas discoveries, enhance production from existing nomination fields of ONGC and Oil India Limited, and promoting ease of doing business by simplification of approval of process of DGH[42].

(g) Enhanced Oil Recovery (EOR): In September 2018, the government approved the policy framework to promote and incentivise Enhanced Recovery (ER) production methods to improve recovery from existing reserves. Use of ER methods have significant potential to increase production from the mature fields which are observing a natural decline in output.

Recent developments – Fiscal framework

The government had introduced the Taxation Laws (Amendment) Ordinance, 2019 in September 2019, passed in the Parliament as Taxation Laws (Amendment) Act, 2019 in December 2019, to carry out certain changes to prevailing corporate income tax rates under the Income tax Act, 1961 (IT Act) and the Finance (No. 2) Act, 2019. Thereafter, the Finance Act, 2020 made amendments to the IT Act.

Recent announcements which may impact the oil and gas sector have been discussed below:

Income-tax updates

1.23 An option to avail following concessional tax regime has been introduced for domestic companies with effect from April 1, 2019 provided it forego certain tax incentives and deductions [enacted vide The Taxation Laws (Amendment) Act, 2019]:

- 15% base tax rate for new manufacturing companies (satisfying prescribed conditions) incorporated on or after 1 October 2019 and commencing manufacturing/production on or before 21 March 2023. Effective tax rate to be 17.16% (applying uniform surcharge rate of 10% and cess of 4%)

- 22% base tax rate for existing companies. Effective tax rate to be 25.17% (applying uniform surcharge rate of 10% and cess of 4%)

Companies opting for any of the above regimes would not be subject to Minimum Alternate Tax (MAT).

1.24 To incentivise investment by Sovereign Wealth Funds (satisfying prescribed criteria) of foreign governments in priority sectors, 100% tax exemption to be allowed on interest, dividend and capital gains income earned from investment made in prescribed infrastructure facility/other (to be) notified sectors. Investment should be made on or before 31 March 2024 and held for at least three years to be eligible for tax exemption.

1.25 Other key tax proposals:

- Dividend distribution tax (DDT) to be replaced by classical system of dividend taxation wherein it will be taxed in the hands of shareholders. This will allow lower tax treaty rates on dividends to apply for foreign investors.
- Sunset date for concessional rate of tax withholding (i.e. 5%) under sections 194LC and 194LD of the IT Act extended to 30 June 2023.
- Tax dispute resolution introduced for settlement of tax disputes to help de-clog the legacy litigation.

Indirect tax updates

1.26 BCD rates reduced as follows:

Product	Previous rate	Reduced rate
Calcined petroleum coke	10%	7.5%
Very low sulphur fuel oil	10%	Nil

2. Key Issues and recommendations

2.1. Rationalisation of tax holiday provisions under section 80-IB(9) of the IT Act

The government, vide Finance Act, 2016, has phased out tax holiday provisions under section 80-IB(9) of the IT Act for E&P businesses commencing commercial production on or after April 1, 2017. However, there are certain legacy tax issues relating to the tax holiday provisions, which need to be resolved by the government, relevant for businesses still eligible for claiming the deduction.

Recommendation:

The government should consider the following aspects:

- Rationalisation of the sunset clause for tax holiday: Phasing out the deduction should be with respect to PSCs (or RSCs) entered into on or after April 1, 2017, and not undertakings commencing commercial production after such date. This would suitably address concerns of businesses which had entered into a PSC with the government on or before the cut-off date for sunset on tax holiday and after duly taking into consideration the tax holiday provisions.
- Clarify the meaning of the term ‘mineral oil’ to include natural gas [irrespective of the New Exploration Licensing Policy (NELP) rounds], eligible for tax holiday, in line with the judicial precedents[43] and assurance given by the Finance Minister in the Parliament.
- Clarify that each oil well/cluster of oil wells would be considered as an ‘undertaking’ for the purpose of tax holiday, and not the contract area under the PSC.

2.2. Rationalise/Extend fiscal incentives under the IT Act to E&P companies

Vide Finance Act 2016, the government had announced phasing out of tax holiday provisions, including for upstream operations under section 80-IB(9) of the IT Act. While section 42 of the IT Act provides for deduction of all exploration and drilling costs, there is no other fiscal incentive for E&P businesses.

Domestic E&P is crucial for the energy security of India and therefore, it is imperative to provide for adequate fiscal incentive for stimulating private investments in the oil and gas industry.

Recommendation:

It is recommended that 100% deduction for development and production costs should also be allowed under section 42 of the IT Act. In this regard, it is relevant to note that the Model RSC published by the DGH allows deduction of all expenditure incurred by a contractor on exploration, development and production under section 42 of the IT Act. Further, it is recommended that the Model RSC should clarify the availability of deduction of unsuccessful exploration expenditure and the manner of deduction of expenses under section 42 of the IT Act, as provided under provisions of the PSC, to avoid litigation on these aspects.

2.3. Encouraging financing of E&P projects

Being highly leveraged, project developers in the oil and gas sector rely on borrowed capital including overseas borrowing to fund their projects.

Vide Finance Act, 2017, the government has extended/provided the benefit of concessional tax withholding base rate of 5% on External Commercial Borrowings (ECB) and masala bonds. On the flip side, the government has also introduced limit on interest deduction in line with recommendations of the Organisation for Economic Co-operation and Development (OECD) Base Erosion and Profit Shifting Action Plan 4. Such provisions are applicable to an Indian company or a permanent establishment of a foreign company incurring interest expenditure exceeding INR10 million in respect of debt owed to a non-resident associated enterprise (AE) or to a non-AE (in respect of debt guaranteed by AE). Interest in excess of 30% of Earnings before Interest, Taxes, Depreciation and Amortisation (EBITDA) or interest paid or payable to non-resident AE or to non-AE (in respect of debt guaranteed by AE), whichever is lower is proposed to be disallowed. Such interest expense to the extent disallowed is henceforth to be carried forward for 8 years for set off against business income of future years, to the extent of maximum allowable interest, i.e. 30% of EBITDA. Considering debt-push down structure is common in oil and gas companies, disallowance of interest cost reckoned with respect to 30% of EBITDA could pose significant challenge for E&P entities as the effective post-tax cost of debt investments could soar.

Recommendation:

Considering that E&P projects are capital intensive and require significant financing, the government should consider the following approaches:

- Exempting E&P projects from the applicability of thin capitalisation rule under the IT Act. Such companies have large capital requirements and are highly leveraged due to commercial imperatives. Any limitation on deductibility of interest cost could significantly inhibit the commercial feasibility of projects in such sectors, which are otherwise crucial for a sustained economic growth.
- Alternately, introducing a much higher ratio (i.e. greater than 30%) for such projects, to ensure the limitation on interest deduction is triggered only in exceptional cases, without rendering debt financing more expensive for developers.
- Scope of section 94B may be narrowed to exclude debt raised through an implicit/explicit guarantee from the AE (in particular for E&P businesses). Group ratio rule for deductibility of interest may be introduced to account for business models which are highly leveraged worldwide due to commercial reasons and not particularly for reason of Base Erosion and Profit Shifting.
- In addition, removing the restrictions on number of years to carry forward interest disallowed under section 94B of the IT Act.

2.4. Clarify permissibility of investments via Foreign Venture Capital Investor (FVCI) route in E&P companies

In recent years, foreign investments in 'infrastructure sector' by a registered FVCI[44] has gained momentum and is fast emerging as an alternate to investments under extant FDI regime. This is primarily driven by the fact that it provides for a more liberalised investment framework; key relaxations are illustratively mentioned hereunder:

- Entry and exit pricing guidelines applicable under the FDI regime do not apply to investment by FVCIs;
- No ceiling on interest pay-outs.

'Infrastructure sector' for this purpose has the same meaning as given in the Harmonised Master List of Infrastructure sub-sectors approved by the government vide Notification F. No. 13/06/2009-INF dated 27 March 2012 as amended/updated from time to time. It may be noted that whilst for the purpose of ECB framework, 'Exploration, Mining and Refinery' sectors have been deemed included in the infrastructure sector, no such notification/clarification has been issued for investments via FVCI route.

Recommendation:

For encouraging foreign investments in the E&P space, it is recommended that the Reserve Bank of India explicitly clarifies that 'Exploration, Mining and Refinery' sector is to be considered as 'infrastructure sector' for the purpose of investments via FVCI route.

2.5. Benefit of concessional tax rate of 5% in respect of specified debt/quasi debt instruments

Presently, lower withholding rate of 5% under sections 194LC and 194LD of the IT Act is applicable to monies borrowed in foreign currency under a loan agreement or by way of issue long term bonds (including infrastructure bonds) or by way of issue of rupee denominated bond subject to conditions prescribed.

Specified funding instruments viz. Compulsorily Convertible Debentures (CCDs), Non-Convertible Debentures (NCDs) and Optionally Convertible Debentures (OCDs) under FVCI route, duly regulated from exchange control standpoint, are emerging as preferred instruments for structuring debt/quasi-debt instruments in E&P sector. Presently there is lack of clarity as to whether interest payments on such specified borrowing instruments would be eligible for concessional tax rate of 5%, owing to following reasons:

- Rupee denominated bond was specifically included vide Finance Act, 2017; memorandum to Finance Bill, 2017 suggests that the intent was to cover only masala bonds (i.e. INR bonds issued outside India); and
- Requirement to take specific approval from the government for instruments not governed by ECB framework.

Recommendation:

In view of the recent liberalisation of the ECB framework and to incentivise debt investments in E&P sector, an explicit clarification should be introduced to extend benefit of concessional tax rate of 5% to funding instruments such as CCDs, OCDs and NCDs (whether or not governed by ECB framework) without any requirement to seek specific approval from the government.

2.6. Inclusion of petro products [LNG, HSD, Motor Spirit, Aviation Turbine Fuel (ATF) and petroleum crude] under Goods and Service Tax (GST) purview

Petroleum products are input to many industries and commercial activities. GST being applicable on the final product and not on the petroleum products which are inputs to value chain defeats the purpose of GST.

Natural gas being a cleaner fuel and taking into account that loss of tax revenue should not be significant, the government must immediately put natural gas under the GST ambit.

Recommendation:

All petroleum products such as petrol, diesel & natural gas should be immediately brought under the ambit of the GST regime. Non-inclusion of the same has pushed up costs for the sector. No input credit is available on goods and services used for petroleum operations. Denial of credits has resulted in massive cascading impact and increased cost of production placing the domestic industry in a competitive disadvantageous position. This has an adverse impact on investments in this sector which is critical for energy self- sufficiency and import substitution.

Alternatively, ensure that incidence of GST flow seamlessly across the value chain by creating a mechanism which allows a refund of the non-creditable input taxes in the hands of the recipient.

2.7. Reversal of input credit relating to Non-GST supplies be made nil

The provisions of the GST law require reversal of input tax credit in respect of exempted/non-taxable supplies. It would be unfair to compel a company to lose common credit merely because it has (non-GST) trade turnover, which would be more than the service income (regasification charges) due to the cost of the traded goods included in non-GST trade turnover. However, it is pertinent to note that the cost of traded LNG is not a value add to the trader and therefore, should be excluded from the definition of exempted turnover for reversals. In other words, only trading margin should be considered for reversals.

Recommendation:

It is accordingly suggested that trading turnover pertaining to petroleum goods (being taxed separately) be excluded from the purview of exempt and total turnover under the GST laws for reversal of credit. Alternatively, trading margins pertaining to the petroleum goods should only be included in the exempt and total turnover for reversals.

2.8. Clarification on non-applicability of GST on cash calls under GST regime

Circular no 35/9/2018-GST dated 5 March 2018 was issued regarding applicability of GST on cash calls. However, the said circular has kept the issue open for interpretation of authorities.

Recommendation:

Clarification should be issued under GST regime that consortium and parties to consortium (which have executed a sharing agreement with the government) are not distinct entities and cash calls are not consideration for services but only a contribution made by contractors. Thus, GST should not apply on such cash calls.

2.9. Exemption from levy of GST on transmission charges included in sale price of gas

Presently, natural gas is sold to the customer including transportation to customer's premises as a bundled activity. The transmission charges form part of sale price of such gas and Value Added Tax (VAT) is being paid on the component of transportation charges (as it forms part of sale price of gas). Accordingly, GST should not be chargeable on the component of transmission charges. However, GST on the component of transmission charges is being demanded by local officers resulting in double taxation.

Recommendation:

Accordingly, it is suggested that suitable clarification should be issued clarifying that GST will not be payable on any activity associated with transaction of sale of petro-products (Motor Spirit, HSD, ATF, petroleum crude and LNG) where the consideration for such an activity forms a part of the total sale price which attracts VAT/Central Sales Tax (CST).

2.10. Valuation of taxable services for naturally evaporating products like LNG should be clarified in detail to apply on the charges for conversion of the delivered product

Naturally volatile and evaporating products like gasoline or LNG are susceptible to continuous erosion of quantity in their natural state. LNG is liquefied natural gas compressed by 600 times and remaining in liquid form only at temperatures of -160 degrees centigrade. Exposed to ambient conditions the entire product evaporates on its own.

The usable form of LNG in its regasified state as natural gas. The process of regasification of LNG involves the passing of the liquid through heat exchangers, compressors and pipelines in a controlled manner. Any repair to the regasification machinery in the normal course involves the venting of the liquid/gas contained therein to the atmosphere under regulated conditions. Due to the continuous nature of losses of the product that is inherent to its handling and processing, it is the norm worldwide to pre-agree on a%age of such losses and consumption or usage of LNG/gas while contracting for the regasification of LNG. This is done with a view to allocate the risk of handling the product between parties and bring certainty to the contractually deliverable quantities and the ad valorem price per unit for the same.

Shortfalls and excess of actual losses over pre-agreed norms are compensated by the service provider or taken as part of stock and disposed of as per provisions of Generally Accepted Accounting Principles (GAAP), VAT and Income tax laws.

Recommendation:

It should be clarified that the value of product lost or consumed during the process of regasification shall not be includible in the charge levied for processing.

2.11. Exemption from GST on import/ domestic procurement of goods required for oil & gas exploration (under Essentiality Certificate 'EC')

Basic Custom Duty and Customs cess continues to be exempted on import of goods required for oil & gas exploration subject to availability of 'Essentiality Certificate' in accordance with Notification

No. 50/2017 – Customs dated 30 June 2017.

However, such imports attract Integrated Goods and Services Tax (IGST) at the rate of 5% (Notification No. 03/2017 IGST (Rate) dated 28 June 2017) on the assessable value of goods subject to Essentiality Certificate being made available to Jurisdictional officer of the Supplier, unless import is covered vide Notification No. 72/2017 – Customs (exemption from payment of IGST on import if IGST payable on lease charges).

Similar to Notification No. 03/2017 – IGST (Rate) and Notification No. 03/2017 Central Goods and Service Tax (CGST) (Rate) dated 28 June 2017, relevant State Goods and Service Tax (SGST) notification provides that GST would be applicable at the rate of 5% on goods subject to the availability of the Essentiality Certificate.

Recommendation:

The government should make a suitable amendment in Notification No. 03/2017 – IGST (Rate) and Notification No. 03/2017 – CGST (Rate) to provide for complete waiver of GST in line with circumstances that existed in the pre-GST regime such that burden to the oil & gas sector is reduced.

Further, exclusion of services from the exemption notification would be prejudicial to the interests of the oil industry and goes against the basic principle behind levy of GST. It is suggested that the exemption notification in this regard be suitably amended thereby enlarging the scope of the items to all goods and services used for petroleum operations.

Conclusion

Oil & Gas industry has been at an inflection point for couple of years now, marked by a spate of policy and regulatory reforms. Government's renewed vigour for enhancing domestic production is an encouraging sign and is expected to catalyse large scale private investments for new field discovery and enhanced recovery from already discovered hydrocarbon acreages. Downstream infrastructure is set for a major capacity additions over next five to seven years, and this could well be a new sunrise sector for investors to look at in this space.

ENDNOTE

1. World Economic Outlook (Oct 2019), International Monetary Fund (can be accessed at https://www.imf.org/external/datamapper/NGDPD@WEO/OEMDC/ADVEC/WEOWORLD/IND)
2. IHS Markit
3. BP Energy Outlook 2019
4. ET Scenario, BP Energy Outlook 2019
5. Petroleum Planning and Analysis Cell (PPAC), Ministry of Petroleum and Natural Gas
6. Article in The Economic Times dated February 25, 2020
7. Article in The Economic Times dated January 21, 2020
8. Indian Petroleum and Natural Gas Statistics 2017-18, Ministry of Petroleum and Natural Gas
9. Petroleum Planning and Analysis Cell (PPAC), Ministry of Petroleum and Natural Gas
10. Energy Statistics 2018 - Ministry of Statistics and Programme Implementation
11. IGU 2019 World LNG Report
12. Petroleum Planning and Analysis Cell (PPAC), Ministry of Petroleum and Natural Gas
13. Petroleum Planning and Analysis Cell (PPAC), Ministry of Petroleum and Natural Gas
14. Petroleum Planning and Analysis Cell (PPAC), Ministry of Petroleum and Natural Gas
15. Fact sheet on FDI (From April, 2000 to March, 2019) by Department of Industrial Policy and Promotion (available at https://dipp.gov.in/sites/default/files/FDI_Factsheet_27May2019.pdf)
16. Source: http://www.investindia.gov.in/sector/oil-gas
17. Presentation by Mr Ranajit Banerjee, Head (HELP), Directorate General of Hydrocarbons (accessible at http://online.dghindia.org/oalp/Content/pdf/Keynote_Presentation_RB_India_Event_Abu_Dhabi_Nov_15.pdf)
18. Press release by Ministry of Petroleum & Natural Gas dated January 02, 2020 and The Hindu article date March 12, 2020
19. Press release by Ministry of Petroleum & Natural Gas dated February 15, 2017
20. Press Release by Directorate General of Hydrocarbons on March 1, 2019 (available at http://dghindia.gov.in/assets/downloads/5c790f6729839Press_Release_Award_of_blocks_DSF_Bid_Round_II_ver1.pdf)
21. Press Release by Directorate General of Hydrocarbons on March 1, 2019 (available at http://dghindia.gov.in/assets/downloads/5c790f6729839Press_Release_Award_of_blocks_DSF_Bid_Round_II_ver1.pdf)
22. Press release by Ministry of Petroleum & Natural Gas dated February 13, 2018
23. Press release by Ministry of Petroleum & Natural Gas dated November 12, 2018
24. Article in The Deccan Herald dated October 30, 2019
25. Article in The Economic Times dated July 17, 2019
26. Article in The Economic Tomes dated October 15, 2019
27. Press release by Ministry of Petroleum & Natural Gas dated December 18, 2019
28. Press release by Ministry of Petroleum & Natural Gas dated January 20, 2022
29. New Initiatives webpage, Ministry of Petroleum and Natural Gas
30. Press release by Ministry of Petroleum & Natural Gas dated December 18, 2019
31. Deloitte Analysis

32. Presentation by Director General of Hydrocarbon, Government of India
33. Article published in The Economic Times dated June 28, 2019
34. Year End Review 2018 - Ministry of Petroleum & Natural Gas
35. Press release by Ministry of Petroleum & Natural Gas dated November 18, 2019
36. Deloitte Analysis
37. Press release by Cabinet Committee on Economic Affairs (CCEA) dated October 23, 2019
38. Year End Report 2018 by Ministry of Petroleum & Natural Gas (http://pib.nic.in/newsite/PrintRelease.aspx?relid=186260)
39. Article published in Business Standard dated January 08, 2020
40. Year End Review -2019 of Ministry of Petroleum & Natural Gas
41. Article published in Business Standard dated August 12, 2019
42. Press release by Cabinet dated February 19, 2020
43. Niko Resources Ltd vs Union of India [2015] 374 ITR 369 (Guj)
44. FVCI investments are regulated by the Reserve Bank of India and Securities and Exchange Board of India (SEBI) pursuant to relevant regulations issued in this regard.

NOTE

Pharmaceuticals

Acknowledgements: Kanchana TK (Boehringer Ingelheim) – Chairman, Pharmaceuticals Sector Committee & its Members
Knowledge Partner: KG Ananthkrishnan and Nitika Garg – OPPI

EXECUTIVE SUMMARY

The healthcare industry in India has continued to grow through 2017, despite a slew of challenges and turbulent regulatory environment. The healthcare market is likely to increase three-fold to INR8.6 trillion (US$133.44 billion) by 2022.[3] The market continues to grow at low double digits (13%) led by a growth in volume, an improved case mix and price increases.

The government has released a Draft Pharmaceutical Policy (2017) that is comprehensive and covers many aspects across the pharmaceutical value chain including research and development (R&D), sourcing and manufacturing plus distribution. With regards to the draft Policy and with an objective for India's healthcare industry, the industry would like to draw the government's attention to four key areas:

- **Access to healthcare**: Promote government health reforms that improve patient access to innovative medicines, promote increased public financing, and establish a framework for expansion of private health insurance. With a view to move towards universal health coverage, the Union Budget 2018–19 has been positive for the healthcare sector with the launch of a one-of-its-kind, National Health Protection Scheme (NHPS) that promises to substantially increase provision of secondary and tertiary care services to the poor, through addressing shortage of manpower and availability of healthcare in rural areas. The government is also cognisant of the impact of medical inflation, reflected in an increased coverage amount per family to `5 lakh (€6,370.88) under the NHPS, compared to `30,000 (€382.25) under the Rashtriya Swasthya Bima Yojana (RSBY) scheme, with the increase in the amount exempt from tax for senior citizens for critical illnesses and deduction for medical insurance.
- **Intellectual property**: Reduce the risk of further negative intellectual property (IP) decisions and secure targeted improvements in India's IP laws and policies in the near-term, while laying the groundwork for a stable longer-term policy.
- **Regulatory**: Encourage government reforms to the regulatory regime that promote innovative clinical research and ensure manufacturing and approval of high-quality medicines.
- **Ethics:** Pharmaceutical companies have been accused of enticements to secure prescriptions from the medical fraternity for a very long time. The government needs to instil confidence in the people by providing a stringent code which removes such unethical practices, if any, from the marketplace.
- The promise of an innovative biopharmaceutical industry in India will only be fulfilled if the government, along with all relevant stakeholders, can work to build, sustain and grow a scientific, economic, and policy ecosystem that promotes and rewards medical innovation in an environment that encompasses predictability, consistency, and sustainability in its policies. Investments in research and innovation are integral to the growth of nation.
- Expansion of drugs under the Drug Price Control Orders (DPCO), price caps on stents and implants, procedure, or service pricing related discussions in West Bengal and Karnataka, and cases of healthcare services licenses being cancelled adversely affected the sector during the year. The price-capping policy in medical devices that the government is focusing on is dynamically changing the environment of the industry leading to withdrawal of certain good quality medical devices from the market to lowering the scale of investments from multinational companies in our country.
- Uncertainty on manufacturing of pharmaceutical products in third party manufacturing/loan licensing, compulsory licensing are amongst many such issues that have been disrupting the industry dynamically.
- While, on one hand, the pharmaceutical industry (called a sunrise industry of the country) has witnessed some significant transformations, lack of predictability continues to remain a concern.
- In summary, the need of the hour is for augmenting the regulatory framework and strengthening the infrastructure keeping the patient at the centre of the healthcare ecosystem. That will make the government's overall healthcare plan successful.

1. INTRODUCTION

1.1 Opportunities and Challenges

The Government of India announced the National Health Policy in 2017. The overall objectives of the patient-centric policy are:

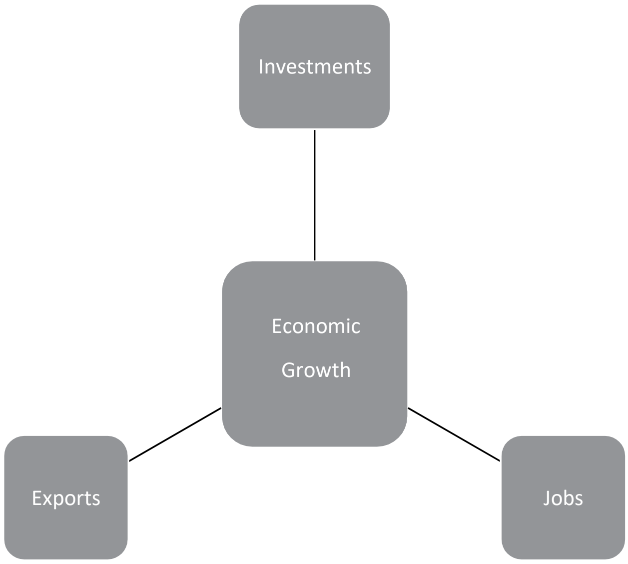
- Improving health status through concerted policy action in all sectors.
- Expansion of preventive, promotive, curative, palliative, and rehabilitative services provided through the public health sector with focus on quality. Attainment of the highest possible level of health and well-being for all at all ages, through a preventive and promotive healthcare orientation in all developmental policies.
- Universal access to good-quality healthcare services increasing access, improving quality and lowering the cost of healthcare delivery.

The pharmaceutical companies that are members of the EBG Federation have lauded the government for the Draft National Health Policy. Members of EBG Federation, through their activities in India, have been working to make these objectives a reality in India. Specific initiatives include:

- Innovative patient assistance programmes from research-based pharma companies, to enhance access to state-of-the-art drugs for oncology, diabetes, and auto-immune disorders.
- In-licensing arrangements from Roche with Curadev, an Indian start-up for immunotherapies.
- Arogya Parivar initiative from Novartis to make drugs available in rural areas.
- Investments by Sanofi Group and GSK in Indian vaccine manufacturing.

EBG Federation members reiterate their commitment to work with the government in furthering these initiatives.

The Indian economy is forecast to grow at 7% per annum. The Government of India has embarked upon an ambitious development agenda with a focus on inclusive growth. The Indian pharmaceutical industry is playing a key role in driving India's growth agenda.



- The Turnover of India Pharma Industry clocked US$38 billion in the year 2019 (Domestic + Exports).[2] India's domestic pharmaceutical market turnover reached US$20.03 billion in 2019 from US$19.73 billion in 2018[1].
  - The drugs and pharmaceuticals sector attracted cumulative foreign direct investment (FDI) inflows worth US$16,397 billion (INR87,067 crores) between April 2000 and December 2019, according to data released by the Department for Promotion of Industry and Internal Trade (DPITT). In February 2019the Indian pharmaceutical market grew by 10% year-on-year. In 2015-16, the FDI equity inflows to Drugs and Pharmaceutical Sector was INR4,975 crores which increased to INR6,502 crores in 2017-18. The FDI inflow however dropped in 2018-19 with INR1.842 crores. Cumulative FDI in pharmaceuticals between April – September 2019 was INR2,065 crores.[3]
- Between July–September 2018, Indian pharma sector witnessed 39 private equity (PE) investment deals worth US$217 million (€192.46 million). Investment (as percentage of sales) in R&D by Indian pharma companies increased from 5.3% in FY2012 to 8.5% in FY2018. In 2017, Indian pharmaceutical sector

witnessed 46 merger and acquisition (M&A) deals worth US$1.47 billion (€1.30 billion). Indian companies received 304 abbreviated new drug application (ANDA) approvals from the US Food and Drug Administration (USFDA) in 2017. The country accounts for around 30% (by volume) and about 10% (value) in the US$70–80 billion (€62.08–70.95 million) US generics market. The total size of the Indian pharmaceutical industry (including drugs & medical devices) is around US$43 billion (INR3,01,000 crore) and is currently having a growth rate of 7-8% in drug sector. Total exports (drugs and medical devices) are to the tune of US$20 billion (INR1,47,420 crore) of which drugs form around 90% of the total exports. The Pharmaceutical sector currently contributes around 1.72% to the country's GDP[4]. The country's pharmaceutical industry is expected to expand at a CAGR of 22.4% over 2015–20 to reach US$55 billion (€48.78 billion).

India exported pharmaceuticals to the tune of INR1,33,910 crore with a recorded growth of 10.72% in 2018-19.

India is the largest provider of generic drugs globally and accounts for 20% of global exports in generics and exports mainly consist of Drug Formulations and Biologicals up to 77% followed by Bulk drugs and intermediates up to 21%. Indian pharmaceutical industry supplies a significant percentage of global supply of medicines including vaccines, APIs and finished products. Pharmaceutical exports include bulk drugs, intermediates, drug formulations, biologicals, Ayush and herbal products and surgicals.

The Turnover of India Pharma Industry clocked US$38 billion in the year 2019 (Domestic + Exports)[2]. India's domestic pharmaceutical market turnover reached US$20.03 billion in 2019 from US $19.73 billion in 2018[1].

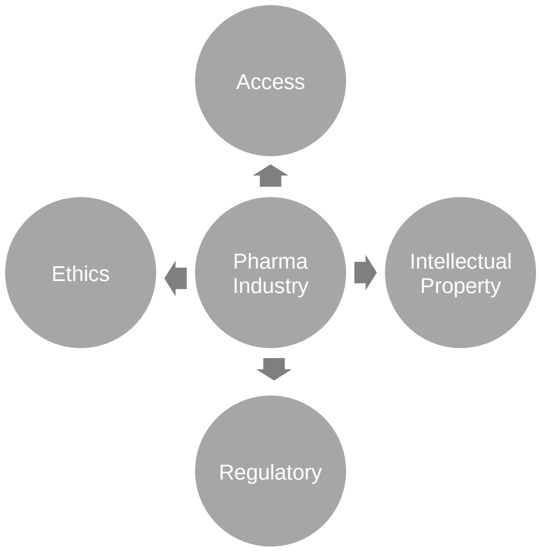
Nearly half of all vaccines delivered globally are manufactured in India. India is the world's largest supplier of vaccines, with 60% of the world's vaccine production, and the largest provider (60%) of anti-retroviral drugs make the sector an attractive proposition for global pharmaceutical companies.

The pharmaceutical industry in India has also provided employment to over 2.7 million people directly or indirectly[5], which are key components of the government's Make in India initiative.

The Indian pharmaceutical industry has been a key player in reducing India's trade deficit. The industry has also played a key role in India's soft power diplomacy in Africa, Asia and Latin America by becoming the 'Pharmacy of the World'.

While the pharmaceutical industry has contributed significantly in India's nation-building efforts, it also faces unprecedented challenges. The industry is battling a perfect storm of fierce competition, shorter time-to-market, expiring patents, slowing sales growth, and declining profitability in developed markets together with pressures on cost and a complex regulatory environment. The next level of growth for the industry lies in sustaining and growing the generics market and promoting the industry to enter the innovative biopharmaceutical space.

However, the promise of an innovative biopharmaceutical industry in India will only be fulfilled if the government, along with all relevant stakeholders, can work to build, sustain and grow a scientific, economic, and policy ecosystem that promotes and rewards medical innovation in an environment that encompasses predictability, consistency, and sustainability in its policies. Investments in research and innovation are integral to the growth of a nation. The government has also released a Draft Pharmaceutical Policy, 2017 which covers few key aspects across the pharmaceutical value chain, key being R&D, sourcing and manufacturing plus distribution. The industry would like to draw the government's attention to four key areas:

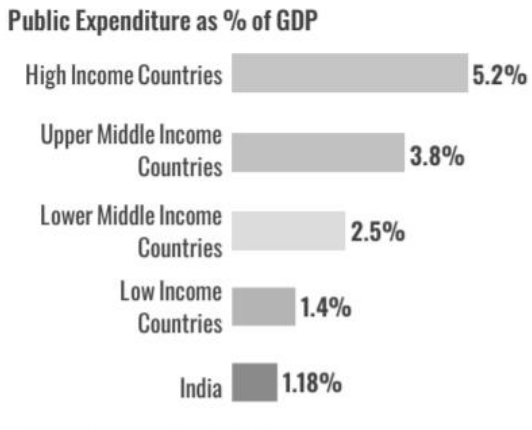


1. **Access to healthcare:** Promote government health reforms that improve patient access to innovative medicines, promote increased public financing, and establish a framework for expansion of private health insurance.
2. **Intellectual property:** Reduce the risk of further negative IP decisions and secure targeted improvements in India's intellectual property laws and policies in the near-term, while laying the groundwork for a stable longer-term policy.
3. **Regulatory:** Encourage government reforms to the regulatory regime that promote innovative clinical research and ensure manufacturing and approval of high-quality medicines.
4. **Ethics:** Pharmaceutical companies have been accused of enticements to secure prescriptions from the medical fraternity for a very long time. The government needs to instil confidence in the people by providing a stringent code which removes such unethical practices, if any, from the marketplace.

2. KEY INDUSTRYISSUES

2.1 Access toHealthcare

The Indian government has issued National Health Policy (NHP), 2017 that calls for greater access for low-income patients. However, India's total expenditure on healthcare is low, close to 4% of the GDP, while the world average is around 10% of the GDP. The public expenditure is also low at ~1% of the GDP, lagging even low-income countries[6].



Source: National Health Profile 2018

Also the overall penetration of health insurance is low. Coverage is limited to inpatient care and rarely extends to outpatient care or medicines. Out of pocket expenditure (OOPE) on health by households is 62.6%[7]. Of the 29% of Indians covered by health insurance, 85% are covered by social and state health initiatives, such as state-level employee insurance for industrial workers and the central government's healthcare plan.

In addition to the 'Asks' below, it would be worthwhile for the government to consider a tiered pricing model on a pilot basis to study the benefits of broadening access. Both central and state governments should allocate reasonable separate budgets for patients suffering from rare and orphan diseases where treatment options are limited and mean all the difference between life and death.

Issue	Short-Term Asks	Medium-Term Asks
Budget 2020-2021	In the 2020 -21 budget, the government announced allocation of INR69,000 crores health sector. Out of this, INR6400 crores were allocated for Ayushman Bharat. Government has also proposed to set up proposed a viability gap-funding for setting up hospitals in PPP in aspirational districts. While the industry fully supports the government in such an endeavor, a roadmap including the interaction of all the stakeholders, bringing in more supply chain efficiency and by bringing more hospitals under the scheme can help in disseminating the scheme benefits to all the households. scheme should now cater to more and more people.	Increase GDP spend on healthcare to 2.5% as envisaged in NHP 2017.
NLEM Revision	The Standing National Committee on Medicines and Health Products has been working on revising the National List of Essential Medicines. The Industry seeks a process of evaluation that is transparent, evidence-based and endeavours to utilise the resources available for healthcare expenditure in an optimal way. Therapeutic category wise stakeholder consultations should be done to ensure transparency and predictability.	
Proposed Drug Price Control Order (DPCO) amendments	• Specific strength and specific dosages based on essentiality criteria as determined by the National List of Essential Medicines committee should only be the basis of addition or deletion of drugs from Schedule I. • Redressal body to be constituted for all orders passed by the National Pharmaceutical Pricing Authority (NPPA). • 10% annual price revision growth rate to be continued for non-scheduled drug. • Implementation of price fixation orders should be effective on prospective batches and not retrospective. • Revision of Schedule I to be done once in five years. Repeated price controls on scheduled drugs must be avoided.	Government should increase its share of essential medicine purchase rather than relying on price control mechanism alone.
Trade Margin Rationalisation	• Trade Margin Rationalisation, if any must be done keeping price to stockist as the base for all drugs irrespective of the source of origin of such drugs. • Instead of the derived Price to Stockist, actual Price to Stockist as per CA certified commercial invoices of manufacturers should be considered for calculation of TMR. • TMR should only be considered for sales through trade channels. All government sales and non-commercial supply to patients/patient groups and NGOs to be kept outside its ambit.	

Issue	Short-Term Asks	Medium-Term Asks
Impediments to implementation of current DPCO 2013 provisions	Multiple issues exist with NPPA interpretation and implementation of orders passed by DPCO. Key issues are highlighted: • Delay in Implementation of Review Orders passed by DoP leads to depriving the industry of legitimate revenue and thus results in huge losses. • DPCO para 13 (1) provides for 45 days for implementation of notified prices. However, NPPA takes the view that notified price takes effect immediately. It is illogical to hold the manufacturers to be responsible for implementation of revised prices at 700,000 retail outlets from the very date of notification. • NPPA acts mechanically on the responses submitted by manufacturers in respect of overcharging notices. No reasoned orders are passed. Further NPPA insists on payment of interest from the date of overcharging in spite of effective court orders against such practice. This highly unstable environment leads to low confidence level to make investments, ultimately affecting consumers and economic activity and job creation. The industry suggests time bound implementation of orders passed by DPCO in addition to a clear time frame on response for applications submitted by the industry.	
Ban on fixed dose combinations (FDCs)	With further FDCs being examined, action should be taken thoughtfully and in the best interest of patients, with bans only against irrational combinations having concerns of safety. Industry should be given due opportunity to represent before all expert committees deciding on the issue.	
Preventive healthcare	Include more vaccines for preventive healthcare which should lead to reduction in the overall healthcare costs for government.	

2.2 Intellectual Property Protection

Despite a period of relative calm, there remains significant unpredictability in intellectual property (IP) in India. The government of India has sought to address IP-related criticisms, including through bilateral dialogue and policy deliberations on A national IP policy, but no progress has been made in terms of meaningful policy changes to address the challenges. The ongoing threat of compulsory licences (CL) and the tendency to use Section 92 for CL, the lack of alignment between the Centre and states, and the continued denial of patent applications under Section 3(d) are potential areas where improvements are possible.

Issue	Short-Term Asks	Medium-Term Asks
Compulsory licences	• Government must give the patentee ample opportunity to meet the requirement of people living below poverty line. • Interpret 'reasonably affordable price' in Sec 84(1). • Recognise and consider efforts taken by companies to provide patient assistance programmes (PAPs). • Clarify that importation would satisfy working of patent in India. • Simplify Form 27 filing requirements by finalising the draft Patent (amendment) Rules, 2019 issued vide G. S.R.396(E) dated May 31, 2019.	• Amendments in Patents Act 1970 to remove language which creates ambiguity regarding whether importation amounts to working of patent, misuse of Section 84(1) which provides multiple triggers for issuance of CL, etc. • Define phrases like 'National Emergency', 'Extreme Urgency', etc. • Provide royalty which reflects true value of the IP.
Section 3(d) — 'enhanced efficacy'	• Issue guidance to specifically define what would constitute 'enhanced therapeutic efficacy' leaving it open to subjectivity and inconsistency. • Issue guidance for uniform interpretation of Section 3(d) and not applying the section indiscriminately in cases of novel pharmaceutical compounds but restrict it to only new use of known compounds.	• Section 3(d) needs more clarity so that incremental innovation is encouraged which in turn will enhance the 'innovation ecosystem' in India. Pharmaceutical patent applications, like all other patent applications, should be granted as long as the applicant can demonstrate that the invention is new, involves an inventive step and is capable of industrial application. • Additional restrictions on patentability for pharmaceutical/biosciences must be done away with.

Issue	Short-Term Asks	Medium-Term Asks

Patent decisions and enforcement	• Currently, CDSCO and DPIIT have no mechanism to promote effective and adequate protection of intellectual property rights. A transparent system will help patentee to take timely legal relief.
	• This could be achieved through implementation of GSR 19(E) dated 1 January 2019 with the following additions:
	  • From application stage itself
	  • Time bound period of 15 days
	  • Non-commercial data to be made public
		• For effective and meaningful enforcement of patents, the New Drugs & Clinical Trial Rules, 2019 and the Drugs & Cosmetics Rules, 1945 and corresponding Forms need to be amended to include a requirement for notification of patent status by the originator/new drug applicant and subsequent applicants not be given marketing approval for products covered by such a patent till the expiration of the patent term, unless consented to by the patent owner.

Regulatory Data Protection	• CDSCO must not rely on the innovator's data to grant subsequent approvals.	• Ministry of Health/CDSCO must bring in a *sui generis* law or effect suitable provisions to the Drugs and Cosmetics Act 1940 and Rules 1945 to provide for Regulatory Data Protection for a minimum of 5 years.
Intellectual Property Appellate Board	• IPAB must be revamped and made functional. • Technical member under the Patents Act 1970 must be appointed.	
Need for Specialised Patent Benches		• Designated Specialised Patent Benches must be set up for trying patent cases in Delhi, Mumbai, Kolkata and Chennai with judges with appropriate technology background. Further, exemplary statutory minimum damages must be provided for IP holders in the event they win in an infringement or revocation case and the challenge is held to be frivolous.

2.3 Drug Regulation, Clinical Trials, and Industrial Relations

Despite having many components to support an ecosystem for drug development, India attracts only 3% of global R&D spending and 2% of global clinical trials (CT). The Central Drugs Standard Control Organisation (CDSCO) has issued the Clinical Trials Rules, 2019. It applies to all new drugs, investigational new drugs for human use, clinical trial, bioequivalence study, bioavailability study and Ethics Committee. The industry urges the government to streamline inconsistencies, if any, and provide clarity in respect of inherent ambiguities in the implementation of the new rules.

Issue	Short-Term Asks	Medium-Term Asks
Waiver of Local Clinical Trials	• The List of Countries to be specified under Rule 101 of the New Drugs and Clinical Trials Rules, 2019 must be notified soon.	• The ambiguities existing in New Drugs and Clinical Trials Rules, 2019 must be removed.
Guidelines on OTC (over the counter) Drugs	• A report on OTC Policy has been endorsed by the Drug Consultative Committee (DCC) which was submitted by a DCC Sub-Committee headed by N.K. Ahooja. The DCC sub-committee has been tasked to work on identification of an OTC drugs list along with requisite amendments to be notified in the Drugs & Cosmetics Act & Rules. The industry supports such a move towards clarity on OTC category and would suggest that the policy enables greater access to patients without over-regulation in the category that could potentially impact the industry's interest in promoting this category. • Such a policy will enable greater self-medication while accounting for patient safety.	• There is a need for robust OTC guidelines to improve access. The availability of OTC drugs can save health systems' valuable resources as well as consumers' time and money, especially for minor ailments. Further, OTC pathway will allow manufacturers to provide safety information and instructions specifically directed to patients on how to use OTC which effectively empowers consumers to take well-informed decisions enhancing positive health outcomes.

Issue	Short-Term Asks	Medium-Term Asks
Guidelines on Similar Biologics 2016	• Ensure that the 2016 guidelines are enforced for giving approvals to biosimilars.	• There should be roll back to the 2012 guidelines by adopting a consultative process. Rationale: • The standards for approval of similar biologics in India as laid down in Guidelines of 2012 have been diluted in 2016. Few examples of dilution: • Guidelines 2016 limits requirement of Phase III CT data to 100 patients for the purposes of obtaining a MA for a biosimilar. • Condition in 2012 guidelines which did not allow a biologic to qualify as reference biologic unless marketed for a minimum of 4 years has been removed in the 2016 guidelines. • Extrapolation of data generated in respect of a clinical indication permitted to other indications if reference biologic is approved for such additional indications in other countries.

3. ETHICS

2.4. Uniform Code for Pharmaceutical Marketing Practices (UCPMP)

The November 2014 UCPMP issued by DoP remains voluntary. It was also suggested that it would be up for further review on the basis of the inputs received by the department. Per UCPMP, no gifts, pecuniary advantages or benefits in kind may be supplied, offered or promised to persons qualified to prescribe or supply drugs, by a pharmaceutical company or any of its agents.

Issue	Short-Term Asks	Medium-Term Asks
UCPMP	The existing ambiguities in the existing voluntary UCPMP have to be removed.	Stakeholders' consultations must take place before making the UCPMP mandatory

CONCLUSION

The Indian pharmaceutical market size is expected to grow to US$100 billion (€88.69 billion) by 2025. The government and regulators have a key role to play if the industry needs to realise this goal.

Some of the major initiatives taken by the government to promote the biopharmaceutical sector in India are as follows:

- The Government of India has announced incentive scheme to bulk drug manufacturers, including both state-run and private companies, to encourage the Make in India programme and reduce dependence on imports of active pharmaceutical ingredients (API), nearly 85% of which come from China.
- The DoP has set up an inter-ministerial co-ordination committee, which would periodically review, coordinate, and facilitate the resolution of the issues and constraints faced by the Indian pharmaceutical companies.
- The DoP has planned to launch a venture capital fund of `1,000 crore (€127.41 million) to support start-ups in research and development in the pharmaceutical and biotech industry.
- Telangana has proposed to set up India's largest integrated pharmaceutical city spread over 11,000 acres near Hyderabad, complete with effluent treatment plants and a township for employees, in a bid to attract investment of `30,000 crore (€3.82 billion) in phases. Hyderabad, which is known as the bulk drug capital of India, contributes almost 20% of pharma exports from India and generates US$15 billion (€13.30 billion) a year.
- At the launch of Cluster Development Programme of the pharmaceutical sector, late. Shri. Ananth Kumar, Minister of Chemicals and Fertilisers, [He is no more] announced that six pharmaceutical parks will be approved and established this year which will have sufficient infrastructure and facilities for testing and treatment of drugs and also for imparting training to industry professionals.
- A lot more still needs to be done. Transparency and predictability in policies will be key to making India the innovation hub for biopharmaceuticals, moving forward.

ENDNOTE

1. Healthcare Industry in India https://www.ibef.org/industry/healthcare-india.aspx
2. IQVIA MAT 2019
3. https://dipp.gov.in/sites/default/files/FDI_Factsheet_December 19_5March2020.pdf
4. DoP Annual Report 2019-20 : https://pharmaceuticals.gov.in/sites/default/files/Annual%20Report%202019-20_0.pdf
5. https://www.ipa-india.org/static-files/pdf/publications/position-papers/2019/ipa-way-forward.pdf
6. National Health Profile 2018
7. National Health Accounts – Estimates for India 2017

Power

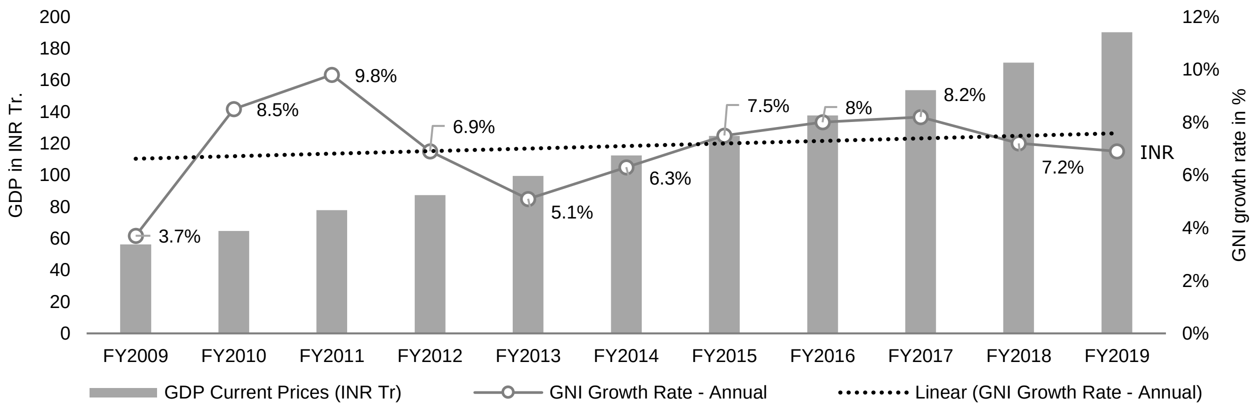
Acknowledgements: Mahadevan Anand (Andritz India) – Chairman, Power Sector Committee & its Members
Knowledge Partner: Gokul Chaudhri, Anuj Agarwal, Gaurav Barchha and Mansi Kakkar – Deloitte Touche Tohmatsu India LLP

1. INTRODUCTION

MARKET DESCRIPTION

1.1 India is the largest democracy in the world with a population of more than 1.35 billion[1]. India's GDP has grown at around 6-7% post the economic liberalisation in 1991, making it one of the fastest-growing large economies in the world. It is attractive for investors predominantly due to the presence of a large market, varied range of industries, diverse investment avenues and supportive policies of the government.

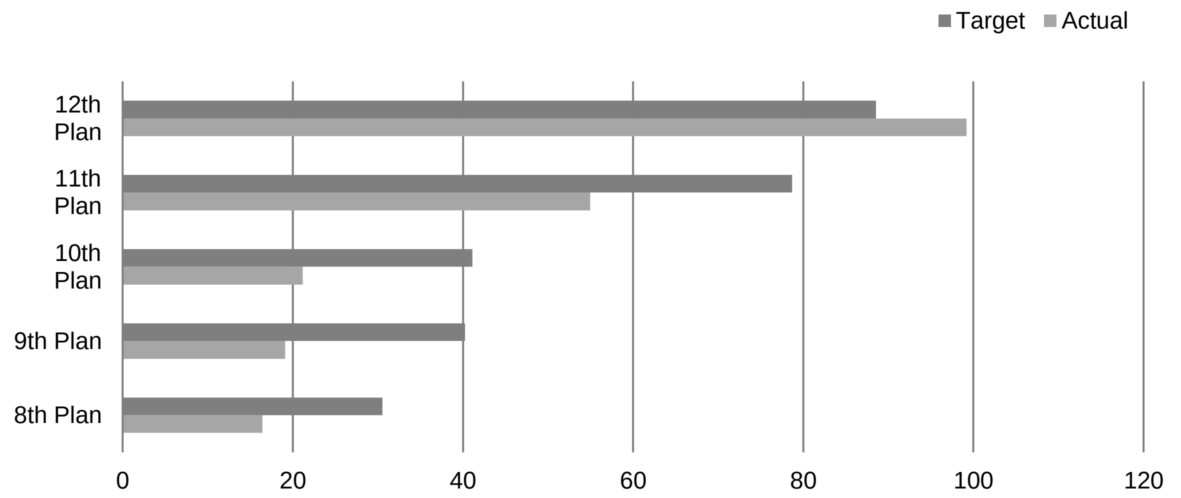
Figure 1: India's GDP growth over the years[2]



1.2 Improvements in macro-economic stability due to ongoing structural reforms, fiscal discipline, efficient delivery of services and financial inclusion have contributed significantly towards the robust growth of the Indian economy. World Bank has pegged India's growth rate at 5% in FY2020 against the global economic growth rate of 2.5% in the current FY. Business investment and exports are expected to be strong, on account of structural reforms including the new Insolvency and Bankruptcy Code, implementation of the Goods and Services Tax (GST), investment in infrastructure, and bank recapitalisation.

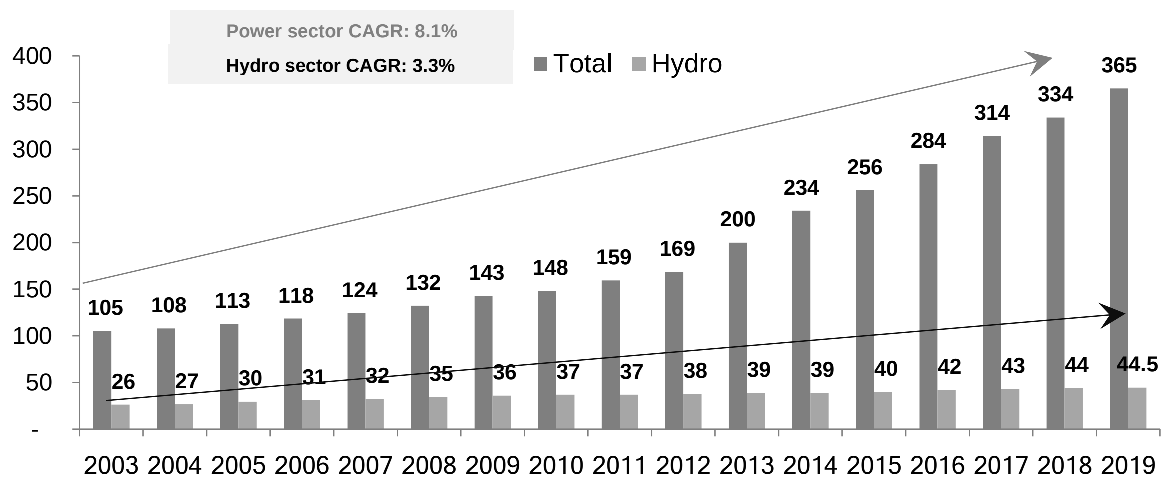
1.3 Electricity has always been one of the critical infrastructures for socio-economic development of any country. The Indian power sector has made significant progress over the years, boosting economic growth in the country. The Government of India (GoI) was successful in achieving 100% village electrification in May 2018. As in March 2019, all states[3] reported electrification of all willing households under the 'Saubhagya' scheme. The impetus is now towards providing reliable, sustainable and affordable electricity for all. The Country will require an exponential rise from present levels to support the growth momentum and reliable power supply. The Indian Power sector surpassed the capacity addition target and added 99.210 gigawatt (GW)[4] against the target of 88.53 GW in 12th plan period 2012-17[5] (from conventional sources). The sector is projected to add around 200 GW during 13th plan period 2017-2022.[6]

Figure 2: Actual Versus Target Capacity additions in the previous five year plans[7]



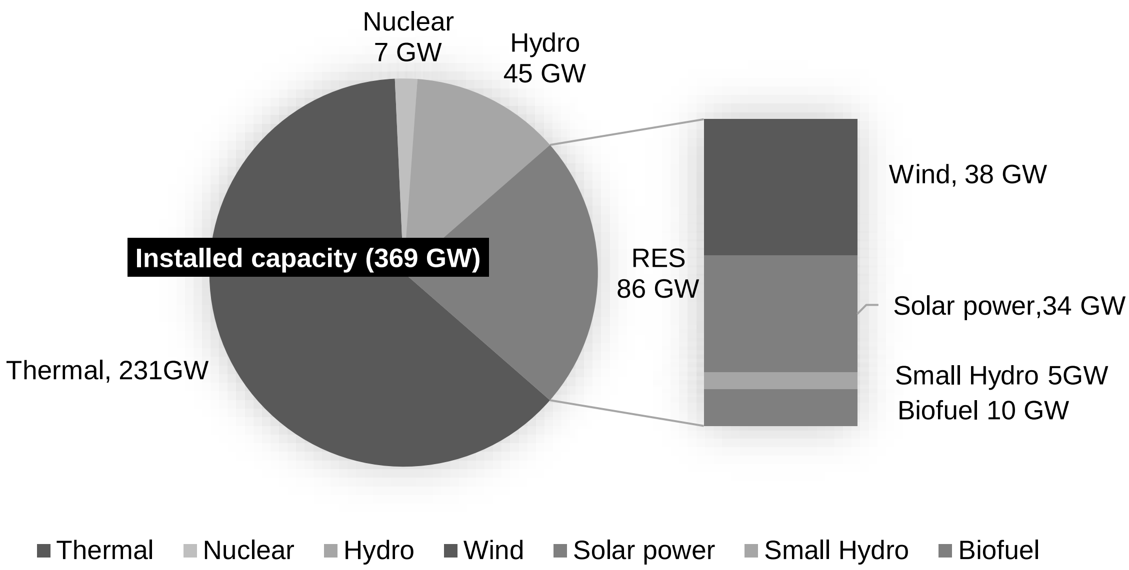
1.4 India power sector has been growing at 8.1% and hydro sector at 3.3% per annum since 2002 (CEA, India). Hydro sector is lagging with lack of financial resources and associated environmental issues. Primary focus remains on Renewable Energy (RE) [PV Solar and Wind]

Figure 5*: Indian Power sector growth trajectory*



1.5 The all-India installed capacity as on 31 December 2019 stood at 369 GW. Out of such installed capacity, thermal based power plants account for ~ 63% of the total installed generation capacity. Of this, coal based generation capacity accounts for 56%, gas 7% and oil 0.14%. Coal is expected to remain as dominant fuel source in future too considering the enormous capacity required to meet the increasing demand. RE sources account for 23% of the total installed generation capacity. Hydro Power contributes to ~ 12% of the total installed capacity. The hydro sector is witnessing a declining growth trajectory primarily due to land acquisition related issues, environmental issues, concerns around economic viability of hydro projects etc.

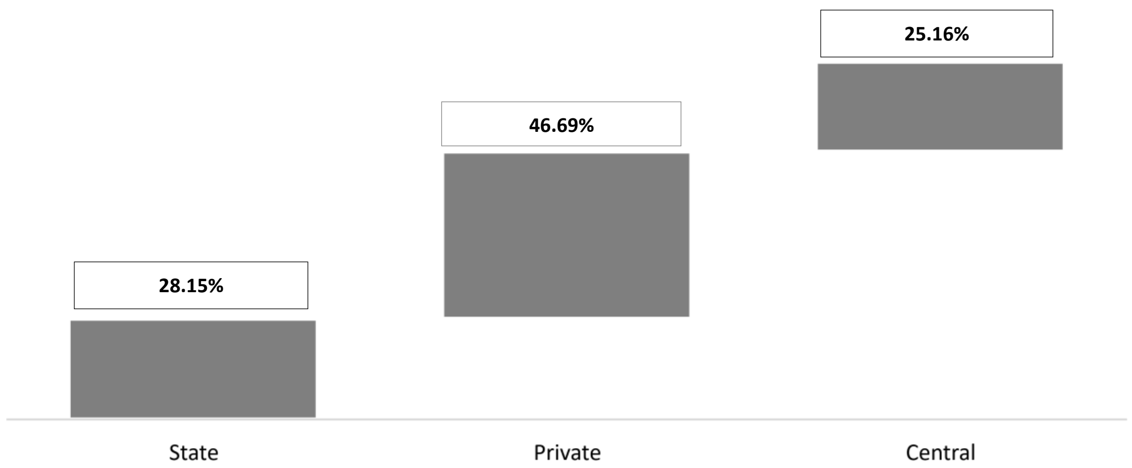
Figure 4: All India installed capacity as on 31 December 2019



1.6 The installed capacity as on 31 December, 2019 has reached 6.78 GW from Nuclear Power. Nuclear power for civilian use is well established in India and has been a priority since independence. The Indian nuclear programme for production of power has been an indigenous effort. It is strategically important to develop core capabilities in critical areas to reduce vulnerabilities to external pressures. India is the only country in the world that has accorded high priority to use of all three main fissionable materials, U-235, plutonium and U-233 to meet the challenge of reaching independence through deployment of domestic nuclear resource.

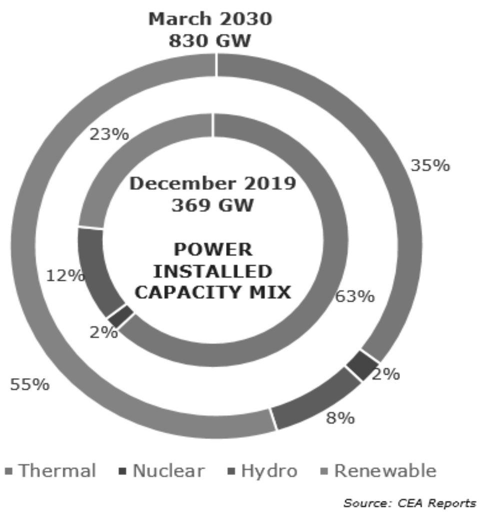
1.7 Currently, the all India installed capacity is majorly dominated by the Private sector with approximately 46% of the installed capacity as on 31 December 2019 owned by private sector and balance 54% by central and state government utilities[8]. The private sector's interest in the sector has grown exponentially on the power generation sector aided by the migration to a competitive bidding framework from the negotiated Power Purchase Agreement (PPA) model.

Figure 5: Sector wise break up all India installed capacity as on 31 December 2019(%)



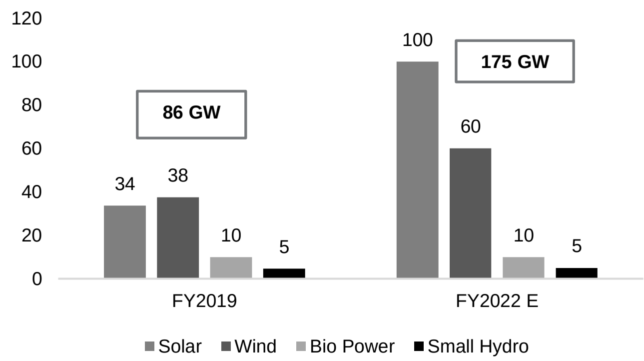
1.8 Going forward, the all India installed capacity in expected to be around 830 GW by 2029-30. The share of coal in the overall generation capacity is likely to come down to around 35% by 2029-30, losing its share to RE, with share of RE increasing from ~ 23% in 2019-20 to 55% in 2029-30.

Figure 6: Growth in All India installed capacity by March 2030[9]



1.9 India has been actively promoting RE and has set a massive target of 175 GW and 455 GW RE installed capacity targets by 2022 and 2030 respectively from the existing RE capacity of 86 GW as on 31 December 2019. Thus, the capacity additions for future years is expected to be dominated by RE.

Figure 7: RE Generation capacity addition targets by FY2022 (GW)[10]



1.10 Penetration of RE in the overall generation capacity portfolio has increased over the years. The need for clean, reliable, and affordable power is the key driver for the growth in RE sector. Going forward, Wind is expected to grow at a Compounded Annual Growth Rate (CAGR) of 9% till 2030, whereas, solar is expected to grow at a CAGR of 70% till 2020.

Figure 8A: Expected growth in Wind capacity by 2030 (GW)

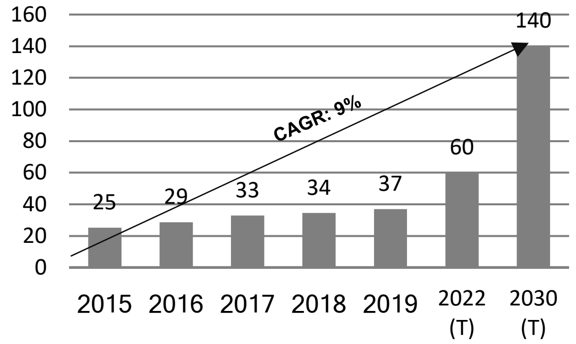
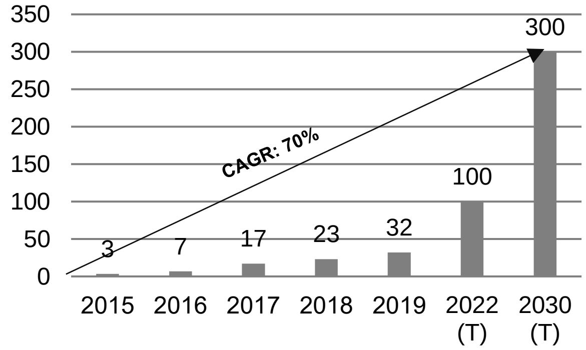


Figure 8B: Expected growth in Wind capacity by 2030 (GW)

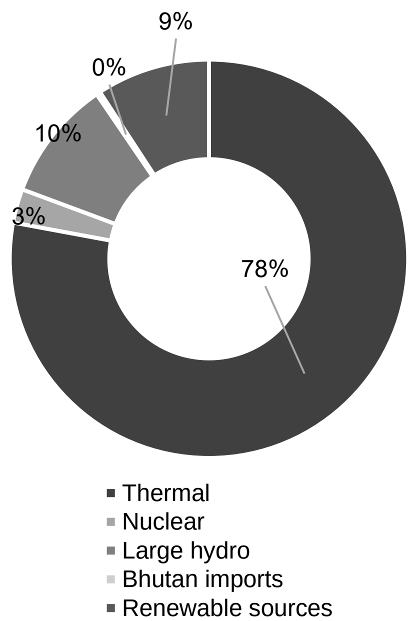


1.11 Power sector has emerged as one of the leading sectors attracting substantial foreign direct investments (FDI). The sector received US$1,106 million (~988 million Euros) in FY2018-2019. Cumulative FDI inflows since 2000 up to September 2019 have been around US$14.58 billion (3% of the total FDI inflows)[11]. Although the power sector is not a major contributor to the exchequer by way of taxes, this industry is a major employment generator both in the public and private sector, directly and indirectly.

ELECTRICITY GENERATION

1.12 India is the third largest producer of electricity in the world after China and the US[12]. The electricity generation during the year 2018-19 was 1,376 billion units (BU)[13], with a contribution of 78% from the thermal sector in the total generation.

Figure 9: Fuel wise break up of Electricity generation in 2018-19



1.13 The actual power supply position in the country during 2018-19 in terms of energy and peak is given in the table below:

Table 1: All India Region-wise Demand Supply Position for 2018-19[14]

Region	Energy				Peak			
	Requirement (MU)	Availability (MU)	Deficit (MU)		Demand (MW)	Availability (MW)	Deficit (MW)	
Northern	382,493	377,595	4,898	1.3%	63,166	61,726	1,440	2.3%
Western	390,349	390,136	212	0.1%	56,675	55,821	853	1.5%
Southern	339,377	338,960	417	0.1%	49,464	49,464	0	0%
Eastern	145,686	144,616	1,070	0.7%	23,141	22,733	408	1.8%
North-Eastern	16,691	16,219	472	2.8%	2,967	2,850	117	3.9%
All India	**1,274,595**	**1,267,526**	**7,070**	**0.6%**	**177,022**	**175,528**	**1,494**	**0.8%**

1.14 Demand for electricity was 1,213,326 Million Units (MU) during the year 2017-18, whereas during the year 2018-19 was 1,274,564 MU. On the other hand, availability during the year 2017-18 was 1,204,697 MU whereas during the year 2018-19 availability was 1,267,209 MU. Whilst the deficit has remained marginal at 0.7% in 2016-17 and 0.6% in 2018-19, the supply needs to increase further to match the growing demand from economic growth, increasing urbanisation and rural electrification.

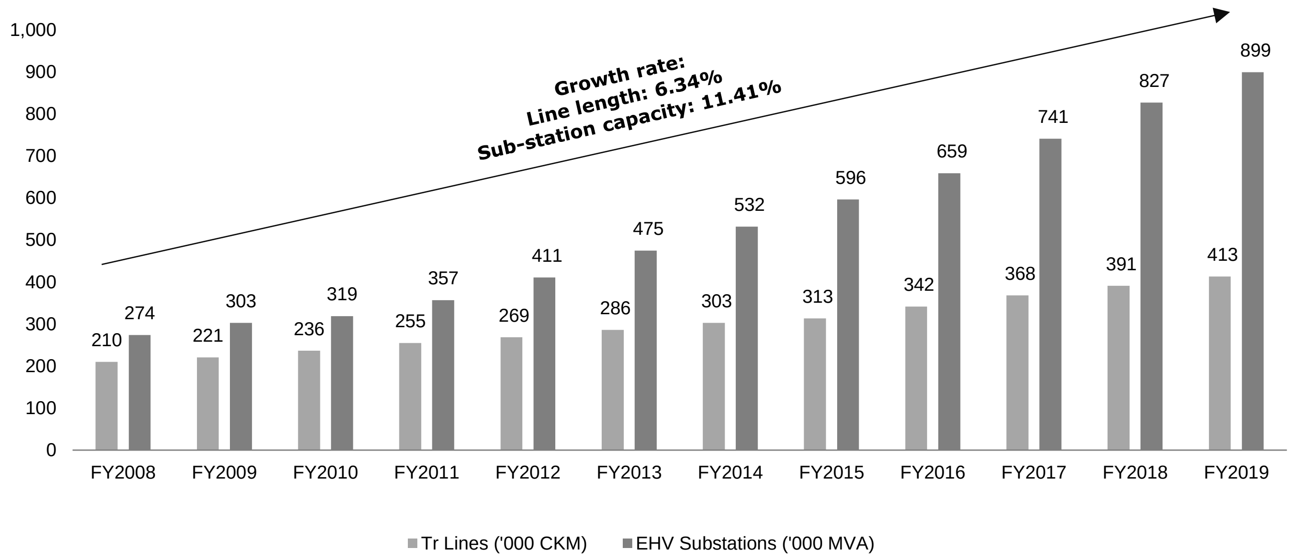
Peak demand for power has increased from 160,752 Megawatt (MW) during the year 2017-18 to 177,022 MW during 2018-19; peak deficit was at 0.8% in the year 2018-19.[15] The overall GDP composition of India has been skewing towards the services sector and this has resulted in lowering of the electricity intensity of GDP consumption from 1.1 to around 0.8.

1.15 India's electricity consumption increased from 1,061,183 Gigawatt Hour (GWh) in the year 2016-17 to 1,123,427 GWh in the year 2017-18, an increase of around 6.5%. The electricity consumption is expected to be 1,196,309 GWh in 2018-19. However, due to India's high population base and low power consumption in rural areas, per capita consumption of electricity was 1,149 kilowatt hour during the year 2017-18 and is estimated to be around 1181 kilowatt hour in 2018-19. The per capita consumption is lower than the global average signifying potential opportunities for migrating to an electricity intense ecosystem[16].

TRANSMISSION AND DISTRIBUTION

1.16 India's capacity of transmission system of 220 kilovolt (KV) and above voltage levels as on 31 December 2019 was 421,244 circuit kilometre (ckm) of transmission lines and 952713 Mega Volt Ampere of transformation capacity of substations.

Figure 10: Transmission line length and sub-station capacity trends



1.17 Almost 100% of transmission facility and 85% of distribution facility in India is owned by the public sector. To enable greater private participation, in recent years a number of transmission projects in different regions have been awarded to private bidders under a competitive bidding model. Also, privatisation of distribution is being attempted by way of sale of government owned distribution licensees and through appointment of private distribution franchisees in select states.

RECENT DEVELOPMENTS

1.18 Indian power sector has seen significant developments with progressive policy-level changes and effective implementation of directives. Some of the key initiatives taken by GOI in last one year to boost the Indian power sector were concluding the existing financial re-engineering measures proposed under Ujwal Discom Assurance Yojana (UDAY) and formulating additional reform frameworks to buttress the efforts under UDAY to achieve a complete financial and operational turn-around of State owned Utilities, setting up of RE Management Centres (REMCs), launch of Power Rail Koyla Availability through Supply Harmony (PRAKASH) Portal, allowing use of linkage coal for short term power procurement and power exchanges, mandated opening of Letter of Credit (LC) to address issue of payment delays by electricity Distribution Companies (Discoms) and ensure sustainability of power sector, shifting State level merit order to National level merit order for Inter-state Generating Station (ISGS) plants to reduce cost of power to the consumers, measures towards revival of stressed assets, promotion of RE power by extension of waiver of Interstate Transmission System (ISTS) charges, release of draft policy for supply of Round-the-Clock (RTC) power to Discoms from a mix of RE and coal-based plants, widespread adoption of peaking and RTC bids, publication of revised guidelines for Charging Infrastructure for Electric Vehicles (EVs).

1.19 GoI had launched UDAY for State owned Distribution Utilities on 20 November 2015 to usher reforms across the power and coal Sectors through competitive and cooperative federalism to pave the way for 24X7 affordable and reliable Power for all. UDAY scheme is now in final stages, with majority of states having completed 3 years at the end of FY2019. The performance from FY2016 to FY2018 (based on the data submitted by states on the UDAY portal) shows a consistent improvement in Aggregate Technical & Commercial (AT&C) losses, and reduction in annual losses by almost 50% of pre-UDAY times. The GoI is now formulating additional reform frameworks to buttress the efforts under UDAY to achieve a complete financial and operational turn-around of state owned utilities.

1.20 Eight REMCs have been commissioned in the states of Andhra Pradesh, Karnataka, Tamil Nadu, Madhya Pradesh, Maharashtra and Gujarat and Southern Regional Load Dispatch Centre and Western Regional Load Centre during 2019. These REMCs would help in grid integration of RE by taking care of intermittency of RE generation and, facilitating real time forecasting, scheduling and real time tracking of RE generation.

1.21 PRAKASH Portal was launched on 3 October 2019. Benefits of Portal to Stake-holders: on a single platform, the following information will be available:

- Summary Dashboard: Summary of generation, coal receipt for power plants, dispatch by coal company and rake placement by railways for month and FY.
- Geo Status: Summary of power plant and siding details on map of India.
- Reports: Following report will be available
- Daily Power Plant Status: Report gives station data related to power generation, coal receipt, consumption and stock.
- Plant Exception Report: Report gives station list having given stock on particular date.
- Periodic Power Plant Status: Report gives station data related to power generation, coal receipt, consumption and stock for selected period. Coal materialisation based on dispatch by coal company is available.
- Coal Dispatch Report: Report gives subsidiary wise coal dispatch for particular period. It also gives source wise details of dispatch. Dispatch trend is also visible.

1.22 For the first time, linkage coal was allowed to power plants for selling power in the Day Ahead Market (DAM) through power exchanges or in short term through a transparent bidding process through Discovery of Efficient Energy Price (DEEP) portal. A methodology in this regard was issued by Ministry of Power (MOP) on 2 December 2019. Till now the Coal Linkage was granted to power generating stations only for selling power through long term and medium term PPA. This move shall de-stress the power generating stations which have not secured long term or medium term PPAs.

1.23 GoI has taken a major step to address the problem of mounting outstanding dues towards generating companies by the distribution companies by issuing an order on 28 June, 2019 regarding opening and maintaining of adequate LC as payment security mechanism under PPAs by distribution licensees. This mechanism has been made effective w.e.f. 1 August 2019.

Under this mechanism, power will be scheduled for dispatch only after LC for the desired quantum of power with respect to the generating stations has been opened. It shall be ensured by the concerned load dispatch centre that such entity, during the period of non-scheduling of power on account of non-opening of LC or advance payment, has no access to procure power from the power exchange(s) and they shall not be granted Short Term Open Access (STOA).

The measure is expected to improve payments to power generators and improve sustainability in the power sector.

1.24 To reduce the cost of power procured by the distribution licensees, a new system has been put in place where for ISGS, the merit order dispatch at national level shall be followed. Hence the cheapest generation will be available at the maximum level. This is a step where for ISGS, the state level merit order has been shifted to national level merit order. This mechanism has resulted in savings of approximately INR30 million every day and has a potential of saving INR12,000 million in a year towards power procurement cost of distribution licensees.

An Order was issued by MOP on 15 November 2019 on “Reduction in cost of power due to pre-payment in entire value chain of power sector”. Electricity Regulatory Commissions are requested to take necessary actions in reduction of cost due to pre-payment as in such cases the working capital requirements get reduced. This initiative reduces the cost of power to the consumer.

1.25 A Pilot Scheme was introduced by MOP in April 2018 to facilitate procurement of aggregated power of 2500 MW for 3 (three) years (covered under medium term) from the generating companies having coal based power plants which are already commissioned without having a PPA for the quantum of power the bidder is willing to bid. Based on the experience gained in the pilot scheme, pilot scheme–II for procurement of another 2500 MW for the period of three years under medium term was notified on 1 December 2019.

1.26 India with rapidly adopting renewables and commitment to reduce carbon footprint is at the cusp of energy transition. With various policies aiming at increasing renewables in energy mix, India has to undergo transformation in technology, system operations, electricity markets and regulation to enable seamless transition.

1.27 To promote the capacity addition of solar and wind power projects, the waiver available for use of ISTS transmission charges and losses has been extended for use of ISTS for transmission of electricity by solar or wind power projects commissioned till December 2022. The waiver shall be applicable for 25 years from the commissioning of such projects.

1.28 With RE gaining traction, emphasis will be on promoting storage technologies. GoI has taken some landmark initiatives in this regard like reduction in custom duties on certain minerals like cobalt, approved the national mission of transformative mobility and battery storage, under which phased manufacturing programs, introduced a wind-solar hybrid policy in May 2018, released a draft policy in Jan 2020 for the supply of RTC power to Discoms which would be a mix of RE and electricity generated in coal-based plants.

1.29 In the past one year, the sector has also witnessed a surge in the issuance of storage based tenders – both big and small. Storage technologies have improved in terms of performance and efficiency. Tariffs too are accordingly becoming more attractive as discovered in the recent SECI 1.2 GW bid with assured peak power supply (“ISTS-VII”). Greenko Energies Private Limited, HES Infra Private Limited, Renew Solar Power Private Limited had participated in the bid at the following Peak tariffs:

Table 2: Bids received in the recent SECI Peaking bid

Bidder	Capacity (MW)	Peak tariff (INR/kWh)
Greenko Group	900	6.66
HES Infra Pvt. Ltd	120	6.90
Renew Group	600	6.95

All 3 bidders were shortlisted for reverse auction; subsequent to the reverse auction, Greenko Group and Renew Power won the bid. While Greenko Group has been awarded 900 MW at a weighted average tariff rate of INR4.04/unit, Renew Power has won 300 MW at a weighted average tariff of INR4.30/kWh. Greenko Group offered the Peak tariff of INR6.12/kWh for PSP based storage technology and Renew offered the Peak tariff of INR6.85/kWh for battery based storage technology.

Table 3: Tariff discovered in the recent SECI Peaking bid after reverse auction

Bidder	Capacity (MW)	Peak tariff (INR/kWh)	Off peak Tariff (INR/kWh)	Weighted Average Tariff (INR/kWh)
Greenko Group	900	6.12	2.88	4.04
ReNew	300	6.85	2.88	4.30

1.30 In February 2020, SECI issued Tender for 14 MW of solar power projects with 42 MWh battery storage system (7MW/21 MWh each) at Leh and Kargil divisions. The tariff to be paid to the Solar Power Developer (SPD) has been set as INR2.00/kWh at the interconnection point, for the entire period of the PPA. The projects should be developed on a build-own-operate basis, and the selected project will be given a viability gap funding (VGF) in line with the terms and conditions of this Request for Selection (RfS). The upper limit for the VGF to be quoted by a bidder has been kept at INR130 million for 1 MW solar project with battery storage of 3 MWh.

1.31 India is committed to the global climate change initiative and has ratified the Paris Agreement on Climate Change in October 2016. As part of the Nationally Determined Contributions (NDC), India has committed to reduce the emissions intensity of its GDP by 33–35% by FY2030 from the FY2005 level. It has set the following strategies to meet these targets:

- To achieve about 40% cumulative electric power installed capacity from non-fossil fuel based energy resources by FY2030 with the help of transfer of technology and low cost international finance including from Green Climate Fund (GCF).
- India aims to become 100% EV nation by FY2030. To give a boost to this plan, GoI has awarded contracts to several automobile and charging companies for procurement of EVs and charging stations for replacing their existing fleet of vehicles to EVs.
- Promoting use of alternate/clean fuels for electricity generation, cooking, transportations, industrial use, etc.
- GOI, under the National Mission for Enhanced Energy Efficiency programme is promoting several energy efficiency schemes like Perform Achieve and Trade (PAT) scheme for industrial energy efficiency and Unnat Jyoti by Affordable LEDs and Appliances for All (UJALA) scheme wherein it has already distributed around 362[17] million LEDs.

1.32 National Electric Mobility Mission Plan (NEMMP) 2020 aims to achieve national fuel security by promoting hybrid and EVs in the country. It has set ambitious target of 6-7 million sales of hybrid and EVs year on year from 2020 onwards.

1.33 Globally, the electric mobility is expanding at a rapid pace. In the EV30@30 Scenario, which accounts for the pledges of the EVI EV30@30 Campaign to reach 30% market share for EVs by 2030, electricity demand to serve EVs is projected to reach almost 1 110 Terawatt Hour (TWh).

1.34 The MOP launched the National e-Mobility Programme in India in March 2018, with an aim to provide impetus to the entire e-mobility ecosystem including vehicle manufacturers, charging infrastructure companies, fleet operators, service providers, etc.

- Aligned with the GoI's vision of 100% e-mobility by 2030, Energy Efficiency Services Limited (EESL) to issue fresh tender for additional 10,000 electric cars.
- Together 20,000 e-cars to annually save 50 million litres of fuel and reduce 0.56 million tonnes of annual CO2 emission.

1.35 In April 2018, the MOP released a clarification that during the activity of charging of battery for use in EV, the charging station do not perform any of the activities namely, transmission, distribution or trading of electricity, which require license under the provisions of the Electricity Act, 2003 (ET Act), hence the charging of batteries of EV through charging station do not require any license under the provisions of the ET Act.

1.36 To promote electric mobility and for enhancing energy security, draft amendments to the tariff policy released in May 2018, laid down that SERC's may issue appropriate tariff framework for electricity supply from the Discom to the charging stations such that:

- Tariff shall be less than or equal to the average cost of supply determined based on AT&C loss level of 15% or actual, whichever is lower, and
- There shall be a single part tariff for this purpose in the initial 3 years.

1.37 The GoI revised the guidelines and standards for charging Infrastructure for EVs on 1 October 2019. Nos of Public Charging Stations Installed by NTPC/EESL till December 2019 are as follows:

- NTPC: 57
- EESL: 65

1.38 In the Indian Budget Speech for 2020, the GoI announced following measures/proposals from policy standpoint:

- Budgetary allocation of INR220 billion to 'Power and Renewables' sector for the FY2020-21.
- To address financial stress faced by distribution companies, States/Union Territories urged to replace conventional energy meters by prepaid smart meters in three years, and consumers to have freedom to choose the supplier and rate. Further reform measures to be introduced.
- India committed to curb carbon footprint as agreed in the Paris agreement in 2015. It is proposed to shut down thermal power projects having carbon emission in excess of pre-set norms.
- To expand solar power generation capacity – a) a scheme to be operationalise to enable farmers to set-up solar power generation capacity on their fallow/barren lands; and b) large solar power capacity to be set-up along-side rail tracks on land owned by railways.

1.39 On tax front, vide Indian Budget 2020 and The Taxation Laws (Amendment) Act, 2019, following has been proposed/enacted:

Income-tax

- An option to avail following concessional tax regime has been introduced for domestic companies with effect from 1 April, 2019 provided it forgo certain tax incentives and deductions [enacted vide The Taxation Laws (Amendment) Act, 2019]:
  - 15% base tax rate for new manufacturing companies (satisfying prescribed conditions) incorporated on or after 1 October, 2019 and commencing manufacturing/production on or before 31 March, 2023. Effective tax rate to be 17.16% (applying uniform surcharge rate of 10% and cess of 4%) [Section 115BAB of the Income-tax Act, 1961 (IT Act)]

    Vide Indian Budget 2020, it has been expressly clarified that generation of electricity business would qualify to be 'business of manufacturing or production of an article or thing for the purpose of aforesaid regime and therefore eligible for 15% base tax rate.
  - 22% base tax rate for existing companies. Effective tax rate to be 25.17% (applying uniform surcharge rate of 10% and cess of 4%) [Section 115BAA of the IT Act]

  Companies opting for any of the above regimes would not be subject to Minimum Alternate Tax (MAT).
- To incentivise investment by Sovereign Wealth Funds (satisfying prescribed criteria) of foreign governments in priority sectors, 100% tax exemption to be allowed on interest, dividend and capital gains income earned from investment made in prescribed infrastructure facility/other (to be) notified sectors. Investment should be made on or before March 31, 2024 and held for at least three years to be eligible for tax exemption.
- Other key tax proposals:
  - Dividend distribution tax (DDT) to be replaced by classical system of dividend taxation wherein it will be taxed in the hands of shareholders. This will allow lower tax treaty rates on dividends to apply for foreign investors.
  - With the intent to provide uniform tax status to listed and unlisted Infrastructure Investment Trusts (InvITs), definition of `business trusts' (which earlier recognised only listed InvITs) to now include unlisted InvITs as well.
  - Sunset date for concessional rate of tax withholding (i.e., 5%) under sections 194LC and 194LD of the IT Acts extended to June 30, 2023.
  - Tax dispute resolution introduced for settlement of tax disputes to help de-clog the legacy litigation.

Indirect tax

- Tariff rate on solar cells (whether assembled or not in modules or panels) increased from Nil to 20%; however, full exemption from basic custom duty (BCD) to continue thereby retaining the effective rate as Nil.

- BCD exemption for Naptha used for generation of electricity by an electricity generating company withdrawn; BCD to be levied on Naptha at 4%.
- BCD exemption on import of electrical energy withdrawn; such electrical energy to now attract BCD at INR2,000 per 1,000 KWH. There is no change in concessional rate of BCD on import of electrical energy originating from Nepal/Bhutan or Special Economic Sone (SES) to Domestic Tariff Area (DTA)
- To support the domestic value addition in assembly of electric vehicles, BCD rates increased on import of passenger electric vehicles/motor cycles falling under heading 8703/8711, to bring them at par with non-electric vehicles/motor cycles. In addition, BCD increased on import of electric commercial vehicles under heading 8702 and 8704.

2. GENERIC INDUSTRY ISSUES

2.1 Although various significant steps have been taken in this direction, there are several areas such as utilities have cancelled RE bids after the outcomes of bid process, gas based power projects are stressed and running at sub-optimal levels due to lack of gas reserves in the country, stressed power plants are struggling for re-financing, delayed payment by electricity distribution utilities, management of cross-subsidies, cross subsidy surcharges, open access, imposition of additional surcharge, commercial revival of the state electricity boards and proper management of grids where more policy thrust is needed.

2.2 RE sector is also facing challenges in recent times; the sector witnessed a hit in recent times due to lack of interest of financial institution to fund RE projects, ambiguity over GST and safeguard duty and low investor sentiment due to delayed or non-payment by Discoms to clean energy developers. This led to difficulty in raising finance especially from scheduled public and private banks who remained reluctant to invest in infrastructure projects.

2.3 To protect domestic cell and module manufacturers, a 25% safeguard duty was announced on solar cell and module imports from China and Malaysia for the period between July 30, 2018, and July 29, 2019. The duty was set at 25% for the first year, followed by a phased down approach for the second year, with the rate reduced by 5% every six months until the duty is set to end after July 2020. Since a majority of solar projects were already under development when the safeguard duty was announced, they came under the Change in Law clause to get compensated for increased project costs as a result of the duty. However, most of the solar developers have been struggling to get the reimbursement for their additional expenses. This has adversely affected their business and the pace of project development in the country.

2.4 Grid congestion is also a regular occurrence in some states such as Tamil Nadu and Rajasthan during peak generation and low demand period, and there were few incidences of curtailment of solar and wind in other RE rich states like Andhra Pradesh and Maharashtra.

2.5 Delay in disposal of cases filed in the regulatory commission/appellate tribunal for Electricity are resulting in additional working capital during the pendency of the case. The AP Power fiasco where the new GoI terminated 21 PPAs, have raised questions on the sanctity of signed legal contracts. The AP High Court has directed the independent power producers to approach the Andhra Pradesh Electricity Regulatory Commission for relief, but has told the State to pay developers, till the matter gets settled, at the rate of INR2.44/unit, the target price of the State GoI in the negotiations. Meanwhile, the state’s dues to the power producers have piled up, putting various stakeholders in the sector, including developers and lenders, in a quandary. RE developers face uncertainty as tariff renegotiation could lead to additional delays in payments from Discoms. Policy changes have been sudden and unpredictable in other states as well. Gujarat decided last year that only projects which supply power to the state Discom could use land within the state, flouting a central procurement agency’s rule for setting up projects under the interstate transmission system. Similarly, Rajasthan, one of the most sought after states for solar power plants have announced its decision to levy additional cess on all projects that sell power outside the state.

2.6 Discoms in some of the top RE generating states are biggest defaulters in paying dues for the power procured from RE projects. Because of SECI's back to back arrangement with the Discoms, if Discoms delay in paying on time, then the payment to generators are also getting adversely affected. The backlog of payments and revision in PPA tariff have shaken investors' confidence tremendously.

2.7 Challenges for power institutions like structure of institutions, power theft and inability of distribution companies to collect revenues also add burden on the power sector.

2.8 Financing power projects is presently a challenge for developers given the high financial stakes involved in power projects. As a result, this sector continues to be affected by way of shortfalls – both in generation and transmission capacity.

The Indian power sector is highly leveraged – as high as 70-80% and continues to struggle for funds. As mentioned earlier, financing power projects has been perennially constrained for developers given the long-gestation period of projects and high financial stakes. Given the high exposure of banks in this sector and sectoral cap on lending by domestic financial institutions, financing power projects has been an impediment. Indian power companies have been exploring opportunities of borrowing overseas funds for their projects.

2.9 Nearly 60% of the corporate debt owed by the private power producers is with companies having interest coverage ratio of sub 1 (hereinafter referred to as "IC sub1 companies"). Cash flows of said IC sub1 companies are on a declining trend, thereby, leading to increased borrowings. These issues have led to cost overruns. Coupled with high cost pressures, falling Plant Load Factors (PLF) and tariff rates aren't helping much:

- PLF are exceptionally low and tumbled to about 60% from 75% levels over the last 5 years.
- Merchant tariffs for electricity purchased in the spot market have slid to around INR3/kwh, far below the breakeven rate of INR4/kwh needed for most plants.

As a result, cash flow for most private power generation companies falls short of what is needed to service interest obligations. This has led to about 40 GW of stressed assets mostly in coal and gas based generation segments.

3. KEY ISSUES AND RECOMMENDATIONS

3.1 Implementation of new technologies

While CO_2 emissions are unavoidable when using coal-fired power generation for electricity due to its nature as a fossil fuel, it is imperative to use and adopt new environmentally sensitive technologies in India that will lead to maximum efficiency and reduce emission of harmful gases and toxics, including mercury emissions. India has committed to reduce its carbon emissions at the UN Climate Change Conference held in Paris in 2015 as a part of its intended nationally determined contributions goals which were subsequently ratified in 2016. The Ministry of Environment, Forest and Climate Change has introduced clear guidelines into the law on allowable emission standards for SOX/NOX/Mercury from coal fired utilities. The guidelines provide for specific measurable emissions norms for all super-critical and sub-critical power plants going into generation from 2017 onwards, in line with Mercury and Air Toxic Standards (MATS) in the US and norms being promulgated in China. For all fossil fuel burning electricity generating plants, incentives are provided to encourage use of emission capturing equipment and processes including use of activated carbon to reduce mercury and other toxic emission.

European companies are well equipped to provide cutting edge know-how to electricity generation businesses in India to meet this critical objective.

Recommendation:

Innovative new technologies such as super-critical, ultra-supercritical, and even solar-thermal in the thermal power sector and high concrete dams, special tunnels, tidal power and offshore wind power projects in the renewable sector have demonstrated high efficiencies worldwide and their proper implementation is vital in achieving the maximum efficiency from the project.

3.2 Promote hydro-power sector

- Recently, MOP has issued measures to revive hydro power projects and announced certain policy measures but the implementation of policy measures is still unclear especially for private developers.

Recommendation:

- Under National Solar Mission, various incentives were offered like: zero import duty on capital equipment, raw materials; low interest rate and priority sector lending; single window mechanism for all related permissions - this gave push to the solar sector. A similar approach for hydro should also be adopted to revive the ailing hydropower market.
- Discussion with states to promote conducive environment to make projects viable for implementation of hydro projects like waiver of water cess and free power; waiver of transmission charges and losses as is available to wind and solar projects.
- GoI needs to intervene to evoke investor's confidence in the sector. Delay in land acquisition and forest clearance issues should be mitigated with a timeline through a systematic system. A default or delay in each step of clearance should be deemed as accepted.
- It is also suggested that Ultra Mega Power Project (UMPP) model as is prevalent in case of thermal projects should be adopted for hydro also where project is brought to the stage of readiness by the Bid Process Coordinator (BPC like REC/PFC) appointed by the GoI. After the allotment of the project to the successful bidder, the cost incurred by BPC should be reimbursed.
- Proper coordination and implementation of policies with all stakeholders (Ministries and States) and timely issuance of policy is the urgent need of the sector. For instance: certain policies like Tariff Policy, proposed amendments to Electricity Act are still in the draft stage and have been pending for long which is affecting the stakeholders.
- Keeping a close watch on the financials of involved entities to safeguard the country against further non-performing assets.
- For strict implementation of policy measures, there have to be stringent penalty mechanism in place. For instance, penalty for non-compliance of RPO/HPO or standard of performance laid down by the regulatory commissions.
- During the course of policy formulation, it is imperative for the GoI to take a holistic view and evaluate its impact on the all stakeholders. For instance: in Andhra Pradesh, reduction in the term of solar PPA from 25 years to 5 years is being deliberated for the PPAs in force, this may hamper the existing projects as well as upcoming projects and may be detrimental for developers.
- For Indian GoI promoted projects in neighbouring countries, it has been seen in some cases that only Public Sector Undertakings (PSUs) are allowed to participate. Global companies that have established their manufacturing facilities in India cater to the regional market also. Such companies do not get a chance to participate in bids. Therefore, it is suggested that tendering process should be open to all legal entities registered in India having requisite experience and manufacturing set up in line with 'Make in India' policy.
- The Indian subcontinent today is seeing exponential growth in RE from photovoltaic solar and wind. Due to unpredictability and variability associated with the RE, there is strong need to balance the grid through storage technology. Presently, Pumped Storage Plants (PSP) is the most matured technology available for large storage requirements. With geography favouring setting of PSPs in India, it would act as a hydro battery to the region. Battery is another form of storage device available but in the long-run, large scale disposal of such devices can be a problem for the environment.

  There is a strong need to establish financial viability of PSPs through policy support for introduction of revenue stream for ancillary services or capitalising the cost of PSPs as part of transmission/distribution network since today its primary role is foreseen to balance the grid.

- RE projects are covered under priority lending which is cheaper than other sources of credit. With all hydro projects categorised as renewables, all hydro projects should now be eligible for priority sector lending.

Banks are reluctant to fund hydro power project and state finances are also constrained for giving subsidies and grants. Therefore, innovative financing solutions should be explored to make hydro self- sustainable (i.e. financing instruments with long-repayment tenure and subsidised interest rate).

3.3 Addressing variability and intermittency of renewable resources

To meet 175 GW of renewables by 2022, India has to work on enabling framework for seamless integration. High incidence of renewables in the grid will pose challenges with respect to variability and intermittency of renewable resources. While there are many ways to address variability and intermittency of renewable resources, adaptation of Battery Energy Storage System (BESS) is widely preferred owing to its modularity, response, flexibility in services and geographic reach. However adaptation of the BESS is in nascent stage due to high cost. The GoI has to have a two-pronged approach aimed at tactical (short term) and strategic (long term) to address existing needs and pave way for increased adoption as costs will come down and developers can tap new revenue streams.

At present storage based base load or RTC supply may not be palatable for off-takers and Discoms. For providing round the clock supply with hybrid solutions will result in deployment of large scale storage systems. For example, recent Greenko project in Andhra Pradesh envisages 2 GW solar, 0.5 GW wind and 1000 MW (8000 MWh) of pumped hydro to provide base firm power of 1.2 GW (peak) and around 500 to 600 MW (off-peak). While the tariff for such proposition is to be assessed, with BESS the same proposition will result in deployment of 8000 MWh BESS system. With the present cost of BESS, this is cost prohibitive as the resulting tariff will be high.

BESS can be broadly categorised based on service as power application or energy application. Power application is characterised by fast response, frequent battery operations, shorter time period (power plant smoothening, frequency regulation, power quality). Energy application is primarily for larger duration of charging and discharging cycles (load shifting, transmission line deferral, peak load shifting). Sizing and chemistry of a BESS system depend upon the defined functionality. Energy application chemistries are generally less costly than chemistries used for power applications.

Recommendation:

Short term policy measures

- **Allow retrofitted renewable plants with storage to participate in ancillary markets:** Presently only un-requisitioned ISTS generating stations (thermal) are participating in ancillary markets. This is basically slow response as thermal power plants ramp rates are slow (15 to 30 minutes). Further quantum of power available for ancillary services is limited and subject to change in real time as original beneficiaries can call back their un-requisitioned power. The proposed discussion paper on revamping ancillary markets by CERC has envisaged participation of all inter-state/intra-state including public and private. However RE generators are excluded. The paper also envisages co optimisation of energy and ancillary markets to determine market clearing price and volume through market engine. Including retrofitted renewable generators will provide operator more flexibility for system operator.
- **Focus on energy applications bids (specific use case) to take advantage of cost economics**: Utilities/State Transmission utilities should focus on single use case for optimisation of BESS sizing (such as firm supply for a particular period). For example, we analyse recent bids called by Andhra Pradesh Discom for flexible power supply of 600 MW with daily energy of 8.76 Mus (60% PLF). Under this tender Andhra Pradesh Discom shall schedule firm 600 MW from 11 to 3 PM (i.e. 2.4 million units) the rest 6.36 million units can be scheduled as desired by Discom daily on day ahead basis. This lends uncertainty w.r.to sizing of battery. Developers have to size their battery and solar plants for worst case scenario in order provide flexible service for around 20 Hrs. Alternatively, if Discom specifies time slots for charging and discharging per their historic load pattern to meet specific requirement (peak power or ramping requirement) and reduces flexible supply time, then

developers can optimise BESS and RE source size resulting in optimal tariff.

- **Encourage/incentivise EV to use bidirectional batteries. Also make mandatory storage for charging infrastructure:** This will create sufficient pool for ancillary services as markets evolve in future for participation.
- **Utilities can plan adoption of BESS in annuity model for transmission line deferral, especially in urban areas:** In urban areas load and peak load requirement is growing. This demands for substation upgradation to meet peak load requirements. Using BESS will help in deferring or avoiding transmission system upgradation. For example, if a particular distribution area is being served from an upstream transmission/distribution substation and there is a need to upgrade upstream substation and transmission line to cater to increased demand. This can be deferred by deploying suitable BESS system in the supply area. This will act as distributed generator during peak while charging during off-peak hours there by deferring the need to upgrade upstream substation and transmission line.

Long term technological and market reforms

- **Markets for standalone Storage systems should be evolved with different business models**
  - **Frequency regulations markets should be operational through auction based pricing:** At present there is no frequency regulation market. Variation in frequency is taken care by balancing load (load shedding) or generation control (increase or decrease of generation). While ancillary markets mechanism is operational, the quantum and response time is not suitable for taking care of frequency. As grid becomes technologically suitable then in future frequency regulation markets should be made operational. This will provide business model and revenue streams for stand -alone BESS service providers.
  - **Tolling model where battery owner stores electricity for utility for a fee (two part tariff can be envisaged for capacity and energy):** Utilities procure power from the market, exchanges to meet their short term and seasonal requirements. This usually happens at the time the demand is high and prices are high at the exchanges there by increasing average cost of procurement of utilities. Utilities can explore standalone BESS providers to store power when the market price is low or demand w.r.to the utility is low and utilise the same when the demand is high. Also utilities can fully dispatch their contracted power with generators (where the tariff is low) during off peak and store the power. Suitable policy, regulatory and market mechanism should be evolved for the same.
  - **Battery owners should be allowed to take price arbitrage (difference between purchasing and selling of power from market):** This will provide additional revenue streams for standalone BESS providers.
- **Smart grid initiatives can enable to take advantage of last mile participation:** Behind the meter, small scale battery systems, EV charging infrastructure to bring into the ambit of ancillary markets
- Encourage round the clock supply from renewables using storage as the costs of storage comes down. GoI can also envisage VGF model to incentivise Discoms as tariff reduces.

3.4 Introduction of reverse auction bidding

Several foreign companies have set up manufacturing facilities in India which aligns well with the GoI’s ‘Make in India’ initiative. This initiative of the GoI was primarily set forth to encourage foreign companies to set up manufacturing base in India to promote FDI. Under this initiative, one primary objective was to provide a purchase preference to the domestic manufacturers to supply from India and enjoy this benefit. Further, foreign companies who have set-up base in India, are needed to pre-qualify for tenders which require procurement of goods and services. Under this scenario, many central PSUs and state utilities, have provided the provision whereby a bidding entity can qualify for a particular tender based on the credentials of its parent company (for electro-mechanical suppliers).

When such safeguarding and welcome measures have been made available to domestic companies to bid in a free and transparent bidding system, the CVC Guideline vide memo dated 11 June 2015, provides a procuring entity to exercise electronic reverse auction (e-RA) to purchase capital equipment for projects where the equipment purchase is substantial in value. This practice of reverse auction usually leads to bidders underbidding one another. This very process of e-RA then contradicts the 'Make in India' initiative, purpose of the GoI fails when these same companies bid through the e-RA, where margins are either diminishing or negative for that matter.

Recommendation:

An appropriate mechanism to safeguard the interest of developers as well as suppliers should be formulated. For instance, reverse auction to be made applicable to select the lowest bidder where more than 50% of the bids are above the budgeted price.

3.5 Extend investment-linked incentive under the IT Act to power sector companies

The GoI's stated policy intent for gradually phasing out tax incentives has led to a sunset on income-linked tax holiday[18] for power generation and distribution, with effect from1 April 2017. Further, accelerated tax depreciation for power businesses in respect of certain block of assets, earlier allowed at the rate of 80%, has been capped to 40% with effect from 1 April 2017.

At the same time to encourage capital investments in large infrastructure projects, Finance Act 2016 had extended the benefit of investment-linked incentive to business of developing and/or operating and maintaining an infrastructure facility including roads, highway projects, water supply/treatment projects, port/airport projects, etc. However, such investment-linked deduction has not yet been introduced in respect of capital costs incurred by power businesses.

It is imperative to provide for adequate fiscal incentive for stimulating private investments in the power industry.

Recommendations:

It is recommended that accelerated depreciation rate of 80% should be continued for specified block of assets. Alternatively, the GoI may consider including generation and distribution operations within the definition of 'infrastructure facility' eligible for investment-linked deduction in respect of capital costs incurred under section 35AD of the IT Act.

3.6 Need for tax consolidation structure

Presently, owing to the PPA or financing requirements, power business end up creating a whole web of companies under a holding company. A power company on an average operates 20-100 SPVs, of which early stage companies incur losses while the advanced stage companies earn profits. However, in the absence of explicit provisions under the IT Act, setting off of losses against the profits of entities is not permissible leading to unnecessary tax pay-outs for the group as a whole.

Recommendations:

To facilitate growth for power companies, GoI may consider allowing multiple SPVs held under the same ownership structure to file a consolidated group tax return, thereby, leveraging group level synergies for an improved tax outcome. This will also enable cash flow efficiencies amongst multiple projects and thus, encourage ploughing back of surplus resources.

3.7 Need for adequate fiscal incentives for encouraging financing of power projects

The GoI has announced significant capacity addition in power sector, especially in renewable space (175GW). One key challenge for the sector, however, shall be to achieve required financing for new projects. Whilst the Indian power sector is highly leveraged, project developers continue to explore opportunities of borrowing overseas funds for the projects.

Vide Finance Act, 2017, the GoI has extended/provided the benefit of concessional tax withholding base rate of 5% on External Commercial Borrowings (ECB) and masala bonds. On the flip side, the GoI has also introduced limit on interest deduction in line with recommendations of the OECD Base Erosion and Profit Shifting Action Plan 4. Such provisions are applicable to an Indian company or a permanent establishment of a foreign company incurring interest expenditure exceeding INR10 million in respect of debt owed to a non-resident associated enterprise (AE) or to a non-AE i.e. third party lenders (in respect of debt guaranteed by AE). Interest in excess of 30% of Earnings before Interest, Taxes, Depreciation and Amortisation (EBITDA) or interest paid or payable to non-resident AE or to non-AE (in respect of debt guaranteed by AE), whichever is lower is proposed to be disallowed. Such interest expense to the extent disallowed is henceforth to be carried forward for 8 years for set off against business income of future years, to the extent of maximum allowable interest, i.e. 30% of EBITDA. Considering debt-push down structure is common in power companies, disallowance of interest cost reckoned with respect to 30% of rule could pose significant challenge for project entities as the effective post-tax cost of debt investments could soar.

Further, guarantee from the parent/group company (i.e. an AE) is generally a pre-requisite for third party loan arrangements, such as initial project finance lending by banks. Accordingly, above provisions seeks to place a restriction on deductibility of such third party interest cost too.

Recommendations:

Considering that power projects are capital intensive and require significant financing, the GoI should consider the following approaches:

- Exempt infrastructure projects, including the power generation and/or distribution projects from the applicability of thin capitalisation rule under the IT Act. Such companies have large capital requirements and are highly leveraged due to commercial imperatives. Any limitation on deductibility of interest cost could significantly inhibit the commercial feasibility of projects in such sectors which are otherwise crucial for a sustained economic growth.
- Introduce a much higher ratio (i.e. greater than 30%) for such projects, to ensure the limitation on interest deduction is triggered only in exceptional cases, without rendering debt financing more expensive for the developers.
- Remove the restrictions on number of years to carry forward interest disallowed under section 94B of the IT Act.
- Scope of section 94B may be narrowed to exclude debt raised through an implicit/explicit guarantee from the AE (in particular of power businesses). Group ratio rule for deductibility of interest may be introduced (like introduced in Norway vide Budget 2019) to account for business models which are highly leveraged worldwide due to commercial reasons and not particularly for reason of Base Erosion and Profit Shifting.

3.8 Enable investments via Foreign Venture Capital Investor (FVCI) route in companies engaged in supporting power sector

In recent years, foreign investments in infrastructure sector by a registered FVCI[19] has gained momentum and is fast emerging as an alternate to investments under extant FDI regime. This is primarily driven by the fact that it provides for a more liberalised investment framework; key relaxations are illustratively mentioned hereunder:

- Entry and exit pricing guidelines applicable under the FDI regime do not apply to investment by FVCIs;
- No ceiling on interest pay-outs.

Presently, whilst ‘infrastructure sector’ for this purpose is defined to include activities involving power generation/ distribution/ transmissions, however, few critical activities supporting power sector (vis. O&M activities, power consultancy, etc.) are not specifically included, thereby, discouraging FVCI investments in power sector on a holistic basis. Furthermore, FVCIs are allowed to invest in companies only and not in other forms of entity vis. partnerships and LLPs.

Recommendations:

For enabling FVCI to invest in Indian power on a holistic basis, it is recommended that critical activities supporting power sector (vis. O&M activities, power consultancy, etc.) be specifically included within the definition of ‘infrastructure’.

Further, given that substantial part of project SPVs are being structures as LLP (specifically SPVs engaged in O&M activities), investment by a FVCI should not be merely restricted to corporates and should be extended to other forms of entities vis. partnership and LLPs.

3.9 Benefit of concessional tax rate of 5% in respect of specified debt/quasi debt instruments

Presently, lower withholding rate of 5% under section 194LC and 194LD of the IT Act is applicable to monies borrowed in foreign currency under a loan agreement or by way of issue long term bonds (including infrastructure bonds) or by way of issue of rupee denominated bond subject to conditions prescribed.

Specified funding instruments vis. Compulsorily Convertible Debentures (CCDs), Non-convertible Debentures (NCDs) and Optionally Convertible Debentures (OCDs) (FVCI route), duly regulated from exchange control standpoint, are emerging as preferred instruments for structuring debt/quasi –debt instruments in power sector. Presently there is lack of clarity as to whether interest payments on such specified borrowing instruments would be eligible for concessional tax rate of 5%, owing to following reasons:

- Rupee denominated bond was specifically included vide Finance Act, 2017; memorandum to Finance Bill, 2017 suggests that the intent was to cover only masala bonds (i.e. INR bonds issued outside India); and
- Requirement to take specific approval from the government for instruments not governed by ECB framework.

Recommendation:

In view of the recent liberalisation of the ECB framework and to incentivise debt investments in E&P sector, an explicit clarification should be introduced to extend benefit of concessional tax rate of 5% to funding instruments such as CCDs, OCDs and NCDs (whether or not governed by ECB framework) without any requirement to seek specific approval from the government.

3.10 GST

- Transmission or distribution of electricity does not attract levy of GST by virtue of specific exemption under the GST Laws. Further, Section 17 of the CGST Act, 2017 restricts input tax credit on procurements obtained for rendering exempt supplies. Accordingly, tax paid on procurements made for generation, transmission and distribution of electricity would not be creditable since the output supply (i.e. electricity) is exempt from GST. Consequently, GST paid on such procurements would form a part of the cost for the power sector.

Recommendation

By including electricity under the ambit of GST, output supply would become taxable and GST paid on procurements would become creditable. This would substantially reduce the cost of power generation.

Alternatively, the GoI may ensure seamless flow of GST credit across the value chain by allowing refund of input GST paid on procurements made by power project owners. Accordingly, such input GST would not form a part of cost leading to reduction in prices.

On one hand, the above recommendation may lead to a loss to the exchequer, on the other hand, such loss may be equalised on account of increased competitiveness in the market and consequent increase in production.

- Taxability of goods and services used for Engineering, Procurement and Construction (EPC) of a solar power generating system has been a critical issue since the advent of GST. Multiple adverse rulings by the GST Advance Rulings on this issue have upheld the view that such supplies would be construed as works contract service taxable at the rate of 18%. Whereas, the industry was of the view that such supplies should be treated as composite supply of goods (taxable at rate of 5%).

  To settle the dispute on characterisation of EPC projects, CBIC issued Notification 25/2018 – Integrated Tax (Rate) dated 31 December 2018 whereby it was clarified that 70% of the gross value of the project would be deemed as the value of supply of goods attracting GST at the rate of 5%. Remaining 30% would be deemed as the value of supply of services and would attract GST at the rate of 18%. However, industry does not view the deemed 70:30 ratio as a fair estimate of the actual split between value of goods and services.

Recommendation

EPC contractors to be eligible to determine the ratio based on actual records, if available.

Additionally, percentage of value of goods involved in EPC to be increased from 70% based on the actual industry estimate which is 90:10 for goods and services. In this regard, it may also be noted that the Solar Power Developers Association has filed a petition with the Delhi High Court challenging the 70:30 ratio for solar power projects.

- Circular no 46/20/2018 dated July 6, 2018 issued by CBIC stated that RE Scrips would be charged to tax at the rate of 12%. However, industry stance is that such scrips are in the nature of 'securities' which are excluded from the ambit of goods as well as services under the GST regime. Further, these scrips are freely traded on power exchanges and were electricity derivatives.

Recommendation

RE Scrips should be exempted from the levy of GST since, these certificates are purchased by the power project owners to comply with environmental norms and the certificates are derivatives based on the power generated in green route. It may be noted that the Delhi High Court has issued notice to the Revenue challenging the aforesaid Circular.

- At present, coal imports are subject to BCD of 2.5% and Integrated-GST (IGST) of 5%. Since there is shortage of domestic coal in India, power plants are compelled to meet the requirement through imports. Since there is no duty on electricity on the output side, any duty imposed on procurement of coal would be a cost for power companies. The present duty structure is unintentionally increasing the cost of power generation and thereby increasing the cost of power, which is directly impacting the common man

Recommendations:

It is recommended that BCD and IGST on coal imported for the usage in thermal power plants should be NIL. Without prejudice to the above, IGST @5% on coal shall be reduced to 2% to bring it in line with levy of countervailing duty being levied on the same goods under erstwhile indirect tax regime

- Coal supply including import is subject to a levy of compensation cess of INR400 per tonne under the GST regime. Compensation cess is creditable against output compensation cess and not against output GST. Thus, compensation cess coupled with tax cost on inputs have led to an exceptional rise in costs for the power project owners (with no output compensation cess or GST liability). Burden of these exorbitant costs are ultimately to be borne by the end customers.

Recommendation

The GoI should consider reduction/exemption from levy of compensation cess on coal procured by power project owners and incidentally control the rising prices

- Cement, which is a vital consumable in hydro power projects is leviable to GST at the rate of 28%. This has a glaring impact on the cost of power produced from hydro power projects due to input GST being non-creditable

Recommendations:

It is recommended that the rate of tax for cement used in hydro power projects be reduced. Alternatively, GoI may also allow refund of taxes paid on inputs used in generating power.

3.11 Miscellaneous recommendations

Contractual issues

- There are no proper provisions relating to claims of the contractor in case of delays or unforeseen measures attributable to the owner. Unlike most global tendering norms practised (ADB, WB, FIDIC, FMO, KFW), Indian utilities do not provide any monetary recourse to the contractor in case of delays in payments and time overruns due to the owner's default. Under such a scenario, the contractor does not receive any monetary compensation for which it has mobilised equipment and manpower. This puts a financial burden on the contractor and ultimately leads to further project delays.

Monetary compensation to the contractor owing to owner's delays should be premeditated by Indian utilities prior to release of tenders.

- Parent company clause in case of hydro-mechanical projects (in cases where credentials of Indian subsidiary are not sufficient to bid) - Until last year, the hydro-mechanical sector was addressed primarily by Indian companies which had a major market share amongst a few foreign companies. Such Indian companies would usually meet the pre-qualifying criteria for any forthcoming tenders in India. In the case of foreign companies, who have forayed in the Indian market recently, it is extremely difficult for them to qualify in similar tenders in the absence of a parent clause. The parent clause is specifically used to enable a locally set-up manufacturing company to pre-qualify based on global credentials and references of its parent company.

  It is therefore suggested that project owners (mainly government/state owned) must provision parent company clause for all companies to participate on a level playing basis for hydro-mechanical tenders as is provisioned for electro-mechanical works.

- The limitation of liability (LOL) clause in most tenders floated by GoI project owners is ambiguous in its entirety. Internationally practised tender conditions include a liability capping of 100% of the contract value on the contractor. In the case of most tenders floated in India, the LOL remains uncapped or includes consequential damages, unforeseen damages and at times even damages by third party.

  The LOL of a contractor should be clearly defined and capped at the value of the contract value without any deemed or unforeseen damages which are not covered under the scope of the contractor in the contractual provisions.

Implementation issues

- There is a mismatch of gestation period of RE sources mainly from solar and wind from setting ussp transmission lines:
  - Gestation for transmission line varies from 3-4 years while for solar and wind projects, it is around 12-18 months.
  - Even if the plant is ready it cannot either dispatch power or else it forced to back down due to inadequate capacity of transmission available.

  Therefore, there is need for upgradation of grid infrastructure to evacuate power from renewable sources.

- Recommendations to improve energy access in India:
  - Encourage development of mini-grids where extension of grid is not a viable solution.
  - Government/research organisations should examine on making rural appliances more energy-efficient.
  - Prepaid metering for rural households; legalising unauthorised electricity connections.

Legal issues

- Arbitration clause should be provisioned in tenders floated by state utilities and dispute resolution mechanism should be time bound to avoid delays in the project.
- Disposal of Appeals/Petitions takes around 2-3 years in Regulatory Commissions. Therefore, creation of additional bench may be considered for faster disposal and early resolution of cases.

CONCLUSION

Arguably, the power sector has witnessed reasonable progress both in terms of policy evolution as well as capacity addition; the sector has certainly tremendous potential for accelerated growth, given the GoI's macro-economic objectives of achieving rapid infrastructure development, increasing urbanisation and rural electrification.

The progressive policy-level changes and effective implementation of directives by the GoI have been well appreciated by the industry and investors. RE achieving grid parity after introducing competitive bidding, improvement in financial of Discoms, coal linkage policy, are select key initiatives amongst various incentives introduced by the GoI that have fared well with the investors. Besides, the GoI's unstinted commitment to scaling up power generation using non-fossil fuel resources, reducing carbon footprints, and ensuring 24X7 power for all, will enable this sector gain more investments in medium to long run.

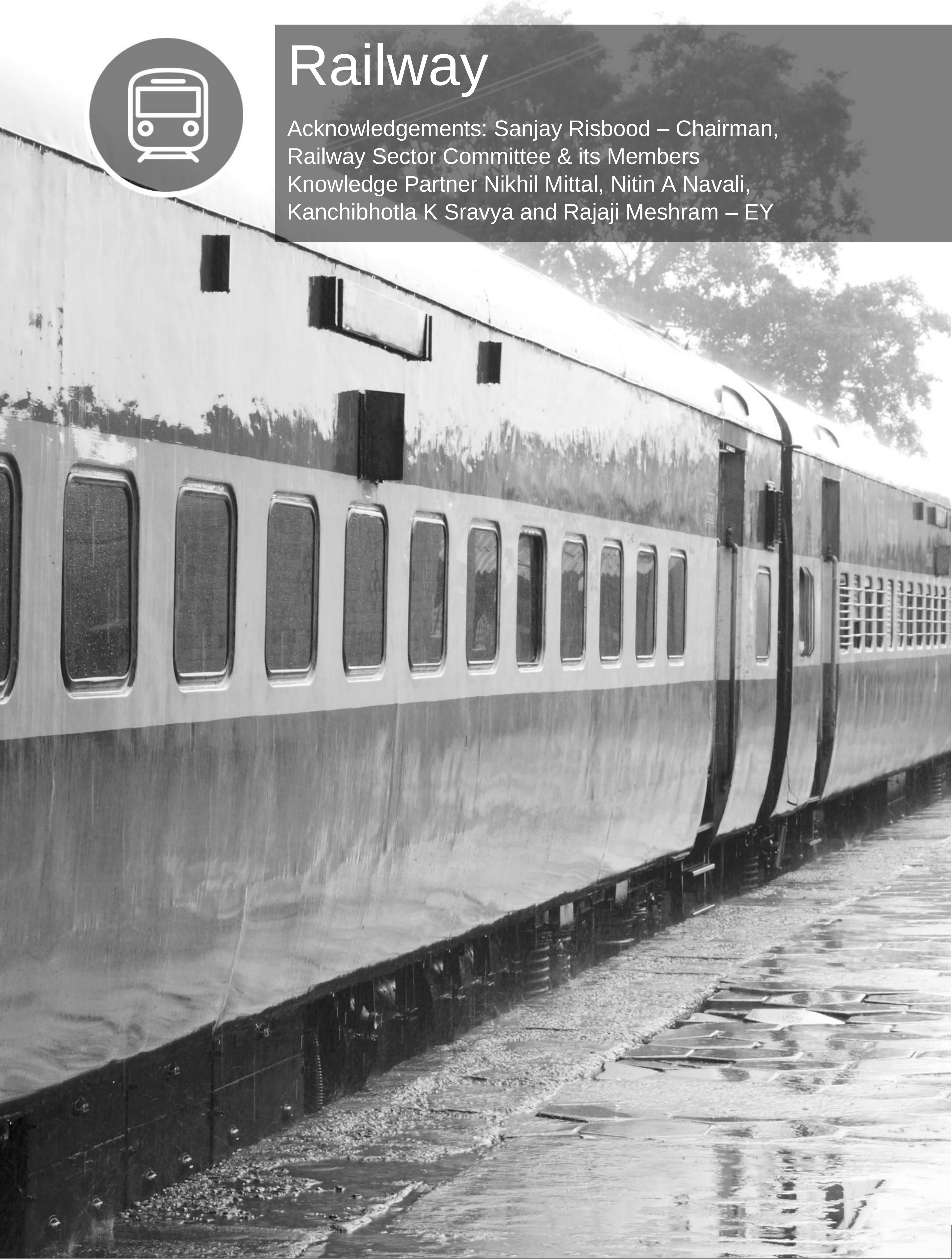
To further incentivise large scale investments in electricity generation projects as well as transmission infrastructures, it is imperatives that the GoI pays heed to concerns of the industry as highlighted in this paper, and responds in a timely manner. Amongst wish-list identified, resolution of GST stalemate for ‘electricity’ will be an important tax policy reform that the industry is hoping to witness in the coming year.

ENDNOTE

1. World Bank
2. Source: Indian Economic Survey FY2019
3. Except few households in LWE affected Bastar region of Chhattisgarh
4. Central Electricity Authority (CEA) monthly report March 2019
5. India follows April-March. FY2012-2017 mean period from 1 April 2012 to 31 March 2017
6. Draft National s Plan
7. Source: NEP 2018
8. CEA: All India installed capacity April 2019 monthly report
9. Source: CEA Executive Summary Reports
10. Source: CEA Installed capacity report, March 2019
11. Department of Industrial Policy & Promotion, India: FDI quarterly factsheet January 2019 to March 2019
12. BP Statistical Review of World Energy 2018
13. CEA: Growth of Electricity sector in India from 1947-2018
14. Source: CEA Power Supply Position March, 2019
15. CEA monthly executive summary reports
16. Growth of Electricity sector in India from 1947-2018, CEA
17. Source: National Ujala Dashboard, as on 17th March 2020
18. Under section 80-IA of the IT Act
19. FVCI investments are regulated by the RBI and SEBI pursuant to relevant regulations issued in this regard.

Railway

Acknowledgements: Sanjay Risbood – Chairman, Railway Sector Committee & its Members
Knowledge Partner Nikhil Mittal, Nitin A Navali, Kanchibhotla K Sravya and Rajaji Meshram – EY



INTRODUCTION

Indian Railways (IR) is a Central Public sector Enterprise that manages the railway network in India. This is the fourth-largest network in the world in size, with route length of 67,415[1] kms. In 2017, it became the world's largest commercial enterprise based on the number of employees, providing employment to about 1.2 million1 people. Today, it carries close to 1.2 billion tonnes of freight and serves over 8.4 billion passengers annually[1]. With the extensive rail network spanning across the length and breadth of India, IR is commonly titled as "Lifeline of the nation".

In the last few decades, with significant improvement in highways, road infrastructure and rapid expansion of aviation, IR has been experiencing competition from alternative modes. This has reduced the traffic share on rail in both segments, viz. freight and passenger.

Adoption of reliable and high-quality railway infrastructure in terms of tracks, capacity augmentation, latest signalling technologies, safety, etc. could prove to be pivotal in shifting the modal share back in favour of the railways.

The Government of India (GoI) has been keen on transforming the railways into a growth engine for the nation. This is being reflected in the form of several transformative measures taken up by IR. Such measures include introduction of new trains (for instance Train 18), electrification of lines, dedicated freight corridors, station redevelopment, etc.

Initiatives by IR

Dedicated Freight Corridors

In India, a majority of the rail freight traffic flows through select corridors (Mumbai – Delhi – Kolkata – Chennai) commonly known as the Golden Quadrilateral (GQ). They cover about 15% of route length but cater to almost 58% of freight traffic[2]. GQ is shown in the adjacent picture.

In the first phase, DFCCIL (an SPV for execution of DFCs) is constructing two corridors – the Western DFC (WDFC) and Eastern DFC (EDFC) – spanning a total length of about 3,360 route km. The project has been estimated at a cost of INR 81,459 crore . The overall financial progress of this project is about 66% up to November 2019[3].

WDFC begins from Dadri in Uttar Pradesh and terminates at JNPT in Maharashtra, passing through Haryana, Rajasthan and Gujarat. The WDFC would have feeder routes serving large Gujarat ports of Mundra, Kandla, Pipavav, Dahej and Hazira. EDFC runs from Ludhiana in Punjab to Dankuni in West Bengal, passing through Haryana, Uttar Pradesh, Bihar and Jharkhand. The EDFC would have feeder routes to different coal mines and thermal power plants. Overall physical progress of the project is 68.5% up to November 2019[3].

High Speed Rail (HSR)

IR is keen on catching up with international railways in terms of train speeds. Average speed of existing passenger and freight trains on IR is far lower than those in leading international railways.

High speed rail programme was introduced with a vision of raising the speed of regular passenger trains to 250-350 kmph on segregated routes, which will bring about a major transformation in train travel[4]. High Speed Rail Corporation of India Ltd (HSRC) was set in 2013 to identify routes for development of such high-speed corridors. In 2016, National High-Speed Rail Corporation Limited (NHSRCL) was incorporated as a Special Purpose Vehicle (SPV) to implement the HSR projects. Currently NHSRCL is implementing the Mumbai – Ahmedabad HSR project.

Private participation in passenger trains

One of the recent initiatives by IR to improve user experience in railways is privatisation of passenger trains. IR aims to attract private players to invest and operate passenger trains on certain clusters of routes.

As part of this programme, private players would be entitled to finance, procure, operate and maintain rakes. Access to rail infrastructure such as track and signalling network, depots and concierge services would be provided to private players by IR based on payment of fixed access charges.

It is expected that with this programme, IR would be able to augment the passenger capacity. Also, passengers would get access to a world-class rail travel experience.

Electrification

For providing an economical, environment-friendly, safe and reliable mode of transportation, electrification of railways has been identified as one of the key focus areas by the GoI[5].

The operating ratio of IR has been deteriorating and reached as high as 98% during 2018-19. About 30% of IR's total cost accounts for fuel expenditure[6]. With electrification of the routes, IR aims to significantly reduce this expenditure.

Targeting to reduce operational costs and making railways an environment-friendly mode of travel, IR is keen to complete 100% electrification of all its broad gauge (BG) routes by year 2021-22[7].

Station redevelopment

There are 7,321 stations on IR network[7]. Out of these, IR selected various stations under its station redevelopment programme. The two focus areas of the programme are:

- Improving passenger experience at stations
- Generating non-fare box revenue

Habibganj Railway station in Bhopal, Madhya Pradesh is the first station that is being developed under the redevelopment programme through PPP.

Key Issues and Recommendations

Procurement

IR procures goods and services from several vendors. There are a total of about 1.25 lakh vendors registered on the Indian Railway E-Procurement System (IREPS) portal. Procurement is done on a Least Cost Selection (LCS) method. In this method, there is generally a minimum technical qualification criterion which the supplier(s) must satisfy in order to be eligible for financial bid evaluation. There is no additional incentive/ advantage for companies which have qualifications higher than the minimum technical qualification criterion. This potentially leads to selection of a supplier which may not have the best/ highest technical qualification.

Adopting a quality-cost-based selection (QCBS) method will incorporate a ranking/scoring mechanism for technical qualification and financial quotes. This way the suppliers will have an additional incentive of scoring higher marks for having higher quality. This shall potentially ensure participation from more technically competent players with global footprint.

Many countries use a QCBS system for their evaluations. For example, SNCF (Société nationale des chemins de fer français, French national rail company) adopts an award criterion[8] for selecting suppliers. For instance, as per the award criterion for supply, installation and delivery of a transit system for the Technicentre of Tergnier of SNCF Mobilities, 45% weightage is given to financial quotes, 35% weightage is given to technical qualifications and 20% weightage is given to Corporate Social Responsibility criteria. Per these criteria, the contract will be awarded to most economically advantageous offer. For another tender related to regeneration works for the fences and access gates of LGV SEE high speed line[9], award criteria was 70% weightage to technical qualifications and 30% to financial quotes.

IR may consider adopting a similar system (especially in high value tenders) wherein the weightages are assigned for technical competence and financial quotes.

Taxation

GoI introduced Goods & Services Tax (GST) replacing the multiple indirect taxes in 2017. It has five different slabs for different goods/services, 0%, 5%, 12%, 18% and 28%. There have been some issues related to GST which have been cited by companies in railways sector.

One of the issues is the inverted duty structure which companies face. This occurs when the tax paid on inputs (parts, raw materials) is higher than the outputs (final product, assembled product). For example, various parts of a locomotive come under different GST slabs varying from 5% to 18%. But GST on the final locomotive was 5%. On October 01, 2019, Central Board of Indirect Taxes and Customs (CBIC) revised the GST on railway goods under the head 8607 from 5% to 12%[10].

Even after the above-mentioned revision, there may exist a difference between input and output tax (input tax credit (ITC)). As per Notification No. 05/2017 – Integrated Tax (Rate) dated 28.06.2017, the ITC is not claimable (refund is not allowed) for railway goods[11]. As a result, suppliers generally increase the cost of final product to compensate the loss owing to non-refund of ITC thereby reducing their competitiveness. IR may consider coordinating with CBIC and making ITC claimable.

Financing

IR has been considering multiple funding options to implement projects including high speed trains, rolling stock procurement, station development, signalling and infrastructure development. One such funding option is loans from multilateral organisations such as ADB, World Bank, European Investment Bank (EIB) and Japan International Cooperation Agency (JICA).

There are mandatory conditions stipulated by select multilateral lenders that are to be followed for availing the loans from them. Such conditions limit the participation of several interested parties who are willing to invest and participate in large infrastructure projects in IR.

One such scenario can be observed in the case of loans from JICA. JICA provides a soft loan at low interest rates and periods extending up to 50 years with a moratorium of 15 years. This model of funding comes under Special Terms of Economic

Partnership (STEP) loan. The condition set under STEP loan is that the contractor for the funded project needs to be either (i) Japanese company or (ii) a Japanese company in a joint venture with an Indian counterpart as a lead partner or a (iii) a subsidiary of Japanese company in India. Such condition automatically restricts the participation of interested competitive players from around the world.

On the other hand, there exist multilateral lenders such as EIB[12], KFW[13] which consider contractors for works and services regardless of the country of origin.

IR may consider waiving off conditions like the ones stipulated under STEP loan thereby allowing firms from around the world to participate in large-scale projects. This would open opportunities for various interested parties which are willing to work with IR thereby resulting into a much more competitive environment of procurement for IR.

Adoption of new technologies

It is expected that technology is going to be the growth driver in railways in times to come. IR is looking forward to providing a world-class experience to its customers by embracing technological advancements. This is essential for IR to keep pace with the changing times and competition from alternative modes such as road and air. IR has been conducting trials/ test runs of advanced technologies present in both domestic and international markets.

IR follows the standards and specifications so set out and approved by Research Designs & Standards Organisation (RDSO) for adopting newer technology and products. These standards are distinct from the ones set by International Union of Railways (UIC). For adoption of new technology/products for commercial use, RDSO approval is mandatory. Such approval process is reported to be time consuming. This hinders the faster implementation of international technologies into IR.

In a knowledge paper prepared by CII & EY titled "RAILway – driver of India's growth story" – October 2019, a study was conducted which included collation of inputs from various leaders in railway manufacturing industry. It was identified from this study that, 'Homologation and difficulty in obtaining RDSO approvals' was ranked as the highest external risk for growth of railway manufacturing sector in India.

IR may consider making the process of cross approvals simpler for implementation of technologies which may be new to IR but successfully operational elsewhere. This is because such technologies have already been subject to trials/tests by standard international organisations.

The way forward

Infrastructure investment in IR drive the domestic railway manufacturing and construction industry in India. Adhoc changes in announced plans can have significant consequences on the industry.

There is a need for IR to increase the horizon of its planning and commit itself for a long term and a stable vision. A process of framing and adhering to a long-term investment plan needs to be formulated.

The vision to transform IR will require extensive development, testing and acceptance of new railway technologies. With the upgradation of technology moving at a brisk pace, the approval and adoption processes undertaken by RDSO will have to be made more efficient in order to increase IR's responsiveness to the market.

With foresight on a long-term vision and faster adoption of latest technologies, IR has true potential of transforming itself into a world class service provider.

ENDNOTE

1. http://www.indianrailways.gov.in/railwayboard/uploads/directorate/stat_econ/Year_Book/Year%20Book%202018-19-English.pdf
2. https://pib.gov.in/PressReleasePage.aspx?PRID=1514320
3. http://www.dfccil.com/Home/ProgressStatusImage
4. http://www.indianrailways.gov.in/railwayboard/uploads/directorate/infra/downloads/VISION_2020_Eng_SUBMITTED_TO_PARLIAMENT.pdf
5. https://core.indianrailways.gov.in/print_section.jsp?lang=0&id=0,294,302,532
6. http://www.indianrailways.gov.in/Mission_41K.pdf
7. http://www.indianrailways.gov.in/railwayboard/uploads/directorate/stat_econ/Year_Book/Year%20Book%202018-19-English.pdf
8. https://sncf.bravosolution.com/esop/toolkit/opportunity/opportunityDetail.do?opportunityId=2296&oppList=PAST
9. https://sncf.bravosolution.com/esop/toolkit/opportunity/opportunityDetail.do?opportunityId=2482&oppList=CURRENT#fh
10. http://www.indianrailways.gov.in/railwayboard/uploads/directorate/stores/downloads/circular/2019/RS(G)_Chapter_86_GST_28112019.pdf
11. http://gstcouncil.gov.in/sites/default/files/NOTIFICATION%20PDF/Notification%20for%20restriction%20of%20ITC%20IGST-5.pdf
12. https://www.eib.org/attachments/strategies/guide_to_procurement_en.pdf
13. https://www.kfw-entwicklungsbank.de/PDF/Download-Center/PDF-Dokumente-Richtlinien/Vergaberichtlinien-2019-Englisch-Internet_2.pdf

NOTE

Retail

Acknowledgements: Pavithra Anand (Decathlon India) – Chairperson, Retail Sector Committee & its Members
Knowledge Partner: Gaurav Karnik and Rounak Chawla – EY

EXECUTIVE SUMMARY

India is one of the fastest-growing economies globally and the fourth-largest retail market in the world. Over the past decade, there has been a significant change in consumer attitudes especially the increasing use of online shopping and sharp rise in population in the 20 to 49 years age band. Thus, the Indian retail market is set on the growth path both horizontally and vertically.

However, the COVID-19 pandemic has hit the retail market hard and shattered hopes of the economy recovery in near future. Not only the demand side but also the supply side has been disrupted by COVID-19 crisis and needs utmost attention and remedial action.

Last year, the current government spelt out its key priorities, which were focused on laying the foundation for making India a US$5 trillion economy by FY2024. Accordingly, the government has been consistently making efforts to liberalise and boost investments in the retail sector. Nevertheless, given the downfall in the retail sector owing to the pandemic, there is a dire need for bringing in certain essential changes in the legal and regulatory framework for fuelling growth in retail sector and also promote the 'Make in India' initiative.

KEY ISSUES AND RECOMMENDATIONS

1. STABLE AND PREDICTABLE POLICY FOR INDIAN RETAIL SECTOR

1.1 Implementation of National Retail Policy

A stable and reliable policy and business regime is a precondition for continued long term investment in any market. In the absence of predictable and stable policy regime, it's difficult for global companies to do business in India and plan long-term investments and expansion plans continuity.

Therefore, in order to create conducive environment for retail trade including by simplifying rules and regulations hindering the growth of retail sector, the government should implement a National Retail Trade Policy immediately which shall include promoting ease of doing business, licensing, access to funds, direct selling, and hyper-market related matters.

1.2 Industry status should be granted to organised retail sector of India

The retail sector faces difficulties in procuring organised financing and fiscal incentives. In order to reform the Indian retail sector, the government should grant industry status to the organised retail sector with a clear articulated policy framework and attempt to ensure a single, national retail sector policy. This will not only make the sector attractive for global investments by ensuring availability of organised financing and fiscal incentives but also make assist in regulating the retail sector.

1.3 Regulate the hike in custom duty

Many global companies seek to keep their costs low across their supply chain in order to offer affordable products. Since 2017, there has been constant increase in custom duties on various goods which has adversely impacted the expansion and investment plans of global companies in India. As a Result, prices of products will increase and the same may not be affordable for customers. Though, such duty hike will promote the 'Make in India' initiative, however, it may hamper future investment from global companies. Further, there is large dependency on imports of raw/semi-finished/finished material/products which cannot be curtailed overnight and would require companies to re-engineer the supply chain gradually to shift to local sourcing/manufacturing. Thus, it is recommended to review the custom duty hike and keep up the openness of Indian economy. This will go a long way in making India competitive to do business and make products affordable to the consumer.

1.4 Provision of adequate time limit for applicability of tax rate amendment notifications

In case of change in rate of taxes, it is made applicable with effect from the date when the notification is published in official gazette which is generally the next day of such decision. However, practically it becomes challenging to make changes in the IT system and the process takes about 2-3 days. Therefore, it is recommended that the applicability of rate change notifications should be made effective after couple of days after the notification is published in the official gazette.

2. REDUCING COST OF DOING BUSINESS IN INDIA

2.1 Pre-conditions to re-labelling and re-packaging

Legal Metrology Act require commodities to be sold with labels containing prescribed declarations only. Further, it casts responsibility on manufacturer/packer /importer to re-pack/re-label as and when required. For a multi-national operating in various countries, it can become challenging to ensure compliance with different labelling requirement in different countries, particularly when, goods concerned are imported than manufactured locally. Given the dynamics of logistics and e-commerce industry, goods are seldom required to be packed/re-packed. Given the complexities involved in fulfilling the conditions for relabelling, it is recommended to streamline the entire process by removing the requirement of relabelling for repacking.

2.2 Revision of laws related to declarations to be made on products

The intent of the declarations is to impart awareness amongst the customers and ensure transparency. However, in the past decade, there has been significant increase in overall consumer awareness along with evolution of new and effective manufacturing and sourcing supply chains models. Additionally, in respect to luxurious goods, declarations such as MRP etc., may not be relevant, given the market such goods targets. However, the extant provisions of the Legal Metrology Act prescribe excessive declaration requirements along with grouping together at one place all the pre-printed information. Such requirements are not economically feasible as it requires changing the supply chain for a single market on stand-alone basis. Moreover, the prohibition on re-labelling of goods at a place other than the bonded warehouse/factory, creates practical difficulties for the importer /manufacturer, especially where the label containing the declaration gets damaged during transit or storage, resulting in penalties being imposed by authorities. Thus, an objective-based impact assessment exercise should be undertaken on labelling regulations so that onerous statutory requirements can be done away with. This will reduce the undue burden on stakeholders and help in reducing costs.

2.3 Relaxation of labelling norms to allow it in non-bonded warehouses along with removing ambiguity between DGFT CBIC norms

Currently imported goods are only required to be labelled before they are cleared for home consumption. Currently, importers are either resorting to labelling in the CFS or in Public /Private Bonded warehouses. MRP labelling is a procedural requirement to ensure compliance to the Legal Metrology Regulations before release for retail sale. Large volume importers face challenge in labelling in public bonded warehouse as there is no infrastructure available to handle the labelling and repacking in a good way. This results in importers having to set up Private Bonded warehouse, which is an additional cost of operations. This also has a direct bearing on the work at customs as importers need to maintain bonds /registers with customs. It also means double the volume of Bills of Entry handled by the officers (2 bills of entry required Into Bond and Ex-Bond). It is recommended that Single Brand Retailers (who are Accredited economic operators (AEO) importers) should be allowed clearance under Home Consumption Bill of Entry and permission to label the goods in their warehouse (warehouses which are already registered with legal metrology)/store before the articles are put up for retail sale. Also, importers warehouse may be subjected to periodic audits to verify the process to secure labelling is done before placing the goods in the stores for sale.

CBIC has provided certain relaxation for importers of AEO-T2 and above category including affixation of MRP label at their premises. However, there is a gap between the provisions of Legal Metrology (Packaged Commodities) Rules, 2011 (LMPC) read with Import Export Policy, 2017 (IEP) which states that the importer either undertakes labelling in bonded warehouse or directs the foreign supplier to affix labels at its end. Both the options create operational difficulties for adherence. Further, with the mismatch in the guideline issued by CBIC v/s the LMPC read with IEP makes the relaxation otiose. In order to pave a clear path for importers and avoid any possible litigations in future, the DGFT should correct this missing link by issuing suitable policy/circular expressly providing this relaxation in line with CBIC's guideline.

2.4 FDI laws for single brand retail to be simplified

I. Multiple brands of same group should be considered as SBRT rather than MBRT under FDI policy

With the booming global economies, a multinational typically owns and operates in multiple brands to target different segment of consumers. Extant FDI policy considers trading by a company of multiple brands of same product as MBRT. In such cases, in order to promote FDI in retail trading sector, it is recommended that trading in multiple brands owned by the same group should be permitted to receive FDI in terms of extant SBRT guidelines rather than MBRT subject to maintaining separate books of account for each brand. This will also provide consumers with more choices under one roof and better experience.

II. Mandatory display of umbrella brand alongside sub-brand to be removed

Though SBRT norms permit marketing sub-brands in Indian stores, however, it mandates display of umbrella brand clearly alongside the 'sub-brand'. This leads to lower attractiveness of consumers to the sub-brand along with development of separate branding elements that are otherwise not made, resulting in increased costs, inconsistency and inefficiency. It is recommended to ease such norms and registration of the sub-brand under the umbrella brand sssin terms of intellectual property laws should be deemed to satisfy said requirement.

3. Promoting ease of doing business in India

3.1 Decriminalisation of offences under Legal Metrology Act

Currently, under the Legal Metrology Act violation of provisions can result in a criminal liability which may attract imprisonment. The inherent subjectivity in the provisions and the discretionary powers given to the field officials makes the industry vulnerable to misuse of these powers and invocation of criminal liability even for the slightest/technical offence. It is requested that the Government replace the criminal liabilities with penalties/fines for technical violations akin to steps taken under other regulations, such as the Companies Act, 2013, wherein it has replaced criminal liability with penalty in case of a default, thus enhancing ease of doing business.

3.2 Numerous regulations in relation to labelling requirements

To promote ease of doing business, the India regulatory authorities should work towards compilation of various laws governing the sector specific labelling requirement into single law. Further, focus should be on permitting modern ways of labelling in line with the global standards. This will not only increase consumer's trust in the product but also help companies to avoid unnecessary modifications in labels for catering to Indian market. Also, keeping in mind the volume of counterfeit products, having modern and new technology in labelling would help in curbing production and distribution of such forged products and boost consumer's confidence in the retail brand.

3.3 Focus on reducing prolonged litigations under the Legal Metrology Act

The Legal Metrology Act intends to cover the declarations on 'Pre-Packaged commodities' only. However, ambiguity exists as to what products can be classified as 'pre-packaged commodities', which has resulted into host of litigation. It is therefore recommended that appropriate clarification should be brought to the definition of the term 'pre-packaged commodities' to ensure redressal of pending litigations and provide clarity to the manufactures/importers on compliance requirements.

3.4 Securing stability for imports:

a) **Leverage AEO (Accredited Economic Operator) importers responsibility with respect validity of samples tested**: AEO certified importers are expected to adhere to self-compliance management at a higher level, in comparison to non-certified importers. In the current regime, the importer can be asked to provide a continuity bond so that the goods can be released to the market only after the NOC against local testing or any other requirement is received. The testing/NOCs should be limited to exceptional cases only and not subject all articles. Further, for Single Brand Retail Traders who are AEO importers, government may consider relaxing the testing norms so that the test results for such goods can be deemed to be valid for a period of 6-12 months.

b) **Review Regulations with a risk-based approach:** There are several regulations that impact the import of goods into the country and need approval from Participating Government Agency (PGA) for No Objection Certificate (NOC) before the goods are released from the customs. This involves physical examination, sampling, testing etc., which causes delay in the customs clearance process and the dwell time at the ports

c) **Review Customs Compliance Requirements (CCR) and instructions to the officers in ICEGATE:** The Customs officers and trade are guided on the compliance requirements/verification through the CCR comments in the system. These sometime lead to confusion and unwanted delays on account of it.

Therefore it is recommended that clearance from customs is based on self-certification for Single Brand Retailers (which are AEO importers) subject to submission of evidence/specifications for the articles being imported under relevant tariff codes and allow test results to be valid for a period of 6-12 months for release of same article without testing.

3.5 Faster resolution of IP infringement matters

Enforcement mechanism of IP laws in the Country is not so effective and efficient, which is giving rise to IPR infringement matters. This is hurting the business sentiments and ease of doing business in the Country.

A long time taken for enforcement of IP challenges. While fakes are being sold on websites rampantly, it is next to impossible to shut down the rogue sites leading to many consumers being duped into buying fake products.

Government should put the vigilance machinery in right motion to unearth IPR infringement matters and effective and efficient enforcement of IP laws for faster disposal of those matters

3.6 Outdated national requirements should be modernised

We propose that outdated national requirements for testing, certification and declaration of conformity should be either modernised or abolished. Test requirements specific for India hinder business. One example fumigation process prescribed for wood-based articles to ensure that the shipment is free from bugs. There are environmentally not friendly methods. The products come with global standards and compliance, then the need for such testing is obsolete. European companies as per production guidelines require that manufacturers are compliant with green/eco-wood treatment methods like Heat treatment and Kiln-Drying as per IPPC norms. These are either done in-house at suppliers or at the raw material source (timber/lumber suppliers).

Hence the Indian Revised PQ regulation amendments of 2018 requiring NPPO issued certificates for converted/carpentry products puts us in very difficult situation, given that each exporting country have their own procedures and limitations for PQ/NPPO intervention. It is requested that the Treatment Certificate issued by global suppliers be accepted and further if it mandates for random physical examination; companies are more than willing to support the official system and consciously contribute towards securing and safeguarding India's flora and fauna.

Further, another area of concern is new standards for certain goods imported in India. Wherever globally accepted international ISO standards are available, these should be harmonised into the BIS standards to avoid redundancy and create trade barriers. Emphasis needs to go into creating the infrastructure to work more on enforcement and monitoring adherence rather than limited to creation of new standards and certifications. Multiplicity of different regulatory bodies makes implementation a tough ask and a bane that needs to be dispensed with. There is additional benefit being derived by having separate quality certification of products already meeting international quality control norms which represent state-of-the-art methods. Requiring conformance to a domestic standard that may deviate from global norms set by bodies such as ISO and IEC creates confusion by introducing inconsistent requirements and has the increased cost, compliance burden and delays to consume goods or sell them in market. Accordingly, it is demanded that Indian authorities may either place reliance on international standards or must accept the tests carried out in foreign accredited laboratories attesting compliance with Indian standards. This will help in removing difficulties faced at the time of import of goods.

3.7 Animal Quarantine NOC Relaxation

It must be noted that there are specific tariff headings 94049011 and 94049091 for articles filled with "Feathers or down" which actually fall under the purview of AQ NOC process. However, the current customs EDI system seeks NOC from the AQ authorities even on non-Animal Origin articles. Though the importer has been importing and getting these articles tested for more than a year and there was not a single case of Animal Origin article in their range. Yet, each import is subjected to this additional process which results in additional handling and damages to the product and each of these articles is destroyed as the department rips the product to check the filling. A fast track approval for large importer or allow companies in AEO tier -1, that are already tested and certified by accredited laboratories, or approved by authorities, would be a big step when it comes to ease of doing business for international retailers. We recommend that based on the past import records, future imports should not be subjected to AQ NOC. One-year import history can be considered or once in a year testing locally should be valid for the whole year.

3.8 Single Window clearance

Starting a business in India requires considerable time as compared to most developed nations across the globe. The procedures to secure permits are rather cumbersome and involve permission to be sought from various departments.

Under Atmanirbhar Yojana 2020, the Government has recently streamlined the processes such as granting of permits and clearance, self-certification and third-party certification etc. Further, measures relating to easy registration of property, fast disposal of commercial disputes and simpler tax regime are under consideration for making India one of the easiest places to do business. It is recommended that a single window clearance for all licenses and approvals be introduced for retailers to ease and accelerate the pace of doing business in India.

3.9 Maximum Retail Pricing

In 2019, the Indian Government notified industry that all domestic or foreign single brand retailers could be exempt from the Maximum Retail Pricing (MRP) labelling requirement for one year on packaged products in retail stores. For single brand retailers MRP-marking does not offer any additional consumer protection. Single brand retailers control their own supply chain and sell their own products through robust sales mechanisms and transparent price communication at all sales channels in an integrated manner. This permission expired on 31st July 2020 and is only valid for physical stores. Given the magnitude of global companies' operations and supply-chain cycle involved, they are making huge investment in ensuring full compliance to all points mentioned in rule relaxation order. To optimise and showcase that this pricing methodology works well and is transparently enjoyed by the many customers, we request government to allow Single brand retailers long-term (at least five-year) extension to this relaxation for both offline and online sales format or channels.

3.10 Clarification on anti-profiteering norms

The Anti-Profiteering clause in the GST law provides for passing on the input tax credit or reduction in rate of tax benefit to the consumer. However, there is ambiguity whether the benefit needs to be seen at company level or product level. Thus, it is recommended that clear methodology and procedure be laid down to avoid ambiguities and litigation.

3.11 Distribution of credit by Input Service Distributor ('ISD') in the same month

The current CGST Rules provides for the distribution of input tax credit available for distribution in a month to be distributed in the same month. However, there does not appear to be any apparent reason for restricting the time within which credit should be distributed. Therefore, it is recommended that a reasonable time limit should be allowed for distribution of GST credit similar to provision in Cenvat credit rules.

3.12 Relaxation of particulars on GST tax invoice to avail input tax credit

As per section 16 of CGST Act, one of the conditions for availing input tax credit is that the recipient should be in possession of tax invoice or debit note. Further, if tax invoice/debit note does not contain all the particulars as required under the rules, then input tax credit of recipient may be subject to litigation. In this regard, reference is drawn to proviso to Rule 9(2) of erstwhile CENVAT Credit Rules, 2004, which provided for admissibility of credit on the basis of the document containing certain specified details. Therefore, it is recommended that section 16 of the CGST act should be amended in order to provide that credit can be availed on the basis of a document that even though does not contain all the particulars prescribed under CGST Rules, but contains certain specified critical details, such as details of tax amount; and name, address and GSTIN of the supplier and recipient/distributor of credit and recipient of credit.

3.13 Input tax credit on free samples, marketing material etc.

In terms of the current provisions of the GST Law(s), input tax credit is admissible on the inputs used for business but is restricted on the goods disposed-off by way of gift or free samples. Further, in the retail sector, the business scenario is as such that many inputs are distributed for promotion or for marketing activities. Therefore, there is a very thin line of difference as to whether the same shall be considered to be in the course of business. Therefore, it is recommended that clarity is provided whether credit shall be admissible on such inputs or not.

3.14 Sales return to be eased

According to the GST law, returned goods necessarily should go to the destination from where goods were delivered originally. However, in case of multi-channel retailers it implies that goods returned by customer should be returned to central/regional warehouse which in most cases are across various states. The cost for such transportation is substantially high and many a times even higher than the actual value of the returned product. Thus, it is recommended to ease the provisions of the GST law(s) with respect to linking of the credit notes in relation to return of such goods to the original invoice against which the same were sold. Further, the return of such goods should be allowed to a different GSTIN obtained under the same PAN.

3.15 Incentivise retail industry and clearing of pending litigations under the Income Tax Act

It is recommended to amend/introduce the following direct tax provisions:

a. Recently, the tax rates for corporates were reduced to 15% (for new manufacturing companies) and 22% (for others) subject to certain conditions. Though, the reduced tax regime allows for deduction u/s 80JJAA of the Income Tax Act, 1961, however the emolument threshold should be increased from INR 25,000 to INR 40,000 per month for additional employee.

b. Clarification regarding characterisation and taxability of advertising, marketing and promotion (AMP) expenses required to end the long pending litigations.

2.5 Clear guidelines for taxation of online transactions, new TCS and TDS provisions

a. Equalisation levy: Recently government introduced equalisation levy (EL) of 2% on turnover of non-resident e-commerce operators (EOP) from any sale of goods, provisions of services or facilitating e-commerce supply/service to Indian customers or non-residents (under specified circumstances), effective from 1 April 2020. Further, e-commerce operator is defined as a person who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both. Clarifications regarding the scope of levy and definition of online sale of goods/service, what comprises digital platform/electronic facility, etc., should be provided to avoid confusion and litigation at later stage. The provisions should also be made akin to the digital taxation regime being implemented in other nations like UK, Spain, Italy, France, etc. Also, the mismatch in the exemption provisions under income tax law should be cleared by the authorities and remove the ambiguity.

b. Issue clarification related to implementation challenges for tax collection at source (TCS) on sale of goods:

Finance Act 2020 introduced new TCS provisions for sale of goods to be collected by seller from the buyer where the sale is more than INR 50 lakh in a particular year. Such levy has posed unnecessary compliance burden on the retail sellers along with additional investment in upgrading the systems to monitor the TCS levy and collection. This levy has not only increased the complexity in doing day-to-day business but also increased scope of litigation in future. It is requested that Government may consider increasing the threshold for such levy and exclude B2B transactions for which payment is collected vide banking modes (Cheque, NEFT, RTGS, ECS, UPI, etc.). This will help ease the burden on the retailers and they can focus on reviving their businesses. Further, with the thrust being on “receipts” rather than on raising invoices, it has put more pressure on companies to focus on cash basis of accounting for this TCS levy rather than following accrual/mercantile basis. Thus, adding to overall complexities in implementing the new law.

c. TDS under section 194-O by e-commerce operators (EOPs) on payments made to e-commerce participants

Government always proposes to boost the e-commerce industry and facilitate the logistics and ease of doing business. However, introduction of such new provision poses humongous compliance burden on the EOPs and impacts the cash flow in hands of e-commerce participants/sellers. This has put the industry to rethink on the business growth. Further, the provisions need to be clarified on various fronts for which many representations have been filed with CBDT.

Accordingly, given the need of the retail industry to revive its business amidst Covid-19 setback, it is requested if the Government may defer such provisions and issue necessary clarifications.

CONCLUSION

The current economic setback seeks immediate action by regulators coupled with coping to modern ways of working. The retail sector shows tremendous growth potential. However, it needs significant support to overcome the obstacles to meet requirements of huge population and high domestic consumption as stated in above points.

Crucial points for Indian Government to consider are:

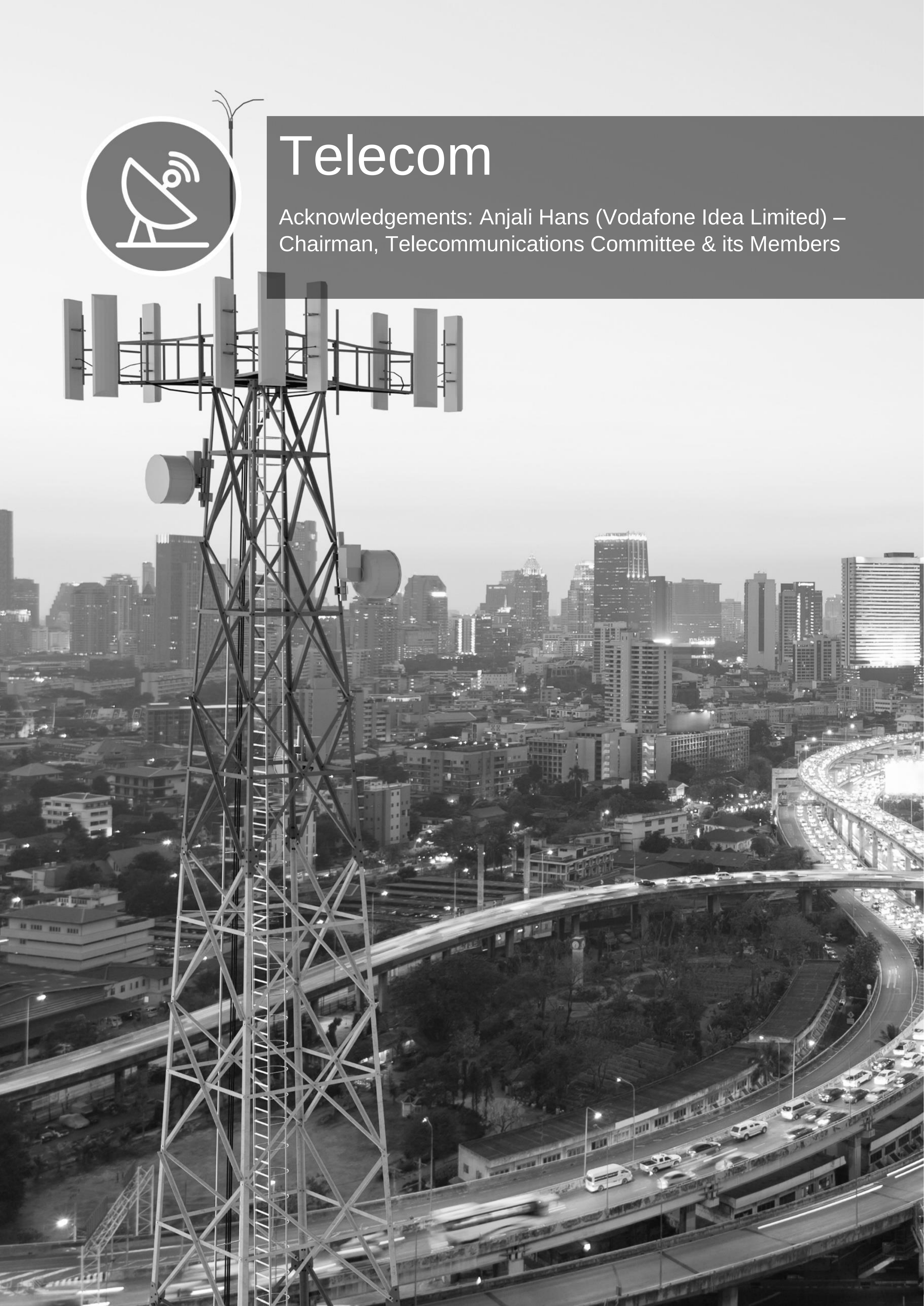
1. Decriminalisation of offences under the Legal Metrology Act
2. Rationalising and revisiting the labelling laws along with compilation of multiple laws
3. Promote the ease of doing business in India through use of self-certification and AEO registration for simplifying customs processes.
4. Clarification regarding availability of input tax credit under GST law on free samples, marketing material etc.
5. Clarification regarding taxation of online transactions (Equalisation levy) and new provisions related to TCS and TDS on certain transactions

We anticipate for a brighter future with implementation of the recommendations proposed in the position paper.

NOTE

Telecom

Acknowledgements: Anjali Hans (Vodafone Idea Limited) – Chairman, Telecommunications Committee & its Members



EXECUTIVE SUMMARY

The year gone by has been a tumultuous one for the industry. While the growth in mobile telephony has brought in unprecedented opportunities and reconditioned the way businesses and citizens functioned, the industry continued to be under severe financial stress, which was further aggravated by the judgment of the Hon'ble Supreme Court on the Definition of Adjusted Gross Revenues (AGR).

The financial stress has not only impacted the operators, but also the government in terms of reduced revenues to the exchequer bysss way of license fees and spectrum usage charges.

However despite all constraints and challenges, the industry put in a stellar performance in maintaining its networks and connectivity during the ongoing pandemic, despite a sharp multi-fold increase in data traffic. During the period, the role of digital connectivity has come to the forefront as the digital ecosystem collaborated to ensure that businesses and the personal connectivity needs of citizens continued to be met in these difficult times.

Some supportive measures were also initiated by the government. Recognising the stress in the sector, a Committee of Secretaries was set up in October end 2019, and based on its recommendations, the government extended the option of a two-year moratorium on spectrum instalment dues. Further, while the government filed an application in the Hon'ble Supreme Court seeking a 20 year staggered payment schedule for payment of AGR dues, the Hon'ble Supreme Court, in its order dated 2 September 2020 allowed only a period of 10 years.

The Regulator, TRAI, after carrying out a Consultation, deferred the Bill & Keep regime by one year. Also, TRAI has completed consultation on the review of International termination charges and notified that the rate of ITC shall be kept under forbearance within a prescribed range of Re. 0.35 per minute to Re. 0.65 per minute. While TRAI has initiated a review of telecom tariffs in December 2019, the consultation is yet to be completed.

On Implementation of the National Digital Communication Policy 2018 (NDCP-2018), work has been initiated on several of the strategies outlined in NDCP 2018 – such as formulation of a broadband readiness index, regulatory consultations on unified numbering for fixed and mobile services, unbundling of network, enhancing the scope of infrastructure providers, etc. However, implementation of the key strategies relating to financial health such as reviewing the AGR definition, principle of input line credit, regulatory levies, customs duties, etc. – all measures to restore financial health and attract investments into the sector by the government is yet to be initiated. Expeditious and time bound implementation of the NDCP financial health strategies should a first and foremost requirement.

Telecom, it is well recognised has a multiplier impact on GDP and economic growth. Growth in telecom creates a positive impact, however, the flip side is also true, de-growth will have a negative multiplier and cascading effect.

Going forward, government needs to address the cost structure of the sector by reducing the burden of regulatory levies and also rationalising the definition of AGR to be such as is fair, rational, proportionate and based on world best practices.

Indian Telecom pays around 29% to 32% of its revenues to exchequer in the form of levies and taxes like License fees [including Universal service Obligation (USO) levy], Spectrum Usage Charges (SUC), etc. and is one of the most heavily taxed sectors when compared to taxes, levies and surcharges levied on telecom service providers in South Asia and ASEAN countries. Given the current stress in sector, the accumulated funds of over INR50,000 crores in the USO Fund, the recovery of market price of spectrum through auctions, there is a strong case for License Fee be reduced to 3% and SUC by 3%.

EBG Federation strongly believes that restoration of the financial health of the sector is of prime importance for the sector to be able to grow and contribute to the development of a ubiquitous and robust digital eco-system designed to meet India's digital objectives. The huge investments that are required in this sector will also come once the sector is healthy and robust.

Moving to the other developments in the sector, the 5G trials are still awaited. The 5G auctions have been deferred and it is likely that the next round of auctions will only be for 4G spectrum. While the auction may take place sometime this year or early next year, the response to the same is likely to be muted, in part, no doubt due to the aftermath of the AGR judgment.

The revised Data Protection Bill whilst diluting the restrictions on cross border data flows, continues to have several restrictive or onerous provisions such as elaborate notice requirements, high penalties, etc. Further, the provision empowering government to exempt any agency of government from the purview of the Act can lead to abuse of power. The Bill creates category of data fiduciaries called "social media intermediaries", which creates an important distinction between mere conduits [such as ISPs] and hosting service providers. The data protection bill is a very important legislative instrument in this increasingly data driven economy. EBG Federation believes that the bill must balance the need for privacy and data protection with the need to fuel and facilitate innovation. A decision on data localisation should be taken only after a cost benefit analysis – balancing business and security concerns. Data localisation should be permitted only for valid security reasons, which should be narrowly defined. The penalty provisions should be reasonable and proportionate and should be based on the harm caused. The data protection and privacy norms should be applied consistently across telecom service providers and OTT communication service providers.

The draft intermediary guidelines shared by the government for consultation, apart from lacking procedural safeguards in several cases, also creates an impractical, onerous and untenable burden by requiring intermediaries to undertake proactive identification, monitoring and filtering of content through automated tools as a pre-requisite to be able to claim exemption from liability. EBG Federation urges that it is important to ensure that the intermediary Guidelines are in line with international norms and strike a careful balance between the rights and obligations of users and intermediaries, promoting and upholding Internet freedom while putting in place appropriate safeguards for the privacy and security of users.

The phased approach adopted by the government for mandatory in-country testing, whilst more practical than the earlier approach, still carries concerns with regard to duplication of efforts and costs and delays in approvals. EBG Federation believes that there is a need to have testing infrastructure fully in place before any large-scale mandate for in-country testing is imposed.

The industry has seen various challenges in implementation of Phase 1 and 2 of DoT's Mandatory Testing and Certification of Telecommunication Equipment (MTCTE) scheme and DoT will need to provide adequate timeline, address discrepancies and concerns of the OEMs and start accepting international test reports going forward. Regular government-industry stakeholder consultations is a must for future success of such testing and certification schemes.

Other issues that continue to subsist include GST related issues. The accumulated input credit of over INR35,000 crores places a great strain on cash flows and needs to be addressed on a priority basis. EBG Federation suggests that as a first step, going forward the imposition of GST on regulatory levies including spectrum payments needs to be done away with. This would be in line with international practices. Furthermore EBG Federation believes that provision must be there for refund of the accumulated input credit as is also the case internationally. At the very least, the GST credit should be allowed to be adjusted or used as a collateral against loans from banks and financial institutions.

The hike in customs duties have only raised the burden on telecom operators and created a distorted market where in cases of Free Trade Agreement (FTA) countries, equipment is brought in at zero duty creating a non-level playing field. EBG Federation urges that customs duties on these products should be brought down to Nil considering the essential nature of these imports to meet the national vision of Digital India and for level playing field for all vendors and operators. Most telecom OEMs, including Nokia and Ericsson, are already manufacturing in India and increase in duties has not resulted in attracting any new global investment in the country.

For local manufacturing, EBG Federation suggests that DoT urgently a) plans an incentive scheme for telecom equipment manufacturers along the lines of PLI scheme by MEITY and b) undertakes extensive industry consultation to make sure every manufacturer in India (both Indian and Global) qualifies for PMI incentives provided by Government of India.

A future fit framework is the need of the hour which should look at lessening the regulatory burden on telecom rather than imposing stringent rules on the OTT players. A future fit regime would be one that is simple and light touch, encompasses all communication services, is technology neutral, encourages innovation and investments and embodies a commitment to address legacy issues.

On the regulatory front, TRAI made a number of recommendations through 2019, notably on Review of Terms & Conditions for OSPs [21.10.2019], Allotment of Spectrum to Indian Railways for Public Safety and Security services [25.10.2019], reforming the Guidelines for Transfer/Merger of Telecom Licenses [21.02.2020], enhancement of scope of infrastructure providers [13.03.2020] and Cloud Services [14.09.2020].

EBG Federation welcomes the TRAI recommendations to reform OSP guidelines and believe that the recommendations are forward looking and have the potential to bring about the required ease of doing business, regulatory certainty and reforms in the outsourcing sector including IT/ITES KPOs/BPOs as well as enterprise sector as a whole. The recommendations have the potential of opening new business opportunities for the telecom service providers and unlock the immense potential of all the stakeholders to become a Digital and Knowledge economy and help in job creation and providing a roadmap to steer the prestigious Skill and Start up India initiatives of our government. EBG Federation urges that the recommendations may be accepted by DoT at the earliest and the guidelines for Other Service Provider (OSP) be suitably amended to incorporate the TRAI recommendations.

In respect of Cloud Services while TRAI has recommended terms and conditions of the registration of industry body, eligibility, entry fee, period of registration, and governance structure, etc., EBG Federation believes that it is desirable to continue with a light touch approach given the role of Cloud services in fostering innovation and accelerating growth.

TRAI also responded to back reference received from the DoT on its recommendations on Auction of Spectrum [08.07.2019] and on 'Licensing framework for Audio Conferencing/Audiotex/Voice Mail Services' [24.12.2019]. On auction of spectrum EBG Federation believes that not only price, but access to spectrum is equally important. Just like for any operator to be relevant in 4G, access to 4G spectrum is a pre-requisite, so will be the case for 5G which will be the dominant technology for the next 10 years. Access to adequate 5G spectrum must be ensured for all operators to remain relevant in the market. EBG Federation recommends that the government allocates sufficient 5G spectrum in low, mid and high (mm waves) bands including E-V bands for microwave backhaul.

TRAI also initiated various telecom related consultations, some of which were of interest to the group, viz. Traffic Management Practices (TMPs) and Multi-Stakeholder Body for Net Neutrality. [02/01/2020], Tariff Issues of Telecom Services [17/12/], Review of Interconnection Usage Charges [08/11/2019] Cloud Services [23/10/2019], Developing a unified numbering plan for fixed line and mobile services [20/09/2019], Reforming the Guidelines for Transfer | Merger of Telecom Licenses [19/09/2019], Duration of alert for the called party [16/09/2019] and most recently 'Provision of Cellular backhaul connectivity via Satellite through VSAT under Commercial VSAT CUG Service Authorisation [29/01/2020].

On tariffs, EBG Federation believes that the current market conditions warrant an intervention by the Regulator to step in and prescribe a floor price for telecom services. This will enable operators to make the heavy investments that are required by the sector for network expansion, technology upgradation, greater fiberisation and ever-increasing appetite for data usage and quality of service for consumers.

As regards traffic management, EBG Federation believes that a self-regulatory approach would be far more desirable and may be preferred over a prescriptive approach that may end up hampering the flexibility of service providers in managing their traffic and ensuring quality of experience for their customers.

TRAI also issued a Pre-Consultation Paper on "Enabling Unbundling of Different Layers through Differential Licensing [09/12/2019]. On this subject, EBG Federation supports continuation with the unified licensing approach but urges for radical reforms to ensure that the regime is future fit and light touch.

1. KEY MARKET TRENDS

The growth in mobile telephony over the last decade, brought in unprecedented opportunities, and reconditioned the way businesses and citizens functioned. The Telecom Service Providers (TSPs) have played a central role in ushering in this mobile revolution and spurring rapid digitisation.

Between 2014 and 2019, the overall subscribers in India increased to 1,205 million (with 98% mobile subscription), increasing at 5% CAGR. The number of landline subscribers declined at 5.3% annually, while mobile subscribers increased at 5.5% CAGR.

India is now the world's second-largest telecommunications market, with around 1178 million subscribers at the end of March 2020 with wireless market segment accounting for 98.28% of the total subscriber base. Urban subscribers accounted for 55% of the wireless subscriber base and 89% of the wireline subscribers. Rural subscribers accounted for 45% of wireless subscribers and only 11% of wireline subscribers, showing that the main form of connectivity in rural areas is through wireless.

India is also the second largest country in terms of internet subscribers. The internet user base in India has crossed 500 million mark and reached 743 million by end March 2020.

India became the world’s fastest-growing market for mobile applications in the first quarter of 2018.

Total wireless data usage in India grew from 15850 million GB for QE March 2019 to 23,403 million GB in QE March 2020, an increase of almost 50%. As of end March 2020, Indians were using data at an average of 11 GB per month. The number of internet and broadband subscribers in the country increased from 636.73 million and 563.31 million in QE March 2019 to reach 743.19 million and 687.44 million respectively in QE March 2020, showing an increase of 17% and 22%.

The contribution of 3G and 4G data usage in total volume of wireless data usage are about 3.49% and 95.83% respectively during the QE March 2020. Share of 2G data usage was only 0.67% during the quarter.

The NDCP-2018 envisages attracting investments worth US$100 billion in the telecommunications sector by 2022 and enhancing the contribution of the Digital Communications sector from ~ 6% of India's GDP in 2017 to 8% by 2022

Foreign Direct Investment (FDI) cap in the telecom sector has been increased to 100% from 74%, wherein up to 49% is allowed through automatic route and beyond 49% under the government route. FDI inflows into the telecom sector between April 2000 and June 2019 totalled US$37.05 billion as per DPIIT, with US$18.7 billion coming between 2015 and 2019.

Gross Revenue and Adjusted Gross Revenue of the telecom sector increased from INR58,414 crores and INR35,932 crores in QE March 2019 to INR67,534 crores and INR44,940 crores respectively for QE March 2020.

India's telecommunications market is expected to experience further growth, fuelled by increased growth in data and data based services revenues and higher penetration in rural market.

Revenues from the telecom equipment sector are expected to grow to US$ 26.38 billion by 2020. The number of internet subscribers in the country is expected to double by 2021 to 829 million and overall IP traffic is expected to grow four-fold at a CAGR of 30% by 2021. The Indian government is planning to develop 100 smart city projects, where IoT would play a vital role in development of those cities. The Indian Mobile Value-Added Services (MVAS) industry is expected to grow at a CAGR of 18.3% during the forecast period 2015–2020 and reach US$23.8 billion by 2020. App downloads in India are expected to increase to 37.21 billion by FY2022.

As per the Ericsson Mobility Report June 2020, LTE subscriptions in India are forecast to increase from 550 million in 2019 to 820 million in 2025, increasing at a compound annual growth rate (CAGR) of 7 percent. LTE remains the dominant technology, accounting for 49 percent of mobile subscriptions in 2019. LTE will continue to be dominant, representing 64 percent of mobile subscriptions in 2025. 5G will represent around 18 percent of mobile subscriptions in India at the end of 2025. Mobile broadband technologies accounted for 58 percent of mobile subscriptions in 2019, and this figure is predicted to reach 82 percent by 2025. The total number of mobile broadband subscriptions is set to exceed 1 billion by 2025. The number of smartphone subscriptions has increased to 620 million in 2019 and is expected to grow at a CAGR of 9 percent, reaching 1 billion by 2025

Around 410 million additional smartphone users are expected in India by 2025 In the India region, the average monthly mobile data usage per smartphone continues to show robust growth, boosted by the rapid adoption of 4G. Low prices for mobile broadband services, affordable smartphones, and people's changing video-viewing habits have continued to drive monthly usage growth. Only 4 percent of households have fixed broadband, making smartphones the only way to access the internet in many cases.2 Total traffic is projected to triple, reaching 21EB per month in 2025. This comes from two factors: high growth in the number of smartphone users, including growth in rural areas, and an increase in average usage per smartphone. Even if the traffic per existing smartphone user continues to grow significantly over time, the increase in average traffic per smartphone is expected to moderate as more consumers in India acquire smartphones. The average traffic per smartphone is expected to increase to around 25GB per month in 2025.

On the market front, the year has been a mixed bag – with consumers enjoying unlimited voice and data services at unbelievably low prices, whilst the operators for most part were struggling under severe financial stress due to a combination of lowering their tariffs and investing heavily in 4G in order to compete in the market.

A summary snapshot of the telecom industry is given below:

	Unit	Q.E. 31-Mar-2019	Q.E. 30-Jun-2019	Q.E. 30-Sep-2019	Q.E- 31 Dec-2019	Q.E. 31 Mar-2020
Telecom Subscribers (Wireless + Wireline)						
Total Subscribers	Million	1,183.51	1,186.63	1,195.24	1,172.44	1,177.97
% change over the previous quarter		-0.79%	0.26%	0.73%	-1.91%	0.47%
Urban Subscribers	Million	669.16	675.58	677.95	662.45	656.46
Rural Subscribers	Million	514.35	511.05	517.29	509.99	521.51
Market share of Private Operators		88.71%	88.75%	88.81%	88.55%	88.54%
Market share of PSU Operators		11.29%	11.25%	11.19%	11.45%	11.46%
Tele density		90.11	90.11	90.52	88.56	87.37
Urban Tele density		159.96	160.78	160.63	156.26	142.31
Rural Tele density		57.47	56.99	57.59	56.67	58.79
Wireless Subscribers						
Total Wireless Subscribers	Million	1,161.81	1,165.46	1,173.75	1,151.44	1,157.75
% change over the previous quarter		-1.21%	0.31%	0.71%	-1.90%	0.55%
Urban Subscribers	Million	650.49	657.27	659.18	643.97	638.48
Rural Subscribers	Million	511.32	508.19	514.56	507.46	519.27
Market share of Private Operators		89.74%	89.73%	89.74%	89.45%	89.36%
Market share of PSU Operators		10.26%	10.27%	10.26%	10.55%	10.64%
Tele density		88.46	88.5	88.9	86.98	85.87
Urban Tele density		155.49	156.42	156.18	151.90	138.41
Rural Tele density		57.13	56.68	57.28	56.39	58.54
Total Wireless Data Usage during quarter	Million GB	15,850	17,940	19839	21,402	23,403
Internet/Broadband Subscribers						
Total Internet Subscribers	Million	636.73	665.31	687.62	718.74	743.19
% change over previous quarter		5.38%	4.49%	3.35%	4.53%	3.40%
Narrowband subscribers		73.42	70.72	62.20	56.81	55.75
Broadband subscribers	Million	563.31	594.38	625.42	661.94	687.44
Internet/Broadband Subscribers						
Wired Internet Subscribers		21.68	21.67	22.26	22.39	22.42
Wireless Internet Subscribers	Million	615.05	643.64	665.37	696.36	720.78
Urban Internet Subscribers	Million	409.72	427.05	439.99	450.31	457.23

	Unit	Q.E. 31-Mar-2019	Q.E. 30-Jun-2019	Q.E. 30-Sep-2019	Q.E- 31 Dec-2019	Q.E. 31 Mar-2020
Rural Internet Subscribers	Million	227.01	238.26	247.63	268.43	285.97
Telecom Financial Data						
Gross Revenue (GR) during quarter	INR Cr	58,414	61,535	59,992	63764.14	`67,533.74
% change in GR over previous quarter		-0.98%	5.34%	-2.51%	6.29%	5.91%
Adjusted Gross Revenue (AGR) during Qtr	INR Cr	35,932	39,124	37,338	40877.46	44,940.32
% change in AGR over previous Qtr		-0.34%	8.88%	-4.56%	9.48%	9.94%
Share of PSUs in Access AGR		9.57%	10.49%	7.88%	8%	7.91%
Monthly Average Revenue Per User (ARPU) for Access Services	INR	72.49	80.65	78.17	85.07	97.64
Revenue & Usage Parameters						
Monthly ARPU of Wireless Service (GSM+CDMA+LTE)	INR	71.39	74.30	74.38	78.65	91.49
Minutes of Usage (MOU) per subscriber per month - Wireless Service (GSM+CDMA+LTE)	Minutes	692	701	691	712	750
Total Outgoing Minutes of Usage for Internet Telephony	Million	197	198.34	197.09	181.34	181.34
Wireless Data Usage						
Average Wireless Data Usage per wireless data subscriber per month	GB	9.06	9.77	10.37	10.40	11
Average cost to subscriber per GB wireless data during the quarter	INR	7.95	7.77	6.98	8,45	11.23

Telecom services are a “raw material” for the rest of the economy – one which acts as a productivity-enhancer and multiplier for all sectors of the economy, more so with new technologies driving rapid digitalisation and increased digital penetration. A robust ecosystem of TSPs is also essential for some of the key nation building initiatives of the Government of India.

It is thus important for India to have a healthy and a vibrant telecom sector both because of the opportunities for investments, growth and employment that the sector itself presents and also, it’s potential as an enabler of competitiveness in the economy and higher and inclusive growth

2. KEY DEVELOPMENTS IN 2019 AND EBG FEDERATION POSITION/RECOMMENDATIONS

A. Financial Stress in the Sector

The Indian telecom sector has been facing severe financial stress since 2016 resulting in a sharp decline of almost 40% in the revenues of the sector, coupled with an unsustainably high debt level of around INR7 lakh crores, the bulk of which is on account of spectrum liabilities. This has resulted in the exit of about 5-6 operators from the sector in the last three years alone.

The judgment of the Hon’ble Supreme Court on Definition of Adjusted Gross Revenues (AGR) in October 2019 has further aggravated the issue, and brought the telecom sector on the brink of an unprecedented financial crisis. The government recognising the implications of this judgment on the sector, filed an application in the Hon’ble Supreme Court seeking a 20 year period be allowed to the operators to pay their AGR dues. The Hon’ble Court however allowed only 10 years directing that there will be no re-assessment of the amounts due and that 10% of the total dues are to be paid by 31.03.2021 and then payment in yearly instalments commencing from 1.4.2021 up to 31.3.2031 payable by 31 March of every succeeding financial year.

The Supreme Court directive that there will be no reassessment of amounts due will deprive industry of the opportunity to even seek correction of computational errors, which will be against all principles of equity and fairness. The government needs to support the right of the licensees to seek correction of computational errors. Further, in case of operators who have already paid 10% or more of the dues, the next payment is due only by 31 March 2022.

Going forward, government needs to address the cost structure of the sector by reducing the burden of regulatory levies and also rationalising the definition of AGR to be such as is fair, rational, proportionate and based on world best practices.

Indian Telecom pays around 29% to 32% of its revenues to exchequer in the form of levies & taxes like License fees [including USO levy], SUC, etc. The sector is one of the most heavily taxed sectors when compared to taxes, levies and surcharges levied on telecom service providers in South Asia and ASEAN countries.

Given the current stress in sector, and the accumulated funds of over INR50,000 crores in the USO Fund there is a strong case for License Fee be reduced to 3%.

The review of regulatory levies as also the AGR definition are also provided for in NDCP-2018 and the same must be implemented expeditiously.

EBG Federation Position: Restoration of the financial health of the sector is of prime importance for the sector to be able to grow and contribute to the development of a ubiquitous and robust digital eco-system designed to meet India’s digital objectives. The huge investments that are required in this sector will also come once the sector is healthy and robust.

B. Goods & Service Tax Regime

The introduction of the Goods Services Tax (GST) Regime, from 1 July 2017 has brought along with it several challenges for the telecom sector, both in terms of complex compliances as also added costs.

The requirement for a GST Registration in each State /Circle versus a centralised Service Tax registration earlier, has significantly increased the costs of compliance. Further, GST for telecom has been set at the higher slab of 18% whereas the Service Tax earlier was 15%. This is also inconsistent with the GST approach adopted for handsets, where GST has been set at 12%. A legacy challenge that has carried through from the previous regime, has been the imposition of Service Tax [and now GST] on regulatory levies as also on payments for auctioned spectrum. The levy of GST on spectrum as well as on the License Fee and spectrum usage charge payments has not only led to a double tax burden on the sector, but because of the present financial circumstances of the sector, has resulted in enormous amount of blockage of input credit to the tune of over INR 350bn.

Internationally, VAT/GST is not applicable to government services as they are considered as ‘out of scope’ or regarded as non-economic activity or sovereign functions which are outside the ambit of tax. It is pertinent to note that the European Court of Justice has held in June 2007[1] that no VAT is payable on the 3G spectrum awarded by the regulatory authority as it should not be regarded as an economic activity.

As regards the accumulated GST credit, there are examples both with India and globally.

Under the erstwhile Value Added Tax (VAT) legislations, several states such as Maharashtra, Karnataka, Kerala, Madhya Pradesh, etc., allowed registered persons to claim refund of input tax credit lying unutilised after certain period of time (as stipulated under respective state laws).

For example, as per Maharashtra Value Added Tax Act, 2002 read with Maharashtra Value Added Tax Rules, 2005 CMVAT Rules), registered dealers could claim refund of unutilised input tax credit lying at the end of the financial year. Relevant extract of Rule 55 of MVAT Rules which provided for refund of unutilised input VAT credit is outlined below:

"(3Xa) Where a dealer has filed a return in respect of any period contained in a year, then he may, subject to the other provisions of these rules, adjust the aggregate of

(i) any payment made in respect of the said period before filing of the said return,

(v) deposit paid towards voluntary registration.

(b) If after making adjustment, if any, as provided in clause (a), there be any excess, then the dealer may claim refund of the excess or part of excess in accordance with the rules, or carry forward the same for adjustment towards the tax payable as *per the returns to be filed for any subsequent period contained in the said year under the Maharashtra Value Added Tax Act, 2002* , *the Central* Sales *Tax Act, 1956 or the Maharashtra Tax on the Entry of Goods into Local Areas Act, 2003."*

Similarly, section 11(6) of Kerala Value Added Tax Act, 2003 (Kerala VAT Act) read with Rule 47 A of the Kerala Value Added Tax Rules, 2005 also contains similar refund provisions which provided for refund of unutilised input VAT credit at the end of the financial year. Relevant extract of Section 11(6) of Kerala VAT Act is outlined below

> *"Provided that where the excess input tax* so *carried forward cannot be fully adjusted during the last return period of that year, the excess input tax credit* so *remaining unadjusted shall be refunded to the dealer* as *if it were a refund accrued under section 13."*

Similarly, provisions for refund of unutilised credit was part of the VAT Acts of other States such as Madhya Pradesh, Karnataka, etc.

Even internationally, there exist provisions allowing refund of unutilised input tax credit such as in European Union and Singapore.

Article 18 of the Sixth VAT Directive [Article 183 of the Recast Directive[2]] in the European Union specifically states as below:

> *Article 18*
>
> *….*
>
> *4. Where for a given tax period the amount of authorised deductions exceed the amount of tax due, the Member States may either make a refund or carry the excess forward to the following period according to conditions which they shall determine.*
>
> *However, Member States may refuse to refund or carry forward if the amount of the excess is insignificant.*

Even Singapore GST allows refund if the GST paid on purchases/expenses during a return period exceeds the GST on output liability. Such refund is granted immediately on filing the periodic return.

At the very least, the GST credit should be allowed to be adjusted or used as a collateral against loans from banks and financial institutions.

EBG Federation believes that there is a need to urgently review the levy of a GST on government levies. EBG Federation suggests that as a first step, going forward the imposition of GST on regulatory levies including spectrum payments needs to be done away with. This would be in line with international practices. EBG Federation submits that the same can be done by issuing exemption notifications as per provisions stipulated under the GST Act. Furthermore, EBG Federation believes that provision must be there for refund of the accumulated input credit as is also the case internationally. At the very least, the GST credit should be allowed to be adjusted or used as a collateral against loans from banks and financial institutions.

C. Personal Data Protection Bill

A revised version of the Personal Data Protection Bill was released in December 2019. The Bill has been referred to a Joint Parliamentary Committee (JPC) under the chairpersonship of Mrs. Meenakshi Lekhi, Hon'ble Member of Parliament. The JPC is presently conducting consultations in the matter and is likely to submit its recommendations to the government by the end of the Budget Session.

A key goal of the National Digital Communications Policy 2018 is to establish a comprehensive data protection regime for digital communications that safeguards the privacy, autonomy and choice of individuals and facilitates India's effective participation in the global digital economy

The preamble to the Bill also enunciates the need for this balance to create a collective culture that fosters a free and fair digital economy, respecting the informational privacy of individuals, and ensuring empowerment, progress and innovation through digital governance and inclusion.

Some suggested modifications in the revised Bill include:

- Under the Bill, sensitive personal data can only be transferred on the basis of explicit consent and other requirements. Critical personal data can only be transferred abroad for emergency processing or pursuant to an 'adequacy' decision. In both cases, the circumstances described to permit cross-border data transfer are too restrictive, and could amount to a de-facto data localisation mandate. The classification /categorisation as critical personal data should be closely linked to national security. This will avoid unintended stringent data localisation. Further, a decision on data localisation should be taken only after a cost benefit analysis – balancing business & security concerns. Data localisation should be permitted only for valid security reasons, which should be narrowly defined.
- The inclusion of inferred or derived data within the ambit of the Bill is concerning, inasmuch as it broadens the scope of the data protection framework significantly in comparison to other regulations. This may be reviewed and reference to inferred data be dropped.
- Anonymised/pseudonymised data sets do not constitute personally identifiable information and should therefore be kept outside the scope of this bill
- The powers of the central government to exempt any government agency from the Act is should be balanced with provision for due process and safeguards to prevent abuse.
- The power of the Central government to direct a company to share with it anonymised or non-personal data if so required needs to be with suitable checks and balances else it could undermine the freedom of companies to operate in India and their ability/incentives to develop innovative data analytics services.
- The penalties continue to be very harsh even in the revised Bill. EBG Federation believes that penalties should be applied in a proportionate manner and only in connection with

the business carried out in India – not worldwide turnover. Also given the nature of technology, it is expected that there may be significant ambiguity around data fiduciaries and processor's obligations under the Act. Hence, a phased approach to penalties should be considered where the DPA can build up a body of precedents and jurisprudence, and where lower fines and penalties may be imposed for some time. Further, the penalties should be only civil not criminal.

- The earlier draft had mentioned 18 months for implementation, which has been removed in present version. Given the need to draft guidance and to set up the new Indian DP Authority, there is a need for providing at least 24 months for implementation. The EU GDPR period was 24 months and was very challenging especially for smaller organisations.

EBG Federation believes that a robust privacy and data protection framework is a must in a data driven digital economy. EBG Federation believes that Data Protection Bill should balances the need for security and to facilitate innovation. A decision on data localisation should be taken only after a cost benefit analysis – balancing business & security concerns. Data localisation should be permitted only for valid security reasons, which should be narrowly defined. EBG Federation believes that the penalty provisions should be reasonable and proportionate and should be based on the harm caused. The data protection and privacy norms should be applied consistently across telecom service providers and OTT communication service providers.

D. Intermediary Guidelines

Towards the end of 2018, MEITY issued a draft of "The Information Technology [Intermediary Guidelines (Amendment) Rules] 2018" seeking to amend the Information Technology (Intermediary Guidelines) Rules, 2011 ("Intermediary Guidelines") under the Information Technology Act, 2000. There are several concerns on the draft guidelines, as illustrated below:

- The requirement for intermediaries to inform their users on consequences of their non-compliance every month is an unreasonable and disproportionate burden and could lead to notice fatigue.
- The mandate on an intermediary to proactively trace the originator of the content is onerous and poses multiple challenges e.g. technical challenges as each intermediary would only be able to assist to the extent of the origin of the information at their end, it also undermines security and privacy of communications and is lacking in procedural safeguards.
- The obligation on intermediaries to take down content upon a court order or being notified by the appropriate government or its agency within 24 hours proposes an unreasonable time limit and is lacking in procedural safeguards. Also requiring service providers to preserve content for an undefined period risk imposing new data retention requirements and would increase legal uncertainty and confront companies with new financial, logistical and technical challenges.
- The mandate on intermediaries to undertake proactive identification, monitoring and filtering of content through automated tools, as a pre-requisite for an intermediary to be able to claim exemption from liability is in violation of the fundamental right to privacy, contrary to Supreme Csssourt Ruling, assigns a censorship role to intermediaries, allows blocking orders to be issued without safeguards, is onerous and in violation of international standards.

EBG Federation Position: EBG Federation believes that it is critical that intermediary Guidelines are in line with international norms and strike a careful balance between the rights and obligations of users and intermediaries, promoting and upholding Internet freedom while putting in place appropriate safeguards for the privacy and security of users.

E. Spectrum Auctions

The TRAI submitted its recommendations on Auction of Spectrum in 700 MHz, 800 MHz, 900 MHz, 1800 MHz, 2100 MHz, 2300 MHz, 2500 MHz, 3300-3400 MHz and 3400-3600 MHz Bands on 1 August 2018. On 1 July 2019 DoT referred some recommendations back to TRAI for its reconsideration. TRAI submitted its reconsidered response on 8 July 2019, as below:

- On the DoT view for a more inclusive approach on the pricing of spectrum, TRAI stated that apart from existing licenses additional players could also participate in the process and that the bidder takes into account various factors and thus no guarantee can be given on the sale of all spectrum.
- With regard to 25MHz in the 3300-3600MHz band to be used by ISRO, TRAI reiterated its recommendations that barring the locations where the spectrum is being used by ISRO, it should be made available to TSPs for access services. However, it further stated that in case DoT decides that the same cannot be allocated to TSPs on account of potential interference, DoT may explore earmarking of this spectrum for captive industrial use, for which separate reference may be made to TRAI
- TRAI reduced the minimum block size in 900MHz from 0.6MHz to 0.2MHz on account of the fact that in some service areas, available spectrum was less than 0.6MHz
- TRAI also reduced the block size in 3300-3600MHz from 20MHz to 5MHz blocks to give flexibility and ensure auction & utilization of entire spectrum. It also stated that assignment of the same frequency spot across LSAs should be subject to feasibility.
- TRAI reiterated its recommendation that no rollout obligations should be mandated in the 3300-3600MHz band, but reduced the lock in period from earlier recommended 5 years to 2 years.
- TRAI reiterated its recommendations that there should be an additional cap of 100MHz in the 3300-3600MHz bands apart from extending the overall cap of 35% and cap of 50% on the sub-1 GHz bands to 3300-3600 MHz band also.
- DoT request to review the spectrum valuation and reserve price in view of likely subdued demand, concerns on the financial health of the sector, reduction in number of bidders, etc., was rejected by TRAI and it reiterated its recommendations
- On TRAI recommendation that SUC should be a flat 3% for all auctioned spectrum, TRAI noted that DoT has already conveyed its decision for a weighted average approach.
- Re issues like type of auction, eligibility conditions for participation on auction, payment terms, consultation with RBI/Finance Ministry and validity of spectrum etc., TRAI opined that these are the settled issues. And that in case, DoT feels that any particular issue requires to be examined, a separate reference be made to TRAI.

EBG Federation believes that not only price, but access to spectrum is equally important. Just like for any operator to be relevant in 4G, access to 4G spectrum is a pre-requisite, so will be the case for 5G which will be the dominant technology for the next 10 years. Access to adequate 5G spectrum must be ensured for all operators to remain relevant in the market. EBG Federation recommends that the government allocates sufficient 5G spectrum in low, mid and high (mm waves) bands including E-V bands for microwave backhaul.

F. Terms and Conditions for registration of Other Service Providers (OSPs)

TRAI issued a consultation paper on "Review of Terms and Conditions for registration of Other Service Providers (OSPs) dated 29 March 2019 where it has clearly recognised the vast changes in technologies that has happened in last two decades which has led to evolution of different network architectures, formats and solutions for setting up an OSP network. There is a need for the OSP guidelines to be reformed to make them future proof, open, flexible and technology neutral.

The National Digital Communications Policy 2018 (NDCP-2018) has also envisaged simplifying and facilitating compliance obligations of OSP by improving the terms and conditions for 'Other Service Providers', including definitions, compliance requirements and restrictions on interconnectivity. The relevant clause from NDCP-2018 is given below:

2.1 (c) Simplifying and facilitating Compliance Obligations by:

iv. Improving the Terms and Conditions for 'Other Service Providers', including definitions, compliance requirements and restrictions on interconnectivity.

Based on the multi stakeholders' responses and comments received and open house discussion, TRAI has submitted its recommendations to DoT on 21 October 2019. These recommendations are liberal in nature and have the potential to bring about far reaching reforms in the sector especially job creation in outsourcing sector as well as to provide impetus to the prestigious government programs like skill and start up India.

EBG Federation Position: EBG Federation welcomes the TRAI recommendations to reform OSP guidelines and believe that the recommendations are forward looking and have the potential to bring about the required ease of doing business, regulatory certainty and reforms in the outsourcing sector including IT/ITES.KPOs/BPOs as well as Enterprise sector as a whole. The recommendations have the potential of opening new business opportunities for the telecom service providers and unlock the immense potential of all the stakeholders to become a Digital and Knowledge economy and help in job creation and providing a roadmap to steer the prestigious Skill and Start up India initiatives of our government.

EBG Federation urges that the recommendations may be accepted by DoT at the earliest and the guidelines for Other Service Provider (OSP) be suitably amended to incorporate the TRAI recommendations.

G. Spectrum Allocation to Indian Railways and PPDR Network

TRAI issued a Consultation on 24 June 2019 seeking views of stakeholders on whether spectrum in 700MHz band should be allotted to Indian Railways for Public Safety and Security services how much spectrum, price, methodology of allotments, use of the spectrum to offer on-board internet services, alternative bands that could be used, any other manner in which the IR requirements could be met – e.g. TSP build deploy and maintain the network for IR or a common integrated network (with common spectrum) for Public Safety.

Proposal to allot 700MHz ban to IR must be seen against the context of the fact that 700 MHz is a globally harmonised band being used worldwide for of 4G and 5G services and availability of sufficient spectrum in 700MHz is crucial for achieving the objectives of 'Digital India', also no commercial services should be allowed to be offered by any other entity except licensed players. Also that the 450MHz was being discussed in ITU for possible regional/global spectrum harmonisation for RSTT.

TRAI has subsequently also come out with its recommendation in this regard on 25 October 2019 recommending that 5MHz in the 700 MHz be allocated to Indian Railways on administrative basis for captive use only and not to offer any commercial services such as Wi-Fi on-board; for Video Surveillance System Railways may explore other communications. TRAI also recommended that the 1.6MHz allocated to Railways in 900MHz band be taken back; further that as Railways would be using the 700MHz spectrum along its railway track network and stations only, DoT may explore the possibility of assigning the same spectrum in other areas for area-specific limited use to other entities for captive use, ensuring that there is no interference to the Railways' network from such use.

TRAI's recommendations for Next Generation Public Protection and Disaster Relief (PPDR) communication networks [04-June-2018] are also pending acceptance by DoT. We hope that DoT takes action on these recommendations for creation of a robust and secure PPDR network in the country.

H. Enhancement of Scope of Infrastructure Providers

The TRAI initiated a consultation on Review of Scope of Infrastructure Providers Category-I (IP-I) Registration on 16 August 2019. On 13 March 2020 TRAI submitted its recommendations for enhancement of the scope of Infrastructure Providers, allowing them to own, establish, maintain, and work all such infrastructure items, equipment, and systems required for establishing Wireline or Radio Access Network and Transmission Links as also Right of Way, Duct Space, Optical Fibre, Tower, Feeder cable, Antenna, Base Station, In-Building Solution (IBS), Distributed Antenna System (DAS), etc.

Accordingly the TRAI has also recommended that the IP-I registration holder should be eligible to apply for and get issue of license under the Indian Wireless Telegraphy Act, 1933 to possess such wireless telegraphy apparatus that is permitted under the scope of IP-I Registration.

TRAI has also clearly stated that the enhanced scope will not include core network elements such as Switch, MSC, HLR, IN or assignment of licensed spectrum. Further, that such infrastructure items, equipment and systems or end-to-end bandwidth using transmission systems can be shared only with eligible service providers – who have been defined as Service Provider with a valid authorisation from the government of India to establish, maintain, and work a telegraph to deliver Telecommunication Services.

The infrastructure providers also cannot use the licensed spectrum, assigned to an eligible service provider, for provisioning of wireless Telecommunication Services to other eligible service providers.

Such sharing is to be on mutually agreed terms and conditions.

I. Cloud Services

TRAI issued a Consultation Paper on "Cloud Services" on 23 October 2019. Some of the issued raised in the Paper include need for a Regulatory Framework for Cloud Service providers (CSPs) through an Industry Body and modalities thereof such as registration, membership requirements & fee, Guiding principles for governance, etc.

Over the years, India has witnessed a gradual surge in the adoption of cloud services with the Indian market successfully adopting cloud across sectors including banking and finance, telecom, and public sector.

However, this market in India is still at a nascent stage, any regulation ought to be light touch so as to foster innovation.

The proposal of regulating cloud service providers through an industry body, as mooted by TRAI, is itself a recognition that a light touch approach is warranted. However, the measures suggested in the consultation such as fixing an entry or recurring fee, furnishing of information, laying down a code of conduct, compliance, etc., run contrary to a light touch approach. The Consultation Paper also cites several industry bodies that are promoting innovation in the cloud sector; these bodies have adopted a voluntary governance structure and regulatory framework.

On 14 September 2020, TRAI submitted its recommendations to DoT on Cloud Services, pertaining to the terms and conditions of the registration of industry body, eligibility, entry fee, period of registration, and governance structure, etc.

EBG Federation Position: EBG Federation believes that it is desirable to continue with a light touch approach towards Cloud services given their role in fostering innovation and accelerating growth.

J. International Termination Charges

The TRAI initiated a consultation on International termination charges on 8 November 2019, seeking views on whether there was a need to change in the regulatory regime for International Termination Charges in view of the changes happening in the international telephony market structure and if so, suggestions on the alternate approach.

EBG Federation noted that the TRAI had, in 2018, reduced the International Termination Charges from 53p/minute to 30p/minute on the rationale that such decease would curb the grey market traffic and increase traffic on the carrier route. However, from the data shared in the consultation, this strategy appears to have met with limited success.

The Consultation Paper highlighted that in many cases, the foreign operators fix comparatively high international termination rates for outgoing calls from India, thus making the domestic access service provider a price-taker in respect of international outgoing call and hence, to ensure level playing field, the foreign access provider must also be a price-taker for an international incoming call.

It was suggested that in case a forbearance regime is considered, then it may be necessary for integrated operators (access cum ILD service providers) to offer matching termination rates in transparent and non-discriminatory manner to standalone ILDOs also.

TRAI also highlighted that a direct transition from regulated to forbearance regime for ITC rates may have the risk of unpredictable behaviour by service providers and that unprecedented changes in the ITC rate may affect other sectors of economy, in addition to international telephony market, and to cover such unforeseen risks, there may be a need for fixing the ceiling rates of ITC.

EBG Federation Position: EBG Federation agrees with TRAI that for an international incoming call, the foreign access provider must be a price-taker, i.e. either through a regulated rate or in case of a forbearance regime, the rate should be driven domestically and not by the foreign access operators. EBG Federation further supports forbearance with matching termination rates offered by the integrated access + ILD operator in transparent and non-discriminatory manner to standalone ILDOs. EBG Federation also agrees that there is a need to safeguard against the risks, and thus support forbearance with a ceiling rate for ITC.

On 17 April 2020, TRAI vide Telecommunication Interconnection Usage Charges (Sixteenth Amendment) Regulations, 2020, notified that the rate of ITC shall be kept under forbearance within a prescribed range of Re. 0.35 per minute to Re. 0.65 per minute.

K. Tariffs

On 17 December 2019, TRAI issued a Consultation Paper on Tariff Issues of Telecom Services. The Paper notes that whilst TRAI has prescribed forbearance on tariffs, it is always open to TRAI to withdraw, wholly or partly, from the forbearance regime, if the situation so demands.

The Paper has also cited precedents where the TRAI had stepped in to determine tariff in respect of services, which were initially kept under forbearance as also highlighted several precedents from around the world, where regulators have stepped in and prescribed floor tariffs as warranted by specific market conditions.

EBG Federation believes that the current market conditions warrant an intervention by the Regulator to step in and prescribe a floor price for telecom services. This will enable operators to make the heavy investments that are required by the sector for network expansion, technology upgradation, greater fiberisation and ever-increasing appetite for data usage and quality of service for consumers.

L. Traffic Management Practices

TRAI issued a Consultation Paper Traffic Management Practices (TMPs) and Multi-Stakeholder Body for Net Neutrality' on 2 January 2020. This was further to its recommendation on Net Neutrality, which were accepted by the DoT and also incorporated into Licenses by way of a License amendment.

The Paper raises various issues pertaining to the types of traffic management practices deployed by the Access Providers (APs) to manage traffic, reasonableness of the said practices, set up needed to detect violations of net neutrality, etc. TRAI also sought views on setting up of a multi stakeholder body for advising on formulation of TMPs and monitoring and enforcement.

It is a well-recognised fact that not all traffic makes equal demands on a mobile network. For example voice is time sensitive, video requires large bandwidths, etc. The inherent nature of mobile networks thus requires that service providers have the flexibility to manage their traffic

By treating different types of data traffic differently, traffic management allows the performance of services to be managed individually to ensure a better overall quality of experience for customers.

A prescriptive regulatory approach would hamper this flexibility and may have unintended impact on quality of service. Further, given that DoT is responsible for enforcing license provisions, establishing a Multi stakeholder body (MSB) will only an additional layer to organisational and decision making complexity as well as costs.

On 22 September 2019 TRAI submitted its recommendations to DoT suggesting a process for creation of a repository of reasonable and necessary TMPs that may be adopted by Internet access service providers, that DoT may frame a policy for Internet access service providers to inform users regarding impact of applied TMPs and the creation of a multi stakeholder body.

EBG Position: EBG Federation believes that a self-regulatory approach would be far more desirable and may be preferred over a prescriptive approach that may end up hampering the flexibility of service providers in managing their traffic and ensuring quality of experience for their customers.

M. Unbundling of Different Layers through Differential Licensing

TRAI issued a Pre-Consultation on "Enabling Unbundling of Different Layers through Differential Licensing" on 9 December 2019.

The paper seeks to understand the possible benefits and anticipated problems in having an unbundled licensing regime and that in case of unbundling, what should be the different layers and their scope and the changes required in licensing regime to enable such a framework. Views were also sought on whether unbundling should be introduced as a new regime with migration or as a parallel incentivised regime for unbundled layers.

Regulatory predictability and certainty are the founding ground for instilling confidence especially in the telecom sector, where operators have made huge investments in building the telecom infrastructure. Frequent changes in policy creates uncertainty which impacts both investments as well as investor confidence.

Unbundling and differential licensing is a step away from the unified licensing regime introduced in 2013. Unified licensing recognised the convergence in the sector and thus a need for a harmonised approach.

It is far more desirable to adopt a future fit light touch approach applicable equally to all layers rather than once again create a differential model that again takes us back to the challenges that were highlighted whilst making a case for a unified licensing regime.

A future fit regime would be one that has:

- Simple and light touch
- Encompasses all communication services
- Technology neutral
- Encourages innovation
- Encourages investments
- One India, One License as an option
- Commitment to address legacy issues

On 20 August 2020, TRAI issued a Consultation Paper on Enabling Unbundling of Different Layers through Differential Licensing.

EBG Federation Position: EBG Federation supports continuation with the unified licensing approach but urges for radical reforms to ensure that the regime is future fit and light touch.

N. Using Wi-Fi to Bridge the Digital Divide in Rural India

The Internet is the single most self-empowering infrastructure available for a citizen in the 21st century. The World Bank observed that a 10% increase in internet penetration leads to a 1.4% increase in GDP.

The growth of Internet penetration in India and realisation of its full potential is closely tied to the proliferation of broadband services. Broadband is essential for the socioeconomic development of the country, many of the industry studies has confirmed the same. A joint study by ICRIER along with BIF estimates that a 10% increase in use of mobile apps results in a 3.3% increase in GDP for India.

Liberalisation and proliferation of public Wi-Fi can provide a significant boost to the government’s digital ambition – ubiquitous connectivity, digital inclusion and enabling infrastructure. In addition, productivity improvements from high speed Wi-Fi for the overall economy can also translate into tangible benefits to GDP.

Providing access to Wi-Fi could be an economical and rapid way of connecting the unconnected throughout the country. Public hotspots hold an important place in the last-mile delivery of broadband to users. Wi-Fi can bolsters connectivity inside buildings, airports, as well as to the rural and remote areas, etc. It can also facilitating for offloading from telecom networks to ease congestion and will be crucial when the next billion IoT devices come online. Yet, there are only 0.4 million (approx.) public Wi-Fi hotspots in India deployed number by public and private players, compared to 13 million in France, and 10 million in the United States of America (based on 2016 figures from iPass).

Wi-Fi networks offer affordable, scalable and versatile technologies that can facilitate the spread of Internet access in rural and urban areas alike. Modern technology also makes it possible to integrate a content server with high storage capacity with the Wi-Fi hotspot equipment. As the cost of such on-Wi-Fi content servers has come down significantly, along with the cost of storage, and the form factors of such devices are very small, it should be possible to cache or download content for easy browsing even when the backhaul connectivity is not available. Such innovative Wi-Fi deployment architecture along with local content server is quite beneficial for rural and remote areas of India, because these areas normally imposes the challenges with outages in internet backhaul connectivity.

Wi-Fi service uses unlicensed spectrum in 2.4 GHz and 5GHz bands. Consumers rely on Wi-Fi these days utilising it seamlessly while they are outside or on the go. Furthermore, unlicensed spectrum will play an important role in proliferation of IoT and smart cities. Seoul, the Korean Capital has almost universal Wi-Fi which is twice the speed of Wi-Fi in the US, whereas, in India, Wi-Fi technology is a highly underused asset. The opportunity cost to use unlicensed spectrum as a gap-filler is being felt in India.

The use of unlicensed spectrum has been one of the key enabling factors in the growth and widespread adoption of the Wi-Fi standard. Accordingly, in an effort to provide maximum flexibility for innovation and lower entry costs for ubiquitous wireless devices including those that utilise the Wi-Fi standards, many countries have set aside certain bands (such as the 2.4 GHz and 5 GHz bands). However, apart from the unlicensed frequencies typically utilised under the Wi-Fi standard, there are several other frequency bands which can be utilised for wireless provision of Internet access.

Early deployment of wireless fibre technologies in the E & V bands could expedite the process of affordable broadband penetration in India. TRAI Recommendations of 2014 are still to be accepted.

O. Improving the Business Case for Unified License – Virtual Network Operators

The DoT issued Guidelines and subsequently license agreement for Unified License – Virtual Network operators in 2016. However despite almost 4 years having passed, the business case for VNOs has not taken off on account of various restrictions and anomalies that need to be addressed.

For example, at present, multi parenting not allowed for access services in VNO. The **c**ondition under UL-VNO License Guidelines states as below:

“VNOs will be allowed to have agreements with more than one NSO for all ***services other than access services*** *and such services which need numbering and unique identity of the customers”.*

This clause impinges on the ability of a VNO to effectively compete in the market by tying its fate to a single access service provider and thereby restricting choice, technology to customers. Such a restrictive condition is not there with respect to any other service authorised to be resold under the VNO license.

It may be noted that NDCP 2018 has also given emphasis on VNO by stating:

“1.1 (j) By encouraging innovative approaches to infrastructure creation and access including through resale and Virtual Network Operators (VNO)”

Further, the VNO license lays down a co-Terminus license period condition a given below.

“This License shall be valid for a period of 10 years from the effective date of this License unless revoked earlier for reasons as specified elsewhere in the document. Validity period for service(s) authorised under any Chapter of Part-II of this Unified License, at a later date, shall be co-terminus with the validity period of this UL (VNO).”

The above condition mandates, different authorisation taken at different times are to be terminated with the end of first license even after paying full entry fees for all licenses. The validity of any additional authorisation will be co-terminus with the validity of the first/existing authorisation without any pro-rata rebate in the stipulated entry fee, thus creating an unfair and inequitable burden amongst similarly placed VNOs.

EBG Federation urges that VNOs should be allowed to have agreements with more than one NSO for all services including access services thus giving the much needed flexibility from the hands of a reseller (VNO) to provide services to its customers. Further, EBG Federation urges that the current validity of the license should be 20 years (not 10 years) to be at par with other licenses. License validity should not be co-terminus with the validity of first authorisation. The license validity should be for full 10 years as full entry fee is required to be submitted. If not, then the entry fee should be reduced on a pro-rata basis on the principle of natural justice.

P. In-country Testing

The Gazette Notification on Testing and Certification of Telegraph dated 5 September 2017 issued by DoT made it mandatory that all telecom equipment shall have to undergo prior mandatory testing and certification of all telecom equipment from TEC certified test labs before they are imported/deployed in Indian telecom networks. This was to come into force from October 2018.

Concerns were voiced to the government on the lack of testing infrastructure in the country, which could lead to the mandatory testing requirements becoming a 'Technical Barrier to Trade', impact ease of doing business, increase costs, cause potential import delays and consequent business disruptions and in a 5G scenario, may even delay the roll out of 5G.

The government, appreciating these concerns, has been granting extensions from time to time before rolling out the Phase 1 of the mandatory testing requirements from 01-Oct-2019, with an initial small group of telecom products. DoT has now launched Phase 2 extending the number of products covered.

The industry has again requested DoT to allow sufficient timelines in Phase 2 besides accepting international certificates. Moreover, industry has repeatedly asked TEC to harmonise the Essential Requirements (ERs) for testing with international testing being done by OEMs to reduce unnecessary testing and avoid product re-design. Also, the Industry has requested that any changes to these ERs are done only after proper government-industry consultation.

EBG Federation believes that there is a need to have testing infrastructure fully in place before any large-scale mandate is imposed for in-country testing. The industry has seen various challenges in implementation of Phase 1 and 2 of DoT's MTCTE scheme and DoT will need to provide adequate timeline, address discrepancies and concerns of the OEMs and start accepting international test reports going forward. Regular government-industry stakeholder consultations is a must for future success of such testing and certification schemes.

Q. Hike in Customs Duties

In 2018, the government hiked the customs duties on various 4G/5G related network products, notably MIMO/LTE products, Soft switches and Voice over Internet Protocol (VoIP) equipment etc., from 10% to 20%. This increase in duties is most unjustified as the equipment impacted are critical items for the networks, required for harnessing new digital technologies and platforms to unlock productivity.

The duty hike has resulted in unexpected costs increase and adverse impact on the network rollouts. The unplanned increase in duty has serious impact on business case of service providers as well as equipment vendors and is causing further constraints on an already financially stressed sector.

The increase in customs duties is also contrary to strategy of rationalising taxes and levies on Digital Communications equipment, which is enunciated in the National Digital Communications Policy 2018 to Propel India and enable Next Generation Technologies and Services.

This is also causing non level playing field as certain vendors from countries with which India has free trade agreements are able to provide the same equipment at NIL duty.

EBG Federation believes that the higher duties have only raised the burden on telecom operators and created a distorted market where in cases of Free Trade Agreement (FTA) countries, equipment is brought in at zero duty creating a non-level playing field. EBG Federation urges that customs duties on these products should be brought down to Nil considering the essential nature of these imports to meet the national vision of Digital India and for level playing field for all vendors and operators. Most telecom OEMs, including Nokia and Ericsson, are already manufacturing in India and increase in duties has not resulted in attracting any new global investment in the country.

R. Local Manufacturing

EBG Federation Members Nokia and Ericsson already have manufacturing facilities in India and supply majority of the radio products from local factories to Indian telecom operators.

There is an opportunity to raise production and Make in India for the World from such telecom factories, generating greater number of jobs and foreign exchange for the country.

To realise this vision, DoT needs to incentivise telecom equipment production and exports along the lines of Ministry of Electronics and IT (MEITY) – which is planning to come up with a Production Linked Incentive (PLI) scheme providing incentives worth over INR 40,000+ Crores for manufacture of mobile phones and component in the country.

DoT needs to urgently support the telecom equipment manufacturers in India, both Indian and Global OEMs, to achieve the NDCP 2018 vision of India integrating with global supply chains.

Also, EBG Federation members are not able to get PMI (Preference to Make in India) incentives despite manufacturing in the country suggesting an urgent need to review DoT's PMI/PMA scheme.

The DoT PMI scheme needs to be urgently revised in direct consultation with industry members who are manufacturing in India.

EBG Federation suggests that DoT urgently a) plans an incentive scheme for telecom equipment manufacturers along the lines of PLI scheme by MEITY and b) undertakes extensive industry consultation to make sure every manufacturer in India (both Indian and Global) qualifies for PMI incentives provided by Government of India.

S. Standardisation

Standards and Standardisation bodies play a key role in the Telecom/ICT technologies. The two main Telecom/ICT focused standardisation bodies in India are Telecom Engineering Centre (TEC) and Telecom Standards Development Society, India (TSDSI).

Telecom Engineering Centre: TEC under DoT (Department of Telecommunications) frames specifications/standards for Telecom Equipment & Network in the country with an objective to enable the deployment and operation of State-of-the-Art, seamlessly interoperable telecom networks. Telecom Equipment Manufacturers/Suppliers (TSPs) get their products tested and certified against these standards/specifications. TSPs specify these standards/specifications while purchasing the equipment for the networks being implemented by them. TEC has been associated with International Standardisation bodies like ITU in respect of developing global standards. National Working Groups in TEC corresponding to various study Groups of ITU contribute to Global Standards making process.

TEC has drafted a policy for adoption of standards of TSDSI/international standards body. "Standardisation Guide" – a policy document for adoption of telecom and related ICT standards defines the process of adoption/ratification of TSDSI/ international standards like institutional mechanism, process of adoption, maintenance of standards, numbering plan, stakeholder consultation etc.

Since 2015, TEC has been regularly releasing study reports on various topics in M2M/IoT domain. Technical Reports (Release 1 and Release 2) of M2M working groups are available on the TEC website.

Department of Telecommunications (DoT) has tasked TEC to evaluate 3GPP and oneM2M Release 2 specifications transposed by TSDSI for ratification/adoption as National standards for M2M/IoT ecosystem in India. TEC has finalised a Report on Adoption of oneM2M standard as National Standards, which is expected to be released soon.

Finalisation of National standards for IoT/M2M technologies in India was entrusted with TEC. India at present is progressively working towards finalisation of these oneM2M as national standards for IoT/M2M.

Telecommunications Standards Development Society, India (TSDSI: Telecommunications Standards Development Society, India (TSDSI), is an autonomous 'Not for profit' standards development organisation for telecom products and services in India. It is registered as a society under Societies Registration act XXI, 1860 and is recognised by Department of Telecom, Government of India as telecom SDO. Developing, promoting & standardising India-specific Telecom/ICT requirements & solutions and taking Indian requirements & Indian Innovations to global standards organisations are the key objectives of TSDSI and its members.

TSDSI is Organisational Partner (OP) of 3GPP , enabling TSDSI members to become individual members of 3GPP through TSDSI and to take their IP into the global arena. Membership of 3GPP enables members to contribute in the development of upcoming standards such as 5G.

TSDSI is also Partner Type 1 of oneM2M, one of the leading forums driving M2M service layer standards.

TSDSI, transposed and adopted the 3GPP and oneM2M Release 2 specifications and has submitted to Department of telecommunication (DoT):

- oneM2M Specifications Rel 2 (comprising 17 specifications and 10 technical reports) into TSDSI Standards. These have already been published on TSDSI website. (click here)
- 295 Specifications of 3GPP (select specifications from Rel 10 to Rel 13) for IMT Advanced (as per ITU-R M.2012-3) also published as TSDSI standards. (click here).

oneM2M has issued Release 3 of its specifications in December 2018. It added a complementary set of oneM2M value-added services to complement IoT features in 3GPP standards. These features help mitigating network congestion and security issues in mobile operator networks, creating a pathway to scalable IoT deployments. TSDSI plans on transposing oneM2M Release 3 soon into TSDSI standards.

EBG Federation Position: EBG Federation supports global harmonisation of Standards as Standards are valuable tools that can help businesses to ensure the quality and safety of products/services, achieve compatibility between products/components, access markets and sell to customers in other countries, satisfy consumers' expectations and requirements, reduce costs, eliminate waste and improve efficiency, comply with relevant national/international legislation and regulations and gain knowledge about new technologies and innovation. TSDSI's proposed 5G standard is not harmonised with 3GPP standards and imposing any mandatory 5G standards by Indian government will lead to huge challenges in inter-operability and other areas.

CONCLUSION & RECOMMENDATIONS

India has the potential to transforming into one of the leading digital economies of the world. Various progressive and market based measures have already been taken by the government and the future roadmap has also been laid down in the form of visionary NDCP-2018.

However, the growing financial stress in the sector, coupled with the recent judgment of Adjusted Gross Revenues has pushed the sector to the brink of an unprecedented financial crisis. A crisis, which if not averted, has the potential to derail all the good work that has been done so far, impacting not just the telecom players, but also the other digital ecosystem players, the banking sector and most importantly the consumers.

There is a need for assertive and affirmative actions. Some measures are already in the pipeline whilst others are being considered.

Implementation of the NDCP-2018 is another important priority area for the government. A world class policy has been formulated – it now needs to be translated from paper to action,

thereby catalysing economic growth and development, generating new-age jobs and livelihoods and ensuring access to next-generation services for India and its people.

INDUSTRY SNAPSHOT

	Unit	Q.E. 31-Mar-2019	Q.E. 30-Jun-2019	Q.E. 30-Sep-2019	Q.E- 31 Dec-2019	Q.E. 31 Mar-2020
Telecom Subscribers (Wireless + Wireline)						
Total Subscribers	Million	1,183.51	1,186.63	1,195.24	1,172.44	1,177.97
% change over the previous quarter		-0.79%	0.26%	0.73%	-1.91%	0.47%
Urban Subscribers	Million	669.16	675.58	677.95	662.45	656.46
Rural Subscribers	Million	514.35	511.05	517.29	509.99	521.51
Market share of Private Operators		88.71%	88.75%	88.81%	88.55%	88.54%
Market share of PSU Operators		11.29%	11.25%	11.19%	11.45%	11.46%
Tele density		90.11	90.11	90.52	88.56	87.37
Urban Tele density		159.96	160.78	160.63	156.26	142.31
Rural Tele density		57.47	56.99	57.59	56.67	58.79
Wireless Subscribers						
Total Wireless Subscribers	Million	1,161.81	1,165.46	1,173.75	1,151.44	1,157.75
% change over the previous quarter		-1.21%	0.31%	0.71%	-1.90%	0.55%
Urban Subscribers	Million	650.49	657.27	659.18	643.97	638.48
Rural Subscribers	Million	511.32	508.19	514.56	507.46	519.27
Market share of Private Operators		89.74%	89.73%	89.74%	89.45%	89.36%
Market share of PSU Operators		10.26%	10.27%	10.26%	10.55%	10.64%
Tele density		88.46	88.5	88.9	86.98	85.87
Urban Tele density		155.49	156.42	156.18	151.90	138.41
Rural Tele density		57.13	56.68	57.28	56.39	58.54
Total Wireless Data Usage during quarter	Million GB	15,850	17,940	19,839	21,402	23,403

No. of total PMRT Services		60,078	58,905	59,118	59,089	66,576
No. of Very Small Aperture Terminals		2,97,465	2,94,590	2,97,047	298,464	300,686
Wireline Subscribers						
Total Wireline Subscribers	Million	21.70	21.17	21.49	21.00	20.22
% change over the previous quarter		-0.79%	-2.43%	1.52%	-3.74%	-3.74%
Urban Subscribers	Million	18.67	18.31	18.77	18.47	17.97
Rural Subscribers	Million	3.02	2.85	2.72	2.53	2.24
Market share of Private Operators		33.58%	34.77%	38.07%	39.53%	58.47%
Market share of PSU Operators		66.42%	65.23%	61.93%	60.47%	41.53%
Tele density		1.65	1.61	1.63	1.59	1.50
Urban Tele density		4.46	4.36	4.45	4.36	3.90
Rural Tele density		0.34	0.32	0.3	0.28	0.25
No. of Village Public Telephones		1,30,376	1,04,466	70,834	68,784	67,762
No. of Public Call Office		2,55,268	2,28,371	2,07,243	1,93,794	1,73,291
Internet/Broadband Subscribers						
Total Internet Subscribers	Million	636.73	665.31	687.62	718.74	743.19
% change over previous quarter		5.38%	4.49%	3.35%	4.53%	3.40%
Narrowband subscribers		73.42	70.72	62.20	56.81	55.75
Broadband subscribers	Million	563.31	594.38	625.42	661.94	687.44
Wired Internet Subscribers		21.68	21.67	22.26	22.39	22.42
Wireless Internet Subscribers	Million	615.05	643.64	665.37	696.36	720.78
Urban Internet Subscribers	Million	409.72	427.05	439.99	450.31	457.23
Rural Internet Subscribers	Million	227.01	238.26	247.63	263.43	285.97
Total Internet Subscribers per 100 population		48.48	50.52	52.08	54.29	55.12
Urban Internet Subscribers per 100 population		97.94	101.63	104.25	106.22	99.12
Rural Internet Subscribers per 100 population		25.36	26.57	27.57	29.83	32.24
Telecom Financial Data						
Gross Revenue (GR) during quarter	INR Cr	58,414	61,535	59,992	63764.14	`67,533.74
% change in GR over previous quarter		-0.98%	5.34%	-2.51%	6.29%	5.91%
Adjusted Gross Revenue (AGR) during Qtr	INR Cr	35,932	39,124	37,338	40877.46	`44,940.32
% change in AGR over previous Qtr		-0.34%	8.88%	-4.56%	9.48%	9.94%

Share of PSUs in Access AGR		9.57%	10.49%	7.88%	8%	7.91%
Monthly Average Revenue Per User (ARPU) for Access Services	INR	72.49	80.65	78.17	85.07	`97.64
Revenue & Usage Parameters						
Monthly ARPU of Wireless Service (GSM+CDMA+LTE)	INR	71.39	74.30	74.38	78.65	91.49
Minutes of Usage (MOU) per subscriber per month - Wireless Service (GSM+CDMA+LTE)	Minutes	692	701	691	712	750
Total Outgoing Minutes of Usage for Internet Telephony	Million	197	198.34	197.09	181.34	181.34
Broadcasting & Cable Services						
Number of private satellisssste TV channels permitted by the Ministry of I&B for uplinking only/downlinking /uplinking		902	908	910	918	926
Number of Pay TV Channels as reported by broadcasters		328	331	330	332	333
Number of private FM Radio Stations (excluding All India Radio)		356	366	367	368	368
Number of net Active subscribers with Pay DTH Operators	Million	72.44	54.36	69.30	69.98	70.26
Number of Operational Community Radio Stations		251	261	275	278	290
Number of pay DTH Operators		5	4	4	4	4

Source: TRAI

ENDNOTE

1. http://curia.europa.eu/juris/document/document.jsf?text=3G%2BVAT&docid=61676&pageIndex=0&doclang=EN&mode=req&dir=&occ=first&part=1&cid=3632266#ctx1

2. https://eur-lex.europa.eu/eli/dir/2006/112/oj

NOTE

NOTE

NOTE

NOTE

NOTE

EBG OFFICES

DELHI
J-8 Green Park Extension
New Delhi-110029
Tel: +91 78382 26855
Email: mamta@ebgindia.com
website: www.ebgindia.com

MUMBAI
C/o Fuchs Lubricants (India) Pvt. Ltd.
Sarjan Plaza, 2nd Floor
100, Dr. Annie Besant Road
Worli, Mumbai – 400 018
Tel : +91 022 66255904
Email: mumbai@ebgindia.com

BENGALURU
C/o Mr Sanjeev Varma
Chairman, EBG Bengaluru Chapter
Email: bangalore@ebgindia.com

Publisher:
EBG Federation, India
Promote, Propagate and Safeguard European Business Interests in India

EBG Federation, India
J-8 Green Park Extension, New Delhi-110029
Tel: +91 78382 26855, Email: mamta@ebgindia.com, website: www.ebgindia.com