

Indian Companies - Need for a Clear Definition

Amit Cowshish

January 22, 2014

Lagging behind the other services, and probably even the Coast Guard, in the race for modernization, Army has drawn up a ‘multipronged plan to boost its capabilities’.¹ That is quite reassuring. But for this plan, or, for that matter, any other such plan to fructify, much ground work needs to be done.

On its part, the Army Headquarters will need to steer specific procurement proposals through the labyrinthine procurement procedure, first up to the Acceptance of Necessity (AoN) stage and later through the tendering stage. But this path is beset with difficulties as many issues concerning the defence procurement procedure and the offset policy have remained unaddressed for far too long, leaving the companies – both Indian and foreign – in a state of perpetual perplexity. Ministry of Defence (MoD) will have to clear the air on all such issues, or, at least, on the issues which fall squarely in its own jurisdiction.

One such critical issue, relevant in the overall context of the procurement procedure and offsets, is the definition of an ‘Indian company’. With ‘Buy (Indian)’, ‘Buy and Make (Indian)’ and ‘Make (Indian)’ categories now occupying the pride of place in that order in the hierarchy of procurement categories, which companies will qualify as Indian companies assumes a great importance as under these categories the Request for Proposal (RFP) can be issued only to the Indian companies. Any ambiguity in this regard could put the procurement proposals in a spin.

¹ See ‘Multipronged plan drawn up to boost Army's capabilities, Gen Bikram Singh says’, the Times of India, January 16, 2014, accessible at <http://timesofindia.indiatimes.com/india/Multipronged-plan-drawn-up-to-boost-Armys-capabilities-Gen-Bikram-Singh-says/articleshow/28840097.cms> (last accessed on January 16, 2014)

This is also important in the context of the offsets. The offset guidelines provide that 'Indian enterprises and institutions and establishments engaged in manufacture of eligible products and/or provision of eligible services, including DRDO, are referred to as the Indian Offset Partner (IOP)' and the IOP shall, 'besides any other regulation in force, also comply with the guidelines/licensing requirements stipulated by the Department of Industrial Policy and Promotion, as applicable.'²

But the Defence Procurement Procedure (DPP) 2013, as also its earlier versions, does not define an Indian company, much less an Indian enterprise, institution and establishment. Some would argue that the answer is very simple: any entity registered in India under the Companies Act, 2013 or any other relevant statute and operating with a valid license, where such a license is required, qualifies as an Indian company, enterprise, institution or establishment. The question is whether it is so. Life would be simple if it is indeed so, but even then, this clarification must be officially notified by the MoD so that there is no ambiguity on this issue.

Ambiguity could derail the procurement proposal even at the very initial stage when the Statement of Case (SoC) is being prepared for consideration by various committees for Acceptance of Necessity (AoN), which clears the way for the tendering process to start. One of the pre-requisites for initiating a case is formulation of the Services Qualitative Requirements (SQRs) on the basis of the inputs to be obtained by issuing a Request for Information (RFI) and through interaction with the maximum number of manufacturers. The DPP also requires additional inputs to be obtained from defence attachés, internet, defence journals/magazines/exhibitions, previously contracted cases, and so on.³ Probably at this stage it is not possible to say which procurement category it will be feasible to put the proposal into. But, at a later stage, this question assumes a critical significance. One of the standard requirements while preparing the SoC is to recommend the mode and source of acquisition.⁴ The officers preparing the SoC, as also those at the higher levels in the decision-making chain, need to be clear about which sources of supply would qualify

² See paragraphs 4.1 and 4.2 of Appendix D to Chapter I, DPP 2013, accessible at <http://mod.nic.in/writereaddata/DPP2013.pdf>

³ See paragraph 14 of Chapter I, DPP 2013, *ibid*.

⁴ See paragraph 6 of Appendix A to Chapter I, DPP 2013, *ibid*.

as an Indian source. Lack of this clarity is detrimental to expeditious processing of the procurement proposal.

It may be mentioned in the passing that the way the information is gathered in the run up to formulation of the SQRs also creates two problems. One, if the SQRs are formulated on the basis of the inputs, largely from the foreign sources of supply, the Indian companies may find it difficult to comply with those SQRs. Secondly, those who respond to the RFI, especially the foreign companies, are not too sure whether the proposal would eventually be so categorized as to make them eligible to participate in the tendering process. Consequently, they are unable to decide whether to immediately form a joint venture with an Indian company so that they could participate in the tendering process if the proposal is categorized as 'Buy (Indian)', etc., or to hold back their horses in the hope that eventually a 'Buy (Global)' RFP will be issued.

This is not the only cause of anxiety for the prospective suppliers. Let us look at the possible scenarios. The first scenario is where a company registered in India, with Foreign Direct Investment (FDI) not exceeding 26 per cent, is manufacturing a defence product, as now notified by the Department of Industrial Policy and Promotion (DIPP)⁵, with at least 30 per cent indigenous content. There is little doubt that such a company would certainly get the RFP in 'Buy (Indian)' cases. A variation of this scenario is that such a company is not already making a product but has a Memorandum of Understanding (MoU) or Technology Agreement with a foreign company which enables it to make the product with the requisite level of indigenous content as and when it gets the contract. The question is whether such a company would also qualify to get the RFP in 'Buy (Indian)' cases. This places the company already making a product with the requisite level of indigenous content at par with another company which only possesses the capability on paper to do so.

The second scenario is where a company with higher percentage of FDI is manufacturing goods or providing services that do not require an industrial license. The question is whether such companies would qualify as Indian companies and get the RFP in 'Buy (Indian)' cases. The answer to this question may not be difficult but a slight variation of

⁵ See the Munitions List notified by the Department of Industrial Policy and Promotion, accessible at http://dipp.nic.in/English/Investor/Investers_Gudlines/defenceProducts_LicencingRequired_26April2013.pdf
Source: http://idsa.in/idsacomments/IndianCompaniesDefence_acowshish_220114

this scenario could pose a problem: what if such a company is engaged in manufacturing a dual use item or providing a service which is common to the non-defence and defence sectors? Will such a company have to obtain an industrial, license if the same item or service is to be provided to the MoD?

The third scenario involves the wholly-owned subsidiaries of the foreign companies which are operating from a base in India. What is their status? Do they qualify as Indian companies for getting RFPs in 'Buy (Indian)' cases and for becoming IOPs?

These are fundamental questions, which are also relevant in the context of 'Buy and Make (Indian)' and 'Make (Indian)' cases. These questions need to be answered, apart from many others, which tend to complicate the procurement process. On its part the Army Headquarters also needs to commission an objective study to analyse why it is lagging behind the other services in its modernization programme. After all, the other services also go through the same procedural rigmarole. This is not a new idea but, for some reason, this has not been implemented. An empirical study of this nature could throw up many surprises.

Views expressed are of the author and do not necessarily reflect the views of the IDSA or of the Government of India.