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Issue Brief

Land Ahoy!

Debarment Systems in Ministry of Defence Start Coming of Age

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Summary

Some initial work was undertaken in 2013 in MoD towards developing its own debarment guidelines, which eventually culminated in the issue of a Policy in November 2016 and quickly followed by the issuance of detailed Procedures in December the same year. However, from a strictly legal viewpoint, it would be naïve for procurement professionals to presume that these implementing procedures are only “procedural”: for instance, the Procedure establishes an upper limit of 10 years as the maximum permissible period for a ban—an important feature the Policy had clearly omitted to mention while specifying five years as the minimum period—thus saving MoD from the embarrassment of having to edit the Policy within just a month of its issue.

Introduction

Despite the Government of India (GoI) having issued perhaps the most advanced and comprehensive guidelines anywhere in the world on blacklisting/debarment¹ as early as 1971, its own Ministry of Defence (MoD) continued with an ad-hoc approach² until as late as 2013. This divergence in approach was stark to the extent that that the ministry's debarment/ suspension decisions were sometimes based simply on newspaper reports of alleged wrong-doing,³ which was contrary to the 1971 guidance discouraging ban or suspension of business dealings even pursuant to a formal criminal investigation against an errant entity.⁴

Some initial work was undertaken in 2013 in MoD towards developing its own debarment guidelines,⁵ which eventually culminated in the issue of a *Policy*⁶ in November 2016 and quickly followed by the issuance of detailed *Procedures*⁷ in December the same year. However, from a strictly legal viewpoint, it would be naïve for procurement professionals to presume that these implementing procedures are only “procedural”: for instance, the Procedure establishes an upper limit of 10 years as the maximum permissible period for a ban⁸—an important feature the Policy had clearly omitted to mention while specifying five years as the minimum period⁹—thus saving MoD from the embarrassment of having to edit the Policy within just a month of its issue. But as *Lina A. Braude* of *BakerMacKenzie* hinted in an insightful legal analysis of the 2016 Policy till date,¹⁰ the actual publication of a “List” of debarred/ suspended entities and any re-assessments of pre-2016 cases would perhaps be a more appropriate time to discuss the robustness of MoD's new debarment system.

Pursuant to the Policy/ Procedures issued by MoD in late 2016, the Ministry has undertaken at least one instance of suspension (MoD orders dated 05 January 2018) *and* (what looks like) one re-assessment of a *pre-Policy* suspension case (MoD orders

¹ Verma, S. (2016), “Debarment and Suspension in Public Procurement: A Survey of Important Executive Guidance and Case Law from India,” 7th IPPC/ SSRN, <http://ssrn.com/abstract=2185219>.

² Braude, L. A. (2016), “Indian Ministry of Defence Issues Guidelines on Suspension and Debarment of Suppliers,” *BakerMcKenzie*, <https://www.bakermckenzie.com/en/insight/publications/2016/12/indian-ministry-of-defense-issues-guidelines>

³ MoD orders dated 20/21 April 2005 forming part of List published by MoD orders dated 19 February 2018, <https://mod.gov.in/sites/default/files/firmshold.pdf>.

⁴ Verma, *supra*, n.2.

⁵ Verma, S. (2014), “Sending Contractors on a Holiday: Proposed Rules for an Integrated and Seamless Approach in the Ministry of Defence to Debarment and Suspension of Erring Entities,” SSRN, <https://ssrn.com/abstract=2441040>.

⁶ MoD ID dated 21 November 2016, *Guidelines of the Ministry of Defence for Penalties in Business Dealings with Entities*, www.mod.nic.in

⁷ MoD ID dated 30 December 2016, *Guidelines of the Ministry of Defence for Penalties in Business Dealings with Entities*, www.mod.nic.in

⁸ MoD, *ibid*, ¶31.

⁹ MoD, *supra* n.7, ¶F.3.

¹⁰ Braude, *supra* n.3.

dated 05 December 2017), as mentioned in a publicly-available List of “on hold”/ suspended/ banned/ “restricted” entities (together with relevant office memos relating to its debarment decisions even prior to the 2016 Policy)¹¹, as well as three reassessment decisions in April, August and September 2018.¹² This may therefore be the right time to examine if the MoD Policy, Procedures and/ or the practice (the “List”) are in need of any further fine-tuning. Such critical self-reflection may be advisable for the twin objectives of: (i) infusing MoD debarment mechanisms with greater robustness so as to better withstand potential legal challenges by affected parties; and (ii) build greater trust amongst the stakeholder community, now that the List has been made publicly available, reflecting a much greater thrust and confidence in MoD leadership for increased openness and transparency.¹³

Analysing MoD’s First (Post-2016 Policy) Debarment Action

The first instance of debarment action, post the 2016 Policy, relates to the suspension of business dealings with a particular corporate entity and its Group companies/ functionaries for a period of six months with effect from the date of these orders;¹⁴ and a quick reading of the order alone reveals at least three areas of concern and consequential and possible reform.

Firstly, it took MoD almost 18 months from the date of the first searches-and-seizures, more than 12 months from the registration of an FIR/ availability of a preliminary investigation report, and more than six months from the issue of a show-cause notice, to issue an order of suspension against the firm¹⁵ when its own Procedures do not require even the issue of a notice to an errant entity prior to an order of suspension.¹⁶ These extended timelines reflect a pressing need for accelerated decision-making in MoD in future suspension/ debarment cases, both to insulate its own procurement officials from undesirable allegations of *unduly benefiting* or *unduly harming* a business entity during such long intervening periods, as well as to avoid any decisional confusion or paralysis over the progression (or termination) of related procurement/ offset cases.

¹¹ MoD ID dated 19 February 2018, “Details of Firms debarred/ put on hold/ suspended etc. from doing business with MoD-reg.,” www.mod.nic.in

¹² MoD ID dated 04 April 2018 (reassessment of a 2009 debarment case); MoD ID dated 02 August 2018 (reassessment of the first post-Policy debarment decision of January 2018); MoD ID dated 05 September 2018 (reassessment of a 2005 debarment case); all available at www.mod.nic.in

¹³ See, for instance, “Ensuring 100% transparency in defence procurement a priority, says Sitharaman,” *The Times of India*, 14 December 2017, <https://timesofindia.indiatimes.com/india/ensuring-100-transparency-in-defence-procurement-a-priority-says-sitharaman/articleshow/62071553.cms>

¹⁴ MoD orders dated 05 January 2018 forming part of List published by MoD orders dated 19 February 2018, <https://mod.gov.in/sites/default/files/firmshold.pdf>

¹⁵ Ibid.

¹⁶ MoD, *supra* n.8, ¶9.

Secondly, while the 2016 Policy allows debarment only of “allied firms” and defines them clearly,¹⁷ the 2018 suspension order contains the relatively ambiguous phrase “Group companies”¹⁸—something left undefined in the 2016 Policy. Similarly, it appears from the 2018 suspension order that some notice was issued to the firm in respect of its “associate/ Group companies”,¹⁹ but the phrase “associate companies” is itself absent in the 2016 Policy. Again, while the 2016 Policy mandates *permanent disengagement* with “employees” and “agents” of a suspended entity well beyond the period of suspension,²⁰ the 2018 suspension order restricts this period of disengagement to only six months while extending the scope of affected personnel to “all functionaries”.²¹ Thus, both the *curtailment of the time period of disengagement* and *extension of scope of suspension* in the 2018 suspension order do not seem to harmonise well with the 2016 Policy; and MoD officials may be well-advised in future to use standardised language as per the 2016 Policy so as to avoid unnecessary disputes and potential litigation with affected parties.

Thirdly, a related issue is that the 2018 suspension order makes no attempt to cross-reference with any specific clause(s) of the 2016 Policy: (i) the specific grounds of suspension; or (ii) the specific authority being invoked for suspension; or (iii) the reasons for extension to “Group” companies; or (iv) the reasons for restriction on engagement with all entity “functionaries”.. Such cross-referencing and correlation with the primary guidance while drafting debarment decisions is a standard precaution practiced by procurement professionals worldwide, particularly in complex litigation-prone cases. It may, therefore, be equally advisable for MoD officials in all future cases: (i) to avoid any mistakes through unintended restriction or extension of scope of suspension/ debarment beyond the principle governing debarment Policy; and (ii) to satisfy strict normative requirements of a “speaking order” that reflects clear application of mind vis-à-vis *specific* requirements of a governing policy, going well beyond a speaking order being just a general statement of facts as presently required under the 2016 Policy.²²

Reflections on Pre-2016 Debarment Cases

The inadvertent use by public procurement officials of undefined non-standard phrases such as “group companies”, “subsidiary companies”, “affiliates” and “associate companies” while issuing actual orders of debarment or suspension while using the relatively standardised and the only clearly-defined phrase “allied firms” as contained in the regulatory guidance on the subject is not a new phenomenon.

¹⁷ MoD, *supra* n.7, ¶B.3; read with MoD ID dated 06 March 2018, *Guidelines of the Ministry of Defence for Penalties in Business Dealings with Entities*, www.mod.nic.in.

¹⁸ MoD, *supra* n.15.

¹⁹ *Ibid.*

²⁰ MoD, *supra* n.7, ¶¶H.1-H.2.

²¹ MoD, *supra* n.15.

²² MoD, *supra* n.8, ¶35.

Within MoD itself, such ambiguous/ undefined phrases have indeed been used by officials earlier on multiple occasions in September 2013 (“allied/ subsidiary firms”),²³ July 2014 (“subsidiaries” and “affiliates”),²⁴ in August 2006 and in July/ August 2014 (“group companies”),²⁵ and in July 2014 (“allied and subsidiaries” companies)²⁶ as is evident from various orders published online by MoD earlier this year. While the legal meaning of “subsidiary firms” and “affiliate companies” can still be discerned from secondary sources such as the Companies Act,²⁷ the other phrases can have contested meanings in different contexts, and could therefore be prone to disputes.

Clearly, the use of such non-standard language can result in an improper extension of the scope of debarment well beyond what is permitted under the principle regulatory policy guidance on the subject limiting penal action to allied entities.²⁸ It is also equally possible that MoD’s debarment orders restricting procurement from such “group”/ “affiliate”/ “subsidiary”/ “associate” companies could perhaps remain unimplemented in practice against such entities, because of a lack of clear understanding of the meaning of such phrases. In any case, either consequence is unwelcome and avoidable in a robust public procurement system; and it may therefore be useful for MoD to either clearly define “affiliates”, “group companies”, “subsidiaries” and “associates” just as it has done in the case of “allied firms”, or for MoD officials to completely avoid using such undefined phrases altogether while issuing debarment decisions.

What’s in a Name? Apparently Quite a Lot!

A study of all cases published online by MoD²⁹ makes it clear that it currently publishes only the *names* of erring individuals and firms in its debarment orders. In this regard, MoD may be well-advised to start mentioning the *unique registration numbers* of the suspended/ banned/ debarred/ “on hold” business entities (such as ROC numbers for corporate entities) as well as the *unique ID numbers* of banned individuals (such as DINs) in its debarment orders, in order to make it easier for procurement officials to track inter-firm relationships/ beneficial ownership patterns to fully implement their decisions against allied/ related firms as required under the

²³ MoD orders dated 17 September 2013 forming part of List published by MoD orders dated 19 February 2018, <https://mod.gov.in/sites/default/files/firmshold.pdf>

²⁴ MoD orders dated 03 July 2014 forming part of List published by MoD orders dated 19 February 2018, <https://mod.gov.in/sites/default/files/firmshold.pdf>

²⁵ MoD orders dated 09 October 2006; MoD orders dated 03 July 2014; and MoD orders dated 22 August 2014 forming part of List published by MoD orders dated 19 February 2018, <https://mod.gov.in/sites/default/files/firmshold.pdf>

²⁶ MoD orders dated 28 July 2014 forming part of List published by MoD orders dated 19 February 2018, <https://mod.gov.in/sites/default/files/firmshold.pdf>

²⁷ Companies Act, 2013 (Act No. 18 of 2013), §2(6) and §2(87).

²⁸ MoD, *supra* n.7, ¶E.4 and ¶G.4.

²⁹ MoD, *supra* n.12.

new Policy.³⁰ This refinement will also help MoD officials to better implement another important provision of the new Policy, where a debarred firm is not allowed to transact contracts under a different name³¹—these prohibited transactions will clearly be much easier to track and prevent via a unique registration number both for domestic and international suppliers, as compared to having to track transactions based just on a name.

Getting In and Out of a Limbo

In another interesting revelation, it appears that a 2005 “on-hold” decision (it is unclear if the case is one of suspension or debarment) was taken by MoD simply on the basis of some newspaper and media reports, while the contract itself was put “on-hold”.³² This action of putting contracts “on hold” (implying suspension of buyer and seller obligations under contract) has been repeated by MoD later in another case in July 2014 as well,³³ although the 2014 “on hold” decision was apparently partially withdrawn after a month for certain ongoing contracts.³⁴ In a further twist to the 2014 case, the affected firm’s status was reviewed³⁵ by MoD in 2017, after the issue of its 2016 Policy, where the firm’s suspension has been continued, but it remains unclear whether the related contract (s) is/are being kept in abeyance as required under the new Policy,³⁶ or the earlier August 2014 clarification allowing continuation of contractual relationships with the suspended firm still holds.³⁷

This “putting a contract (including payments) on hold” or “in abeyance”—instead of simply terminating contracts forthwith within a reasonably short period of time—is a non-standard practise in professional public procurement; and certainly one that is inadvisable since it can have adverse legal consequences for MoD in terms of a supplier claiming breach of contract and damages for *buyer-caused* hindrances and non-payment during performance of contract, rather than the buyer claiming breach and damages for *supplier-originated* problems as should justifiably be the case when a supplier breaches the integrity of a public procurement process.

Where a contract has not been finalised, a better approach, as compared to keeping a procurement process “on hold”, could be to eliminate an errant vendor even when it has been found to be lowest-priced technically-acceptable, while moving forward with remaining bidders, or to restart a procurement process as soon as possible. In

³⁰ MoD, *supra* n.7, ¶E.4 and ¶G.4.

³¹ *Ibid*, ¶I.5.

³² MoD, *supra* n.4.

³³ MoD, *supra* n.27.

³⁴ MoD orders dated 22 August 2014 forming part of List published by MoD orders dated 19 February 2018, <https://mod.gov.in/sites/default/files/firmshold.pdf>

³⁵ MoD ID dated 05 December 2017 forming part of List published by MoD orders dated 19 February 2018, <https://mod.gov.in/sites/default/files/firmshold.pdf>

³⁶ MoD, *supra* n.7, ¶I.3.

³⁷ MoD, *supra* n.35.

this context, it is interesting to note that the 2016 Policy takes a clear and pragmatic view in such cases, even though it restricts available options to restarting the procurement process alone,³⁸ and, for some reason, directs procurement officials to generally wait for the bid validity period to get over before restarting procurement in cases of *suspension* of an L-1 bidder.

Substantively, there may be a case for tightening MoD's 2016 Policy from an anti-corruption perspectives to the extent that its provisions allowing continuance of purchases from banned/ debarred entities, simply based on a certificate of operational necessity,³⁹ (termed "restricted procurement" in the List) effectively creates space for "backdoor" entry of the erring firms straight into the folds of mainstream defence procurement. To this extent, MoD's Policy is very different from advanced international debarment systems such as those in the US, which latter are so rigid that a suspension/ debarment decision places an absolute restriction on procurement from an errant firm by any public procurement agency of the Federal Government. It is therefore not surprising that a suspension/ debarment decision in the US system is taken very seriously both by a debarring official as well as by an errant contractor.

Further Clarifications and pre-2016 Reassessments

While issuing the 2016 Policy, MoD had used a definition for "allied firms"⁴⁰ along the same lines of GoI's 1971 office memos. It however appears that some need for further clarification arose, and MoD therefore issued a clarification in this regard in March 2018.⁴¹ Issuance of such clarifications is indeed a welcome practice; and MoD could perhaps consider issuing similar clarifications of its debarment policy and procedures to unambiguously address more complex contractual issues such as (in)eligibility of debarred IOPs by a foreign supplier for discharging offsets, and (in)eligibility of debarred entities as sub-contractors/ technology partners/ non-lead members of a joint venture agreement or consortium in procurement cases under various categories. Such clarifications may now be necessary and unavoidable since the 2016 Policy is silent on these important aspects, while a previous, pre-2016, Policy FAQ issued by MoD in 2014 seems to allow the continuation of debarred/ suspended companies as "sub-contractors".⁴²

³⁸ MoD, *supra* n.7, ¶E.3 and ¶G.3.

³⁹ *Ibid*, ¶I.4. The prescribed certificate under the 2016 Policy more or less resembles the usual certifications that a user agency has to provide anyway while undertaking normal procurement under the DPP/ DPM for obtaining "Acceptance of Necessity" (*see, e.g.*, ¶16 of Chapter II *read with* Appendix C/ Chapter II, Defence Procurement Procedure 2016), and thus, the 2016 Policy appears to place no significantly onerous conditions for procurement from a suspended/ banned firm vis-à-vis firms that have not been suspended/ banned.

⁴⁰ MoD, *supra* n.7, ¶B.3.

⁴¹ MoD, *supra* n.18.

⁴² MoD, *supra* n.35, Item VI.

As mentioned earlier, MoD has till date undertaken a total of four reassessments of its debarment decisions in line with the 2016 Policy—three of these relate to pre-2016 debarments, while one relates to a post-2016 debarment case.⁴³ This is an encouraging trend and reflects a more mature approach to debarment, especially since the new Policy places an upper limit of one year as the maximum period of suspension⁴⁴, together with mandatory six-monthly reviews.⁴⁵ In contrast, some of the suspension/ “on hold” decisions are now as much as 12 years old, significantly more than the new 1-year limit, and in any case, clearly well past the mandatory 6-monthly review.

Replicating the New Banning Procedures Elsewhere in MoD

While the 2016 Policy applies to all departments/ wings of MoD,⁴⁶ the 2016 Procedures are restricted in their application to procurements undertaken within the contours of the Defence Procurement Manual (DPM) and the Defence Procurement Procedure (DPP) only.⁴⁷ It was expected by MoD that its other departments/ wings conducting procurement under *alternative* procurement frameworks—such as DRDO under its 2016 *Procurement Manual*, or other departments/ wings conducting procurement under the *Defence Works Manual*—would come up with their own but similar procedures⁴⁸ equally compliant with the new 2016 Policy framework. However, until now, , the DRDO Procurement Manual has not yet been updated in alignment with the 2016 Policy; and DRDO therefore apparently continues with its debarment/ suspension clauses and terminology that were inspired by GoI’s 1971 office memos⁴⁹ rather than by the newer 2016 Policy of the MoD.

To the extent that the 2016 Policy applies only to departments forming part of the MoD,⁵⁰ it appears that DPSUs under the administrative control of MoD have been allowed to continue with their own respective debarment regulations. However, given that DPSU/ PSU debarment regulations are largely inspired by the 1971 office memos,⁵¹ the omission of DPSUs from the ambit of the 2016 Policy could perhaps be

⁴³ MoD, *supra* n.12-n.13.

⁴⁴ MoD, *supra* n.7, ¶D.3.

⁴⁵ Ibid.

⁴⁶ Ibid, ¶B.1.

⁴⁷ MoD, *supra* n.8, ¶3.

⁴⁸ Ibid, ¶46.

⁴⁹ Notable instances being differing grounds of suspension/ debarment in the DRDO Procurement Manual as compared to MoD’s 2016 Policy, as well as the fact that the DRDO Manual still mentions possibilities of GoI-wide debarment. GoI-wide debarment—the application of MoD’s debarment orders to other Ministries in GoI – is clearly not permissible under MoD’s 2016 Policy; Braude, *supra* n.3.

⁵⁰ MoD, *supra* n.47.

⁵¹ Verma, *supra* n.2. See, also, Verma, S. (2010), “Integrity Pacts and Public Procurement Reform in India: From Incremental Steps to a Rigorous Bid-Protest System,” Inaugural International Conference on Public Procurement Regulation in Emerging Economies 2010, SSRN, <https://ssrn.com/abstract=1656722>.

a deliberate decision, quite unlike the DRDO case where the latter is fairly and squarely covered under the 2016 Policy and expected to align its debarment framework with the 2016 Policy. It is therefore important that these other-than-DPM/DPP frameworks are quickly aligned with the overarching 2016 Policy to avoid inconsistencies and disputes in other wings/ departments of the MoD.

Summary and Conclusions

Debarment (including ban and suspension of business dealings) is one of the most complex aspects of public procurement frameworks. It is administratively easy and politically appealing to debar an errant entity, but the unintended consequences of debarment can be challenging to handle in high-technology areas such as defence where vendor lock-in, “Too Big to Debar”⁵²-type roadblocks and monopsonies are a common occurrence.

Cutting down procurement delays has been declared a “must” and “to-do” reform agenda by MoD’s senior leadership⁵³. Therefore, the various reform suggestions as contained in the aforesaid analysis, including but not limited to refinement and clarifications in furtherance of the existing Policy/ Procedures, while also conducting regular re-assessments of pre-2016 debarment cases, can be particularly useful for cutting down specific procurement delays occurring due to policy gaps or because of uneven understanding amongst multiple stakeholders in the context of debarment and suspension of erring entities.

⁵² Stevenson, D.D. and Wagoner, N.J. (2012), “FCPA Sanctions: Too Big to Debar?,” *Fordham Law Review/ SSRN*, <https://ssrn.com/abstract=1811126>

⁵³ See, e.g., “Defence ministry approves measures to simplify procurement of military platforms and weapons,” *First Post*, 22 May 2018, <https://www.firstpost.com/india/defence-ministry-approves-measures-to-simplify-procurement-of-military-platforms-and-weapons-4478869.html>

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