



ECONOMIC
LAWS
PRACTICE
ADVOCATES & SOLICITORS

ELP Knowledge Series

India Update – Part 1 of 2018

TABLE OF CONTENTS

Foreword.....	2
Indian economy: A snapshot	3
Corporate governance in listed companies: From the abyss into the sunshine	4
Enforcement of foreign awards in India: Key considerations	6
Emerging trends & issues under The Insolvency & Bankruptcy Code, 2016.....	8
Competition law roundup – Key developments.....	11
General Data Protection Regulation : Impact on India-based businesses	12
Recent trends in anti-dumping investigations.....	14
International trade – Sectoral highlights from India	16
Defence & Aerospace: Analyzing the opportunity in India	18
Summary of judicial decisions defining the indirect tax landscape in India.....	20
India’s pharmaceuticals sector: Facing headwinds	22
Annexure.....	24
Contributions by	25

FOREWORD

Dear Reader,

‘India Update – Part 1 of 2018’ is the latest addition to the ELP Knowledge Series.

This document is intended to keep you updated on the latest legal, policy and regulatory developments in India. While many such developments have ramifications across sectors, an equally significant number pertains to specific industry sectors. It is our endeavour to short-list, collate and analyse the available data in order to curate information that provides a succinct overview of selected topics and issues.

Many developments over the recent past – especially regarding the Insolvency & Bankruptcy Code, data privacy and liability concerns stemming from GDPR, ramifications of the Kotak Committee report for corporate governance in the country, etc. – have forced companies to revisit several fundamental aspects of their operations and corporate structures. We have presented detailed analysis of these topics. Additionally, we have also added a section discussing renewed foreign interest in India’s defense & aerospace sector.

The document also examines the inherent challenges in enforcing foreign arbitration awards in India and the post-GST judicial pronouncements that are shaping the country’s indirect tax landscape. We conclude by summarising the latest trends in anti-dumping investigations in India and notable developments in our competition laws framework.

We hope you will find the information contained in the subsequent sections to be helpful. For any clarification or further information, please reach out to your point of contact at ELP or any member of our team who has contributed to this iteration of the ‘India Update’.

Happy reading.

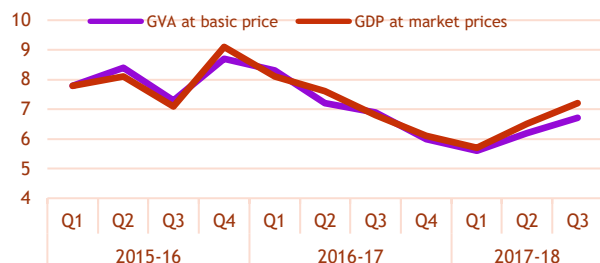
Regards,

Team ELP

INDIAN ECONOMY: A SNAPSHOT

ECONOMIC GROWTH

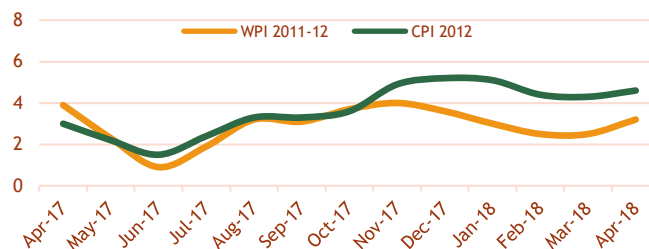
Quarterly Growth of GDP and GVA (%) at constant prices



Source: Central Statistical Organisation (CSO)

INFLATION

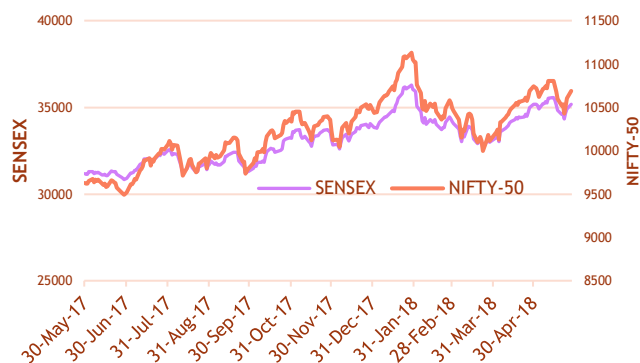
Inflation in WPI and CPI (%)



Source: Office of Economic Adviser- DIPP and CSO

SHARE MARKET

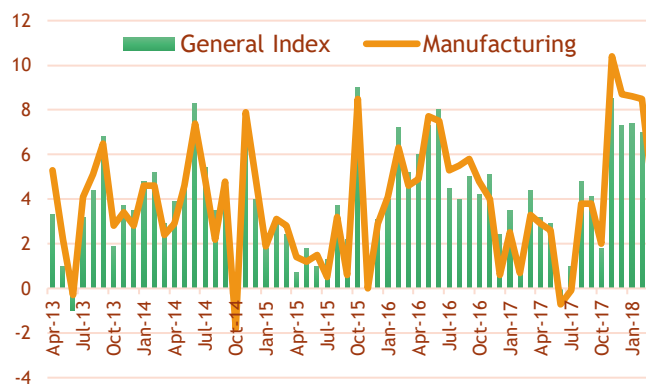
SENSEX and NIFTY-50



Source: BSE and NSE

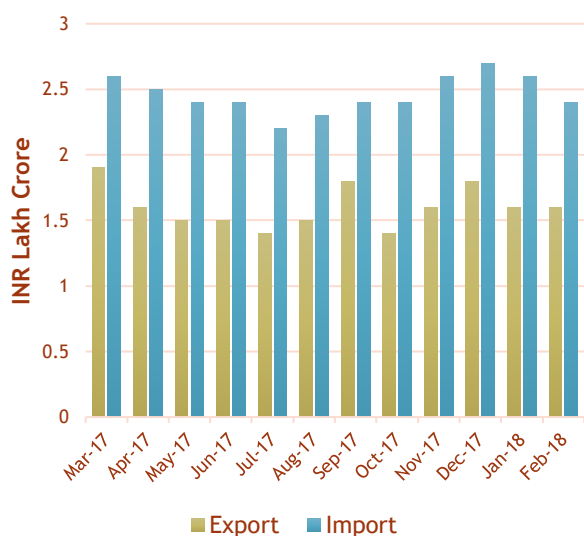
PRODUCTION GROWTH

Index of Industrial Production (IIP) growth in %



Source: CSO

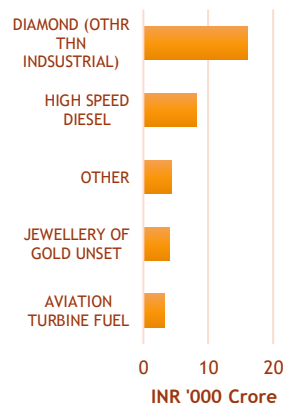
EXTERNAL TRADE



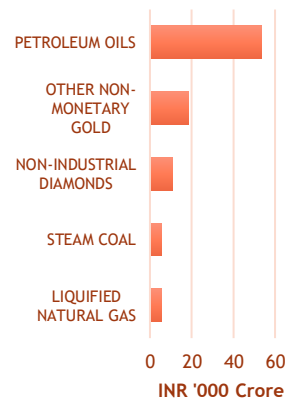
Source: Ministry of Commerce

MAJOR GOODS TRADED

TOP EXPORT FROM INDIA IN FEB 2018



TOP IMPORT INTO INDIA IN FEB 2018



Source: Ministry of Commerce

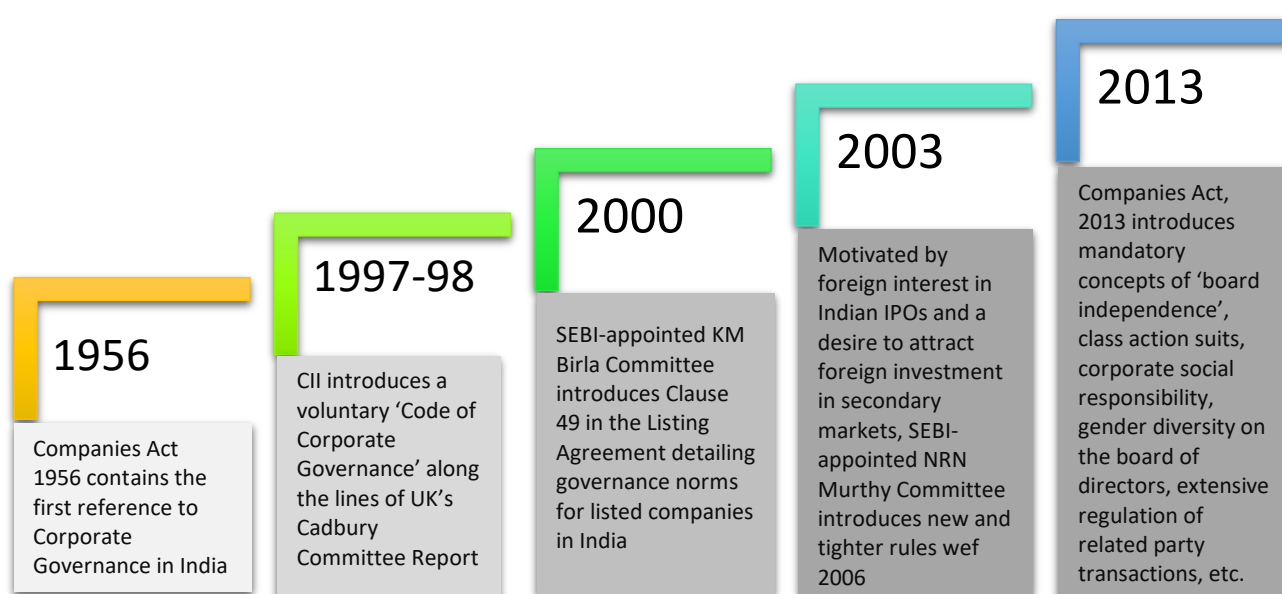
CORPORATE GOVERNANCE IN LISTED COMPANIES: FROM THE ABYSS INTO THE SUNSHINE

The concept of corporate governance can be best described as a system of checks and balances within the corporate structure to facilitate long term value creation for stakeholders (and shareholders) due to the separation of ownership and management in companies. Sir Adrian Cadbury, in the UK Commission Report: Corporate Governance 1992 has correctly referred to 'corporate governance' being concerned with holding the balance between economic and social goals and between individual and communal goals.

Evolution of Corporate Governance in India

The first reference to corporate governance in India's legal framework can be found in the Companies Act, 1956. While our corporate governance norms have been developing over various years, the 2017 World Bank 'Doing Business' report ranks India at the 13th place in terms of minority protection, attesting to the progress made on this front in the recent years.

The Satyam scandal in 2009, was a watershed moment in the history of governance regulation in India. Involving falsification of accounts by the top echelons of management and a fraud of over 1 billion dollars, this scandal motivated the Government of India to enact the Companies Act, 2013 which introduced wide-ranging changes to India's corporate governance framework.



The LODR Regulations

The enactment of the 2013 Act brought about a shift from a voluntary approach to an ultra-mandatory approach towards corporate governance, with detailed governance norms being included in the primary legislation itself. Thereafter, the Listing Agreement was replaced by the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 ("**LODR Regulations**"), which dealt extensively with governance matters, replacing the regime under Clause 49 thereof. Based on core concepts of adequate, timely and accurate disclosures of material information to all stakeholders, equitable treatment of all shareholders, recognition of the role of all stakeholders in governance, effective board supervision of the management, the **LODR Regulations** prescribed standards of governance higher than that contained in the Companies Act, 2013, given that the interests of small, retail shareholders required additional protection from acts of the majority.

Kotak Committee Report, 2017: The Watershed Moment for India's Corporate Governance Regime

Motivated by various developments across the globe in the realm of corporate governance and in continuation of its role as a proactive regulator, SEBI constituted a committee under the Chairmanship of Mr. Uday Kotak in June 2017 to suggest suitable policy and regulatory changes to enhance the efficiency of corporate governance norms for Indian listed entities ("**Kotak Committee**").

This committee submitted its report ("**Report**" or "**Kotak Committee Report**") on October 5, 2017 recommending a plethora of regulatory changes to align Indian corporate governance norms with global best practices, while being premised on local business realities unique to India, such as the prevalence of large, concentrated shareholding blocks (as opposed to a dispersed shareholding pattern observed in few developed markets such as the USA), family run businesses and "promoter-raj". In light thereof, SEBI recently amended the LODR Regulations to incorporate certain recommendations of the Kotak Committee. These changes, *inter alia*, will have the effect of increasing transparency by means of:

- Enhanced disclosure requirements (*inter alia* in respect of reasons for resignation of independent directors; proposed fees payable to the statutory auditor(s) along with terms of appointment and in case of a new auditor, any material change in the fee payable to such auditor from that paid to the outgoing auditor along with the rationale for such change; basis of recommendation for appointment including the details in relation to and credentials of the statutory auditor(s) proposed to be appointed, etc.)
- Reshaping the institution of the Board of Directors (*inter alia*, by mandating separation of office of the Chairperson and the Managing Director for the top 500 listed companies by April 1, 2020; the requirement of one independent woman director for the top 500 listed entities by April 1, 2019 and the top 1000 listed entities by April 1, 2020 etc.)
- Enhancing the role of committees of the Board of Directors
- 'Down-streaming' corporate governance to unlisted subsidiaries of listed companies by making secretarial audit mandatory for material unlisted subsidiaries incorporated in India and the mandatory appointment of an independent director of the listed parent company on the board of the material subsidiary incorporated outside India, etc.
- Increasing shareholder participation and involvement by *inter alia* mandating webcast of annual general meetings of certain companies etc.

Conclusion

Corporate governance in India has indeed come a long way. While these developments will inevitably enhance the regulatory compliance burden on companies, this is undoubtedly an impressive array of measures when viewed from the lens of corporate governance. Gone are the days when investors (*including shareholders*) would shoot in the dark with respect to their investments, relying on hearsay and tip-offs from friends and family while praying that they are not taken for a ride by the promoters and management. In marked contrast, the Indian investor of today is sufficiently empowered by robust corporate governance norms to take informed decisions. With effective implementation of the evolving norms, the evolving next phase of corporate governance in India seems to be on a fitting course.

ENFORCEMENT OF FOREIGN AWARDS IN INDIA: KEY CONSIDERATIONS

India has over time acquired a reputation as a 'difficult jurisdiction' from an arbitration perspective, especially given heightened concerns on enforcement of foreign awards and the frequent judicial intervention from Indian courts under the Arbitration and Conciliation Act, 1996 (the "Act").

The Arbitration and Conciliation (Amendment) Act, 2015 ("Amendment Act") was an attempt by the Indian legislature to address many of these factors. This article explores some of the key issues for parties to consider to ensure a smooth enforcement process of foreign seated arbitration awards in India.

- **How does the seat of arbitration impact enforcement in India?** While the Arbitration Act mandates that a foreign award can be directly enforced in India if it originates from a country which is a party to the New York Convention (Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958) and has been notified for reciprocal enforcement of awards by the Government of India, it is noteworthy that presently only 48 out of 196 signatory countries to the New York Convention have been so notified (*for list of these countries, please refer to the annexure*). Therefore, it becomes important for parties to ensure that their arbitration proceedings are seated in one of these 48 countries.
- **Which courts can arbitration proceedings be initiated in?** In order to prevent foreign parties from being dragged to lower domestic courts while challenging international arbitration proceedings and awards, the new Act now clarifies that only the High Courts – which have better trained judges and are often in the capital cities of various states – will have jurisdiction to entertain court proceedings in relation to an international commercial arbitration. Thus, for purposes of enforcement of foreign awards in India, a party must only consider the jurisdiction of the High Court in which the judgement debtor or their assets are located.
- **What is the procedure for filing of enforcement proceedings?** In the case of *Fuerst Day Lawson*,¹ Supreme Court of India has held that a sole execution application before the relevant High Court would suffice to cover the two-step process required for execution of the foreign award; i.e. (i) testing enforceability of the award in terms of sections 47 to 49 of the Act; and (ii) if the award was found to be enforceable, the procedure for execution of the award as a decree of the court. It must be noted that the execution application requires filing of the original or copy of the award (in English language), duly authenticated in the manner required by the law of the country in which the award was made, and the original or copy of the arbitration agreement, pursuant to which the arbitration was initiated.²
- **Can the enforcement of award still be challenged on the (infamous) 'public policy' ground?** Once the application for executing the award is filed, enforcement of an award can be contested on the grounds enumerated at Section 48 of the Act. While many of these grounds are similar to those contained in the New York Convention, refusing enforcement on the ground that 'enforcement of the award will be contrary to the "public policy" of India' had emerged as the most contentious (and staple) method of resisting enforcement of arbitral awards in India. To address this, the Amendment Act has now clarified that an award can be held to be against "public policy" only if (a) the award suffers from fraud or corruption; (b) conflicts with the fundamental policy or Indian law or (c) conflicts with most basic notions of morality and justice. The Amendment Act has also clarified that when judging whether an award is against fundamental policy of Indian law, the courts will not review the merits of the dispute. Following suit, the Indian courts have now become quite strict in entertaining the "public policy" argument. In *Cruz City*³ and *NTT Docomo*⁴, the Delhi High Court while upholding the foreign awards (allegedly in violation of provisions of Foreign Exchange and Management Act, 1999), noted that the violation of specific provisions of an enactment is

¹ *Fuerst Day Lawson v. Jindal Exports Ltd.*, (2001) 6 SCC 356.

² See Section 47 of the Act.

³ *Cruz City 1 Mauritius Holdings v. Unitech Ltd.*, 2017 SCC OnLine Del 7810.

⁴ *NTT Docomo Inc. v. Tata Sons Ltd.*, 2017 SCC OnLine Del 807.

not synonymous with violation of public policy of India. Similarly, in the case of *Kandla Export*,⁵ the Supreme Court has clarified that there is no statutory appeal allowed under the Act against an order enforcing foreign awards.

- **How can you secure an award during the pendency of a challenge to enforcement?** The courts have recently been willing to secure the amounts due from a judgment debtor under a foreign award, in order to ensure that the interests of award holders are protected pending enforcement. The Bombay High Court, in *Aircon Beibars*⁶, secured the sums due under a foreign award pending enforcement while noting that ‘recourse to Indian courts for interim measures in relation to a foreign seated arbitration is a transitory provision and can be invoked pending enforcement of the foreign award’. Similarly, in *TRAMMO DMCC*⁷, the Bombay High Court allowed the holder of a foreign award to apply for interim relief to a court which enjoyed jurisdiction over the assets of the judgment debtor. Additionally, any such remedies which are available in respect of a final award to a party are equally available in respect of any interim award, as Section 2(c) of the Act provides that “arbitral award” includes interim award.

Conclusion

The Amended Act is indeed a step in the right direction. The judiciary has also done its bit to uphold the intent of the legislature by passing several landmark orders recently that have fostered the faith of the parties in the enforcement process in India.

There are still issues that remain, such as the debate on enforcement of emergency awards. As an example, the concept of emergency arbitrator has not been statutorily recognised in India even under the Amendment Act, even though institutional arbitration rules in India - Mumbai Centre for International Arbitration (“MCIA”) rules and Indian Council of Arbitration rules - provide for an emergency arbitration proceeding; however, it remains as yet untried whether courts in India will enforce an award granted by an emergency arbitrator in a domestic arbitration and the judicial position as of now remains that a suit may have to be filed for seeking enforcement of such awards by emergency arbitrator.

While scepticism continues to follow arbitration processes in India, there is definitely a positive trend towards easing the ability of foreign parties to enforce their contractual rights and allowing disputes to reach a conclusion by positive enforcement of arbitral awards.

⁵ *Kandla Export Corporation & Anr. v. OCI Corporation & Anr.*, 2018 SCC OnLine SC 170.

⁶ *Aircon Beibars FZE v. Heligo Charters Pvt. Ltd.*, 2017 SCC Online Bom 631.

⁷ *TRAMMO DMCC v. Nagarjuna Fertilizers and Chemicals Ltd.*, 2017 SCC Online Bom 8676.

EMERGING TRENDS & ISSUES UNDER THE INSOLVENCY & BANKRUPTCY CODE, 2016

India's jump from Rank 130 to 100 in World Bank's ease of doing business⁸ rankings can be largely attributed to various legal reforms in the country, including the Insolvency and Bankruptcy Code, 2016 ("IBC"), which has been notified with a vision to resolve the rampant insolvency situation.

IBC essentially provides for revival of insolvent corporate entities through a corporate insolvency resolution process ("CIRP") in a time bound manner, failing which such entities undergo liquidation. Over the past one and half years, IBC has proved instrumental in addressing the corporate insolvency situation in the country. However, several crucial issues have emerged under IBC framework. With a view to address some of those issues, the Government of India promulgated the Insolvency and Bankruptcy (Amendment) Ordinance, 2018⁹ ("2018 Ordinance") on 6 June 2018. Despite this move, certain issues still remain unresolved and require proper analysis. A few critical points are discussed below.

- **In practice, is the process time-bound?** Even though IBC lays down that the CIRP has to be concluded within a period of 270 days (including an extension of maximum 90 days), the adjudicating authorities under IBC, namely the National Company Law Tribunal ("NCLT") and the appellate body, National Company Law Appellate Tribunal ("NCLAT"), across various jurisdictions have started to allow exclusion of certain days from computation of this period 'if the facts and circumstances justify such exclusion', largely due to increased litigation on various unsettled issues under IBC. The NCLAT has also laid down a few grounds as illustrations for claiming such exclusion (for example, if CIRP is stayed, or resolution professional is not functioning). This has made strict adherence to the timelines contemplated under IBC a practical challenge. The press release issued by the Government¹⁰ with respect to the 2018 Ordinance stated that further clarity would be brought about vide regulations laying down mandatory timelines, processes and procedures for CIRP by addressing some of the specific issues including non-entertainment of late bids, no negotiation with the late bidders and a well laid down procedure for maximizing value of assets. The existing regulations, once amended, to bring in place the proposed strict timelines will need to be examined.
- **Is the Limitation Act, 1963 applicable to proceedings under IBC?** The law relating to limitation of suits and other legal proceedings is covered under the Limitation Act, 1963 ("Limitation Act"). IBC earlier did not clearly set out whether the Limitation Act was applicable to the proceedings under it. Though NCLAT had in the matter of *Speculum Plast Private Limited. v/s PTC Techno Private Limited* (Speculum Case) held that the Limitation Act was not applicable to the proceedings under IBC, an appeal was referred to the Supreme Court. Pending the appeal, the 2018 Ordinance has shed some light on this issue by making the provisions of the Limitation Act applicable to the proceedings under IBC. The status of various applications pending before the NCLTs and pending appeal before the NCLAT or the Supreme Court may need to be seen in view of this newly inserted provision, especially since the new provision does not clarify whether the pending applications are protected under this provision. Also, the status of various applications which could not be filed in light of the Speculum Case, needs to be clarified. Interestingly, the NCLAT in the Speculum Case had observed that even if the Limitation Act were to be made applicable to IBC, the period of limitation of 3 years as per the Limitation Act would begin to run from the date when the right to apply under IBC accrued, i.e. 1 December 2016 (when IBC was notified). If the NCLTs take a cue from these observations of the NCLAT, could it mean that virtually no application can be rejected on the grounds of expiry of limitation period until 1 December 2019 or 3 years from the date of enforcement (6 June 2018) of the 2018 Ordinance?
- **Obligations on the insolvency professional?** IBC has provided various obligations upon an insolvency professional including keeping the corporate debtor as a going concern. In addition, the 2018 Ordinance has cast another responsibility for complying with the requirements under any law for the time being in force on behalf of the corporate debtor. In many instances, the regulator (Insolvency and Bankruptcy Board of India) has imposed penalties on insolvency professionals who have failed to comply with their obligations. However, as a practical matter, insolvency professionals (being individuals) may find it difficult to ensure strict compliance with IBC rules and

⁸ As per the World Bank Group Flagship Report on Doing Business, 2018

⁹ The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018 (No. 6 of 2018), dated 6 June 2018

¹⁰ Issued by the Ministry of Corporate Affairs on 6 June 2018

regulations therein, as sole responsible persons appointed for the purpose. We may expect a change in the existing rules and regulations permitting a corporate body or a firm to be appointed as an insolvency professional to run the CIRP. Such an amendment would enable safeguarding and ring fencing the value of a corporate debtor under CIRP.

- **Mandatory sale of shares of existing shareholders in a resolution plan?** As per the provisions of IBC, a resolution plan may provide for the measures required for implementing it, including but not limited to the substantial acquisition of shares of the corporate debtor. It will be an interesting situation to see whether a contemplation in the resolution plan to require the sale of shares of an existing shareholder/promoter can be made binding against such shareholder/promoter, especially as IBC makes the resolution plan binding against the shareholders. In fact, IBC also provides that a provision in a resolution plan which would otherwise require the consent of the members or partners of the corporate debtor, under the terms of the constitutional documents of the corporate debtor, shareholders' agreement, joint venture agreement or other document of a similar nature, shall take effect notwithstanding that such consent has not been obtained. These provisions seem to largely undermine the rights of the shareholders of the corporate debtor, especially when IBC has been introduced as a *non-obstante* law.
- **What are the difficulties in withdrawing an application under IBC?** Until the 2018 Ordinance, the language under IBC did not specifically provide for withdrawal once a petition for initiation of CIRP against a corporate debtor was admitted. Many parties had explored the settlement options after their cases were admitted. The NCLAT and Supreme Court of India had also allowed withdrawal on a case-by-case basis, which led to plethora of litigations. The Supreme Court had been exercising its powers under Article 142 of the Constitution of India (which gives it the power to pass orders for doing complete justice) to allow withdrawal. The 2018 Ordinance now provides for withdrawal after admission of an application under IBC, subject to the approval of the Committee of Creditors ("COC") with 90% of the voting share. Since the procedure for such withdrawal has not been laid down yet, it will be interesting to see whether this mechanism proves viable, in practice. Also, keeping such a high threshold for withdrawal may pose practical difficulties, especially for operational creditors who do not form part of the committee of creditors.
- **Whether moratorium is applicable to personal guarantor?** IBC provides for applicability of 'moratorium' upon the admission of an application by the NCLT against a corporate debtor. The moratorium is essentially a period wherein no suits or proceedings for recovery, enforcement of security interest, sale or transfer of assets, or termination of essential contracts can be instituted or continued against a corporate debtor. However, whether personal guarantee of the corporate debtor can be invoked pending the proceedings under IBC and in the light of the moratorium, was a question that created a lot of stir. While the Allahabad High Court in *Sanjeev Shriya v/s State Bank of India & Ors*, and *Deepak Singhania & Anr v/s State Bank of India*, ("**Sanjeev Shriya Case**") vide order dated 6 September 2017 had answered the question in negative, with the ratio that while the liability of guarantors is co-extensive, but the entire proceeding which is going on before IRP under IBC is still in fluid stage and for the same cause of action, two split proceedings cannot go simultaneously before the debt recovery tribunal as well as NCLT. The 2018 Ordinance has intended to resolve the confusion, by stating that moratorium shall not apply to the surety in a contract of guarantee to a corporate debtor. This move could, however, give rise to multiple parallel proceedings as certain creditors would choose to rather invoke the guarantee than wait for CIRP to conclude. This might also lead to reconstitution of many COCs which have already been formed. It will also be interesting to see how the guarantors parallelly run two proceedings in light of the ratio of *Sanjeev Shriya case*.
- **Whether operational creditors have any say in CIRP?** As per IBC, the resolution plan requires approval from the COC which is constituted of financial creditors only even if there are operational creditors; however, in case there are no financial creditors, the COC comprises of operational creditors. There can be circumstances where a corporate debtor may have higher exposure of operational debt than financial debt – in such a scenario, it is not right to allow only the financial creditors to have the ability to adopt or reject a resolution plan. The 2018 Ordinance has in fact brought the allottees of any real estate project within the ambit of the "financial creditors". Such allottees would also enjoy the rights available to a financial creditor such as forming a part of the COC and voting during the CIRP, but the operational creditors have been kept out of it.
- **Criteria for eligibility of 'resolution applicant': too stringent?** With an aim to put in place certain safeguards to prevent unscrupulous, undesirable persons from misusing or vitiating the provisions of IBC, amendments have been made vide the Insolvency and Bankruptcy Code (Amendment) Act, 2018 and further by the 2018 Ordinance, to IBC to keep-out such persons who have wilfully defaulted, or are associated with non-performing assets, or are habitually non-compliant and, therefore, are likely to be a risk to successful resolution of insolvency of a company.

However, the grounds for eligibility of such a resolution applicant have been made quite stringent – given that the amendment is new, and its effects are still being tested, there is an apprehension that it might become impractical for bona-fide resolution applicants to submit a resolution plan, thereby defeating the spirit of IBC for revival of insolvent corporate entities. The 2018 Ordinance however states that the eligibility criteria as amended thereunder shall apply to the resolution applicant who has not submitted a resolution plan as on 6 June 2018. It would mean that the eligibility criteria applicable to the resolution applicants who have already submitted a resolution plan would be different from the eligibility criteria applicable to the resolution applicants who are yet to submit a resolution plan vis-à-vis the same corporate debtor. This might lead to an unfair advantage to certain resolution applicants over the others, so far as their eligibility criteria is concerned.

- **Special resolution (75%) under Section 10 (*suo-moto* initiation of CIRP by corporate debtor)?** Section 10 of IBC contains a provision whereby the corporate debtor itself can file an application for initiation of CIRP. This provision was earlier misused by certain promoters to avoid the attachment of their personal property which was secured against the loan facilities availed by the corporate debtor by obtaining an order of admission and hence moratorium. In order to rectify this shortcoming, the 2018 Ordinance has inserted a requirement of special resolution of the shareholders of the corporate debtors to trigger insolvency resolution under Section 10 of IBC. Given that this change is nascent and has not been tested, in case of a typical joint venture structure (51%-49%), just one JV partner of a loss making JV may find it difficult to invoke the provisions of Section 10 of IBC for initiating CIRP.

Conclusion

IBC has brought about various welcome changes in the insolvency regime in India, such as incorporation of insolvency professional entities (“**IPE**”), through which both Indian and foreign insolvency professionals can provide services, thereby increasing the pool of talented and experienced insolvency professional in the country. In fact, IBC also contemplates and contains provisions whereby the Indian Government can enter into bilateral treaties with other countries for application of IBC to assets or property situated outside India.

Further, with a view to boost the micro, small and medium sector enterprises (“**MSME**”), the 2018 Ordinance has empowered the Government of India to provide a special dispensation under IBC. The immediate benefit it would provide is that, it would not disqualify the promoter to bid for his enterprise undergoing CIRP, provided he is not a wilful defaulter and does not attract other disqualifications not related to default. It has also empowered the Central Government to allow further exemptions or modifications with respect to the MSME Sector, if required, in public interest.

Though it is true that there are various gaps which need to be filled and various practical difficulties which need to be addressed under IBC, it has so far proved to be effective in meeting its purpose. As this law evolves, it is likely to further boost India Inc’s corporate governance practices and help the country optimally address the widespread problem of mounting corporate debt.

COMPETITION LAW ROUNDUP - KEY DEVELOPMENTS

CCI allows 100% exemption from penalty under Competition Commission of India (Lesser Penalty) Regulations, 2009 ("Lesser Penalty Regulations")

The CCI, for the first time, has granted a 100% exemption from penalty in a leniency case. In *re: Cartelization in respect of zinc carbon dry cell batteries market in India vs. Eveready Industries India Ltd & Ors*, Panasonic received 100% exemption from penalty, Eveready and Nippo received 30% and 20% exemptions, respectively.

Google penalized for abuse of dominance

The CCI in its recent decision has imposed a penalty of INR 136 crore on Google Inc., Google India Ltd., and Google Ireland for abuse of dominance i.e. for violation of Section 4 of the Act, by a majority of 4:2. The CCI found that Google was not displaying its search results by relevance, amongst other issues. The minority order, on the other hand, stated that there was not enough evidence to prove that Google had abused its dominance.

Mens rea not an essential ingredient for violation of Section 43A of the Competition Act, 2002 ("Act")

The Supreme Court in the matter of *Competition Commission of India vs. Thomas Cook (India) Ltd*¹¹, reiterated that a penalty for breach of a civil obligation, as attracted under Section 43A of the Act, does not require *mens rea* as an essential ingredient. Thomas Cook was penalized by the CCI for non-notification of its demerger/amalgamation and share purchase settlement forming part of the same transaction. Thomas Cook had notified only a part of the transaction and had later claimed exemption under Section 5 of the Act for the remainder part of the same transaction. The CCI, under Section 43A of the Act imposed a penalty of INR 1, 00,00,000, which was upheld by the SC.

Supreme Court holds on objective justification in abuse of dominance cases

The Supreme Court in the matter of *Competition Commission of India vs. Fast Way Transmission*¹², indicated that though the conduct of the Respondent was in contravention of Section 4 of the Act, i.e. abuse of dominance, the conduct was objectively justified and hence no penalty should have been imposed. Fast Way Transmission had failed to telecast the Informant's channel in violation of its agreement with the informant. Fast Way Transmission had justified its failure to telecast the channel due to the limited available transmission space and informant's low TRP rating.

Power of review/recall of the CCI available only before receiving investigation report of the DG

The Delhi High Court, in the matter of *Cadila Healthcare Limited vs. Competition Commission of India*¹³, has clarified that the power of review/recall of its order, which was conferred upon the CCI by the Delhi High Court in *Google Inc. vs. Competition Commission of India*¹⁴ was not available after the report of the Director General has already been received by CCI.

Government companies in oil and gas sectors exempted from application of combination provisions of the Act

Vide notification dated 22 November 2017, the Government has exempted combinations under Section 5 of the Act involving Central Public Sector Enterprises operating in the Oil & Gas Sector as per the Petroleum Act, 1934 from the application of provisions of Sections 5 and 6 of the Act. This exemption is applicable for the period of five years, i.e., till 22 November 2022.

Nationalized banks exempted from application of combination provisions under the Act

The Government vide notification dated 30 August 2017, exempted nationalized banks from application of combination (merger control) provisions of the Act, for a period of ten years.

Lesser Penalty Regulations amended to include individuals

The CCI has suitably amended the Lesser Penalty Regulations to include individuals as well enterprises, who are now covered under the regulation for imposition of lesser penalty under the Act.

Government decides to downsize the CCI

The Union Cabinet in April 2018 expressed its intention to downsize the CCI eventually have one Chairperson and three Members (from one Chairperson and six Members currently under the Act). This decision, according to the government, is aimed at achieving 'minimum government - maximum governance'. However, no legislative action has been initiated in this regard so far.

Diagnostic tool for procurement for officers

The CCI has issued this guideline document in March 2018, to act as a guide to the Act. It is aimed at functioning as a practical guide for procurement officials who can use it for review of the public procurement system.

¹¹ Civil Appeal No.13578 of 2015

¹² Civil Appeal No. 7215 of 2014

¹³ WP(C) No. 2106 of 2016

¹⁴ LPA No. 733 of 2014

GENERAL DATA PROTECTION REGULATION: IMPACT ON INDIA-BASED BUSINESSES

General Data Protection Regulation (“**GDPR**”), approved and adopted by European Parliament in April 2016, is a ‘rights based’ data protection model which allows the users to have greater rights over his/her data. This came into force on May 25, 2018 GDPR and is today an important topic for most businesses, given the extra-territorial reach of these regulations. This article explores some of the key facets of GDPR and highlights pertinent points.

- **Applicability:** Primarily, GDPR lays down rules in relation to protection of natural persons with regard to their personal data. The GDPR is applicable not only to organisations located within the European Union (“**EU**”), but also applies to organisations located outside of the EU if they ‘process’ personal data of EU subjects as a ‘controller’ or a ‘processor’, and where the processing activity relates to (a) offering of goods or services (including for free) to data subjects in EU; or (b) monitoring their behaviour if the behaviour takes place within EU.¹⁵

Even though GDPR is fairly wide in its scope, mere website accessibility of a service in the EU is not sufficient to trigger its application. However, factors such as offering a service in the languages or currencies used in a member state (if not also used in the third country) or mentioning customers or users in a member state may trigger application of the GDPR.

- **Processing of personal data:** ‘Processing’ in the context of GDPR means any operation or set of operations which is performed on personal data or on sets of personal data, whether or not by automated means, such as collection, recording, organisation, structuring, storage, adaptation or alteration, retrieval, consultation, use, disclosure by transmission, dissemination or otherwise making available, alignment or combination, restriction, erasure or destruction.
- **Data Protection Principles:** GDPR lays down specific data protection principles for processing of personal data. Each ‘controller’ and ‘processor’ needs to ensure that the personal data is (a) processed lawfully, fairly and in a transparent manner, (b) collected for a specific, explicit and legitimate purpose, (c) adequate, relevant and necessary in relation to the purposes for which it is collected, and (d) accurate and is kept up to date. There is not only a requirement to comply with the prescribed principles but the ‘controller’ should be able to demonstrate the compliance.
- **Obligation to comply with GDPR:** The obligation to comply with the above principles is not only on the entity collecting personal data of EU subjects but also the entity which stores, transmits, alters, uses such personal data on behalf of the data controller.
- **Lawful data processing under GDPR:** Data processing will be considered lawful under GDPR if the data subject has given consent to the processing of personal data for one or more specific purposes. But mere consent of the data subject is not sufficient. The controller shall be able to demonstrate that the data subject has provided the consent. The request for consent by the controller shall be presented in a manner which is clearly distinguishable from other matters, in an intelligible and easily accessible form, using clear and plain language.¹⁶ The data subject shall also have the right to withdraw his/her consent at any time, and it shall be as easy to withdraw consent as it is to give consent.
- **Sensitive personal data:** Information which is considered specifically sensitive such as racial or ethnic origin or physical or mental health condition etc. cannot be obtained, stored, transmitted, processed, unless *explicit consent* for processing of such personal data has been provided by the data subject for one or more specified purposes.

¹⁵ Article 3 of GDPR

¹⁶ Regulation 7 of GDPR

Thinking Ahead to Minimize Exposure And Liabilities

Key takeaways for India-based organisations

The world's 500 biggest corporations are on track to spend a total of \$7.8 billion to comply with GDPR, according to consultants Ernst & Young.¹⁷ In light of the significant compliance cost and burden, companies need to start thinking about the impact on their business model and pricing strategies.

Penalties under GDPR: GDPR imposes substantial penalties for non-compliance of the above principles. In case of a breach, an entity can be fined up to the higher of 4% of annual worldwide turnover and EUR20 million. GDPR implements a tiered approach – other specified infringements would attract a fine of up to the higher of 2% of annual worldwide turnover and EUR 10 million.

Immediate To-Do's: Some of the steps that Indian organisations falling within the ambit of GDPR can take are:

- ✓ Have in place a standard operating procedure (SOP) for ensuring day-to-day compliance
- ✓ Provide training to employees to sensitise them on the risks to business from GDPR non-compliance
- ✓ Put in place a mechanism to deal with notification of data breaches
- ✓ Adopt a robust security management system and monitor the system on regular basis
- ✓ Adopt a procedure for collecting and storing employee data if such employees are EU subjects.

These measures may not be exhaustive but will help Indian businesses in taking a step in the right direction.

GDPR provides the data subjects greater access to ascertain the manner in which their data is processed. Each controller is now required to maintain a record of processing activities under its responsibility and there are stringent conditions prescribed for notification of the personal data breaches. Given the strict compliance norms and the quantum of penalty involved, it has become imperative for organizations to have dedicated teams for ensuring ongoing GDPR compliance.

GDPR's extra-territorial application could potentially have a significant impact on Indian organisations, making it critical for companies to analyse and assess whether GDPR is applicable to them. The sectors which are most likely to be affected are IT and ITeS services, business process outsourcing (BPO) units, e-commerce companies catering to customers in EU etc.

¹⁷ <https://www.bloomberg.com/news/articles/2018-03-22/it-il-cost-billions-for-companies-to-comply-with-europe-s-new-data-law>

RECENT TRENDS IN ANTI-DUMPING INVESTIGATIONS

India is a frequent user of anti-dumping measures, having levied duties on 609 investigations since the inception of the World Trade Organization (“WTO”) in 1995. There have been several changes in the trend of anti-dumping duty investigations conducted by Directorate General of Trade Remedies (“DGTR”) recently.

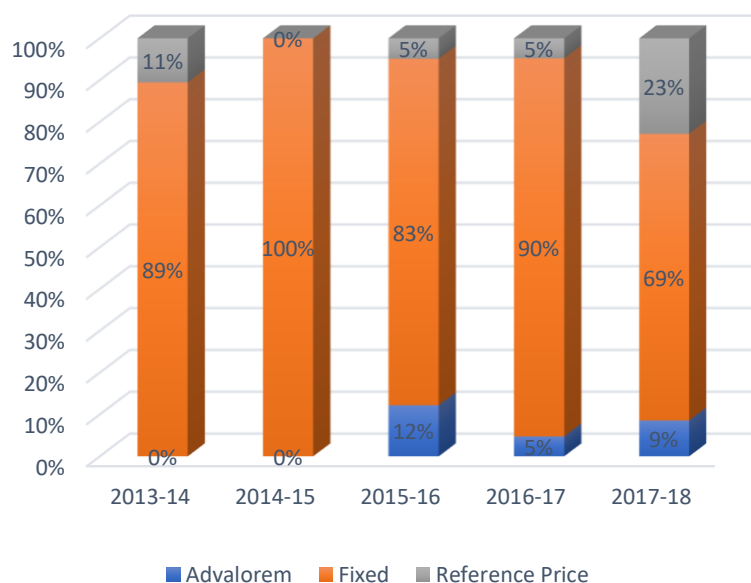
Consolidation of trade remedy forums and creation of DGTR

- The Government of India, through an amendment to the *Government of India (Allocation of Business) Rules, 1961* on May 7, 2018, has consolidated multiple trade remedial forums under the umbrella of the “Directorate General of Anti-Dumping and Allied Duties” (“DGAD”).
- The DGAD, previously in charge of conducting anti-dumping and anti-subsidy investigations, has accordingly been rechristened the DGTR.
- The amendment creates a single integrated authority which will oversee both outbound as well as bound investigations on various trade remedial measures such as anti-dumping, anti-subsidy, safeguards and quantitative restrictions.

Greater flexibility on ‘form’ of duty

- Three forms of duties under the anti-dumping framework are ‘fixed duties’ (fixed duty in USD per unit); ‘*ad valorem* duties’ (a fixed percentage of duty based on value); and ‘reference price duties’ (duty being levied based on the difference between the benchmark and import prices).
- While India has historically favoured fixed duties for a majority of its anti-dumping levies, in recent times the Hon'ble Designated Authority has been considering different forms of anti-dumping duties at the time of recommending duties by way of final findings, in order to seek a balance between interests of all involved parties on a case to case basis.

Form of Duty over the last 5 years



Impact of different ‘forms’ of duties:

Depending on the market behaviour, product characteristics and performance of the domestic producers, using the right form of duty can help maintain a fair balance between the interests of the domestic industry and the importer/user industries.

For example, fixed duties can sometimes be disproportionately punitive in cases where price trends show an increase during the course of the investigation and after that, whereby importers would have to continue bearing a fixed duty rate even when their import prices are not causing injury – in such a case, a reference price benchmark would be much fairer.

Source: www.dgtr.gov.in

Reduction in duration of duty levy to 3-years

- The DGTR has the discretion to impose duties up to five years.
- Since April 2017, there have been five separate cases (out of thirty-six investigations) where the DGTR has recommended duties only for three years, taking a balanced position between the interests of the domestic industry and the interests of the opposing parties.
- Prominent illustrations: Reference Price: MEK¹⁸, Ofloxacin¹⁹, O-Acids²⁰

Record 'No Duty' recommendations made by the office of the DGTR

- Since the year 2017-18, there has been a considerable increase in the proportion of cases where the DGTR has recommended 'No Duty' on at least one of the subject countries involved.
- The largest impact of 'No Duty' recommendations has been observed in sunset reviews in over 45% of the cases in the year 2017-18 and 100% thereafter (3 sunset reviews issued in April and May 2018).
- For the first time in the last five years, there were also four instances of the DGAD rejecting applications for sunset reviews in 2017-18.

Increasing focus on imports from Preferential Tariff Agreement sources such as Japan, Korea, Malaysia, Thailand and others

- With the signing of the various preferential tariff agreements, there has been a consistent increase in trade volumes and value between signatory countries. This has inevitably led to an increased focus on these countries during anti-dumping investigations.
- Once such example is the Japan-India Comprehensive Economic Partnership Agreement and its impact on Japan's increasing prominence in India's anti-dumping investigations – there has been an increase of approximately 300 % for anti-dumping investigations for imports originating in Japan in year 2017-18 when compared to previous year.
- At the same time, 'No Duty' results constituted 37.5% of these findings – consistent with the 36% ratio overall – which is promising.
- Prominent Illustrations: Hot Rolled flat products of alloy or non-alloy steel²¹, Caustic Soda²²

Impact of Brexit on trade remedial targeting

- The DGTR has, in recent years, maintained a steady focus on European Union ("EU") as one of the subject countries in its anti-dumping investigations.
- With Brexit looming around the corner, it is likely that the United Kingdom ("UK") will no longer be subjected to the same duties that are presently applicable to imports from the EU except during the transition period subject to specified terms and conditions. However, the Indian model of levying duties provides for combination duties recommended for cooperating producers and/or exporters involved in exports to India.
- Another important factor is that India's duties are levied on imports 'originating in' or 'exported from' a subject country. While the implications of origins are clear, 'exported from' can mean the country from where the product is invoiced or shipped. This has a direct impact on UK based exporters in two ways post-Brexit:
 - Exports to India which originate in the EU but are invoiced/shipped from the UK will continue to remain within the purview of previously levied duties
 - Exports to India which originate in the UK but are invoiced/shipped from the EU will also continue to remain within the purview of previously levied duties
- Lastly, there is always the possibility of fresh levies being proposed specifically against the UK.

18 Final Finding in the Anti-dumping investigation concerning imports of "Methyl Ethyl Ketone" or MEK, originating in or exported from China PR, Japan, South Africa and Taiwan dated February 1, 2018.

19 Final Finding in the Anti-dumping duty investigation on the imports of Ofloxacin originating in or exported from China PR dated December 22, 2017.

20 Final Finding in the Antidumping investigation concerning imports of O-Acid originating in or exported from China PR dated December 19, 2017.

21 Final Finding in the Anti-dumping investigation concerning imports of "Hot-Rolled flat products of alloy or non-alloy steel" originating in or exported from China PR, Japan, Korea RP, Russia, Brazil and Indonesia dated April 10, 2017.

22 Final Finding in the Anti-Dumping Investigation concerning imports of Caustic Soda originating in and exported from Japan and Qatar dated January 10, 2018.

INTERNATIONAL TRADE - SECTORAL HIGHLIGHTS FROM INDIA

Per the latest economic data, India's global trade has increased by 16.32% to USD 767.9 billion in 2017-18. As India continues to create a modern, vibrant economic framework for business, developments in international trade law can have far-reaching impact on local companies and their competitiveness on the global stage. This risk gets even more amplified in light of India's growing integration in the global economy. Notable highlights pertaining to several emerging industrial sectors are enumerated below:

Electric Vehicles

- Government of India ("GoI") is likely to extend incentives to the tune of USD 1.4 billion for promoting use of electric vehicles under the Faster Adoption and Manufacturing of Hybrid and Electric Vehicles in India ("FAME") – II Scheme
- The GoI is planning to offer capital investment subsidy of 20% - 25% (proposal is currently awaiting cabinet approval)
- While this surely will augment the market for electric vehicles in India, it remains to be seen whether the scheme would have any domestic content requirement which may trigger WTO-incompatibility issues

Textiles and Clothing

- India acquired export competitiveness in textiles by crossing the 3.25% threshold in 2010. As per WTO law, it is expected to phase out export subsidies in this sector by the end of 2018
- The GoI is currently devising strategies for subsidising to producers/exporters that will be compliant with WTO law
- While it remains to be seen what programs/schemes are formulated by the GoI, the Indian textile sector would need to compete aggressively in the world market once the current subsidies are phased out

E-Commerce

- India is one of the fastest growing B2B and B2C e-commerce markets. The recent Walmart-Flipkart deal proves the huge potential of this market in India
- While India formally opposed any new negotiation on e-commerce at MC11 until the outstanding issues of Doha Ministerial Agenda are resolved, it has ignited discussions to set-up a task force to finalize comprehensive set of recommendations by September 2018
- The task force includes representatives from several technology and e-commerce players. This is a good time to file representations before the GoI to put forward views of various stakeholders, given the complexities surrounding e-commerce, including customs clearance, data localisation, market access and consumer protection

Renewable Energy

- India has developed one of the world's largest renewable energy program with an ambitious target of developing a capacity of 175 GW by 2022
- While the DSB report in DS 516 required India to phase-out subsidies contingent on domestic content requirement, the GoI has been planning to come up with WTO-consistent support schemes to incentivise solar cells/modules manufacturers and solar power developers
- Industry can expect few schemes/programs soon from the GoI making this market more attractive for global renewable energy players to set up manufacturing facilities in India

Electric and IT Equipment manufacturing and Make in India

- Indian electrical equipment industry exceeded USD 25 billion and contributes nearly 1.5% of India's overall GDP
- The GoI has promulgated a Preferential Market Access ("PMA") policy for electronic products. The policy provides preferences to domestically manufactured electronic products. This is WTO consistent till such time that the GoI uses the procured products without a view to commercial resale or use in production of goods for commercial sale
- To promote manufacturing in India, the GoI, in February 2018, hiked customs duties on certain IT products, including smartphones and smartwatches, by 15-20%
- WTO Members have raised their concern on this increase as they view it as being inconsistent with India's obligations under the Information Technology Agreement of the WTO

WTO Challenge to India's export subsidy schemes

- The United States has complained and alleged that some of the key exports subsidies of India under its Foreign Trade Policy including Export Oriented Unit, Special Economic Zones scheme and Merchandise Exports from India scheme are prohibited export subsidies
- The consultations between both countries have been concluded and a formal request by the United States to establish a panel is likely to be placed on DSB agenda sometime in 2018
- Should India be unable to defend its schemes successfully, it would have major ramifications on India's foreign trade policy and would require a complete overhaul of its subsidy programs

India's Public Procurement and Preferential Market Access Policies

- In 2017, the GoI introduced a public procurement policy with an aim to promote manufacturing and production of goods and services in India
- The policy, which includes domestic content requirements, is currently being used by the railways and defence sectors
- To the extent that procurement is limited to governmental agencies, this scheme is consistent with India's commitment at the WTO. Presently, India is not a signatory to the WTO Government Procurement Agreement
- Notably, this policy should not be confused with the PMA policy which has been adopted for the electronics, steel and telecommunication sectors

DEFENCE & AEROSPACE: ANALYSING THE OPPORTUNITY IN INDIA

Driven by an ambition of creating a local military-industrial complex in India, Defence & Aerospace has been a priority sector for the government over last several years and has been the subject of frequent policy and regulatory updates in response to various industry concerns. Along with large procurement programs, the urgent need to focus on war preparedness – as highlighted by an internal report submitted by Minister of State for Defence last year – is expected to boost the business case for creating an even more enabling framework for private sector participation.

There are several encouraging signs:

- Swifter decisions by Defence Acquisition Committee for purchasing equipment for the armed forces (many of these purchases are being made from Foreign OEMs and Ordnance Factories to enable quicker deliveries, followed by a 'Make-in-India' purchase)
- Delegation of power to Secretary (DP) for Tier I sub-vendors in certain specified scenarios, and to Army Commanders for securing bases of armed forces
- Formation of a high-level 'Defence Planning Committee' under the Chairmanship of National Security Advisor and membership of the Foreign Secretary, three Service Chiefs, and the Secretary (Expenditure), Ministry of Finance, to draft the national security strategy and facilitate a comprehensive and integrated planning for defence matters, including in-country capacity creation
- In a clear indication of its desire to focus on exports of indigenous equipment, India invited all of its 44 'Defence Attaches' posted across the world for a specialised briefing along the side lines of the recently concluded DefExpo 2018, for exploring new markets for indigenous defence equipment and promoting 'Make-in-India' (India is already in talks with Vietnam for export of its Akash Surface to Air Missile)

Emerging opportunities for the industry

The Government has taken many encouraging steps to bring the defence manufacturing sector out of its present state of inertia; however, the effects of these steps will only be felt in the medium to long term. The present focus on purchase of arms and ammunition is succinctly limited to addressing the immediate war preparedness. This, however, will not yield the desired results for the market stakeholders – India's Ministry of Defence ("MoD") and Armed Forces to achieve the much-elusive self-reliance and the Industry (both foreign and Indian) to have enough orders to keep their factories running. To this end, the following developments are noteworthy:

- **FDI liberalisation:** A much-awaited decision pertains to increasing the FDI cap from the present 49% to now 74% - this proposal is contained in the Defence Production Policy 2018, a draft of which was circulated by Department of Defence Production ("DDP"), Ministry of Defence for comments to the public. However, the draft has not yet been notified in light of conflicting views from the industry. If this proposal gets notified, a significant number of concerns envisaged by foreign defence manufacturing companies are likely to be addressed under India's corporate laws framework applicable to 74% holding structures. Concerns of domestic industry, however, are not misplaced and will need to be resolved.
- **Swifter discharge of offset obligations:** The government has invited comments on Draft Modifications to Defence Offset Guidelines wherein the Ministry of Defence has proposed three additional avenues for discharge of offsets (investment in Specified Projects, invest in defence manufacturing through equity investment, and investment in specified SEBI regulated Funds for Defence, Aerospace and Internal Security), which, if notified, are likely to ease access to funds and technology and benefit foreign vendors by providing quicker ways of discharging offset obligations. Furthermore, a draft amendment modifying the Offset Procedure proposes very high multipliers (4/5) for all investments made in the Defence Industrial Corridors towards discharge of an OEM's offset obligation.
- **Announcement to setup Defence Industrial Corridors:** In February 2018, Government of India announced setting up of Defence Industrial Corridors ("DIC") in two states in India (Tamil Nadu and Uttar Pradesh). Investment in these

Corridors is likely to attract many incentives such as 10-25% reimbursement of land cost, 70-90% GST reimbursement, etc., details of which are under finalisation - Defence Production Policy 2018 - This Policy was expected to be publicly announced and notified at DefExpo 2018 in Chennai earlier this year. When notified, the Policy has several measures including Competency Mapping of Indian Industry, simplifying MAKE II procedure, liberalising licensing norms, including lifetime support for large platforms which would enable making a credible business case for Industry, etc. and stands to benefit all the stakeholders in the industry.

The Road Ahead

While there are several positive developments that signal the Government of India's increasing business-friendly attitude toward this sector, legacy issues persist. The government had earlier introduced the 'Make' procedure under DPP 2006 for boosting indigenous defence manufacturing – as it happened, not a single program was finalized under this initiative. The recent 'Strategic Partnership' model – introduced with much fanfare as the 'mother of all out-of-box policies' – seems set for a similar fate with the first RFI issued under this program already awarded to Mazagon Dock Shipbuilders Ltd, a Defence Public Sector Undertaking.

These developments have further boosted the industry's scepticism on the government's intent and have been quite a pushback to Government's intent to induce pace in this sector. While focusing on immediate preparation for a worst-case scenario of a two-front war is critical, Government of India will need to be mindful of its long-term aim for the sector at large and thus will have to take concrete, definitive steps to reassert its intent to the Industry.

SUMMARY OF JUDICIAL DECISIONS DEFINING THE INDIRECT TAX LANDSCAPE IN INDIA

Indian tax litigation landscape assures a plethora of court rulings, given the 24 High Courts and various benches of the Tribunal pronouncing verdicts on a regular basis. Broadly speaking, various issues involved in all types of indirect taxes levied (in the pre-GST era) pertained to classification, valuation, taxability, benefits of exemptions and/or Notifications/Circulars, eligibility of CENVAT credit, input tax credit, refund/rebate/drawback, availability of various schemes under the Foreign Trade Policy for the promotion of exports from India, constitutionality of entry tax, etc. These issues *inter alia* constitute the major litigation defining indirect taxes landscape in India.

Pursuant to the roll out of GST wef 01 July 2017, the judiciary has been instrumental in disposing of the cases in relation to the erstwhile legislation expeditiously. New Tribunal Benches have been formed and Tribunal Members have resorted to faster ways of disposal of cases by clubbing matters involving similar issues and bulk disposals. Adjudicating authorities and First Appellate Authorities have been transitioned into GST regime and rigorous training is imparted for faster understanding of the new legislation and resolution of queries/issues.

A few of the recent landmark judgments have had industry-wide ramifications for the indirect tax landscape in India. These are summarised below.

State of Kerala & Others vs. Fr. William Fernandez & Others

11.10.2017

TS-296-SC-2017-VAT

Supreme Court upholds levy of entry tax on imported goods - 'Origin' of goods held as irrelevant for chargeability of taxes

- The Supreme Court of India ("SC") upholds levy of entry tax on goods imported from outside the country into local areas for consumption, use or sale, under entry tax acts of Orissa, Kerala and Bihar.
- Concludes that "goods imported after having been released from customs barriers are not immune from any kind of State Taxation, which fall equally on other similar goods", thus rejecting the assesses' contention that such immunity shall continue till goods reach the premises where they are to be taken for consumption, sale and use.
- Legislation is concerned only with entry of goods into a local area for consumption, use or sale, and the 'origin' of goods has no relevance with regard to chargeability of entry tax.
- This judgment is likely to force companies to reassess their sourcing and supply chains and re-visit pricing for goods being imported for local consumption in an area.

The Supreme Court of India held that Entry Tax legislations are within the competence of State Legislatures and do not "intrude the legislative domain of Parliament as reserved in Entry 41 & Entry 83 of List I".

SC rejected the applicability of Original Package Theory as developed by American Supreme Court in case of *Brown vs. State of Maryland* and observed that import comes to an end when goods enter into customs frontiers of India and are released for home consumption and hence, entry tax is leviable under Entry 52 of List II.

Commissioner of Trade & Taxes, Delhi vs. Arise India Ltd.

11.01.2018

TS-2-SC-2018-VAT

Supreme Court upholds High Court's quashing of Input Tax Credit disallowance to bona-fide purchaser for seller's default.

- SC dismisses Revenue's Special Leave Petition and refuses to interfere with order of Delhi High Court ("HC") that held Section 9(2)(g) of Delhi VAT Act - to the extent it disallows Input Tax Credit ("ITC") to purchaser due to default of selling dealer in depositing tax - as violative of Articles 14 and 19(1)(g) of the Constitution of India.
- According to the HC, Section 9(2)(g) gave a free hand to Department in deciding to proceed either against the purchasing dealer or selling dealer. In the present instance, the defaulting party was the selling dealer for which the purchasing dealer was expected to bear the consequence. HC observed that failure by Legislature to distinguish between bona fide and non-bona fide purchasing dealers resulted in Section 9(2)(g) applying equally to both the classes of purchasing dealers, which was certainly hit by Article 14 of Constitution.

- SC grants liberty to Revenue to move the HC with particulars of cases where purchase transactions are not *bona-fide* to have the matters therein remitted back to the competent authority.
- This judgement is a big relief to all the *bona-fide* purchasing dealers across different industries, who could otherwise be held liable for default by the selling dealers

M/s JSW Energy Limited (Maharashtra)

Advance Ruling Authority [No. GST-ARA-05/2017/B-04]

- The conversion of coal (supplied by M/s Jindal Steel Limited to the Applicant) into power is considered to be a “manufacture” under GST Act as the product undergoes a complete transformation and electricity is a new commodity which is delivered to M/s Jindal Steel Limited.
- Supply of power by the Applicant is not covered under the ambit of job work and shall be considered as a supply between related persons.

M/s Deepak & Co. (New Delhi)

Advance Ruling Authority [No. 02/DAAR/2018]

- Supply of food served on-board trains shall be considered as pure supply of goods and levied to GST according to individual GST rates
- Supply of newspaper shall attract ‘nil’ rate of GST in accordance with Notification No. 2/2017-Central Tax (Rate) dated June 28, 2017
- Supply of food in stalls of platform at the rates fixed by Indian Railways shall be classified as “supply of goods” and not as “supply of service” and leviable to individual rates

These cases are shaping the indirect tax framework in the post-GST era in India and are vital for providing clarity to many of the new provisions under this Act. Tax Litigation in India is in a volatile state at present; however, with time, many of the issues will stabilize and a cleaner and a transparent system as envisaged by the Government. The ‘One Nation One Tax’ dream is on its way to be realised.

INDIA'S PHARMACEUTICALS SECTOR: FACING HEADWINDS

Indian pharmaceutical industry accounts for 3.1- 3.6 % (value terms) and approximately 10% (volume terms) of the global industry and is expected to grow to USD 100 billion by 2025. The pharmaceuticals market in India comprises of medical drugs (generic drugs -70 %; Over-the-counter medicines - 21%; patented drugs - 9%) and medical devices, etc, with prevalence of loan licensee model (drug manufacturing outsourced to licensed manufacturer). This industry has contributed immensely to Indian as well as global healthcare, being material in manufacturing critical, high-quality and low-cost medicines, with exports of USD 16.84 billion in 2016-17 (expected to reach USD 20 billion by 2020²³).

Introduction of GST in India in July 2017 with a view to overcoming the tax inefficiencies prevalent under the earlier regime has had far reaching implications for the industry. With the onset of GST, pure economic and commercial considerations have taken prominence over tax cost considerations in deciding the operation and distribution structures, all of which has triggered structural changes within the industry in terms of product plant re-allocation, depot rationalisation, etc.

Challenges under the GST regime

The GST journey has been a rather bumpy ride for the industry - without undermining the inherent GST-related benefits, it is important to also underscore the corresponding challenges that need to be addressed:

- **Multiple credit blockages:** Contrary to the promise of seamless credit, there are potentially multiple credit blockages qua transactions peculiar to the industry involving distribution of free samples, disposal/ destruction of expired stock, control samples and testing samples. Further, for organisations which have operations spread across different States, having a proper mechanism for distribution of credits pertaining to common expenses (which includes, royalty payments, technical fees, advertisement expenses) to its each location for discharging the output tax liability becomes important.
- **Inaccuracies in tax rates:** Contrary to the objective of replicating the pre-existing rate structure in terms of the 'equivalence principle', there have been inaccuracies, including for certain orthopaedic and surgical items and life-saving drugs, to name a few, which have been taxed at a higher rate, thereby impacting the transaction costs.
- **Suspension of tax concessions:** With GST, the tax concessions extended under the earlier tax regime to manufacturing facilities set up in certain backward regions for incentivizing investments, have been suspended mid-way, with only marginal benefit correlated to the GST levied by the Centre being recompensed back.
- **Anti-profiteering provisions:** These provisions, constituted with the benevolent objective of ensuring percolation of tax cuts under GST to the end consumer, have been a nightmare to comply with, owing to limited guidance and complex trade dynamics. Up till now, several entities have been slapped with notices for proving proper compliance, and the threat of prescribed penal consequences continues to loom.
- **Continuation of several legacy issues:** While the industry is in the process of adjusting to these changes, there are certain legacy issues under the erstwhile tax regime which have continued under GST – these include classification of certain OTC medicines as 'drug' or 'cosmetics', where 'cosmetics' attract a significantly higher tax rate, and, treatment of research activities outsourced to India as "exports" (i.e. zero-rated).

The Indian pharmaceutical industry's proven track record of achieving continuous growth amidst the challenging environment, complemented by the Indian government's resolve and commitment to simplifying the tax and regulatory environment is a positive bell weather for this industry. However, challenges continue to loom.

The industry has had its share of issues with the customs administration in the recent past. Some illustrations include, disputing the valuation of samples imported for non-commercial use (example, for stability testing), the controversial

²³ As per news article- <https://www.businesstoday.in/sectors/pharma/india-plans-measures-to-facilitate-drug-exports/story/274428.html>

denial of the benefit under Served From India Scheme (“SFIS”) correlated to service exports made by Indian entities (rendering R&D services) to its foreign affiliate entities. Additionally, the extent of scrutiny of cross border transactions (including rigid country by country reporting norms) from an anti-avoidance and transfer pricing perspective, has seen a manifold increase, which is also true for indirect acquisitions of India-based entities.

New policy initiatives by the government

- **Medical Device Rules, 2017:** In an effort to promote domestic manufacturing of medical devices of world standard, the Medical Device Rules, 2017 (“Rules”) were notified on January 31st, 2017. These Rules came into effect on January 1, 2018 and should help the industry by enabling greater access to the market in India as well as abroad. Prior to introduction of the Rules, medical devices were governed solely by the Drugs and Cosmetics Act, 1940 which were not customised to suit the needs of the medical devices industry.
- **New pharma policy:** This is expected to bring about exhaustive reform of rules and regulations governing pharma and medical devices with the goal of ensuring that ease of doing business and ease of living can go hand in hand. It is expected that domestic manufacturers will be given a push with policy aimed at encouraging end to end domestic manufacturing, including preference in public procurements. Also, quality control mechanisms would be gradually streamlined to foster better control over quality while at the same time removing systemic bottlenecks.
- **Protecting consumer interest:** In light of heightened scrutiny by US regulators, there have been a spate of amendments to the Drugs and Cosmetics Act, 1940 which appear to be aimed at achieving stricter scrutiny of drugs by the Government before their entry into the market.
- **New pharma pricing policy:** The government has sought views of experts on whether the National List of Essential Medicines (NLEM) should be linked to the Drug Price Control Order (“DPCO”), to ascertain which drugs are to come under price control and how price caps should be determined. The intent is to overhaul the drug pricing system to ensure a transparent pricing structure for essential medicines.
- **National database of pharma manufacturers:** India's drug regulatory body - Central Drugs Standard Control Organization (“CDSCO”) - is creating a national digital database of pharmaceutical manufacturers and their medicines so that regulators can be more effective when acting on problems like drug shortages and quality issues.

The FDC controversy

The industry and Govt have constantly engaged to find the right balance in the regulatory domain as well. In March 2016, the Central Government issued 344 notifications prohibiting at a single stroke, the manufacture and sale of 344 Fixed Dose Combination (“FDC”) drugs. IPI petitioned various High Courts resulting in quashing of all 344 notifications by the Hon’ble High Court of Delhi.

In the second round, the Government appealed before the Supreme Court and also filed transfer petitions seeking transfer of pending matters in other High Courts. The Supreme Court, in a detailed judgment referred all 344 FDCs as well as others which were subject matter of proceedings pending before the Madras High Court to the statutory body competent to examine the same.

Such examination is currently underway, and the issue will hopefully be resolved in a timely manner to assure both the industry about the future of FDC business as well as the patients who use many of these FDCs for treatment of highly infectious diseases.

Conclusion

Challenges to Indian pharmaceutical industry are manifold, and companies will have to re-invent their strategies to remain relevant in the market. Increased domestic and international regulatory compliance requirements; emerging concerns around data privacy and pricing; increasing M&A and consolidation; heightened concerns from a competition law perspective; emerging policies on pricing, etc. have all added to the headwinds faced by the industry. However, these changes, if legislated and implemented with the proper intent, should help the industry emerge as a potent force on the global landscape.

ANNEXURE

List of signatories to the New York Convention (Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958) notified by Government of India

- Australia
- Austria
- Belgium
- Botswana
- Bulgaria
- Central African Republic
- Chile
- China (including Hong Kong and Macau)
- Cuba
- Czechoslovak Socialist Republic
- Denmark
- Ecuador
- Federal Republic of Germany
- Finland
- France
- German Democratic Republic
- Ghana
- Greece
- Hungary
- Italy
- Japan
- Kuwait
- Mauritius
- Malagasy Republic
- Malaysia
- Mexico
- Morocco
- Nigeria
- Norway
- Philippines
- Poland
- Republic of Korea
- Romania; Russia
- San Marino
- Singapore
- Spain
- Sweden
- Switzerland
- Syrian Arab Republic
- Thailand
- The Arab Republic of Egypt
- The Netherlands
- Trinidad and Tobago
- Tunisia
- United Kingdom
- United Republic of Tanzania
- United States of America
- United Arab Emirates

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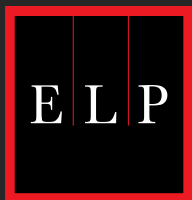
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