



Authors:

Suhas Srinivasiah

suhas.srinivasiah@bgl.kochhar.com

Ajay Prasad

ajay.prasad@bgl.kochhar.com

Deepesh

deepesh.d@kochhar.com

US-India Partnership in the Defence Sector under the Atmanirbhar Bharat

Background and about Atmanirbhar Bharat

The idea of Atmanirbhar Bharat, or self-reliance, was at the heart of the Hon'ble Prime Minister of India, Shri Narendra Modi's address to the nation on 12 May 2020 when he announced an economic package towards building a Atmanirbhar Bharat, or a self-reliant, resilient India. It is basically a re-enforcement of 'Make in India' concept with more benefits for encouraging private participation in various sectors, escalating Foreign Direct Investment in the defence sector and many more.

India has now embarked on a journey of self-reliance to enable business survival and continuity and transform India into a hub for global manufacturing and services with strong supply chain that will make India attractive for foreign investments.

Objective of Atmanirbhar Bharat is not to oust US Companies

The mission of Atmanirbhar Bharat is not being self-centric but being self-sufficient. Atmanirbhar Bharat does not suggest cutting off relations from global platform, instead it enables Indian economy to adapt to the present problems caused by the pandemic and develop global opportunities for a post-COVID world.

Further, it is not so much self-reliance, but ensuring that domestic products match their imported counterparts in cost and quality. To aid the objective, the Government of India has also announced various initiatives and reforms to help and promote the US – India partnership in India.

Recent initiatives/reforms undertaken by the Indian Government to promote the Defence Sector under the Atmanirbhar Bharat

Increase in Foreign Direct Investment ("FDI") limit in defence production from 49% to 74%.

The Hon'ble Finance Minister of India, Smt. Nirmala Sitharaman recently announced a slew of reforms in eight major sectors including Defence. One such reform in the Defence Sector was to raise the FDI limit in defence production from 49% to 74%.

Thereafter, on 17 September 2020, the Department for Promotion of Industry and Internal Trade ("DPIIT"), Ministry of Commerce and Internal Trade issued a press note permitting FDI in defence production up to 74% under the automatic route subject to certain conditions, the key being security clearance by the Ministry of Home Affairs and as per guidelines of the Ministry of Defence.

This is a welcome move by the Government of India and there is a belief that global defence players will now set up manufacturing hubs in India and bring niche technology without hesitation as the firms will have majority and controlling stakes in their Indian subsidiaries.

India to become Global Hub for Aircraft Maintenance, Repair and Overhaul (MRO).

The Government of India aims to increase the aircraft component repairs and airframe maintenance to Rs. 2000 crores (USD 271 million). To support this initiative, major engine manufacturers are expected to set up their engine repair facilities in India in the coming years.

The US – India defense partnership in the past decade

The US – India defense trade increased from roughly USD 1 billion to over USD 15 billion. This included procurement of: (a) thirteen C-130 Hercules aircraft from Lockheed Martin; (b) ten C-17 Globemaster; (c) twelve P-8 Poseidon aircraft from Boeing; and (d) twenty-two AH-64 Apache and fifteen CH-47 Chinook helicopters.

The two countries also entered into contracts for the procurement of 145 US

made M777 ultra-light howitzers which are likely to be deployed at the highly volatile India-China border, in the regions of Arunachal Pradesh and Ladakh (in Jammu and Kashmir). The M777s, which have been used by US forces in Afghanistan and Iraq, will help India secure its borders with China.

The US – India defense partnership in the year 2020

Pre-Atmanirbhar Bharat

Earlier this year in February 2020, India hosted the Hon'ble President of the United States, Mr. Donald Trump. During the visit, President Trump announced a defense deal of more than USD 3 billion, under which India will buy additional U.S. military equipment, including MH-60R naval and AH64E Apache helicopters. This was followed by a subsequent announcement in April 2020 where US approved sale of:

- missiles, torpedoes worth USD 155 million;
- ten AGN Harpoon Block 11 air-launched missiles worth USD 92 million;
- MK54 All Up Round Lightweight Torpedoes and three MK 54 Exercise Torpedoes worth USD 63 million. Post –Atmanirbhar Bharat

In July, there were reports that India may buy MQ-9 Reaper (Predator B) armed drones under toned down US Export restrictions.

Further, the Government of India has said it is committed to work towards achieving a USD 26 billion defense industry by 2025. Thus, the wider US – India ties will continue to be the lodestar for the

Challenges faced by US Companies in India

US Companies have been and are staunch supporters of all major initiatives of the Hon'ble Prime Minister of India, Mr. Narendra Modi including "Make in India",

“Skill India” and “Digital India” and made invaluable contributions to the Indian economy over the past several years. They have long term plans to contribute to India's defence sector and its economy.

However, some of the most common challenges and difficulties which create an impediment for the US Companies on future business decisions are summarized as under:

I. Verification of Offset Credits:

The US companies have been submitting offset claims in a timely manner but unfortunately never received any offset credits and a limited number of verifications of their claims. This presents a problem because until offset credits are awarded, it exposes the Companies to heavy penalties and will adversely affect future business decisions.

II. Imposition of penalty:

The un-timely decisions in the verification of offset claims, results into imposition of penalty by the Defence Offset Management Wing ('DOMW') of the Ministry of Defence. The imposition of penalty leads to highly adverse media coverage, negative publicity which is disparaging to the image and reputation of the US companies.

It is not all bad news as far as offset is concerned and there are positive developments on the anvil. Certain amendments have been introduced to the Defence Offset Guidelines to rationalize the penalties and the consequences of not fulfilling the offset requirements. A foreign vendor may request re-phasing of the offset obligations within the period of the offset contract. The first re-phasing request of the vendor will be processed without any disincentives if the spread of re-phasing is restricted up to the following

year. However, if the re-phasing of offset value is proposed over the subsequent years, then 5% additional obligation will be imposed on re-phased value of every year. The re-phasing request for second and subsequent attempts will be processed by imposing 5% on proposed yearly re-phased offset value irrespective of the spread of re-phasing. This yearly additional 5% offset obligation for processing re-phasing request will be over and above the outright financial penalty on short fall specified in the Defence Offset Guidelines. It will be ideal if the Government amends the guidelines/regulations to include the 5% penalty within the overall financial penalty.

Further, in order to make the defence procurement process more efficient, the Government intends to set up a Project Management Unit to support contract management, formulate general staff qualitative requirements of weapons/platforms and increase the trial and testing procedures

US companies have long-term plans for India and if correct policy amendments such as the ones mentioned above are undertaken, India can expect substantial investments in the defence sector from US Companies which would lead to creation of jobs for thousands of people and infusion of state of the art and futuristic defence technology.

Conclusion

Atmanirbhar Bharat is a welcome philosophy and needs to be put in practice. India is one of the biggest importers of defence goods. While reduction of import dependency is a welcome step, what must also be taken into consideration is the capability of the existing ordnance factories and the public sector undertakings to meet the current requirement of the Armed Forces. It is also

important to ensure that any restrictions placed on import of defense equipment and goods (like banning any weapons or platforms) does not put India to a competitive disadvantage vis-à-vis its rather unfriendly neighbours.

President Trump's visit to India was an important reaffirmation of the US-India strategic partnership. However, critical requirements and operational capabilities required to meet external threats will need to remain at the top of the priorities, especially since the two countries face a joint challenge of the fragile global strategic environment created by the pandemic on their respective territories.

A high-level cooperative US - India relationship, buoyed by security and defence cooperation activities, is one that can and should be replicated by the world order to maintain global peace and harmony.

Suhas Srinivasiah is a Senior Partner and a founding member of Kochhar & Co. Bangalore. Ajay is a Principal Associate in the corporate law practice at Kochhar & Co. Bangalore and Deepesh is a Principal Associate in the Dispute resolution & Litigation law practice at Kochhar & Co. Delhi.
