India

Piyush Joshi has multi-sectoral experience in both project development and project financing transactions. He has advised on the development, financing, operations and maintenance of projects in the energy sector (power, renewable energy, natural gas sectors), urban infrastructure sector (urban planning, township development, urban transport, metro railway networks, tramways, bus rapid transit, regional railways networks, urban mobility), and environment infrastructure sector (municipal solid waste projects, landfill development, landfill capping and landfill reclamation projects). Piyush also specialises in providing strategy and approach for addressing complex project disputes. He has authored the book *Law Relating to Infrastructure Projects* (LexisNexis – Butterworths).

RV Anuradha heads the team on international trade and investment, and climate change, and has advised on the development and financing of environment infrastructure projects and agreements for sale of carbon emission reductions generated from such projects. She advises both government and private sector clients on legal issues arising from India's engagement at the World Trade Organization and other trade and investment agreements, including on international trade and investment disputes.

Sumiti Yadava focuses on project development and project financing transactions, and general corporate law. She blends her knowledge of corporate law with sector specific laws, to enable effective structuring of project transactions and investments in the infrastructure sector. Sumiti has extensive experience in the natural gas sector, urban infrastructure sector and the environment infrastructure sector, including on disputes arising in these sectors.

1 What have been the trends over the past year or so in terms of deal activity in the project finance sector in your jurisdiction?

'Project financing', in terms of 'non-recourse' project financing as prevalent in more evolved markets, does not exist in India. This is because the regulatory requirements governing lending require promoter guarantees and undertakings, as well as other recourse outside of the relevant project. As a result, there is no complete reliance on project and project revenues, and the term 'project financing' in India has morphed to refer to any form of financing of infrastructure projects generally. Furthermore, financing of infrastructure projects is primarily undertaken by banks, which are public sector undertakings (PSUs), controlled by either the government of India or state governments.

The 2020 Union Budget (2020 Budget) has sought to create higher incentives for investments in the infrastructure sector by creating a framework for 100 per cent tax exemption for sovereign wealth funds of foreign governments in respect of their interest, dividend and capital gains income from investments made in infrastructure, on the condition that such funds are invested for a minimum period of three years.

The 2020 Budget has also announced a National Infrastructure Pipeline that intends to comprise of over 6,500 infrastructure projects to boost infrastructure development. The details of these projects are awaited and are expected to be disclosed in the near future.

In an acknowledgement of the increasing importance of natural gas in the Indian Energy basket, the 2020 Budget has announced that the national gas grid will be expanded from 16,200 kilometres to 27,000 kilometres and a national level natural gas exchange will be developed.

Another important element of the 2020 Budget was the announcement of future public–private partnership (PPP) expansion of Indian railways to enable expansion of freight transportation and the development of a national cold supply chain for perishables such as meat, milk and fish and equipping freight trains with refrigerated coaches.

The 2020 Budget also prioritised inland waterways for development to enable economic development along rivers.

However, because of the inherent risks in investing in India, the general trend has been for project developers predominantly taking on the role of executing projects as contractors or sub-contractors, where there is revenue certainty and a buffer from the risks to which infrastructure development is exposed to in India. Strategies for mitigating legal risks has always been a core function of a project finance lawyer. This has been gaining higher significance in India in view of 'public interest litigation' (PILs) against infrastructure projects. Judicial rulings resulting

Piyush Joshi

RV Anuradha

Sumiti Yadava

"The 2020 Union Budget has sought to create higher incentives for investments."

from PILs may lead to uncertainty of enforcement of long-term contracts. As a result, a project finance lawyer in India needs to be adept at developing strategies for handling dispute resolution scenarios and advising on long-term risk mitigation measures.

In our comments in the 2018 edition of this *Market Intelligence*, we discussed the example of a PIL that impacted a toll road project in India. A key highlight in the past year that has had an impact on the regulatory landscape for projects relates to regulatory actions to address non-performing assets (NPAs) across all sectors. The government's one-size fits all solution of declaring all stressed assets as NPAs and triggering the insolvency process is premised on blame-apportionment on the promoter or developer of a project. This, however, does not account for the underlying regulatory and policy bottlenecks that are often responsible for the stressed assets in the first place. With regard to gas-based power plants in India, a recent report of a Parliamentary Committee has examined the issue and observed that policy flip-flops by the government have had a crippling effect on private sector investments in this sector. The report recommends several steps for the government to address the same. This could potentially provide the basis for a

Photo by Md Shairaf on Unsplash

more nuanced and sector-specific approach to resolving the stressed assets issue. However, concrete solutions are yet to emerge

In the meantime, the absence of clear solutions for the gas power projects stranded since 2018 has resulted in the only foreign investment in the natural gas power generation sector in India crystallising into a bilateral investment treaty dispute. Korea Western Power Company Limited (KOWEPO), which had invested in Pioneer Gas and Power Limited, has sent the Indian government a notice of arbitration under the investor-to-state dispute settlement provisions of the India–Korea Comprehensive Economic Partnership Agreement in December 2019, alleging, inter alia, that the absence of clear gas allocation practices adopted by the government, has resulted in violation of the commitments to a foreign investor.

2 In terms of project finance transactions, which industry sectors have been the most active and what have been the most significant deals to close in your jurisdiction?

The most active infrastructure sectors in the past year have been city gas distribution, roads, highways and airports.

City gas distribution

In city gas distribution (CGD) sector, the ninth and tenth bid rounds were successfully concluded by the Petroleum and Natural Gas Regulatory Board (PNGRB), wherein 128 geographical areas, spread across the country, were awarded among 19 successful bidders during the ninth round and 12 successful bidders during the tenth bid round. With the completion of the tenth CGD bidding round, CGD networks will now be developed for more than 70 per cent of the country's population across 228 geographical areas spread over 27 states and union territories. It is expected that over the next five years, this will result in availability of gas for domestic, commercial and industrial use across the country thereby being a critical factor for overall growth. The CGD sector has captured the interest of large industrial houses and private sector investors in India. The provision of marketing exclusivity and infrastructure exclusivity within the identified geographical area is a material factor for generating interest from the private sector in the CGD projects.

Following the success of the tenth CGD bid round, the PNGRB has initiated the 11th CGD bidding round and has released a list of 44 geographical areas that may be offered for bidding in the course of 2020.

Highways

In the 2020 Budget, development of additional 2,500 kilometres of access controlled highways, with an additional 200 kilometres of strategic highways, is envisaged.

The National Highway Authority of India (NHAI) introduced the Toll Operate and Transfer (TOT) model for partnership with private developers in the road sector, under which NHAI passes on the toll collection rights and operation and maintenance obligations for 30 years to the private developer against payment of upfront, one-time, lump sum concession fees quoted by the private developer as part of the bidding process. This has attracted investments in existing and operational roads, the most significant of which was the investments by Australia's Macquarie Group in a bundle of nine highway projects in the states of Andhra Pradesh and Gujarat. The bid won by Macquarie Group is for an amount of 96.8 billion rupees, as against the base bid price of 60.5 billion rupees set by NHAI. The second round of TOT bidding that had an aggregate of 586 kilometres of national highways in the states of Rajasthan, Gujarat, West Bengal and Bihar and a base price of 53.6 billion rupees after certain extensions and delays concluded in December 2018 with Cube Highways submitting the highest bid of 46.1 billion rupees with other bids by Adani and IRB Infrastructure Developers being lower at 36.7 billion rupees and 27.1 billion rupees. This reflects the liquidity issues being faced in the infrastructure and financial markets since second quarter of 2018. This resulted in the second TOT bid process being cancelled in February 2019, as the highest bid received in December 2018 (of Cube Highways of 46.1 billion rupees) was lower than the base price of 53.62 billion rupees. The third round of the TOT bid was held in second half of 2019 and Cube Highways submitted the highest bid of 50.11 billion rupees and was awarded the TOT package.

Aviation

Airport development has been another core area of focus. The Airport Authority of India (AAI), which is a statutory authority responsible for airport infrastructure in India, undertakes certain projects on its own and, like the NHAI, bids out other projects. AAI had undertaken a competitive bidding process for selection of a private operator to undertake development of six government owned airports of Ahemdabad, Jaipur, Mangaluru, Thiruvananthapuram, Lucknow and Guwahati, all of which were won by the Adani Group. This is expected to result in an investment of 2,600 billion rupees in the airport sector.

Another development in the aviation sector is that of the government's efforts to launch disinvestment in Air India – the government owned airline. Air India's dismal financials have however been a disincentive and the government's first attempt to divest did not attract any bidders. Plans to transfer Air India's debt worth 290 billion rupees to a special purpose vehicle (SPV) are being considered as a

precursor to reviving the disinvestment process. The disinvestment was expected to be undertaken in 2019, however the failure of Jet Airways in 2019 destabilised the Indian aviation sector and the disinvestment of Air India is now expected to be implemented in 2020.

3 | Which project sponsors have been most active in driving activity? Which banks have been most active in providing debt finance?

Photo by Towering Goals on Shutterstock

With regard to City Gas Distribution, large private sector industry groups, such as Adani and Torrent, participated and submitted bids for several geographical areas – going toe-to-toe with large public sector undertakings such as Indian Oil Corporation, GAIL (India) Limited, Bharat Petroleum Corporation Limited and Hindustan Petroleum Corporation Limited. In the 9th round, the maximum geographical areas were won by Adani Gas Limited at 13, with Torrent winning nine areas. In 2019 the tenth round of CGD bidding was undertaken, covering 50 geographical areas that were awarded to 12 successful entities. Nine of the geographical areas were awarded to the Indian arm of the Manila-based Atlantic Gulf & Pacific Company of Manila Inc. HPCL and

> "The participation of banks in the financing of infrastructure sectors in India continued to be severely constrained."

IOCL were also among the successful bidders. In 2019, the Mundra LNG Terminal was commissioned, bringing the total number of operational LNG terminals in India to six – Dahej, Hazira, Dabhol, Kochi, Ennore and Mundra – of which five are on the west coast along the Arabian Sea and one (Ennore) in the East Coast. However, nine more LNG terminals are under various stages of development.

The participation of banks in the financing of infrastructure sectors in India continued to be severely constrained, carrying on from 2018 primarily on account of Reserve Bank of India (RBI) tightening norms relating to refinancing. The RBI had issued a circular titled 'Resolution of Stressed Assets – Revised Framework' in February 2018 (RBI Stressed Assets Circular) directing banks to trigger insolvency proceedings under the Insolvency and Bankruptcy Code (IBC), 2016 in respect of projects or corporate debtors having dues aggregating to 20 billion rupees or more (taking principal and interest into account). This resulted in a severe liquidity crunch for infrastructure projects, which require refinancing every few years particularly in light of revenue and expenditure mismatch in operations, manifesting in a domino impact of defaults by projects and multiple promoters and financing institutions.

One of the most significant upheavals in the financial services sector was the collapse, under liquidity stress, of Infrastructure Leasing & Financial Services Limited (IL&FS), which was India's largest non-banking financial services company engaged in the financing of infrastructure projects. The government sought to present the IL&FS crisis as a consequence of mismanagement and fraud. However, after two years of investigations, it is becoming clear that collapse of IL&FS was a result of liquidity crisis that can be attributed to specific actions of the government itself, as well as the RBI, which resulted in severe shortage of refinancing liquidity. The collapse of IL&FS had a debilitating impact on the funding availability for infrastructure projects and the system is still to recover from the same.

The RBI Stressed Assets Circular was challenged at the Supreme Court and, in April 2019, the Supreme Court, in the matter of *Dharani Sugars and Chemicals Ltd v Union of India*, struck down the RBI circular as ultra vires the provisions of the Banking Regulation Act, 1949. The ruling was a welcome respite to various debtors against whom action had been taken pursuant to the RBI Stressed Assets Circular. It is expected that by 2022 or 2023, some further developments will have occurred to alleviate the crisis of financing in the infrastructure sector.

4 What are the biggest challenges that your clients face when implementing projects in your jurisdiction?

The biggest challenges in implementing projects in India are legal risks relating to enforceability of long-term agreements in India and procurement of land required for the project.

As discussed in our response to question 2, judicial interference with executed long-term contracts through the use of PIL poses a significant challenge in implementation of projects in India. Another aspect of concern is availability of land, which has always been an issue in relation to infrastructure projects in India. The government has been developing structures whereby the land is either pooled or acquired by a government authority in advance and leased to the identified developer project to mitigate the land risk that has stalled and delayed projects across sectors.

The World Bank's Ease of Doing Business Reports (EDOIB) have consistently identified the main bottlenecks in India as being the difficulties in obtaining construction permits, enforcing contracts and resolving insolvency issues. However, India has jumped 14 places to reach rank 63 in the EDOIB in 2020 on the basis of recent regulatory developments.

The risk of having a business plan that essentially has the government of India or state government or other government authorities as counter-parties came into sharp focus with the events relating to IL&FS, as recounted in question 3. A majority of the more than 300 infrastructure projects being implemented by IL&FS were facing revenue shortfalls and delayed payments or ongoing disputes that had locked up more than 100 billion rupees in disputes. The government took over the company alleging mismanagement by the then-existing management claiming that over-leveraging was undertaken in a reckless manner. However, the plan to overcome the revenue shortfall being presently contemplated by the new Board of Directors of IL&FS, which was of selling all the existing infrastructure projects and was expected to result in a large number of infrastructure sector acquisition transactions in 2019. However little progress was made in this regard in 2019 and sale process of only five asset bundles of IL&FS are under process. The collapse of IL&FS, which was earlier touted to have been because of fraudulent management practices and sought to be labelled as a ponzi scheme, appear to be attributable to more systemic issues resulting in a liquidity crisis precipitated, in part, by the directions of RBI and the failure of the government to understand requirement of refinancing of infrastructure projects, particularly in light of the constraints of Indian banking sector that had only limited long term institutional lenders. It is expected that the issues finally find some resolution over the next two to three years.

5 Are there any proposed legal or regulatory changes that may give rise to new opportunities in project development and finance? Do you believe these changes will open the market up to a broader range of participants?

India has a fairly liberalised regime across all infrastructure sectors. However, private sector participation in development and financing has been limited.

As explained in answer to question 4, legal risk mitigation is a core area that needs to be addressed in any project in any sector. Equally, there are regulatory incentives and opportunities that we highlight to our clients. These include:

- evolution of the regulatory framework governing infrastructure financing funds, which are funds established with the specific purpose of financing the development of infrastructure;
- enactment of regulations to facilitate issuance of municipal debt and listing of debt securities by municipalities in India;
- liberalisation of the foreign direct investment regime, which has led to majority of infrastructure sectors being open to 100 per cent foreign direct investment;
- creation of regulatory framework for the pooling of land in most states as an alternate to cumbersome land acquisition process; and
- greater focus on urban infrastructure and development of specific framework in several states in India relating to urban infrastructure.

> "Logistics development has been receiving increasing focus from the government."

Logistics development has been receiving increasing focus from the government with the establishment of a Department of Logistics under the Ministry of Commerce and Industry. Multilateral financing institutions, such as the World Bank and the Asian Development Bank, are collaborating with the government to accelerate the focused development of this sector. The World Bank's Logistics Performance Index ranks India at 44 worldwide. India's ratification of the WTO's Trade Facilitation Agreement (TFA) in 2016 was accompanied by the establishment of a National Committee on Trade Facilitation (NCTF) to act as a national level body, which could facilitate effective domestic coordination and implementation of TFA provisions. In 2017, India adopted the National Trade Facilitation Action Plan, which, inter alia, addresses areas of infrastructure augmentation – particularly the road and rail infrastructure leading to ports and the infrastructure within ports, airports, inland container depots and land customs stations, for which various ministries like Shipping, Civil Aviation, Railways, Road Transport and Highways, Home Affairs, Finance and Commerce have been assigned specified targets.

One of the major changes in the legal framework governing infrastructure sector projects in India has been the introduction of section 20A in the Specific

Relief Act 1963 by the Specific Relief (Amendment) Act 2018, which introduced a special framework for contracts relating to infrastructure projects. It has now been stipulated under section 20A(1) Specific Relief Act 1963 that infrastructure projects cannot be stopped by way of injunctions by courts in suits seeking specific relief. This provides a much-needed protection against the implementation of infrastructure projects being held up on account of disputes with construction contractors or under other contracts. Section 20B Specific Relief Act 1963 provides a framework for the government to designate or create one or more courts specifically for trying suits relating to infrastructure projects, while also mandating that suits relating to infrastructure projects be disposed within a period of 12 months from the date of service of summons to the defendant. This framework is much-needed relief to protect infrastructure projects from delays on account of litigation and have contributed a great deal in mitigating litigation risks associated with development of infrastructure projects in India.

Photo by Vivek Dhanda on Unsplash

6 What trends have you been seeing in terms of range of project participants? What factors have influenced negotiations on commercial terms and risk allocation? Are there any particularly innovative features?

The CGD sector has seen robust interest from private sector participants for the first time since CGD geographical areas started being authorised pursuant to competitive bid process.

However, the impact of IL&FS issues (as discussed in question 3) that have arisen in 2018 and the manner in which the sale of the various infrastructure projects that were being implemented by the IL&FS Group would be undertaken and may result in availability of a large number of developed infrastructure projects for potential inventors in 2020. What remains to be seen is how the issues relating to liability, representation and warranties, and revenue flows relating to such projects are eventually resolved with respect to the investors coming in.

Sectors such as transportation and urban infrastructure rely significantly on government funding schemes. As explained in our response to question 1, there are regulatory requirements for banks to seek promoter guarantees and undertakings, and there are no exclusive, non-recourse project financing deals in India.

In order to enable development of suitable structures, it is critical for the risks and regulatory issues surrounding the sector to have been, if not resolved, then at least quantified and contained. The creation and success of an equity investment platform for national highways in India by Cube Highways clearly indicates the potential for creation of similar platforms for other major infrastructure sectors, if the risks and regulatory issues in those sectors can be suitably mitigated and contained.

7 What are the major changes in activity levels or new trends you anticipate over the next year or so?

In the energy sector particularly the LNG and natural gas sector, the trend has shifted to short- to medium-term contracts rather than long-term contracts. The ever-evolving and developing technologies are having impact on various infrastructure sectors from natural gas to urban transportation.

It is expected that 2020 will see the rise of distributed LNG projects and usage in India, which would enable larger parts of the country to participate in the gas chain and enable offtake and use of LNG. What was earlier limited to or possible by pipeline connectivity, may in 2020 change to and be made possible by smaller scale and lower capital-intensive distributed LNG projects, enabling development of virtual pipelines by fleets of LNG trucks and allowing for conversion of larger commercial vehicles to LNG-based fuel.

In public transport, with the growth of electric vehicles, the requirement for supporting infrastructure and consequential management and disposal of used-batteries will grow. The growth of waste to energy is likewise expected in 2020 to tackle the issue of rapid growth in municipal solid mixed waste and shortage of land in urban areas in India.

Logistics development will continue to see further progress, with the collaboration between the government and multilateral agencies including the World Bank and the Asian Development Bank.

The National Digital Communications Policy (NDCP), announced in September 2018, is another significant development that envisages infrastructure convergence of IT, telecom and broadcasting. The policy details measures such as amending the Indian Telegraph Act 1885 and other relevant acts for the purpose of convergence in coordination with respective ministries, and establishing a unified policy framework and spectrum management regime for broadcast and broadband technologies. Convergence will also require appropriate restructuring of legal, licensing and regulatory frameworks. The NDCP seeks to establish a National Digital Grid, which will be regulated by a National Fibre Authority. Implementing the NDCP will witness legal and policy review and amendments, which is expected to translate into attracting private sector investments in communications infrastructure.

Overall, in the area of project development and project finance, we see private sector role as focusing on the role of contractors, sub-contractors or service providers, rather than actual project development. Projects that are vested with the government or a government authority and bid out for various specific scope of works such as design, construction, refurbishment, operation, toll collection and maintenance are likely to increase across roads and highway sector and also the airport sector. This would be a sensible and practical approach in order to mitigate the exposure of the private sector to risks relating to land, clearances and legal risk of court interference.

The restructuring and reorganisation of stranded or suspended infrastructure projects is an activity that will increase and receive more attention in the next few years as both project developers and project lenders seek to unlock the trapped investments and potential values from infrastructure projects that are either stranded or have been suspended or mothballed over the past decade. It is expected that the use of the IBC 2016 by lenders to stranded or suspended projects will lead to spurt in restructuring opportunities.

Investment in infrastructure is clearly a national priority for the government. For instance:

"With the growth of electric vehicles, the requirement for supporting infrastructure and consequential management and disposal of used-batteries will grow."

- states and PSUs have been encouraged to enter into power purchase agreements for renewable energy;
- there are aggressive plans for enhancing connectivity through road, rail and telecom networks; and
- there has been evolution of the hybrid annuity structure for highways as well as a growth in private sector interest in the CGD sector

These are some of the key developments that are likely to spur investment in the infrastructure sector. With greater appreciation of the risks associated with large infrastructure projects, lending institutions are expected to channel more investment once liquidity in financial sector eases in 2020.

Piyush Joshi
piyush.joshi@claruslaw.com

R.V. Anuradha
anuradha.rv@claruslaw.com

Sumiti Yadava
sumiti.yadava@claruslaw.com

Clarus Law Associates
New Delhi
www.claruslaw.com

The Inside Track

What three things should a client consider when choosing counsel for a complex project financing?

Given the legal risks arising from the enforceability of complex documentation in India, the focus of the client has to be choose a counsel that has both extensive transactional experience, as also experience in addressing disputes relating to such projects. The task of legal risk mitigation in the infrastructure sector starts at the stage of documentation itself, to ensure that the underlying documents are specifically geared towards ensuring that the key provisions survive dispute scenarios and would remain enforceable. In-depth knowledge of sectoral regulation, and interface with related areas, such as competition and investment laws, are other key strengths for a project finance lawyer.

What are the most important factors for a client to consider and address to successfully implement a project in your country?

Project structuring is crucial in order to effectively mitigate land, legal and regulatory risks. For instance, aspects such as land acquisition and other major clearances would necessarily need to be backed by adequate state support. Regulatory uncertainties pertaining to taxes, particularly tax laws which are applied with retrospective effect, need to be hedged with carefully drafted provisions.

What was the most noteworthy deal that you have worked on recently and what features were of key interest?

Noteworthy deals in the recent past include legal advice and representation for a foreign investor in the CGD participating in the ninth and tenth CGD rounds; participants and stakeholders in two LNG terminals currently under development in India; a solid waste management company in India to raise private equity participation; a large scale waste-to-energy plant in Delhi that has successfully commenced operations; a foreign investor in a gas based power plant in India; a private sector operator for a 24/7 potable water supply project in one of the states in India relating to issues arising from its contract with the state government; and the Metro Rail project for the city of Vishakhapatnam in the State of Andhra Pradesh.