Chandrawat & Partners

INFRASTRUCTURE INDUSTRY IN INDIA

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INTRODUCTION

The infrastructure industry is a major economic engine in India. The sector is significantly responsible for accelerating India's overall growth and receives intense government attention for introducing measures that would assure the country's timely building of world-class infrastructure. Power, bridges, dams, highways, and urban infrastructure development are all part of the infrastructure industry. In other words, the infrastructure sector serves as a catalyst for India's economic growth by propelling the development of allied industries such as townships, housing, built-up infrastructure, and building development projects.

Infrastructure development is part of India's goal to become a $5 trillion economy by 2025. To boost the expansion of the infrastructure industry, the government has developed the National Infrastructure Pipeline (NIP), in conjunction with other programmes such as "Make in India" and the production-linked incentives (PLI) plan.

Historically, more than 80% of infrastructure expenditure in the United States has gone into transportation, energy, and water and irrigation; while in India these industries remained the primary emphasis, the government has begun to shift its attention to other areas due to India's changing environment and demography. There is a compelling need for enhanced and improved infrastructure delivery across the entire infrastructure spectrum, from housing provision to water and sanitation services to digital and transportation demands, to ensure economic growth, improve quality of life, and boost sectoral competitiveness.

CURRENT SCENARIO

The Indian economy is built on infrastructure. Highways, energy, airports, smart cities, industrial corridors, metro projects, healthcare, logistics, and other infrastructure projects are expected to cost $1.4 trillion by 2026. The growing momentum in the infrastructure sector not only prepares the path for its development but also for the expansion and development of other economic activities and social upliftment. The sector drives economic growth, creates jobs, and lays the groundwork for long-term, sustainable economic development. Providing infrastructure services to residents has traditionally been the duty of the Government of India (GoI), as these are often high-risk and capital-intensive projects.

In the next five years, India expects to invest $1.4 trillion in infrastructure through the "National Infrastructure Pipeline." In Fiscal Year ("FY") 2021, infrastructure operations accounted for 13% of total Foreign Direct Investment ("FDI") inflows of US$ 81.72 billion. To realise the objective of housing for all by 2022, India would need to build 43,000 dwellings every day until then. Under the Pradhan Mantri Awas Yojna plan, 122.69 lakh dwellings have been sanctioned, 103.01 lakh houses have been grounded, and 62.21 lakh houses have been finished as of August 22, 2022.

Overall infrastructure investment is expected to expand at a 11.4% Compound Annual Growth Rate ("CAGR") between FY 2021 and FY 2026, led by spending on water supply, transportation, and urban infrastructure. The Indian Planning Commission proposed a $ 1 trillion infrastructure investment, with the private sector providing 40% of the funding.

GOVERMENT INCENTIVES

Some of the recent government initiatives and investments in the infrastructure sector are as follows:

In the Union Budget 2022–23:

- The government has given the infrastructure sector a massive boost by allocating Rs. 10 lakh crore (US$ 130.57 billion) to improve infrastructure.
- The government has given the National Highways Authority of India (NHAI) Rs. 134,015 crore (US$ 17.24 billion).
- The government announced a budget for the Ministry of Road Transport and Highways of Rs. 60,000 crore (US$ 7.72 billion).
- The Ministry of Housing and Urban Affairs will receive Rs. 76,549 crore (US$ 9.85 billion) from the government.
- The government has given the Department of Telecommunications Rs. 84,587 crore (US$ 10.87 billion) to build and upgrade telecom infrastructure in the country.
- Railways' total revenue expenditure is expected to be Rs. 234,640 crore (US$ 30.48 billion).
- Over the next three years, 100 PM-GatiShakti cargo terminals for multimodal logistics facilities will be developed.
- The focus was on the PM GatiShakti—National Master Plan—for multimodal connectivity to economic zones. The PM GatiShakti National Master Plan will incorporate everything from roads to trains, aviation to agriculture, as well as many ministries and departments.

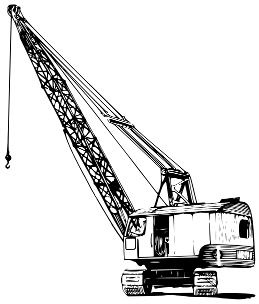
In Financial Year 2022, government initiatives such as the National Infrastructure Pipeline, the National Monetization Pipeline, the Bharatmala Pariyojana, changes in the Hybrid Annuity Model ("HAM"), and a fast pace of asset monetization will boost road construction.

To encourage Rooftop Solar ("RTS") throughout the country, notably in rural regions, the Ministry of New and Renewable Energy is undertaking Rooftop Solar Programme Phase II, which aims to install RTS capacity of 4,000 MW in the residential sector by 2022 with the provision of a subsidy.

The Mega Investment Textile Parks ("MITRA") scheme was launched to establish world-class infrastructure in the textile sector and establish seven textile parks over three years.

Over the next five years, the government will invest Rs. 305,984 crore (US$ 42 billion) in a revamped, reform-based, and result-linked new power distribution sector scheme.

GOVERNING REGULATIONS



The infrastructure sector, which consists of numerous sectors, is controlled by statutes unique to each area. The modalities and mechanisms of private involvement are explicitly defined in these statutes. Private engagement is often permitted through the granting of licences to private developers or through contractual relationships. The breadth and level of private engagement are set by the relevant state government and can vary in degree, for example, on a Build Own and Operate ("BOO"), Build Operate and Transfer ("BOT"), or Build Lease and Transfer ("BLT") basis, to mention a few prevalent options.

The following is a summary of the legislative framework within which the infrastructure sectors operate:

Power - India has taken bold steps to restructure its power sector. With the passage of the Electricity Act of 2003 on June 10, 2003, the whole legislative structure regulating this sector was altered. The new Act repealed the Indian Electricity Act of 1910, the Electricity (Supply) Act of 1948, and the Electricity Regulatory Commission Act of 1998. Private participation in generating companies and Captive Generating Plants is permitted without a licence. However, transmission, distribution, and trade of electrical energy are permitted with a licence from the relevant Electricity Regulatory Commission (ERC). The License is valid for 25 years and can be obtained subject to specified rules and limitations.

Airports - Governed by the Airports Authority of India Act, 1994, the Aircraft Act, 1934, and the Aircraft Rules, 1937. The aforementioned laws allow for private participation through the issue of a licence for an airport that is not controlled by the central government and the creation of a joint venture with the Airports Authority of India. The establishment of private airports and the leasing out of airports to private entities are now permitted, subject to the prior approval of the Central Government.

Roads - The National Highways Act of 1956 and the National Highways Authority of India Act of 1988 control national highways. The National Highways Authority of India is in charge of the creation, maintenance, and administration of national highways.

Water - The Indian government has enormous ambitions to use its large rivers to provide a less expensive, pollution-free, and comparatively more efficient mode of transportation. Wherever possible, the National Water Policy of 2002 supports private sector engagement in the design, implementation, and administration of water resource projects for a variety of applications. This industry offers significant investment potential for investors, with an ambitious goal of connecting rivers across the country.

Railways - Railways are the principal mode of transport in India. Railway transport is covered in the list of industries reserved for the public sector and is therefore not exempt from industrial licensing requirements. However, several railway components have been delicensed.

Ports - The central and state governments have implemented a number of incentives to encourage private investment in this sector through open and competitive bidding. Ports are governed by the Major Ports Trusts Act, 1963, and amendments thereto.

Oil and Natural Gas - Natural gas is projected to be a critical component of India's energy market in the near future. In exploration and production, Indian oil and gas fields are open to the private sector and for foreign participation up to the prescribed limit under production sharing contracts.

In addition to the key infrastructure sectors mentioned above, the Government of India has designated telecom as infrastructure.The government's new telecom policy has revolutionised the telecom industry.The reforms, backed by a large number of statistics on projects, confirm that the infrastructure sector is presently booming in India. A phenomenal growth is expected, making now an excellent time to invest in this sector.

The table below shows the regulatory bodies that govern the infrastructure industry in India:

Sub Sector	Governing Body	Acts/Laws
Transport - Roads & Highways	• Ministry of Road Transport and Highways: The National Highway Authority of India (NHAI) is an autonomous body responsible for the development, maintenance, and management of national highways, totaling over 92,851.05 km in length. The National Highway Authority of India (NHAI) is also responsible for toll collection on several highways. • State Highway Authorities • Ministry of Rural Development	• National Highways Act of India, 1998 • Central Road Fund Act, 2000 • The Control of National Highways (Land and Traffic) Act, 2002
Energy – Power Sector	• Ministry of Power and its various agencies: The Ministry of Power is mainly responsible for evolving general policy in the field of energy. It mainly deals with general policymaking for the power sector and administering various electricity-related laws.	• Electricity Act, 2003
Water Sanitation and Urban Waste Management	• The Ministry of Drinking Water and Sanitation (also known as the Ministry of Jal Shakti) is responsible for the overall policy, planning, funding, and coordination of the Government of India's two flagship programs, the National Rural Drinking Water Program (NRDWP) for rural drinking water supply and the Swachh Bharat Mission (Gramin) [SBM (G)] for sanitation in the country.	• Municipal and Parastatal laws

TAXATION AND EXEMPTIONS

Each year, as part of its annual budget exercise, the government brings about several amendments to the Income Tax Act through the Finance Act. Recently, there has been a thrust from the Finance Ministry to incentivize investment in the infrastructure sector. To facilitate the same, the government announced that it would set up a Development Financial Institution ("DFI") to act as a provider, enabler, and catalyst for infrastructure financing, and a sum of INR 20,000 crores has been provided to capitalise this institution. The aim is to have a lending portfolio of at least INR 5 lakh crore for this development financial institution ("DFI") in 3 years' time.

A high tax rate, combined with a slowdown in economic growth, discouraged new economic investments. To boost investments and rationalise the corporate tax rate, the government has reduced the corporate tax rates significantly for certain domestic companies to 22% (the effective maximum tax rate is 25.17%) and for certain domestic manufacturing companies to 15% (the effective maximum tax rate is 17.16%) by insertion of Sections 115BAA and 115BAB in the Income Tax Act, pursuant to The Taxation Laws (Amendment) Act 2019, applicable from assessment year 2021.

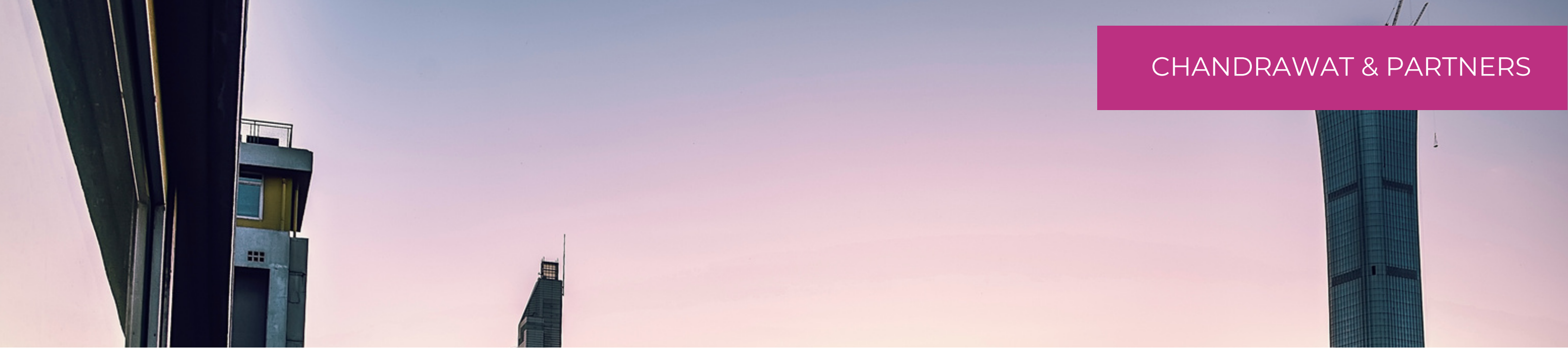
The Income Tax Act provides several investment-linked allowances, tax holidays, and deductions in respect of certain expenditures by entities in the infrastructure sector. A company engaged in eligible business is eligible to enjoy a tax holiday (i.e., 100% of the profits derived from such business are allowed as deductions) under Section 80IA for a period of any 10 consecutive assessment years out of 20 or 15 years, beginning from the year in which the company begins operations. Any enterprise carrying on the business of (i) developing, (ii) operating and maintaining, or (iii) developing, operating, and maintaining any infrastructure facility that fulfils all the conditions mentioned in Section 80IA

FOREIGN DIRECT INVESTMENT

In FY 2021, infrastructure activities accounted for 13% of the total FDI inflows. FDI in the infrastructure development sector (townships, housing, built-up infrastructure, and construction development projects) and infrastructure activities stood at $28.64 billion and $26.22 billion, respectively, between April 2000 and June 2022.

Under the automatic method, 100% FDI in the infrastructure industry in India is authorised in completed projects for the operations and administration of townships, malls, shopping complexes, and business developments.

Under the automatic method, 100% foreign direct investment in urban facilities such as urban transportation, water supply, sewerage, and sewage treatment is permitted. Following foreign investment, residents may transfer ownership and/or management of the investee firm to non-residents. However, a three-year locking period would apply to each tranche of FDI, and transfers of immovable property or portions thereof would be prohibited during this time.



Following are the FDI policies as per the different infrastructure industry's sub sectors -

Power - 100% Foreign Direct Investment is permitted for hydro electric power plants, coal/lignite based thermal power plants and oil/gas based thermal power plants projects.

Fiscal incentives like a 100% tax holiday for new power projects in any block of 10 years within the first 15 years of operations, tax exemptions for interest and dividends, long-term capital gains, concessional rates of import duties, and deemed export benefits are available.

Roads - FDI up to 100% (with total foreign equity up to 1500 crore) is permitted in construction and maintenance of roads, highways, toll roads, vehicular tunnels, rail beds, non-vehicular bridges, non-vehicular tunnels, pipelines, ropeways and runways.

Fiscal incentives include duty-free imports, 10 years of corporate tax holiday within 20 years of commissioning the project, exemption on profits of financing institutions, exemption on long-term capital gains of investors, a concession period up to 30 years, and toll rates indexed to the wholesale price index.

Fiscal incentives like a 100% deduction in profits for the first five years followed by a 30% deduction for the next five years, a full deduction to run for a continuous ten out of twenty fiscal years of the assessor's choice, and a deduction of 40% of the profit to financial institutions from long-term financing of infrastructure projects are available.

Railways - FDI in the railway sector has been allowed with sectoral caps. FDI up to 51% is permitted for manufacture of railway containers used in container traffic. FDI up to 74% is permitted in construction and maintenance of railbeds, bridges and tunnels under automatic route.

Oil and Natural Gas - In refining sector 100% FDI is allowed under the automatic route in the private sector. However, FDI up to 26% is permitted where the joint venture is with public sector undertaking. Foreign Direct Investment up to 51% is permitted for petroleum products and pipeline sector.

Ports - FDI up to 100% is allowed.

Airport - FDI in joint ventures relating to airport infrastructure is permitted up to 74% under automatic route and up to 100% with prior approval. The equity participation could also be made by foreign airport authorities.

DISPUTE RESOLUTION

Disputes are a common feature of the infrastructure sector and can potentially have a far-reaching impact on the project in the form of costs, delayed completion, and opportunity costs. Disputes in the infrastructure industry are primarily technical in nature. They may arise during the execution of the project or after the project's completion. More often than not, if the dispute is not resolved quickly and efficiently, it has a cascading effect on the project and leads to inefficiencies like cost overruns and time overruns for the owner and cash flow issues for the contractor.

The infrastructure sector has made significant progress in the past few decades in developing cost-effective and expedient modes of dispute resolution. The various methods available for settling disputes are as follows:

- **Arbitration:** Arbitration is a form of dispute resolution that is used as an efficient, confidential, and generally cheaper alternative to litigation, especially in India, where the perception is that the judicial system has become an unattractive forum for dispute resolution due to inordinate delays. It allows parties a large degree of flexibility and control over the process of dispute resolution and the freedom to choose a tribunal with the skill set and specialised knowledge required to give a just and fair award. This is an important factor for infrastructure contracts where technical knowledge is, more often than not, essential for dispute resolution.

- **Dispute boards:** These are an increasingly common mode of dispute resolution in infrastructure contracts that are used in combination with arbitration clauses to resolve time-sensitive disputes that arise during the execution of the contract. A dispute board may be set up at the start of the project or when a dispute arises. The appointment of the members of the Dispute Board is by agreement of the parties.

- **Expert Determination:** Another mode of dispute resolution that can be used in combination with either arbitration or litigation is expert determination. This is a novel mode of dispute resolution that is well suited to variation or extra work claims.It essentially allows a technical expert to decide disputes that arise during the execution of the contract and give a quick and binding decision. The parties can decide by agreement whether or not the decision of the expert can be challenged in a subsequent, final dispute resolution process (either arbitration or litigation). In any case, expert determination allows disputes to be readily adjudicated in the first instance, thereby preventing delays in the project and avoiding a cash crunch.

- **Litigation:** It is pertinent to mention herein that litigation is no longer an unattractive option for dispute resolution in light of the recently enacted Commercial Courts, Commercial Division, and Commercial Appellate Division of the High Courts Act, 2015 (the "Commercial Courts Act"), which came into force with effect from October 23, 2015. The aim of the Commercial Courts Act is to simplify and speed up the adjudication process with respect to commercial disputes. An attempt has been made to revamp the Indian judicial system and ensure the disposal of cases fairly, expeditiously, and at a reasonable cost to the parties.

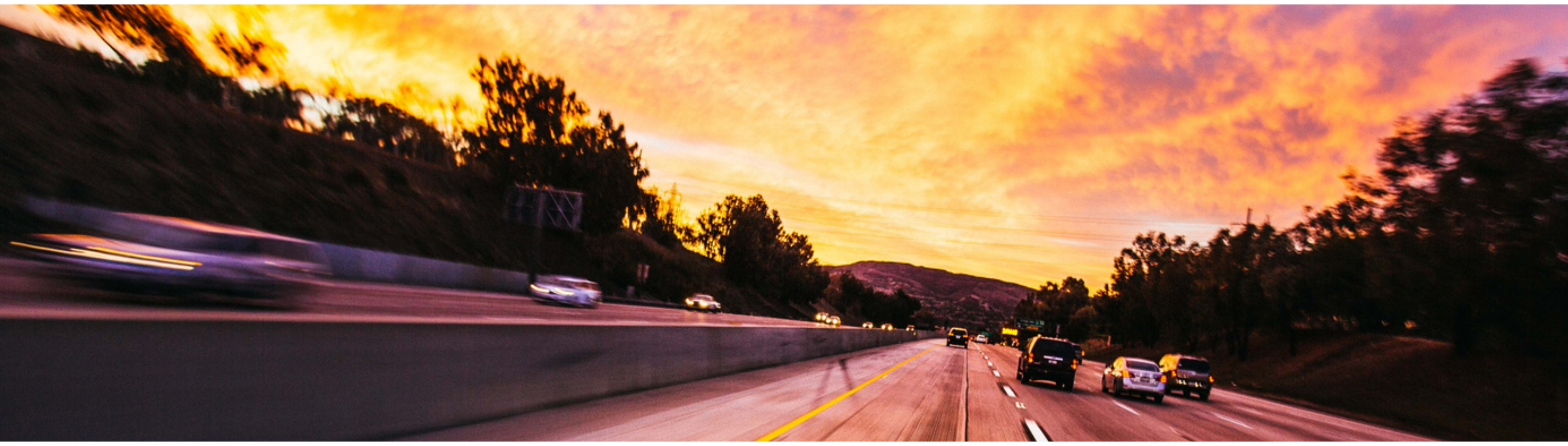
However, in light of the concurrent amendments to the arbitration regime, the latter is still a more effective mechanism for dispute resolution in the construction sector, although it is certainly advisable that arbitration be used in combination with other mechanisms to make it more successful.

WAY FORWARD

Infrastructure in India is an essential component of the country's economic ecology. A dramatic change in the sector has occurred, resulting in the building of world-class infrastructure across the country in areas such as roads, canals, trains, airports, and ports, among others. National smart city programmes have proven to be industry game changers.The infrastructure industry has undergone a huge surge as a result of India's requirement and desire for rapid development, owing to its essential role in the nation's prosperity. Urbanization and more foreign investment in the sector have assisted the expansion.

The infrastructure sector has become the Government of India's primary emphasis. According to S&P Global Ratings, India's GDP is predicted to rise by 8% over the next three fiscal years, one of the fastest rates among major emerging nations. India and Japan have joined forces to improve infrastructure in India's northeastern states, as well as to establish an India-Japan Coordination Forum for Northeast Development to execute important infrastructure projects for the area.

As a growing country, India is poised to seize the chance for infrastructure growth, so it is logical to assume that India's infrastructure has a bright future ahead of it.



HOW WE CAN HELP ?

Our team has extensive expertise and experience in the infrastructure sector, and we understand the demands of both global and domestic clients.

We are ideally positioned to serve our clients and assist them in navigating the country's complicated regulatory framework due to our regular connection with authorities in India, along with our legal experience.

We are able to structure transactions that meet the objectives of our clients by staying ahead of the curve in terms of sectoral knowledge, perception of business considerations, understanding the thought process of regulators, and having a strong pulse on the regulatory framework. This includes several large, marquee, innovative, and first-of-its-kind transactions.

We offer integrated services on all kinds of mega-projects, complex deals, and innovative deals. This is routinely possible given our rich experience spanning acquisitions, divestments, private equity investments, project finance, structured finance, and securitization, as well as project documentation work.

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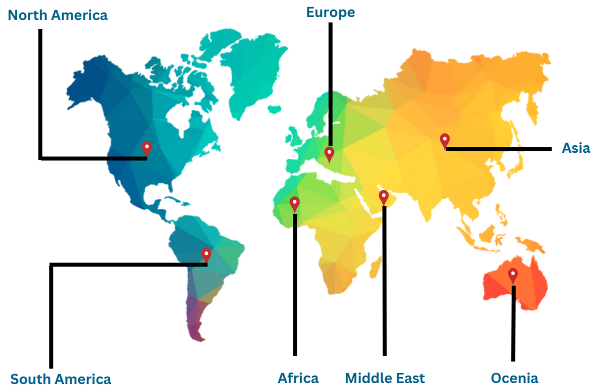
SERVING CLIENTS WORLDWIDE



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