

B K Syngal writes Vodafone case shows that FDI has helped neither the telecom sector, nor the consumers, but crony capitalists and surrogates who held the baby until legitimised and baptised

In second of the two-part series article, Syngal argues that only a few people have got direct benefit of increasing FDI cap from 49% to 74% and then to 100%. And not only have the key decision makers failed to crush these colluding entities that have repeatedly cheated the country, they have also encouraged fiscal irregularities and illicit structuring by adjusting FDI caps ex post facto. In the disputed transaction that happened outside Indian territory, Li Ka-Shing took home a neat US\$ 11.076 billion, Essar Group some US\$ 5 Billion and as a result of the recent FIPB approval we will now see US\$ 1.6 billion being shared by Anajit Singh and Piramal Enterprises. How much has come into India out of the much touted US\$ 18 Billion or so? Zilch

The Vodafone tax case has stuck out like a sore thumb in the judicial landscape of India, known for its pragmatism with respect to tax disputes. This has happened because the executive has underplayed the Supreme Court's decision to "look at" the transactions in Cayman Islands between Vodafone's subsidiary and Hutchison Essar's holding company, rather than "looking through" them, do not treat the disease, but only the symptoms.

The government had drawn up the General Anti-Avoidance Rule (GAAR) to address the issue, but it was postponed till 2016 as a result of the intense advocacy against it by foreign investors in name but in reality the crony capitalist and the surrogates who benefit from it must be gloating over the fact that it got postponed.

Further, the other reason for us to stand strong on these issues is the fact that today India is a robust entrepreneurial economy in its own right. On 15 January 2008, Reliance Power had attracted USD 27.5 billion of domestic bids on the first day of its initial public offering (IPO), equivalent to 10.5 times the stock on offer. This incident in itself should be enough to enable the Indian policy environment to sanitise itself from foreign investors who reap the unfair benefits of investing in India through entities resident in tax havens such as Mauritius and Cayman Islands.

This is just one example amongst others demonstrating the availability of resources within India with rampant black economy, which no one wants to address. Of late another of the legislation to declare notes issued before 2005 as legal tender, which could have sucked in black money, has been withdrawn and postponed. There is absolutely no will to take the issues head on with hard decisions for the sake of Aam Admi.



The recent cabinet decision to consider calling off negotiations with Vodafone and collect its dues would have been, therefore, a strong message to global players operating in India, but has been passed on to the next government. Further, these developments reinforce Chinnappa Reddy's Supreme Court judgment back in 1985, in the *McDowell and Company Limited vs Commercial Tax Officer* case which said that, *"It is neither fair nor desirable to expect the legislature to intervene and take care of every device and scheme to avoid taxation. It is up to the court to take stock to determine the nature of the new and sophisticated legal devices to avoid tax and...to avoid the devices for what they really are and to refuse to give judicial benediction."*

Besides raising some interesting legal questions, the Vodafone case has also opened up the floor for a scrutiny of how FDI has actually worked in India. Hutchison Max Telecom Ltd., a joint venture between Hutchison Whampoa and the Max Group, was established on 21 February 1992. Between 1992 and 2006, Hutchison acquired interests in all 23 mobile telecom circles of India. However, during this period Max ensured that the stocks of this joint venture were issued as depository shares by Kotak Mahindra so that ostensibly the 49% cap on FDI was respected. Therefore the initial seeds of breaching FDI norms through pyramid structures and preferential shares were sown in this first phase. This complicated matter to a great extent for the regulators of a roaring telecom sector and at the behest of the finance minister, the cap was raised to 74% in order to flatten out these irregularities, because of the breach in 74% by direct and indirect investments.

Vodafone Group Plc. on 10 February, 2007 made a final binding offer of US\$ 11.076 billion "in cash over Hutchison Telecommunications International Limited's interest" (67%), based on an enterprise value of US\$ 18.800 billion of Hutchison Essar Limited. Following this, in 2011 Vodafone acquired Essar's 33% stake in the Joint Venture at around US\$ 5 billion and therefore owned 74% of the company by some convoluted structuring. Finally, earlier this month, the company's proposal to buy out the minority stakes of its local investors, businessman Analjit Singh and Piramal Enterprises and take full ownership of the entity, was approved by the Foreign Investment Promotion Board (FIPB).



This move was quite expected, considering the FDI cap of 74% was the only reason Vodafone was sharing the pie with these investors, and now with the cap being increased to 100% there was room for the company to consolidate. Also, considering insiders are of the opinion that the cap was increased to allow full FDI only because with direct and indirect investments made by Vodafone amounting to about 97% anyway, a pyramid structure had emerged yet again. The 100% FDI provided respectability, legitimacy and most importantly few bucks for the high and mighty for holding the can in a conspiratorial, conniving and convenient way.

Therefore, what we see here is an extremely shoddy approach to FDI. On various occasions, i.e., when the cap was increased from 49% to 74% and then to 100% a very limited number of people have walked away with the direct benefits. **And not only have the key decision makers failed to crush these colluding entities that have repeatedly cheated the country, they have also encouraged fiscal irregularities and illicit structuring by adjusting FDI caps ex post facto.** It is no mere co-incidence that every time the cap has been pushed up, share holding has become regularised among these trans-national interests and a select group of investors have cashed out.

In the disputed transaction that happened outside Indian territory, Li Ka-Shing took home a neat US\$ 11.076 billion, Essar Group some US\$ 5 Billion and as a result of the recent FIPB approval we will now see US\$ 1.6 billion being shared by Anajit Singh and Piramal Enterprises. How much has come into India out of the much touted US\$ 18 Billion or so? Zilch. There is a clear exclusion of the larger group of shareholders who could have gained much more from a US\$ 18.8 billion entity resident in India. Had the policy regime been a little more pragmatic and disallowed this pyramid-structured ownership of equity, India would not have had to pay the cost of surrogacy.

Today critics of Indian business point at the fact that we have not been able to create global companies such as Google and Amazon because product development capacity is low in our country. This perception can be reversed if full or 100% FDI is allowed as soon as an innovation is conceived in terms of either product development or service delivery or an infrastructure Hydroelectric power project or Coal or Nuclear.



Let them in and allow them to invest 100 % in the projects identified in all sectors of infrastructure, with all clearances given. Such an approach will test the seriousness and the appetite of the MNCs. Taking a step-by-step approach to FDI provides tremendous scope for crony capitalism and the benefits of a truly open economy are denied to the citizens. Further, analysts have made a habit of calling the telecom sector “debt-ridden” but one wonders why they have not asked the more pertinent question about the real beneficiaries of FDI in this sector. In the mind of this author at least, FDI in telecom has helped neither the fiscal health of the sector, nor the consumers, but crony capitalists and surrogates who held the baby until legitimised and baptised.

For its own good Vodafone should stop this Quixotic tilting at the windmills, and not pursue a debilitating war with a sovereign government.

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(The views are entirely personal and in no way must be associated with any past and present affiliations)

First of the two-part series:-

[B K Syngal writes that Vodafone tax evasion case and its historical FDI pattern is a classical example of crony capitalism](#)

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