

# Plugging the Gaps

## Need for a policy and regulatory relook

Several policy and regulatory issues have been plaguing the telecom sector and impeding growth. These include complicated licence requirements, multi-tiered approval processes, and high taxes and levies. There is also the lack of an overarching regulatory set-up, which has often led to industry face-offs. Most recently, the Telecom Regulatory Authority of India (TRAI) drew flak from some industry analysts for stepping into the Competition Commission of India's (CCI) jurisdiction with regard to its predatory pricing order. As the sector heads towards a course correction, the time is right for its regulatory landscape to undergo a major overhaul as well. Legal experts share their views on the key regulatory issues in the sector and make recommendations for improving the existing legal framework...

### What are the key legal and regulatory issues faced by the telecom industry?

#### Saurav Kumar

A key issue facing the Indian telecom sector is that it is over-regulated. There are various authorities involved on the regulatory front, often resulting in an overlap in jurisdictions. For example, if a newly licensed telecom service provider (TSP) wants to import equipment to set up a base in India, it would have to first approach the Department of Telecommunications (DoT) and then need clearances from the Wireless Planning and Communication wing and the Standing Advisory Committee on Radio Frequency Allocation (SACFA). Another example pertains to the interconnection of internet protocol (IP) and public switched telephone network (PSTN). Current regulations do not allow an entity

to interconnect a PSTN call to an IP telephony call and vice-versa.

The second issue is that there is limited incentive for operators to increase tele-density in rural and remote areas. Right of way (RoW) is a big challenge for rolling out networks in rural areas. Further, the paying capacity in these areas is low even as the cost of service provisioning is quite high. Operators already pay a portion of their revenues as a contribution to the Universal Service Obligation (USO) Fund. The last issue deals with the lack of clarity on the definition of adjusted gross revenue (AGR) that is used to calculate the fee structure for operators.

#### Vaibhav Parikh and Arvind Ravindranath

Apart from the economic disruption caused by the new entrant, there are several issues that have been plaguing the tele-

com sector. These are as follows:

- **Disconnect between TRAI and DoT:** In terms of a regulatory framework, India is unique as there are two governing authorities for the telecom sector. TRAI has limited powers such as setting of tariffs, regulating the quality of services and interconnection. However, DoT still formulates the licensing and regulatory framework for telecom services and has the ultimate say in deciding auctions, licensing terms, etc. This dual authority may cause confusion among participants in the sector.
- **Extremely high spectrum costs:** Even though spectrum prices are set through auctions, these auctions should be allowed to price themselves through the market forces of supply and demand. However, DoT sets high reserve prices, sometimes even against TRAI's recommenda-



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tions. As a result, there are large spectrum bands lying unused, for instance the 700 MHz band, which could have yielded significant economic benefits to the telecom sector and the country.

- Inconsistent and unclear drafting of regulations: Several of the regulations drafted by DoT may not be very clear, and are hence unsuitable for fast-changing business models. For instance, DoT's 2009 public Wi-Fi circular, which used ambiguous words to describe the process of authentication. Another example is the language of the clauses in the unified licence, which has not been clarified for several years.
- Reluctance to adopt new technologies swiftly: DoT is conservative in revising the regulatory framework to facilitate the adoption of new technologies. Policy-level decisions are significantly delayed. This affects the long-term development and deployment of such technologies in India. Examples of this include the long delayed process of liberalising spectrum for machine-to-machine communications and the outdated requirement to ensure that there is no interconnectivity between PSTN networks and the internet.
- RoW policy: Telecom infrastructure developers face difficulties in obtaining RoW to set up telecom towers and lay fibre. Moreover, the local municipal authorities have restricted the growth of telecom towers, citing concerns regarding radiation, etc. The government needs to come out with a policy to facilitate the orderly growth of telecom infrastructure, which would also help solve the call drop problem.
- High cost of diesel and lack of electricity: Low power supply reliability forces telecom towers to rely on expensive diesel generators, especially in semi-urban and rural areas. This affects the economics of building and maintaining telecom towers.

#### Harsh Walia

The Indian telecom industry is going through turbulent times as, on the one hand, TSPs are engaged in cut-throat competition over tariffs and on the other, they

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are heavily debt-ridden and in some cases are filing for bankruptcy. While profit margins have shrunk and operator debt is rising (owing to high spectrum costs and other operational expenditure), the legal and regulatory framework applicable to TSPs has not provided any breather, except the recent decision to increase the term for the payment of deferred spectrum liability. The following are some of the key legal and regulatory issues facing the sector:

- Delay in government approvals: Broadly speaking, mergers and acquisitions (M&A) in the telecom sector have seen inordinate bureaucratic delays. A key issue that TSPs have also raised is that once a court or the National Company Law Tribunal approves of a merger or any other business transfer, DoT does not grant approval in a time-bound manner. It is to be noted that the M&A guidelines issued by DoT in 2014 do not provide a specific timeline within which DoT needs to approve or reject a proposal.
- Delay in approvals and security clearances with regard to foreign investments: Despite the turmoil, the sector continues to attract interest from foreign investors. Delay in approvals and security clearances have further added to the woes of the sector. A flexible approach with quick turnaround times is the need of the hour. Even though the foreign direct investment policy provides for fixed timelines for the approval process at each stage, it is to be seen whether such timelines are followed strictly.
- Infrastructure provider Category-I (IP-I)

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**V. Parikh and A. Ravindranath**

entities are currently not covered under the RoW rules: In 2016, the government had notified the RoW rules applicable to TSPs. As of now, the IP-I entities have been excluded from the scope of these rules, which will only lead to delays in the installation or provisioning of passive infrastructure in the country.

- Revision of the existing penalty structure: Various telecom licences provide for the imposition of penalties to the tune of Rs 500 million. There is no clear-cut methodology to determine when the maximum penalty amount should be imposed – it is sometimes imposed for even violations of a lesser degree. Therefore, the government should devise a suitable matrix for the imposition of financial penalties and that the penalty should correspond to the severity of the breach.
- Simplification of processes: The process of filing for electro-magnetic field compliance, SACFA approvals or import of equipment needs to be simplified. Currently, the processes are not entirely paperless and the delay in the grant of approvals for the import of equipment affects operations and business.
- Clarity on the calculation of AGR: The definition of AGR is a subject of debate and has been litigated for over a decade now. The main issue that has been contested is the inclusion of various components of revenue in the computation of AGR, which are not based on the use of spectrum resources or originate from licensed activities.

### **Is the current tax structure for telcos and tower companies in India comparable to international best practices?**

**Vaibhav Parikh and Arvind Ravindranath**

When compared to the US, Australia and some European Union countries, India has among the highest indirect tax and licence fees levies in the world. Operators in India have to pay goods and services tax (GST), spectrum usage charge (SUC), licence fees and USO Fund levy. This adds up to almost 30 per cent of the gross receipts of telecom companies. In addition, telecom tower companies are required to pay prop-

erty tax as per the Supreme Court's order. Meanwhile, in other countries, the taxes on the sector are much lower. For instance, in the US, the total tax burden including the licence fees ranges from 8 per cent to 25 per cent depending on the state; in Australia, the licence fees is as low as 0.0-018 per cent of revenues, in addition to GST of 10 per cent.

### Harsh Walia

The aggregate of taxes and levies applicable to TSPs in India is around 33 per cent, which includes GST, licence fee, SUC and tax on profits. India's tax rates are comparable to the tax rates of most developed countries like China and the US, where tax rates range from 33 per cent to 35 per cent. However, India's tax structure for telecom is comparatively higher than that in other countries or the world average. The licence fee charged from TSPs is the key differentiator and is significantly higher in India compared to other jurisdictions. For instance, in some countries, the licence fee is charged as a percentage of revenue while in other countries, it is levied to cover regulatory and administrative costs only. In certain other countries, it is a mix of these two components. In South Africa, TSPs are required to pay a licence fee as per different slab rates, which are well below 1 per cent of revenues. Similarly, in Singapore, TSPs pay an annual fee as a percentage of their annual gross turnover and a maximum cap

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of 1 per cent applies. Further, the incidence of local/municipal or state taxes on IP-I entities has been largely irregular and ambiguous. The issue relating to the levy of arbitrary and exorbitant property tax on telecom towers at different rates/amounts by local authorities including municipal corporations and municipalities, coupled with coercive actions such as sealing of towers and disconnection of power supply has been an area of concern for IP-I entities. The tax on telecom towers has been an issue not only in India but in developed countries like the US as well. Tower companies in Sri Lanka are also facing the heat as the government has introduced a tax on mobile phone towers to discourage their proliferation as the government considers these an environmental and health hazard.

**What are your views on the incumbent operators challenging TRAI's predatory pricing order?**

**Saurav Kumar**

TRAI issued the 63rd amendment to the tariff order in mid-February 2018, regard-

ing a regulation on predatory pricing. Airtel and Idea have filed cases challenging this amendment, which are pending before the Telecom Disputes Settlement and Appellate Tribunal (TDSAT). TDSAT has given two weeks to TRAI to respond but has not granted a stay on these regulations. The regulations are effective as of February 2018.

According to the amendment, in case a tariff is found to be predatory, the service provider will be liable to pay, by way of financial disincentive, an amount not exceeding Rs 5 million per tariff plan for each service area. This is huge because an operator is allowed to have 25 tariff plans across 22 circles.

In terms of predatory pricing, the onus is only on players with significant market power (SMP) while players with no SMP do not need to abide by these regulations. In addition, SMP has been defined in a very narrow manner in this order as "30 per cent of total activity in a relevant market". This activity is determined on the basis of subscriber base or gross revenue. Notably, neither the CCI regulations nor the world market perspective on this subject provides for such a narrow definition of SMP.

For example, according to the Office of Telecommunications of the UK, which governs the telecommunications practice, high market shares are less indicative of SMP in countries where telecom markets are emergent or growing more quickly. This is because the subscriber base can change very quickly. These regulations allow the new entrant to capture the market more quickly than what normally competitive forces would have allowed.

The new regulations have put a lot of burden on the incumbents. I hope that TDSAT comes out with a ruling that ensures the prevalence of consistent principles of non-predation and market forces governing competition. CCI should be left with the task of looking after cases of market dominance or its abuse.

**Vaibhav Parikh and Arvind Ravindranath**

Ultimately, telecom is a game of economies of scale. The larger the scale on which a telecom network is deployed, the lower the unit costs. The new entrant



seems to have utilised this strategy effectively. The question on pricing cannot really be answered, unless one witnesses a detrimental effect of such pricing. There is no denying that competition has vastly increased access to telecom services, especially mobile data among the masses. However, the detrimental effects of “predatory pricing” and its impact on the new telco under competition law will only come into play where there is an “appreciable adverse effect on competition” in the market, which would require a significantly higher threshold of predatory pricing than what is in effect at present.

### Harsh Walia

Until recently, the telecom regulations did not provide adequate clarity on the concepts of dominance in the market and predatory pricing. TRAI had received several representations from various TSPs to review the existing tariff-related provisions. After the consultation process with the industry stakeholders, TRAI has now notified regulations pertaining to predatory pricing and activities through the recent amendment to the Telecommunication Tariff Order, 1999 (Amendment).

In my opinion, this amendment has been long due and is extremely important. It has been introduced to determine what constitutes dominance in the market by a TSP and concepts related to predatory pricing. The amendment lays down standards as to what would constitute predatory pricing and provides clarity on issues related to transparency in tariff plans. Most importantly, TRAI has issued the amendment considering consumer interest to be of paramount importance. It should be seen as a stepping-stone to providing clarity on the subject. Although the incumbent operators have challenged the amendment in the TDSAT, no stay has been granted by the court so far.

**What are your suggestions to improve the legal framework for telecom services and infrastructure?**

### Saurav Kumar

The regulatory regime should be streamlined in a way that it is not over-regulated.



There should be a single-window clearance system for applying for licences. Moreover, there have been instances where TRAI or DoT have sometimes stepped into the shoes of the other regulators, which makes the situation extremely complex from a TSP's point of view. As far as infrastructure providers are concerned, they should have a single-window clearance mechanism for setting up sites and lay cables in an efficient manner.

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A competitive telecom sector can only exist when the mindset of the government changes from treating the sector as a source of revenue to one that can act as an enabler of economic and social progress.

Therefore, a good way to support the recent surge in competition in the sector would be to reduce the unnecessary high levies of taxes and licence fees. GST at 18 per cent for telecom services is already much higher than the global average, but the telecom sector in India has to deal with levies to support the USO Fund, SUC and telecom licence fees. The sum of all these levies means that at least 29 per cent of the revenues of the sector go straight to the government. If this number can be reduced to a more reasonable amount, it would go a long way in helping the telcos financially to scale up their infrastructure and compete in

the new mobile data landscape.

### Harsh Walia

The licensing framework may require reconsideration so that the entry of new telecom players becomes easier. To be specific, the virtual network operator (VNO) regime in India has not taken off in the same manner as it has in other parts of the world. Many intending applicants have been discouraged as the VNO licence and authorisations under it have high capital requirements for applicants and lead to double taxation. The government could possibly provide some flexibility in this regard to provide the much-needed impetus to the sector. The TSPs contend that the telecom market in India remains one of the most highly taxed sectors with multiple levies being imposed on them. In my view, DoT may provide financial incentives to the debt-ridden TSPs and, in general, may reconsider certain levies to allow the sector to recuperate from the present situation.

High spectrum costs have proved to be a major challenge for some operators. Unable to cope with the rising debt, they are contemplating filing for bankruptcy or shutting down operations. Therefore, conditions pertaining to spectrum sharing, spectrum trading and spectrum liberalisation should be made simpler to facilitate the optimal use of spectrum amongst TSPs. ▲