

# The Indian Telecom Sector

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## Legal and Regulatory Framework

July 2014

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## Contact

For any help or assistance please email us on [ndaconnect@nishithdesai.com](mailto:ndaconnect@nishithdesai.com) or visit us at [www.nishithdesai.com](http://www.nishithdesai.com)

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# 1. Introduction

The word “telecommunication” is a compound of the Greek prefix “*tele*” meaning ‘far off’, and the Latin “*communicare*”, meaning ‘to share’. In its current usage, it refers to transmission of signals over a distance for the purpose of communication. In early days, communication between persons took place by means of drums, smoke signals, flags etc. Emerging from such humble beginnings, the means now involve sophisticated high-speed, submarine optical cables laid on ocean floors and artificial satellites circling the Earth in space. As the demand for signal transmission has increased, the speed of transmission has also increased.

The telecommunications industry has impact on every aspect of our lives, from the simple reality of enabling telephonic communication between people in different locations to enabling supply-chains to work seamlessly across

continents to create products and fulfill demands. Telecommunication services are now recognized as a key to the rapid growth and modernization of the economy and an important tool for socio-economic development for a nation.

Telecommunications in India can be traced back to the 19th century when the British East India Company introduced telegraph services in India. The past two decades have been considered as the golden period for the telecommunications industry in India with exponential growth and development in terms of technology, penetration, as well as policy. All this has paralleled with the liberalization in this sector and huge investment by both domestic and foreign investors.

## 2. An Overview

The modern system of communications in India started with the establishment of telegraph network. In order to ensure telegraph network's exclusivity and establish government control over electronic communications, various telegraph statutes were enacted by the Government of India which laid the foundation of the present regulatory framework governing telecommunications (both wired and wireless). In early days, India witnessed increasing number of wired telephone connections. Even when wireless communication was introduced in the form of cellular phones, it was not immediately accepted by the Indian masses, mainly on account of high price of cellular phones as well as high tariff structure prevalent at that point in time. Gradually, with the price of cellular handset as well as mobile (wireless) tariff reducing there was increasing adoption of wireless communications. Today the Indian telecom industry is already witnessing the lowest telecom tariff globally.

Like elsewhere, telecommunications in India started as a state monopoly. In the 1980s, telephone services and postal services came under the Department of Posts and Telegraphs. In 1985, the government separated the Department of Post and created the Department of Telecommunications ("DoT"). As part of early reforms, the government set up two new public sector undertakings: Mahanagar Telephone Nigam Limited ("MTNL") and Videsh Sanchar Nigam Limited ("VSNL"). MTNL looked after telecommunications operations in two megacities, Delhi and Mumbai. VSNL provided international telecom services in India. DoT continued to provide telecommunications operations in all regions other than Delhi and Mumbai. It is important to note that under this regime, telecommunication services were not treated to be a necessity that should be made available to all people but rather a

luxury possible for select few.

In the early 1990s the Indian telecom sector, which was owned and controlled by the Indian government, was liberalized and private sector participation was permitted through a gradual process.<sup>1</sup> First, telecom equipment manufacturing sector was completely deregulated. The government then allowed private players to provide value added services ("VAS") such as paging services. In 1994, the government unveiled the National Telecom Policy 1994 ("NTP 1994"). NTP 1994 recognized that existing government resources would not be sufficient to achieve telecom growth and hence private investment should be allowed to bridge the resource gap especially in areas such as basic services. As markets and telecom technologies started converging and the differences between voice (both fixed and wireless) and data networks started blurring, the need for developing the modern telecom network became an immediate necessity. Accordingly, private sector participation was allowed in basic services.

The government anticipated that a major part of the growth of the country's GDP would be reliant on direct and indirect contributions of the telecom sector and accordingly the need for a comprehensive and forward looking telecommunications policy was felt. This then paved way for New telecom Policy 1999 ("NTP 1999") which largely focused on creating an environment for attracting continuous investment in the telecom sector and allowed creation of communication infrastructure by leveraging on technological development. The main objectives and targets of NTP 1999 were as follows:

- Availability of affordable and effective communications for citizens;
- Strive to provide a balance between the

1. In fact the law as it currently stands still bestows an exclusive privilege on the Government to provide telecommunications services. We have discussed in Chapter IV how the Central Government derives the power to grant licenses to private companies in India to enable them to provide telecommunication services.

- provision of universal service to all uncovered areas, including the rural areas and the provision of high-level services capable of meeting the needs of the country's economy;
- Create a modern and efficient telecommunications infrastructure taking into account the convergence of IT, media, telecom and consumer;
- Protect the defense and security interests of the country.

NTP 1999 allowed private operators providing cellular and basic services to migrate from a fixed license fee regime to a revenue sharing regime which made it financially viable for such operators to function in the market. Most importantly, the government recognized the necessity to separate the government's policy wing from its operations wing so as to create a level playing field for private operators. Accordingly the NTP 1999 directed the separation of the policy and licensing functions of DoT from the service provision functions. The Government corporatized the operations wing of DoT in October 2000 and named it as Bharat Sanchar Nigam Limited ("BSNL") which operates as a public sector undertaking. Thereafter in 2002, the monopoly of VSNL also came to an end.

Since the Government was unable to meet keep up with the demand for telephone connections coupled with the fact that there was a waiting list for telephones in India, the Government moved to involve / invite the private sector in telecom. Further to this, the Government introduced the Cellular Mobile Telephone Service ("CMTS") license and the Basic Telecom Service ("Basic") license allowing private players to provide telecom services in India. The private sector responded positively to this move and the Government issued 39 CMTS licenses and 2 Basic licenses.<sup>2</sup> Thereafter, the Government simplified the licensing regime and introduced the Unified Access Service ("UAS") License, combining the two licenses, i.e. Basic and CMTS thereby allowing

UAS licensees to provide both services under the ambit of one license. Various new licenses issued by the Government coupled with other measures undertaken to unshackle the Indian telecom market led to an inflow of more than 12 billion dollars of foreign investment from 2000 to 2013<sup>3</sup> by various international telecom operators. The Indian telecom story was one of large volumes and low ARPU<sup>4</sup> which presented a huge opportunity for international telecom operators who were experiencing stagnation in the growth of their subscriber base in other parts of the world.

Due to the stagnation of growth of this industry over the past couple of years for various reasons, the DoT introduced the National Telecom Policy 2012 ("NTP 2012") in an attempt to align efforts of policy makers, stakeholders and law makers to achieve a common goal.

The preamble to the NTP 2012 reads as follows:

*"Telecommunication has emerged as a key driver of economic and social development in an increasingly knowledge intensive global scenario, in which India needs to play a leadership role. National Telecom Policy-2012 is designed to ensure that India plays this role effectively and transforms the socio-economic scenario through accelerated equitable and inclusive economic growth by laying special emphasis on providing affordable and quality telecommunication services in rural and remote areas."*

The mission of the NTP 2012 is as follows:

- To develop a robust and secure state-of-the-art telecommunication network providing seamless coverage with special focus on rural and remote areas for bridging the digital divide and thereby facilitate socio-economic development.
- To create an inclusive knowledge society through proliferation of affordable and high quality broad band across the nation.

2. <http://www.dot.gov.in/access-services/introduction-unified-access-servicescellular-mobile-services>

3. <http://www.indianexpress.com/news/telecom-sector-received-rs-58782-cr-fdi-in-last-13-years/1156800/>

4. Average Revenue Per User

- iii. To reposition the mobile device as an instrument of socio-economic empowerment of citizens.
- iv. To Make India a global hub for telecom equipment manufacturing and a centre for converged communication services.
- v. To promote Research and Development, Design in cutting edge Information and Communications Technology and Electronics (“ICTE”) technologies, products and services for meeting the infrastructure needs of domestic and global markets with focus on security and green technologies.
- vi. To promote development of new standards to meet national requirements, generation of IPRs and participation in international standardization bodies to contribute in formation of global standards, thereby making India a leading nation in the area of telecom standardization,
- vii. To attract investment, both domestic and foreign.
- viii. To promote creation of jobs through all of the above.

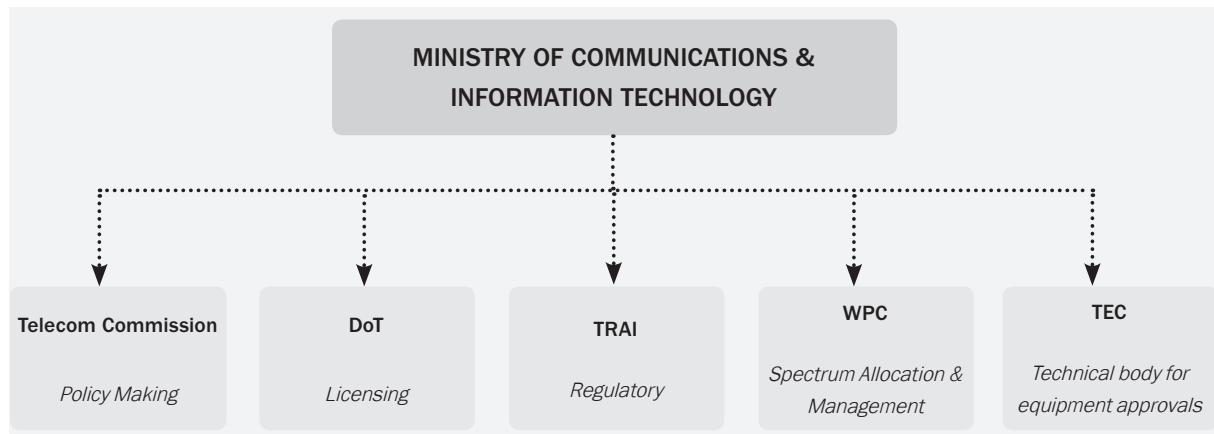
The NTP 2012 seems to be progressive in its outlook. For instance it proposes to work towards **One Nation - Free Roaming** allowing subscribers to receive free incoming calls anywhere in India without paying additional roaming charges, similarly allowing subscribers to make outgoing calls at local tariffs without roaming charges anywhere in India along with the introduction of the **One Nation-One License** regime. It is designed

to ensure that India plays an effective role to transform socio-economic scenario by providing affordable and quality telecommunication services in not just urban but rural areas too. NTP-2012 recognizes that the rapid growth in the telecom sector requires to be supported by an enhanced pace of human capital formation and capacity building. Introduction of new technologies has posed fresh challenges in network security, communication security and communication assistance to law enforcement agencies. NTP- 2012 provides a strategy for achieving these goals, however major concerns remain with respect to actual implementation of the NTP 2012 along with timelines for the same.

Following the introduction of the NTP 2012, the government appears to be determined to bring about much needed reforms in the telecom sector. The Unified Licensing regime, which has been discussed in detail below has been introduced in furtherance of the One Nation-One License policy. Similarly, foreign investment restrictions have been lifted which earlier necessitated having a local partner for all telecom business. Though there remains one major area that has not yet been addressed, i.e. Mergers and Acquisitions. The telecom sector is quite fragmented and consolidation is considered crucial at this stage and to that extent the industry awaits the the government’s policy on Mergers and Acquisitions in the telecom sector.



## 3. Indian Telecom Authorities



We have discussed below some important aspects of various Indian telecom authorities.

### I. Telecom Commission

The Telecom Commission is an inter-ministerial high level government body. The Commission consists of a Chairman, four full time members, who are ex-officio, Secretary to the Government of India in the Department of Telecommunications and four part time members who are the Secretaries to the Government of India of the concerned Departments. The essential functions of the Telecom Commission are as under:

- policy formulation, licensing and coordination matters relating to telegraphs, telephones, wireless, data, facsimile services and other similar forms of communications;
- international cooperation in matters connected with telecommunications;
- promotion of standardization, research and development in telecommunications;
- promotion of private investment in telecommunications;
- preparing the DoT budget and supervising its operations

### II. Department of Telecommunications (“DoT”)

As per the Indian Telegraph Act, 1885 and

the Indian Wireless Telegraphy Act, 1933 **the Central Government has the exclusive privilege of establishing, maintaining and working telegraph and wireless telegraphy equipment and is the authority to grant licenses for such activities.**

The Central Government acts through the DoT. Some of the important functions of the DoT are as follows:

- licensing and regulation
- international cooperation in matters connected with telecommunications (such as International Telecommunication Union (ITU), International Telecommunication Satellite Organization (INTELSAT), etc;
- promotion of private investment in the Indian telecommunications sector;
- promotion of standardization, research and development in telecommunications.

### III. Telecom Regulatory Authority of India (“TRAI”)

TRAI is an autonomous statutory body established under Telecom Regulatory Authority of India Act, 1997 (“**TRAI Act**”) (discussed In Chapter IV of this paper). Liberalization made it necessary for the Government to ensure that there is an independent communications regulator. TRAI acts as an independent regulator of the telecommunications industry in the country. One of the main objectives of TRAI is to provide a fair and transparent policy environment which

promotes a level playing field and facilitates fair competition amongst various telecom players. TRAI's powers are recommendatory, mandatory, regulatory and judicial.

The important recommendatory powers of TRAI are as follows<sup>5</sup>:

- recommendations regarding the need and timing for introduction of new service providers
- recommendations pertaining to the grant of telecom licenses including their terms and conditions
- recommend revocation of license for non-compliance of terms and conditions of license.

TRAI is the sole authority empowered to take binding decisions on fixation of tariffs for

provision of telecommunication services. Emphasis needs to be placed on the interplay between the recommendatory powers of TRAI and the policy making powers of DoT. While the DoT is the sole authority for licensing of all telecommunications services in India, it is mandatory for the DoT to have before it TRAI's recommendations with regard to matters over which TRAI has recommendatory powers (mentioned above). Having done so, the DoT has the discretion to either accept or reject the recommendations of TRAI.<sup>6</sup> TRAI has over the years come out with a number of recommendations; DoT has accepted some such recommendations either wholly or partially or has rejected such recommendations. Below is the status of some of the recommendations made by TRAI to the DoT:

TRAI Recommendation/s	Status
Recommendations on Next Generation Networks (2006)	Not accepted by the DoT
Recommendations on Allocation and Pricing of Spectrum for 3G and Broadband Wireless Access Services (2006)	Some of the recommendations were accepted by the DoT
Recommendations on issues related to Internet Telephony	Not accepted by the DoT
Recommendations on Infrastructure Sharing	Most of the recommendations were accepted by the DoT
Recommendation on Growth of Value Added Services and Regulatory Issues (2009)	Decision of DoT is awaited
Recommendations on approach towards Green Telecommunications. (2011)	Most of the recommendations were accepted by the DoT
Recommendations on Terms and Conditions of Unified License (Access Services) (2013)	Some of the recommendations were accepted by the DoT

In this respect, there have been concerns that the very reason for the establishment of TRAI has been nullified in that a regulatory body whose specialist recommendations are not bound to be followed may be considered to be a paper tiger after all especially when comparisons are drawn with the more advanced regulatory agencies of the world such as the Federal Communications

Commission (FCC) of the US which has been entrusted with very wide powers in telecom regulation including the granting of licenses. There have been some recent reports wherein the government is considering giving wider powers to TRAI<sup>7</sup>, however there has been no formal policy change as yet.

5. Section 11(t) of the Telecom Regulatory Authority of India Act, 1997

6. This stipulation was brought about by an amendment to the TRAI Act in 2000

7. <http://www.livemint.com/Politics/R8aX6xKx7IyuGJmw6PB5iN/DoT-to-see-increase-in-Trai-powers.html>

## IV. Telecom Disputes Settlement and Appellate Tribunal (“TDSAT”)

The TDSAT was established in 2000 under an amendment to the Telecom Regulatory Authority of India Act, 1997 (discussed In Chapter 0 of this paper). The TDSAT has been vested with exclusive powers to adjudicate any dispute between:

- the licensor (DoT) and a licensee;
- service providers; and
- service providers and groups of customers.

Any appeal from the decision of the TDSAT can be filed only with the Supreme Court of India which is the apex court of the country.

## V. Wireless Planning and Co-ordination Wing (“WPC”)

The WPC was created in 1952 and is a wing of the DoT which is responsible for Frequency

Spectrum Management, including licensing of wireless stations and caters to the needs of all wireless users (Government and Private) in India. It exercises the statutory functions of the Central Government and issues licenses to establish, maintain and operate wireless stations. WPC is divided into (i) Licensing and Regulation (LR), (ii) New Technology Group (NTG) and (iii) Standing Advisory Committee on Radio Frequency Allocation (SACFA). The WPC is also the central agency for the purpose of representing India and to adhere to India’s commitments at the International Telecommunication Union (“ITU”)<sup>8</sup>, Asia-Pacific Telecommunity (“APT”)<sup>9</sup> and other organizations that India is a member or signatory of. The WPC is headed by the Wireless Advisor to the Government of India.

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8. ITU is the leading UN agency for information and communication technology issues, and the global focal point for governments and the private sector in developing networks and services.

9. APT is an Intergovernmental Organization operating in conjunction with telecom service providers, manufacturers of communications equipment, and research and development organizations active in the field of ICT in the Asia-Pacific region.

## 4. Telecommunications Laws and Regulations

### I. The Indian Telegraph Act, 1885

This Act is one of the oldest legislations still in effect in India and is an Act to amend the law relating to telegraphs<sup>10</sup> in India. Some of the salient features of this Act are:

- it empowers the Government of India to take control of the existing telegraph lines and lay down the necessary infrastructure for further expansion of telecommunications in India.
- it authorizes the Government of India to grant telecom licenses on such conditions and in consideration of such payments as it thinks fit, to any person to establish, maintain, work a telegraph within any part of India.
- it authorizes the Government of India to take possession of licensed telegraphs and to order interception of messages on the occurrence of any public emergency or in the interest of public safety.
- any dispute concerning a telegraphic appliance/ apparatus/ line between the telegraph authority and a licensee (for whose benefit the line, appliance or apparatus is, or has been provided) shall be determined by arbitration by an arbitrator appointed by the Central Government.

We would like to place emphasis on the power bestowed on the Government to grant licenses to private bodies to provide telecommunication services in India on conditions it deems fit.

This power is in fact a proviso of the exclusive privilege granted by the Indian Telegraph Act, 1885 to provide telecommunications services in India. In this respect it is interesting to note the observations made by the Supreme Court in the case of *Delhi Science Forum v Union of*

*India*:<sup>11</sup> “Central Government is expected to put such conditions while granting licences, which shall safeguard the public interest and the interest of the nation. Such conditions should be commensurate with the obligations that flow while parting with the privilege which has been exclusively vested in the Central Government by the Act”

It is also relevant to note that though the provision pertaining to dispute resolution through arbitration is well settled in law, there have been instances where the courts/ other judicial bodies have assumed jurisdiction over matters which should be settled by arbitration under the provisions of the Indian Telegraph Act, 1885. In the case of *General Manager, Telecom v M. Krishna and Anr*<sup>12</sup> a dispute arose regarding the non-payment of bills by the respondent due to which the telephone connection of the respondent was disconnected. The respondent filed a complaint before the District Consumer Disputes Redressal Forum, Kohzikode, which allowed the complaint and directed the appellant to reconnect the telephone and pay compensation. A writ filed by the appellant in the High Court of Kerala challenging the jurisdiction of the consumer forum was dismissed. The appellant then came before the Supreme Court by way of special leave. The Supreme Court held that as there is a special remedy by way of arbitration provided in the Indian Telegraph Act, and the remedy under the Consumer Protection Act, is by implication barred. It is well settled that a special law overrides a general law. Accordingly, the Supreme Court set aside the order of the Kerala High Court as well as the order of the District Consumer Forum.

10. “telegraph” means any appliance, instrument, material or apparatus used or capable of use for transmission or reception of signs, signals, writing, images and sounds or intelligence of any nature by wire, visual or other electro-magnetic emissions, Radio waves or Hertzian waves, galvanic, electric or magnetic means. - Preamble to the Act

11. 1996 SCC (2) 405

12. AIR 2010 SC 90

## II. The Indian Wireless Telegraphy Act, 1933

This Act was enacted to regulate the possession of wireless telegraphy apparatus.<sup>13</sup> According to this Act, the possession of wireless telegraphy apparatus by any person can only be allowed in accordance with a license issued by the telecom authority. Further, the Act also levies penalties if any wireless telegraphy apparatus is held without a valid license.

## III. The Telecom Regulatory Authority of India Act, 1997

The Telecom Regulatory Authority of India Act, 1997 enabled the establishment of the TRAI. The role and functions of the TRAI have already been discussed in Chapter III above. Interestingly, the 1997 Act empowered the TRAI with quasi-judicial authority to adjudicate upon and settle telecom disputes. Later this Act was amended by the Telecom Regulatory Authority of India (Amendment) Act, 2000 to bring in better clarity and distinction between the regulatory and recommendatory functions of TRAI.

Further, the 2000 amendment served a very important purpose in completely differentiating the judicial functions of TRAI by setting up of the TDSAT. The jurisdiction of civil courts has been expressly barred in cases where the TDSAT has jurisdiction. The role and functions of the TDSAT has already been discussed in Chapter III above.

## IV. The Information Technology Act, 2000

In 2000, the Indian Parliament passed the

Information Technology Act, 2000 which was amended in 2008 (“ITA”). The amendment provided additional focus on information security as well as added several new sections on offences including cyber terrorism and data protection. The ITA provides for penalties for various offences such as cyber crimes, various e-commerce frauds like cheating by impersonation and pornography. Though the ITA was not enacted to directly apply to the telecom industry, it is a fact that the information technology sector and the telecom sector are closely linked and the 2008 amendments have in fact explicitly made the ITA applicable to the telecom industry.<sup>14</sup> Further, through the 2008 amendments a new section has been inserted which defines “communication device” as cell phones, personal digital assistance or combination of both or any other device used to communicate, send or transmit any text video, audio or image. This revised definition clearly brings the telecom sector within the ambit of the ITA.

We discuss below some of the important provisions of the ITA which are relevant for the telecom industry

### A. Monitoring

Section 69-B of the ITA gives the Government the right to authorize any of its agencies to monitor and collect traffic data or information generated, transmitted, received or stored in any computer resource. By virtue of the definition of ‘computer resource’, this section would include within its ambit cell phones along with all the servers and other data processing systems which are used by telecom operators. Therefore, telecom operators will need to comply with directions for monitoring and collection of data in the interest of cyber security issued by the Secretary, Department of

13. ‘wireless telegraphy apparatus’ means any apparatus, appliance, instrument or material used or capable of use in wireless communication, and includes any article determined by rule made under Sec. 10 to be wireless telegraphy apparatus, but does not include any such apparatus, appliance, instrument or material commonly used for other electrical purposes, unless it has been specially designed or adapted for wireless communication or forms part of some apparatus, appliance, instrument or material specially so designed or adapted, nor any article determined by rule made under Section 10 to not to be wireless telegraphy apparatus;

14. Section 2(W) of the ITAA 2008 defines “Intermediaries” as follows: “Intermediary with respect to any particular electronic records means any person who on behalf of another person received, stores or transmits that record or provides any service with respect to that record and includes telecom service provider, internet service providers, web hosting service providers, search engines, online payment sites, online auction sites, online market places and cyber cafes”.

Information Technology or any other such officer as may be notified by the Government.

## B. Intermediaries

As per the ITA, an intermediary (which by definition includes a telecom service provider) is liable for any offence under the ITA. Under Section 79 of the ITA, an intermediary is exempt from liability in relation to any third party information or communication link, provided:

- i. The role of the intermediary is limited to providing access to a communication system over which third party information is transmitted or temporarily stored; or
- ii. The intermediary does not initiate, select the recipient of or select / modify the information in the transmission; and
- iii. The intermediary observes due diligence while discharging his duties.

Notwithstanding the above qualifications, Section 79 further goes on to provide that irrespective of the exemptions provided above and irrespective of the exercise of due diligence, an intermediary would still be liable where:

- ii. The intermediary has conspired, aided, induced or abetted in any unlawful activity; or
- iii. The intermediary upon obtaining knowledge or upon being notified fails to expeditiously remove or disable access to any information, data or communication link controlled by the Intermediary which is being used to commit an unlawful act.

The essential element which needs to be proved in order to pin liability on an intermediary is control. The basic premise is that an intermediary, in the ordinary course of business, is merely acting as a conduit and is not in a position to exercise control over any material or information which is transmitted through its platform unless required to do so under the provisions of the ITA

The DoT, introduced certain rules in exercise of powers conferred under the ITA. These rules will

act as enablers to particular sections of the ITA. One such rule is the Information Technology (Intermediaries guidelines) Rules, 2011.<sup>15</sup>

As per the rules, the intermediary has to observe the necessary due diligence while discharging his duties which includes publishing rules and regulations, privacy policy and user agreement. Such rules and regulations, etc shall inform the users of computer resource not to host, display, upload, modify, publish, transmit, update or share any information, *inter alia*, that:

- belongs to another person and to which the user does not have any right to.
- is grossly harmful, harassing, blasphemous, defamatory, obscene, pornographic, libelous, invasive of another's privacy, disparaging, relating or encouraging money laundering or gambling, etc or otherwise unlawful in any manner whatever.
- harm minors in any way.
- infringes any intellectual property right or other proprietary rights.
- violates any law for the time being in force, etc.

The following actions by an intermediary shall not amount to hosting, publishing, editing or storing of any such information:

- temporary storage of information automatically within the computer resource as an intrinsic feature of such computer resource, involving no exercise of any human editorial control, for onward transmission or communication to another computer resource.
- removal of access to any information, data or communication link by an intermediary after such information, data or communication link comes to the actual knowledge of a person authorized by the intermediary pursuant to any order or direction as per the provisions of the ITA.
- The intermediary upon obtaining knowledge by itself or been brought to actual knowledge by an affected person in writing or through email signed with electronic signature about any such information as mentioned in aforesaid

15. [http://www.mit.gov.in/sites/upload\\_files/dit/files/GSR314E\\_10511\(1\).pdf](http://www.mit.gov.in/sites/upload_files/dit/files/GSR314E_10511(1).pdf)

point under this Rule, shall act within thirty six hours and where applicable, work with user or owner of such information to disable such information that is in contravention of the said aforesaid point. Further the intermediary shall preserve such information and associated records for at least ninety days for investigation purposes.

- The intermediary shall inform its users that in case of non-compliance with rules and regulations, etc, the intermediary has the right to terminate access or usage rights of the users to the computer resource of Intermediary and remove non-compliant information.
- The intermediary shall provide information / assistance to Government agencies who are lawfully authorized for investigative, protective, cyber security activity. The intermediary shall report cyber security incidents and also share cyber security incidents related information with the Government agency.
- The intermediary shall take all reasonable measures to secure its computer resource and information contained therein following the reasonable security practices and procedures as prescribed in the Information Technology

(Reasonable security practices and procedures and sensitive personal information) Rules, 2011.

- The intermediary shall publish on its website the name and details of the grievance officer as well as mechanism by which users or any victim who suffers as a result of access or usage of computer resource by any person can notify their complaints against such access or usage. Such grievance officer shall redress the complaints within one month from the date of receipt of complaint.

We believe that the introduction of this rule seems to have been introduced due to the increased litigation against intermediaries who were accused as parties / co-accused in cases of unlawful or illegal conduct by end users.

## 5. Telecom Services / Licenses and Infrastructure in India

There have been some important regulatory changes which were introduced post liberalization which have provided an immense boost to development of this sector. These regulatory changes by and large trace their roots to the objectives and vision set out by the Government in NTP 99.

### I. Universal Service Obligations

It is an accepted fact that improved rural penetration is a key priority area for most developing countries. The concept of Universal Service Obligation (“USO”) has been mooted by many developing countries and is grounded on the principle that effective means of communication is a must for economic and social development. NTP 99 envisaged the provision of basic telecommunications services to all at affordable rates. Keeping in line with NTP 99 and the recommendations of the Telecom Regulatory Authority of India on the issues relating to the Universal Service Obligation the Universal Service Support Policy was framed and came into effect from April 2002. The Indian Telegraph (Amendment) Act, 2003 gave statutory status to the Universal Service Obligation Fund (“USOF”). USOF is used to subsidise developments in the telecom sector in the rural areas such as:

- increasing wireless network;
- providing public access through public or community phones;
- providing individual household telephones.

The resources for meeting the USOF are to be generated through a Universal Service Levy (“USL”), which would be a percentage of the revenue earned by the operators under various licenses. The USL presently is 5% of the Adjusted Gross Revenue earned by all operators except pure value added services providers like voice mail and e-mail.

### II. Interconnection

India today has a plurality of service providers and service networks. In such a situation, efficient interconnection between a variety of access networks (such as fixed, mobile, national long distance and international long distance) has to interconnect to make national and international connectivity possible. In 2003 TRAI implemented the Telecommunications Interconnection Usage Charges Regulation to fix terms and conditions of interconnectivity between service providers and to regulate arrangements among service providers for sharing their revenue derived from provision of telecommunication services.

### III. Unified License

Further to NTP 2012, the DoT introduced the much awaited and much delayed Unified License in August 2013. The Unified License paves the way for the implementation of DoT’s One Nation - One License plan by consolidating license terms for different telecom services under the ambit of one license, i.e. the Unified License. The Unified License replaces the old regime of a telecom operator applying for separate licenses for separate services proposed to be offered by bringing all the major telecom services under one license.

The Unified License includes within its ambit the following services:

- Access Service (Land Line Telephony Service along with Mobile Phone Telephony Service);
- Internet Service;
- National Long Distance Service (“**NLD Service**”);
- International Long Distance Service (“**ILD Service**”);
- Global Mobile Personal Communication By Satellite Service (“**GMPCS Service**”);
- Public Mobile Radio Trunking Service (“**PMRTS Service**”);



- Commercial Very Small Aperture Terminal Closed User Group (“**Commercial VSAT CUG Service**”);
- INSAT Mobile Satellite System-Reporting Service (“**INSAT MSS-R Service**”); and
- Resale of International Private Leased Circuit Service (“**Resale of IPLC Service**”).

The Unified License is a sort of umbrella document which all companies seeking to provide telecom services will need to obtain. Apart from this, the company would also need to obtain separate authorization from the DoT for specific services which the company wishes to provide. One company can have only one Unified License, but the same company can apply for authorization for more than one service and / or service area subject to fulfillment of all the conditions of entry, simultaneously or separately at different times. At the time of applying for Unified License, the applicant has to apply for authorization of at least one service that is listed in the Unified License.

The Unified License shall be issued on a non-exclusive basis for a period of 20 years. The license may be renewed by the DoT for an additional period of 10 years at a time upon request of the service provider, if made during the 19th year of the license period.

We have circulated a detailed analysis of the Unified License which is attached as Annexure A.

The Unified License covers a variety of services for which authorizations can be obtained. We have discussed two of main services being covered by the Unified License; Access Service and Internet Services

## A. Access Services

Access Service providers can provide, within

their area of operation, wireline (basic) as well as wireless (cellular) services in a service area. Access Service providers have also been permitted to provide internet telephony, internet services including IPTV, broadband services and triple play i.e voice, video and data.

Importantly, Access Service is the only authorization which is permitted to provide full-fledged Internet Telephony, i.e. they are permitted to interconnect Internet Telephony network with the PSTN network.

In order to provide the above mentioned services, licensees will have to separately acquire spectrum once a license has been acquired, rather than spectrum being bundled with the license as was the norm under the erstwhile licensing regime.

Existing UAS Licensees are permitted to migrate to Unified License regime. The service providers migrating to Unified License will continue to provide wireless services in already allocated/contracted spectrum and no additional spectrum will be allotted under the migration process.

Access Service providers are required to pay a certain percentage of Adjusted Gross Revenue (“AGR”)<sup>16</sup> as license fee apart from paying spectrum charges. Specifically for those entities holding spectrum, the Unified License has introduced the concept of presumptive AGR which places a premium on spectrum even where the spectrum holder does not utilize the spectrum made available to them. A spectrum holder is required to pay license fees in the form of a percentage of notional revenues or a percentage of the actual revenues, whichever is higher. Notional revenue which is essentially a minimum amount of revenue for this purpose will be calculated in accordance with the relevant provisions of the Notice Inviting Application document of the

16. Gross Revenue shall include installation charges, late fees, sale proceeds of handsets (or any other terminal equipment etc.), revenue on account of interest, dividend, value added services, supplementary services, access or interconnection charges, roaming charges, revenue from permissible sharing of infrastructure and any other miscellaneous revenue, without any set-off for related item of expense, etc.. For arriving at the AGR, following shall be excluded from the Gross Revenue: PSTN related call charges (Access Charges) actually paid to other eligible/entitled telecommunication service providers within India; Roaming revenues actually passed on to other eligible/entitled telecommunication service providers; Service Tax on provision of service and Sales Tax actually paid to the Government if gross revenue included Sales Tax and Service Tax

auction of spectrum or conditions of spectrum allotment depending on the service and service area. Therefore, unlike the previous regime whereby license fee was determined on the basis of revenue generated by an operator, spectrum holders will now have to pay a minimum pre-determined percentage as license fee or actual AGR or the minimum license fee whichever is higher.

## B. Internet Service Licenses (ISP)

ISP licensees are primarily allowed to provide services such as internet access (through any method including IPTV) and internet telephony (which is a service to process and carry voice signals offered through the internet by the use of personal computers ("PC") or internet protocol based equipment). Currently the ISP license allows limited internet telephony by permitting connections between the following:

- PC to PC (within or outside India).
- PC / a device / Adapter conforming to standard of any international agencies like ITU or IETF etc in India to PSTN/PLMN abroad.
- Any device / Adapter conforming to standards of International agencies like ITU, IETF etc. connected to ISP node with static IP address to similar device / Adapter within or outside India.

Thus, ISP Licensees offering Internet Telephony are not allowed to interconnect Internet Telephony network with the PSTN network.

Further, ISP Licensees are not permitted to offer Virtual Private Network ("VPN") / Closed User Group services to its subscribers.

## IV. Mobile Number Portability ("MNP")

MNP allows mobile subscribers to retain their existing telephone numbers when they switch from one telecom operator to another irrespective of mobile technology. India has long

felt the need for MNP. The TRAI introduced the Telecommunications Mobile Number Portability Regulations, 2009 in September 2009. As per the regulations, the subscribers would be allowed to retain their mobile number while moving from (within the same service circle):

- one access provider to another irrespective of the mobile technology / platform; or
- one cellular mobile technology to another of the same access provider.

Thus effectively a subscriber can move from a CDMA service provider to a GSM service provider in a seamless manner. Nevertheless, a big drawback of the current MNP regime is that it is restricted to intra-circle transfers and prohibits porting of a number from one circle to another.

However, the Government seems to have recognized this need, considering that one of the objectives of the NTP 2012 is to achieve *One Nation - Full Mobile Number Portability*. News reports suggest that the TRAI has suggested that pan-India MNP should be introduced by April 2014<sup>17</sup>, which would mean that subscribers can use the same number while moving from one mobile circle to another, regardless of the service provider.

India is one of the world's fastest growing telecom markets and it continues to be amongst the world's lowest telecom tariff destinations. As such the implementation of MNP will ensure that every telecom mobile service provider offers mobile number portability to all its subscribers both post paid and pre-paid on a non-discriminatory basis. The telecom operators on their part, would have to incur huge expenses by way of capital expenditure and operational expenses in order to effectuate and operationalize MNP. With the Indian tariff structure already at the lowest in the world, the revenues of the telecom operators are likely to be affected with the implementation of MNP with subscribers having the freedom to migrate to better service providers. This in turn is likely to compel the telecom service providers to

17. [http://articles.economictimes.indiatimes.com/2013-09-26/news/42426745\\_1\\_mnp-interconnection-telecom-solutions-number-portability-syniverse](http://articles.economictimes.indiatimes.com/2013-09-26/news/42426745_1_mnp-interconnection-telecom-solutions-number-portability-syniverse)

improve the quality of their service to avoid losing subscribers. This can be seen as maturing element of the Indian telecom industry and a natural step for the industry to go forward.

## V. Anti – Spamming Regulations

The Telecom Commercial Communications Customer preference Regulations, 2010 (“**SMS Regulations**”) have completely come into force from September 27, 2011 and prohibit Unsolicited Commercial Communications (“**UCC**”) and in turn require all telemarketers to register under the SMS Regulations.

The SMS Regulations have mandated the creation of a National Customer Preference Register, a national database with a list of the telephone numbers of all subscribers who have registered their preferences regarding receipt of commercial communications.

Subscribers have been given the option of indicating their preference by registering either under the fully blocked category or the partially blocked category.

In the fully blocked category, a subscriber opts not to receive any type of commercial communication, while the partially blocked category enables subscribers to receive commercial communications only in the categories they have chosen.

Subscribers under the partially blocked scheme may choose from a selection of categories including: banking, insurance, financial products and credit cards; real estate; education; health; consumer goods and automobiles; communication, broadcasting and entertainment; IT; and tourism.

However, transactional messages, i.e. messages that represent a transaction undertaken by the subscriber have been exempt from the purview of these regulations.

After the much litigated<sup>18</sup> cap of 200 messages per day per sim, the TRAI introduced a rule whereby any person, other than a registered telemarketer or an entity sending transactional messages, which sends more than one hundred SMS per day per SIM will have to pay an additional charge over the regular applicable SMS rates. Thus, while consumers have been allowed to send any number of messages, the TRAI has tried to de - incentivize unregistered telemarketers from using normal SIM Cards by levying an additional charge for more than 100 messages per day per sim.

## VI. Audiotex / Voicemail / Ums License

This license is a notable exclusion from the realm of the Unified License., thus a person desirous of providing such services, would need to obtain a separate Audiotex / Voicemail / UMS license before providing these services. While the Audiotex / Voicemail / UMS license does not define the services to be provided under this license, however, it is understood to include the authorization to provide, voicemail services or call conferencing services or unified messaging services. With 100% foreign investment being permitted for this license, an applicant can provide the aforementioned services upon obtaining the requisite ‘*Audiotex / Voicemail / UMS*’ license from with the DoT. However, it is pertinent to note that a prerequisite of obtaining a UMS license is having an ISP Authorization under the Unified License. In our view it will make technical and operational sense to include this license within the scope of the Unified License.

## VII. Other Services Providers (OSP)

Other Service Providers (OSPs) do not require a specific license; however a registration process is required to be fulfilled subject to fulfilling certain criteria. The most important of which is the Other Service Providers registration.

18. This matter is still sub - judice and is being heard by the Supreme Court of India

Call centers (international and domestic), BPOs, Network Operation Centers, Vehicle Tracking Systems, services with respect to tele-banking, tele-medicine, tele-education are allowed to operate (with 100% FDI) upon registration as “*Other Service Provider*” or “*OSP*” with the DoT. These OSP’s operate the service using the telecom infrastructure provided by licensed telecom service providers. There are various security related obligations imposed on various telecom licensees (as discussed later in this paper). As security related conditions are applicable to all licensed telecom service providers, the security conditions shall not be separately enforced on OSPs. An interesting development in the OSP registration policy is the amendment that was announced in August 5, 2008 which officially recognized the “*work from home*” provided certain financial guarantees are provided.<sup>19</sup>

## VIII. Telecom Infrastructure

The telecom sector is a very capital intensive sector and requires large investments. The telecom licenses permit the telecom operators to share passive infrastructure such as building, tower, dark fibre, etc. However the procurement and maintenance of active infrastructure proves to be a very expensive affair for operators. With the robust growth in the telecom sector, the government recognized that infrastructure sharing would greatly reduce costs for the operators. The DoT accepted TRAI’s recommendations and issued Guidelines on sharing of Infrastructure. Consequently, the Unified License permits sharing of infrastructure, subject to the specific conditions laid down for different authorizations. Sharing of “passive” infrastructure viz., building, tower, dark fiber, duct space, etc. between licensees is permitted for Access Services. However, sharing of active infrastructure amongst licensees shall be governed by the license conditions/amendments issued by the DoT. Similarly, ISPs, NLD and ILD authorization holders have been permitted to share “passive” infrastructure namely building,

tower, dark fiber, duct space, Right of Way owned by other authorization holders.

As a result of this policy, new entrants who are allotted spectrum by the WPC can easily launch their telecom services within a short period by taking the assistance of the existing active infrastructure of other telecom service providers will not have to incur huge infrastructural costs.

Over the years, Bharti Airtel had made huge investments to create the cellular infrastructure across the country. Soon it hived off its mobile tower business into a separate subsidiary to become a major player in the tower sharing business. Another major player, Reliance Communication (RCom), has already hived off its tower business into a separate subsidiary. With increasing operational and infrastructure costs, many telcos are now joining hands to share their existing infrastructure. Some of the deals include the following:

- In December 2007, Quippo Telecom acquired 1000 towers from Spice Telecom.
- In January 2009, Quippo Telecom and Tata Teleservices Limited merged its passive infrastructure businesses to create one of India’s largest Independent Telecom Infrastructure Company, i.e. Viom Networks.
- Vodafone, Bharti Airtel and Aditya Birla Group (Idea) have come together to form a joint venture in the form of the world’s largest tower company ‘Indus Towers’.
- Bharti Airtel in addition to its stake in Indus Towers recently went public via an initial public offering (“IPO”) for its tower business subsidiary, i.e. Bharti Infratel raising around \$800 million) from the sale of 10% of its paid-up equity in December 2012.
- Reliance Jio a new entrant into the telecom market has entered into an agreement for leasing 32,000 telecom towers owned by Reliance Infratel Limited (“RITL”), a subsidiary of Reliance Communications Limited.
- In addition to tower companies which

19. DoT Office Memorandum (Ref: No.18-2/2008-CS-I) dated August 05, 2008. <http://www.dot.gov.in/osp/Review%20of%20%20terms%20and%20conditions%20of%20osp.pdf>, visited on April 24, 2010

are owned by telecom companies other independent telecom infrastructure sharing companies like American Tower Corporation and GTL Infrastructure have expanded their reach in the past few years.

## IX. Government Departments to Grant Preferential Market Access to Indian Telecom Equipment Manufacturers

Following the lead of Department of Information Technology<sup>20</sup>, the DoT on October 5, 2012 issued a notification<sup>21</sup> granting preferential market access to domestic telecom manufacturers. The notification, mandates that domestically manufactured telecom products must be given preference, when the same is being procured by Government departments and agencies (with the exception of the Ministry of Defense which has been exempted) for their own use and not with a view to commercially resell or with a view to use

in the production of goods for commercial sale. It is proposed that the policy will be in force for a period of 10 years from the date of its notification in the official gazette.

Each Government ministry or department will now have to procure minimum percentage of their telecom product requirement fulfilling minimum value addition prescribed against each item.

The main object of the government behind this notification appears to be to protect Indian security interest as well as to give an impetus to manufacturing of high quality domestic products in India thus, lowering the effective cost of the products and elevating local innovation.

Foreign vendors have voiced concerns on this proposal and it may be challenged as a non-tariff barrier for market access.

20. Notification No. 8(78)/2010-IPHW dated 10th February, 2012

21. Notification No. 18-07/2010-IP, dated 5th October, 2012.

## 6. Spectrum Management

Spectrum refers to the use of radio waves or frequencies in telecommunications. Since spectrum is the cornerstone of telecom services worldwide and is by its very nature a scarce resource, spectrum management has become very important in recent times. In this chapter we discuss some of the important aspects of spectrum management in India as well as internationally.

### I. Ownership of Spectrum

It was once believed that spectrum is the property of the government, and hence the government could use it in a manner that suited it and that the government had exclusive rights to regulate and allocate spectrum. But post 1995 this belief has changed. This has been possible due to a historic judgment given by the Hon'ble Supreme Court of India in 1995 in the case of *Secretary, Ministry of Information and Broadcasting, Govt. of India v. Cricket Association of Bengal*<sup>22</sup> which decided that spectrum is actually public property. This judgment has changed the perception of ownership of spectrum in India and the way the government handles and manages spectrum in today's scenario.

Specifically, the Supreme Court in the aforementioned case held as follows:

*There is no doubt that since the airwaves/frequencies are a public property and are also limited, they have to be used in the best interest of the society and this can be done either by a central authority by establishing its own broadcasting network or regulating the grant of licences to other agencies, including the private agencies.*

This view of the Supreme Court was further propounded by the Supreme Court in the case of *Reliance Natural Resources Limited v. Reliance Industries Ltd*<sup>23</sup> whereby it was observed that

natural resources are vested with the Government as a matter of trust in the name of the people of India, thus it is the solemn duty of the State to protect the national interest and natural resources must always be used in the interests of the country and not private interests.

Most recently, the Supreme Court in the case of *Centre for Public Interest Litigation and Ors. Vs. Union of India (UOI) and Ors*<sup>24</sup> held that “*In conclusion, we hold that the State is the legal owner of the natural resources as a trustee of the people and although it is empowered to distribute the same, the process of distribution must be guided by the constitutional principles including the doctrine of equality and larger public good.*”

India is not the only country to hold the view that the spectrum is public property. Most of the developed countries like USA, Canada, UK, etc, hold the same view that spectrum is public property and the government is only the caretaker of this public property.

### A. Management of Spectrum in India

Spectrum management is the combination of administrative and technical procedures with legal connotations necessary to ensure efficient operation of radio communication services without causing harmful interference. There are two levels at which spectrum is managed:

1. National
2. International

#### i. International Management of Spectrum

Humans have divided territory into countries and continents, but spectrum knows no such bounds. Thus there has to be international co-operation in the management of spectrum. There are various

22. 1995 SCC (2) 161

23. (2010) 7 SCC 1

24. (2012) 3 SCC 1

international organizations for the purpose of harmonizing the use of spectrum between countries. The organizations that are addressed are ITU and APT. The role played by these organizations have already been discussed earlier.

## ii. National Management of Spectrum

Every country has different agencies managing the spectrum of that particular country. It is also a very important task as it involves an issue that affects almost the entire population of that country, the business of that country and indeed the social structure, harmony and the unity of that country.

In the Indian context, the Indian Telegraph Act, 1885 and the Indian Wireless Telegraphy Act, 1933 and Rules and Procedures made under these Acts provide the legal basis for spectrum management.

## II. Note on National Frequency Allocation Plan (“NFAP”)

The NFAP is the basis on which spectrum frequencies are allocated in India. The ITU issues the international frequency table for the purpose of giving the member countries a basis on which they can formulate their own frequency allocation plan. The NFAP is the frequency allocation plan of India. This plan clearly allocates different frequency bands for different radio-communication services. Although it allocates frequency bands for certain services, it does not give ownership rights to those services. NFAP-81 was in force till December 31, 1999 for commercial and other uses. NFAP-81 was formulated for a time, when usage of frequency bands was primarily done by the government agencies with some exploitation by private parties for their dedicated networks. However with the proliferation of new technologies in the country and the entry of the private sector in the telecommunication field the government decided it was prudent to revise NFAP-81. Accordingly, from January 1, 2000 the

NFAP-2000 replaced NFAP-81 in order to better manage the increased use of spectrum. Later NFAP 2008 which was made effective from April 1, 2009 replaced NFAP 2000. NFAP 2011 has been developed with special emphasis to encourage / promote indigenous manufacturing / technologies by provisioning of small chunk of spectrum in certain frequency band<sup>25</sup>/sub-bands in limited geographical area.

The WPC Wing of the DoT is now amidst reviewing / revising NFAP 2011 to come out with the NFAP 2013 in line with the decisions taken in the World Radio communication Conference – 2012 of the ITU.

The NFAP 2013 is not only expected to take into account the decisions of the World Radio communication Conference and the NTP 2012 but also account for the introduction of new technologies in the form of LTE, 3G and digitization of broadcasting (TV and Radio).<sup>26</sup>

## III. Standing Advisory Committee on Frequency Application (“SACFA”)

SACFA is a wing of the DoT which gives approval for radio frequency (spectrum) used by telecom service providers. Obtaining a telecom license is not enough for the operator to begin rolling out the services; a no objection from SACFA is required. This involves a detailed technical evaluation including field studies in order to determine inter alia possible aviation hazards and interference (Electro Magnetic Interference (EMI)/Electro Magnetic Compatibility (EMC)) to existing and proposed networks.

Functions of SACFA:

- i. To recommend on major frequency allocation, issues requiring co-ordination amongst the various wireless users in the country.
- ii. To formulate/review the National Frequency Allocation Plans.

25. <http://www.dot.gov.in/as/Draft%20NFAP-2011.pdf>

26. <http://www.wpc.dot.gov.in/Docfiles/Minutes%20of%201st%20NFAP%20review%20committee.pdf>

- iii. To formulate national proposals for international conferences/ meetings and to co-ordinate nationally all activities pertaining to the ITU, etc.
- iv. To deal with frequency co-ordination problems referred to the committee by the administrative Ministries/Departments.
- v. To clear sites of all wireless installations in the country.

At present, spectrum is managed through WPC Wing, SACFA and NFAP, all of which have already been discussed earlier.

## A. Auction of Spectrum

It should be noted that the government is bound to ensure that its licensing decisions are rational, transparent and free from arbitrariness. The courts have time and again upheld this principle of transparency.<sup>27</sup> In the case of *Delhi Science Forum v Union of India*,<sup>28</sup> the decision of the government to invite tenders from non-governmental and private entities for license to provide telecommunications services was challenged in a writ petition wherein it was contended that the sensitive nature of telecommunications mandated that it should not be placed in the hands of the private sector and any step in this direction would not only endanger the national security of the country but would not serve the economic interest of the country. The Supreme Court dismissed the writ and categorically held that the privatization policy adopted by the government is a necessary consequence of liberalization and the grant of telecommunications licenses to non-governmental organizations would greatly improve telecom services. However the Supreme Court also

emphasized the procedures adopted for such grant should be “*reasonable, rational and in conformity with the conditions which have been announced.*”

The Supreme Court of India in the case of *Centre for Public Interest Litigation and Ors. Vs. Union of India (UOI) and Ors*<sup>29</sup> concluded that spectrum was a natural resource and national asset and belonged to the public at large. The Apex Court criticized the first come first served policy of the government for distribution of 2G spectrum and held that a duly publicized auction is the best way of disposing public property. Consequently, the Supreme Court delivered an order against thirteen respondents<sup>30</sup> holding that such respondents had been favored by the government and had been illegally granted telecom licenses. The Supreme Court consequently issued an order cancelling 122 telecom licenses granted in various service areas for 2G spectrum. The Supreme Court also imposed financial penalties ranging from 50 lakhs (approximately USD 8333.3) to 5 Crores (approximately USD 83333.3) on the grounds that such respondents had benefited at the cost of public exchequer by a wholly arbitrary and unconstitutional decision taken by the DoT for grant of licenses and spectrum. Further, the Court also ordered the re-auction of the spectrum that had been made available due to the cancellation of the telecom licenses.

Thus, going forward the disposal of spectrum will only be done via a duly publicized auction.

Our detailed analysis of this judgment of the Supreme Court is available in our hotline which is available as Annexure B.

27. AIR 1996 SC 1356

28. (2012)3SCC1

29. 1996 SCC (2) 405

30. Respondents in this matter are as follows (1) Union of India through its Secretary, Department of Telecommunications, (2) Etisalat DB Telecom Pvt. Ltd. (Swan Telecom), (3) Unitech Wireless Group (4) Loop Telecom Pvt. Ltd. (ShippingStop Dotcom P. Ltd.), (5) Videocon Telecommunications (Datacom Solutions Pvt. Ltd.) (6) S Tel Ltd., (7) Allianz Infratech (P) Ltd., (8) Idea Cellular Ltd. & Aditya Birla Telecom Ltd. (Spice Communication Pvt. Ltd.), (9) Tata Teleservices Ltd., (10) Sistema Shyam Tele Services Ltd. (Shyam Telelink Ltd.) (11) Dishnet Wireless Ltd. & Aircel Ltd., (12) Vodafone Essar South Ltd. & Vodafone Essar Spacetel Ltd., (13) TRAI



## 7. Foreign Investment

### I. Foreign Investment Regime in India

India's foreign investment regime is governed by the Foreign Direct Investment ("FDI") policy. As per the FDI policy, there are certain sectors wherein 100% FDI is allowed (such as software development and telecom), whereas there are certain sectors wherein no FDI is allowed at all (such as gambling).. Furthermore some investments can be made under the automatic route (i.e. without any government approval) whilst others require prior approval of the government. The Department of Industrial Policy & Promotion ("DIPP") is responsible for formulation and implementation of promotional and developmental measures for growth of the industrial sector, keeping in view the national priorities and socio-economic objectives.

The telecom sector in India has always been a sensitive and regulated sector and the government has been wary of allowing foreign participation. However the outlook of the government and the

industry is fast changing. For the longest time, the intention of the government was that the majority of the shares of a telecom licensee company should be held by Indian shareholders; as a result foreign companies and investors were only allowed to hold up to 49% of the equity of a telecom licensee. Since liberalization, every successive government has encouraged FDI. In 2005, in pursuance of the government's commitment to further liberalize the FDI regime, the government revised the percentage sectoral cap to allow total foreign equity in telecom licensee companies to as much as 74%.<sup>31</sup>

In 2013, the government in an attempt to attract additional foreign investment has allowed 100% foreign investment into the telecom sector.<sup>32</sup> This move is expected to give an impetus to funding, consolidation, restructuring and exits for telecom operators and their shareholders including private equity investors.

The current regime in respect of permissible FDI in the telecom sector is as follows:

Sector	FDI Permitted	Method
Basic, Cellular, United Access Services, National/ International Long Distance, Commercial V-Sat, Public Mobile Radio Trunked Services (PMRTS), Global Mobile Personal Communications services (GMPCS), All types of ISP licences, Voice Mail/Audiotex/UMS, Resale of IPLC, Mobile Number Portability services, Infrastructure Provider Category-I (providing dark fibre, right of way, duct space, tower) except Other Service Providers	up to 100%	Automatic up to 49% and FIPB approval required beyond 49%
Manufacture of telecom equipments	100%	Automatic
Other Service Providers	100%	Automatic

The total FDI equity inflows in telecom sector have been USD 12,865 million from April 2000 till May 2013.<sup>33</sup>

31. Press Note No. 5 (2005 Series): Enhancement of the Foreign Direct Investment Ceiling from 49% to 74% in the Telecom Sector. Refer [http://siadipp.nic.in/policy/changes/pn5\\_2005.pdf](http://siadipp.nic.in/policy/changes/pn5_2005.pdf), visited on May 26, 2009

32. Press Note 6 (2013 Series)

33. <http://www.indianexpress.com/news/telecom-sector-received-rs-58782-cr-fdi-in-last-13-years/1156800/>

## Sector-wise FDI Inflows from APRIL 2000 to FEBRUARY 2011

Sl. No.	Sector	% of Total Inflows
1.	Services Sector	21
2.	Telecommunications	8
3.	Computer Software & Hardware	8
4.	Housing & real estate	7
5.	Construction activities	7
<b>Sector Total</b>		100.00

*Source: Department of Telecommunications<sup>34</sup>*

## II. Calculation of FDI

Foreign Investment can be direct or indirect.

- Direct foreign investment means investing directly into the investee (licensee) company; and
- Indirect foreign investment means foreign investment in the company/companies holding shares of the investee (licensee) company and their holding company/companies or legal entity (such as mutual funds, trusts, etc).

Both direct and indirect foreign investment in the licensee company shall be counted for the purpose of FDI ceiling. The FDI Policy further lays down that Foreign Investment shall include investment by:

- i. Foreign Institutional Investors (FIIs);
- ii. Non-resident Indians (NRIs);
- iii. Foreign Currency Convertible Bonds (FCCBs);
- iv. American Depository Receipts (ADRs);
- v. Global Depository Receipts (GDRs); and
- vi. Convertible preference shares held by foreign entity.

Calculation of FDI in the telecom sector shall be calculated in the following manner:

- i. Both direct and indirect foreign investment in the Licensee Company shall be counted for the purpose of FDI ceiling. Foreign Investment shall include investment by Foreign Institutional Investors (FIIs), Non-resident Indians (NRIs), Foreign Currency Convertible Bonds (FCCBs), American Depository Receipts

(ADRs), Global Depository Receipts (GDRs) and convertible preference shares held by foreign entity.

- ii. All investments directly by a non-Indian resident entity into the Indian investee company would be counted towards foreign investment.
- iii. Though indirect investment would continue to be considered and included for the purpose of calculating FDI in the company, for the purpose of calculating indirect foreign investment, foreign investment through the investing Indian company would not be considered in case the investing Indian company is 'owned and controlled' by resident Indian citizens on a look through basis.
- iv. The indirect foreign investment in 100% owned subsidiaries of operating-cum-investing/ investing companies, will be limited to the foreign investment made in the operating-cum-investing/ investing company.
- v. An investing company is said to be 'owned' by resident Indian citizens when more than 50% of the equity interest of such investing company is beneficially owned by (a) resident Indian citizens and (b) companies which are owned and controlled by resident Indian citizens.
- vi. An investing company is said to be 'controlled' by (a) resident Indian citizens and (b) Indian companies which are owned and controlled by resident Indian citizens are which if such Indian citizens and Indian companies have the power to appoint the majority of the directors of the investing company.

<sup>34</sup> [http://dipp.nic.in/English/Publications/FDI\\_Statistics/SECTOR-WISE-INFLOWS.pdf](http://dipp.nic.in/English/Publications/FDI_Statistics/SECTOR-WISE-INFLOWS.pdf)

The Unified License, requires licensee to declare the Indian and Foreign equity structure (both direct and in-direct) in the licensee company and submit a compliance report regarding compliance with FDI norms and security conditions on 1st day of January and 1st day of July of every year to the DoT certified by Company Secretary or Statutory Auditor, countersigned by duly authorized Director of such company.

### III. Down Stream Investments

The government has also introduced guidelines for downstream investment by Investing Indian Companies 'owned or controlled by non-resident entities' which states that if FDI is provided to a company ("Investing Company") 'owned' or 'controlled' by non-resident entities, any downstream investment made by such Investing Company would require FIPB approval, irrespective of the amount of investment. The intention of the government is very clear that they want to control the activities of foreign owned or controlled investment holding companies in India and their downstream investments. Therefore even though FIPB approval is required only if FDI exceeds 49% in the telecom sector, in the aforesaid example, any amount of FDI would require the prior approval of the government. As an exception the indirect foreign investment in only the 100% owned subsidiaries of operating cum investing/ investing companies will be limited to the foreign investment in the operating cum investing/ investing company. This exception is made since the downstream investment of a 100% subsidiary of the holding company is akin to investment made by holding company and the downstream investment should be a mirror image of the holding company. This exception however is strictly for those cases where the entire capital of the downstream subsidiary is owned by the holding company.

*Illustration: Telecom Company A has FDI of 74%. If Company B is 100% held by Telecom Company A, then 74% of Company B would be treated as indirect foreign equity and the balance would be treated as resident held equity.*

## IV. License Provisions

The licenses themselves have a number of provisions which can be seen as quite restrictive. These are mostly security driven restrictions and have not led to any dampening of foreign interest in this sector. Some of these restrictions are discussed as follows:

- i. Telecom licenses are only granted to companies which are registered in India;
- ii. The majority of directors of the board of the company have to be Indian citizens;
- iii. Certain positions which are instrumental to the operations of the company such as Chief Officer in charge of technical network operations, Chief Security Officer and Officials dealing with lawful interception of messages have to be occupied by resident Indian citizens;
- iv. Certain key positions (such as chairman, managing director, chief executive officer and/ or chief financial officer), if held by foreign nationals are required to be security vetted by the Ministry of Home Affairs.

### A. Other Security Related Requirements

- Details of infrastructure/network diagram could be provided on a need basis only to telecom equipment suppliers/manufacturers and affiliate/parent of licensee company. Clearance of DoT would be required if such information is to be provided to anybody else.
- Licensee company should ensure that the information transacted through their network is secure and protected.

## 8. Mergers and Acquisitions in The Indian Telecom Sector

With the liberalization of the Indian economy, the telecom sector has become very attractive for mergers and acquisitions. Some of the big deals that have taken place in the Indian telecom include the following:

- SingTel increasing its stake in Bharti telecom from 30.8 % to 32.34 % in 2013;
- Reliance Industries Limited acquiring 95% of the equity shares of Infotel Broadband Services to gain access to the BWA spectrum won by Infotel Broadband Services.
- Aditya Birla Telecom acquiring Spice Telecom
- Providence's investment into Aditya Birla Telecom in 2009
- Vodafone taking over Hutchison-Essar in 2007
- Malaysia Telekom's 49% stake in Spice Telecom
- Temasek Holdings' 9.9% stake in Tata Teleservices through its wholly-owned subsidiary Aranda Investments Mauritius

M&A in India is subject to various laws the principle of them being The Companies Act 1956, Income Tax Act 1961 and the Takeover Code (for public listed companies). Regulatory considerations are also equally important to take note of in telecom M&A.

### I. DoT Guidelines on M&A

The much awaited merger guidelines in the telecom sector were issued by the Ministry of Communications and Information Technology, Department of Technology (“DoT”) on February 20, 2014. The ‘*Guidelines for Transfer/Merger of various categories of Telecommunication service licences/authorisation under Unified Licence on compromises, arrangements and amalgamation of the companies*’ dated February 20, 2014 (“**M&A Guidelines**”) supersede the earlier ‘*Guidelines for intra service area merger of Cellular Mobile*

*Telephone Service (CMTS)/ Unified Access Services (UAS)*’ dated April 22, 2008 (“**Old M&A Guidelines**”).

These M&A Guidelines follow in the wake of the decision of the DoT to remove foreign investment limits in this sector, introduction of the Unified License regime and TRAI’s recommendations<sup>35</sup> on this subject.

We have analyzed some important aspects of these guidelines:

#### A. Prior Approval of the DoT

The Unified License requires prior written approval of the DoT before transfer or assignment of any existing license. The Unified License has clarified that with respect to court approved mergers and acquisitions, any scheme of amalgamation or restructuring filed with the court must be drafted in a manner that the transaction requires the prior written approval of the DoT.

Presently neither the Unified License nor the M&A Guidelines provide clarity as to when the DoT needs to be approached for its approval, i.e. whether such approval may be sought simultaneously with the court approval process or if one would need to seek such approval from the DoT after the completion of the court approval process.

The M&A Guidelines also state that the DoT must provide its recommendations / objections to a scheme for compromise, arrangement or amalgamation of a company within 30 days of receipt of notice of such compromise, arrangement or amalgamation. This is a welcome step as it

35. TRAI Recommendations on Spectrum Management and Licensing Framework- Response of the Authority on DoT reference dated 03.11.2011 and TRAI Recommendations on Spectrum Management and Licensing Framework dated 11.05.2010 available at [www.trai.gov.in](http://www.trai.gov.in)

seeks to bind the DoT in providing a time bound response to any application placed before it. However the M&A Guidelines do not provide guidance as to grounds on which the DoT may reject the scheme. As such there are no guidelines which interested parties may keep in mind which drawing up the scheme for compromise, arrangement or amalgamation. Given this position, it may be worthwhile for parties to consider approaching the DoT before approaching the Courts.

## B. Validity of the License

Consequent to a merger or amalgamation the acquired company's license is subsumed into the resultant entity. The term of the resultant entity's license will be the higher of the two periods of the former licenses.

Importantly it has been clarified that the validity period of the spectrum shall remain unchanged regardless of any merger. This is in line with the government's policy of delinking spectrum from the license which has also been specifically included in the Unified License. The implication is that the resultant entity's cannot piggy back on the (longer) license term of the acquired entity and claim to have longer spectrum validity – since spectrum is considered a separate asset, it will have a life of its own.

## C. Lock In on Sale of Shares

Under the Old Guidelines, mergers were only allowed after completion of 3 years from the effective date of the license. While the M&A Guidelines do not contain any such express restriction they mandate that any lock in imposed on an entity pursuant to any spectrum auction shall also be applicable on the shares issued pursuant to an amalgamation or merger. This basically means that there would be no easy exit for new entrants. Before the Unified License was

announced, the provisions of the old UAS license contained a three year lock in restriction for the sale of shares on persons whose share capital in the company was 10% or more and whose net worth has been taken into consideration while determining the eligibility of the company for the UAS license.<sup>36</sup> At that time, spectrum was bundled with the license and such restriction were necessary in order to restrict non serious players from acquiring UAS licenses (and therefore the spectrum that came along with the license) with the sole purpose of profiting from trading in spectrum. However in today's scenario where spectrum is de linked from the license and operators have to pay dearly to acquire spectrum, it may be argued that there is a presumption that only serious players would enter this market. In such a case, operators may find such a restriction very onerous. Additionally, this change in policy also seems to be in line with the Government's proposed strategy of allowing spectrum trading,<sup>37</sup> whereby telecom operators will be allowed to buy and sell spectrum. Guidelines for spectrum trading are expected to be announced soon.

## D. Easing of Rules to Avoid Monopoly in the Market

### i. No Prohibition on Number of Service Providers in the Market

The Old Guidelines prohibited any mergers or amalgamations if the number of service providers fell below 4 in any circle where such merger or amalgamation was being proposed. There is no such prohibition in the M&A Guidelines. This cap on minimum number of players in a particular market was prohibitive towards consolidation activity since it would lead to multiple players having a small share of the market. Additionally, it appears that the introduction of an anti-trust regulator in the form of the Competition Commission of India would in turn assuage concerns of market concentration which was one

36. Our analysis on the lock in of shares is available at: [http://www.nishithdesai.com/information/research-and-articles/nda-hotline/nda-hotline-single-view/article/indian-government-mandates-equity-lock-in-for-telecom-company.html?no\\_cache=1&cHash=93bb3214edbc4c1fb405eod97bo7564b](http://www.nishithdesai.com/information/research-and-articles/nda-hotline/nda-hotline-single-view/article/indian-government-mandates-equity-lock-in-for-telecom-company.html?no_cache=1&cHash=93bb3214edbc4c1fb405eod97bo7564b)

37. <http://www.thehindubusinessline.com/economy/dot-set-to-allow-spectrum-trading/article5706826.ece>

of the primary reasons for having a minimum number of players in the market.

## ii. Cap on Spectrum the Resultant Entity can hold in an Area and the Cap on Total Spectrum Holding

The M&A Guidelines lay down that the resultant entity cannot hold more than 25 % of the total spectrum assigned for access services and 50 % of spectrum assigned in a given band in every circle. The guidelines further lay down that companies will be given a period of one year to surrender the excess spectrum over the above mentioned threshold failing which suitable action may be initiated by the DoT.

## iii. Cap on Market Share of the Resultant Entity Raised to 50%

The Old Guidelines stated that a merged entity could not hold more than 40% of the revenue or users in any particular telecom circle. Under the M&A Guidelines, the merged entity will now be allowed to have up to 50 % market share in any circle calculated on the basis of the subscriber base and Adjusted Gross Revenue. Entities which exceed this threshold have a window of one year to reduce their market share to 50% failing which DoT would have the liberty to take suitable action against the entity.

India has one of the most fragmented telecom industries in the world with 10 to 12 operators in each of the country's 22 telecom circles.<sup>38</sup> It was long felt that the stringent anti-monopoly rules in the Indian telecom sector were proving to be a roadblock to consolidation efforts. In an effort to boost consolidation the Government has removed the requirement to have a minimum number of operators in a circle. However the increase in the market cap from 40% to 50% may not prove to be a very significant increase for the bigger players since any acquisition by them may breach these caps. However smaller companies may find it

easier to enter into acquisitions either by being acquired by larger companies or merging with each other. Airtel recently announced its intention of acquiring Loop Mobile's assets in Mumbai by virtue of which Airtel would become the largest operator by subscriber base beating the existing market leader, Vodafone.<sup>39</sup>

## E. Acquirer to Pay Difference Between the Market Price of Spectrum and the Entry Fee Paid by the Target

One of the most stringent guidelines introduced is when a company acquires another company which holds spectrum, allotted to it under the old regime (i.e. spectrum bundled with license). In such a situation, the resultant entity must pay the Government the difference between the entry fee paid by the target and actual market price of spectrum. The amount to be paid is to be calculated from the date of approval granted by the relevant authority till the remainder of the license, on a pro-rata basis. This basically means that acquirers will need to pay a huge amount as spectrum fees to the government in addition to consideration that it would anyways have to pay for the acquisition. Acquirers may argue that this is an attempt to retrospectively apply auction prices to spectrum that was allocated as part of license as per the prevailing law at that time. However the governments could support their stand by their commitment to create a level playing field, especially in the background of the spectrum scam.

The guidelines have set out a mechanism for calculation of market price, i.e. SBI PLR to be added to the last auction determined price. Such calculation shall be done only after one year since the auction determined price of spectrum is valid for one year.

Such fees will not be applicable to spectrum acquired through auction such as the valuable 3G spectrum.

38. [http://www.business-standard.com/article/companies/m-a-policy-fails-to-stir-telecom-sector-114030301244\\_1.html](http://www.business-standard.com/article/companies/m-a-policy-fails-to-stir-telecom-sector-114030301244_1.html)

39. <http://www.thehindubusinessline.com/features/smartbuy/powered-by-loop-airtel-to-challenge-vodafone-in-mumbai/article5714100.ece>

Further if there any disputes with respect to such one-time fee, the M&A Guidelines have laid down that pending resolution of the dispute, the amount computed as the one-time fee must be deposited with the DoT in the form a bank guarantee. Therefore, this would effectively mean that companies will not be able to use the funds set aside for the bank guarantee until their dispute is finally resolved, which in the Indian context may take considerable time. However, this may also mean that if the dispute is solely with respect to the computation of the one-time fee, the company should be allowed to use the spectrum as soon as it has deposited the bank guarantee and should not be precluded from using the same until the resolution of the dispute.

## II. Unified License

The Unified License, has introduced a clarification that has been made with respect to court approved merger and acquisitions which provides that any scheme of amalgamation or restructuring filed with the court must be drafted in a manner so that such amalgamation or restructuring shall be effective only after the written approval of the DoT for such transaction. It should be noted that there have been various rounds of litigation wherein the DoT's role has been challenged vis-à-vis approval from the Courts in the case of a court approved merger.<sup>40</sup> As such this clarification makes clear the DoT's position in this issue.

However, there is no clarity on when the DoT will need to be approached for such approval. It is not clear whether such approval may be sought simultaneously with the court approval process or if one would need to seek such approval from the DoT after the completion of the court approval process.

## III. Competition Act, 2002

In the context of discussing SMPs it would also

be relevant to keep in mind the provisions of the Competition Act 2002 which provides that no company shall abuse its dominant position. It should be noted that dominance per se is not illegal; its abuse is. The aim of the Competition Act is to prevent enterprises taking advantage of their market strength to abuse their dominance by using anti competitive business practices. The Competition Act (Section 4(2)) prescribes a list of practices which are broadly classifiable into exploitative and exclusionary, engaged by a dominant enterprise, alone or in concert, which are prohibited;

- i. Imposing of unfair or discriminatory price (including predatory price) or condition, directly or indirectly, in purchase or sale of goods or services; or
- ii. Indulging in practices resulting in denial of market access in any manner; or
- iii. Making conclusion of contracts of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts; or
- iv. Using the dominant position in one relevant market to enter into, or protect, another relevant market; or
- v. Limiting or restricting the production or provision of, or the technical or scientific development relating to, goods or services.

It is pertinent to note that the practices prohibited under Section 4(2) of the Competition Act are only with respect to abuse by enterprises which enjoy a dominant position. The Competition Act defines "dominant position" as a position of strength enjoyed by an enterprise in the relevant market in India, which enables it to:

- i. Operate independently of competitive forces prevailing in the relevant market; or
- ii. Affect its competitors or consumers or the relevant market in its favour.

Further, the Competition Commission of India ("CCI") on May 11, 2011 issued the Competition

40. [http://articles.economictimes.indiatimes.com/2012-07-13/news/32663691\\_1\\_idea-spice-merger-licence-and-merger-guidelines-tdsat](http://articles.economictimes.indiatimes.com/2012-07-13/news/32663691_1_idea-spice-merger-licence-and-merger-guidelines-tdsat)

Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 (“**Combination Regulations**”). These Combination Regulations will now govern the manner in which the CCI will regulate combinations which have caused or are likely to cause appreciable adverse effect on competition in India (“AAEC”). For more details on other

requirements, please refer to our analysis at the links

[http://www.nishithdesai.com/New\\_Hotline/Competition/Competition\\_Law\\_hotline\\_May1311.htm](http://www.nishithdesai.com/New_Hotline/Competition/Competition_Law_hotline_May1311.htm) and

[http://www.nishithdesai.com/New\\_Hotline/Competition/Competition%20Law%20Hotline\\_May3111.htm](http://www.nishithdesai.com/New_Hotline/Competition/Competition%20Law%20Hotline_May3111.htm)



## 9. Security Issues in the Telecom Industry

The DoT has constantly been trying to keep up with changes in technology and in this regard has been introducing various amendments to existing licenses with respect to security. The DoT has issued various notifications imposing onerous obligations and restrictions particularly with respect to foreign telecom vendors.<sup>41</sup> These notifications created a lot of uncertainty in the industry both within the vendor community and among the telecom licensees as to the scope and ambit of the requirements. However, the government has included a separate chapter on security conditions as part of the Unified License, which consolidates all the security conditions that are to be complied with by licensees.

### I. Salient Features of the Security Conditions Applicable under the Unified License

#### A. Certification and Internal Security Policy

All telecom licensees are required to induct only those network elements which have been tested as per relevant contemporary Indian or International Security Standards. For example, IT and IT related elements must be tested against ISO/IEC 15408 standards, for Information Security Management System against ISO 27000 series Standards etc. The certification shall be done only from authorized and certified agencies/ labs in India or as may be specified by the DoT. Thus, network elements must be tested in Indian laboratories unless otherwise allowed by the DoT. The DoT is to provide an illustrative list of certain certified agencies on their website. Further the telecom licensees also have to conduct a yearly audit on their networks from a security standpoint. The first audit may be carried out in the financial year succeeding the financial year of the signing of a particular license/

service authorization under the Unified License. Audit may be carried out by any agency as per relevant ISO standards.

In addition:

- i. The telecom licensee is obligated to (i) maintain relevant security standards while procuring the telecom equipment, and (ii) a list of features, equipments, software, which list must be open to inspection at the discretion of DoT (iii) create facilities for intrusion detection and monitoring within 12 months of effective date of the license/ authorization under the Unified License.
- ii. Only Indian residents shall be eligible to be employed as key officers<sup>42</sup>
- iii. Telecom licensee has been obligated to maintain a record of operation and maintenance procedures, not limited to, operation and maintenance command log, user-ids; software updates and changes and supplier chain.

#### i. Analysis

The security conditions do not clarify which elements of the telecom network need to be audited. As such the scope of the audit is apparently very broad. Further, in light of the fact that the security standards to be followed are international standards, mandating testing to be performed only by Indian laboratories may not be necessary and may pose impediments to the efficiency of the entire process and raises a number of intellectual property and confidentiality concerns.

#### B. Inspection

The telecom licensees must ensure that their vendor agreements with their vendors contain

41. [http://www.nishithdesai.com/information/research-and-articles/nda-hotline/nda-hotline-single-view/article/stringent-rules-for-foreign-telecom-vendors.html?no\\_cache=1&cHash=a3cd62e63933be995067d24aad21605e](http://www.nishithdesai.com/information/research-and-articles/nda-hotline/nda-hotline-single-view/article/stringent-rules-for-foreign-telecom-vendors.html?no_cache=1&cHash=a3cd62e63933be995067d24aad21605e)

42. Chief Technical Officers, Chief Information Security Officer, Nodal Executive and System Administrators.

provisions enabling the , the telecom licensee and/ or DoT (or its agencies) to inspect the hardware/ software, design, development, manufacturing facility and supply chain and subject all software to a security/threat check at any during the supply of telecom equipment by the vendors. Such inspection shall be limited to two per purchase order .....under the vendor agreements. Where the relevant purchase order value if more than INR 50 crores and the duration of such visits exceeds 40 man days per visits, the costs shall be borne by the telecom licensee or can be passed on to the vendors.

The Unified License also lists out the contours of the provisions which may be incorporated into the agreement to be executed between the telecom licensee and the vendor so that the vendor supplied equipment is “safe to connect” in the network. The DoT has made available a template agreement with suggested clauses which the telecom licensees and vendors may use as a base template.

#### i. Analysis

This provision appears to be quite onerous and invasive.

- i. As emphasized above, the likelihood of manufacturing facilities and supply chain stretching across multiple geographies is very high. While the DoT’s mandate of being allowed to inspect all stages and components of a supply chain (including the actual manufacturing facilities) may be agreed contractually with the telecom licensee and the vendor, in spirit this requirement is akin to the DoT assuming extra-territorial jurisdiction which it and the telecom licensee may not be able to enforce. Further, in any event, the local regulatory environment of such geographies may not permit such interference by a foreign regulator which in turn may defeat the implementation of this provision. The Vendor will generally be bound by strict confidentiality provisions with its suppliers and manufacturers and it will be impossible for them to agree to such provisions without

committing a breach of their confidentiality obligations.

- ii. Since the Unified License does not provide any specific instances which would trigger the DoT’s inspection rights, it could be interpreted that the DoT has an unfettered right of inspection irrespective of any actual cause or reason to believe that a security breach has occurred or is threatened.
- iii. The Unified License does not specify the manner in which the inspection costs are to be borne for purchase orders whose value is less than INR 50 crores or where the inspection duration is less than 40 man days.

### C. Penalties

#### i. Monetary

The Amendment has attempted to differentiate between an intentional breach and an inadvertent breach.

- i. Penalty of up to INR 50 crores has been prescribed for any security breach caused due to inadvertent inadequacy (“**Inadvertent Breach**”). The DOT shall set up a five member panel which will determine whether the breach is due to such inadvertent inadequacy and the amount of penalty.
- ii. Penalty of INR 50 crores has been prescribed for any intentional omissions / deliberate vulnerability or deliberate attempt for security breach (“**Intentional Breach**”).

#### ii. Cancellation and Blacklisting

In addition to the monetary liabilities on the telecom licensees, the DoT may also cancel the license of the telecom licensee as well as blacklist any vendor/supplier of telecom equipment from doing business in India. The DoT has mandated the insertion of a clause in agreements with vendors / suppliers allowing the DoT, to blacklist such vendor/supplier in all equipment procurement agreements entered into by the telecom licensee.

### a. Analysis

Although the DoT has attempted a differentiation between an Intentional Breach and an Inadvertent Breach, they have not defined what would be deemed to be an “inadvertent inadequacy”. The telecom licensee or the Vendor have not been provided the right to any due process or appeal from the decision of the DoT committee. This is against the principles of natural justice.

The Unified License does not prescribe any procedure which is to be followed in the determination of an Intentional Breach. It is also unclear whether the DoT committee (*which determines events of Inadvertent Breach*) would determine events of Intentional Breach. Further, since Intentional Breach implies a higher degree of culpability on the telecom licensee and/or the Vendor, it is surprising that the DoT has not prescribed any adequate due process to be followed in determining such liability.

The provisions pertaining to blacklisting are perhaps the most draconian. The DoT has assumed absolute power to discredit the vendors/suppliers without following the principles of natural justice. However, it is unclear what “blacklisting” means. Various interpretations could arise, e.g.: (i) the vendor not being able to carry any further business in India (*this could be time bound of perpetual*); (ii) the vendor not being able to supply only those products which caused the security breach; (iii) the vendor not being able to supply products for a particular territory etc.

In our view, apart from clarifying the various ambiguities in the Unified License with respect to intentional and inadvertent breach, the DoT must ensure a transparent due process in determining whether any breach has been committed.

The aim of the Government in implementing the Unified License is to address the concerns of the industry arising out of the notifications issued in the past by the DoT and address security concerns connected with this industry.

## II. Phone Tapping under the Indian laws

The Indian Telegraph Act, 1885 gives the government the right, for reasons to be recorded in writing, to intercept messages on the occurrence of any public emergency, or in the interest of the public safety, if the government is satisfied that it is necessary or expedient so to do in the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States or public order or for preventing incitement to the commission of an offence. The government is also planning to table a Right to Privacy Bill in Parliament shortly. News reports suggest that this bill will stringently deal with unauthorized interception of telephone calls and unauthorized disclosure of content to the public.

## III. Encryption

It is often difficult to physically secure access to networks. Encryption is a method of sending secured messages or data from one network to another or over networks.

Various telecom licenses, especially ISP Agreements, have a standard clause in the license agreement which states

*“The Licensee shall ensure that Bulk Encryption is not deployed by ISPs. Further, Individuals/Groups/Organizations are permitted to use encryption up to 40 bit key length in the symmetric key algorithms or its equivalent in other algorithms without obtaining permission from the Licensor. However, if encryption equipments higher than this limit are to be deployed, individuals/groups/organizations shall obtain prior written permission of the Licensor and deposit the decryption key, split into two parts, with the Licensor.”*

Though the law permits encryption only up to 40 bits, modern technologies enable much higher encryption. Research in Motion Limited, the makers of BlackBerry services of 256 bits.

The Ministry of Home Affairs has been raising concerns over this issue since 2008. The BlackBerry security architecture for enterprise customers is specially designed to exclude the capability for RIM or any third party to read encrypted information under any circumstances. It appears that BlackBerry had to finally setup a server in India to aid Indian intelligence agencies to monitor suspicious activities.<sup>43</sup>

The IT Act also empowers the Government of India to make specific rules relating to the modes or methods of encryption of; however the government has not yet come out with specific guidelines

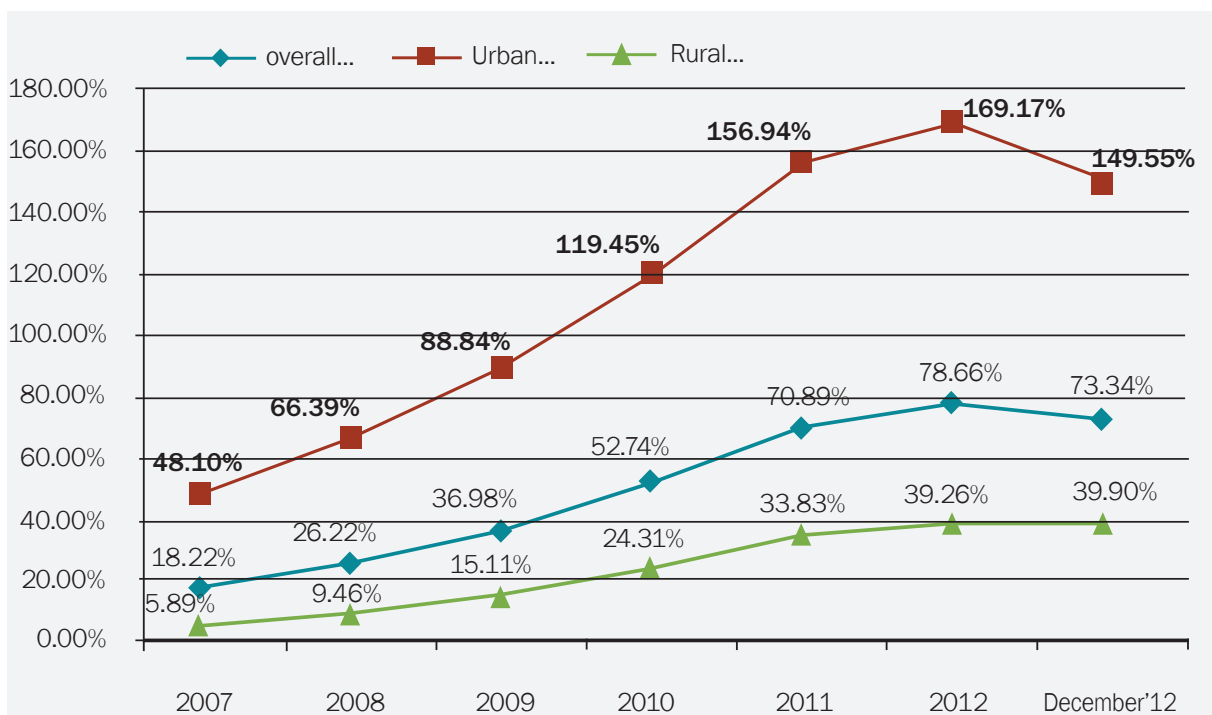
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43. <http://timesofindia.indiatimes.com/tech/tech-news/telecom/BlackBerry-sets-up-server-in-Mumbai-to-aid-interception/articleshow/11969224.cms>

## 10. Opportunities in the Telecommunications Industry in India

Today the Indian telecommunications sector with an approximate subscriber base of 906.8 million connections (as of the financial year 2013).<sup>44</sup> In a knowledge based economy, it is natural that broadband connectivity directly correlates with the growth of economy, as it helps improve the flow of information across various elements of the economy. As per the Department of

Telecommunications Annual Report, 2012-13,<sup>45</sup> the broadband subscribers grew from a meager 0.18 million as on March 2005<sup>46</sup> to about 14.98 million at the end of December 2012. This report also places reliance on the objectives of the NTP, which aim to achieve 175 million broadband connections by the year 2017 and 600 million by the year 2020 available at minimum 2 Mbps speed of download.



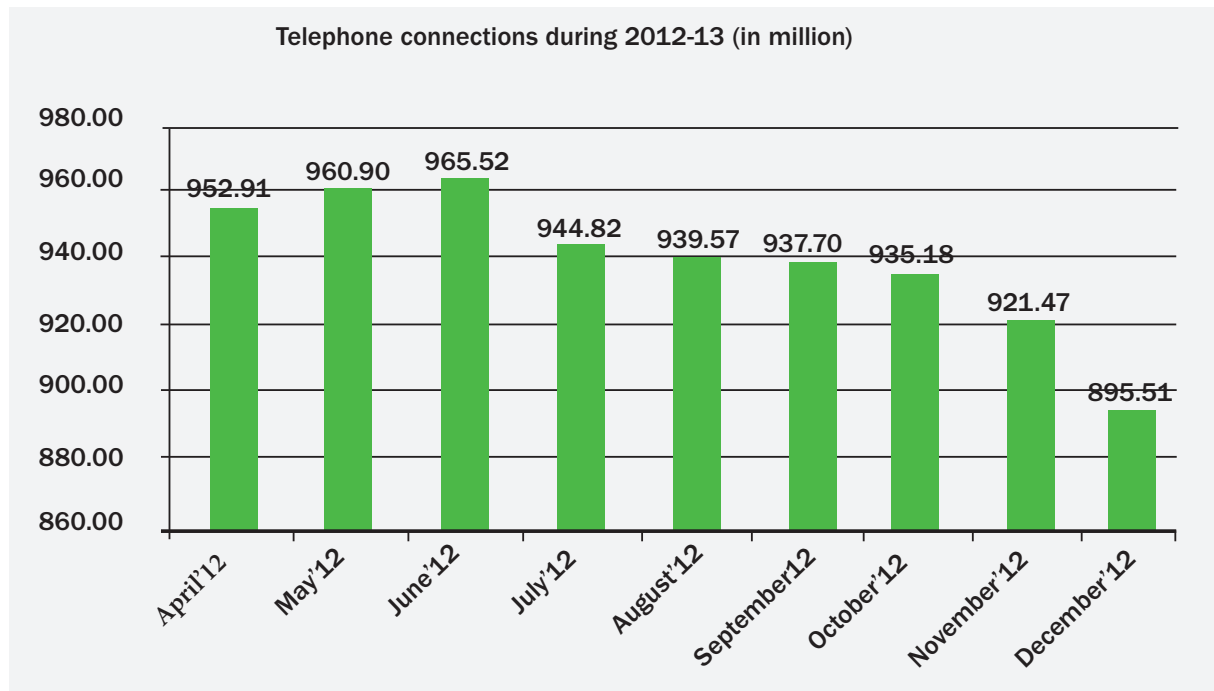
Source: Department of Telecommunications, Annual Report 2012 – 2013 at page 3

44. <http://traai.gov.in/WriteReadData/WhatsNew/Documents/PR-TSD-Aug,%202013.pdf>

45. [http://www.dot.gov.in/sites/default/files/Telecom%20Annual%20Report-2012-13%20\(English\)%20\\_For%20web%20\(1\).pdf](http://www.dot.gov.in/sites/default/files/Telecom%20Annual%20Report-2012-13%20(English)%20_For%20web%20(1).pdf)

46. [http://www.dot.gov.in/sites/default/files/AR\\_English\\_2008-09\\_o.pdf](http://www.dot.gov.in/sites/default/files/AR_English_2008-09_o.pdf)

## I. Tele-Density



*Source: Telecom Regulatory Authority of India: Annual Report 2013 - 2014*

While there has been a slowdown in the growth of the telecom sector, experts believe that there still remains huge untapped potential in the Indian telecom market. AT Kearney, a global management consulting firm, in their report on the Indian Telecom Sector in 2012,<sup>47</sup> have made the following predictions in this regard:

- Mobile data traffic is expected to grow at 126% CAGR from 2011-2016 and account for 75% of wireless operator's traffic and over 30% of revenues by 2016.
- Smart Phones in 2008 occupied roughly 3.8% of telecom hardware related sales, recorded a slight growth of 8.1% in 2011 and is estimated to touch a figure of 25% in 2016.
- Mobile Value Added Services are expected to grow to a size of INR 48000 Crore by 2015 at a CAGR of more than 30%.

Various factors are believed to fuel the growth and attractiveness of the Indian telecommunications industry, such as:

- i. An expanding Indian economy with increased focus on the services sector;

- ii. Favourable demographics with population mix moving favorably towards a younger age profile;
- iii. Rising disposable income of consumers;
- iv. Falling tariffs; and
- v. Presence of skilled labour pool particularly in the metros and tier 2 cities.

## II. Challenges Faced by the Indian Telecommunications Industry

Even though the Indian telecommunications sector has come a long way since the time of liberalization and promises growth, there are a number of issues which still pose a challenge to its progress. Two critical issues are:

### A. Declining Average Revenue Per User ("ARPU")

The Indian telecommunications sector is a highly competitive sector. A sustained price war in the

47. Accessible at [http://www.atkearney.in/images/india/pdf/AT-Kearney-Telecom-Report-2012\\_Upload.pdf](http://www.atkearney.in/images/india/pdf/AT-Kearney-Telecom-Report-2012_Upload.pdf)

industry has resulted in declining ARPUs. In the present market conditions, between March 2007 and September 2012, the ARPU for India's CDMA mobile users declined by 61.5% whereas the decline in the ARPU for GSM mobile users has been 68.1%.<sup>48</sup> The minutes of usage per user (or connection) for GSM has decreased by 27.38% while CDMA users reported a decline of 52.22%.<sup>49</sup>

## B. Lack of Telecom Infrastructure

Operators have to incur huge capital costs to provide telecommunications services in the rural areas of India. Added to this cost is the logistical challenge posed by the lack of supporting

infrastructure such as lack of roads and electricity. For example, one of the biggest costs being incurred by tower operators is towards diesel / generator costs since supply of electricity in India is very erratic. Research reports suggest that, on average, 70 percent of the approximately 400,000 mobile towers in India face electrical grid outages in excess of 8 hours a day.<sup>50</sup> The telecom tower industry in India is estimated to consume over 2.5 billion litres of diesel annually making it the second largest consumer of diesel in the country.<sup>51</sup> The resulting energy costs alone account for 25 percent of the total network operating costs affecting the profitability of the operators.<sup>52</sup>

48. Chart: ARPU vs Minutes Of Use For India's CDMA & GSM Mobile Base – March 2007 to September 2012 accessible at [www.medianama.com/2013/04/223-india-mobile-arp-minutes-cdma-gsm-2/](http://www.medianama.com/2013/04/223-india-mobile-arp-minutes-cdma-gsm-2/)

49. Chart: ARPU vs Minutes Of Use For India's CDMA & GSM Mobile Base – March 2007 to September 2012 accessible at [www.medianama.com/2013/04/223-india-mobile-arp-minutes-cdma-gsm-2/](http://www.medianama.com/2013/04/223-india-mobile-arp-minutes-cdma-gsm-2/)

50. <http://www.gsma.com/membership/wp-content/uploads/2013/01/true-cost-providing-energy-telecom-towers-india.pdf>

51. <http://www.gsma.com/membership/wp-content/uploads/2013/01/true-cost-providing-energy-telecom-towers-india.pdf>

52. <http://www.gsma.com/membership/wp-content/uploads/2013/01/true-cost-providing-energy-telecom-towers-india.pdf>

## 11. Conclusion

There is consensus on the fact that the growth of India as a knowledge based economy will not be possible without the growth and expansion of the Indian telecommunications and IT sectors. While the IT sector has grown phenomenally, the growth trajectory of the telecom sector seems to have been interrupted mid-flight.

However, the Government seems to have realized the need for urgent reforms to give an impetus to the growth of the sector and in pursuance of the same we have seen the introduction of the Unified License and removal of the foreign investment restriction in this sector.

However, it cannot be denied that India still has a lot of ground to cover to achieve a growth rate equal to that of other developed and developing economies. India is among the last countries to access 3G technology at a time many countries have already deployed 4G technologies. As such, the government still has to go a long way to

introduce policies, regulations, guidelines, etc in the interest of not only the government or the telecom operators but also in the interest of the end consumers and that too without any delay. The Government further appears to be relaxing its position on certain contentious issues so as to make doing business easier in India, for example, the Government has finally allowed 3G roaming pacts, which were a major pain point for various telecom operators.

Another area which needs immediate attention is the need for flexibility in the regulatory mechanism. The telecom legislation at present seems to be archaic laws and the need of the industry right now is a mechanism that can continuously adapt itself to the changing needs of the industry.

There is no doubt at all that the coming years are going to be exciting years for the Indian telecom sector.



# Annexure A

## Foreign Investment Norms Eased and ‘One Nation - One License’ Becomes a Reality

The Department of Telecom, Ministry of Communications and Information Technology, (“DoT”) released the much awaited Unified License, paving the way for the implementation of DoT’s *One Nation - One License* plan. The Unified License seeks to consolidate license terms for different telecom services. The Unified License has also introduced certain new concepts and clarified some key areas which need to be kept in mind. Notably, spectrum has been officially delinked from the license, cross holding has been prohibited and 3G roaming pacts have been recognised.

This change in policy was accompanied by the Government of India (“GoI”) fulfilling a long standing demand of the industry, i.e. allowing 100% foreign investment in the telecom sector.

One crucial aspect which is yet awaited is the policy on mergers and acquisitions in the telecom sector. The telecom sector is quite fragmented and consolidation is considered crucial at this stage. We hope to see consolidation activity pick up as soon as the M&A guidelines are notified.

We now discuss the changes in the FDI policy and some of the key provisions of the Unified License.

### I. FDI Policy

The GoI through an amendment to its Foreign Direct Investment (“FDI”) policy has allowed 100% foreign investment in the telecom sector as opposed to the previous limit of 74%. FDI upto 49% continues to be under the automatic route, and any investment above 49% (upto 100%) will require prior approval from the Foreign Investment Promotion Board.

100% FDI is expected to give an impetus to

funding, consolidation, restructuring and exits for telecom operators and their shareholders including private equity investors. It is interesting to note that India is one of the few countries that has permitted 100% foreign ownership of telecom operators.

### II. Unified License

The DoT has released the final version of the license agreement for Unified License along with the guidelines for grant of Unified License and migration of existing telecom licenses into the Unified License regime. The Unified License is replacing the old regime of a telecom operator applying for separate licenses for separate services proposed to be offered by bringing all the major telecom services under one license.

The National Telecom Policy (“NTP”) is the main policy document that lays down the broad objectives that are sought to be achieved so as to align efforts of policy makers, stakeholders and law makers to achieve a common goal. The latest version of the NTP, i.e. NTP 2012 lays down creation of One Nation - One License across services and service areas as one of its main objectives. With respect to the Unified License, NTP 2012 specifically provides as follows:

*“To move towards Unified Licence regime in order to exploit the attendant benefits of convergence, spectrum liberalisation and facilitate delinking of the licensing of Networks from the delivery of Services to the end users in order to enable operators to optimally and efficiently utilise their networks and spectrum by sharing active and passive infrastructure. This will enhance the quality of service, optimize investments and help address the issue of the digital divide. This new*

*licensing regime will address the requirements of level playing field, rollout obligations, policy on merger & acquisition, non-discriminatory interconnection including interconnection at IP level etc. while ensuring adequate competition.”*

In the following paragraphs we shall discuss the scheme of the Unified License, some important provisions of the Unified License and some salient changes with respect to the provision of specific telecom services.

### III. Scheme of the Unified License

#### A. Services Offered

The Unified License includes within its ambit the following services:

- Access Service;
- Internet Service;
- National Long Distance Service (“**NLD Service**”);
- International Long Distance Service (“**ILD Service**”);
- Global Mobile Personal Communication By Satellite Service (“**GMPCS Service**”);
- Public Mobile Radio Trunking Service (“**PMRTS Service**”);
- Commercial Very Small Aperture Terminal Closed User Group (“**Commercial VSAT CUG Service**”);
- INSAT Mobile Satellite System-Reporting Service (“**INSAT MSS-R Service**”); and
- Resale of International Private Leased Circuit Service (“**Resale of IPLC Service**”).

The Unified License is split into two portions; part one contains general conditions such as security and technical conditions which is applicable to all service categories and part two contains specific conditions applicable to specific services.

#### B. Application

The Unified License is a sort of umbrella document

which all companies seeking to provide telecom services will need to obtain. Apart from this, the company would also need to obtain separate authorization from the DoT for specific services which the company wishes to provide. One company can have only one Unified License, but the same company can apply for authorisation for more than one service and / or service area subject to fulfilment of all the conditions of entry, simultaneously or separately at different times. At the time of applying for Unified License, the applicant has to apply for authorisation of at least one service that is listed in the Unified License.

#### C. Tenure

The Unified License shall be issued on non-exclusive basis for a period of 20 years. The license may be renewed by the DoT for an additional period of 10 years at a time upon request of the service provider, if made during the 19th year of the license period. Where any additional service has been authorized during the tenure of the license, the tenure of such additional service shall be co-terminus with the license.

### IV. Migration to Unified License Regime

In order to ensure the smooth transition of licensees from their existing licenses to the Unified License regime, the guidelines for grant of Unified License lay down the manner for migration of the existing licenses. Licenses of any of the existing operator shall be eligible to migrate to the Unified Licenses with any number of additional services, however, in such a case, the operator needs to migrate all of its existing licenses.

Currently, migration has been made completely voluntary until such time that the existing license of operators expires. All renewals / extension of license will be made only under the Unified Licensing regime. However, it would be mandatory for an existing licensee to migrate to Unified License regime under following conditions:

- i. Expansion of scope of the license / service to include any additional service or any service area;
- ii. Merger or acquisition between entities who have not migrated to the Unified License. In such a case, the merged entity must migrate to Unified License regime.

On migration, Unified License shall be valid for a period of 20 years from the effective date of issuance of the Unified License, regardless of the validity period of the license already held;

The Entry fee applicable for migration of all existing licenses to Unified License shall be equal to the entry fee laid down for a new Unified License. This entry fee is applicable for all services / licenses other than for an Internet Service Provider with BWA spectrum. This exception appears to have been made after the DoT's clarification<sup>53</sup> allowing the carriage of voice over the BWA Spectrum, following which an additional fee equal to the difference between the entry fee for UASL (Voice Service Providers) and entry fee paid for ISP license shall be payable in addition to the entry fee as applicable for a new Unified License.

## V. Salient Features and Significant Changes

### A. De-linking Spectrum from the License

In line with the recommendations of the Supreme Court in its judgment<sup>54</sup> whereby it canceled 122 telecom licenses, the Unified License has un-bundled spectrum and the license. Under the earlier regime, spectrum was considered as an integral part of the license, whereas, under the Unified License, spectrum will now have to be separately acquired once a license has been acquired. This change has been in line with NTP 2012 which suggested that spectrum should be

made available at a price determined through market related processes, rather than being bundled with the License.

### B. Entry Fee

While the Unified License mandates that separate entry fees must be paid according to the services proposed to be offered, the Unified License has imposed an overall cap on the entry fees payable for multiple services under the Unified License, at INR 15 Crores.

### C. License Fees

Important changes have been brought about with respect to license fees.

#### i. Change in Calculation of License Fee

In the earlier regime, differential percentage of the Adjusted Gross Revenue ("AGR") was to be paid as license fees on the basis of the circle in which services were offered. The Unified License now mandates a flat license fee of 8% of the AGR, inclusive of Universal Service Obligation which is presently 5% of AGR. However, from the second year of the effective date of service authorization, the license fee shall be subject to a minimum of 10% of the Entry Fee of the respective authorized service and service area.

#### ii. Presumptive AGR

Presumptive AGR is a concept that has been made applicable to all spectrum holders and places a premium on spectrum even where the spectrum holder does not utilize the spectrum made available to them. This move appears to be recognition by the DoT of spectrum as a scarce national resource and to that extent an attempt has been made to ensure that only serious players enter and operate in this industry. A spectrum

53. <http://www.livemint.com/Industry/tZ2wA8sa2XYrBbHXctzD7M/DoT-says-there-was-never-any-bar-on-BWA-spectrum-holders-for.html>

54. Centre For Public Interest Litigation & Ors. Vs Union Of India & Ors (2012)1CompLJ497(SC) our analysis of the same is available at Opens internal link in current window <http://www.nishithdesai.com/1/?item=Research+and+Articles/NDA+Hotline/Telecom+Hotline&article=115>

holder will now be required to pay license fees in the form of a percentage of notional revenues or a percentage of the actual revenues, whichever is higher. Notional revenue which is essentially a minimum amount of revenue for this purpose will be calculated in accordance with the relevant provisions of the Notice Inviting Application document of the auction of spectrum or conditions of spectrum allotment depending on the service and service area. Therefore, unlike the previous regime whereby license fee was determined on the basis of revenue generated by an operator, spectrum holders will now have to pay a minimum pre-determined percentage as license fee or actual AGR or the minimum license fee whichever is higher. Further, this move also appears to be an attempt by the DoT to speed out rollout of services by spectrum holders since they will now have to pay license fees regardless of the actual revenue earned and will reduce hoarding of spectrum.

#### D. Prohibition on Cross Holding

The old licensing regime allowed one licensee to hold an equity interest of up to 10% in another licensee in the same service area - this concept was known as "Cross Holding". Under the Unified License, this de-minimis exemption has been done away with. Licensees are no longer allowed to hold any equity interest (directly or indirectly) in any other licensee which provides services in the same service area. The Unified License provides a window of one year for entities to comply with this provision from the date of migration to the Unified License. This provision may have been included to prevent cartelisation in light of the allegations levelled against telecom operators for forming cartels in the last round of auction of spectrum by the Comptroller and Auditor General of India (CAG).<sup>55</sup> This particular provision will directly impact licensees such as Vodafone and Bharti Airtel since most of their licenses are due for renewal in the next year following which their

licenses would only be renewed under the Unified Licensing regime and in such a situation Vodafone would need to divest its minority stake in Bharti Airtel.<sup>56</sup>

#### E. Transfer of license

In the section of restriction on 'transfer of license', there is a clarification that has been made with respect to court approved merger and acquisitions which provides that any scheme of amalgamation or restructuring filed with the court must be drafted in a manner so that such amalgamation or restructuring shall be effective only after the written approval of the DoT for such transaction. It should be noted that there have been various rounds of litigation wherein the DoT's role has been challenged vis-à-vis approval from the Courts in the case of a court approved merger.<sup>57</sup> As such this clarification makes clear the DoT's position in this issue. However, there is no clarity on when the DoT will need to be approached for such approval. It is not clear whether such approval may be sought simultaneously with the court approval process or if one would need to seek such approval from the DoT after the completion of the court approval process.

#### F. Dispute Resolution

With respect to the appropriate forum for settlement of any disputes under the Unified License, it has now been clarified that all disputes which lie outside the domain of the Telecom Disputes Settlement Appellate Tribunal ("TDSAT") will lie in the jurisdiction of competent Courts in the National Capital Territory ("NCT") of Delhi only. The TDSAT currently has jurisdiction to adjudicate disputes between (i) a licensor and a licensee; (ii) two or more service providers; and (iii) between a service provider and a group of consumers. Therefore, it appears that the Unified License attempts to contractually restrict jurisdiction to competent Courts in NCT of Delhi

55. [http://articles.economictimes.indiatimes.com/2013-05-21/news/39418944\\_1\\_cartelisation-telecom-firms-spectrum](http://articles.economictimes.indiatimes.com/2013-05-21/news/39418944_1_cartelisation-telecom-firms-spectrum)

56. <http://gadgets.ndtv.com/telecom/news/bharti-has-no-intention-to-buy-back-vodafone-stake-in-airtel-sunil-mittal-415121>

57. [http://articles.economictimes.indiatimes.com/2012-07-13/news/32663691\\_1\\_idea-spice-merger-licence-and-merger-guidelines-tdsat](http://articles.economictimes.indiatimes.com/2012-07-13/news/32663691_1_idea-spice-merger-licence-and-merger-guidelines-tdsat)

for their disputes such as Writ Petitions. The move by the DoT to restrict jurisdiction to courts in NCT of Delhi may be challenged since jurisdiction of courts is to be determined in accordance with the Code of Civil Procedure, 1908.

### G. Applicability of Other Statutes

It has now been clarified that in addition to the Indian Telegraph Act, 1885 or Indian Wireless Telegraphy Act, 1933 the statutory provisions and the rules made under the Information Technology Act, 2000 and / or the Telecom Regulatory Authority of India (“TRAI”) Act, 1997 and the rules and regulations thereunder shall govern the provision of service under the Unified License. Further, any order passed under these statutes shall also be binding on the licensees.

### H. Electromagnetic Radiation and Renewable Energy

The DoT has incorporated their notifications on the permissible level of electromagnetic radiation from base stations as part of the Unified License. The Unified License requires the licensee to audit and self-certify that the base stations are conforming to the limits for public exposure. Similarly, the DoT has included its obligation to adopt Renewable Energy Technologies as part of the Unified License.

### I. Discontinuation of Service

With respect to discontinuing a service launched by an operator, a new provision has been added by the Unified License under which notice must be given to the DoT as well as the TRAI of at least 60 calendar days in advance with reasons. Additionally a notice must also be given to all the subscribers by sending a 30 calendar days notice to each such subscriber. However, the DoT reserves the right to reject such request. As such it appears that the DoT has reserved with itself the right to review an operator’s proposal for discontinuation

and even reject such proposal.

## VI. Notable Exemptions From The Unified License

### A. Other Services Provider (“OSP”) Registration

The Unified License does not include services that fall under the category of “Application Services” under the OSP regime (such as call centres). However, the OSP regime is in any case separate from the regular telecom licenses since it is a registration process under the OSP regulations as opposed to a license.

### B. Voice Mail/Audiotex/ Unified Messaging Services

Prior to the Unified License, this service was governed under a specific license. This service has not been identified as a separate service category under the Unified License. The decision not to include a separate service category for this service under the Unified License may raise questions on whether this services would continue be governed by the old license agreement or if the intention of DoT is that there would be no license applicable to this service. The Unified License mentions that Access Service providers will be allowed to provide Voice Mail/Audiotex/ Unified Messaging Services by itself; however this was the case under the old regime as well. It is not clear how operators who do not wish to invest in the Access License may provide Voice Mail/Audiotex/ Unified Messaging Services. There have been discussions on creating a separate license category for value added services<sup>58</sup> - it may be that the GoI is contemplating categorising Voice Mail/Audiotex/ Unified Messaging Services as a value added service subject to a separate licensing regime. It is not yet clear what such a licensing regime would entail.

58. TRAI’s Recommendations on Application Services issued on May 14, 2012 wherein the TRAI has inter alia recommended that value added services be subject to a licensing regime.

## C. Mobile Virtual Network Operator (“MVNO”)

MVNO essentially is the provision of telecom services using the bandwidth / spectrum of a licensed service provider under a separate brand name. TRAI had issued its recommendations in 2008 suggesting that the DoT should issue a separate license category for MVNOs,<sup>59</sup> however, no notification has been made by the DoT giving effect to these recommendations. MVNO gains even more significance under the Unified License due to the introduction of the concept of Presumptive AGR, whereby a spectrum holder will be required to pay license fees in the form of a percentage of notional revenues or a percentage of the actual revenues, whichever is higher, regardless of the actual revenues earned. Therefore, the introduction of MVNO would help spectrum holders utilize excess spectrum by leasing the same to MVNO operators.

## VII. Provisions with Respect to Specific Services - Salient Points

### A. Access Services

- i. It has been clarified that the Access Service are the only license category which can interconnect Internet Telephony Network to a normal landline (PSTN) / Cellphone. In the earlier license, while it was clear that Access Service providers could provide internet telephony, it was not expressly stated that Access Service providers could provide interconnection between the data network and the PSTN (that is expressly prohibited for ISPs).
- ii. An important change that has been introduced under this license is the recognition of roaming arrangements specifically allowing 3G intra-circle roaming (ICR) pacts. The license now provides that an operator may enter into

agreements for roaming facilities (within the same service area or other service areas) with other service providers. It has been clarified, that any such roaming arrangement will not entitle such operator to acquire customer in the spectrum band / technology not held / not deployed or for services / facilities not offered by the operator in its home network. This change in policy has come after various rounds of litigation and disputes regarding 3G Roaming Pacts and is a welcome change in this regard and will incentivize the adoption of the Unified License by existing licensees.

### B. Internet Service

- i. The erstwhile ISP license regime provided for two kinds of licenses, i.e. one an authorization to provide services at a national level (Category A) and an authorization to provide services at telecom circle level (Category B). The Unified License has introduced an authorization for an additional service area, i.e. Secondary Switching Areas (“SSAs”) (Category C) which is more concentrated than a Telecom Circle and has divided the country into 322 SSAs. This means that ISP service providers can now opt for providing services in smaller service areas. However, in the event that an entity applies for a Category C authorization for more than 4 SSAs such entity must obtain a Category B authorization. This would encourage deeper penetration of data networks in the country.
- ii. The position with respect to Internet Telephony remains unchanged, i.e. ISPs are allowed to offer limited Internet Telephony<sup>60</sup> in India and cannot connect an Internet Call to a landline / cellphone in India. The recommendations of TRAI<sup>61</sup> for unrestricted IP telephony have not been accepted in this round of reforms.

The DoT has permitted internet service providers

59. TRAI’s Recommendations on Mobile Virtual Network Operator (MVNO) issued on August 6, 2008.

60. ISPs were allowed to provide internet telephony connecting the following: (i) PC to PC; within or outside India (ii) PC in India to PSTN/PLMN abroad and (iii) Any device connected to ISP node with static IP address to similar device within or outside India

61. TRAI’s Recommendations on Issues related to Internet Telephony issued on August 18, 2008

who also have a DTH service license from the Ministry of Information and Broadcasting, to allow customers for downloading internet data through DTH after obtaining necessary permission from the DoT.

Apart from the changes and clarifications that have been discussed above, the Unified License has consolidated within its ambit various other services such as the GMPCS Service, PMRTS Service and Resale of IPLC service. The Unified License has been a long pending demand of the

industry and was widely considered as one of the most important reforms required to help revitalize this sector. With the increase in FDI Limits and a new mergers and acquisitions policy on the anvil the telecom sector looks like it may be able to regain some of the sheen that it lost in the last few years.

- **Kartik Maheshwari, Rakhi Jindal and  
Vivek Kathpalia**

# Annexure B

## Supreme Court Cancels 122 Telecom Licenses With Good Intentions

### I. Can India's International Investment Agreements Rescue Affected Foreign Investors?

Several non-governmental organizations and individual citizens (“**Petitioners**”) had filed a public interest litigation<sup>62</sup> against the Union of India and various private companies in relation to allocation of 2G spectrum. In relation to this public interest litigation, on February 2, 2012 the Supreme Court of India (“**SC**”) criticized the first come first served policy of the government for distribution of 2G spectrum and delivered an order against thirteen respondents<sup>63</sup> (“**Respondents**”) cancelling 122 telecom licenses granted in various service areas for 2G spectrum. The SC has also levied fines against certain telecom operators and directed the Telecom Regulatory Authority of India (“**TRAI**”) to formulate a fresh policy for allocation of 2G spectrum.

Vide this order the SC has not only sent out a very clear message that when a government policy is not transparent or fair, it is liable to be struck down, but the SC has also gone ahead and quashed the very licenses which the government issued under the said policy. As such the order of the SC has resulted in mixed reactions and is bound to have far reaching consequences particularly in the following respects:

- i. The foremost effect will be on the Respondent operators and their investors whose licenses have been cancelled by the order. This cancellation has resulted in investor uncertainty and while the order is clear that the

allocation of 2G spectrum is to be done afresh, it is to be considered whether the operators who were legitimately conducting business in India should be given certain ‘grandfathering’ treatment with respect to the investments already made by them or be compensated in some other form.

- ii. The order will also impact the telecom supply chain in the Indian telecom industry. There are various companies which have large orders and commitments from these licensees for supply of various telecom network hardware, software and services; the potential loss of a major customer/s in India is a cause of serious concern to such vendors. It will need to be examined whether the supply arrangements under which such vendors operate would provide them with any contractual remedies. Disputes and litigation may ensue at various levels.
- iii. The SC order does not mention what is to become of the end subscribers of the affected Respondent operators. Such customers may be ported to other service providers as part of the mobile number portability regime introduced in India.

### II. Brief Background

- The National Telecom Policy 1999 (“**NTP 1999**”) was formulated with one of its main objectives ‘to achieve efficiency and transparency in spectrum management’ and ‘have a transparent policy of allocation of frequency spectrum’
- Guidelines for Unified Access Service Licenses

62. Writ Petition (Civil) No 423 of 2010

63. Respondents in this matter are as follows (1) Union of India through its Secretary, Department of Telecommunications, (2) Etisalat DB Telecom Pvt. Ltd. (Swan Telecom), (3) Unitech Wireless Group (4) Loop Telecom Pvt. Ltd. (ShippingStop Dotcom P. Ltd.), (5) Videocon Telecommunications (Datacom Solutions Pvt. Ltd.) (6) S Tel Ltd., (7) Allianz Infratech (P) Ltd., (8) Idea Cellular Ltd. & Aditya Birla Telecom Ltd. (Spice Communication Pvt. Ltd.), (9) Tata Teleservices Ltd., (10) Sistema Shyam Tele Services Ltd. (Shyam Telelink Ltd.) (11) Dishnet Wireless Ltd. & Aircel Ltd., (12) Vodafone Essar South Ltd. & Vodafone Essar Spacetel Ltd., (13) TRAI



- (“UAS Licenses”) were announced by the Department of Telecommunications (“DoT”) in 2003 that allowed the basic service providers to provide full mobility based services with a stipulated entry fee based on the bid price paid by operators in 2001. The payment of this entry fee enabled the licensee to become eligible for spectrum allocation in specified bands (without the need to pay any additional spectrum fee) subject to availability of spectrum; however the operators paid royalty on spectrum use on revenue share basis.
- Through its recommendations dated August 28, 2007 TRAI recommended that there should be no change in the 2G pricing (“**TRAI Recommendations**”), so as to allow level playing field for all players.
  - Meanwhile the DoT continued to receive applications for UAS Licenses. As on September 2007, there were 167 license applications from 12 companies for 22 service areas.
  - A note dated October 26, 2007 was sent to the Department of Legal Affairs, seeking the opinion of the Attorney General of India on the mechanism to deal with situation created to due receipt of large number of UAS License applications. The reply to the note contained four alternatives to deal with the situation. On November 2, 2007, the Telecom Minister approved the note and recorded on his own that Letter of Intent (“**LoI**”) may be issued to the applications received up to September 25, 2007; he also indicated that the DoT has decided to continue the first-cum- first served policy of DoT for processing the applications received before September 25, 2007 and may continue adopt the same policy for the application post September 25, 2007 in the event that the spectrum is available.
  - Thereafter there was correspondence between various departments (including the office of the Prime Minister, the then Telecom Minister and the Finance Secretary) debating this issue. On December 26, 2007 Mr. A Raja (the Telecom Minister) sent a letter to the Prime Minister in order to establish that the Prime Minister had provided consent with respect to issuance of LoI to the applicants.
  - The DoT issued a press note on September 24, 2007 that no new applications would be accepted after October 1, 2007 (“**Press Note**”). Between September 24, 2007 and October 1, 2007 over 300 applications were received.
  - On January 10, 2008, DoT decided to issue letters of intent on first come first served basis, suo-moto bringing forward the cut-off date to September 25, 2007 from October 1, 2007. Later on the same day, DoT posted an announcement on its website saying those who apply between 3.30 PM and 4.30 PM of the same day would be issued LoIs in accordance with the said policy.
  - Subsequently the Respondent operators were granted UAS Licenses.
  - S Tel who had applied for grant of license pursuant to the Press Note but was ousted because of the advancing of the cut off date filed a writ petition in the Delhi High Court wherein the Court held that the DoT had in effect changed the rule of the game ‘after the game began’. While the Union of India had challenged this order in the SC, a compromise was reached between the parties and the SC disposed of the appeal.
  - Currently there are pending criminal investigations into various allegations of corruption against various persons and irregularities in the allocation of spectrum to the Respondent operators.

### III. Grounds of Challenge

The Petitioners have questioned the manner of grant of UAS Licenses to the Respondent operators on the ground that the procedure adopted by the DoT in granting of the UAS Licenses to them was arbitrary, illegal and in violation of Article 14 of the Constitution of India (which guarantees equal treatment). The submissions made by the Petitioners inter alia include the following:

- i. Spectrum is a national asset and a policy of distributing it on a first come first serve basis with no defined criteria (such as advertisement and auction) is fundamentally flawed.
- ii. The DoT violated the recommendations made

- by the TRAI that there should be no cap on the number of service providers in a service area.
- iii. The Petitioners relied upon reports prepared by the Comptroller and Auditor General (“CAG Report”) and claimed that a large number of ‘ineligible applicants’ were considered.
  - iv. The TRAI Recommendations of 2007 in fixing of entry fee as per prices determined in 2001 was arbitrary and unconstitutional.

## IV. Questions Raised By The Supreme Court

We provide below the gist of the SC decision and our analysis on some of the pertinent points raised and answered by the SC.

### A. Whether the Government has the Right to Alienate a Natural Resource other than by Following a Fair and Transparent Method? Whether the TRAI Recommendations were Flawed?

#### i. Decision of the SC

The SC concluded that spectrum was a natural resource and national asset and belonged to the public at large. It referred *inter alia* to the SC’s decision in *Sachidanand Pandey v. State of West Bengal*<sup>64</sup> where the SC had opined that one of the best ways of securing the public interest when disposing of a public property is to sell the property by public auction or by inviting tenders. The SC opined that the auction method was the only rational transparent method of distribution of national resources.

The SC held that the TRAI Recommendations had overlooked not only the main objectives of NTP 1999 of achieving a transparent process of frequency allocation but also basic constitutional principles of equality by effectively preventing a majority of people from participating in the

distribution of spectrum. The SC held the TRAI Recommendations to be flawed.

#### ii. Analysis

The decision on treating spectrum as a national asset is in keeping with the past policy of the government, judicial precedent and international trends.

However the comments of the SC that auction method seems to be the only rational and transparent method for distribution of national resources appears to be simplistic. This may not be true of all resources and in all cases. In the case of *Sachinand Pandey v State of West Bengal*<sup>65</sup> the government of West Bengal had not floated a tender for granting government land for construction purposes but had negotiated with interested parties. While the SC in this case had opined that auction is a preferable way of disposing of public property, the SC had also held that the absence of auction does not necessarily nullify the grant and that auction is not the invariable rule in distribution of resources. Whatever process is selected by the government to distribute national resources needs to follow a sound and transparent policy.

In the case of spectrum while auction may be a preferred market driven method (especially in scenarios where spectrum is scarce and there are a large number of applicants), it is a policy level decision to be taken by the government. In this order the SC has directed the TRAI to make fresh recommendation for grant of license and allocation of 2G spectrum. The TRAI has since issued a pre-consultation paper on the allocation of 2G spectrum on February 6, 2012.<sup>66</sup>

While the SC may have made broad remarks about the distribution of national assets, the underlying point which the SC seems to be making is that where the government policy for distribution of a national asset is not transparent or clear, it may

64. (1987) 2 SCC 295

65. 1987 AIR 1109

66. [http://www.trai.gov.in/WriteReadData/trai/upl\\_oad/ConsultationPapers/277/Consultation%20Paper.pdf](http://www.trai.gov.in/WriteReadData/trai/upl_oad/ConsultationPapers/277/Consultation%20Paper.pdf)

lead to corruption and nepotism and is liable to be struck down. This stand taken by the SC is also in keeping with the objectives of NTP 1999 which stresses on the need for transparency in spectrum management.

## **B. Whether the Grant of UAS Licenses to the Respondent Operators is Flawed due to Arbitrariness and Malafides and is Contrary to Public Interest?**

### **i. Decision of the SC**

The SC held that various actions such as bringing forward of the cut-off date, the manner of issue of the licenses were tinged with irregularities and contrary to public interest and hence the grant of the UAS Licenses to the Respondent operators was illegal.

The Respondents had argued that if the exercise undertaken for the grant of UAS Licenses was flawed in the case of the Respondents then such irregularity should actually be extended to all UAS Licenses which were issued since 2001 under the said first come first served policy and before issue of the Press Note (and not be restricted to solely the Respondent operators). The SC dismissed this argument by stating that operators who got the licenses prior to issue of the Press Note are not respondents in this case and hence the legality of their licenses is not in question.

### **ii Analysis**

It is interesting to note that though the Petitioners relied heavily on the CAG Report; since the CAG Report is currently under review by certain government committees, the SC did not find it proper to refer to the findings and conclusions drawn in the CAG Report. That being the case, the fact remains that the Respondents had followed the extant policies of the government and had applied for licenses as per the declared government policy. They and their investors have made huge investments for creating infrastructure in the

country. Cancellation of their licenses at this point could be held to be against the doctrine of legitimate expectation insofar as it relates to the expectations of such players to operate in a field of regulatory certainty and protection from unjust expropriation.

## **C. Whether the Principle of first come first Served Followed by the DoT for grant of the UAS Licenses to the Respondent Operators is Ultra Vires Article 14 of the Constitution.**

### **i. Decision of the SC**

The SC held that there is a fundamental flaw in the principal of first-come-first-served inasmuch as it involves an element of pure chance or accident and may be misused. The SC further observed that it is essential for the government to adopt a rational method for disposal of public property and no attempts should be made to scuttle the claim of worthy applicants. Accordingly the SC held that the principle of first come first serve violates constitutional principles.

Further while admitting that the courts have limited judicial review in policy decisions particularly in financial matters, the SC opined that the courts were justified in exercising their jurisdiction when it is abundantly clear that any policy framed by the government is against public interest.

### **ii. Analysis**

While the principal of first come first served and its constitutional validity requires deeper study, it is also important to analyse whether alternate methods such as auction would always be fair and equitable. There could be an argument that an auction process would work in the favour of those who have deep pockets and itself therefore be in some way in violation of Article 14.

## **D. Whether the Licenses Granted to Ineligible Applicants and Those who Failed to Fulfill the Terms and Conditions of the License are Liable to be Quashed?**

### **i. Decision of the SC**

The Supreme Court held that all licenses granted to the Respondent Operators on or after January 10, 2008 and subsequent allocation of spectrum to the licensees were declared illegal and are quashed. The reason for this quashing was limited to the fact that the policy of the government was illegal. The SC did not go into the merits of each license.

### **ii. Analysis**

Whilst the intention of the SC in ensuring a fair and transparent framework is laudable, the cancellation of all 122 licenses without going into the merit of each case raises many questions. Since the Central Bureau of Investigation is seized of criminal proceedings in the 2G spectrum case, it may have been preferable for any decision on cancellation of license to be based on proven criminal culpability. It is interesting to note the SC's view that this order should have no bearing on the pending criminal investigations.

## **V. Possible Remedies**

### **A. Review**

The first remedy that is available to the Respondent operators is to file an application for review of the SC's judgment.

By virtue of Article 137 of the Constitution of India the SC has the power to review its judgment on the grounds of error apparent on the face of record and also in unusual cases to avoid injustice.

It is further settled law that the SC is not powerless to correct its error which has the effect of depriving a person of his fundamental rights. It can do so in exercise of its inherent jurisdiction

in any proceeding pending before it without insisting on the formalities of a review application. Powers of review can be exercised in a petition filed under Article 136 or Article 32 or under any other provision of the Constitution if the Court is satisfied that its directions have resulted in the deprivation of the fundamental rights of a citizen or any legal right of the petitioner.

The review under law is placed before the same judges who passed the earlier judgment and hence an administrative order by the Chief Justice of India to appoint an alternate judge to replace Justice A. K Ganguly (now retired) would be necessary.

If the Respondents in their review petition can prove that the inference by the SC in the government's policy decision is contrary to the principles laid down by the SC in its past judgments or there is any other conflict between other precedents set by the SC and the present judgment they also will have an opportunity to request the court to place the matter before a larger bench of the SC for adjudication.

This process of review will be available to all Respondent operators and other entities who had a direct interest in the license and who deserved to be heard before the license could be canceled.

### **B. Investment Arbitration**

The remedy which could be available to foreign investors is that of invoking an Investment Arbitration under the International Investment Agreement ("IIA") India has with their parent states. This remedy may be available not only to the foreign investors holding direct interest in the entities whose licenses were cancelled such as Telenor, Sistema and Bahrain Telecommunications but also to those foreign investors who have indirectly lost their business due to the sudden cancellation of the licenses.

The foreign investors may have various claims which might be available to them on case to case

basis. But the important ones would be claims of breach of legitimate expectation; denial of justice and expropriation which would in turn entitle the foreign investors to compensation equaling the value of loss to investment.

The investor whose parent jurisdiction does not have an IIA with India but has routed their investment through any other jurisdiction which might have an IIA with India could use those treaties to invoke such claims.

An important takeaway is that, if the home state of a foreign investor investing into India does not have an IIA with India it is advisable to revisit India's IIAs with other nations before making an investment and make use of the available window of corporate structuring to ensure full protection and security of one's investment.

### C. Approach the TDSAT

In accordance with the TRAI Act, the TDSAT (i.e. the Telecom Disputes, Settlement And Appellate Tribunal) is the appropriate jurisdiction for any dispute between the DoT and a licensee.

It is to be noted that while the SC has declared the licenses granted to the Respondent operators to be illegal, the method of cancellation/ termination is not clear. It is not the case against the Respondent operators that they are in breach of the terms of the UAS License; as such it is not clear under what ground the government would terminate the license. The terms of the UAS License have the following provisions with respect to cessation of

the license:

- i. The DoT may terminate the license in cases of breach of license conditions and breach of applicable law;
- ii. The DoT has the right to suspend the operation of the license if it is of the opinion that it is necessary to do so in public interest;
- iii. The DoT may revoke the license at any time.

Keeping the above in mind, the Respondent operators may approach the TDSAT to claim compensation from the DoT.

## VI. Conclusion

Legal, tax and regulatory certainty is a non-negotiable pre-requisite in today's investment environment. The recent judgment of the SC in the Vodafone case<sup>67</sup> on taxation of cross-border transactions involving investments in India provided some much needed certainty to investors. This order may dampen investor confidence.

While the SC seems to have been aggressive in penalizing entities for following existing policies, it is not to be doubted that the SC has to be commended for passing a courageous judgment upholding the need for transparency in government policies which paves the way for ensuring that all policy decisions should be reasonable and clear.

By Telecom Practice Group

67. Please see our analysis at [http://www.nishithdesai.com/New\\_Hotline/Tax/Tax%20Hotline\\_Jan2312.htm](http://www.nishithdesai.com/New_Hotline/Tax/Tax%20Hotline_Jan2312.htm)

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## Research @ NDA

**Research is the DNA of NDA.** In early 1980s, our firm emerged from an extensive, and then pioneering, research by Nishith M. Desai on the taxation of cross-border transactions. The research book written by him provided the foundation for our international tax practice. Since then, we have relied upon research to be the cornerstone of our practice development. Today, research is fully ingrained in the firm's culture.

Research has offered us the way to create thought leadership in various areas of law and public policy. Through research, we discover new thinking, approaches, skills, reflections on jurisprudence, and ultimately deliver superior value to our clients.

Over the years, we have produced some outstanding research papers, reports and articles. Almost on a daily basis, we analyze and offer our perspective on latest legal developments through our *"Hotlines"*. These *Hotlines* provide immediate awareness and quick reference, and have been eagerly received. We also provide expanded commentary on issues through detailed articles for publication in newspapers and periodicals for dissemination to wider audience. Our *NDA Insights* dissect and analyze a published, distinctive legal transaction using multiple lenses and offer various perspectives, including some even overlooked by the executors of the transaction. We regularly write extensive research papers and disseminate them through our website. Although we invest heavily in terms of associates' time and expenses in our research activities, we are happy to provide unlimited access to our research to our clients and the community for greater good.

Our research has also contributed to public policy discourse, helped state and central governments in drafting statutes, and provided regulators with a much needed comparative base for rule making. Our *ThinkTank* discourses on Taxation of eCommerce, Arbitration, and Direct Tax Code have been widely acknowledged.

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We would love to hear from you about any suggestions you may have on our research reports. Please feel free to contact us at [research@nishithdesai.com](mailto:research@nishithdesai.com)

# Nishith Desai Associates

LEGAL AND TAX COUNSELING WORLDWIDE

## MUMBAI

93 B, Mittal Court, Nariman Point,  
Mumbai 400 021 India

Tel: +91 - 22 - 6669 5000

Fax: +91 - 22 - 6669 5001

## SILICON VALLEY

220 S California Ave., Suite 201,  
Palo Alto, CA 94306, USA

Tel: +1 - 650 - 325 7100

Fax: +1 - 650 - 325 7300

## BANGALORE

Prestige Loka, G01, 7/1 Brunton Rd,  
Bangalore 560 025, India

Tel: +91 - 80 - 6693 5000

Fax: +91 - 80 - 6693 5001

## SINGAPORE

Level 30, Six Battery Road,  
Singapore 049909

Tel: +65 - 6550 9855

Fax: +65 - 6550 9856

## MUMBAI BKC

3, North Avenue, Maker Maxity  
Bandra - Kurla Complex,  
Mumbai 400 051, India

Tel: +91 - 22 - 6159 5000

Fax: +91 - 22 - 6159 5001

## NEW DELHI

C-5, Defence Colony  
New Delhi - 110024, India

Tel: +91 - 11 - 4906 5000

Fax: +91 - 11 - 4906 5001

## MUNICH

Maximilianstraße 13  
80539 Munich, Germany

Tel: +49 - 89 - 203006 - 268

Fax: +49 - 89 - 203006 - 450

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For any help or assistance please email us on [ndaconnect@nishithdesai.com](mailto:ndaconnect@nishithdesai.com) or  
visit us at [www.nishithdesai.com](http://www.nishithdesai.com)