Bharti Airtel Response to the Consultation Paper on 'Definition of Adjusted Gross Revenue (AGR) in License Agreements for provision of Internet Services and minimum presumptive AGR'

NTP-2012 envisions Broadband on Demand and envisages leveraging telecom infrastructure to enable all citizens and businesses, both in rural and urban areas, to participate in the Internet and web economy thereby ensuring equitable and inclusive development across the nation.

The stated, third objective of the NTP 2012 is to "*Provide affordable and reliable broadband-on-demand by the year 2015 and to achieve 175 million broadband connections by the year 2017 and 600 million by the year 2020 …*"

Internet & Broadband services in India have witnessed a very slow growth. Most of the broadband targets set by the Regulator and by the Licensor in the past have never been achieved. Unlike growth of Voice and SMS the penetration of Broadband has been under severe stress. As on 31st Dec 2011 there are more than 388 registered Internet Service Providers across all the categories **(103 in Category A, 155 in Category B and 130 in Category C)**. This clearly indicates that while the sector has witnessed entry of several players the growth has not been commensurate with it. The main driver for growth of Internet services is Mobile wireless access providing ease of use and access. There is an urgent need to review and address the impediments for growth in Internet and Broadband through various access medias' like Wireline and Wireless.

Therefore, at the outset we are not in favour of any additional regulatory cost arising due to proposed inclusion of revenue from pure internet services in the AGR.

I: Present scenario

- At present, the ISP and ISP-IT licensees have been allowed to deduct Revenues from Pure Internet Services i.e. Internet Access and Internet Content from Gross Revenue under the License, in particular for calculation of AGR and thereby payment of License Fee. The existing ISP, ISP-IT licensees have been paying their license fee basis the same definition of AGR in the license agreement.

- As of now, Internet access is provided through various mediums 2G, 3G, 4G, CDMA 2000 1X , CDMA EVDO, DSL, Dial up PSTN and Leased Lines. Internet access on Mobiles using 2G, 3G, CDMA 2000 1X and CDMA EVDO under the UAS license and in 4G LTE under the UASL and ISP licenses. These Internet access provided through various mediums are perfectly competitive products. However, there is a competitive disadvantage for UASLs to offer Internet due to a far higher License fee and Spectrum Usage fee applicable compared with that applicable on ISPs.

- Given the predominant role of wireless in delivery of Internet and Broadband today, Mobile/ Wireless internet access is a key driver of change in the economy. However, the Internet access provided under a UASL license is subjected to a revenue share of 11-16% [8% (License Fee) and 3-8% (Spectrum Usage Charge)] as compared with Internet access through cable/ISP, standalone ISP licenses. Therefore, to provide an impetus to the growth of internet/broadband, the revenue from pure internet service should be excluded from AGR of UASL/CMTS also.

- In recent developments post the 2010 auctions for Broadband Wireless Access ('BWA') spectrum in 2.3 GHz some ISP licensees acquired this Spectrum. There is currently a recurring charge of 1% on AGR of the ISP/entity. However, the present definition of the Gross Revenue and 'AGR' is the

same for an ISP licensee holding BWA spectrum as a normal ISP. ISPs holding BWA spectrum end up paying a much lower License and Spectrum Fee as compared to their UASL/CMTS counterparts providing internet on Wireless. We would like to submit that the mobile/wireless internet provided by ISPs holding BWA spectrum and a CMTS/UASL holding 2G/3G or BWA spectrum are perfectly substitutable and therefore any arbitrage of License or Spectrum Fee creates a non level playing field and creates a competitive disadvantage to CMTS/UAS Licensees.

- **Therefore, apart from continuation of allowed deduction for revenue from pure Internet Services under ISP License, there is a need of rationalization of the License Fee for UAS/CMTS License to bring the LF on Pure Internet at par with ISP, ISP-IT.**

- In addition to the continuation of the allowed deduction for pure internet services, the definition of Gross Revenue under the license should be limited to the revenues derived from offering services under the scope of the license and not on entire revenues of the company holding the license.

II: Key challenges

The **key challenges** that have arisen in the current circumstances with respect to the revenues from licensed activities on which service providers should pay license fee as a percentage:

1) Definition of the Gross Revenue of a Licensee to be strictly restricted to the revenues generated by offering services under the scope of the respective licenses. And subsequent deductions to arrive at the AGR to consider payments made to other eligible license telecom service providers, taxes and levies paid to the government.

2) Deductions from Gross Revenue should be on Accrual basis. All payments made to other eligible telecom service providers, Government imposed taxes and levies paid should be considered on accrual basis.

3) Deductions should apply for telecom resources taken from other telecom service providers to delivery services, since the applicable license fee is paid on such revenues by the respective service providers. Double taxation of such licensed resources should be avoided as per similar treatment followed in G.S.T/Service Tax. As also Dual Charging of revenues in the hands same and other service providers should be avoided.

4) There is no level playing field between License Fee and Spectrum Fee paid by ISPs offering Wireless Internet Access and the LF/SF paid by UASLs offering Mobile Wireless Broadband/Internet access. Therefore the revenue from pure internet services under CMTS/UAS License shall also be allowed to be deducted from AGR.

5) GR should **exclude** items **not** related to revenues from services offered under the scope of the licenses. As per TRAI recommendations dated 21st September 2006 too the following were recommended for exclusion from AGR. We feel the same should be reiterated:

    a. Revenue on account of sale of immovable property, securities, warrants or debt instruments, other items of fixed assets

    b. Gains from upward valuation or devaluation on account of fluctuation of foreign exchange

c. Interest Income from deposits other than telecom related refundable deposits. i.e, Interest income from Term deposits, Margin Money deposits for Bank Guarantees and other such deposits should be excluded from GR and therefore AGR.

d. Dividend Income

e. Reversal of Revenues on account of Bad Debt and Vendor's Credit

f. Revenue on account of Property Rent

g. Revenue from Sale of Fixed Assets in the nature of Capital Receipts and Insurance claims

h. Revenue from sale of handsets / CPE

i. Receipts from USO Funds

These issues may kindly be addressed vide this consultation exercise as a step in the direction of achieving the Broadband and Internet Access targets set in the New Telecom policy 2012 ('NTP 2012').

III: Our Comments to Consultation Comments

We request the Authority to consider our entire submission while considering our comments on the questions raised vide the consultation paper issued by TRAI is below:

1. Stakeholders are requested to give their comments on definition of AGR for all three categories of ISP licences.

Bharti Airtel's Response

1) The definition of Gross Revenue needs to be dealt with before arriving at the definition of AGR. This issue requires a detailed consultation.

a. Section 4 of the Indian Telegraph Act, 1885 (hereinafter referred to as the '**Telegraph Act**') is the charging provision which entitles the central government to levy licence fees for telecom activities from the telecom operators. Under section 4 of the Telegraph Act, the exclusive privilege of the Central Government is limited only to *'establishing, maintaining and working telegraphs'*. The first proviso to Section 4(1) of the Telegraph Act empowers DoT to grant a Licence to a private party to establish, maintain or work a Telegraph, on such conditions as it thinks fit. Thus, these conditions must necessarily relate to and have a direct nexus to the establishment, maintenance or working of a Telegraph. Any condition which does not relate to or does not have a direct nexus to the establishment, maintenance or working of a Telegraph is over and above the scope of the licenses. Therefore, License Fee can and should only be levied on the revenue which has a direct nexus with the telecom activities and services licensed by the government to the telecom operators i.e. relating to 'establishment, maintenance and working of telegraph'.

b. As per the Guidelines for granting Unified Access Service License (UASL) an applicant is required to be a registered Indian Company under the Indian Companies Act 1956. Hence, an already established and registered company is granted a License to operate Telecommunications Services under the Indian Telegraph Ac 1885. The license is a subset of a

registered and established company implying that it is already envisaged that any registered company would already have other avenues of generating revenues that may not arise out of a cellular mobile/telecommunications activities under the license granted i.e, the "UASL" in this case. And therefore, it may not be construed that a company will only be formed solely for the conduct of telecommunications activities. Clause No 1. of the UASL Guidelines dated 14.12.2005 ("Guidelines") is reproduced below for reference:

1. *"1. The applicant must be an Indian company, registered under the Indian Companies Act'1956 "*

c. It is also pertinent to mention that the "Guidelines" also envisage Compliance to License conditions to be acknowledged by the Memorandum of Association of a Company and the Obligation to comply with License Conditions to be incorporated in the Articles of Association of a Company. This also supports the view as mentioned above that incorporation of a company was not the requirement for obtaining a UASL instead any registered Indian company could in addition to its other businesses also apply for a UASL. The Clause 5G iii) of the "guidelines" is reproduced below for reference:

a. *"5 G iii) The Company shall acknowledge compliance with the license agreement as a part of Memorandum of Association of the Company. Any violation of the license agreement shall automatically lead to the company being unable to carry on its business in this regard. The duty to comply with the license agreement shall also be made a part of Articles of Association."*

d. It can be inferred from above that **any registered Indian Company** may and could **have revenues from their other businesses as well e.g, Real Estate, Banking, Insurance etc**. Therefore, Telecommunication as a business activity can be envisaged under **any registered Indian Company** which meets the requirements of the Department of Telecommunications, Government of India under the said "Guidelines." The consideration of Gross Revenues of a Company for the purposes of arriving at the Adjusted Gross Revenue as per UASL condition 19.1 would and ought to be only revenues earned under the specific scope of services of the UASL for telecom related activities.

e. **The genesis of the definition of Gross Revenue** and in effect the Adjusted Gross Revenue ('AGR') was in the **year 1999** when the Cellular Mobile Telecom Service Providers were offered a **Migration Package**. Migration Package offered by the DoT on 29th January 2001 as envisaged under the New Telecom Policy of 1999, Licensees of Cellular Mobile Telephone Services were required to pay a License fee as a percentage share of gross revenue under the License. An extract of the "Migration Package" is below for reference:

1. *" The licensee will be required to pay one time Entry fee and License Fee as a **percentage share of gross revenue under the license**. The Entry fee chargeable will be the license fee dues payable by existing licensees upto 31.07.1999, calculated upto this date duly adjusted consequent upon notionall extension of effective date as in para (ix) below, as per the Conditions of the existing license."*

f. The Telecom Regulatory Authority of India vide its recommendations dated **23rd June 2000** also recommended a definition of revenue for the purpose of calculating revenue share

wherein, it was specifically recommended that considering only revenues accruing to a licensee by way of operations of Cellular Mobile Telephone Services. Relevant extract from the TRAI recommendations dated 23rd June 2000 is reproduced below:

i. *"C. Definition of revenue for the purpose of calculating revenue share:*

ii. *6. The TRAI recommends the following definition of adjusted gross revenue for the purpose of the revenue share set out at (ii) above:*

a. *"Adjusted Gross Revenue" for the purpose of levying license fee as a percentage of Revenue Share shall mean the* ***"Gross Revenue" accruing to the Licensee by way of operations of the Cellular Mobile Service mandated under the license*** *(inclusive of revenue on account of value-added services, supplementary services, and the sale of handsets) plus revenue accruing through resellers, franchisees etc. plus any revenue foregone through subsidies on handsets or any other rebates,…."*

Similarly, TRAI in its recommendations dated 30.8.2000 and DoT in its references of 9.10.2000 and 31.10.2000 also conveyed charging of Revenues License Fee as a **percentage share of gross revenue under the license.**

g. Further, the Department of Telecommunications notified rules for the maintenance of books of account or other documents by the service provider vide its notice dated 27th November 2002. **This clearly establishes that the activities under the License granted to an Indian Registered Company were to be monitored and accounted for separately from the other activities conducted by the registered company and its established business.** This notice lists down the rules which are only related to services of a Cellular Mobile Telephone Services Licensee.

h. It is clear from the above facts that the levy of license fee as a percentage of revenue should and can only be levied on the revenues under the specific scope of services as contained in license condition 2 of the UASL.

i. In this regard, the definition of Gross Revenue (GR) as provided in the License Agreement must have a nexus with the licence activities. Further, the definition of the GR cannot be read in isolation and rather it has to be read along with the terms of the CMTS Migration Package, which was the genesis of license fee as a revenue share under the Revenue Sharing regime introduced vide NTP 1999, whereby it was clearly agreed between the parties that LF would be paid as a percentage of GR under the License. While we reserve our right to make detailed submissions in this regard at the appropriate stage and forum, both on validity and interpretation, it is submitted that even if we were to go by a plain reading of the definition, it cannot be concluded that all revenues from whatsoever source or activity are to be included into the definition just because of the same being inclusive and under the head of Miscellaneous Revenues etc. The contract has to be read in totality wherein the definition as provided in the License cannot be read in isolation and has to be read and informed by the true intent and spirit of the Migration Package wherein only revenues arising under the License i.e. from licensed activities are to be covered. It may also be noted that in any event, this question is presently pending adjudication.

j. DoT's stand in its statement dated 11 August 2011, submitted to the Hon'ble Supreme Court by way of the various affidavits filed by it, had agreed that it did not intend to charge LF on activities other than on licensed telecom activities. The Counsel for DoT, in a proposal submitted to DoT, had agreed that DoT had never intended to impose LF on non telecom revenues. The relevant extract of the DoT's statement filed with the Hon'ble Supreme Court in the AGR matter is reproduced below:

> *"The department's stand is that revenue from non telecom business which is entirely different from telecom business of the licensee is not included in the definition of GR. (this is also the consequence of maintaining separate accounts)"*

This affidavit is enclosed as Annexure - I.

k. Hence, our request to the Authority is to formulate its recommendations for the definition of Gross Revenue to be applicable uniformly of all licenses as Revenues from services offered under the scope of services of the respective licenses. The deductions to arrive at the AGR value should be also be uniform for each substitutable service offered by various licensees. i.e, ISPs and UASL utilizing Spectrum to deliver Internet access should be allowed the same deductions from the revenues derived for the services.

2) The **Adjusted Gross revenue** for the purpose of levy of License Fee charged on revenue share basis must exclude the revenue generated from the provision of pure internet services.

3) The **exclusions or deductions** from the Gross Revenues from Internet services should be uniform across different licenses offering the same services i.e, UASL and ISP, ISP-IT.

4) In its recommendations dated 21st September 2006 TRAI had recommended for several items for deductions from the Gross Revenue for the purposes of arriving at the AGR of licensees. These are listed in "*point no 4 of Section II*" of our submission above.

5) The **deductions** on account of Pure **Internet Services**, both Wireless and Wireline, should include the revenue from Internet Content services and charges paid to other eligible telecom service providers such as NiXi, Upstream ISPs, NLDOs, ILDOs for provisioning of internet bandwidth.

6) **Deduction of Taxes:** Some State Governments have started levying entertainment tax on the VAS components of telecom service across many Service Areas and therefore the scope of service/sales tax deduction allowed under license presently should be extended to include the entertainment tax as well.

7) Deductions should apply for telecom resources taken from other telecom service providers to delivery services, since the applicable license fee is paid on such revenues by the respective service providers. Currently, the payments made for critical inputs like bandwidth are not allowed as deductions while calculating AGR on which license fee is payable by a telecom operator. This is even when the bandwidth provider has already paid license fee on revenue received from the end service provider. This would hamper the objectives of NTP 2012 which envisages high growth of affordable internet & broadband in the country while leading to **double taxation**. Therefore, it is suggested that the license / spectrum fee to DoT should be treated on lines of G.S.T. /service tax; accordingly every service provider would charge the license/spectrum fee as part of the invoice to the recipient of such services and would deposit the same to DoT. However, the license fee so reimbursed by the customer be allowed to be deducted

out of total license/spectrum fee payable by the recipient service provider/telecom operator. This would be on the same line as G.S.T. or service tax where set off of amounts paid on inputs are allowed against amount of G.S.T. or service tax payable on output. As also Dual Charging of revenues in the hands same and other service providers should be avoided.

8) **The deductions should be on accrual basis**: The payments may not actually be credited within the same quarter but, payments made are critical to calculating the true license fee hence, allowed deductions – payments should be considered on accrual basis. This is also in line with the Accounting concepts and conventions (matching concept). TRAI's Recommendations dated 21st September 2006 should be reiterated wherein Taxes and IUC was recommended in point '3.24.3.4' to be shown on accrual basis for both inclusion and exclusion for the purpose of AGR.

It is further submitted that the format of AGR and the items allowed as deductions on account of pass through should be consistent and must be same in the definition of AGR across the various Licenses i.e. the deductions allowed as pass through in one license should also be allowed as pass through in the other licenses to maintain uniformity. Moreover, a minimum presumptive AGR is against the principle of NTP 99 whose objective was to reduce a fixed burden on the operators but to instead charge them on a revenue sharing principle.

2. Should minimum presumptive AGR be applicable to BWA Spectrum holders under Internet Service/Access Service license(s) and other licenses with or without spectrum, including access service licenses? If yes, what should the value of minimum presumptive AGR?

Bharti Airtel's Response

- As of now BWA is in a very nascent stage. The technologies for delivery of services in BWA i.e, LTE etc. are not yet fully mature or standardized. There are further developments still taking place in these technologies.

- At the time of allocation of BWA spectrum Roll out obligations were prescribed to be met in a defined period. There is still time for the roll-out obligations to be met by respective service providers and while the technology may also take longer to mature.

- Hence, this issue may be better reviewed after the prescribed Roll out obligations period and based on the technology and market related conditions prevalent at that stage.

3. Please suggest the amendments required in the formats of statement of revenue and licence fee reported by various categories of Internet service licensees and UAS licensees.

Bharti Airtel's Response

1) As submitted in our response above:

   a. Be uniform across different licenses offering the same services i.e, CMTS, UASL and ISP, ISP-IT etc.

   b. The deductions on account of Pure **Internet Services**, both Wireless and Wireline, should include the revenue from Internet Content services and charges paid to other eligible telecom service providers such as NiXi, Upstream ISPs, NLDOs, ILDOs for provisioning of internet bandwidth.

c. **Deduction of Taxes:** Some State Governments have started levying entertainment tax on the VAS components of telecom service across many Service Areas and therefore the scope of service/sales tax deduction allowed under license presently should be extended to include the entertainment tax as well.

d. Deductions for telecom resources such as Bandwidth, Leased Lines obtained from other eligible telecom service providers should be applicable. In the absence f a valid deduction the issues leads to Double Taxation of the same resources. Hence, license fee and spectrum fee to DoT should be treated on lines of G.S.T. /service tax wherein the license/spectrum fee so reimbursed by the customer be allowed to be deducted out of total license fee payable by the recipient service provider/telecom operator. As also Dual Charging of revenues in the hands same and other service providers should be avoided.

e. **The deductions should be on accrual basis**: The payments may not actually be credited within the same quarter but, payments made are critical to calculating the true license fee hence, allowed deductions – payments should be considered on accrual basis. This is also in line with the Accounting concepts and conventions (matching concept).

2) The Statement of Revenue – AGR

- **For ISP, ISP-IT and UASL:**

a. For **revenues from Internet Services** the AGR should be simplified to show the revenue under the following broad categories:

- Revenue from Internet Access Service
- Revenue from Internet Content Service, Web Hosting, Web Co-location
- Revenue from Internet Telephony Services
- Revenues from Roaming Services

b. The following deductions should be added to the respective formats

- Revenue from Internet Access Service
- Revenue from Internet Content Services, Web hosting, Web co-location
- Roaming Revenue Passed on to other eligible telecom service providers.
- **Deduction of Taxes:** In line with our recommendation in the matter of AGR definition, the format of AGR should be modified to include the deduction towards Entertainment Tax.
- Deductions for revenues passed onto / payments made to other eligible service providers including bandwidth, leased line and other such revenues to avoid dual charging of such revenues as license fee / spectrum fee.

c. Other deductions that should rightly apply in the AGR Statements for UASL and ISP and as suggested in our response above that those gains and revenues not arising out of activities

under the scope of services of the license should not be considered in the 'Gross Revenue' of the License.' Therefore these items should also be excluded from the AGR as well. Such incomes, gains and revenues have been recommended for exclusion in TRAI's Recommendations dated 21st September 2006. Changes may be applied appropriately to the respective statements of all licensees I.e, UASL, ISP, ISP-IT, NLD, ILD. These as requested should not form a part of 'GR' notwithstanding which, they should be allowed a deduction from the GR.

DoT Handover. 11/08/2011

Statement of Behalf of DoT

(1) The department's stand is that revenue from non telecom business which is entirely different from telecom business of the licensee is not included in the definition of GR. (this is also the consequence of maintaining separate accounts)

(2) Interest and dividend which were specifically included in the definition of AGR/GR and mentioned in the Appendix-II at Page 349, Vol II is to be included only to the extent the interest or dividend is attributable to that particular service area(license) at page 343, Vol II. This is a necessary consequence of the licence and Appendix-II being in respect of that particular service area.

(3) In order to attribute interest to a particular service area the following formula of apportionment is to be applied:-

$$\frac{\text{Interest} \times \text{Revenue from that licence area}}{\text{Total revenue}}$$

This necessarily follows from the obligation to provide reconciliation statement as stipulated in para 20.7 (pg. 247, Vol II).

It should be noted that the interest earned by the main corporate entity can never be reconciled with the A/cs of each service area unless the interest attributable to each area and other business adds up to the total interest earned by the corporate entity.

(4) At no stage the department seeks to levy the revenue share in respect of various licences held by the company on the same revenue receipt more than once.

(5) All discounts mentioned in the price list filed before TRAI are excluded. However alleged ad hoc discounts which are not reflected in the price list are not excluded.