

Leading Indian Telco faced with fine of INR 6000 million.

Summary

Even as the industry prepares itself for consolidation in a crowded telecom market, service providers are fending off massive fines for violating cross-holding norms under Indian regulations.

The latest casualty in the list of telecom companies penalized by the Department of Telecommunications (DoT) is Idea Cellular, which has been fined to the tune of INR 6,000 million for allegedly violating license conditions in its merger with Spice Communications. Under the unified access service (UAS) license, no entity is allowed to hold more than 10% equity in multiple telecom companies offering the same service in the same area.

In 2008, Idea Cellular acquired 41.09% stake in Spice Communications and the two companies subsequently merged resulting in overlapping licenses in six circles - Andhra Pradesh, Delhi, Haryana, Maharashtra, Punjab and Karnataka. Wary of any anti-competitive behavior seeping into the industry, the government was quick to investigate the alleged breach and issued a notice to Idea Cellular demanding payment of the penalty amount so that the DoT could record the merger. A similar allegation mars Essar Group, which is alleged to have held more than 10% equity stake in two telecom companies in the Mumbai telecom circle.

Since the notice sent to Idea Cellular is not publicly available, the methodology used by DoT to determine the penalty is not known. The UAS license does not prescribe any guidelines on the imposition of the penalty and simply provides that the DoT can impose a financial penalty not

exceeding INR 500 million, exclusive of liquidated damages, for violation of terms and conditions of the license. Since this matter involves six UAS licenses, it is unclear how DoT arrived at the figure of INR 6,000 Million.

Telecom companies in India have been crying foul, alleging that in most cases, the penalties imposed on them have been arbitrary and have demanded clearer guidelines for calculating the penalty. Though the recently introduced unified license (UL) regime (which will replace the existing UAS license) has clarified the penalty clause to some extent, it still fails to lay down any guidelines on how the quantum of penalty is to be calculated. The Telecom Regulatory Authority of India (TRAI) has recommended classifying the penalty amounts into two categories - minor and major. It has suggested the imposition of a maximum penalty of up to INR 2.5 million in the case of a minor violation and up to INR 100 million for a major violation. While several jurisdictions, such as the United States and Singapore, have adopted a graded penalty system based on the severity of the offence, the recommendations of the TRAI are yet to be implemented.

On the cross-holding rule, it is interesting to note that the newly introduced UL regime has imposed a stricter condition on cross-holding by prohibiting an operator from acquiring any equity in a company that holds spectrum in

the same service area. Although a complete prohibition on cross-holding may appear to be extreme, the government has advanced several reasons to justify this condition. Most notably, it has contended that the former regime permitted companies to hold up to 10% equity stake in multiple firms through complex holding structures, with the objective of circumventing such restrictions.

Even the preliminary task of identifying promoters and deciphering the complex holding structure has been a source of difficulty for the Government. This is evident from the fact that the cross-holding allegation against the Essar Group is being investigated by various government departments such as the Central Bureau of Investigation, DoT, Ministry of Company Affairs and the Enforcement Directorate. In order to avoid further embarrassment, the government has now closed the loopholes in the UL. For one, it has specifically defined the term 'beneficial interest' to mean the holding of any equity, directly or indirectly, 'including through a chain of companies' in another operator holding spectrum in the same service area, allowing exceptions only for investments by financial institutions, scheduled banks and the central government.

Existing operators that hold even a minority stake in competing operators (for example Vodafone, which holds 4.4% equity stake in its rival Bharti Airtel) will have to grapple with the new licensing regime and the attendant prohibition on cross-holding of equity. Keeping this in mind, telecom companies would do well to ensure that previous cross-holding violations, if any, have been settled once and for all.