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To:
Shri Rajeev Agrawal,
The Secretary
Telecom Regulatory Authority of India
New Delhi

Dear Sir,

Sub: Response to Consultation paper on ‘Auction of Spectrum’

1. This is in response to the consultation paper put up by TRAI, inviting suggestions as to the modus of implementing the Supreme Court’s order for auctioning the 2G spectrum for mobile telephone services.
2. At the outset I wish to declare that I am 75 years of age, a Cost Accountant by profession and retired from service nearly two decades ago, the last position held being that of Director (Finance) in a PSU under the MoPNG. I also wish to state that I do not represent any interest groups in the telecom sector. However, the paper is written keeping in view of the core objectives of NTP 1999 viz, Affordability, Growth, Competition and a Level Playing Field to all operators.
3. Telecom sector has been an area of my interest of my studies and have been fascinated by its explosive growth in the recent years, making it affordable to even to those in the low income groups, bringing them immense benefits from its usage, both economic and social. My interest grew greater when the CAG brought out the irregularities in the issue of 2G licences in Jan 2008 and placed the presumptive loss at Rs 176645 cr, by issuing them at the entry fee prevailed in 2001.
4. My examination revealed that, while admittedly there were serious irregularities in the issue of licences, there was no loss to the exchequer and that the quantification of loss was flawed. All that happened was instead of the licences being issued to A, B and C they were given to X, Y and Z the latter jumping the queue by devious means. However, the pricing was based on sound reasoning with a view to keep the tariff affordable to all and at the same time to ensure

a fair competition in the sector by providing a level playing field to all. Therefore, the question of exchequer losing any money did not arise, despite the criminality in issuing them to ineligible entities. Based on my findings I had made a 35-page presentation both to the PAC as well as to the JPC, examining the 2G Scam, copies of which were also made available to the DoT.

5. The criticism made by both CAG as well as by the Supreme Court on the role of TRAI in the pricing of 2G spectrum and giving them at 'throw away prices' was rather disappointing and reflected a lack of appreciation of TRAI's stand on the issue. In fact the TRAI was truthfully implementing the objectives of NTP 1999 viz, to make mobile telephones available on demand and affordable to all by creating competition and a level playing field to all operators; explained later.
6. Having read the consultation paper and the 36 questions posed therein, I wish to confine my submissions to the first two questions only viz :

Q1. How can the various principles outlined by the Hon'ble Supreme Court in various observations brought out in para above be sufficiently incorporated in the design of spectrum auction?

Q2. What are the key objectives to be kept in mind in the auction of the spectrum?

7. The key observations/principles/directives laid down by the Hon. Supreme Court with reference to the above could be summarized as under:
 - a. While distributing/allocating scarce resources the state should act in a just and equitable manner keeping the larger public good in mind.
 - b. Its actions should not be arbitrary or capricious.
 - c. In awarding contracts the state to ensure competition and not discrimination.
 - d. They can augment their resources but the object should be to serve the public cause and to do public good by resorting to fair and reasonable methods.
 - e. The procedure adopted for distribution is just, non-arbitrary and transparent and that it does not discriminate between similarly placed private parties.
8. On the face of the above observations it would appear that the allocation of licences in Jan 2008 suffered from the above

inadequacies, as the directive for auctioning the licences is consequential to those observations. However being respectful of the observations of the apex court, one would wish to highlight how an auction can go against the public good, that the court is trying to protect.

9. It was based on a transparent auction process in 1994-95 the licences were awarded in the metro areas. The fee committed by the bidders was high at Rs 500000 for every 100 subscribers, (an average monthly levy of Rs 400 p.m per subscriber towards licence fee alone) regardless of revenue earned. The tariff was accordingly fixed high at Rs 16 per minute which very few could afford. The ARPU during the period 1997-99 was around Rs 1500 p. m in the metros; consequently the growth suffered and the industry became sick.

[In the context of the auction of licences/spectrum now planned, this is an important point that cannot be missed. A high upfront charge realized towards licence fee/spectrum charges is bound to be built into the tariff and would impact on growth and therefore not in the interest of either the subscribers or the exchequer.]

10. The government of the day therefore came out with a new policy viz, NTP 1999 that set the objectives among others, as under:

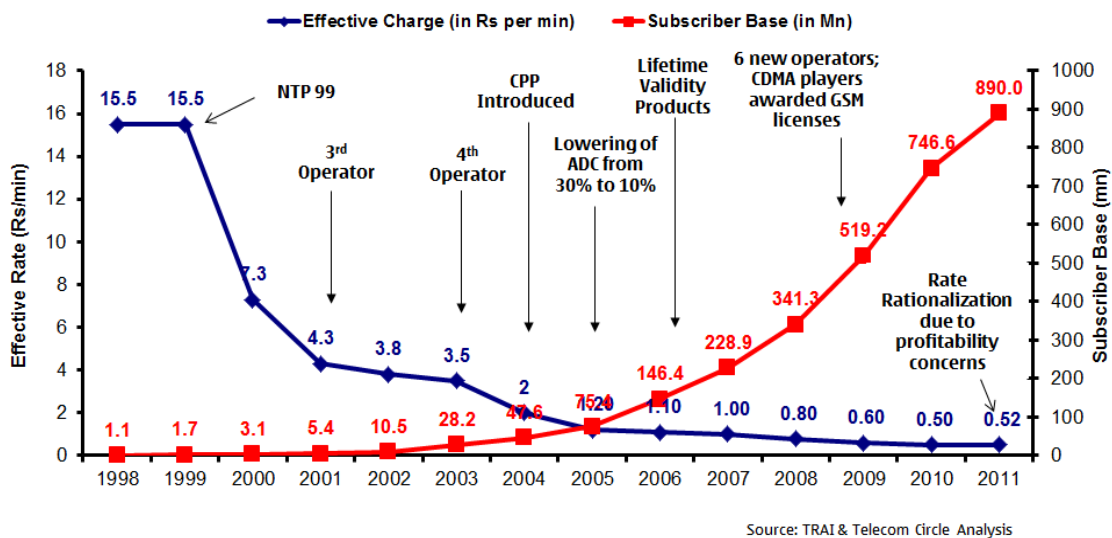
“Availability of affordable and effective communications for the citizens is at the core of the vision and goal of the telecom policy...”

“Transform in a time bound manner, the telecommunications sector to a greater competitive environment in both urban and rural areas providing equal opportunities and level playing field for all players”.

Later, the 10th plan (2002-07) objectives of the government for the sector reiterated the objective of NTP-1999, ***that “revenue generation should not be a major determinant of the macro policy governing the [telecom] sector..... spectrum policy needs to be promotional in nature; revenue considerations playing a secondary role”*** (emphasis added)

11. In accordance with the above policy objectives, the industry was given remission of the outstanding fee payable for the remaining licence period, provided they opted for a revenue sharing arrangement and also agreed to remove the cap of two operators per circle. All operators agreed to migrate to NTP 1999 in lieu of an upfront licence fee/spectrum charges.

12. It was only because of the removal of the high upfront fixed charges that enabled the operators to reduce the tariff, which in turn led to a higher growth and at the same time brought increased revenue to the exchequer. The reduction in tariff and the growth resulted in a virtuous cycle, on the one hand bringing down the tariff from a high of Rs 16 per minute in 1999 to the present level of about 50 paise and an exponential growth from less than a million in 1998 to more than 900 million as of Jan 2012. This is well presented in the graph put up by TRAI, which is reproduced below.



The ARPU that was around Rs 1500 p. m in 1999 has come down to Rs 93 in QE Sep 2011 making mobile telephone affordable to all. The fall in tariff and ARPU is even greater if one took into account of the fall in the rupee value during the past 12 years.

13. The exchequer has not been a loser either. As against the licence fee forgone in 1999, (according to one unauthenticated estimate as much as Rs 43000 cr) by way of revenue sharing, the govt would have already collected more than Rs 100000 cr towards licence fee and spectrum charges till March 2012 and continues to collect Rs 14000 cr p. a. Today about 13.5 percent of the Adjusted Gross Revenue goes to the exchequer on these counts alone. Further, the govt would have collected service tax of the order of Rs 75000 cr from mobile telephony till now.

14. However, it appears that the Hon: Supreme Court has not taken cognizance of the huge income to the exchequer that has accrued by way of revenue sharing in place of a one-time upfront levy by auction, that alone led to the exponential growth in the sector.

15. In Dec 2007 there were 234 m subscribers serviced by an average of six operators in each circle. All these operators had paid an entry fee of Rs 1659 cr or thereabouts for a pan-India licence and had already well established in the market. The purpose of issuing more licences was to create increased competition. Now, if the new operators were to be given licences at an entry fee higher than that, how could that have been equitable to them? **Would that not have created discrimination instead of competition and gone against the very principle enunciated by the Hon: court that “In the field of contracts, the State and its instrumentalities should design their activities in a manner which would ensure competition and not discrimination”?**
16. To illustrate the extent of discrimination that would have inflicted upon the newcomers, let us assume that the process of auction would have fetched an additional Rs 176645 cr as contended by the CAG. i. e at a rate of Rs 16750 cr for a pan-India licence as against Rs 1659 cr at which they were given to the existing operators. Assuming that the cost of servicing this additional investment to be at 15 percent towards financing cost and amortization of the increased fee payable, this would have imposed an extra burden of Rs 27000 cr per annum on the industry as a whole. (Of this the burden to a new operator holding a pan-India licence would be as much as Rs 2250 cr p.a.) For the year 2007-08, the Adjusted Gross Revenue of the industry was 101485 cr; therefore in order to stay afloat, the industry would have had to increase tariff across the board by 27 percent. But the new entrants would be severely handicapped as they had to bear an additional servicing cost of Rs 2250 per annum each. As against that the existing operators would be affected only on the extra spectrum procured over and above 4.4 MHz at the higher price. Under these circumstances how could the new operators be competitive, more so as TRAI had pointed out in one of its recommendations that, the cost of procuring subscribers to the new entrants would be higher as they have to go deeper into the areas so far not covered by the existing operators?
17. If the exchequer had suffered a loss of Rs 176645 cr by issue of licences at the entry fee prevailed in 2001, as alleged by the CAG, there ought to have been a corresponding gain to the operators and should have been reflected in their working results. But on the contrary what one has seen is, while there was substantial increase in the subscriber base from 234 m in Dec 2007 to 903 m in Jan 2012, there was a continuous reduction in the tariff and erosion in the ARPU as well as in the bottom line (PBT) of the mobile companies.

18. If the spectrum is to be auctioned now, one cannot wish away the tariff being increased by the operators which would be detrimental to the subscribers and impact upon the future growth. It is to be noted that the capacity to pay by the hitherto not covered rural sector is lower than those who already possess the mobile phones.
19. Thus while one cannot see the rationale for auctioning the licences to new operators who would be handicapped vis-à-vis the existing operators who got them at an entry fee of Rs 1659 cr, since it is a directive of the Hon: Supreme Court that has to be implemented, one would make the following suggestions:
- a. The bids for licence/spectrum should be subject to the condition that the tariff charged shall not exceed say, 40 paise per minute, excluding the governmental levies like, licence fee/spectrum charges, service tax etc at rates prescribed from time to time. Thus, at the existing rates of 8 percent for licence fee, 5 percent for spectrum charges and 12 percent for service tax, the total charge to the subscriber would be 50 paise per minute. This would dissuade the bidders from quoting high prices in anticipation of the same being passed on to the subscribers by way of a hike in tariff.**
 - b. The new bidders (including those cancelled) should be given a bidding credit of 50 percent vis-à-vis the old operators quoting for additional spectrum. This would help giving a level playing field to the new comers in order to be able to compete with the existing operators. However, there should be safeguards provided, against the misuse of the cheap spectrum so obtained, by diverting it to another operator by devious means, or trading the same for profit.**
 - c. If the above principle was accepted, the percentage of revenue sharing towards the licence fee and spectrum charges should be the same for all, regardless of the quantum of spectrum held, albeit it may vary from circle to circle.**
 - d. A minimum guaranteed quantum of spectrum should be bundled with the licence as was done before. It is meaningless to issue a UAS licence without spectrum as no operator would be able to survive by offering fixed line telephones alone, the demand for which is on the decline.**

- e. As spectrum is scarce, it is important that it is used efficiently. While more number of operators in a circle would, no doubt, provide increased competition, it results in higher wastage of spectrum as a certain percentage of bandwidth allotted to each operator would be used for signaling channels, interference management etc and therefore not available for carrying voice/data signals. This opportunity should therefore be made use of in order to limit the number of operators in each circle to an optimal level from the present 12. It is believed in several developed countries they manage with less number of operators not exceeding 5, and therefore able to get more spectrum.**

I shall be pleased to provide you any clarifications or supporting data if needed. The delay for submitting the response may kindly be condoned.

Thanking you,

Yours faithfully,

C S Jacob