

EXECUTIVE SUMMARY

A summary of the submissions made by Unitech Wireless (Tamilnadu) Pvt. Ltd. in the following sections in response to the Consultation Paper No. 04/2012 dated March 07, 2012 issued by the Telecom Regulatory Authority of India (“**TRAI**”) is stated as under:

1. Competition

- 1.1 The Indian telecommunication sector expanded significantly since 2008, both in customer numbers and infrastructure reach, predominantly driven by increased competitive forces resulting from the introduction of new and innovative operators.
- 1.2 The Indian consumer and society has been the main beneficiary of this increased competitive landscape through increased choice of operators, tariffs and products. These benefits have been a direct result of the Government of India’s (“**GoI**”) focus on a policy of increased competition and efficiencies and the policy of the GoI to provide the start-up spectrum of 4.4 MHz to the new operators bundled with the UAS Licenses.
- 1.3 The safeguarding of competition should be the focal point while designing the structure and strategy for the 2G auctions, such that the process of issuance of fresh licenses and spectrum is carried out in a prudent, transparent and time-efficient manner.
- 1.4 Without prejudice to the reliefs sought in the review petition all possible efforts should be made to complete the auction of spectrum and grant licenses no later than June 2, 2012 so as to prevent disruption of services to a substantial number of mobile subscribers using the services offered by operators affected by the verdict of the Hon’ble Supreme Court. In our view, the four month timeline after which the order of the Hon’ble Supreme Court is to be effective was intended to minimize this disruption. A break in our ability to offer services to our customers because of a long drawn auction process would imply a long period of uncertainty for customers, employees and vendors and would seriously affect our long term competitiveness and the strong market position that we have been able to build.
- 1.5 The benefits of competition, if not safeguarded through the 2G auction recommendations undertaken by the TRAI, could be severely affected to the detriment of the public interest, and must be avoided by TRAI and the GoI.
- 1.6 Ensuring a level playing field among operators will ultimately benefit the Indian consumer. Conversely, permitting a very high upfront costs for spectrum driven by well entrenched incumbent operators or otherwise will ultimately have an adverse impact on the competitive landscape and will prevent a level playing field from being created.
- 1.7 A deferred payment schedule for the winning bid price of spectrum won in the auction will enable new operators to direct their available capital towards the expansion of networks and services. Such arrangements have been employed globally. It may be noted for the record, that in the Indian context also, for the first two circle licenses in 1998, the entry fee structure was designed for payment via annual installments adding up to bid price.

2. Auction Structure and Rationale

- 2.1 The primary objectives of the government should be the larger public good in the following sense:
- i. A fair and transparent procedure ensures that the public can be confident that the larger public good has actually been driving auction design and auction-related decisions.
 - ii. Efficient outcomes (taking the auction's effect on competition into account) promote welfare and growth directly.
 - iii. Maximizing government revenue *insofar compatible with objective (i) and (ii)* makes sense from a public policy perspective and ensures that Indian citizens enjoys the "resource rent" which can be collected without distorting the use of the frequency resources.
- 2.2 We propose a multi-stage auction procedure. In the primary stage, the cancelled 1800 MHz spectrum should be offered to bidders that were actually, or could have been, eligible for receiving spectrum in 2008 had they applied. Given that on an average in each circle, 4 licenses holding 1800 MHz spectrum have been cancelled by the Hon'ble Supreme Court, a **minimum of two blocks per circle of 6.2 MHz each of the cancelled 1800 MHz spectrum should be made available for auction in the primary stage**. To ensure a timely procedure within the deadline we propose that in the primary stage, the simultaneously ascending e-auction design, which has been previously successful in India in recent auctions, be used. **The reserve price should be set at the same per MHz level (adjusted for inflation, if required) as used in the auction of 2.1 GHz spectrum in 2010**. The auction process for the primary stage should be completed and fresh licenses and spectrum issued by June 2, 2012, in accordance with the Hon'ble Supreme Court's ruling. We also propose that the winning prices discovered in the primary stage should also be used as reference price for charging of spectrum held by incumbents beyond 4.4 MHz or 6.2 MHz as applicable per government policy. In the subsequent secondary stage(s), all available 2G spectrum should be included. All operators, including incumbents and those eligible for the primary stage should be permitted to participate in the subsequent secondary stage(s)
3. The issues of liberalization, re-farming, 700 MHz, spectrum sharing and spectrum trading should be handled at a later stage as outlined later in this document.

4. Rollout Obligations:

In order to ensure a level playing field, the new license and spectrum that may be given through the auction should not have roll out obligations different from the roll-out obligations already in place.

5. Validity of Spectrum

The period of validity of the spectrum and license should be 20 years as proposed in the Draft Unified License consultation.

In Conclusion:

- **A multi-stage auction should be held.**
- **Only those eligible, or would have been eligible for license and spectrum in 2008 had they applied be allowed to participate in the primary stage.**
- **A minimum of 2 blocks per circle of 6.2 MHz each of the cancelled spectrum to be made available in the primary stage.**
- **Reserve price for the primary stage be same as 3G reserve price (adjusted for inflation, if required)**
- **Auction Format for the primary stage: simultaneously ascending e-auction design that has been used in the India 3G auctions in 2010.**
- **Timelines: The primary stage of auction to be completed by June 2, 2012.**
- **Deferred Payment schedule to be allowed on winning bid price.**
- **The winning prices discovered in primary stage to be used as reference price for charging of spectrum held by incumbents beyond 4.4 MHz or 6.2 MHz as applicable per government policy.**
- **In the subsequent secondary stage(s), all available 2G spectrum should be included and all operators, including incumbents and those eligible for the primary stage should be permitted to participate.**

1. PREAMBLE

- 1.1 These submissions are being made by Unitech Wireless (Tamilnadu) Pvt. Ltd. (“**Uninor**”) pursuant to Consultation Paper No. 04/2012 dated March 7th, 2012 issued by the TRAI inviting consultation comments from stakeholders in respect of “Allocation of Spectrum”. At the outset, it is submitted that these submissions are *without prejudice* to any rights and contentions that Uninor may have before any Court of law and/or authority in connection with the Hon'ble Supreme Court's judgment dated February 2, 2012 in writ petitions no. 423/2010 and 10/2011 (“**SC Judgment**”).
- 1.2 The Indian telecommunication sector expanded significantly since 2008 both in customer numbers and infrastructure reach, predominantly driven by increased competitive forces resulting from the introduction of new and innovative operators. The Indian consumer and society has been the main beneficiary of this increased competitive landscape through increased choice of operators, tariffs and products. These benefits have been a direct result of the GoI focus on a policy of increased competition and efficiencies and the policy of the GoI to provide the start-up spectrum of 4.4 MHz to the new operators bundled with the UAS Licenses. The competitive landscape in 2012 is significantly altered since 2008 through above competitive forces created by the new operators. As outlined in Para 1.9 of our response to the Pre-consultation document, it is imperative that the process mandated by the SC Judgment is executed within the shortest possible time period in order to minimize the entry barriers for new operators affected by the SC judgment.
- 1.3 It is to be noted that eligibility for license and consequent spectrum allocation in 2008 was restricted to fresh applicants only. In the current case, the Supreme Court has effectively stepped back to 2008 and without requiring any change to the eligibility criteria, has held that:
- The first-come-first-served policy used by DoT in 2008 was flawed.
 - The method of selection of successful licensees by fixing a certain cut-off date was arbitrary.
- 1.4 To correct the above situation the Supreme Court has ordered that “*TRAI shall make fresh recommendations for grant of license and allocation of spectrum in 2G band*”. In recognizing that those eligible applicants below the cut-off date were unfairly treated, the Supreme Court has said that the procedure adopted for distribution should be just, non-arbitrary and transparent and that it should not discriminate between similarly placed private parties. The spirit and letter obviously is to ensure that all the then eligible parties should have been treated at par while selecting the successful licensees.
- 1.5 **From the above, it is evident that the SC Judgment did not intend that the auction of 2G license and spectrum should also be open to parties, who, in 2007/2008 already held UASL / CMTS licensees.**

- 1.6 In light of the profound impact on operators affected by the SC judgment and the pressing timing issues, we submit that TRAI focus on the recommendations for the allocation of spectrum by auction as outlined in the SC Judgment. The recommendations on licenses is currently ongoing through the Unified Licensing Consultation and therefore do not form part of this submission. Although, we view that the issues of re-farming, 700MHz, spectrum sharing and spectrum trading are important issues in their own right, we submit that these issues should be part of separate consultation process after the auction of the spectrum as mandated by the SC Judgment. This will give all relevant parties the opportunity to fully contemplate and evaluate the most optimum solution to these very fundamental issues. For the sake of time, consumer interest and maintaining the competitive landscape we submit that the process should strictly comply with the above referenced judgment.
- 1.7 We also request that all possible efforts be made to prevent disruption of services to the substantial number of customers who are using services of operators, such as, Uninor, who have been affected by the SC Judgment. In our view, the four month timeline after which the order of the Hon'ble Supreme Court is to be effective was indented to minimize this disruption. A break in our ability to offer services to our customers because of a long drawn auction process would imply a long period of uncertainty for customers, employees and vendors and would seriously affect our long term competitiveness and the strong market position that we have been able to build.
- 1.8 The principle of competition has been a constant thread throughout the SC Judgment, as we will illustrate in the following section on Competition in this submission. The same principle is also enshrined in the Indian Competition Act 2007 where the objective is as follows:
- “An Act to provide, keeping in view of the economic development of the country, for the establishment of a Commission to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interests of consumers and to ensure freedom of trade carried on by other participants in markets, in India, and for matters connected therewith or incidental thereto”*
- 1.9 Taking due account of the above and the principle of non-discrimination as outlined in the SC Judgment (Para 66), relating to access to fundamental State spectrum resources, we submit that the recommended auction structure and process needs to contain relevant provisions and mechanisms for prevention of reduced competition.
- 1.10 TRAI must recognize that the incumbents and new operators form profoundly different classes. Whereas the new operators are operating with the minimal spectrum of 4.4 MHz and have been in the business for 2-3 years only, the incumbents possess significantly larger chunks and collectively the lion's share of the entire allocated spectrum. They have also been in the business much longer and built significant market power on the back of these spectrum allocations. The auction format should reflect these differences to ensure that the benefits brought by the competition created by the new operators of 2008 are not lost. For the same reason TRAI must also ensure that it does not apply any rollout obligation to new operators that is more onerous

than that applied to the incumbents in the past. It may also be noted that whereas success in the auctions would be a life and death issue for operators impacted by the SC Judgment, but for the incumbents it would be purely a business choice.

- 1.11 Although, it is our position that the policy of the GoI to provide the start-up spectrum of 4.4 MHz bundled with the UAS licenses has been in public interest and has made telecommunications services affordable to the masses, we do not see contradictions in the principle of competition for scarce State resources and the maintenance of a healthy competitive telecommunication market *if* the State puts into this auction all 1800 and 800 spectrum on hand and ensures that the relevant safeguards are put in place to comply with both the SC Judgment and the principles contained in the Indian Competition Act 2007. The main issues here are prevention of collusion between parties, limitation to the amount of scarce resources allocated to each operator and avoidance of speculative spectrum purchases by incumbents with the aim of reducing competition.
- 1.12 In light of above, we enclose an extract from the Indian Competition Act which is pertinent in light of this issue:

“(3) Any agreement entered into between enterprises or associations of enterprises or persons or associations of persons or between any person and enterprise or practice carried on, or decision taken by, any association of enterprises or association of persons, including cartels, engaged in identical or similar trade of goods or provision of services, which—

- (a) directly or indirectly determines purchase or sale prices;*
- (b) limits or controls production, supply, markets, technical development, investment or provision of services;*
- (c) shares the market or source of production or provision of services by way of allocation of geographical area of market, or type of goods or services, or number of customers in the market or any other similar way;*
- (d) **directly or indirectly results in bid rigging or collusive bidding, (emphasis added)***

shall be presumed to have an appreciable adverse effect on competition:”

- 1.13 The most certain way to shield new operators from predatory bidding, and from the *exposure risk* described by TRAI in its Consultation Paper, is to hold a multi-stage auction of spectrum:
- 1.13.1 In the primary stage, the cancelled 1800 MHz spectrum should be offered to bidders that were actually, or could have been, eligible for receiving spectrum in 2008, had they applied. Given that on an average in each circle, 4 licenses holding 1800 MHz spectrum have been cancelled by the Hon’ble Supreme Court, a **minimum of two blocks per circle of 6.2 MHz each of the cancelled 1800 MHz spectrum should be made available for auction in the primary stage**. The same rules as the simultaneously ascending e-auction format previously used in India in the 3G auction could be applied directly as long as bidder can buy at most one of these blocks in the primary stage. **The reserve price should be set at the same per MHz level (adjusted for inflation, if required) as used in the above mentioned auction of 2.1 GHz 3G spectrum.** The auction

process for the primary stage should be completed and fresh licenses and spectrum issued by June 2, 2012. We also propose that the winning prices discovered in the primary stage should also be used as reference price for charging of spectrum held by incumbents beyond 4.4 MHz or 6.2 MHz as applicable per government policy.

1.13.2 *In the subsequent secondary stage(s), any available 1800 MHz spectrum (subsequent to the primary stage) should be included. All operators, including incumbents and those eligible for the primary stage should be permitted to participate.*

1.14 Certain parties may argue that limiting the primary stage to specific entities would be discriminatory, by quoting the clause from the SC judgment, which says that the auction process “*does not discriminate between similarly placed private parties*”. We disagree with such an argument. While the SC judgment does stipulate that the auction process shall “*not discriminate between similarly placed private parties*”, the **Hon’ble Supreme Court DOES NOT PRECLUDE safeguards** being made in the case where the **parties are NOT SIMILAR PLACED**. The concerned clause is quoted below:

*“the doctrine of equality, which emerges from the concepts of justice and fairness, must guide the State in determining the actual mechanism for distribution of natural resources”.....*demands that the procedure adopted for distribution is just, non-arbitrary and transparent and that it *does not discriminate between similarly placed private parties*”. (Para 69).

Clearly, the licensees impacted by the SC Judgment and the incumbents are not “similarly placed”.

1.15 Finally, to enable new operators to direct their available capital towards the expansion of networks and services, a deferred payment schedule for approved bid price of spectrum won in the auction. Such arrangements have been employed globally. It may be noted for the record, that in the Indian context also, for the first two circle licenses in 1998, the entry fee structure was designed for payment via annual installments adding up to bid price. We propose that 25% of the winning bid price in the auction be payable up-front soon after the auction. The remaining 75% should be payable in equal installments over 10 years subject to interest at SBI’s Prime Lending Rate + 1%.

2. COMPETITION

2.1 The Indian market has changed considerably since 2008, mainly through the activities of the new entrants. They have made significant impact in the circles where they are present, and taking due account of that the time since issuance of these licenses has been very short, such impacts have already given major benefits to consumers and Indian society.

2.2 We would like to outline that the benefits of competition, if not safeguarded through the 2G auction recommendations undertaken by the TRAI, could be a permanently lost to the extreme

detriment of the public interest, and must be avoided by TRAI and the GoI.

2.3 Ensuring a level playing field among operators will ultimately benefit the Indian consumer. Conversely, allowing a very high upfront costs for spectrum driven by well entrenched incumbent operators or otherwise will ultimately have an adverse impact on the competitive landscape and will prevent a level playing field from being created.

2.4 The Supreme Court Judgment

2.4.1 The SC Judgment has placed “*the public interest*” front and central while considering the issue of the government’s right to “*alienate, transfer or distribute natural resources / national assets.*” In the SC Judgment, the Hon’ble Supreme Court has observed that:

- “the State is bound to act in consonance with the principles of equality and public trust and ensure that *no action is taken which may be detrimental to public interest.*” (Para 63)
- “In Article 39 (b) of the Constitution, it has been provided that the ownership and control of the *material resources of the community should be so distributed so as to best sub-serve the common good, ...*” (Para 63)

“In the field of contracts, *the State and its instrumentalities should design their activities in a manner which would ensure competition and not discrimination.* 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.*” (Para 66)

- “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.*” (Para 72)

2.4.2 The “*public interest*” as emphasized by the SC Judgment is best served by government policies that lead to optimum ‘welfare outcomes’ for the society as understood in economics terminology. In the Telecom Sector, specifically, government actions that promote and safeguard effective competition in the marketplace, thus leading to affordable, high-quality services for the end consumer, are an important pillar of ensuring such an optimum welfare outcome.

2.5 NTP-99 and Draft NTP 2011

2.5.1 While designing the auction process for new licenses, one needs to ensure that competition, one of the pillars of the New Telecom Policy, 1999 (“NTP-99”), is not compromised in any fashion. In clause 2.0, the NTP-99 lays out, as one of its objectives:

*“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”*

- 2.5.2 In clause 3.1.1, on Cellular Mobile Service Providers, NTP-99 emphasizes the need for regular spectrum reviews and more operators in light of, inter-alia, competition:

*"It is proposed to review the spectrum utilisation from time to time keeping in view the emerging scenario of spectrum availability, optimal use of spectrum, requirements of market, **competition** and other interest of public. The **entry of more operators** in a service area shall be based on the recommendation of the TRAI who will review this as required and no later than every two years."*

- 2.5.3 The same focus on competition is in fact replicated under every category of service conceived in NTP-99, like Fixed Service Providers, Radio Paging Service Providers et al, indicating thereby that competition was considered an important aspect of NTP-99.

- 2.5.4 In the preamble to the Draft National Telecom Policy, 2011, it is stated that:

*"For the continued growth trajectory of telecom sector, it is **crucial to establish appropriate mechanisms to achieve balance between competition and consolidation** while dealing with the legacy issues in the sector, thus benefiting both the users and providers of telecommunication services. (Point 4).*

The preamble also states that:

"In achieving the goals of National Telecom Policy 2011 revenue generation will play a secondary role." (Point 2).

- 2.5.5 Over the years, the faith bestowed by the Government policy on the merits of competition in meeting the interests of subscribers has been reinforced again and again, as every time new licensees were introduced, the industry reacted with renewed vigor to woo its customers with more choice, and attractive offerings.

2.6 **TRAI on Competition and its validation following the grant of 2008 UAS Licenses**

- 2.6.1 A milestone worth mentioning is the introduction of the Unified Access Services License (UASL) regime in November 2003. In its recommendations of October 2003, TRAI recognized in para 2.1 that:

"Tariffs dropped by more than 50% with the entry of WLL(M) players in early 2003."

and in para 2.8 of the same recommendations, clause 11(1)(a)(iv) of the TRAI Act was quoted which requires TRAI to make recommendations on:

"measures to facilitate competition and promote efficiency in the operation of telecommunication services so as to facilitate growth in such services."

in the same document in para 3, TRAI further acknowledged that:

*"Technological developments over the past few years have made the mobile wireless phone, the phone for the common man from the earlier image of a phone for the elite. Of course, **increasing and intense competition leading to reduced tariffs and falling capital costs have also contributed to this phenomenon.**"*

and in para 6.3, TRAI stated that:

"(subscriber) growth has multiplied manifold only after intense competition started between cellular and WLL and also the 3rd Mobile Operator and the consequent fall in tariffs."

2.6.2 In November 2003, DoT accepted TRAI's recommendations, which meant that the hitherto WLL(M) operators would thence expand the list of full mobility operators. In its guidelines for the new UASL licences, DoT opened the document by reiterating the objectives of NTP-99, and cited the steep reduction in tariffs due to competition:

*"Given the central aim of NTP-99 to ensure rapid expansion of teledensity; given the **unprecedented expansion of telecom services that competition has brought about**; given the **steep reductions in tariffs that competition has ensured**; given the recommendations of TRAI in this regard; Government, in the public interest in general and consumer interesthas decided to move towards a Unified Access Services Licensing regime."*

2.6.3 The monumental impact of introduction of new mobile operators on reduction in tariffs, and the impact it had on the affordability of telecommunication services for the masses is now etched in history.

2.6.4 The next important milestone, vis-à-vis the beneficial impact of enhanced competition occurred in 2007. In its recommendations of August 2007 on the "Review of licence terms and conditions and capping the number of access providers", **TRAI reinforced the merits of not curbing competition while recommending that the number of access providers should not be capped**. In para 2.1, it opined that:

"...The increase in the number of service providers has brought with it specific benefits.....Additionally, the subscriber base and coverage have increased dramatically due to increased competition and the effort by service providers to capture the largest market share.

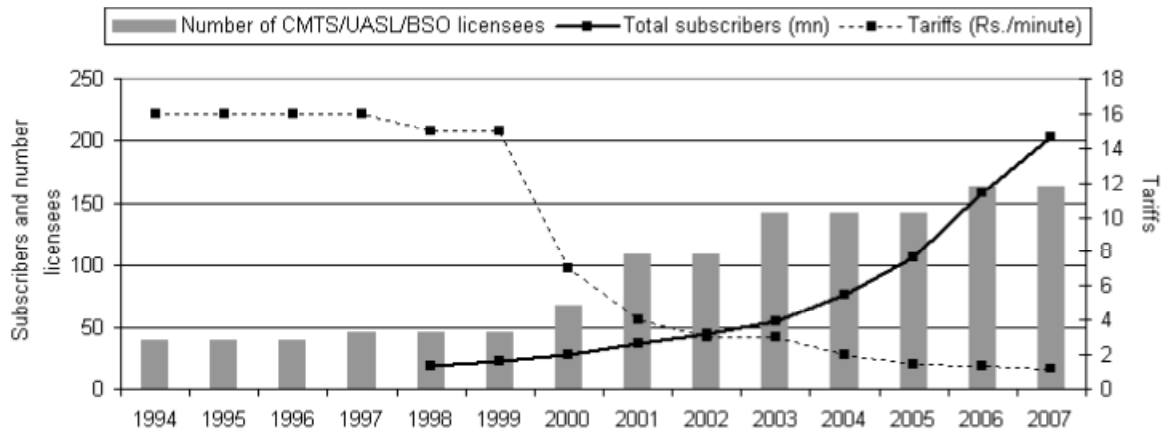


Figure 1: The market has benefited from competition"

2.6.5 The 2007 recommendations of TRAI reiterated the relevance of NTP-99 in arriving at its conclusions, and in para 2.13, it was stated that:

*"It is evident from the policy that there is **no intention of placing any artificial cap on the number of access service providers**. Clearly, the underlying theme is to ensure optimality for existing operators so as to provide good quality service but at the same time **it has not barred entry of new operators.**"*

2.6.6 The 2007 recommendations of TRAI included a special section on "Principles of fair competition....", certain relevant paragraphs of which are quoted below:

Para 2.17:

"From the perspective of competition in the market, it is important to ensure that existence of potential competition ensures that competition is sustained. The existence of potential competition is negated when barriers to entry are erected by way of policy. Threat of entry is an important stimulant for competition in the market."

Para 2.18:

"Threat of potential entry may prevent incumbent firms from raising prices above competitive levels. However, if there are significant barriers to entry this threat may be weak or absent. Incumbent operators in such situations are then likely to raise prices and make persistent excess profits without attracting additional competition."

Para 2.19:

"It is clear from the above that ensuring a potential competition in the market would

mean no barrier to entry. Needless to say, competitive market provides the greatest benefits to consumers. Low or nil barriers to entry facilitate a high degree of innovation."

Para 2.27:

"....Empirical evidence suggests that interests of consumers are best served by the forces of market and thus the Authority is convinced that to sustain competition in the market in the long run, it is necessary to ensure that barriers to entry into the market are reduced/removed."

2.6.7 The emphasis placed by TRAI on ensuring competition in the telecommunications sector was validated once again, when DoT accepted TRAI's recommendation against capping the number of UAS licensees in a service area. As a result, while new telecom operators were awarded UAS licenses in 2008, the very same that have been quashed by the SC Judgment.

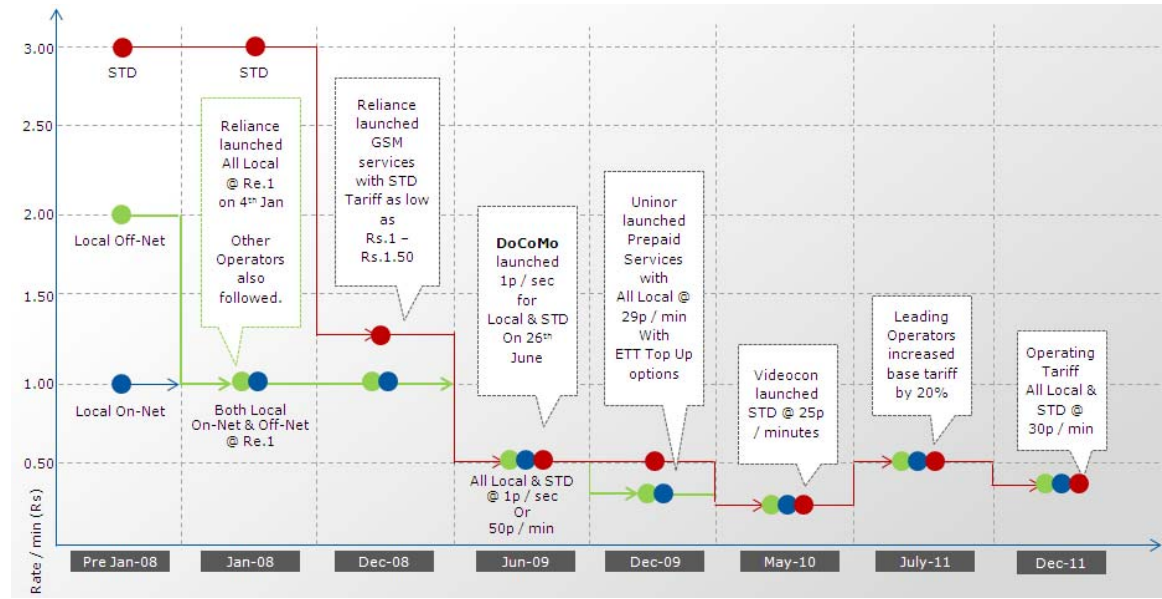
2.6.8 The significant beneficial impact on the Indian mobile users' community made by these new operators is borne out by the detailed statistics provided in the following section on this paper. The same has also been independently recognized by TRAI itself in para 1.20 of its consultation paper on "Review of Policy of Forbearance in Telecom Tariff" released recently on 6th February, 2012:

"After entry of new operators, in the year 2008, the market witnessed competition in the form of reduced tariff, including introduction of innovative tariff plans such as per second billing....."

2.6.9 It would be unfortunate for the consumers if the benefits of the enhanced competition and the resultant consumer affordability, choice and rapid increase in tele-density across remotest areas, were to be permanently reversed by causing the new telecom operators, whose licenses have been quashed by the SC Judgment, to exit. Hence, it is urged that TRAI should evolve, in a timely manner an appropriate, fair and transparent policy framework in compliance with the SC Judgment, which provides a fair opportunity to the licensees whose licenses were quashed by the SC Judgment to continue, in order to sustain the extant vibrant competitive atmosphere.

2.7 Positive Market Implications Resulting From Entry of New Operators

2.7.1 The Indian telecom industry has witnessed a major tariff shift in last 3 years, led by new operators to gain customer and revenue market share. Ultimately it has benefited the customer by affordability and availability.



2.7.2 Operating Tariff Comparison between Delhi and Mumbai and Impact of New Operators

- (i) Launch of services by new operators in fast growing Indian telecom market, has resulted into a huge saving for the customers, both for obtaining a new connection & in terms of the running cost.
- (ii) Comparison of two Metro Circles, Mumbai & Delhi:
 - (a) Number of Operators – 9 in Delhi vs. 12 in Mumbai – Uninor not operational in Delhi; and
 - (b) In Mumbai, new operators like Uninor, Videocon & Tata DoCoMo are actively competing and acquiring new customers, whereas in Delhi, the effective competition is only between pre-2008 operators.
- (iii) As per available information, operating tariff in Mumbai is more than 50 % lower than Delhi on account of innovative and aggressive offering by new operators

Delhi Vs Mumbai		Delhi		Mumbai	
Product Benchmarking		Incumbent 1	Incumbent 2	Incumbent 1	Incumbent 2
New Connection		Rs.80 (Talktime Rs.90)	Rs.80 (Talktime Rs.90)	Rs.5 (Talktime Rs.30)	Rs.50 (Talktime Rs.95)
Operating Tariff	On Net Tariff	60p/min 1.2p/sec	60p/min 1.2p/sec	10p/min	10p/min
	Off Net Tariff	60p/min 1.2p/Sec	60p/min 1.2p/sec	30p/min	30p/min
	STD Tariff	40p/min	60p/min 1.2p/sec	30p/min	30p/min
Talktime	Smallest FTT	Rs.51	Rs.351	Rs.10	Rs.33
TT in Rs.10	TT in Rs.10	Rs.7	Rs.6.07	Rs.10	Rs.6

- (iv) The industry has already witnessed concerted efforts by large operators to block smaller competitors. For example, the incumbent operators have offered extremely low on-net tariffs to their own consumers where we have seen clear sign of both margin squeeze and below cost on-net selling. In absence of the spectrum / network effect advantages, as available to the incumbents, the smaller operators faced a clear competitive barrier in the market. We note that TRAI's recent recommendation to reduce interconnect rates will help address this issue in a big way.
- (v) As brought out in the above submissions, the safeguarding of competition should be the focal point while designing the structure and strategy for the 2G auctions, such that the process of issuance of fresh licenses and spectrum is carried out in a prudent, transparent and time-efficient manner.

2.8 Global Examples of Competitive Safeguards in auctions (as quoted by TRAI in the Consultation Paper)

2.8.1 TRAI, has in this consultation paper, given several examples of the global experience in spectrum auction. **A common thread running through several of these international examples is the recognition by global regulators and telecom authorities of the objective of promoting and safeguarding competition while formulating auction strategies.** These safeguards can take the form of *“Set asides”, “Spectrum Caps”, “Bidding Credits”* for new entrants or smaller players, as noted by TRAI in:

“FCC has used both Spectrum Cap and Set Asides in its spectrum auctions. For the broadband PCS A and B blocks, incumbent cellular carriers were prevented from buying in-region licenses because of a 45MHz spectrum cap. In that auction, FCC also

set aside the Broadband PCS C block for small businesses.”

- 2.8.2 TRAI notes the example of the Danish National IT and Telecom Agency (NITA) which safeguarded against competitive distortion while re-farming the 900 MHz and 1800 MHz spectrum.

“Therefore, there was a fear of distortion of market competition, if the usage of 900 MHz and 1800 MHz bands is liberalised in the hands of incumbent operators. To ensure that the competition in the market for mobile communication was not distorted, NITA decided that it was necessary that the fourth operator also be given access to 900 MHz and 1800 MHz bands.

“In order to prevent potential distortion of competition in the mobile markets concerned, the mobile service providers already holding licenses in the 900 MHz and 1800 MHz frequency bands were excluded from participating in the upcoming auctions”.

- 2.8.3 TRAI also notes examples of Spectrum Caps having been used in the Swedish 800 MHz auction in 2011, where”

“a spectrum cap of 2x10 MHz was laid out”

and Ofcom proposing a cap in the auction of 4G spectrum in the 800MHz and 2.6GHz bands in 2012

“to prevent any one mobile operator holding a disproportionate amount of spectrum”

For the same auction, Ofcom is also considering a set-aside by:

“reserving certain block of frequencies to ensure the entry of fourth operators. Any auctions that do not result in at least four operators winning the minimum amount of spectrum necessary to provide high-quality mobile broadband services would be disregarded”.

3. AUCTION STRUCTURE AND RATIONALE

3.1 Introduction and motivation of proposal for auction design and auction parameters

- 3.1.1 Without prejudice to our position that the policy of the GoI to provide the start-up spectrum of 4.4 MHZ bundled with the UAS licenses has been in public interest and has made telecommunications services affordable to the masses, we support the transition to a market-based regime for spectrum management in India. Worldwide, this transition, and the use of auctions as a spectrum management tool, has been largely motivated by insight from economic theory. Fair and transparent procedures and efficient outcomes promote “welfare” in economical terminology and also foster economic growth. Auctions based on best-practice principles, including measures to

promote or safeguard competition, promote welfare and growth and therefore also the larger public good.

3.1.2 As with almost all previous spectrum auctions worldwide, the primary objectives of the government should indeed be the larger public good in the following sense:

- i. A fair and transparent procedure ensures that the public can be confident that the larger public good has actually been driving auction design and auction-related decisions.
- ii. Efficient outcomes (taking the auction's effect on competition into account) promote welfare and growth directly.
- iii. Maximizing government revenue *insofar compatible with objective (i) and (ii)* makes sense from a public policy perspective and ensures that Indian citizens enjoys the "resource rent" which can be collected without distorting the use of the frequency resources.

3.1.3 In the current situation, the government should be particularly concerned with competition both in the wireless market and in the auction itself. The following issues are important if the government wishes to avoid reduced competition as an unintended consequence of the SC Judgment:

- (i) *Timing*: Delays increase likelihood of new entrants exiting the market prior to the auction. Large operators may have an incentive to attempt to postpone the auction. This would reduce competition in the wireless market but also in the auction itself. Indian businesses and citizens may face higher wireless connectivity prices, less innovation and lower direct auction revenues as a result. In our view, the four month timeline after which the order of the Hon'ble Supreme Court is to be effective was indented to minimize this disruption to the competitive landscape.
- (ii) *Predatory bidding*: It may be rational for the large operators to buy spectrum to reduce competition. New entrants, who *anticipate* that large operators will be allowed to do so, should rationally exit prior to the auction instead of wasting resources in the period leading up to the auction. It is therefore important that measures to safeguard competition are decided upon and incorporated well ahead of the actual auction. The earlier and firmer the government can commit to such safeguards, the less likely it will be that new entrants exit or stay out.
- (iii) *Exposure risks (most prevalent in the frequency dimension)*: New entrants without an existing spectrum portfolio need a minimum amount of spectrum to continue their operation. Large lots are needed to remove this risk.

3.1.4 The most certain way to shield new operators from predatory bidding, and from the *exposure risk described* by TRAI in its Consultation Paper, is to hold a multi-stage auction of spectrum:

- (i) In the primary stage, the cancelled 1800 MHz spectrum should be offered to bidders that were actually, or could have been, eligible for receiving spectrum in 2008 had they applied. Given that on an average in each circle, 4 licenses holding 1800 MHz spectrum have been cancelled by the Hon'ble Supreme Court, a **minimum of two blocks per circle of 6.2 MHz each of the cancelled 1800 MHz spectrum should be made available for auction in the primary stage**. The same rules as the simultaneously ascending e-auction format previously used in India in the 3G auction could be applied directly as long as bidder can buy at most one of these blocks in the primary stage. **The reserve price should be set at the same per MHz level (adjusted for inflation, if**

required) as used in the above mentioned auction of 2.1 GHz 3G spectrum in 2010. We also propose that the winning prices discovered in the primary stage should also be used as reference price for charging of spectrum held by incumbents beyond 4.4 MHz or 6.2 MHz as applicable per government policy.

- (ii) *In the subsequent secondary stage(s), any available 1800 MHz spectrum (subsequent to the primary stage) should be included. All operators, including incumbents and those eligible for the primary stage should be permitted to participate.*

3.1.5 Certain parties may argue that limiting the primary stage to specific entities would be discriminatory, by quoting the clause from the SC judgment which says that the auction process “*does not discriminate between similarly placed private parties*”. We disagree with such an argument. While the SC judgment does stipulate that the auction process shall “*not discriminate between similarly placed private parties*”, the **Hon’ble Supreme Court DOES NOT PRECLUDE safeguards** being made in the case where the **parties are NOT SIMILARY PLACED**. The concerned clause is quoted below:

“the doctrine of equality, which emerges from the concepts of justice and fairness, must guide the State in determining the actual mechanism for distribution of natural resources”.....”demands that the procedure adopted for distribution is just, non-arbitrary and transparent and that it *does not discriminate between similarly placed private parties*”. (Para 69).

Clearly, the licensees impacted by the SC Judgment and the incumbents are not “similarly placed”.

3.1.6 Additionally, to enable new operators to direct their available capital towards the expansion of networks and services, a deferred payment schedule for approved bid price of spectrum won in the auction. Such arrangements have been employed globally. It may be noted for the record, that in the Indian context also, for the first two circle licenses in 1998, the entry fee structure was designed for payment via annual installments adding up to bid price. We propose that 25% of the winning bid price in the auction be payable up-front soon after the auction. The remaining 75% should be payable in equal installments over 10 years subject to interest at SBI’s Prime Lending Rate + 1%.

3.1.7 The 900 and 1800 MHz bands will be most profitably used for GSM for a considerable period of time. Our position is therefore that liberalization needs not be implemented prior to the auction. Furthermore, re-farming should be market-based and follow liberalization and the introduction of spectrum trading. The Government’s role should primarily be to reduce transaction costs and to address market failure, either by facilitating voluntary re-farming or, as a last resort, by intervening directly if market mechanisms fail.

3.1.8 In the event, the private respondents who face the prospect of the cancellation of their UAS licenses pursuant to the Judgment win the bid in a service area by entry fees already paid by along with interest should be adjustable along with the bid amount. Conversely, such private

respondents who are unsuccessful in the auction process should be entitled to a refund of the entry fees already paid by them along with interest.

3.2 **Setting spectrum auction reserve prices**

3.2.1 In auction theory, reservation (or “*reserve*”) prices are discussed as tools to maximize revenue to the seller, and are therefore the solution to an optimization problem. Reserve prices that are too high or too low generate less revenue than optimal prices.

3.2.2 In practical auction settings, reservation prices are set based on a trade-off between the risk of unsold spectrum and the risk of creating incentives for collusion among bidders. It is based on some rough assessment or estimate of bidders’ valuation.

3.2.3 Unsold spectrum is unfortunate for the seller for several reasons:

- Efficiency and the larger public good require all available spectrum to be sold and used.
- Unsold spectrum undermines the legitimacy of auction prices since setting high reserve prices is equivalent to creating artificial spectrum scarcity by holding back spectrum.
- Future attempt to sell unsold spectrum at a lower price might be challenged legally or administratively by successful bidders who paid more in the first auction.

3.2.4 High reserve prices (or the creation of “artificial scarcity” by holding back spectrum) also *introduce uncertainty*: Bidders must decide whether they should and wait until prices go down (or additional spectrum is offered for sale) or whether they should buy immediately¹, possibly at inflated prices.

3.2.5 Low reserve prices create incentives for *collusion*: Bidders would potentially gain a lot if they are able to avoid bidding aggressively against each other, but rather bid for e.g. a “fair share” of the available spectrum. Low prices are unfortunate from a revenue point of view, but also for those concerned with the political legitimacy of the auction procedure: The public opinion may conclude that the “taxpayers” resources have been squandered away if prices are low.

3.2.6 Spectrum scarcity is decreasing as governments are succeeding with freeing up more frequencies for the wireless sector. Technology performance is improving, allowing the transfer of more data per Hz and thereby reduces spectrum value further because improved technology is equivalent to price reduction of a substitute for spectrum (one needs fewer towers to make up for the loss of a MHz). Increased competition in the markets for wireless services reduces expected profits, and, to the extent expected profits drive spectrum valuation, also bidders’ willingness to pay for spectrum.

3.2.7 In some recent auctions, spectrum has been left unsold, indicating that governments have over-estimated the value of spectrum. A possible explanation is that “benchmarks”, such as prices in previous auctions, are used to estimate future prices. If the trend is that spectrum value (measured

¹ The academic literature on “*the Coase Conjecture*” discusses this situation implicitly.

on a per MHz level) is declining, then such benchmarking will have a tendency to overshoot and to result in value estimates that are too high.

- 3.2.8 Keeping in mind, the above principles, and also to ensure a timely procedure we have proposed that the reserve price for the first stage of the auction should be set at the similar per MHz level (adjusted for inflation, if required) as used in the above mentioned auction of 2.1 GHz 3G spectrum in 2010.

4. OTHER IMPORTANT ISSUES

4.1 Rollout Obligations:

In order to ensure a level playing field, the new license and spectrum that may be given through the auction should not have roll out obligations different from the roll-out obligations already in place.

4.2 Validity of Spectrum

The period of validity of the spectrum and license should be 20 years as proposed in the Draft Unified License consultation.

4.3 Spectrum Sharing and Trading, Spectrum Re-farming, Allocation of 700 MHz

As previously stated, the present consultation should focus on the recommendations for the allocation of spectrum by auction as outlined in the SC Judgment.

5. Response to individual Questions 1-36.

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?

AND

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

Response. We list the various principles and key objectives to be borne in mind:

- *To be in the public interest:* An auction which promotes the continuance of the competition being offered by the operators impacted by the SC Judgment would meet this objective.
- *To ensure competition:* As above
- *To be equitable and non-discriminatory between similarly placed parties:* For example, the operators impacted by the SC Judgment and those eligible applicants that were not allotted licenses in 2007/08 would be similarly placed, but not those who held UASL / CMTS licenses at that time.
- *Procedure to be just, non-arbitrary and transparent:* It would be achieved by DoT issuing a detailed Information Memorandum in advance (which includes the spectrum inventory), and structuring the auction in a manner that ensures non-collusion amongst bidders.

Q3. What should be the amount of spectrum which should be auctioned?

Response. The SC Judgment is directed towards rectifying a wrong done in 2007/08. In doing so, it has cancelled 101 licenses holding 1800 MHz GSM spectrum, issued at that time and has ordered fresh auctions for the licenses and spectrum. The cancellation of the above licenses will release 413.6 MHz in 1800 MHz band across the 22 circles (Table 1.2 Page 9 of the CP). Given that on an average in each circle, 4 licenses holding 1800 MHz spectrum have been cancelled by the Hon'ble Supreme Court, a **minimum of two blocks per circle of 6.2 MHz of the cancelled 1800 MHz spectrum should be made available for auction in the first stage** our two stage auction proposal as described in our response to Q.14.

The above approach would still allow a significant chunk of the cancelled spectrum (50% or more in many circles) to be released in the second (open) stage of the auction.

Q4. Should the spectrum be liberalised before it is put to auction?

Response. The SC Judgment specifically orders auction of 2G spectrum. Therefore, any attempt of liberalization of the above mentioned spectrum would not be compliant with the SC order. Additionally, it would lead to delays associated with the complicated nature of the exercise and possible legal challenges.

Q5. For the refarming of 800 and 900 MHz bands from the existing licensees, which of the three options given above should be adopted? Please elaborate with full justification.

AND

Q6. What are the issues that may arise in the above mentioned refarming process?

AND

Q7. For new technologies e.g. UMTS/LTE, 5 MHz is the minimum amount of spectrum required. Certain licensees have only 4.4 MHz spectrum in 900 MHz band and 2.5 MHz spectrum in 800 MHz band. What are the possible options in case of such licensees?

AND

Q8. Some GSM spectrum allocations may be interleaved between operators; to avoid fragmentation, reconfiguration between operators may be required. Whether frequency reconfiguration is required and what are the challenges and possible solutions?

AND

Q9. Should the refarming of spectrum in 800/900 MHz bands be dealt independently or should a comprehensive approach be adopted linking it with the availability and auctioning of 700 MHz band?

AND

Q10. Which of the two approaches outlined above be adopted?

AND

Q11. When should 700 MHz spectrum be auctioned?

AND

Q12. Should the auction in 700 MHz band be linked with the granting permission for the liberalised use of 800/900 MHz band?

AND

Q13. How much spectrum in 700 MHz band should be put to auction initially and what should be the amount of spectrum which a licensee should be allowed to win in that auction?

Response (to Q5 – Q13). The re-farming of 800 and 900 MHz and allocation of spectrum in the 700 MHz band should be part of separate consultation process *after* the auction of the 2G spectrum as mandated by the SC Judgment. This will give all relevant parties the opportunity to fully contemplate and evaluate the most optimum solution to these very fundamental issues. For the sake of time, consumer interest and maintaining the competitive landscape we would argue that the process should strictly comply with the above referenced judgment and not have a broader scope.

Q14. What should be the structure of the auction process?

Response. We propose a multi-stage auction procedure.

In the primary stage, the cancelled 1800 MHz spectrum should be offered to bidders that were actually, or could have been, eligible for receiving spectrum in 2008 had they applied. Given that on an average in each circle, 4 licenses holding 1800 MHz spectrum have been cancelled by the Hon'ble Supreme Court, a minimum of two blocks per circle of 6.2 MHz each of the cancelled 1800 MHz spectrum should be made available for auction in the primary stage. To ensure a timely procedure within the deadline we propose that in the primary stage, the simultaneously ascending e-auction design, which has been previously successful in India in the recent 3G auctions, be used. The reserve price should be set at the same per MHz level (adjusted for inflation, if required) as used in the above mentioned auction of 2.1 GHz 3G spectrum. We also propose that the winning prices discovered in the primary stage should also be used as reference price for charging of spectrum held by incumbents beyond 4.4 MHz or 6.2 MHz as applicable per government policy.

In the subsequent secondary stage(s), all available 1800 MHz spectrum (subsequent to Stage 1) should be included. All operators, including incumbents and those eligible for the primary stage should be permitted to participate.

Q15. Should auction be held in single stage or multi stage?

Response. We propose a multi-stage auction procedure as outlined in our response to Q14 above.

Q16. Should there be a simultaneous auction for spectrum in 800 and 1800 MHz bands?

Response. The bands are not strong substitutes and auctioning them simultaneously will increase the complexity of the procedure. The interrelation between the 850 MHz band and the 1800 MHz band is weak but it is probably not zero. Conventional wisdom suggests that in such cases, the most valuable of the interrelated goods should be sold first. We therefore propose that 1800 MHz be auctioned first, with 850 MHz quickly afterwards.

Q17. What should be the block size of the spectrum?

Response. As per our proposal of a multi stage auction, for the primary stage of the auction of 1800 MHz spectrum, the block size should be 6.2 MHz. (Please refer to our response to Q.14 above). For the subsequent secondary stage(s), blocks of 1 MHz may be considered.

Q18. Should the block size be dependent on the frequency? If so, what should be the block size in each band?

Response. For the primary stage of 1800 MHz auction, as per our proposal, the block size should be 6.2 MHz.

Q19. Should there be a cap on amount of spectrum one can bid? If so, what should it be?

Response. For the primary stage of 1800 MHz auction, as per our proposal, the bidder can bid for only one spectrum block of 6.2 MHz in each circle.

Q20. Should there be a separate cap on the total amount of spectrum one can hold; if so, what amount should it be?

Response. In the Press Release of 15 February 2012 by the Hon'ble MOC a cap of 25% of the total assigned spectrum in a circle has already been announced: "*....., the total spectrum held by the Resultant entity shall not exceed 25% of the spectrum assigned, by way of auction or otherwise, in the concerned service area in case of 900 and 1800 MHz bands*"

Q21. Should there be a cap on the amount of spectrum one can hold in respect of sub-GHz spectrum? If so, what should it be?

Response. This should be a part of the scope of a consultation on re-farming, which should be held at a later stage.

Q22. Who all should be eligible to participate in the auction?

e. Only licensees whose licences have been cancelled;

f. Only eligible applicants as on 10.01.2008;

g. Only licensees whose licences have been cancelled and all new eligible entrants at the time of auction; or

h. Open to all including the existing Licensees.

Response. In our view **Option (g)** is the only one which fully complies with the SC Judgment and therefore in our proposed multi stage auction, in the primary stage only those applicants who were, or would have been eligible for license and spectrum in 2008 had they applied should be allowed to participate. In the subsequent secondary stage(s), all operators, including incumbents and those eligible for the primary stage should be permitted to participate.

It is to be noted that eligibility for licenses and the consequent spectrum allocation in 2008 was restricted to fresh applicants only. . In the current case, the Supreme Court has effectively stepped back to 2008 and, without requiring any change to the eligibility criteria, has held that:

- The first-come-first-served policy used by DoT in 2008 was flawed.
- The method of selection of successful licensees by fixing a certain cut-off date was arbitrary.

To correct the above situation the Supreme Court has ordered that “*TRAI shall make fresh recommendations for grant of license and allocation of spectrum in 2G band ...*”, In recognizing that those eligible applicants below the cut-off date were unfairly treated, the Supreme Court has said the procedure adopted for distribution should be just, non-arbitrary and transparent and that it should not discriminate between similarly placed private parties. The spirit and letter obviously is to ensure that all the then eligible parties should have been treated at par while selecting the successful licensees.

From the above, it is evident that the SC Judgment did not intend that the auction of 2G licenses and spectrum should also be open to parties, who, in 2007/2008 already held UASL / CMTS licensees.

Q23. What should be reserve price per MHz of spectrum in the year 2012 for 1800 MHz band?

Response. In the interest of simplicity and timeliness, we are recommending that the most recent used reserve price be applied. Therefore, for the primary stage of the auction, the reserve price should be set at the same per MHz level (adjusted for inflation, if required) as used in auction of 2.1 GHz 3G spectrum in 2010.

Q24. What should be the reserve price per MHz of spectrum in the 700/800/900 MHz bands.

Response. To be addressed in later consultations.

Q25. Whether the reserve price should be uniform across the country or service area wise?

Response. For convenience, for the primary stage of the auction, the reserve prize for each service area should be the same on a per MHz basis (adjusted for inflation, if required) as used in auction of 2.1 GHz 3G spectrum in 2010.

Q26. What should be the roll out obligations linked to the auctioned spectrum?

Response. In order to ensure a level playing field, the new license and spectrum that may be given through the auction should not have roll out obligations different from the roll-out obligations already in place.

Q27. What should be the annual spectrum usage charge for the spectrum being auctioned?

AND

Q28. Should the spectrum usage charge be in line with present criteria of escalating charge with the amount of spectrum holding or a fix percentage as was done for 3G and BWA spectrum?

Response. Since the licensees impacted by the SC Judgment would now be paying a market determined price for the spectrum, we believe that in principle the annual spectrum usage charge should be limited an amount to offset the cost of management of the spectrum by WPC.

Q29. What should be the period of validity of spectrum?

Response. The period of validity of the spectrum and license should be 20 years as proposed in the Draft Unified License consultation.

Q30. What should be the period of price of spectrum?

Response. The meaning of the question is not clear to us.

Q31. Should the government allow deferred payment schedule of the spectrum auction fee, or should the payment be upfront in nature?

Response. To enable new operators to direct their available capital towards the expansion of networks and services, a deferred payment schedule for approved bid price of spectrum won in the auction. Such arrangements have been employed globally. It may be noted for the record, that in the Indian context also, for the first two circle licenses in 1998, the entry fee structure was designed for payment via annual installments adding up to bid price. We propose that 25% of the winning bid price in the auction be payable up-front soon after the auction. The remaining 75% should be payable in equal installments over 10 years subject to interest at SBI's Prime Lending Rate + 1%.

Q32. Should Spectrum trading be allowed in India?

AND

Q33. (a) Among the various models discussed above, in your opinion which model of spectrum trading is best suited for India?

(b) In your opinion is there any other model which can be implemented in India? If yes, please describe.

AND

Q34. What should be the eligibility criteria to trade the spectrum?

AND

Q35. Whether the spectrum assigned for 3G and BWA services be allowed to trade? If yes, give reasons.

Response to (Q32-35). The policy statement of the Hon'ble MOC dated 15 February 2012 has already indicated that: "*Spectrum trading will not be allowed in India, at this stage. This will be re-examined at a later date.*"

Q36. Can spectrum be allowed to be mortgaged for raising capital for telecom purposes?

Response: The mechanism of the tripartite agreement between DoT, licensee and lender has worked smoothly in facilitating capital for the business. Therefore, a similar mechanism which allows spectrum to be used as collateral for bank borrowing is very essential for the health of the industry.

Corrigendum

To,

*Shri. Sudhir Gupta,
Principal Advisor (MS),
Telecom Regulatory Authority of India,
Mahanagar Door Sanchar Bhawan,
Jawahar Lal Nehru Marg (Old Minto Road), New Delhi-110002.*

Subject: Response to Consultation Paper on “Auction of Spectrum”

Respected Sir,

This is with reference to, our submission to TRAI’s Consultation Paper on “Auction of Spectrum” dated 7th March, 2012.

In our response to Q.31 :

“Should the government allow deferred payment schedule of the spectrum auction fee, or should the payment be upfront in nature?”

We have responded:

*“ We propose that 25% of the winning bid price in the auction be payable up-front soon after the auction. The remaining 75% should be payable in equal installments over 10 years subject to interest at **SBI’s Prime Lending Rate + 1%**”*

We, however note, that the Reserve Bank of India, through a guideline issued on April 9, 2010, has stated that “The Base Rate system will replace the BPLR system with effect from July 1, 2010” . BPLR, here refers to the benchmark prime lending rate. A copy of the said guideline is attached here.

*We, therefore submit, that the phrase “**SBI’s base rate + 1%**” should replace “**SBI’s Prime Lending Rate + 1%**” in our response to Q.31, and all references elsewhere in our submission on the same Q.31.*

Thanking you

With kind regards

Subodh K. Singh
a telenor unitech company



भारतीय रिज़र्व बैंक

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April 9, 2010

All Scheduled Commercial Banks (excluding RRBs)

Dear Sir/Madam

Guidelines on the Base Rate

Following the announcement in the Annual Policy Statement for the year 2009-10, Reserve Bank of India constituted a Working Group on Benchmark Prime Lending Rate (Chairman: Shri Deepak Mohanty) to review the present benchmark prime lending rate (BPLR) system and suggest changes to make credit pricing more transparent. The Working Group submitted its report in October 2009 and the same was placed on the Reserve Bank's website for public comments. Based on the recommendations of the Group and the suggestions from various stakeholders, the draft guidelines on Base Rate were placed on the Reserve Bank's website in February 2010.

2. In the light of the comments/suggestions received, it has been decided that banks switch over to the system of Base Rate. The BPLR system, introduced in 2003, fell short of its original objective of bringing transparency to lending rates. This was mainly because under the BPLR system, banks could lend below BPLR. For the same reason, it was also difficult to assess the transmission of policy rates of the Reserve Bank to lending rates of banks. The Base Rate system is aimed at enhancing transparency in lending rates of banks and enabling better assessment of transmission of monetary policy. Accordingly, the following guidelines are issued for implementation by banks.

बैंकिंग परिपालन और विकास विभाग, केन्द्रीय कार्यालय, सेन्टर 1, कफ परेड, कोलाबा, मुंबई - 400005

Department of Banking Operations and Development, Central Office, Centre 1, Cuffe Parade, Colaba, Mumbai - 400005

टेलिफोन /Tel No: 91-22-22189131 फैक्स/Fax No: 91-22-22183785 Email ID:cgmicdbodco@rbi.org.in

हिन्दी आसान है, इसका प्रयोग बाहिए

Base Rate

- i. The Base Rate system will replace the BPLR system with effect from July 1, 2010. Base Rate shall include all those elements of the lending rates that are common across all categories of borrowers. Banks may choose any benchmark to arrive at the Base Rate for a specific tenor that may be disclosed transparently. An illustration for computing the Base Rate is set out in the **Annex**. Banks are free to use any other methodology, as considered appropriate, provided it is consistent and is made available for supervisory review/scrutiny, as and when required.
- ii. Banks may determine their actual lending rates on loans and advances with reference to the Base Rate and by including such other customer specific charges as considered appropriate.
- iii. In order to give banks some time to stabilize the system of Base Rate calculation, banks are permitted to change the benchmark and methodology any time during the initial six month period i.e. end-December 2010.
- iv. The actual lending rates charged may be transparent and consistent and be made available for supervisory review/scrutiny, as and when required.

Applicability of Base Rate

- v. All categories of loans should henceforth be priced only with reference to the Base Rate. However, the following categories of loans could be priced **without** reference to the Base Rate: (a) DRI advances (b) loans to banks' own employees (c) loans to banks' depositors against their own deposits.
- vi. The Base Rate could also serve as the reference benchmark rate for floating rate loan products, apart from external market benchmark rates. The floating interest rate based on external benchmarks should, however, be equal to or above the Base Rate at the time of sanction or renewal.
- vii. Changes in the Base Rate shall be applicable in respect of all existing loans linked to the Base Rate, in a transparent and non-discriminatory manner.
- viii. Since the Base Rate will be the minimum rate for all loans, banks are not permitted to resort to any lending below the Base Rate. Accordingly, the current stipulation of BPLR as the ceiling rate for loans up to Rs. 2 lakh stands withdrawn. It is expected that the above deregulation of lending rate will

increase the credit flow to small borrowers at reasonable rate and direct bank finance will provide effective competition to other forms of high cost credit.

- ix. Reserve Bank of India will separately announce the stipulation for export credit.

Review of Base Rate

- x. Banks are required to review the Base Rate at least once in a quarter with the approval of the Board or the Asset Liability Management Committees (ALCOs) as per the bank's practice. Since transparency in the pricing of lending products has been a key objective, banks are required to exhibit the information on their Base Rate at all branches and also on their websites. Changes in the Base Rate should also be conveyed to the general public from time to time through appropriate channels. Banks are required to provide information on the actual minimum and maximum lending rates to the Reserve Bank on a quarterly basis, as hitherto.

Transitional issues

- xi. The Base Rate system would be applicable for all new loans and for those old loans that come up for renewal. Existing loans based on the BPLR system may run till their maturity. In case existing borrowers want to switch to the new system, before expiry of the existing contracts, an option may be given to them, on mutually agreed terms. Banks, however, should not charge any fee for such switch-over.
- xii. In line with the above Guidelines, banks may announce their Base Rates after seeking approval from their respective ALCOs/ Boards.

Effective date

- xiii. The above guidelines on the Base Rate system will become effective on July 1, 2010.

Yours faithfully

(P.Vijaya Bhaskar)
Chief General Manager-in-charge
Encl: as above

Illustrative Methodology for the Computation of the Base Rate

$$\text{Base Rate} = a + b + c + d$$

a - Cost of Deposits/funds = D_{cost}

(benchmark)

$$b - \text{Negative Carry on CRR and SLR} = \left[\left[\frac{\{D_{cost} - (SLR * T_r)\}}{\{1 - (CRR + SLR)\}} \right] * 100 \right] - D_{cost}$$

$$c - \text{Unallocatable Overhead Cost} = \left(\frac{U_c}{D_{ply}} \right) * 100$$

$$d - \text{Average Return on Net Worth} = \left[\left(\frac{NP}{NW} \right) * \left(\frac{NW}{D_{ply}} \right) \right] * 100$$

Where:

D_{cost} : Cost of Deposits/funds

D : Total Deposits = Time Deposits + Current Deposits + Saving Deposits

D_{ply} : Deployable Deposits

= Total deposits less share of deposits locked as CRR and SLR balances, *i. e.*

= $D * [1 - (CRR + SLR)]$

CRR : Cash Reserve Ratio

SLR : Statutory Liquidity Ratio

T_r : 364 T-Bill Rate

U_c : Unallocatable Overhead Cost

NP : Net Profit

NW : Net Worth = Capital + Free Reserves

Negative Carry on CRR and SLR

$$\text{Negative Carry on CRR and SLR} = \left[\left[\frac{\{D_{cost} - (SLR * T_r)\}}{\{1 - (CRR + SLR)\}} \right] * 100 \right] - D_{cost}$$

Negative carry on CRR and SLR balances arises because the return on CRR balances is nil, while the return on SLR balances (proxied using the 364-day Treasury Bill rate) is lower than the cost of deposits. Negative carry on CRR and SLR is arrived at in three steps. In the first step, return on SLR investment was calculated using 364-day Treasury Bills. In the second step, effective cost was calculated by taking the ratio (expressed as a percentage) of cost of deposits (adjusted for return on SLR investment) and deployable deposits (total deposits less the deposits locked as CRR and SLR balances). In the third step, negative carry cost on SLR and CRR was arrived at by taking the difference between the effective cost and the cost of deposits.

Unallocatable Overhead Cost

$$\text{Unallocatable Overhead Cost} = \left(\frac{U_c}{D_{ply}} \right) * 100$$

Unallocatable Overhead Cost is calculated by taking the ratio (expressed as a percentage) of unallocated overhead cost and deployable deposits.

Average Return on Net Worth

$$\text{Average Return on Net Worth} = \left[\left(\frac{NP}{NW} \right) * \left(\frac{NW}{D_{ply}} \right) \right] * 100$$

Average Return on Net Worth is computed as the product of net profit to net worth ratio and net worth to deployable deposits ratio expressed as a percentage.