Bharti Airtel Response to the draft Telecommunication (B&C) service (Fourth) (Addressable systems) Tariff (Second Amendment) Order

1. Introduction:

- TRAI vide the Telecommunication (B&CS) Services (Fourth) (Addressable Systems) Tariff order 2010, dated 21 July 2010 mandated a-la-carte offering of channels in addressable system, throughout the territory in India. However, TRAI vide the same order did not prescribe any cap/ceiling on the pricing of a-la-carte channels and left it to market forces. Further, TRAI introduced a retail price regulation on a-la-carte channels in the form of twin conditions vide first amendment order dated 30th April 2012. The DTH industry expressed its concerns regarding implementation of twin conditions at retail level. Subsequently, TRAI issued a consultation paper dated 20th December 2012 which suggested revised twin conditions. The twin conditions in the current draft amendment dated 4th June 2013 is similar to the earlier proposal of TRAI and the concerns /suggestions made by the DTH players have not been given due consideration.

- Today the choice of bouquets and channels lie with the consumer. There are multiple choices available in the form of bouquets and a-la-carte channels for consumers at one of the lowest tariffs across the global DTH industry. DTH industry currently offers a plethora of channels at an average low price point of Rs. 220- per month and operators offer very innovative packages to suit the various customer needs on a national level. **Therefore the retail tariffs if forborne would continue to fuel the growth of DTH industry in India.**

- In view of above, it is submitted that **the retail tariffs should be left to forbearance.** Any implementation of retail tariff ceiling in the form of twin conditions will put an additional financial burden on the beleaguered DTH Industry.

2. Present DTH Industry:

- DTH platform provides a national digital footprint for television signals. The DTH services market is very competitive with 6 operators and 55 million subscribers, in addition to direct competition from other platforms like Cable TV and IPTV operators. DTH operators have altogether invested between INR 22,000-23,000 crores over the past six-seven years. Major costs for a DTH operator include satellite bandwidth, Head-end, technology platform, national sales & distribution network, installation, servicing logistics, broadcasters/content fees, customer care, license fees, applicable customs duty and high taxes. Currently, **DTH is burdened by an arduous tax regime to the tune of approx. 35% which includes licence fee (10%), service tax (12.36%) and average entertainment tax (11%).** The entertainment tax varies from state to state and is as high as 30% (GR based) in Tamilnadu. Moreover, there are states which charges entertainment tax in the range of Rs. 5- Rs. 50 per subscriber, which is absorbed by DTH operators, leading to deteriorate their profit margins. We are enclosing state wise entertainment Tax **(Annexure-1)** for the kind reference of the Authority.

- Additionally, there is a huge capital deployed by the DTH operators at the start of the business and non- recovery of above stated costs will make the survival of the DTH business difficult/unviable.

We believe that the proposed tariff order prescribing 'Twin Conditions' for a-la-carte rate pricing of the channels, threatens to put additional financial liabilities upon DTH operators impacting their margins while impeding their growth.

3. <u>**Key issues w.r.t. implementation of 'TWIN Conditions':**</u>

- **Proposed TWIN Conditions for the a-la-carte pricing of channels:**

  a. The a-la-carte rates of pay channels forming part of bouquet(s) shall not exceed two times the a-la-carte rate of the channel offered by the broadcaster at wholesale level for addressable systems; (*Will be termed as Rule1 in this response)*
  b. The a-la-carte rate of a pay channel forming part of bouquet shall not exceed three times the ascribed value of the pay channel in the bouquet. (*Will be termed as Rule 2 in this response)*

  The implementation of this order is fraught with several issues and challenges, thus making it impossible to implement. A detailed rationale is below for the kind consideration of the Authority:

3.1 **Retail price protection should commensurate with wholesale price protection:**

- For DTH operators implementing prices based on twin conditions will require restructuring the pricing and channel composition of bouquets consisting of channels offered by various broadcasters to bring them in line with the ceilings proposed, that too without any control over broadcasters' pricing. Also subscriber numbers of a bouquet containing hundred(s) of channels could depend on a variety of genres and channels; hence, ascribing a value to pay channels should be free of dependence on other channels. To elaborate, since a channel may be placed in more than one bouquet and also it may be added or deleted from the bouquet frequently, therefore, ascribing a value to pay channel would lead to the frequent changes in the bouquet prices/A-la-carte prices.

- Assuming that the TWIN conditions be applied dynamically and a service provider carries out changes or need to recalibrate both in prices and compilation of bouquet, but the DTH (QoS) Regulation of 2007 prohibits the operators to make the changes in the composition of package during first six months of enrolment . This anomaly has not been addressed by the Regulation.

- Thus, to overcome the above issue as a one-time exercise, the DTH operators should be allowed to recalibrate their pricing and compilation of **bouquet without any restriction from the 6 month tariff protection Regulation**.

- Additionally, since the prices of a pay channels are fixed by broadcasters and any change in price of a channel will require DTH Operator to recalibrate all subscription packs/bouquets. Hence, this exercise will have to be repeated with the frequency of change in broadcasters' wholesale RIO rates. The interconnection regulation allows a broadcaster to change their tariffs with a prior notice of 21 days. We therefore request that **Retail price protection should be reduced to 21 days to match the wholesale price protection regulation.**

- **In view of the above, <u>concept of ascribed value is neither practical nor viable and should not be taken into consideration while arriving at retail rate on a-la-carte basis</u>.**

3.2 **A-la-carte price will be lower than the wholesale a-la-carte prices**

- The tariff order has regulated the pricing of retail tariff of a channel in a bouquet by imposing the twin conditions. It is significant to highlight that the application of these conditions shall result in a-la-carte pricing of channel to fall significantly below the wholesale rate of the broadcaster for the said channel. With reduced prices many channels will become unviable for the operators to offer. Some of the channels wherein the final a-la-carte price will be lower than the wholesale RIO rate are as below:

Channel	DTH RIO rate (Rs)	Rule 1 Pricing (Rs)	Rule 2 Pricing (Rs)	New Pricing (Rs
Jaya TV	3.8	7.56	2.4	2.4
Maa Movies	7.8	15.5	7.6	7.6
Sarthak TV	4.0	7.9	3.2	3.2

- Table above shows that the final a-la-carte price of a channel determined by the TWIN conditions is lower than the DTH RIO rate offered by the Broadcaster. Thus implementation of TWIN conditions will result in a situation wherein DTH operators would have no choice but to remove the below cost channels from the bouquet. This will not be a consumer friendly move. But expecting DTH operators to offer below cost does not make economic sense and is against the TRAI own stated principle/position of cost based regime.

3.3 **Rule 1 threshold too low for business sustainability:**

- Rule 1 allows a DTH operator to offer a pack or channels at max 2 times the RIO rates. So, if a DTH operator is buying content at a cost of Rs. 100 from the broadcaster, it will be allowed to offer that content at max Rs. 200, out of which 33% (i.e, Rs. 66) will be the applicable taxes/duties. That means DTH operator is left with only Rs. 34 (after deducting content cost and taxes, from the total earning of Rs. 200) or gross margin of only 15-20% (Rs. 34 divided by Rs. 200) from which it has to bear the operating cost of over 25%(incl. S&D, manpower, network and customer service cost) etc. thereby leading to **<u>negative operating margin of approx. 10%.</u> This will threaten the survival of the DTH businesses.**

- In view of the above, there should not be any ceiling on a-la-carte pricing/Rental of the channels. However still in case Authority wishes to stipulate some conditions, then the Authority may mandate that **<u>the channel in a-la-carte offering by the platform should not be priced more than 'three times' the wholesale RIO Rates offered by the broadcasters.</u>**

3.4 **Rule 2 (Ascribed condition) will override, making Rule 1(2* RIO rate) redundant in most cases:**

- TRAI has mentioned in the draft order that the Rule 1 and Rule 2 will give enough head room to the operators to price their channels accordingly. However it is not the fact, our estimate/calculations shows that in almost 55-60% of the cases Rule 2 will override the Rule 1 thereby making the Rule 1 redundant in these cases. To elaborate please refer to **Annex-2** wherein an example of our value sports pack shows how Rule 2 is negating the Rule 1, depriving operators to have any flexibility while packaging the channels. Moreover, average new price of the channels derived using Twin conditions **is only 1.6 times** the RIO rate, whereas Rule 1 gives choices to place the a-la-carte rate at 2 times the RIO rate. Thus, the implementation of Ascribed value will not only take away the flexibility/innovation of pricing the channels from the DTH operators but will also further lower their business margins in comparison to Rule 1.

3.5 **Depriving operators of flexibility in pricing:**

- DTH operators are national players and the impact of these conditions shall deprive DTH operators of the flexibility in pricing currently available with them to compete with the regional players viz. cable operators and therefore the capability to respond to competitive forces at regional market will be lost. On the other hand, most of the cable operators being regional specific players will be benefited in the form of reduced competition. Therefore, the DTH operators shall lose out on regional competing edge in terms of pricing.

3.6 **Impact on customer value proposition:**

This tariff order will adversely impact the consumers since it will require either a substantial change in the DTH subscription packs with the number of channels decreasing or an increase in retail prices. Today, the DTH subscribers enjoy a plethora of channels at an average low price point of Rs. 220/- per month and operators offer very innovative packages to suit the various customer needs on a national level. However, the implementation of this order in the same form will remove the innovative tariff schemes from the market as well as adversely impact the subscribers as the value being delivered today to DTH subscribers will no longer be available on offer.

3.7 **Financial impact of 'TWIN conditions':**

- The proposed Tariff order **by way of TWIN Conditions will impose substantial <u>revenue loss to Airtel DTH business</u>** thereby adding an additional financial burden/negative operating margin to the beleaguered DTH business of the company**.**

- Presently, DTH industry in India is working on one of the lowest ARPU in the world i.e. around $4, whereas the ARPU of other DTH operators worldwide is very high. We are enclosing the ARPU figs prevailing internationally are enclosed as **Annexure-3.**

- Additionally, DTH industry subsidizes CPEs in the range of Rs. 2,200 and Rs. 2,700/- to make them affordable for customers. This subsidy is a substantial cost on DTH industry adding to the accumulated losses mentioned above each year. TRAI has also issued a tariff order on 27th May 2013 prescribing mandatory rental plans or CPE (STB + Dish Antenna) arrived at a below cost value of Rs. 2,250/- per CPE.

- The TWIN conditions will further increase the content costs for us without commensurate returns from retail prices. The Authority is well aware of the present financial state of the DTH industry therefore imposing any such ceiling on retail pricing of channels will make the DTH business unviable for the companies. To exemplify, table below shows the negative trend of Airtel DTH business EBIT (Earnings before interest and tax) margin and operating cash flow for last two years and therefore the implementation of this tariff order will further worsen the financial health of the company.

Description	UOM	FY12	FY13
EBIT	Rs. Mn	(7,198)	(8,105)
EBIT %	%	-55.5%	-49.7%
Operating cash flow	Rs Mn	(7,643)	(7,095)

- Considering the competitive landscape and current financial position of the DTH business, we request TRAI not to regulate **retail tariffs** or put any uneconomic tariff ceilings on channels pricing.

4. **<u>Our request on the issue of twin conditions in the said draft order are as follows:</u>**

- **A-la-carte Retail tariffs should be forborne. Notwithstanding which:**
  - **Rule 1 of the Twin conditions should be increased to "3 times" from "2 times" considering the additional expenditure incurred and the financial burden on DTH operators in serving channel on a la carte basis**.
  - **Rule 2 (Ascribed value) of the Twin conditions are not implementable due to its impact on consumers and financially detrimental impact on DTH operators. Therefore, Rule 2 (ascribed value) should be removed from the proposed 2nd tariff order amendment.**

5. **<u>Response to 'Clause 4' on Minimum Monthly Subscription:</u>**

- TRAI in the Telecommunication (Broadcasting and Cable Services) (Fourth) (Addressable Systems) Tariff order, 2010 had prescribed a minimum monthly subscription of Rs. 150 (excl. of taxes) per month per subscriber, towards channels chosen by the subscriber, either on a-la-carte or bouquet basis. The rationale of Rs 150 was arrived at on the basis of the entry level packs range of Rs 125 - Rs 160 offered by the DTH operators during that period.

- However, over the last 3 years, the cost of providing DTH services has been increased and there is a substantial increase in other costs viz. Call centre, processing cost, bandwidth cost conditional access cost, manpower cost, high content cost offered by the Broadcasters, increase in diesel price, forex fluctuation, inflation etc. thereby increasing financial burden on the beleaguered DTH industry.

Moreover, most of the entry level packs offered by the **DTH operators have also been increased to Rs 220.** **<u>We are therefore of the view that the minimum monthly subscription fee should be increased to Rs. 200 from prescribed Rs 150</u>**.

- Moreover, there should be **<u>annual price escalation in minimum monthly subscription fee</u>**, so that DTH operators would be able to recover the increase in cost due to inflation and other costs escalations

Annexure-1

State wise entertainment Tax:

SL. NO.	STATE ↓	MODE ↓	ENTERTAINMENT TAX (Rs)
1	ASSAM	SUBSCRIBER BASED	25.00
2	CHHATTISGARH	SUBSCRIBER BASED	10.00
	CHHATTISGARH	SUBSCRIBER BASED	20.00
3	DELHI	SUBSCRIBER BASED	20.00
4	GOA	SUBSCRIBER BASED	30.00
5	GUJRAT	SUBSCRIBER BASED	16.67
6	MAH : Mumbai City	SUBSCRIBER BASED	45.00
	MAH : Mumbai Suburban	SUBSCRIBER BASED	45.00
	MAHARASHTRA –REST	SUBSCRIBER BASED	15/30/45
7	UTTRAKHAND	SUBSCRIBER BASED	25.00
	UTTRAKHAND-Commercial	SUBSCRIBER BASED	50.00
8	WEST BENGAL - KOLKATTA	SUBSCRIBER BASED	10.00
	WEST BENGAL - REST	SUBSCRIBER BASED	5.00
9	Nagaland	SUBSCRIBER BASED	10.00
SL. NO.	**STATE ↓**	**MODE ↓**	**ENTERTAINMENT TAX %)**
10	KARNATAKA	REVENUE BASED	6%
11	KERALA	REVENUE BASED	2%
12	PUNJAB	REVENUE BASED	10%
13	UTTAR PRADESH	REVENUE BASED	25%
14	MADHYA PRADESH	REVENUE BASED	20%
15	ORISSA	REVENUE BASED	5%
16	BIHAR	REVENUE BASED	15%
17	TAMIL NADU	REVENUE BASED	30%
18	Jharkhand	REVENUE BASED	10%

- Note: Assam, Chhattisgarh, Delhi, Goa, Gujarat, Maharashtra, Uttrakhand, WB, Nagaland has Rs. per sub based entertainment tax while other states have % of revenue as basis.

Annexure 2

Value sports pack ('Twin conditions' simulation):

	DTH RIO Rate	Rule 1	Rule 2	New Pricing	New price/ RIO Rate
STAR PLUS	7.87	15.73	13.88	13.88	1.76
ZEE TV	5.83	11.66	10.26	10.26	1.76
COLORS	8.99	17.98	13.88	13.88	1.54
SONY	8.99	17.98	10.26	10.26	1.14
SAB TV	6.17	12.35	12.07	12.07	1.95
STAR ONE/Life Ok	9.21	18.43	13.88	13.88	1.51
STAR GOLD	7.42	14.83	7.24	7.24	0.98
Movies Ok	7.14	14.28	9.05	9.05	1.27
UTV HINDI MOVIES/UTV Movies	6.30	12.60	-	-	-
SUVARNA	5.04	10.08	3.62	3.62	0.72
ETV-MARATHI	4.67	9.34	8.45	8.45	1.81
SAHARA ONE	8.61	17.22	7.24	7.24	0.84
Sahara Filmy	6.93	13.86	12.07	12.07	1.74
Jaya TV	3.78	7.56	2.41	2.41	0.64
NDTV India	3.37	6.74	3.62	3.62	1.07
IBN 7	3.15	6.29	3.62	3.62	1.15
History TV 18	6.72	13.44	9.05	9.05	1.35
SONIC	5.46	10.92	9.05	9.05	1.66
ETV - GUJRATI	4.67	9.34	8.45	8.45	1.81
ETV BENGALI	4.67	9.34	8.45	8.45	1.81
HISTORY	1.98	3.96	-	-	-
Jaya Plus	1.68	3.36	2.41	2.41	1.44
ZEE BUSINESS	2.16	4.32	4.22	4.22	1.96
CHANNEL 8	4.20	8.40	6.64	6.64	1.58
ETV-ORIYA	4.67	9.34	8.45	8.45	1.81
Zee Salaam	6.30	12.60	9.05	9.05	1.44
ETV MP	4.67	9.34	8.45	8.45	1.81
ETV UP	4.67	9.34	8.45	8.45	1.81
ETV BIHAR	4.67	9.34	8.45	8.45	1.81
ETV RAJASTHAN	4.67	9.34	8.45	8.45	1.81
ETV-URDHU	4.67	9.34	8.45	8.45	1.81
SET MAX	7.64	15.28	24.14	15.28	2.00
ZEE CINEMA	5.83	11.66	12.07	11.66	2.00
CARTOON NETWORK	5.62	11.23	12.07	11.23	2.00
NICK	2.70	5.39	9.05	5.39	2.00
BINDASS MOVIES/UTV action	4.20	8.40	12.07	8.40	2.00
Zee classic	4.49	8.99	10.26	8.99	2.00
STAR VIJAY	1.80	3.60	3.62	3.60	2.00
BINDASS	4.20	8.40	8.45	8.40	2.00
DISCOVERY	6.74	13.48	13.88	13.48	2.00
AAJ TAK	3.15	6.29	9.05	6.29	2.00
9X MUSIC	2.94	5.88	6.64	5.88	2.00
CHANNEL V	0.45	0.90	9.05	0.90	2.00
NGC	2.58	5.17	6.64	5.17	2.00
ZOOM	3.51	7.01	7.24	7.01	2.00
ZEE NEWS	3.37	6.74	7.24	6.74	2.00
SONY MIX	1.32	2.65	9.05	2.65	2.00
ANIMAL PLANET	2.25	4.49	9.05	4.49	2.00
ETC	1.35	2.70	3.02	2.70	2.00
IBN LOKMAT	3.30	6.60	6.64	6.60	2.00
JAYA MAX	2.52	5.04	7.24	5.04	2.00
Discovery Kids	5.57	11.13	12.07	11.13	2.00
CNBC AWAAZ	2.02	4.05	4.83	4.05	2.00
NGC Wild	6.72	13.44	15.09	13.44	2.00
Zee Bangla Cinema	2.86	5.71	6.03	5.71	2.00
ZEE TRENDZ	0.45	0.90	2.41	0.90	2.00
Average					**1.67**

The above table shows that average new price of the channels derived using Twin conditions **is only 1.6 times** the RIO rate.

Annexure 3

DTH ARPU (Internationally):

Company	Country	ARPU in $
DirecTV	USA	93
Comcast	USA	137
Dish	USA	77
Virgin	UK	73
Sky	Germany	41
Austar	Australia	89
Airtel	India	4
Astro	Malaysia	29
Skylife	Korea	8
Foxtel	Australia	97
True Corp	Thailand	25
Sky	Indonesia	17
Sky	New Zealand	59
Dialog	Sri Lanka	7
Sky	Italy	55
Sky	Japan	48