

IMCL's RESPONSE to DRAFT TARIFF ORDER FOR STB's OF MSO's

The Telecommunication (Broadcasting and Cable) services () (Digital Addressable Cable TV Systems) Tariff Order, 2013 (No. of 2013)

In the captioned Draft Tariff Order, we submit our comments as under:

We would like to put on record that the proposed regulation of Standard Tariff Package (STP) in respect of hardware would amount to over- regulation of the cable sector...

The current practice of provision of hardware by distribution /MSOs is working very well. In fact the bulk of the hardware being provided is already subsidized by the distribution / MSO.

The coupling of hardware with content is akin to CDMA technology in Telecom segment. Any regulation in STP in hardware provision will only lead to overregulation and will be a retrograde step.

Further there are no consumer complaints in this segment as of now. MSOs are already publishing the price and schemes of hardware, as directed by TRAI.

In the last tariff order of July 2010 for Digital addressable system, it was decided that the pricing and packaging of STB schemes will be left to market forces and the prices of STBS have already come down.

During CAS era, the STB price used to be around Rs. 4000. We reproduce some of the details from the same document of TRAI (July 2010, Digital Addressable Tariff Order)

TRAI's July 2010 tariff order on STB from addressable systems:

Explanatory Memorandum of the Tariff order for Digital Addressable systems, July 2010

"Tariff regulation for set top box:

41. Most of the broadcasters are of the view that tariff for supply of set top box should be left to market forces

.....Most of the MSOs suggested that tariff should be left to market forces.....

.....Different associations from cable industry stated that this should be left to market forces.....

43. The provisions relating to standard tariff packages for set top boxes for cable services in CAS areas were necessitated by the need for keeping entry barriers low for subscribers opting for pay channels in CAS areas. This was required to ensure easy migration of existing cable subscribers in the wake of compulsory implementation of CAS.....

.....*However the present circumstances are quite different. More than one addressable system is available to subscribers to choose from and competition amongst these platforms and amongst service providers within the same platform will help to keep prices of set top boxes in check. Prices for set top boxes are already exhibiting a downward trend with growth in the market and rise in volumes.....*

.....*All these factors are expected to give an impetus to the rapid growth of the digital addressable segment of the market. With growth in volumes, prices of set top boxes are likely to fall further. The Authority therefore, is of the view that setting a retail tariff for set top boxes is not necessary.....* “

“G. Niche channels requiring specialized set top boxes:

45. In case of niche channels requiring specialized set top box e.g. HDTV channels, the stakeholders are generally of the view that such channels have recently appeared in the market and all equipment relating to HD programs including the set top box and TV set are relatively costly as compared to standard definition TV sets etc. Therefore, no regulation is necessary. The niche TV channels can only be viewed in an addressable environment and that too with the help of specialized set top boxes. These channels which have been recently introduced employ advanced technology and therefore, can be considered premium in nature.

.....*As these channels are viewed by an elite section, the Authority is of the view that there is no general public interest involved and the tariff dispensation for niche channels requiring specialized set top box TV channels should be left to market forces.....*”

Basic Assumptions :

The basic assumptions for Standard Tariff Package (STP) are to be re-considered because of the following as under:

a) Life span of STB's

Under Note 3 to all the options, the regulator has prescribed as under:

“No repair or maintenance charges would be levied by cable operator on the subscriber, towards repair or maintenance of Set Top Box up to the period of five years from activation of the Set Top Box. The subscriber, however, shall be liable to pay repair and maintenance charges from sixth year onwards”

The note above assumes the life of box warranted by supplier is for five years. To the best of our knowledge there does not exist any study that the life of box is five years.

The reasonable warranty that MSO have been able to obtain from vendors is between 12 to 18 months. None of the electronic products specially one used for long hours have a life span of greater than three years and warranty not greater than 12 to 18 months.

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Post warranty period no MSO can take the onerous obligation of providing hardware without any cost for repair and maintenance, specially, when an MSO is not manufacturer of hardware and is relying on third party for supply of hardware.

- b) **The cost of the STB** has been considered along with all the elements of interest i.e. till the final installation is done at the homes. Here we have the cost of STB i.e.
- The smart card (the viewing card)
 - The interest component (as the money is borrowed at the cost varying from 11 to 15%),
 - The logistic cost (this includes the cost of warehousing, transit from port to warehouse and warehouse to branch office and branch office to the operator and then to the customer homes).
 - The other cost of logistic includes any additional wiring requirement, manpower cost for re-setting and installing of boxes and formalizing the activation.
 - Installation and activation cost - Hence from above there is definitely an element of installation and activation cost which needs to be considered.
- c) **Repairs and Maintenance** - There is no electronic product of a similar value in the market anywhere in this country (or perhaps anywhere in the world), where the maintenance and repair charges are not there during the life span. Hence it is not understood why repair and maintenance charges are not be levied. We are all aware that the maximum warranty / guarantee for such products are one year at the best.
- d) We should also keep in mind that the top quality model internationally for the similar model are available close to Rs. 4000/-. For obvious reasons the price sensitivity to all the consumers the MSO's selected the most economical and viable STB for which it is not possible to consider a no maintenance charge for a period of 3 years or 5 years.

The maintenance and repair charges are always at actual amounts. Also it has been found that, many a times maintenance and repairs are required for the STB which are tampered with or mishandled at the household level. For such cases, it becomes complete illogical to say that there can be no maintenance charges. We recommend the maintenance and repair charges waiver could be for a period of 1 year at the best.

e) **Schemes prescribed by TRAI**

In all the schemes prescribed in the captioned draft Tariff order, TRAI has prescribed certain common features which are as under:

- Monthly rental
- Security Deposit
- Return of security deposit
- No return of security deposit (adjustment in monthly rentals)

All the schemes prescribed by TRAI as above entail one common feature, which is MSOs have to record the above transaction **as Finance lease under Accounting Standard – 19**. Such prescription of scheme forces MSO to follow Finance lease only; will be in our view an illegal and business restriction. MSOs should be allowed to follow their own method of accounting.

A transaction is regarded as Finance lease if the following conditions are met:

- a) A lease that transfers substantially all the risk and rewards incident to ownership of an asset.
- b) Title to lessee may not be eventually transferred (TRAI is prescribing even transfer of ownership)

Some of the characteristics of Finance lease are:

- c) Risk and rewards are substantially transferred to the lessee by the lesser at the inception of the lease.
- d) Title to the assets may or may not exchange hands at the end of the term
- e) Assets lie in the books of the lessee and depreciation is claimed by the lessee.

Some of the consequences that would flow from above are as under:

- 1) The legal owner of the asset would have to recognize interest income – whereas the intention would be to earn Business income from the usage of the Asset
- 2) The income would have to be classified as Other income (valuation would suffer as no one would take into account Other income)
- 3) Hardware cannot be recorded as Asset in the books of MSO
- 4) Banks will not get lien on assets lying with MSO as MSO would not record hardware as assets in Finance lease
- 5) Receivables would rise as entire amount of rentals would have to be shown as receivable, thereby enlarging current assets of MSO
- 6) Tax complication would be both for direct tax and indirect tax
- 7) VAT would still be applicable as under state VAT laws there is no distinction between interest and rental
- 8) Under direct tax laws, the whole rental may be liable for income tax and depreciation may be denied as asset is being used by customer (Finance lease complications)

Given the above complications and restricted clarity until GST and Direct tax code is introduced, it is in the interest of sector to keep the tariff order in abeyance

No other method prescribed other than rental:

The failure to prescribe any other method is restrictive of business. Under clause 3 of the draft Tariff order, the MSO is permitted to offer alternative tariff packages for set top box, in accordance with the existing regulatory framework. The existing regulatory framework prescribes only STP and therefore we fail to understand how an MSO can offer any tariff package other than STP for hardware.

Restriction of Installation & Activation charges:

The draft tariff order in all the four schemes prohibits recovery of Installation & Activation charges. MSO are investing heavily into conditional access system, subscriber management system, call centre and ground on staff. All the efforts from all these systems are required to install and activate the hardware. Therefore restriction on charging any money towards Installation & Activation is a retrograde step and would hamper investments by MSO. The draft Tariff order may either delete the same or suitably modify.

We need to be provided the study on the following:

- Life span of the box (which must be shared with MSOs)
- Technological obsolesces (which must be shared with MSOs)
- Upgrade of hardware and return of old hardware by consumer (which must be shared with MSOs)
- Study of funding pattern on Capex by distribution chain
- Accounting standard implications and books of accounts and health of sector in growing economy
- Taxation structure

Until the study is done and is shared and discussed with MOS, the draft order must be put on hold.

These mandatory Standard tariff packages for STBs are not required as of now because of above.