

Dispute Resolution Hotline

April 29, 2014

SUPREME COURT: PRIVATE TELECOM SERVICE PROVIDERS UNDER CAG SCANNER

- Supreme Court has held that the books of account of telecom service providers would be subject to CAG audit.
- CAG will have the power to examine accounts of telecom service providers, specifically, the revenue sharing contract.
- This ruling has implications for private entities carrying on business under PPP model or businesses which contribute towards Consolidated Fund of India.

Recently, the Supreme Court of India ("**Supreme Court**") in *Association of Unified Tele Services Providers and Ors. v. Union of India*.¹ has ruled that the Comptroller and Auditor General ("**CAG**") is empowered to examine the accounts of private telecom companies. This is a landmark ruling and will have far-reaching implications across various business sectors as more business will come under the purview of the CAG audit. The Supreme Court's reasoning is influenced by the need for accountability and transparency in relation to transactions that involve natural resources. This ruling could have far-reaching consequences in the context of subjecting private entities to governmental regulation.

BACKGROUND

The **Indian Telegraph Act, 1885**, gives '*exclusive privilege*' to the Central Government ("**Government**") for establishing, maintaining and working of telegraph and the Government is empowered to give licenses on such conditions and in consideration of such payment, as it thinks fit, to any person, to establish, maintain or work on a telegraph in any part of India. Further, in terms of New Telecom Policy of 1999 ("**NTP**"), licenses were granted to various cellular mobile telephone service operators ("**telecom service providers**") in various cities and circles. Therefore, the Department of Telecommunications ("**DoT**"), the nodal agency under Ministry of Communications and Information Technology, issues licenses to telecom service providers in consideration of a license fee to DoT. Paragraph 22 of the **license agreement** ("**UAS License Agreement**") prescribes for accounting requirements. More specifically, Clause 22.3(a) empowers the licensor (i.e. DoT) or the Telecom Regulatory Authority of India ("**TRAI**") to call for or examine any books of accounts of the licensee at any time without assigning any reason thereof, and places an obligation on the licensee to supply these documents. Clause 22.5 and 22.6 respectively empower the DoT to get an audit and a special audit of the licensee's accounts carried out.

FACTS

On January 28, 2010, TRAI issued a notice to one of the telecom service providers, directing them to submit books of accounts for inspection to the CAG, under Rule 5 of the **Telecom Regulatory Authority of India, Service Providers (Maintenance of Books of Accounts and other Documents) Rules, 2002** ("**Rules**").² Subsequently, both the notice as well as Rule 5 was challenged in a writ petition filed by the **Association of Unified Tele Services Providers** ("**Service Providers**"), on the ground that the aforesaid is in violation of Section 16 of the **Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971** ("**CAG Act**") and Article 149 of the Constitution of India, 1950 ("**Constitution**"). Delhi High Court opined that CAG has the powers to conduct the revenue audit of all accounts drawn by the licensees. The Service Providers aggrieved by the decision appealed against the Delhi High Court ruling.

Separately, the DoT on March 16, 2010 issued a notice to one of the telecom service providers directing them to provide details of their books of accounts for the previous three years to the CAG for audit. The Service Providers challenged the notice before the Telecom Disputes Settlement and Appellate Tribunal ("**TDSAT**") as being in violation of the terms of the UAS License Agreement. The TDSAT allowed the challenge and quashed the Notice, holding that under Clause 22.5 of the UAS License Agreement, an audit was permissible only if the DoT were to form an opinion that the accounts submitted by the telecom service providers were inaccurate and misleading, which was not done in the instant case. The DoT filed an appeal before the Supreme Court. Accordingly, the appeal arising out of the Delhi High Court ruling and the TDSAT were heard together.

ISSUE

The sole issue before the Supreme Court was the legality of the subjecting private companies to a CAG audit in terms of Section 16 of the CAG Act read with Rule 5(ii) of Rules.

JUDGMENT

The Supreme Court dismissed the appeal of the Service Providers and upheld the power of CAG to examine the accounts of private entities. The Supreme Court rejected Service Providers contention that private companies could not be subject to CAG audits. It also rejected the contention that the power of CAG to carry an audit under the UAS Licence Agreement was beyond the powers of CAG as envisaged under the CAG Act. Examining the powers of the CAG under the CAG Act, the Supreme Court held that the CAG had the power to audit all transactions, including

Research Papers

Compendium of Research Papers

January 11, 2025

FAQs on Setting Up of Offices in India

December 13, 2024

FAQs on Downstream Investment

December 13, 2024

Research Articles

INDIA 2025: The Emerging Powerhouse for Private Equity and M&A Deals

January 15, 2025

Key changes to Model Concession Agreements in the Road Sector

January 03, 2025

The Revolution Realized: Bitcoin's Triumph

December 05, 2024

Audio

Securities Market Regulator's Continued Quest Against "Unfiltered" Financial Advice

December 18, 2024

Digital Lending - Part 1 - What's New with NBFC P2Ps

November 19, 2024

Renewable Roadmap: Budget 2024 and Beyond - Part I

August 26, 2024

NDA Connect

Connect with us at events, conferences and seminars.

NDA Hotline

Click here to view Hotline archives.

Video

"Investment return is not enough" Nishith Desai with Nikunj Dalmia (ET Now) at FIIB event in Riyadh

October 31, 2024

Analysing SEBI's Consultation Paper

receipts, which have a nexus with the Consolidated Fund of India (“CFI”).

The Supreme Court held that that the license fees paid by the telecom service providers would accrue to the CFI and thus be amenable to audit by the CAG under Article 149 of the Constitution. On an examination of Section 13, 16 and 18 of the CAG Act, Supreme Court held that CAG was not actually carrying out an audit but was examining receipts to ensure that the Union had received its due share by way of licence fee. The Supreme Court has placed a lot of reliance on the need for transparency and accountability while dealing with natural resources and has considered the role of CAG as an independent examiner of the receipts of the Union.

Examining the clauses of the UAS Licence Agreement, the Supreme Court held that an audit by CAG was independent of other audit mechanism under the UAS Licence Agreement. Significantly, the Supreme Court has held that the CAG’s powers under the Constitution to be a part of its basic structure, thereby preventing the Government from taking away these powers by legislation or Constitutional amendment.

ANALYSIS

This ruling of Supreme Court will have huge implications as every project or service carried out under public-private partnership (“PPP”), involving a revenue sharing model as well as the companies that contribute to the CFI, can be audited by the CAG. The ruling reiterates the well-settled principle of need for accountability and transparency while dealing with the nation’s natural resources. The ruling however goes further and emphasizes the need for transparency and accountability in respect of transactions having a connection with CFI. The interpretation of CAG Act makes it clear that independent of provisions any licence / other agreement, CAG will have the power to examine the accounts of such a private party purely based on the CAG Act and the Constitution.

Although the Supreme Court has sought to limit the power of CAG to examine receipts which have a connection with CFI, the CAG must guard against excessive regulation which might adversely affect investments in PPP projects.

– Alipak Banerjee, M.S. Ananth & Vyapak Desai
You can direct your queries or comments to the authors

¹ Civil Appeal No. 4591 of 2014, 4592 of 2014, 10748 of 2011 and 10749 of 2011.
² Rule 5 requires telecom service providers to produce books of accounts, documents and related statements and information to TRAI for enabling an audit by the CAG under Section 16 of the CAG Act.

DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.