

Telecom Hotline

May 03, 2007

REVISED GUIDELINES UNDER PRESS NOTE NO. 3 (2007 SERIES) FOR FOREIGN DIRECT INVESTMENT IN THE TELECOM SECTOR

INTRODUCTION

Amidst industry and governmental debate over a roll back of the liberalized telecom sector ceiling (of up to 74% FDI), the Department of Industrial Policy and Promotion on April 19, 2007, issued a Press Note upholding the upper ceiling in the sector, but laying down new security- related guidelines.

HISTORY

Liberalization of the Foreign Direct Investment (FDI) policies play a vital role in encouraging foreign investors and enhancing competitiveness within the domestic market. In furtherance of its efforts to regularize investments, the government of India has recently undertaken a comprehensive review of Press Note No. 5 (of 2005) Series dated 3.11.2005 and issued certain guidelines under Press Note No. 3 (2007) Series dated April 19, 2007¹.

Although Press Note No. 5 (2005) Series dated 3.11.2005 had enhanced Foreign Direct Investment (FDI) from 49% to 74% in the telecom sector, it had enough caveats to subject it to various controversies. The foremost criticism of Press Note No. 5 (2005) Series was that majority directors on the board of a company including the chairman, managing director and chief executive officer would have to be resident Indian citizens. This came under severe scrutiny and multinationals questioned the rationale behind holding 74% in a telecom company as they still did not have the liberty to appoint a chairman, managing director or CEO of a foreign nationality.

Another criticism under the earlier Press Note No. 5 (2005) Series was that it was mandatory for all telecom operators to locate their network monitoring centers within the country and thus remote access was limited to within the boundaries of India. This again generated criticism as multinational telecom companies would have to invest huge amounts for setting up remote access within India as oppose to their already existing large network monitoring set ups elsewhere in the world.

The revised guidelines under Press Note 3, 2007 Series allows telecom companies to extend their remote access to approved location(s) outside India but via the approved location(s) in India and whereas such approvals would only be given by the government in consultation with the appropriate security agencies.

The other directives under the earlier Press Note No. 5 (2005) Series, which stand revised by the release of the current Press Note 3, 2007 Series are as follows:

INDIRECT FOREIGN INVESTMENTS

The current Press Note 3, 2007 Series has expanded the definition of indirect foreign holding by including proportionate investments made by a foreign entity in a telecom company through mutual funds, trusts or a holding company. In any case, the Indian' shareholding will not be less than 26 per cent.

Henceforth, "Indirect foreign investments" shall mean, foreign investments in the company/ companies holding shares of the licensee company and their holding company/companies or legal entity (such as mutual funds, trusts) on proportionate basis.

Therefore unlike Press Note No. 5, 2005 Series which only specified investments through holding companies as FDI, the current Press Note further clarifies the ambit of indirect foreign investments.

APPLICABILITY

The current Press Note 3, 2007 Series expressly states that the guidelines for security would be applicable to all licensee companies operating in the telecom sector irrespective of the level of Foreign Direct Investment (FDI). However what remains uncertain is whether these security conditions would be applicable if there is no FDI at all because the current guidelines are silent on those aspects.

In the previous Press Note 5, Series 2005 there wasn't any classification undertaken in accordance with the level of FDI or on the applicability of such security conditions.

OTHER SALIENT FEATURES OF PRESS NOTE NO. 3, 2007 SERIES

Apart from the above mentioned carve outs, the release of Press Note No. 3 (of 2007) also sets out certain security conditions which have to be adhered to by prospective investors in the telecom sector. Mentioned below are the revised security conditions, which were brought about by the release of the current Press Note.

- Timely and adequate measures to be undertaken to ensure that information which is transacted through the network is secured and well protected.

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- The officers / officials who would be officially intercepting the messages should be Indian resident citizens.
- The telecom service provider should be able to provide the geographical location of any subscriber on the request of the government.
- However, no remote access to be extended to Lawful Interception System (LIS), Lawful Interception Monitoring (LIM) or any other sensitive data.
- Technical device should be made available so as to create a mirror image for remote access information for on line monitoring purpose.
- An audit trail of the remote access should be maintained for a period of six (6) months and details of the same to be provided on request to the government.
- The telecom service providers should be updated with the Vigilance Technical Monitoring system (VTM) and the other relevant security agencies for the operations of their systems.
- This Press Note will also be applicable to service providers providing services like call centers, Business Process Outsourcing (BPO), tele-marketing, tele-education etc. using the telecom infrastructure. In this case the FDI up to 100% is permissible.

CONCLUSION

The government of India by the release of this current Press Note 3, 2007 Series has expressed its own decision to improve the investment climate in the country and protect the monies brought in by foreign investors. Although there is an anomaly in the current Press Note on whether the security conditions are applicable even if there is no FDI, nevertheless the government has sought to rationalize its policies under the current Press Note and categorically lay guidelines for ensuring FDI enhancement under well-regulated security conditions in the telecom sector. The release of this Press Note has lead to broadening the scope of policy application to sectors such as BPO, telemarketing, expansion of the definition of Indirect Foreign Investments, allowing foreign nationals to hold key posts and many other reformative measures. The guidelines under this current Press Note assist in striking an appropriate balance between the security conditions and the operability under the telecom sector. The release of this Press Note can also be construed as a prospective and liberal approach on behalf of the Indian government towards the telecom industry.

- **Huzefa Tavawalla & Vaibhav Parikh**

¹F. No. 12/2/2006-FC dated April 19, 2007

Source:

- Press Note No. 5 (2005) Series
- IndLaw.com, April 19, 2007
- The Indian Express, March 23, 2007
- DNA, March 22, 2007

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Vaibhav Parikh, Partner, Nishith Desai Associate on Tech, M&A, and Ease of Doing Business

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