

Telecom Hotline

April 28, 2008

REVISED GUIDELINES FOR MERGER IN THE TELECOM SECTOR

On April 22, 2008 vide circular No.20-100/2007-AS-I the Indian telecom authority ("Government") issued revised guidelines ("Guideline") for intra-service area merger of Cellular Mobile Telephone Service/Unified Access Services ("CMTS/UAS or Licenses") superceding the earlier guideline issued in 2004. The Government has revised the guidelines keeping in mind the recommendations forward by the Telecom Regulatory Authority of India ("TRAI") [1] in October last year.

HISTORY

The Department of Telecommunications ("DoT") [2] in February 2004 issued merger guidelines ("2004 Guidelines") for merger of licenses in the same service area ("Service Area") [3]. Same Service Area is an area where two merging entities operate within the same telecom circle such as two telecom service providers operating within Southern part of India. A telecom service provider can merge with another telecom service provider only if both the merging service providers are operating within such Service Area. Therefore telecom service providers offering services in Maharashtra and Tamil Nadu will not be allowed to merge under the 2004 Guidelines and even under the revised Guideline. Further, under the 2004 Guidelines, the merger between the merging entities was not permitted if the merger would lead the merged entity's market share within the relevant area [4] to 67% or more.

SALIENT FEATURES OF THE GUIDELINES

- Prior approval of DoT shall be necessary for merger of all licence(s) and such mergers shall be restricted to the same Service Area. As per the 2004 Guidelines DoT would normally approve / reject any application for merger within a period of four weeks from the date of its submission. The current Guideline are silent on the time frame for such approval / rejection.
- Any permission for merger(s) shall be accorded only after completion of three years from the effective date of the licence being granted to the telecom operators by the relevant government authority. The 2004 Guidelines did not specify the completion of any term before granting permission for any merger.
- The combined market share of any merged entity has been lowered from 67% to 40%. Under the earlier 2004 Guidelines the market share was calculated only in terms of subscriber base as oppose to the current Guidelines where the market share is now to be determined in terms of subscriber base as well as in terms of revenue.
- The DoT would not give approval for any merger if such merger reduces the number of service providers below four as oppose to three as per the 2004 Guidelines.
- The merged entity shall be entitled to the total amount of spectrum held by the merging entities, subject to the condition that after approval of the merger, the merged entity shall within a period of three months fulfill the prevailing spectrum allocation criteria. The 2004 Guidelines did not specify any time period for fulfilling the required spectrum criteria.
- However, if the merged entity fails to meet the spectrum allocation criteria within 3 months, then such merged entity shall surrender the excess spectrum, if any, failing which the same shall be treated as a violation and DoT / TRAI shall have the right to initiate the necessary action. In addition to initiating such action, the merged entity shall also be charged double for holding additional spectrum for every 3 months.
- The discretion to choose the band in surrendering the excess spectrum beyond the permissible limit shall be at the option of the new merged entity.
- The guidelines issued on "substantial equity" for regulating acquisitions shall continue to be applicable and the telecom operator(s) will not be able to take more than 10 per cent equity stake in rival operators in the same Service Area.
- All outstanding dues attributable to the merging entities shall be cleared by either of the two entities before being granted approval for merger.
- The duration of the license of the merged entity in the relevant Service Area shall be equal to the remaining duration of license of the two merging entities, whichever is less, as on the date of the merger.
- The dispute resolution shall lie with the Telecom Dispute Settlement and Appellate Tribunal ("TDSAT") as per TRAI Act, 1997 as amended by TRAI (Amendment) Act 2000.
- Subsequent to the merger the merged entity will be subject to the rules & regulations applicable to Significant Market Power ("SMP").

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- Percentage of Market Share** - Unlike the 2004 Guidelines where the merged entities could hold market share upto 67%, the merged entities under this Guideline cannot hold market share of more than 40%. . As a result it will become difficult for existing telecom service providers to acquire additional market share within their Service Areas by way of acquisition of small players. **Vaibhav Parikh**^[5] feels that that *"as a result of a merger the merged entity could provide services in more than one circle and that could result in a situation in which the merged entity has revenue or a subscriber base beyond 40% in one Service Area and less than 40% in another Service Area"*. Thus such merged entity may be restricted in providing services in one circle as compared to the other circle. It is further quoted that, *"it is yet to be examined whether DoT would provide its approval in such situations?"*
- Qualifying Period for Approval** - The 3 year obligation for a licensee before becoming eligible for a merger under the Guideline will certainly be a barrier for all new entrants as they will not be able to merge with existing licensees unless they fulfill this time period. **Vivek Kathpalia**^[6] feels that *"one of the possible reasons for the introduction of this limitation period is to increase service providers and thereby competition in a service area leading to expansion in India's telecom infrastructure and better utilization of services"*. However, Vivek Kathpalia further observes *"that such objectives could also be achieved by undertaking a merger prior to the completion of three years and therefore may not be looked upon favorably by the telecom industry"*.
- Roll-Out Obligations** – The current Guidelines have not adopted the recommendations of TRAI in respect of fulfillment of the contingent roll out obligation which envisage that the licensee would need to extend its services in the Service Area in accordance with the terms as detailed under the UAS Licence Agreement.
- Spectrum Allocation** - Since the operations of the merged telecom operators will be based on the existing spectrum allotments, industry experts claim that the 3 months period to return excess spectrum was not technically feasible as prior to surrendering the excess spectrum, the telecom operators would need to migrate and transform their existing subscribers / operations on another frequency. Worldwide examples have shown that such transformation usually ranges between 12 - 24 months.

CONCLUSION

India is one of the world's fastest growing telecom markets and it continues to be amongst the world's lowest telecom tariff destinations. Government sources claim that the revised Guidelines have been introduced to increase competition, better utilization of services and to ensure the optimal use of scarce spectrum. However, these Guidelines have attracted some criticism from the telecom operator's lobby as it restricts their ability to consolidate. Furthermore the Guidelines leave certain room for interpretation, as highlighted above. The telecom industry is bound to approach the Government and seek possible amendments / clarifications to these Guidelines over the next few days.

- **Telecom Practice Team**

[1] TRAI is the regulatory body set up under the Ministry of Communications & Information Technology which issues from time to time various regulations, orders and directives for the evolution of Indian telecom market.

[2] DoT is the licensing authority set up under the Ministry of Communications & Information Technology which issues various telecom licenses and approvals.

[3] Service Area means any of the 23 service areas identified by DoT, consisting of 19 telecom circle service areas and 4 metro service areas for providing CMTS.

[4] The relevant area would be that relevant geographic area within which the merging entities are providing the same or similar type of services to the consumers for the purpose of determining whether the merger is anti-competitive or not.

[5] Vaibhav Parikh heads the telecom practice at Nishith Desai Associates.

[6] Vivek Kathpalia is a senior member of the telecom practice at Nishith Desai Associates.

Sources:

- Guidelines for intra service area Merger of Cellular Mobile Telephone Service (CMTS)/ Unified Access Services (UAS) Licenses - No.20-100/2007-AS-I 22nd April, 2008
- Government of India, Ministry of Communication and Information Technology Department of Telecommunications Office Memorandum No. No.20-232/2004-BS.III Dated, the 21st February, 2004.
- The Economic Times April 23 / 24, 2008.
- Reuters News April 23, 2008.
- Business Standard April 23, 2008.

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