



Cellular Operators Association of India

TVR/COAI/037
March 03, 2009

The Telecom Regulatory Authority of India
Mahanagar Doorsanchar Bhawan
Jawahar Lal Nehru Marg (Old Minto Road)
Next to Zakir Hussain College
New Delhi – 110 002

Subject: Issues discussed at the 2nd Open House Discussion on the review of IUC held at Hyderabad on 26th February, 2009

Dear Sir,

This is with reference to the 2nd Open House on the ongoing review of IUC which was held at Hyderabad on February 26, 2009.

In this regard, please find our response to the issues raised by the Authority in the abovementioned open house.

We hope that our submissions will merit your kind consideration.

Sincerely,

T V Ramachandran
Director General

Encl: as above

Distribution

- : Shri Nripendra Misra, Chairman, TRAI
- : Shri A. K. Sawhney, Member, TRAI
- : Shri R. N. Prabhakar, Member, TRAI
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Issues discussed at the 2nd Open House Discussion in Hyderabad

I. INTRODUCTION

1. We would like to thank the Authority for giving us the opportunity to present our views in the 2nd Open House on IUC which was held at Hyderabad on February 26, 2009.
2. At the outset, we would like to state that we were rather surprised by the significant change in format of the Second Open house, wherein a new set of consultation questions were posed by the Authority.
3. This departure from the past practice was completely unexpected as a result of which, many of our member companies may have presumed that the format of the open house would be the same as has been the past practice and issues discussed would be those which were listed in the Open House in Delhi. Consequently, many of our member operators were not present for the second open house in Hyderabad and hence were not able to contribute in the fresh discussions initiated by the Authority.
4. It is most respectfully submitted that the Authority could have ensured a more effective discussion and fruitful participation in Hyderabad, had the new format as well as the fresh issues for consultation, being communicated in advance to all the stakeholders/ service providers .
5. Furthermore, in light of the fact that new issues/ questions have been raised by the Authority, both past practices as well as principles of natural justice require that adequate time be given to all stakeholders to respond to these set of questions raised by the Authority.
6. We would also like to bring to your kind attention that the submissions made by COAI with regard to the ongoing review of IUC have been finalized through a consensus approach which involved detailed discussion and deliberation with all the stakeholders. Several meetings were held to seek inputs from all members/ stakeholders and the same were also incorporated in the model. The Model submitted was thus based on data and assumptions which were arrived at after seeking and incorporating consensus views of all the members.
7. In this regard, we would also like to submit that interconnection is a bi-partite agreement between two operators and operators will always have different commercial and strategic interest and perspective. We respectfully submit that the Authority should take inputs from all, but should eventually adopt an approach which is forward looking and encourages investment and facilitates growth of the sector.
8. Although various cost models have been submitted to the Authority as a part of the ongoing IUC review, the fact is that the model developed by SVP for COAI is the only model which has been developed through a consensus approach and has been transparently shared with all the stake holders. The same is also based on the internationally accepted FLLRIC approach, which approach has also been endorsed by the Authority way back in 2003. Hence, we request that due importance and consideration may please be given to the same.

II. PRELIMINARY SUBMISSIONS

In light of the above, we would like to make our preliminary submissions on the issues raised for consultation by the Authority:

Q1 Service Providers have taken divergent assumptions for calculating MTC by FLLRIC method. If at all TRAI decides to move to FLLRIC what set of assumptions should be taken that would reflect correct MTC both for incumbents and new entrants keeping in view growth of the sector and consumer welfare.

Q2 The estimates of MTC given above are based on the data submitted by service providers including that from their confidential accounting separation reports. Stakeholders opinion is sought whether individual operators calculations be made public.

A. Costing Methodology

1. First and foremost, we wish to most respectfully clarify and correct a wrong impression which is being given that COAI is championing for adoption of FLLRIC approach. We wish to clarify that COAI is not wedded to FLLRIC approach, or for that matter to any other specific methodology. COAI's main concern is that the Authority should adopt a robust cost model which includes all cost elements that are involved in the termination of a call and one that justifies investment for expansion of service.
2. COAI is of the view that the proposed IUC Regime should be within the four corners of sound economic policy. The Regime should draw from international best practices and should facilitate the much needed investment in the telecom sector.
3. Interconnect pricing should thus be based on a robust cost based model, which justifies investment for expansion of service. Also, to be in line with international best practices, this cost model should take into account all the internationally accepted cost elements which are taken into consideration while preparing a cost based model for determination of termination charge. It may be appreciated that the accuracy of the model depends on, inter alia, the cost elements which are taken into consideration. In case some cost elements which should be included are not taken into consideration, the model can give inaccurate results, which might be a disincentive for investment.
4. However, we do believe that since several hundred million subscribers are yet to be connected, FLLRIC approach is the way to go forward and will give better results than any other cost based methodology.
5. The **TRAI in one of its notifications has mandated the need to gradually shift towards the FLLRIC approach.** In fact the Authority has stated that a shift to FLRIC approach is imperative. The Authority in its notification (No. 409-5/2003/FN, dated 29th October 2003), has stated that there is a need to eventually move to LRIC based MTC estimation model. An extract from TRAI's notification of 2003 is given below:

“The Authority considered the framework used for calculating the IUC under the previous exercise, and noted that the cost basis used had

*been historical average costs from audited accounts of BSNL. It noted that **for costing purposes, several countries had used Forward Looking Long Run Incremental Costs (FLLRIC)**, i.e. a methodology under which only a portion of stranded costs (or costs arising due to past high equipment prices or old technologies) is included in the calculation of costs.”*

*“The Authority noted that the difference between historical costs and forward looking costs would be large, and relying on costs based only on modern and forward looking technologies would imply a large burden from the stranded costs for BSNL. While **the Authority feels that change over to FLLRIC model is imperative**, it examined the implications of a sudden changeover against a gradual changeover. Since BSNL is the major supplier of telecom services in the country and has also contributed the maximum for achieving the targets of rural teledensity and in supporting low paying subscribers, a changeover to FLLRIC at present would adversely affect the services provided not only to rural and low paying subscribers but also the telecom industry in the country as a whole. The Authority noted that BSNL is already deploying latest technology and lower cost equipment in its expansion programme. Since wireless technology is being used, it is expected that some of the existing network will also be gradually replaced by such equipment. **In short, the approach is to achieve full shift to FLLRIC cost in a gradual manner over a few years rather than a single year change.**”*

6. It is evident from the above that the Authority too, has recognized that **the FLLRIC is used by several countries and that a changeover to the same is imperative**, but that this should be done in a gradual manner. It is most respectfully submitted that over five years have elapsed since the above views were enunciated by the Authority and we believe that it is indeed both necessary and desirable that in the ongoing IUC review, the Authority should seriously consider changing over to the FLLRIC approach.
7. It is again reiterated that while we are not wedded to any specific methodology, we nevertheless believe that FLLRIC would be more appropriate for India than FAC. The FLLRIC approach builds into the model greater efficiency and gives more accurate cost based charges which reflect efficiency and are hence lower than the results achieved using an FAC approach.
8. In view of the fact that FLLRIC builds in efficiency and leads to lowest cost based termination charges, many countries are gradually moving towards the FLLRIC model. There is an emerging consensus amongst the National Regulatory Authorities in many countries that hybrid FLLRIC approach is the most conducive to promoting market entry and competition.

B. Bridging the Digital Divide

1. Even, one of the respondents in the open house correctly submitted that the present regime is backward looking, since it is based on / or is built upon the data and the

methodology of 2003. In the year 2003, the number of subscribers was much lower and share of prepaid subscribers was much less.

2. Since then, the telecom scenario has undergone a significant change and hence also, there is a need to consider a change in methodology that will take into account the changed scenario and put in place a methodology/approach that is both forward looking and robust enough to facilitate growth and penetration of services, especially in the rural areas so as to and overcome the existing concerns regarding the ever growing digital divide.
3. The Authority is aware that despite of the rapid growth in the telecom sector, India is faced with the problem of growing urban-rural digital divide. The national coverage objectives with regard to population and geographic coverage are yet to be achieved. It is important to ensure that benefits of connectivity are available to all across the length and breadth of the country.
4. The proposed IUC Regime thus needs to address the growing digital divide, which will require investment to the tune of thousands of crores. The proposed IUC regime should be such that it serves as one of the key drivers for bridging the digital divide.

C. Transparency

1. It is further submitted that it is both necessary as well as desirable that the entire exercise of determination of IUC charges be carried out in a transparent manner as is done by the Regulators in many other countries of the world. Transparency lies at the core of any determination of cost based IUC charges.
2. In this regard, it may be noted that COAI has shared its assumptions, cost elements used, methodology and the cost model with the Authority and also all our member companies in a detailed and a completely transparent manner. All the capex and opex line items used in the model and the value of these line items have been explained to our member companies and the Authority.
3. We request that a similar approach be followed by the Authority. The Authority may kindly share with us its assumptions, details regarding cost elements, methodology and the cost model in order to ensure more meaningful participation in the IUC exercise. We believe that internationally as well, most Regulators in other countries make available the assumptions, methodology and the cost model to all the stake holders for receiving their comments.
4. Hence, we most respectfully request the Authority to also make available in a transparent manner, its own cost model as well as the cost models, submitted by other stakeholders, so as to enable us to review and comment on the same. It may be appreciated that it is only with the full and transparent sharing of the model that the stakeholders will be able to effectively participate in the consultation process. Merely sharing the results of the model, with just a few explanations will not serve the desired purpose.
5. Furthermore, since clearly divergent assumptions and costing methodologies for calculating MTC by FLLRIC model have been submitted to the Authority, it may be desirable for the Authority to consider setting up a joint industry working group or a

steering committee to deliberate and decide on the same. This approach has been followed by the Authority in the past when it formed a steering committee to evolve a consensus view among all stakeholders for preparing guidelines for implementation of MNP.

6. The steering committee for MNP, which was set up under the leadership of TRAI, has carried out its mandate very well by enabling an effective and fruitful exchange of ideas among all the stakeholders.
7. A similar approach was also adopted by the Authority in the case of UCC (Unsolicited Commercial Communication) wherein a steering committee was formed with all the stakeholders as participants to discuss and decide on the key issues being faced by the industry.
8. We believe that **it is all the more important that a similar approach be adopted by the Authority in the case of IUC review, where important commercial considerations are at stake.**
9. As regards the operator specific data, we believe that the same should not be put on the website, but may be shared and discussed in the steering committee. The formation the steering committee will thus address the concern of confidentiality of data submitted by various service providers. The set of assumptions to be used can also be discussed and finalized in the steering committee. As per the international practices, the steering committee formed by TRAI could also include international experts/ consultants on the subject.

Q3 Whether the Authority should continue with the existing methodology of taking relevant OPEX for calculation of termination charge by deducting following from the OPEX:

- | | |
|----------------------------------|--------------------------------------|
| (a) Sales and Marketing Cost | (b) Bad debt, provision for Bad Debt |
| (c) Billing and Customer Care | (d) Customer acquisition cost |
| (e) Financial Charges | (f) Collection expense |
| (g) Loss from sale of asset etc. | |

It is first submitted that any costing methodology that is adopted by the Authority should transparently gives details of all costing elements are are being included as also all costing elements that are being excluded along with a justification thereof. It may be appreciated that a negative list of cost elements deducted / proposed to be deducted from the costs, will never give the stakeholders complete clarity on what cost elements have been included. Such an approach will invariably give rise to both conjecture as well as contentiousness which will hamper the development of an consensus in the matter.

A. Treatment of Capex

1. It is submitted that the existing methodology followed by the Authority of recovering “relevant” opex from call charges/airtime and capex from rentals is totally unfair and incorrect. In this regard it is first submitted that such an approach is not in line with the international best practices adopted by regulators in other parts of the world.

2. It is most respectfully submitted that whilst the Authority purports to adopt a “cost-based” approach, it is actually following a revenue /retail tariff based approach as both call charges as well as rentals are recovered from subscribers and not from other service providers. In fact, the Authority is following a flawed and confusing approach wherein “relevant” opex is recovered from other operators through MTC and capex from “rentals”
3. Such an approach is completely anomalous and out of line with all international practices.
4. It may also be appreciated that whilst IUC/MTC is a prescribed “cost-based” charge, tariffs are under forbearance. By under prescribing the cost based charges, the Authority is actually encouraging subsidy on incoming traffic and higher tariffs/outgoing call charges on outgoing calls. It may be appreciated that purchase decisions are made on the basis of outgoing call tariffs and by encouraging higher call charges, the model adopted by the Authority is actually against public interest and further growth and penetration of service.
5. Furthermore, the approach followed by the Authority overlooks a very important aspect which is that, in the case of mobile, prepaid forms the bulk of the subscriber base at 95% or more. Since there are no rentals in case of prepaid, we fail to understand how the Authority expects capex costs to be recovered from rentals.
6. Telecom is highly capital intensive, each subscriber adds to cost, in fact, traditionally, operators always talk in terms of capex per subscriber. This cost goes up significantly when the rollout is in the rural areas. It is therefore important that capex /cost of capital be taken into consideration for determination of cost based IUC charge.
7. All internationally accepted cost based methodologies take capex/cost of capital into account for determination of termination charge. While FAC approach takes into account historical capex, the FLLRIC approach takes into consideration the incremental capex of the network elements used for completion of the calls.
8. Hence, the approach followed by the Authority is not only out of sync with international best practices but is also deeply flawed.

B. Treatment of Opex

1. Firstly, it is not clear as to what the Authority means by “relevant” Opex as we are not aware of the cost elements used by the Authority. As submitted above, transparency requires that the Authority share with the stakeholders all elements of cost that are being included or excluded from the cost model. Whilst, COAI has shared the details of opex and capex line items used by us in our costing model, a similar transparent approach has not been adopted by the Authority thus far. It is again reiterated that transparency lies at the very core of introducing a robust and effective IUC regime.
2. It is thus most respectfully reiterated that the Authority may kindly share with us its assumptions, methodology and the cost model in the same manner as COAI has done with the Authority. This would entail sharing the complete list of opex items included as well as excluded (along with a justification thereof) rather than a list of

just the deductions. This will enable all stakeholders to understand the approach followed by the Authority and engage effectively and constructively in the consultation process.

Q.4 How should the revenue generated from value added services should be taken into account so that it remains rational and reasonable

1. We would first like to submit that the above issue suffers from the same flaw pointed out above that the Authority is mixing up a cost based approach and a retail tariff based approach.
2. In a costing methodology, the attempt is to discover the cost of all elements that are involved in origination, carriage and termination of a call. This has no nexus with the retail tariffs /revenues that are earned by the service providers.
3. By deducting / factoring revenues from the cost model, the Authority is encouraging the operators to recover from revenues what they are deprived in terms of costs. A robust cost model that allows the operators to correctly recover their costs from IUC will in fact lead to a lowering of tariffs for voice as well as non-voice services.
4. It is therefore important to keep in mind that the key objective of the Hybrid FLRIC model is to arrive at the “cost” of voice termination based on the cost elements which are used for the same. The purpose of the routing table is to allocate costs associated with network elements to the specific services being modeled i.e. on-net and off-net calls, SMS and Data services etc. To the extent network elements like the Base Transceiver Station etc. are used for services other than call termination, a proportionate cost is allocated to the these services. The model does not strive to forecast revenues and accordingly the Hybrid FLRIC model does not focus on revenues from VAS.
5. This is also in line with the international best practices. Regimes in other parts of the world also do not take into account revenues from VAS.
6. So as to ensure that the approach remains rational, reasonable and in line with international best practices, the cost associated with provisioning of VAS services should also not be taken into account. And hence the revenues generated from VAS need not be considered.
7. Without prejudice to the above, it is submitted that the VAS revenues in India are very low at 10% as compared to other parts of the world, especially in countries like Philippines where it is as high as 46% of the net service revenues¹. VAS revenues are generally 20% to 30% in other countries.

Q.5 During the Consultation process some of the service providers have also raised that SMS termination charges should also be prescribed by the TRAI. Can it be presumed that by and large the present arrangement is based on one of the following:

- (a) Bill and Keep (b) Reciprocity**

¹ Source: Merrill Lynch Global Matrix 2008

AND

Q6 Presuming that by and large the above arrangements exist and would continue to exist, should forbearance on SMS termination charges as propounded earlier

(a) Be continued

(b) Be continued as interim arrangement till TRAI finally decides SMS termination charges based on fresh consultations.

1. It is pertinent to note that in the last three to four years the growth of the SMS usage is limited. This is primarily due to the fact that the voice call tariffs are very low and people are using voice more than SMS services. Hence, we believe that regulating the SMS termination rates may not serve any purpose.
2. It may be noted that any examination of SMS termination charge should be done keeping in mind that the same may encourage Spam SMSs and will result in undue utilization of network resources. This will put an unnecessary burden on the network. We would also like to request that while deliberating on this issue, the aspect of UCC SMS may also to be kept in mind and accordingly, a holistic view may please be taken on this issue.

Q7 Which of the following options should be considered for international incoming call termination rate

Option 1: Forbearance

Option 2: Reciprocal arrangement

Option 3: Increase from present level

Option 4: Maintain at present level of 30 p/min

Option 5: Same as domestic termination charge

1. As the Authority has itself observed, the Indian operators are paying weighted average cost of Rs 3 per minute for termination of their calls in other countries as compared to a termination charge of just Rs 0.30 per minute on incoming ILD calls in India.
2. India is a net importer of international traffic, with a nearly 3 to 1 ratio i.e. for every minute that we send out, we receive 3 minutes. With such a high ratio in our favor, our country should get precious foreign exchange from other countries for incoming ILD traffic.
3. However, while our average cost of sending the traffic ranges between 8 – 10 cents whereas our termination charge for incoming ILD calls is only 0.75 cents. As a result, India is a net out-payer in term of actual flow of money even though we receive more traffic.
4. It is expected that next year we will be sending out about 9 billion minutes, at an average rate of 8.8 cents per minute and India will pay out \$ 792 million. We will receive 25 billion minutes at current termination rate of 0.75 cents, accruing revenue of about \$ 188 million. Thus on the whole we will end up paying \$ 604 million to International Carriers even though we will be receiving 16 billion minutes more than we send out.

5. There thus exists an imbalance which needs to be corrected. And this imbalance is only increasing with time. It may be noted that recently Etisalat has increased the termination from 10cents/minute to 13cents/minute w.e.f 1st April 2009.
6. In light of the above we would like to submit that termination charge for international calls should be higher than that for domestic calls and more in line with the international termination rates paid by us to our counterparts abroad. The Authority may thus consider that the termination charge for international incoming calls be prescribed at a ceiling of Rs 3 per minute.
7. A higher termination on incoming ILD calls will also result in higher revenues for the Government. It is estimated that an increase of Rs. 1.50 per minute in the international termination charge, Indian operators will receive Rs.37,500 million extra in the year. Also, assuming a licence fee of 10%, the Government will be receiving an extra Rs. 3,750 million apart from other taxes / levies.
8. Further, increasing the termination charge on incoming ILD calls will make more funds available for all service providers for expansion of service without increasing the burden on the Indian consumers.
9. This step would thus also be in line with the policy objective of increasing the expansion of affordable service to rural areas.
10. We would like to place on record our appreciation of the work done by the TERM cells in the area of vigilance and monitoring. We believe that the issue of grey market can be addressed through stricter monitoring and control. DoT also has a network of Telecom Enforcement Resource & Monitoring (TERM) cells in place which is already carrying out monitoring and vigilance functions. These resources can be used for stricter monitoring and control of the grey market.

Q8 Should the 3G voice termination charge be kept same as 2G voice termination charge?

1. It is submitted that presently the take-up and usage of 3G services is uncertain. Also, there are a number of cost related factors with a 3G network (relative to a 2G network that are required to be considered in the near term such as:
 - Migration to the new technology.
 - Demand risk due to uncertain take up in the near term.
 - Costs to the early adopters of 3G technology.
2. There might also be issue of Non- level Playing field if there is different termination charge for the 3G services and the 2G services.
3. Hence, we are of the view that the issue of setting the termination charge of 3G mobile services should be considered at the later stage, when there is more clarity regarding the pricing of 3G spectrum.
