Grant Thornton

UnionBudget 2010-11

Telecom Industry

The story in the sector can be summed thus; robust growth momentum, especially in segments related to wireless telecommunication, aggressive pricing by new entrants and therefore consequent EBIDTA erosion resulting from falling Average Revenue Per Users (ARPU).

Up, Up and Away:-

- Figures from the recently released Economic Survey indicate an astounding CAGR of 60 % since 2004 mainly in the wireless segment. This had the impact of pushing up the overall subscriber base beyond 500 million. With approximately 525.1 million wireless connections alone, the Indian telecom has become the second largest network in the world.
- Teledensity – a barometer of telecom penetration showed an increase from 12.7% levels in March 2006 to the present 47.9% in December 2009.
- Internet/broadband subscribers also contributed to the overall growth which rose from about 0.2 million subscribers in 2005 to about 7.98 million subscribers by December 2009.

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The road ahead

- Growth expected from Value Added Services (VASs) like streaming videos, m-commerce/ m-banking applications and various menu based services & 3G technology
- Mobile Number Portability (MNP) will be introduced shortly and the recent announcement of guidelines towards the same will force service providers to improve quality or lose customers
- Manufacturing in the telecom sector benefited because of the availability of cheap labour, progressive policies, and huge R&D talent base. Exports in telecom manufacturing increased from Rs.402 crore in 2002-03 to Rs. 11,000 crore in 2008-09.
- Foreign Direct Investment (FDI) ceilings have been raised from 49% to 74%. However, in the area of telecom equipment manufacturing and provision of IT-enabled services, 100% FDI is permitted thus making this sector attractive for investors

Waiting for 3G

Finally the story for 3G seems to be moving with the government announcing guidelines for penetration of 3G telecom services. Existing operators and those waiting on the fringes would be provided with a good opportunity to bring in new technology and innovations, and operate in an ever growing but highly competitive market

Key Expectations

Direct Taxation

- The rationalisation of provisions under Section 80-IA be allowed to provide benefits in line with other industries, availing of benefits towards reorganization, tax holidays for new licenses issued, extension of period for which deduction is allowed
- Clarity is required in respect of the definition of royalty under section 9(1)(vii) specifically clarifying payments towards expenses of transponders
- With the withdrawal of Circular 23 clarity is required in respect of non resident company selling goods from abroad to its Indian subsidiary

Indirect Taxation

- There is no system to procure services by EOU's without payment of service tax. A change in service tax regulations facilitating such a move would help the service sectors in telecom to a large extent. Alternatively, expedite the process of Service tax refunds
- There is no clarity towards reimbursement of expenses, other than commission, in respect of advertisement services, with respect to applicability of service tax
- There is a need to relook into the provisions of Cenvat Credit Rules so as to grant relief from Additional Customs Duty (ACD) either by providing the credit of such duty paid, or grant a complete exemption of ACD for the telecom sector
- Taxability of coupons sold over the counter or by e-recharge needs to be clarified – is it goods or a service?

Direct Tax Proposals

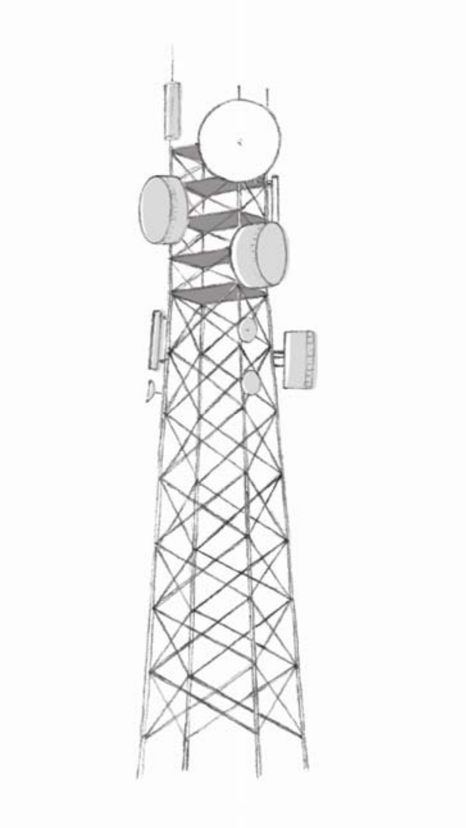
There are no Direct Tax proposals specifically affecting the Telecom industry. However, some changes applicable to all companies in general will apply to this sector as well

- Increase in MAT from **15% to 18%**
- Reduction in surcharge from **10% to 7.5%** - Gradual reduction in effective corporate tax rate lifts the business sentiment
- But Government's increasingly aggressive posturing on international tax matters by emphasising Source rule under Section 9 may make imports costly if the foreign vendors pass on the additional India compliance and tax cost to the Indian buyers

Indirect Tax Proposals

Customs

- Parts for manufacturing battery, charger and headphone of mobile phones exempt from basic customs duty, additional duty of customs and special additional duty
- Import of mobile phones for retail sales exempt from special additional duty



Expert Viewpoint

- Encouraged by the growth in manufacturing in the telecom sector and coupled with increased teledensity, introduction of new services and technological innovation, the government has realised the potential this sector has and therefore provided impetus for further growth

- Expect cost of mobile phones to further reduce on account of the exemptions in basic customs duty, additional and special additional duty

- Cheaper mobile phones could spur rural wireless connectivity and also help easier roll out of technology enabled services like 3G

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