

2G scam: another blow for India investors?

By Pauline Renaud

The Indian parliament recently ended its winter session without passing any legislation. The reason for the legislative deadlock: the 2G scandal.

For weeks, opposition lawmakers blocked parliamentary proceedings, asking for a comprehensive probe into the allocations of underpriced 2G spectrum in 2008 and allegations of favouritism.

This started in November when a report from the Comptroller and Auditor General of India (CAG), the government's auditor, explained that the 2G scam caused a Rs1.76trn (US\$40bn) loss to the government, after licences were sold to mobile operators based on a price determined in 2001.

The conclusions of the report claimed the head of former telecom minister A. Raja who was replaced by Kapil Sibal. But other officials were also reportedly also involved in the scam.

In the meantime, the Telecom Regulatory Authority of India (Trai) argued that some operators that received licences in 2008 did not meet their roll-out obligations, which include covering at least 10% of the district headquarters within 12 months of receiving licences.

Others reportedly did not fulfil certain eligibility requirements – such as meeting share capital minimums. Some experts claim that licences were sold so cheaply that it actually encouraged bad behaviour.

"The government is under intense pressure to take some decisive action. But determining the right penalty to impose is going to be challenging," explained Mahesh Uppal, telecoms analyst, director of Com First (India).

Trai has recommended cancelling as many as 38 telecom licences held by Aircel, Dishnet Wireless, Etisalat DB, Loop Telecom, Sistema Shyam Teleservices and Unitech Wireless. Another 31 licences might be examined, which could lead to further cancellations.

"Cancellations would be a really tough solution but it might happen in some cases. In particular for the operators that both didn't fulfil eligibility requirements and didn't meet their rollout obligations," according to Kunal Bajaj, director India, Analysys Mason.

It remains unclear whether the government will follow those recommendations but in early December, Sibal said that the telecom ministry would soon be sending notices to the companies asking them to explain why their licences should

not be cancelled. After receiving the letters, companies will have two months to respond.

"I wouldn't be surprised if they decided to go ahead with some cancellation, as the country has lost a lot of money in the 2G scam – and the government reports make clear that at least some operators knew they were doing something wrong to obtain licences," said Glenn Gerstell, head of the global telecoms practice at international law firm Milbank, Tweed, Hadley & McCloy.

"India as well as other countries have gone back and fixed irregularities in licence awards, so a re-auction of spectrum is definitely possible," he added.

Besides potential cancellations, the government might also decide to impose some fines. It was recently reported that a few Indian and foreign mobile companies may have to repay up to US\$1bn each for additional spectrum they received in 2008.

In the meantime, an investigation into the country's licence attribution process to see what went wrong is ongoing. "The Indian Parliament is still to make headway over the issue of a Joint Parliamentary Committee probe into the 2G spectrum scam. But The Central Bureau of Investigation recently told the Supreme Court in an affidavit that it will soon wrap up its investigations and file the charge sheet within a month thereafter," explained Ravishankar Raghavan, a principal in the tax group at Indian law firm Majmudar.

However, it could take another 9-12 months before the 2G saga comes to an end, with potential cancellations expected to take some time to go into effect.

More worrying than the penalties themselves is the actual signal they send to foreign companies, analysts argue. "India still remains a very attractive country for investment with strong fundamentals. This should not be overlooked. But the country has had a mixed record in terms of foreign investments because of its regulatory framework and concern over speedy judicial resolution. Most foreign companies know they have to be much more careful now when looking at deals in India," explained Gerstell.

After the Vodafone tax case, the 2G scandal will be seen as another glaring uncertainty. Although it might not act as a deterrent, telcos are expected to be constantly looking over their shoulder to make sure they haven't fallen foul of the law.