

Chapter V

Revenue shared by M/s Reliance Communications Limited and M/s Reliance Telecom Limited

5.1 Brief Profile of M/s Reliance Communications Limited (RCL) and Reliance Telecom Limited (RTL).

Reliance Infrastructure Developers Private Limited was incorporated on 15 July 2004 as a private limited company. During July-August 2005, the company changed its name to Reliance Communication Ventures Limited (RCoVL) and converted into a public limited company. In March 2006, RCoVL merged with Reliance Infocomm Limited (RIC) which had originally obtained telecom licences in 1997 and renamed as Reliance Communications Limited (RCL) (June 2006).

Reliance Telecom Limited (RTL) was incorporated on 1 March 1994.

5.1.1 Licences granted to RCL and RTL

RIC obtained its first licence for Basic Services (Basic licence) in Gujarat in September 1997 and basic licences in eighteen¹ more LSAs in July 2001. These basic licences migrated to UASL in November 2003. It obtained UASL for Jammu and Kashmir in September 2004. Thus by September 2004, RCL (formerly RIC) held UASL in all LSAs except Assam and North East. It also obtained NLD and ILD licences in January-February 2002.

RTL obtained original CMTS licences in seven² LSAs in December 1995 (migrated to UASL in October 2007) and acquired one more CMTS licence in Kolkata in September 2001 (migrated to UASL in April 2009). Thus, both RCL and RTL were simultaneously holding UAS and CMTS Licences respectively in six LSAs of Bihar, HP, MP, Kolkata, Orissa and WB.

Reliance Communications Infrastructure Limited (RCIL) and Reliance WiMax Ltd, both subsidiaries of RCL, hold ISP licences and another subsidiary, Reliance Infratel Ltd (RITL) (Formerly in 2006-2007 known as Reliance Telecom Infrastructure LTD (RTIL)) had registration for IP-I services.

5.1.2 Spectrum allotted to RCL/RTL

Initially RCL was a CDMA operator whereas RTL was a GSM operator. In 2008, RCL obtained GSM spectrum and RTL got CDMA spectrum and hence they provide services on dual technology³. LSA wise spectrum allotted to RCL/RTL as on 31 March 2010 was as follows:

- 1 AP, Bihar, Delhi, Haryana, HP, Karnataka, Kerala, Kolkata, MP, Maharashtra, Mumbai, Orissa, Punjab, Rajasthan, Tamil Nadu, UP (E), UP (W), WB,
- 2 Assam, Bihar, HP, MP, NE, Orissa, WB.
- 3 Though RTL obtained CDMA spectrum but it didn't provide services using CDMA spectrum.

Table 5.1

Reliance Communications Limited			
Sl.No.	Technology	Spectrum	Licenced Service Area
1	GSM	2 × 4.4 MHz	Andhra Pradesh, Delhi, Gujarat, Haryana, J&K, Karnataka, Kerala, Maharashtra, Mumbai, Punjab, Rajasthan, TN, UP(E) and UP(W)
2	CDMA	2 × 5 MHz	Andhra Pradesh, Bihar, Delhi, Karnataka, Kerala, Kolkata, MP, Maharashtra, Mumbai, TN, UP(E) and UP(W)
3	CDMA	2 × 3.75 MHz	Gujarat, Haryana, Orissa, Punjab, Rajasthan, WB
4	CDMA	2 × 2.5 MHz	HP, J&K
Reliance Telecom Limited			
1	GSM	2 × 8 MHz	Bihar
2	GSM	2 × 6.2 MHz	HP, Assam, MP, Orissa, Kolkata, NE, WB
3	CDMA	2 × 2.5 MHz	Assam, NE

5.1.3 Subscriber base of RCL/RTL

RCL provides both wireless and wireline services whereas RTL provides only wireless services. Wireless subscribers of RCL/RTL increased from 2.80 crore as on March 2007 to 10.24 crore as on March 2010 and wireline subscribers of RCL increased from 0.06 crore to 0.12 crore during the period. The market share of Reliance Group was 14 *per cent* as on March 2007 which increased to 17 *per cent* as on March 2010.

5.1.4 Gross Revenue (GR), Deduction, Adjusted Gross Revenue (AGR) reported and revenue share paid by RCL/RTL

As brought out in Para 1.5, Telecom Service Providers are required to pay LF and SUC at a percentage of AGR on quarterly basis on self-assessment basis. The GR, Deductions and AGR of RCL/RTL for the years 2006-07 to 2009-10 are as shown in the table below.

Table 5.2

(₹ in crore)

Year	GR	Deductions	AGR	Percentage of AGR to GR	Revenue Share (LF + SUC)
2006-07	14264	4229	10035	70.35	1043
2007-08	16997	5158	11839	69.65	1229
2008-09	17507	5557	11950	68.26	1249
2009-10	17392	6000	11392	65.50	1163
Total	66160	20944	45216	68.34	4684

5.1.5 Arrangement between RCL and its subsidiary RCIL for Value added Services, Selling/Marketing and Billing:

RCL and its subsidiary RCIL entered into Value Added Services (VAS) and Selling/Marketing agreements as detailed below to carry out their business:

i) Value Added Services (VAS) agreement:

Reliance Communications Infrastructure (RCIL) is a subsidiary having 'A' category ISP licence and is in the business of providing internet, miscellaneous applications, content and other allied services under the brand names R Connect, R World, Reliance World, 1234, 2345 and SMS content services. An agreement was signed between RCL (UAS Licence holder) and RCIL in April 2006 for three years and was subsequently extended up to March 2012.

As per this agreement, RCIL was to provide all the above services to RCL's subscribers and RCL would provide the access services required to facilitate the same.

'R Connect' is an internet service and the same is provided to RCL subscribers through dial up. As per the agreement, the revenue was to be shared between RCIL and RCL for 'R Connect' services.

'R world' is a one-stop-shop for applications and content which include mobile TV, videos, games, cricket updates, music and ring tones, etc. As per the agreement, revenue was to be shared between RCL and RCIL for applications and content services (including 'SMS' or 'MMS' based applications and content services).

ii) Selling and marketing agreement:

RCIL also entered into a selling and marketing agreement with RIC (subsequently RCL) in October 2004 valid up to September 2007. This agreement was renewed in October 2007 between RCIL and RCL for a further period of 3 years.

The term 'business' was defined under Section I of the agreement as the means of marketing of RCLs services or various tariff plans relating to telecommunications services offered by RCL including fixed wireless terminals/fixed wireless phones, etc., and any other services to be provided by RCL from time to time.

Clause 2.3 stated that while marketing the services, RCIL was free to bundle the tariff plans of RCL with other products or services as it deemed fit and offer composite schemes to customers.

Clause 2.4 stated that RCIL, if required could enter into agreements with distributors, retailers or any other person for promotion of the schemes and services.

As per Clause 2.8, nothing contained in the said agreement shall deem RCIL to be a telecom service provider and in no circumstances shall RCIL be a reseller of RCLs services.

Under Clause 3.9, RCIL shall on behalf of RCL, bill and collect the amount due from RCL's subscribers. For this purpose, RCIL shall procure and install all billing and other software and necessary infrastructure as directed by RCL from time to time.

The fees for the marketing, billing and collection were detailed in Clauses 7.1 and 7.2 of the agreement. Thus through this arrangement RCL effectively diverted a significant non determinable portion of revenue to a subsidiary resulting in avoidance of payment of LF and SUC on such diverted revenues.

5.2 Under reporting of Gross Revenue in the books of accounts of Reliance Communications Limited (RCL)/Reliance Telecom Limited (RTL)

As mentioned in para 1.4 (a), the GR shall be inclusive of all types of revenue stated therein without any set-off for related item of expense, etc, and as brought out in Para 1.5, service revenue (amount billable) shall be shown gross and details of discount/rebate indicated separately.

Audit examination of records/books of accounts of RCL/RTL and its related subsidiaries revealed that these companies had not adhered to the provisions of the licence agreement as discussed in following paragraphs.

5.2.1 Booking of Prepaid Revenue net of Free Air Time/Commission by RCL/RTL

Audit examination of records/books of accounts of RCL/RTL for the years 2006-07 to 2009-10 revealed that

- Free Air Time (FAT) given to subscribers was not accounted for in the financial systems at all.
- Revenue accounted was net of commission given to distributors/agents which was in violation of the licence agreement.

On being pointed out by audit, Management replied that

- Tariff means rates and related conditions w.r.t. rentals, deposits, installation fee, free call usage charges and any other related fees or service charge. This shows that while any tariff was introduced, it was essential that tariff should include details of free minutes. As free minutes were not chargeable and billable, same cannot be considered for revenue. Company are not generating any revenue from such free minutes hence no question of any revenue/business promotion expenses does arise.
- Free talk time/free air time were not in nature of discounts and rebate hence there was no need to account for or to show the same in accounts. It's a service to subscriber free of cost and no revenue was earned from free talk time/free air time and hence cannot be considered as rebate/discount.

- Hence such minutes were eliminated in billing cycle for charging to subscriber as the same were offered free of charge to subscribers.
- Considering value of free talk time/free air time was not correct. TDSAT also vide its judgement dated 23 April 2015 very categorically held that inflow should be real and income should not be notional.
- In this case no real inflow to the Company and no value was earned by the Company; hence it was justified not to include free minutes in billing to subscribers.

The reply of the management is not tenable as –

- Free talk time/free airtime over and above the tariff plans submitted by the Company to TRAI was in the nature of business promotion activity, cost of such offers amount to expenses. Further in view of provisions of UASL agreement, service revenue should be shown in gross without any set off. It should be booked separately in the books of accounts and should not have been eliminated at “Mediation level⁴”. While noting that the TDSAT judgment dated 23 April 2015 referred by the Management in its reply has been challenged in the Hon’ble Supreme Court by DoT in July 2015, Audit is of the view that elimination of free talk time at mediation level itself and not showing it in books of accounts was in violation of the licence agreement.
- Similarly, netting off of commission given to distributors/agents was also in violation of the agreements.

Though DoT was aware of the accounting of RCL/RTL through the notes/schedules of annual reports, no action was found to be taken to prevail upon the Company to furnish the GR as mandated in the Annexure III of the licence agreement.

5.2.2 Booking of revenue by RCL net of commission given to its subsidiary (RCIL) and booking of revenue in the subsidiary (RCIL) books of accounts instead of RCL’s accounts

Reliance Communications Infrastructure Limited (RCIL) which had got Category “A” ISP licence was a wholly owned subsidiary of RCL during the years 2006-07 to 2009-10. As detailed in para 5.1.5, RCL and RCIL entered into agreements for providing Value Added Services (VAS) to RCL’s subscribers and Selling/ Marketing products of RCL by RCIL. Consequent to these agreements, revenue from VAS was accounted in the books of RCIL and only a portion of the total revenue was passed on to RCL. By this arrangement, RCL paid LF only on the portion of revenue passed on by RCIL and not on GR earned from subscribers of VAS which was in violation of the licence agreement.

⁴ A mediation device is a network component in Telecom network that receives, processes, reformats and sends information to other formats between network elements and are commonly used for Billing and Customer Care systems.

Also, the revenue earned towards sale of handsets working under CDMA technology which cannot be independent from telecom service, Subscriber Identity Module (SIM) cards and installation charges from subscribers which were essential telecom services, was accounted in RCIL's books of accounts. Total understatement of GR by RCL owing to its arrangement with its subsidiary (RCIL) worked out to ₹ 5594.63 crore. The income booked in the RCIL's accounts instead of RCL's has been apportioned among the UAS licences on the basis of percentage of GR for calculation of impact on short/non-payment of LF and SUC on the basis of rates applicable for respective service areas. Audit considers this to be the most suitable and conservative method of determining the under reporting of revenue share.

Details are furnished in following paragraphs:-

(A) Commission/discount paid to RCIL by RCL for selling and marketing of its services netted off from its revenue for computation of GR/AGR.

As per the marketing agreement between RCL and RCIL, RCIL was an agent and authorized person for selling the product of RCL. As per the agreement, RCL would sell the prepaid vouchers to RCIL at the rate as agreed from time to time and RCIL would sell the same to its distributors at the same net price.

From the books of accounts of RCIL for the period from 2006-07 to 2009-10, it was found that the discount/commission received by RCIL from RCL amounting to ₹ 1170.51 crore for selling its product was shown as "Billing Income" which was in turn the commission paid to the distributors by RCIL. However, RCL had netted off the commission/discount paid to RCIL on sale of prepaid cards and only the net realized value was accounted as revenue that was considered for AGR.

The value of commission/discount given to distributors/agents for sale of pre-paid products (SIM cards/recharge vouchers) was to be treated as business expenses by RCL and the gross value of the prepaid cards i.e. the value of the telecommunications service being provided by the operator (RCL) was required to be considered as revenue without any set off.

On being pointed out by Audit, it was replied by the management that-

- The arrangement was principal to principal. The invoices were issued to the distributor on agreed price and the same is considered as revenue.
- Inclusion of notional income in the form of discount on prepaid vouchers in AGR was not tenable. Only realized value to be considered in the AGR.

The reply of the management is not tenable as

- RCIL was an agent of RCL under a marketing agreement and as clearly mentioned in the agreement, RCIL shall not be deemed to be a telecom service provider and in no circumstances RCIL be a reseller of RCLs services. The transaction between

RCIL and RCL were in the nature of distributor acting on behalf of the company and in substance there exists a principal to agent relationship only as explained in para 3.2.1 (A).

- Discount paid on prepaid vouchers was not a notional income as stated by the Management in its reply. Discount paid was marketing expenses.

While the matter is *sub-judice* at Hon'ble Supreme Court, Audit view is that netting of commission/discount paid to RCIL on sale of prepaid cards was against the UAS licence agreement and hence GR/AGR of RCL for the years 2006-07 to 2009-10 was understated by ₹ 1170.51 crore resulting in short payment of LF and SUC by ₹ 106.88 crore and ₹ 30.88 crore respectively (**Annexure - 5.01**).

(B) Non consideration of gross value of revenue on account of R world and SMS content services in the GR/AGR of RCL

As mentioned in para 1.4 (a), the GR shall be inclusive of revenue from VAS along with other revenues stated therein without any set-off for related item of expense.

RCL provides telecommunication services under UASL. RCIL, a wholly owned subsidiary of RCL, having ISP licence provided internet, miscellaneous content and other allied services under the brand names 'R Connect', 'R world', 'Reliance world', '1234', '2345', and 'SMS content services'. As stated in para 5.1.5, RCL and RCIL have entered into agreement for providing VAS to RCL subscribers.

On scrutiny of the books of accounts of RCIL and RCL, it was observed that as against revenue from RCL's subscribers on account of VAS (R World and SMS content services) amounting to ₹ 1273.45 crore booked in the accounts of RCIL, only ₹ 265.58 crore was passed on to RCL. Hence ₹ 265.58 crore only was considered in GR/AGR of RCL for computation of revenue share.

On being pointed out by audit it was replied by the Management that VAS (R world and content SMS) providers are neither regulated nor licenced and they mainly act as channel partners to mobile network. RCIL had paid relevant access charges to RCL on which RCL had already paid the licence fee and hence question of additional licence fee does not arise.

The reply of the management is not tenable as R World and SMS content services are varied bundle of VAS over SMS, voice etc. When the content delivery was not over the internet but over SMS and voice etc., the same was not within the scope of ISP licence held by RCIL. VAS to subscribers could be provided by only UAS/CMTS licensee. Hence, the GR from subscribers on account of VAS should be booked in RCL's accounts and to be included in the GR for computation of revenue share. Any amount payable to RCIL, being VAS/ content service provider, should be charged to expense in RCL's accounts.

Hence, the revenue of ₹ 1007.87 crore (₹ 1273.45 – ₹ 265.58) should have been included in GR/AGR by RCL.

The Impact on short payment of LF and SUC on this account was ₹ 91.99 crore and ₹ 26.76 crore respectively (**Annexure - 5.02**).

(C) Non-inclusion of revenue from Caller Ring Back Tones for computation of GR/AGR by RCL.

Caller Ring Back Tones (CRBT) is a type of VAS that was introduced by RCL for its subscribers and intimated to TRAI (May 2006). As explained in above paragraph, revenue from VAS should be included in GR/AGR.

On scrutiny of the books of accounts of RCIL and RCL for the years 2006-07 to 2009-10, it was observed that the revenue of ₹ 540.84 crore pertaining to CRBT was booked in RCIL's books of accounts. No revenue from CRBT was found to be booked in RCL's books of accounts. Thus, non accounting of ₹ 540.84 crore in the books of RCL resulted in under reporting of GR/AGR.

On being pointed out by Audit, it was replied by the Management that the CRBT service was introduced by RCL for its subscribers in May 2006 for only one month on promotional basis. When this service was launched on commercial basis, the same was provided by RCIL under VAS/content services (R World services). RCIL was providing content services on standalone basis as separate legal entity. No licence is required to provide content services.

The reply is not tenable as CRBT is a VAS provided over SMS and voice, etc. and Audit opines that this could be provided only by UASL/CMTS licensee. Thus revenue from CRBT (VAS) should be included in GR for computation of revenue share.

Hence, the revenue of ₹ 540.84 crore from CRBT should have been included in GR/AGR by RCL. The impact on short payment of LF and SUC on this account was ₹ 49.34 crore and ₹ 14.40 crore respectively (**Annexure - 5.03**).

(D) Non-inclusion of revenue from sale of SIM cards for computation of GR/AGR by RCL.

As stated in para 5.1.5, RCIL, a wholly owned subsidiary of RCL and having Category "A" ISP licence entered into an agreement with RCL for selling/ marketing products of RCIL.

During the course of audit of accounts of RCL and RCIL for the years from 2006-07 to 2009-10, it was found that the revenue from sale of SIM cards amounting to ₹ 103.17 crore were booked in the accounts of RCIL for the years 2008-09 and 2009-10.

SIM card is an integral part of telecom services without which service cannot be activated. SIM cards cannot be sold as goods, independent from the services provided by the UAS licensee. SIM cards on its own without the services would hardly have any value. Further, even in terms of selling and marketing agreement between RCIL and RCL, RCIL was not a telecom service provider and in no circumstances RCIL would be a reseller of RCL's services.

Hon'ble Supreme Court of India in its judgment dated 4 August 2011, in an appeal by IDEA Mobile Communications Ltd. versus Commissioner of Central Excise and Customs, Cochin held that the amount received by the cellular company from its subscribers towards SIM card would form part of the taxable value for levy of service tax, for the SIM cards were never sold as goods independent from services provided.

In view of all the above facts, the value of SIM cards sold should form part of the GR of RCL who was a telecom service provider and not with RCIL, an ISP licence holder and a subsidiary of RCL.

The impact of short payment of LF and SUC on this account was ₹ 9.40 crore and ₹ 2.69 crore respectively (**Annexure - 5.04**).

Reply to an Audit observation issued to the company (May 2015) in this regard was awaited (January 2016).

(E) Non-inclusion of revenue from sale of handsets for computation of GR/AGR by RCL

As mentioned in para 1.4 (a), the GR shall be inclusive of sale proceeds of handsets (or any other terminal equipment etc.), along with other revenues stated therein without any set-off for related item of expense.

As stated in para 5.1.5, RCIL, a wholly owned subsidiary of RCL and having category "A" ISP licence, had entered into an agreement with RCL for selling/ marketing products of RCIL.

During the course of audit of accounts of RCL and RCIL for the years 2006-07 to 2009-10, it was found that the revenue from sale of CDMA handsets amounting to ₹ 2523.95 crore were booked in the accounts of RCIL for the years 2006-07 to 2009-10. No revenue on account of sale of handsets was booked in RCL.

It was observed from the tariff plans submitted to TRAI during April/June 2006 that RCL offered bonus talk time to prepaid customers on selected handsets (CDMA) models. Further, internal correspondences within the Company during 2006, 2007 and 2009 showed that the handsets were bundled with schemes offered by RCL.

On being pointed out by Audit, it was replied by the Management that-

- RCL was not dealing in handset sale. All sales are by RCIL through its distributors/dealers and not to any customers.
- No free minutes are given by RCIL to the distributors/dealers. RCL provides free promotional minutes on activation by the subscribers as a promotional offer. Since these are free minutes, no revenue was accrued to RCL.
- Sale of handsets does not require any telecom licence. RCIL had not done bundling as RCIL had not shared any handset revenue with RCL.
- As per August 2007 judgment of TDSAT, 'bundling of telecom services will mean that if somebody buys from a company and that company give concession in services or reduce monthly rental'.
- As per Hon'ble Supreme Court verdict, it is open to the licensees not to undertake activities for which they do not require telecom licence and shall transfer these activities to any other person, firm or company.

The reply is not tenable as-

- Though RCIL sold the handsets on behalf of RCL as per the marketing agreement entered between them, sale of handsets and rendering of services under the CDMA technology were not independent activities but an integral part of telecom activity under UAS Licence. Hence sale of handsets (CDMA) by RCIL in the guise of selling and marketing agreement between it and its holding company RCL could not be termed as an independent non licenced activity. Hence the entire revenue on sale of handsets should be considered for revenue sharing.
- RCL provided various concessions to the customers/distributors and bundled the services and RCIL is only selling the handsets on behalf of RCL as per the marketing agreement.
- Audit is not stating that sale of handsets was a licenced activity but contends that under CDMA technology, sale of handsets and rendering of services were inseparable.
- TDSAT judgment of August 2007 was set aside by Hon'ble Supreme Court in October 2011.

Hence, the revenue from sale of handsets (CDMA) of ₹ 2523.95 crore should be included in the GR/AGR of RCL. The impact on short payment of LF and SUC on this account was ₹ 231.64 crore and ₹ 64.51 crore respectively (**Annexure - 5.05**).

(F) Non-inclusion of revenue from installation charges of Fixed Wireless Phone/Terminal (FWP/T) in subscribers' premises for computation of GR/AGR by RCL.

As mentioned in para 1.4 (a), the GR shall be inclusive of installation charges along with other revenues stated therein without any set-off for related item of expense.

From scrutiny of the books of accounts of RCL and RCIL for the period from 2006-07 to 2009-10, it was observed that the revenue on account of installation charges of FWP/T at the subscribers' premises amounting to ₹ 248.29 crore was booked in the accounts of RCIL.

FWP/T instruments were integral to the provision of telecom service to be provided by RCL to its subscribers. Since RCL was a UAS licensee, the revenue of ₹ 248.29 crore pertaining to instrument cost, installation and upfront charges received from the subscriber should be part of GR of RCL.

On being pointed out by Audit, it was replied by the Management that-

- RCL entered into an agreement with RCIL for providing FWP/T installation services. RCIL provides services of installation of the instruments at subscriber's premises for which RCIL receives amount directly from the subscriber. It was carried out by RCIL at its own risk. Therefore, revenue accrued from this activity rightly belongs to RCIL. The activity of installation can be undertaken by anybody i.e. even by the persons who do not have any telecom licence. TDSAT in its judgment in May 2010 held that the installation charges are given back to the person who does the installation work and hence it would not come in the purview of AGR.
- As per Hon'ble Supreme Court judgment, it was open to the licensees not to undertake activities for which they do not require licence.

The reply of the management is not tenable-

- As it is evident from the letter dated 1 April 2006 from RIC to RCIL that the FWP/Ts were the property of RIC (later changed into RCL) and it had requested RCIL to install it in the premises of the subscriber. Though RCIL could undertake the job of installation of FWP/T but it would be only an agency function and in terms of UASL agreement, GR from subscribers for installation of terminal equipment (FWP/T) should be revenue of UAS licensee (RIC/RCL) and charges payable to installation agency (RCIL) should be expense of the licensee. TDSAT judgment of May 2010 referred in management reply is not related to telecom operators but related to Direct to Home (DTH –related to TV broadcast) operators.
- Audit does not question who was undertaking the activity but contends that revenue from installation charges of FWP/T should be considered for Revenue Share in accordance with Licence Agreement.

Hence, the entire revenue of ₹ 248.29 crore accounted in RCIL's books on account of installation of FWP/T should have been taken to the GR/AGR of RCL. The impact on short payment of LF and SUC on this account was ₹ 22.71 crore and ₹ 6.50 crore respectively (**Annexure - 5.06**).

5.2.3 Netting of commission from the revenue by RCL for computation of GR/AGR

On scrutiny of the records furnished by RCL, it was noticed that the commission paid on broadband prepaid vouchers amounting to ₹ 1.11 crore was netted off from the revenue and the net revenue was booked in the accounts of RCL.

On being pointed out by audit, it was replied by the Management that it was just the discount given on prepaid vouchers which was netted off with the GR and was not liable to LF payable to GOI.

The reply of the Management is not tenable as netting of commission from revenue was not in conformity with the licence agreement. The impact on short payment of LF and SUC on this account was ₹ 0.09 crore and ₹ 0.03 crore respectively (**Annexure - 5.07**).

5.2.4 Netting of revenue earned from channel partners/Franchisees from expenses for computation of GR/AGR by RCL

On scrutiny of the books of accounts of RCL for the years 2006-07 to 2009-10, it was noticed that the income from the provision of broadband connectivity to channel partners/franchisees amounting ₹ 4.50 crore were credited to expense heads. This resulted in non-consideration of the revenue in the GR/AGR.

On being pointed out, it was replied by the Management that the adjustments involve setting off reimbursement of one cost, viz. cost of access from another cost viz. commission payable by the Company. It was not a case where an item of revenue and an item of cost were netted off so that revenue was recorded short or not recorded.

The reply is not tenable as the franchisees were paid commission for their activities. While cost of access actually was a cost to the franchisee and revenue to the licensee, on the other hand commission payable by company was an expense of licensee. Therefore contrary to licensee's claim, it was indeed pairing off an item of revenue with an item of cost.

The impact on short payment of LF and SUC on this account was ₹ 0.42 crore and ₹ 0.12 crore respectively (**Annexure - 5.08**).

5.2.5 Netting of revenue by discount given to distributors/dealers/franchisees on sale of prepaid products for computation of GR/AGR by RTL

As per the Accounting Policy of Reliance Telecom Limited (RTL) for the year 2006-07 "Revenue is recognized as and when the services are provided on the basis of actual usage of the company's network." This policy was revised for the years 2007-08 to 2009-10

which states that Revenue from telecommunication services is recognized on the basis of actual usage of the company's network in accordance with contractual obligations and is stated net of taxes and trade discounts.

It was observed during audit that a sum of ₹ 11.95 crore (₹ 10.69 crore in respect of RTL and ₹ 1.26 crore in respect of Reliable Internet Services Limited (RISL) which later merged with RTL in September 2007), was shown under expenses as discount granted to distributors/dealers/franchisees for sale of prepaid cards and recharge vouchers for the first quarter of 2006-07. However, this discount was netted off with the "Billing Revenue" in the Annual Accounts of the Company and also with the GR in the AGR statement (for the year 2006-07).

From 1 July 2006 onwards, the revenue on sale of prepaid cards and recharge vouchers was accounted net of discounts given to distributors/dealers and the netted off revenue only was considered for GR/AGR instead of including the gross value.

Based on the amount of discount booked and corresponding prepaid revenue (net) submitted under AGR statements for eight LSAs of RTL/RISL for the quarter I of 2006-07, the quantum of discount was projected by audit for the years 2006-07 (for quarter II to IV), 2007-08, 2008-09 and 2009-10. Total amount of discount netted off from revenue for the years 2006-07 to 2009-10 worked out to ₹ 392.99 crore.

The above amount of ₹ 392.99 crore was calculated after taking into account the ratio of discount to prepaid revenue (net) booked for the first quarter of 2006-07 as the booking of discount was dispensed with from the second quarter of 2006-07 onwards by the company.

On being pointed out by Audit about the netting of discount from revenue, it was replied by the Management that-

- The revenue from prepaid voucher was recognized net of discount. The arrangement with distributors was Principal to Principal. The invoices were issued to distributor on agreed price and the same was considered as revenue. Only realized revenue was to be considered in the AGR.
- Over a period of time various ranges of prepaid products were launched and applying same ratio for all years was not correct.

The reply of the management is not tenable in view of audit explanation given in para 3.2.1 (A). Regarding projection of amount of discount by Audit, since the Company dispensed with the booking of discount from the second quarter of 2006-07 and also the details of the actual GR figures was not disclosed either to the DoT or Audit, therefore, Audit had to take recourse to the application of the ratio of discount to prepaid (net) pertaining to the quarter I of 2006-07 to project the amount of discount for the quarters II to IV of 2006-07 and for the years 2007-08 to 2009-10.

While the matter is *sub-judice* at Hon'ble Supreme Court, Audit view is that netting of commission/discount paid to distributors/dealers on sale of prepaid products was against the UAS licence agreement and hence GR/AGR of RTL for the years 2006-07 to 2009-10 was understated by ₹ 392.99 crore resulting in short payment of LF and SUC by ₹ 25.72 crore and ₹ 14.04 crore respectively (**Annexure - 5.09**).

5.2.6 Non-inclusion of value of Free of Charge (FOC) recharge vouchers given to distributors for computation of GR/AGR by RTL

Examination of the books of accounts of RTL for the period 2006-07 to 2009-10 revealed that service tax of ₹ 12.12 crore paid on free of cost recharge vouchers given to the Distributors was booked under expense as 'service tax paid – not billed'.

Also ₹ 85,218 and ₹ 11,09,799 were booked under expense as "Channel Associative –SE Incentive" for 2006-07 and 2007-08 respectively representing the service tax paid on Free Recharge coupon given to distributors. Though the service tax was paid, the gross value of FOC vouchers was not found to be included in the GR of RTL.

On being pointed out by Audit, it was replied by the Management that

- The LF was payable on realizable revenue only. No LF was payable on the notional income. Income which was not accrued to Licensee cannot be charged for LF. In the aforesaid cases, company has not earned any revenue from these vouchers and no inflow was there. Hence notional revenue from these vouchers cannot be included in the revenue of the company.
- TDSAT vide its judgment dated 23 April 2015 also held that in order to be counted as "GR", the item of inflow must not be notional but real.

The reply of the management is not tenable as

- Free recharge coupons given to distributors on which Service Tax was paid by the Company was nothing but discounts/commission paid to them. In view of explanation given in para 3.2.1 (A), commission paid to distributors should not be netted off from revenue for computation of GR/AGR. Free recharge coupons given to distributors are equivalent to cash for them as these can be sold on the basis of airtime available in the coupons.
- While noting that TDSAT judgment dated 23 April 2015 referred in reply was challenged in Hon'ble Supreme Court by DoT in July 2015, Audit is of the view that licensee instead of giving cash as commission had passed on benefit of use of telecom service for which revenue was forgone and hence it was not a case of notional revenue.

Based on the amount of service tax paid, the gross value of FOC recharge vouchers have been worked out to ₹ 87.32 crore. The impact on short payment of LF and SUC on this account was ₹ 5.70 crore and ₹ 3.00 crore respectively (**Annexure - 5.10**).

5.3 Under reporting of revenue in the Statements of Revenue and LF (AGR Statements) though reported in the books of accounts.

5.3.1 Non consideration of forex gain in GR/AGR by RCL and RTL:

In the books of accounts of RCL/RTL, total net balances under the account codes operated for booking transactions related to foreign exchange gain/loss were included in the Schedule of “Financial Charges (net)” as Foreign Currency Exchange Fluctuation (gain)/loss (net).

From quarterly GL balances of all account codes operated for accounting Forex gain for 2006-07 to 2009-10, it was noticed that out of total Realized gain of ₹ 1934.72 crore (₹ 1820.49 crore for RCL and ₹ 114.23 crore for RTL), only ₹ 600.86 crore (RCL ₹ 590.56 crore and RTL ₹ 10.30 crore) was considered by the licensee for GR/AGR in the year 2007-08. Thus realised forex gain of ₹ 1333.86 crore (RCL ₹ 1229.94 crore and RTL ₹ 103.92 crore) was not considered for GR/AGR.

It is pertinent to mention here that the above realised gain calculated from the data extracted from the reports generated from Financial System (SAP) did not represent the actual gain of that particular item since the Company recasts the value of all the items included under the foreign exchange gains/losses head every year, the matured items are accounted under realised gains and the un-matured items remain under unrealised gain. Thus, the realised gain of a particular item in that year would not be the actual gain due to accounting of the gains /losses of that item during the intermediate period under unrealised. Audit could not arrive at the actual value of items accounted under realised gain every year for want of original value of each item. Further, audit has considered the quarterly net gain, head of account-wise and LSA-wise, as it was not possible for audit to segregate/collect the figures of gains only from the data made available. The operator should calculate the gain of each item with reference to its initial value of accounting and include the total forex gain in GR/AGR.

On being pointed out by Audit, it was replied by the Management that,

- As per the TDSAT judgment dated 30 August 2007, the said item was not considered for the calculation of LF.
- Kerala High Court in its judgment dated 10 July 2012 stated that the revenue earned from Non Telecom activities should not be included for the purpose of calculation of LF.
- AS-9 does not recognize forex gain as revenue. As per the TDSAT judgment dated 23 April 2015, the aforesaid income was not liable for LF.
- The Company, till Quarter 3 of 2008-09 was paying LF on non-Telecom revenue also and subsequently claimed refund from DoT of the LF paid on such non-Telecom revenue. The unrealized gain was notional and not liable to LF.

The reply of the management is not tenable in view of audit explanation already given in para 3.2.5. Further, regarding specific reply of the Management, Audit views are as follows:

- TDSAT judgment dated 30 August 2007 was set aside by Hon'ble Supreme Court in October 2011.
- Kerala High Court order dated 10 July 2012 is an interim order. Audit view is that since Licence Agreement provided "GR shall be inclusive of any other miscellaneous revenue, without any set-off for related item of expense, etc," and forex gain was part of Miscellaneous Revenue, this should be included in GR for computation of revenue sharing.
- TDSAT judgment dated 23 April 2015 referred in reply was challenged in Supreme Court by DoT in July 2015. While the matter was *sub-judice* at the Hon'ble Supreme Court, Audit opines that non-consideration of forex gains in the GR by the Company was a deviation from the licence conditions.

The understatement of GR by ₹ 1333.86 crore due to non - inclusion of forex gain resulted in short payment of LF and SUC ₹ 107.63 crore and ₹ 26.93 crore respectively (Annexure - 5.11).

5.3.2 Non consideration of Interest/Other income for computation of GR/AGR by RCL/RTL

As mentioned in para 1.4 (a), the GR shall be inclusive of interest, dividend and any other miscellaneous revenue along with other revenue stated therein without any set-off for related item of expense. Audit scrutiny of books of accounts of RCL/RTL revealed that Interest/other income have been partly considered for computation of GR/AGR during the period 2006-07 to 2009-10 as discussed below-

(A) Non - inclusion of interest/dividend income in GR/AGR by RCL/RTL

In respect of RCL, total interest/dividend income booked in the accounts for the years from 2006-07 to 2009-10 was ₹ 1328.40 crore, out of which ₹ 98.88 crore had been considered in GR/AGR for computation of revenue share. Thus interest/dividend income of ₹ 1229.52 crore was not considered in GR/AGR.

Similarly, in respect of RTL, total interest income booked in the accounts for the years 2008-09 and 2009-10 and income from investment in 2009-10 of ₹ 139.52 crore was not considered for GR/AGR by RTL.

The income from investment of RTL for the year 2008-09 has been commented separately under para 5.3.4 due to netting of some income with expenses.

(B) Non - inclusion of other income in GR/AGR by RCL/RTL

The total other income booked in the accounts of RCL for the years from 2006-07 to 2009-10 was ₹ 161.78 crore, out of which ₹ 81.73 crore had been considered in GR/AGR for computation of revenue share. Thus other income of ₹ 80.05 crore was not considered in GR/AGR.

Similarly in respect of RTL, the total other income (profit on sale of securities/bonds, miscellaneous, etc.) booked for the years 2008-09 and 2009-10 was ₹ 537.40 crore. Out of total other income, only ₹ 0.78 crore had been considered for GR/AGR for computation of revenue share and ₹ 536.62 crore (₹ 537.40 crore - ₹ 0.78 crore) was not considered for GR/AGR.

On being pointed out by Audit, it was replied by the Management that-

- As per the TDSAT judgment dated 30 August 2007, Licensees are required to pay a share out of the revenue generated from Telecom activity. This income was not related to Telecom Activity and so not liable for LF.
- Hon'ble Kerala High Court in its order dated 10 July 2012 restricted DoT from raising any demand for LF under which it seeks to include revenues arising from any non licenced telegraph activities.
- TDSAT in its judgment dated 23 April 2015 excluded various non telecom revenue items which have not been specifically provided in definition of GR in the Licence agreement. Hence the said income was not liable for LF.

The reply of the Management is not tenable as

- TDSAT judgment dated 30 August 2007 was set aside by the Hon'ble Supreme Court in its judgment dated 11 October 2011.
- Kerala High Court order dated 10 July 2012 referred in reply is an interim order.
- While noting that the TDSAT judgment dated 23 April 2015 has been challenged in the Hon'ble Supreme Court by DoT in July 2015, Audit is of the view that Licence agreement clearly prescribes the inclusion of interest, dividend and any other miscellaneous revenue in GR/AGR.

In view of above, non - inclusion of interest, dividend and other miscellaneous income as mentioned above in para 5.3.2 (A) and 5.3.2 (B) has resulted in understatement of GR/AGR by ₹ 1985.72 crore. The impact on short payment of LF and SUC due to under reporting of interest and miscellaneous income was ₹ 153.44 crore and ₹ 48.56 crore respectively **(Annexure - 5.12)**.

5.3.3 Interest free loan to subsidiary by RCL resulted in avoidance of payment of LF/SUC

Test check of Annual Accounts of RCL revealed that interest free un-secured loan was given to its subsidiary Champion Properties Limited (CPL) and Reliance Tech Services Private Limited (RTSPL). The accounts revealed that the loan amount at the end of 2006-07, 2008-09 and 2009-10 against these subsidiaries were ₹ 36.78 crore (CPL), ₹ 3.63 crore (RTSPL) and ₹ 15.27 crore (RTSPL) respectively. As these two companies were not wholly owned subsidiaries of RCL during these particular years, the grant of interest free unsecured loan was in violation of Section 372A of Companies Act, 1956 and not in line with the arm's length relation to be maintained between the holding and subsidiary companies.

On being pointed out by audit, it was replied by the management that as per section 372A (8) (a) (i), provisions of section 372A does not apply to any loan made by a company providing infrastructural facility. RCL being telecom service provider was exempted from the provision of section 372A. These companies were promoted to support activities of RCL and therefore it was necessary for RCL to provide financial support repayable at demand, to carry out their activity smoothly in overall interest of RCL, hence it was not prejudicial to the interest of RCL. Notional income was not liable to LF.

The reply of the management is not tenable as RCL was a telecom service provider and was not established with the object of providing infrastructural facilities and hence the exemption under section 372A (8) (a) (i) was not applicable to it. Thus, GR/AGR of RCL was lower by the amount of interest receivable and thereby short payment of LF and SUC. The impact on short payment of LF and SUC could not be quantified since the date of release of loan and period for which above interest free loan remained outstanding was not available.

5.3.4 Netting off of loss on sale of investment and non - inclusion of balance profit on sale of investment for computation of GR/AGR by RTL

As per financial statements of RTL for the year 2008-09, income from non-trade investments was ₹ 108.92 crore.

However no income on this account was considered for computation of GR/AGR.

On being pointed out, it was replied by the management that-

As per TDSAT judgment dated 30 August 2007, various revenues which were not related to telecom activities should not be included in the AGR for the purpose of LF.

Only interest/dividend income with direct nexus with the provision of telecom service merits inclusion in the AGR. The profit on sale of investments was received on borrowed funds and company was paying interest on the same. Hence it was not included in the AGR.

The reply of the management is not tenable in view of audit explanation given under para 5.3.2.

Hence, non-inclusion of profit on sale of investments of ₹ 108.92 crore has resulted in understatement of GR/AGR resulting into short payment of LF and SUC by ₹ 7.30 crore and ₹ 3.94 crore respectively to Government of India (**Annexure - 5.13**).

5.3.5 Different standards for payment of dividends - RCL

As mentioned in para 1.4 (a), GR shall be inclusive of dividend along with other revenue stated therein. This implies that licence agreement intended to include the revenue from investment (dividend) for the purpose of revenue share. An analysis of the annual accounts of RCL for the period from 2006-07 to 2009-10 indicated that its investments in the form of equity shares and preference shares in its subsidiaries and associates had increased approximately five times from ₹ 5434.42 crore in 2006-07 to ₹ 31898.30 crore in 2009-10 (**Annexure - 5.14**).

RCL was the majority shareholder in most of these subsidiaries and associates. However, RCL did not receive any return on these investments during this period in form of dividend or otherwise in spite of the fact that the total profit of these companies after tax was ₹ 708.61 crore, ₹ 668.65 crore, ₹ 1118.01 crore and ₹ 1499.98 crore during each of the years from 2006-07 to 2009-10 respectively (**Annexure - 5.14**).

It was seen in audit that RCL had adopted different standards for declaration of dividend in respect of RCL itself and for other non-licensee companies where it had investments and majority shareholdings. While RCL had declared a dividend of 10 to 17 *per cent* on face value of shares for 2006-07 and 2009-10, no dividend was declared by any of the subsidiaries and associates where RCL had a majority shareholding. While dividend paid by RCL was an expense for RCL and was not subject to LF and SUC, the dividends received by it from companies/entities it had invested in would have attracted imposition of LF and SUC as per terms of the licence agreement.

Thus non-declaration of dividend by subsidiaries and associates in which RCL had invested was not in accordance with RCL's own action of declaration of dividend and resulted in reduction of revenue of RCL and consequently lower payment of LF and SUC.

5.4 Revenue considered for Licence Fee but not considered for Spectrum Usage Charges (SUC)

5.4.1 Non consideration of revenue from sale/lease of bandwidth for computation of SUC

UASL agreement provides that “while calculating AGR for limited purpose of levying spectrum charges based on revenue share, revenue from wireline subscribers shall not be taken into account”. Further, in the format of statement of revenue and licence fee (AGR Statement) prescribed for the UASL agreement-

- Item 1 A has been prescribed to reflect the “revenue from wireline subscribers” and
- Item 8 has been prescribed to reflect the “revenue from sale/lease of bandwidth, links, R&G cases, turnkey projects etc.”

In the statement of revenue and licence fee (AGR Statement) for the years 2006-07, 2007-08, 2008-09 and 2009-10, revenue from sale/lease of bandwidth links, R&G cases, turnkey projects etc. amounting to ₹ 1588.19 crore was shown under item 8 of the statements. However, this revenue was not considered for payment of SUC though considered for payment of LF which was in contravention of the provisions of the licence agreement.

The Management replied that the UASL agreement provides for the limited purpose of levying annual royalty/SUC and the revenue from wire line subscribers shall not be taken into account. Hence, the revenue from lease line and bandwidth subscribers was not required to be added in the AGR for the purpose of calculation of spectrum charges.

Audit view on above has been brought out in para 3.4.3.

As such, above revenue of ₹ 1588.19 crore should be considered for computation of SUC. This resulted in short payment of SUC by ₹ 40.66 crore to Government of India (Annexure - 5.15).

5.4.2 Non consideration of income from investment for computation of SUC

As per AGR Statements submitted by RCL, Income from investment (item 4 of the statement) for the four quarters of 2006-07 was ₹ 70.60 crore. However, amount of ₹ 17.83 crore of fourth quarter alone was considered in the AGR for computation of SUC (CDMA) and amount for the remaining three quarters of ₹ 52.77 crore was not considered in AGR for SUC.

However in subsequent years i.e. 2007-08, 2008-09 and 2009-10, income from investments, if considered for LF, was also considered for SUC by the company.

On being pointed out by audit, the management replied that the SUC shall be payable on revenue earned from wireless subscribers only. As investment income is not wireless revenue, the inclusion of it in the AGR for SUC does not arise. It was also stated that the SUC paid on Q4 income from investment had been claimed as refund from DoT.

The reply of the management is not tenable as for the purpose of SUC, revenue from wireline subscribers only depicted in item 1A of AGR statement was to be excluded. Income from investment was to be included in item 4 of the AGR statements. In view of above, income from investment of ₹ 52.77 crore should have been considered for payment of SUC.

The impact on short payment of SUC is ₹ 0.94 crore (Annexure - 5.16)

5.5 Transfer of infrastructure assets by RCL/RTL to its subsidiary Reliance Infratel Ltd (RITL)

5.5.1 Transfer of Optic Fibre Undertaking (OFU) by RCL to RITL

Reliance Communications Limited (RCL) had transferred the assets and liabilities relating to its Optic Fibre Undertaking (OFU) to its subsidiary RITL engaged in providing Telecom Infrastructure services. This was done pursuant to the scheme of arrangement under sections 391 to Section 394 of Companies Act for the transfer of optic fibre undertaking approved by the Hon'ble High Court of Bombay on 18 July 2009 with the appointed date as 01 April 2008. The total value of the OFC Network of RCL as on 1 April 2008 was taken as ₹ 7206.42 crore as the consideration payable on account of transfer.

Profit of ₹ 3063.27 crore arising from such transfer which was arrived at by deducting net block of ₹ 4137.95 crore and capital work in progress of ₹ 5.20 crore from the consideration amount of ₹ 7206.42 crore was credited to the Profit and Loss account.

It was noticed that the Company did not include the above profit in the GR/AGR.

On being pointed out by Audit about non inclusion of profit on transfer of asset in GR/AGR, the Management replied that

- The Company was paying licence fee as per the TDSAT judgment dated 30 August 2007.
- Kerala High Court in its judgment dated 10 July 2012 stated that the non telecom revenue should not be included in the AGR for the purpose of calculation of LF. Hence the Company excluded the profit arising as a result of transfer of OFU undertaking which was not related to Telecom activities.
- The transaction was not a sale but a transfer and no actual gain was received. Also notional gain cannot be included.
- The transaction was an income and not revenue. It is clear that the connotation of 'revenue' as that received from ordinary activities of an enterprise is not endorsed by AS-9.
- The said income was not liable to licence fee as per the TDSAT judgment dated 23 April 2015.

The reply of the Management is not tenable as-

- TDSAT judgment dated 30 August 2007 was set aside by the Supreme Court in its judgment dated 11 October 2011.
- Kerala High Court order dated 10 July 2012 was an interim order.

- RCL and RITL were two different legal entities and hence transfer of asset from RCL to RITL is the disposal of assets and the company itself has recognised the profit on disposal of its assets in its profit and loss account.
- Profit on transfer of OFU by RCL to RITL, though not endorsed as revenue under AS-9, it should be included in GR/AGR for computation of LF and SUC as per licence agreement.
- While noting that the TDSAT judgment dated 23 April 2015 has been challenged in Supreme Court by DoT in July 2015, Audit is of the view that gains on account of transfer of OFC network was part of Miscellaneous Revenue and thus, was to be included in GR in accordance with licence agreement.

Hence, in view of licence agreement, the profit of ₹ 3063.27 crore credited to the Profit and Loss account should also have been taken to GR/AGR. The impact on short payment of LF and SUC was ₹ 279.27 crore and ₹ 81.37 crore respectively (**Annexure - 5.17**).

5.5.2 Transfer of passive infrastructure by RCL/RTL to its subsidiary (RITL) at ‘nil’ value

Reliance Infratel Limited (RITL), a subsidiary of Reliance Communications Limited (through Reliance Communications Infrastructure Limited (RCIL)), was incorporated in 2001 as a private limited company. Reliance Communications Limited (RCOM) had filed a Scheme of Arrangement⁵ with the High Court of Judicature at Bombay on 5 December 2006 for the separation of its wireless towers assets owned by RCOM and its wholly owned subsidiary Reliance Telecom Limited (RTL). The High Court’s approval was received on 16 March 2007 and the scheme became effective from 10 April 2007. Pursuant to the scheme, the passive infrastructure assets of RCL and RTL having book value of ₹ 3200.74 crore and ₹ 866.80 crore respectively were transferred to RITL at ‘nil’ value. RITL recorded⁶ the value of assets transferred from RCL and RTL at fair value of ₹ 3327.46 crore and ₹ 1188.36 crore respectively.

RCL, RTL and RITL, being separate entities and also RITL was not a fully held subsidiary of RCL/RTL⁷, transfer of assets was not a transaction at arm’s length. As the market value of the assets transferred from RCL and RTL were ₹ 3327.46 crore and ₹ 1188.36 crore respectively, as revalued by RITL, the difference between the book values and the values as accounted by RITL were profits foregone on transfer of asset. Amount of profits foregone by RCL and RTL were ₹ 126.72 crore and ₹ 321.56 crore respectively in the year 2007-08. In view of licence agreement, these profits foregone on transfer of asset should be considered for computation of LF and SUC.

5 under sections 391 to section 394 of the Companies Act, 1956, for the transfer of passive infrastructure of RCL and RTL to RITL.

6 in its books of accounts for the year 2007-08.

7 RCL was holding only 79.71 per cent of the Share in RITL as on 31 March 2008.

On being pointed out by Audit, it was replied by the Management that

- The said transactions and fair valuations were pursuant to the scheme of arrangement approved by the Hon'ble High Court of Bombay and no actual purchase and sale of assets/liabilities took place.
- Further, TDSAT in the judgment pronounced on 23 April 2015 in a separate but related context affirmed that *"in order to be counted as "gross revenue", the item inflow must not be notional but real"*. Consequentially, it would be inappropriate to consider such notional income in the determination of the GR under the licence agreement.
- RITL had revalued assets in its books of accounts. Increase in value of assets on account of any revaluation of assets cannot be considered as revenue. If this revaluation is considered as income, the same would be accounted in RITL and not in RTL.

The reply of the Management is not tenable as –

- RCL, RTL and RITL were separate entities and RITL was not a fully held subsidiary of RCL/RTL. Assets transferred were written off from the books of RCL/RTL and debited to their profit and loss accounts. Hence these transactions were similar to sale/disposal of assets.
- Gain on revaluation of assets transferred was not notional as it accrued consequent to disposal of assets from one entity to another entity. While noting that the TDSAT judgment dated 23 April 2015 has been challenged by DoT in July 2015 in the Hon'ble Supreme Court, Audit view is that transfer of assets from RCL/RTL to RITL at value other than a 'fair value' was not a transaction at arm's length.
- Since asset was not disposed at fair value in line with arm's length transaction, increase in value of assets on account of any revaluation of assets by transferee Company (RITL) was the profit foregone by the transferor companies (RCL/RTL).

Thus non consideration of the amount of ₹ 126.72 crore in GR/AGR resulted in short payment of LF and SUC of ₹ 11.56 crore and ₹ 3.44 crore respectively by RCL for the year 2007-08 (**Annexure - 5.18**).

Similarly, non consideration of the amount of ₹ 321.56 crore in GR/AGR resulted in short payment of LF and SUC of ₹ 17.62 crore and ₹ 11.72 crore respectively by RTL for the year 2007-08 (**Annexure - 5.19**).

5.6 Non-consideration of Refund of Service Tax for GR during the year 2009-10

Audit observed that an amount of ₹ 51.45 crore being the refund of Service Tax was accounted under Operational Income during the year 2009-10. However, the said amount was not considered while computing GR for the purpose of LF and SUC.

Management stated that the Company had provided certain services which were in the category of export of services and paid service tax on same from accumulated credits, the same was claimed as rebate from the Service Tax department which on receipt, was shown as miscellaneous income in annual accounts, this refund was an incentive on export of services and hence, not liable for LF. The Management also stated that Service Tax paid was not claimed as deduction in AGR and hence, any rebate/incentive/refund cannot be liable for LF.

The reply is not tenable since RCL is a telecommunication company and any income that accrues to it by virtue of its business of telecom activities has to be a part of its revenue. Audit is of the view that any monetisation of export credit or any other incentive received by the Company constitutes part of miscellaneous income and as per the terms of Licence Agreement, has to be included in GR for computation of LF and SUC.

Non-inclusion of the amount has resulted in short payment of LF and SUC by ₹ 4.69 crore and ₹ 1.36 crore respectively (**Annexure – 5.20**). It is also pertinent to mention that the issue was noticed in Reliance during test check and hence commented upon.

5.7 Interest on short/non - payment of LF and SUC

On issues raised above (from paras 5.2 to 5.5) short/non-payment of LF and SUC worked out to be ₹ 1125.40 crore and ₹ 381.85 crore respectively. The interest on this short/non-payment of LF and SUC is ₹ 2221.29 crore (**Annexure-5.21**). The calculation of interest was based on the rate prescribed in the licence agreement i.e. *2 per cent* above the prime lending rate of State Bank of India existing as on the beginning of the financial year and the period considered for the calculation was from the end of the concerned financial year up to March 2015. The interest has been compounded monthly as prescribed in the licence condition.

5.8 Reply from DoT on issues raised above

Audit observations on the revenue shared by RCL/RTL were communicated to DoT in September 2015. DoT in reply (January 2016) informed that demands for understatement of GR as pointed out in paras pertaining to commissions/discounts paid to RCIL by RCL (5.2.2 A), VAS/CRBT revenue not included in GR/AGR of RCL (5.2.2 B and 5.2.2 C); non-inclusion of installation charges of FWP/T in GR/AGR of RCL (5.2.2 F); commissions/discounts paid to distributors by RTL (5.2.5); FOC coupons given to distributors by RTL (5.2.6); under reporting of revenue due to non-inclusion of revenue/income in GR/AGR from forex gain (5.3.1), interest and other income (5.3.2); profit from sale of investment (5.3.4) and gain on transfer of passive infrastructure (5.5.2) were raised on the PSP in 2012 for the years 2006-07 and 2007-08, based on the report of Special Audit conducted in 2009. But the demands were challenged by the operator in TDSAT/Hon'ble High Courts.

The matter is still *sub-judice* in the court. It was also informed that action would be taken as and when the final court judgment was pronounced.

Thus, DoT agreed to the issues raised by Audit. However, it pleaded helplessness in realising the revenue from RCL/RTL on account of these issues being *sub-judice*. Considering that a substantial amount of government revenue is blocked for many years on account of litigation, DoT should play a proactive role in getting these legal issues settled at the earliest.

DoT in its reply also pointed out to the variation in the amounts quantified by CAG Audit and the demands raised by DoT as a consequence of the Special Audit. These variations could be on account of the difference in methodology adopted in quantifying the understatement of revenue. Audit has determined the understated amounts on the basis of actual entries identified through clear descriptions in the books of accounts of RCL/RTL for 2006-07 to 2009-10. However, the details of working papers of the Special Auditors were not seen by CAG Audit.

In respect of paras pertaining to non-inclusion of revenue from sale of SIM cards (5.2.2 D); sale of handsets (5.2.2 E); understatement of GR by netting of broadband commission from revenue (5.2.3) and non-inclusion of gain on transfer of optical fibre (5.5.1), the DoT stated that reply received from the PSP was under examination.

In reply to para relating to booking of revenue net of FAT/commission (by eliminating it at mediation level itself) (5.2.1), it was stated that DoT had sent a notice to the company (June 2015) to prepare the accounts as per the norms mentioned in the licence agreements and in respect of para relating to netting of revenue from expenses (5.2.4), it was stated that show cause notice was issued to RCL to submit information on gross basis for items which have been netted off as required under clause 22.3 of UASL agreement.

In respect of para pertaining to interest free loan to subsidiary (5.3.3), it was stated that DoT had taken a decision in 2005, in consultation with Ministry of Law and learned AG, that notional interest can neither be reckoned nor included in AGR.

Audit view is that DoT's decision of not reckoning the due interest on interest free loan given to subsidiaries for AGR purpose was not in line with the provisions of the Companies Act 1956. By providing interest free loan to its not fully owned subsidiary, RCL's revenue was lower by the amount of interest receivable and ultimately the LF and SUC thereon was short paid to the Government of India to that extent.

In respect of paras relating to non-consideration of revenue from sale of bandwidth for SUC (5.4.1) and non-consideration of income from investment for SUC (5.4.2), it was stated that reply from WPF wing of DoT was awaited.

DoT also stated that the basic definition of GR and AGR was challenged by the PSP in 2002-03. Since then, there has been protracted litigation and is continuing till date. Also, some of the licensees have also filed (2012) writ petitions before various High Courts invoking the writ jurisdiction under Article 226 of the Constitution challenging the Section-4 of Indian Telegraph Act, 1885, as violative of the Article 14 and 19(1) (g) of the Constitution of India. The process of deduction verification by the CCA offices and the LF Assessment work by the DoT Headquarters was adversely impacted due to this. DoT admitted that the numerous disputes are causing delays in assessment of the revenue share due from the operator.

The response of DoT indicates that though the revenue share regime was introduced as part of NTP-1999, the Department has not been able to realise its due revenue share as envisaged in the licence agreement even after more than 16 years of its implementation.

It would be pertinent to mention here that when the government decided to reduce the licence fee for all operators by two *per cent* effective from April 2004, DoT expected that the reduction would prompt operators to withdraw the challenges against the government. However, the reduction in licence fee did not have the expected impact and the operators continue to institute litigations against the government challenging the definition of GR/AGR and demand notes. Thus the PSPs got the benefit of reduction in rate of licence fee but the government didn't get the reciprocal benefit of reduction in litigations.