CHAPTER-III

Revenue Shared by Vodafone India Limited

3.1 Brief profile of M/s Vodafone India Ltd

Brand Vodafone was launched in India in 2007 when Vodafone Plc, the British multinational communications company, acquired majority stake in M/s Hutchinson Essar which was providing GSM based cellular mobile services in sixteen licensed service areas in the country. The decision of the Government of India in 2005 to raise the Foreign Direct Investment (FDI) in telecom sector to 74 *per cent* helped the British company to make major foray into the Indian telecom space. By 2007-08, the operator was allotted seven more licenses and had established pan India presence with operations in all existing twenty three Licensed Service Areas (Circle) in the country. Vodafone India provides wireless mobile telephone services which include voice/data and total high-quality, innovative communication solutions.

3.1.1 Licenses held by Vodafone Group

In addition to access service license in 23 service areas, Vodafone Group has carriage licenses i.e. National Long Distance (NLD) as well as International Long Distance (ILD) and Internet Service Provider (ISP) license.

The Circle wise service provision and related accounting activities are performed under the aegis of the Corporate Head Office of Vodafone India Limited (erstwhile Vodafone Essar Ltd) at Mumbai and its seven subsidiary Companies.

3.1.2 Spectrum held by Vodafone Group

License area-wise quantum of spectrum held as on 01 April 2010 and 31 March 2015 is as follows-

Table 3.1

Sl. No.	Names of Circles	GSM Spectrum held as on 1.4.2010 (in MHz)	GSM Spectrum held as on 31.3.2015 (in MHz)	MW Access spectrum	MW Backbone spectrum
				(in MHz)[1]	
1	Himachal Pradesh	4.4	5.65	112	56
2	Andhra Pradesh	6.2	6.8	224	56
3	Assam	4.4	6.9	112	56
4	North East	4.4	6.9	112	56
5	Orissa	4.4	6.9	112	56
6	Bihar	4.4	6.9	112	56
7	Jammu & Kashmir	4.4	6.9	112	56
8	Madhya Pradesh	4.4	6.9	112	56

[1] One Carrier = 56 MHz

9	Rajasthan	6.2	7	180	56
10	Punjab	6.2	8.05	224	-
11	UP West	6.2	8.7	112	56
12	Haryana	5	9.9	180	56
13	Tamil Nadu	7.2	12.2	180	112
14	Maharashtra	6.2	12.45	180	112
15	Chennai[2]	8	13	224	-
16	Karnataka	8	13	224	56
17	West Bengal	6.2	13.7	112	112
18	Kerala	6.2	14.45	112	112
19	Delhi	5	18	392	-
20	UP East	8.2	18.45	180	112
21	Gujarat	9.8	19.2	224	56
22	Mumbai	5	24.2	392	-
23	Kolkatta	9.8	29.8	224	-

3.1.3 Gross Revenue, Deductions, Adjusted Gross Revenue reported and revenue share paid by Vodafone group:

Telecom Service Providers (TSPs) are required to pay LF and SUC at a percentage of AGR quarterly on self-assessment basis. The combined GR/AGR reported and revenue share paid by Vodafone India Limited (VIL) for the five years from 2010-11 to 2014-15 is as shown below:

Table 3.2

(₹in crore)

Year	No. of Subscribers (in crore)	GR	Deductions	AGR	Percentage of AGR to GR	Revenue share paid (LF+SUC)
2010-11	13.46	29971.54	8912.82	21058.72	70.26	3038.81
2011-12	15.04	36290.66	11336.42	24954.24	68.76	3262.96
2012-13	15.23	40367.11	12900.90	27466.21	68.04	3659.70
2013-14	16.67	45565.90	14083.80	31482.10	69.09	4394.70
2014-15	18.39	46650.36	13709.27	32941.09	70.61	5091.90
Total		**198845.57**	**60943.21**	**137902.36**	**---**	**19448.07**

As evident from the above, Vodafone had a subscriber base of 13.46 crore as on March 2011, which grew to 18.38 crore by March 2015, registering a growth of 36.55 *per cent* with a market share of 18.95 *per cent* and occupied second place behind Bharti Airtel Limited.

3.2 Under reporting of revenue by Vodafone India Limited

Audit examination of records/Books of accounts of VIL and its subsidiaries revealed that these companies had not adhered to the provisions of the Licence Agreement on the following issues:

[2] The migration process for merger of Chennai and Tamil Nadu LSAs was in progress as on 31 March 2015

3.2.1 Under reporting of revenue due to 'netting off' of revenue pertaining to discounts/margins offered to dealers and free airtime offers to subscribers

From the examination of data/records furnished by VIL and its subsidiaries for the period from FY 2010-11 to 2014-15, it was observed that –

- The discounts/ margins given to distributors/agents were netted off from the revenue
- Offers to the subscribers viz. Free Air Time (FAT), Free of Cost (FOC) Talk time, Promotional offers like Full talk time (FTT), Full pe Full (FPF) talk time, Bonus talk time and other charges were set-off from the revenue.
- As no separate General Ledgers (GLs) were maintained for pre-paid and post-paid services, no segregation of service wise understatement of revenue and revenue share impact was done.

Item wise details are furnished below:

A) Discount/Margin

The licensee company appoints distributors/franchises/dealers for selling telecom services on commission basis. The company supplies to its distributors/franchises/agents various prepaid products for sale to subscribers either at a discounted rate or with margin on MRP in lieu of commission.

During review of data/records furnished by VIL and its subsidiaries for the period from 2010-11 to 2014-15, it was observed that the prepaid products viz. re-charge coupons, e-top ups, etc. were supplied to the distributors/franchises/dealers either at a discounted rate or with margins vis-a-vis maximum retail price (MRP) which was in lieu of commission. The discount/margin offered to the distributors/franchises/dealers was netted off from revenue and as a result Net Revenue was considered in Financial Statements as well as AGR statements submitted to DoT.

Total amount netted off from revenue on account of discounts/margins to the distributor/franchisees/agents/dealers during 2010-11 to 2014-15, as confirmed by VIL, was ₹ 4196.21 crore. Since the discount/margin extended to the distributors/franchises/dealers were in the nature of business expenses (marketing expenses), set-off of such expenses with revenue was against the licence condition.

Vodafone management stated (November 2016) in reply that;

- The company's policy of appointing distributor/dealer/franchisees depends purely on the business need of the organization. The arrangement with distributors was on Principal-to-Principal basis. Discounts were given at the time of primary billing. Discount was configured in the prepaid billing system and discount accounting was done through interface from this billing system.

- The only inflow into the Company was the amount paid by the distributor i.e. distributors price and not the MRP.
- The sale is on agreed price which is stated on the invoice and the same is reflected in the Profit and Loss (P&L) account. Neither discount was shown as an expense nor was there netting off of any expense as the billing to the distributor was at the agreed/stated price.
- The company has preferred an appeal along with stay application on TDSAT's judgment dated 23 April 2015 before the Hon'ble Supreme Court. DoT has filed cross appeals challenging the said order of TDSAT and the matter is pending before the Hon'ble Supreme Court. Considering the above, VIL is under legal advice not to include discounts in computation of AGR subject to final outcome of the case.

  The reply of the Management is not tenable as –

- VIL is rendering the services ultimately and had VIL sold the cards directly to the customers, revenue would have been accounted for full value of service rendered and selling expenses would have been accounted as expenditure. On same analogy, discount/ commission accorded to distributors would be in the nature of Marketing Expenditure and thus, should not be deducted from Revenue. This is in accordance with stipulation in license agreement. Further, Audit opines that this transaction is not covered under Principal to Principal since the ultimate responsibility of rendering the service to the customer rest with VIL and not with the distributors.
- While the matter is sub-judice at Hon'ble Supreme Court, Audit view is that commission/margin paid to the distributors/franchises/dealers is in the nature of marketing expenses; therefore, set-off of such expenses with revenue was against the license condition. For the purpose of licence fee, the revenue is to be recognised "Gross" without set-off of related expenses as mandated under licence agreement.

Thus, netting off of Discount/Margin resulted in understatement of GR/AGR by ₹ 4196.21 crore **(Annexure – 3.01).** Resultantly, LF and SUC amounting to ₹ 351.77 crore and ₹ 213.52 crore respectively were not paid on the said revenue by the Company **(Annexure – 3.01).**

B) Promotional offers to customers

During review of data/records furnished by VIL and its subsidiaries for the period from 2010-11 to 2014-15, it was observed that in order to accommodate promotional offers to the subscribers, debits under certain revenue account heads were found on account of expenses viz. Free Air Time (FAT)/Free of Cost (FOC) air time, Full talk-time (FTT), Full Pe Full (FPF) talk time, bonus talk time, etc. The value of above promotional offers was debited against service revenue received upfront and thus, was not recognised in the GR/AGR.

Since these promotional offers to customers were part of overall commercial strategy to enhance business, the cost of such promotional offers were in the nature of expenses. Further,

as per the conditions of the licence agreement, service revenue should be shown in gross without any set-off. Item wise details, as confirmed by Vodafone, are as follows:

Table 3.3

(₹ in crore)

Nature of Promotional Offer	Under reporting of GR	Remarks
Free Airtime (FAT)/ Free of Cost (FOC) airtime	728.23	**Annexure-3.02**
Full Talk Time (FTT)/ Full Pe Full (FPF) talk time	560.23	**Annexure-3.03**
Promotional Talk time (PTT)	127.15	**Annexure-3.04**
Bonus talk time	5.33	**Annexure-3.05**
Total	**1420.94**	

Vodafone Management stated (November 2016) in reply that;

- As per various marketing scheme, the Company offers full talk time to the selected prepaid customers. These schemes are generally informed to TRAI. All Telecom Companies offer such schemes. Generally, if customer has purchased recharge of ₹ 112.36, revenue was recognized to the extent of ₹ 100 and the recovery of service tax payable to government was credited to service tax liability account by ₹ 12.36.
- Similarly, with full talk time offer, in case a customer purchases recharge of ₹ 224.72 and gets the full talk time of ₹ 224.72, revenue was recognized to the extent of ₹ 200 and the recovery of service tax payable to government was credited to service tax liability account of ₹ 24.72.
- The service tax deposited by the Company with the Government was to be excluded under Clause 19.1 from definition of AGR. The balance amount was the amount which is received by the Company for the services rendered and the same is accounted as revenue.
- The Company does not receive anything over and above this amount and no deduction is being made from revenue contrary to Clause 19.1. This treatment was in accordance with AS-9.
- The talk-time offered for the amount received was not relevant as the receipt of the amount from customer was recorded in books as such and included in "revenue" and no additional revenue accrued/was received by the Company.

Audit view on the reply of the Management is as follows:

- Audit is not questioning the accounting in accordance with AS-9 but contends that Airtime is not a free commodity, had an intrinsic value and by giving FAT/FTT/ FOC etc., the licensees are foregoing the revenue instead of booking these separately as expenses resulting in avoidance of payment of LF and SUC.

- The details of FAT/FTT/FOC, etc. offered as per the tariff and that offered as promotion to customers/agents were not furnished.

Thus, netting off of FAT/FTT/FOC/PTT/Bonus talk time resulted in understatement of GR/AGR by ₹ 1420.94 crore **(Annexure – 3.02 to 3.05).** Resultantly, LF and SUC amounting to ₹ 116.66 crore and ₹ 70.95 crore respectively were not paid on the said revenue by the Company **(Annexure – 3.02 to 3.05).**

3.2.2 Under reporting of Roaming Revenue due to set-off of Inter Operator traffic discounts paid/credited to other Operators

VIL and its subsidiaries had arrangements with other International telecom Operators for continuation of services of the subscribers during roaming. It was noticed that the Inter Operator Traffic (IOT) discounts paid/credited to these operators' accounts were debited/deducted from the revenue heads.

Having roaming arrangement with other national/international operators was a matter of mutual agreement between two operators and giving discounts over and above the agreed charges for roaming was part of overall commercial strategy to enhance business between the two operators. As such, these discounts were in the nature of expenses and hence, in terms of licence agreements, should not be deduced from revenue.

It was observed that IOT Discounts amounting to ₹ 294.53 crore during the period 2010-11 to 2014-15, as confirmed by Vodafone, were debited from roaming revenue.

Vodafone management stated (November 2016) in reply that;

- The discounts, which are given by credit notes, are not in the nature of income/revenue as it does not result in any inflow of cash or recoverable or other consideration and also cannot be considered as an expense. It is to be noted that AS -9 itself excludes discounts from definition of revenue and therefore, discounts are not to be added under Clause 19.1 as revenue.
- TDSAT in the AGR case held that the discounts are to be added to the revenue, the Company had preferred an appeal along with stay application before the Hon'ble Supreme Court against the same. DoT too has filed cross appeals challenging the said order of the TDSAT. The matters are presently pending before the Hon'ble Supreme Court.
- In view of the long standing litigation on the subject which was pending before the Hon'ble Supreme Court, Vodafone was under legal advice not to include discounts by credit notes on international roaming in computation of the AGR subject to final decision by the Hon'ble Supreme Court in this regard.

Audit view on the reply of the Management is as follows:

- Giving discounts over and above the agreed charges for roaming was part of overall commercial strategy to enhance business between the two operators; hence these discounts were in the nature of expenses. Since the licence agreement does not permit any netting off, such expenditure cannot be deducted and therefore, have to be included in the GR.
- While the matter is sub-judice at the Hon'ble Supreme Court, Audit view is that for the purpose of licence fee, the revenue is to be recognised "Gross" without set-off of related expenses as mandated under licence agreement.

Thus, netting off of IOT discounts resulted in understatement of GR/AGR by ₹ 294.53 crore **(Annexure – 3.06).** Resultantly, LF and SUC amounting to ₹ 24.92 crore and ₹ 15.00 crore respectively were not paid **(Annexure – 3.06).**

3.2.3 Under reporting of revenue from Infrastructure sharing with other telecom operators

Telecom infrastructure (towers, network equipment etc.) owned by VIL and its subsidiaries were being shared with other telecom companies. VIL and its subsidiaries entered into agreements with other telecom companies for infrastructure sharing.

Review of data/records pertaining to Infrastructure Sharing Charges furnished by VIL and its subsidiaries for the period from 2010-11 to 2014-15 revealed that Infrastructure sharing charges recoverable/recovered on account of rent, fuel (Diesel), Electricity, Operation and Maintenance, Insurance, Security, etc. were netted off from the expense heads and hence not included in the revenue. Total amount netted off from the expenses was ₹ 381.91 crore as confirmed by Vodafone. This amount should have been considered for computation of GR/AGR.

Vodafone Management stated (November 2016) in reply that;

- The Company entered into arrangements with other Telecom Operators for sharing of infrastructural facilities and to proportionately bear the operational expenditure incurred in running and maintaining such facilities. After determining the actual cost incurred as operational expenditure, the company divides the costs between itself and the other Telecom Operators sharing the facilities with the Vodafone. It is pertinent to note that the Telecom operator sharing the facilities with the company pays its agreed share of operational expenditure actually incurred for running the sites to the Vodafone. The amount received by the Company represent certain proportion of the actual cost incurred for running the sites and did not include any margin of the Company.
- The operating expenditures were reimbursed on actual basis and thus, the amount received towards operations incurred for other Telecom operators cannot be considered as revenue from the sharing of infrastructure facilities as amounts received

are nothing but payments of the expenditure incurred on behalf of such telecom operators. It is also pertinent to note that since the amounts received from the other telecom operators are towards reimbursement of expenses incurred on their behalf, the same are deducted from the costs incurred by the Company.

- Payments made by other operators on account of capex are included in Gross Revenue and licence fee has already been paid on account of that.
- The Learned TDSAT held that the reimbursements are not to be included in the revenue and in our facts; the reimbursements are discernible from the invoice itself. Therefore, the reimbursements received cannot be added to the revenue under clause 19.1.

Reply of the Management is not tenable as:

- In terms of license agreement, GR specifically includes revenue from permissible sharing of infrastructure without any set-off for related item of expense and license agreements do not distinguish infrastructure sharing revenue between CAPEX and OPEX. Hence, set-off of revenue from infrastructure sharing against the expenses is not allowed. Revenue towards diesel expenses, security expenses, repair & maintenance expenses and electricity charges did not constitute reimbursement since they had to be incurred irrespective of whether the towers were shared or not. In fact, by sharing the expenditure, the company benefitted through additional income.
- DoT had filed an appeal before Hon'ble Supreme Court against the TDSAT Judgement dated 23 April 2015 as referred in the reply. While the matter is sub-judice at the Apex Court, Audit view is that as UASL does not provide for any deductions from revenue other than those permitted under Clause 19.2, deducting OPEX from infrastructure sharing revenue was not in conformity with the UASL agreement.

Thus, netting off infrastructure site sharing revenue (rent, Diesel, Electricity, Operational and Maintenance, Insurance, Security etc.) from the expenses during 2010-11 to 2014-15 resulted in understatement of GR/AGR by ₹ 381.91 crore **(Annexure – 3.07).** Resultantly, LF and SUC amounting to ₹ 27.75 crore and ₹ 16.12 crore respectively were not paid on the said revenue by the Company **(Annexure – 3.07).**

3.2.4 Non consideration of forex gain

Review of data/records furnished by VIL and its subsidiaries for the period from 2010-11 to 2014-15 revealed that the realised gain on the basis of individual transactions of foreign exchange (forex) rate fluctuations worked out to ₹ 169.07 crore. As confirmed by Vodafone, this amount of forex gain was not considered for computation of GR/AGR.

Further, 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. 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.

Vodafone Management stated (November 2016) in reply that;

- Income from fluctuations in foreign exchange(s) was notional in nature and not revenue. The accounting standards require this notional gain or loss on forex fluctuations to be accounted at the end of the year so that the profit/loss of the company was fairly stated as on the balance sheet date. It is reiterated that in respect of cost or purchase items like operating expense on account of consultancy, purchase of equipment or loan taken in foreign currency, the fluctuations due to foreign currency do not form part of revenue as such fluctuations ultimately result in increase or reduction in cost or purchase price and have no linkage with the revenues.
- TDSAT (April 2015) had ruled that Forex gains were not to be included in the AGR. DoT has filed cross appeals challenging the said order of the TDSAT. The matters are presently pending before the Hon'ble Supreme Court.
- In view of the long standing litigation on the subject which is pending before the Hon'ble Supreme Court, Vodafone is under legal advice not to include income from interest and dividend in computation of the AGR subject to final decision by the Hon'ble Supreme Court in this regard.

Contention of the Management was not acceptable. Audit view on the treatment of forex gains for revenue share has been explained under Para 2.2.5 of this Report. Audit noted that DoT had gone on appeal against the TDSAT judgement of April 2015. While the matter is *sub-judice* at the Hon'ble Supreme Court, Audit view is that forex gains should be a part of the GR computed for payment of revenue share since it falls within the broad definition of GR given in the UASL agreement.

Non inclusion of the Forex gain amounting to **₹ 169.07 crore** for computation of GR/AGR resulted in short payment of LF and SUC by **₹ 13.55 crore** and **₹ 6.58 crore** respectively **(Annexure – 3.08).**

3.2.5 Interest Income not considered for revenue share

Review of data/records furnished by VIL and its subsidiaries for the period from 2010-11 to 2014-15 revealed that interest income of ₹ 5971.24 crore was not considered in computation of AGR.

While confirming the facts and figures, Management stated (November 2016) that;

- "Adjusted Gross Revenue"- (AGR) relates only to the revenue directly derived from licensed telecom operations in a service area. The Licensor/DoT cannot claim any share in the incomes derived from activities which are neither covered nor have any

connection with the licenses granted by it and are in regard to non-telecom activities, for which no license was required.

- To the various intervening legal claims and counter claims made at various legal forums by Vodafone and DoT respectively, the TDSAT, vide its judgment (April 2015) sought to include the income from interest and dividend in the computation of AGR which has been challenged by Vodafone in the Hon'ble Supreme Court (September 2015).
- In view of the long standing litigation on the subject which is pending before the Hon'ble Supreme Court, Vodafone is under legal advice not to include income from interest and dividend in computation of the AGR subject to final decision by the Hon'ble Supreme Court in this regard.

Contention of the Management was not acceptable. Audit view on the treatment of interest income for revenue share has been explained under Para 2.2.6 of this Report.

Non-consideration of interest income resulted in understatement of GR/AGR by ₹ 5971.24 crore. Resultantly, LF and SUC amounting to ₹ 525.48 crore and ₹ 307.67 crore respectively were not paid **(Annexure – 3.09).**

3.2.6 Income from Dividends not considered

As per license agreement, the Gross Revenue shall include all service revenue, miscellaneous revenue and other income including dividend without any set-off for related item of expense, etc. Audit noticed that dividend income of ₹ 2265.56 crore during the three years from 2012-13 to 2014-15 was not considered for computation of GR/AGR.

While confirming the facts and figures, Management stated (November 2016) that

- The company was of the view "Adjusted Gross Revenue" (AGR) relates only to the revenue directly derived from licensed telecom operations in a service area. The Licensor/DoT cannot claim any share in the incomes derived from activities, which are neither covered nor have any connection with the licenses granted by it and are in regard to non-telecom activities, for which no license was required.
- To the various intervening legal claims and counter claims made at various legal forums by Vodafone and DoT respectively, the TDSAT, vide its judgment (April 2015) sought to include the income from interest and dividend in the computation of AGR which has been challenged by Vodafone in the Hon'ble Supreme Court (September 2015).
- In view of the long standing litigation on the subject which is pending before the Hon'ble Supreme Court, Vodafone is under legal advice not to include income from interest and dividend in computation of the AGR subject to final decision by the Hon'ble Supreme Court in this regard.

Contention of the Management was not acceptable. Audit view on the treatment of dividend income for revenue share has been explained under Para 2.2.8 of this Report.

Non-consideration of dividend income resulted in understatement of GR/AGR by ₹ 2265.56 crore. Resultantly, LF and SUC amounting to ₹ 186.31 crore and ₹ 120.65 crore respectively were not paid **(Annexure – 3.10).**

3.2.7 Income from profit on sale of fixed assets not considered for revenue share

In terms of conditions under license agreement, the Gross Revenue shall be inclusive of revenue on account of interest, dividend and any other miscellaneous revenue without any set-off for related item of expense, etc. From the examination of data/records furnished by Vodafone and its subsidiaries, it was noticed that gain on sale of fixed assets of ₹ 649.60 crore was not considered for computation of GR/AGR.

While confirming the facts and figures, Management stated (November 2016) that

- In the financials, the net of profit and loss on sale of capital assets during the year is shown as one net item.
- Such profits arising from sale of capital assets are in the nature of capital receipt. Capital gain is artificial income.
- The definition of "gross revenue" would include only revenue receipts and not capital receipts and para 3(i) of AS-9 specifically excludes capital gains from the ambit of revenue.
- It was also stated that TDSAT had upheld the views of the Company in its ruling of April 2015, which incidentally has been challenged by DoT vide an appeal which was taken up (September 2015) and the matter is presently pending before the Hon'ble Supreme Court.
- In view of the long standing litigation on the subject which is pending before the Hon'ble Supreme Court, Vodafone is under legal advice not to include gain on sale of assets in computation of the AGR subject to final decision by the Hon'ble Supreme Court in this regard.

Vodafone Management's reply is not tenable since;

- Licence agreements expressly provide that miscellaneous revenue/income should be included in GR/AGR for computation of revenue share and profit on sale of assets/scraps falls in the nature of miscellaneous revenue/income. Also it is not only revenue receipts but receipts from capital is also subject to revenue share i.e. interest and dividend. Therefore capital gains are also subject to revenue share.
- Regarding TDSAT judgment of 23 April 2015, an appeal was filed by DoT before Hon'ble Supreme Court against the judgment.

While the matter is sub-judice at Hon'ble Supreme Court, Audit view is that profit on sale of assets/scraps should be included in GR/AGR for computation of revenue share. Thus non inclusion of profit on sale of assets/scraps has resulted in understatement of GR/AGR by ₹ 649.60 crore**.** Resultantly, LF and SUC amounting to ₹ 53.35 **crore** and ₹ 29.76 crore respectively were not paid **(Annexure – 3.11).**

3.2.8 Miscellaneous revenue not considered for revenue share

In terms of conditions under license agreement, the Gross Revenue shall be inclusive of revenue on account of interest, dividend and any other miscellaneous revenue without any set-off for related item of expense, etc. From the AGR statements, it was found that miscellaneous income amounting to ₹ 13.72 crore was not considered for AGR in the years 2010-11 to 2014-15.

While confirming the facts and figures, Management stated (November 2016) that

- under the license agreement, miscellaneous income are not required to be added to the AGR
- TDSAT in the AGR case has upheld the contention of the company. Further, receipt of scrap sales, insurance claims etc. which do not accrue either from subscriber or from telecom service provisioning should not be part of the AGR.
- Miscellaneous income is not subject to LF as it is a capital receipt and it cannot be termed as revenue in ordinary course of business.
- Appeals were taken up by the Supreme Court on 30 September 2015 wherein it was submitted that DoT would not take any coercive action to enforce any demands
- In view of the longstanding litigation on the subject before the Hon'ble Supreme Court, the company is under legal advice not to include miscellaneous income in the computation of AGR, subject to the final decision that may be taken by the Hon'ble Supreme Court in this regard.

Vodafone Management's reply is not tenable since;

- Licence agreement provides that miscellaneous revenue should be included in GR for computation of revenue share.
- TDSAT judgment of April 2015 referred to in the reply has been challenged by DoT in the Hon'ble Supreme Court.

While the matter is sub-judice at Hon'ble Supreme Court, Audit view is that Miscellaneous Income should be included in GR/AGR for computation of revenue share in accordance with Licence Agreement. Non-consideration of miscellaneous income resulted in understatement of GR/AGR by ₹ 13.72 crore and non-payment of LF and SUC amounting to ₹ 1.14 crore and ₹ 0.73 crore respectively **(Annexure – 3. 12).**

3.2.9 Irregular Deduction claimed for 'Bad debts written off' from GR to arrive at AGR

Definition of GR/AGR does not permit for deduction of expenses on account of bad debts written off.

Review of data/records provided by Vodafone and its subsidiaries for the period from 2010-11 to 2014-15 revealed that an amount of ₹ 507.25 crore was deducted from GR on account of "Bad debts Written Off" while arriving at AGR.

While confirming the facts and figures, Management stated (November 2016) that

- Under the license agreement, bad debts are not required to be added to the AGR. Annexure-III appended to the License Agreement specifically provides the format under which "Details of reversal of previous years' debits, if any, shall be shown component wise, under the miscellaneous heads (e.g. Bad Debts recovered etc.)". The question of including bad debts recovered as part of revenue would arise only in a situation where the bad debt had been allowed as a reduction in an earlier period from the revenue. The Company has added to AGR bad debts recovered. The inclusion of bad debts again as proposed would lead to double charge which is not permissible. It is to be noted that bad debts represent income that has not been received and as such cannot be considered as revenue and is notional in nature.
- While the Learned TDSAT in the AGR case has held that the bad debts are to be added to the revenue, the Company has preferred an appeal along with stay application before the Hon'ble Supreme Court against the same. DoT too has filed cross appeals challenging the said order of the TDSAT. The matters are presently pending before the Hon'ble Supreme Court.
- Appeals were taken up by the Supreme Court on 30 September 2015, wherein it was submitted that DoT would not take any coercive action to enforce any demands.
- In view of the long standing litigation on the subject, the statement made by the learned Additional Solicitor General of India and pendency of the matter before the Hon'ble Supreme Court, VIL is under legal advice to not include Bad debts written off in computation of AGR. Needless to add that the above is subject to the final decision that may be taken by the Hon'ble Supreme Court in this regard.

The contention of the Management is not acceptable as;

- The license agreement does not provide for deduction of bad debt from GR to arrive at AGR.
- The Company had filed appeal against the TDSAT judgment and the matter was sub-judice at the Hon'ble Supreme Court.

While the matter is sub-judice at the Hon'ble Supreme Court, Audit view is that Bad debts written off was an expenditure and hence, should not be deducted from GR of the Company.

Thus, deduction of bad debts from GR to arrive at AGR resulted in understatement of AGR by ₹ 507.25 crore and non-payment of LF and SUC amounting to ₹ 44.48 crore and ₹ 26.56 crore respectively **(Annexure – 3.13).**

3.2.10 Transfer of Passive infrastructure Assets by Vodafone licensee companies to its subsidiary at Nil value:

There were eight telecom licensee companies under Vodafone India Group viz.

i) Vodafone India Ltd. (VIL) {formerly known as Vodafone Essar Ltd}(VEL)

ii) Vodafone Mobile Services Ltd (VMSL), {formerly known as Vodafone Essar Mobile Services Ltd.} (VEMSL)

iii) Vodafone East Ltd. (VEL) {formerly known as Vodafone Essar East Ltd.} (VEEL)

iv) Vodafone South Ltd. (VSL) {formerly known as Vodafone Essar South Ltd} (VESL)

v) Vodafone Digilink Ltd. (VDL) {formerly known as Vodafone Essar Digilink Ltd} (VEDL)

vi) Vodafone Cellular Ltd. (VCL) {formerly known as Vodafone Essar Cellular Ltd.} (VECL)

vii) Vodafone West Ltd. (VWL) {formerly known as Vodafone Essar Gujarat Ltd} (VEGL)

viii) Vodafone Spacetel Ltd. (VSpL) {formerly known as Vodafone Essar Spacetel Ltd.} (VESpL)

The last seven companies were wholly owned subsidiaries of the first company. Another wholly owned subsidiary of VIL namely Vodafone Infrastructure Limited {formerly known as Vodafone Essar Infrastructure Limited (VEIL)} was incorporated under Companies Act, 1956 on 19 January 2007 and got registered with DoT as IP-1 service provider on 17 June 2008.

Scheme of Arrangements (SoAs) for transfer of Passive infrastructure (PI) assets of first seven licensee companies (transferor) to Vodafone Infrastructure Limited (transferee) were approved by different High Courts and accordingly the PI Assets were transferred without any consideration. Book values of the PI assets were debited to Profit and Loss Account/ treated as expenditure to be amortised in the books of the transferor companies and these assets were also carried at NIL value in the books of the transferee company. Particulars of PI assets transferred were as under:

Table 3.4

Name of the transferor company	Date of Approval by High Court	Year in which transferred in the books of transferee company	Book Value of PI assets transferred (₹ In crore)
Vodafone East Ltd.	28 October 2009	2010-11	92.38
Vodafone Cellular Ltd.	17 November 2009	2010-11	619.53
Vodafone India Ltd.	17 December 2009	2010-11	97.80
Vodafone Mobile Services Ltd.	29 March 2011	2010-11	168.82
Vodafone South Ltd.	29 March 2011	2010-11	1730.21
Vodafone Digilink Ltd.	29 March 2011	2010-11	985.95
Vodafone West Ltd.	27 August 2012	2011-12	292.11
		Total	**3986.80**

These assets were ultimately transferred to Indus Tower Limited (Indus), a joint venture of Vodafone, Airtel and Idea, through a SoA approved by Delhi High Court on 18 April 2013. Indus recorded these PI assets at their fair value in its books of accounts whose details are not available with audit.

Transfer of PI assets by Vodafone licensee companies to its subsidiary without any consideration, which was ultimately transferred to a joint venture at their fair value (details of which was not available to audit) was not a transaction at arm's length. It is pertinent to mention that Bharti Airtel Limited (BAL), another partner in Indus, had similarly transferred its PI assets having book value of ₹ 5739.60 crore to its subsidiary {Bharti Infratel Limited (BIL)} at Nil value during 2007-08 and BIL recorded these assets at their fair value of ₹ 8235.97 crore (1.434 times of book value). Transfer of PI assets of Airtel at "nil" value was commented upon in C&AG's audit report No.4 of 2016.

Transfer of PI assets by Vodafone having book value of ₹ 3986.80 crore at 'Nil' value instead of its fair value has resulted in profit foregone with consequential non-payment of Licensee Fee and Spectrum Usage Charges as per licenses, amount of which could not be quantified by audit.

Vodafone Management stated in reply that:

- The scheme, which was approved by respective High Courts, provided for transfer and vesting of the PI assets of VIL group into another subsidiary VEIL from 1.4.2009 being the appointed date.
- The scheme was intended to restructure the holding of PI assets in the VIL Group in a more efficient manner consistent with the diverse needs of business within VIL Group and does not involve any movement of assets and liabilities to any party outside the VIL Group and accordingly the transfer was made without any consideration.

- Though the VIL Group companies wrote-off the value of assets from their books of account, they did not claim any deduction on account of such write-offs while calculating license fee.
- Gross revenue includes only revenue receipts and not capital receipts.
- In view of the long standing litigation on the subject, the statement made by the learned Additional Solicitor General of India and pendency of the matter before the Hon'ble Supreme Court, VIL is under legal advice to not include gain on sale of assets in computation of AGR. Needless to add that the above is subject to the final decision that may be taken by the Hon'ble Supreme Court in this regard.

The contention of the Management is not acceptable as transfer of PI assets by Vodafone licensee companies to its subsidiary without any consideration, which was ultimately transferred to a joint venture (Indus Towers Ltd) at their fair value, was not a transaction at arm's length. The difference between the book value and the value accounted by Indus Towers ltd. was profit foregone on transfer of asset. This profit foregone on transfer of asset should be considered for computation of LF and SUC.

3.2.11 Interest on revenue share short paid

On issues raised above (from paras 3.2.1 to 3.2.09), short / non-payment of LF and SUC worked out to ₹ 1345.41 crore and ₹ 807.54 crore respectively. The interest on this short/non-payment of LF and SUC was ₹ 1178.84 crore (**Annexure-3.14**). 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 2016. The interest has been compounded monthly as prescribed in the licence conditions.

3.3 Disclosures in the Statement of Revenue and License fee (AGR statements)

Clause 20.7 of the UAS/CMTS licence agreements provide that the Annual Financial Account and the Statements of Revenue and Licence Fee (AGR Statement) shall be prepared following the norms as prescribed in Annexure. Annexure III of the UAS/CMTS licence agreement provides norms for preparation of Annual Financial statements. Scrutiny of AGR statements, Annual Financial statements and related accounting records furnished to audit indicates that all these norms had not been complied in full. In particular, it appears that norms relating to Service Tax, Sales Tax, Discount/rebate, Sale of goods, Inventory, Set off of income against expenditures and unbilled numbers had not been complied.

On being pointed by audit the Management stated that they submitted in Notes on accounts forming part of audited AGR for respective years wherein it is mentioned that there are certain deviations from applicable disclosure norms as indicated in note 5 in annexure-I-notes to the statement of revenue and license fee as required by the Annexure-III to the

UASL Agreement 842-1017/2008-AS-IV dated 20.10.2008. However, this does not have any impact on the computation of adjusted gross revenue and license fee dues.

Instances of understatement of revenue as brought out in the report would confirm that the revenue recognised for payment of licence fee were not in line with the licence conditions nor the preparation of accounts was fully compliant with the norms prescribed by DoT. Few such instances are given below:

- As per the norms revenue was to be shown as gross without any deductions. However, as detailed in paragraph of this report it can be seen that Discount/ Commission/ Waivers, Free airtime etc., were netted off from revenue and not disclosed to DoT.
- DoT was asked for its response on non-compliance of these conditions of the contract by the PSPs. DoT has not given any response till date.
- In view of the above DoT has over the years failed to issue and enforce instructions to the Service Providers to comply with the norms for preparation of Annual Financial Statement as required under Annexure-III of the License Agreement which were vital. Consequently during the years 2010-10 to 2014-15, the Company understated its GR/AGR and DoT could not detect the same.

Further, Audit observed that during the years 2010-11 to 2014-15 the GR of Vodafone group was ₹ 198846 crore, the deductions claimed was ₹ 60943 crore and the average deduction percentage works out to 31 *per cent* of the GR. Though the deductions claimed by Vodafone group were subject to verification by Offices of Controllers of Communications Accounts (CsCA), 69 *per cent* of the Gross Revenue is merely assessed based on self-declaration made by the Company at DoT Level.

Also, the LF Wing of DoT has failed to obtain the information as required to be maintained by the TSP in accordance with Annexure-III of the License Agreement and absence of these data would render the process of verification and assessment ineffective.

Thus, the entire verification and assessment of Revenue Share of the Service Provider is focused on the verification of deductions claimed by the Service Providers instead of on their GR.

3.4 Response of DoT/ VIL to the audit observations

Audit observations on the revenue share payable by M/s VIL were communicated to DoT and VIL during August 2016 for their further comments. VIL had reiterated once again (September/November 2016) vide their submission made in reply to audit observations issued during the course of premises audit. DoT reply is as mentioned in the para 2.4.