R.P.A.D.

Date: 06th May 2010 "without Prejudice"

To:

Telecom Regulatory Authority of India,
Mahanagar Doorsanchar Bhawan,
Jawaharlal Nehru Marg
New Delhi- 110002.

Sub: Response to Telecom Regulatory Authority of India consultation paper dated 25th March 2010 on issues for non CAS Areas

Dear Sir,

We write with reference to the aforementioned Consultation Paper issued by TRAI on related issues for non Cas Areas.

We herewith submit the following response to the consultation paper:

1. **Are the figures in Annexure B3 representative for the different genres of broadcasters? If not, what according to you are the correct representative figures? When providing representative figures, please provide figures for the genre, and not of your company?**

   Given our experience in MSO business, we believe that broadcasters recover more than 70% of the content and operating costs through subscription revenue, a fact that is not borne out of this annexure. For example in Bangalore Market of 1.5 Million Cable & Satellite homes broadcasters with an annual increase of 12-15% subscription revenue, secure a monthly subscribscription revenue of Rs 12 Crores with an estimated Ad revenue of Rs 10 Crores per month.

2. **Are the figures in Annexure B5 representative for aggregators? If not, what according to you are the correct representative figures? When providing representative figures, please provide figures for the category, and not of your company?**

We understand that given the huge MSO payout to the aggregators in the last two years, the three year averages are not representative as the industry in more skewed towards higher profitability in the last two years.

3. **Are the figures in Annexure B7 representative for the national MSOs? If not, what according to you are the correct representative figures? When providing representative figures, please provide figures for the category, and not of your company.**

We submit that PBT is the right measure to understand MSO business profitability than EBITDA as significant capital expenditure is incurred by the MSOs in digitizing headend and network and subsidizing Set Top Boxes at customer home. Depreciation to Turnover Ratio for MSO is significantly higher as compared to all other industry players since MSO business is the most capital intensive in the value chain. MSOs invest in Head ends, transportation, CPEs, and variety of other technologies. While it is inappropriate to evaluate MSO business on EBITDA, profitability, for understanding business sustainability as part of the value chain, a minimum EBITDA level of 30% to 35% needs to be earned by MSO to meet high depreciation costs and cost of capital required by the investments mentioned earlier.

After studying the EBITDA summary presented in B7, we submit that the information collated neither represents the MSO business model at National level nor at regional level. The business model of MSO is that of significant EBITDA losses, more likely represented in annexure B6. Any exclusion from the current business model as an aberration is being prejudicial.

In our experience, the MSO industry has seen significant increase in pay channel costs almost to the tune of 50% increase in the last two years, thanks to Content oligopoly by broadcasters and ever increasing number of pay channels.

We exhort that the MSO business model as it exists today is highly fragile and needs fair trade principles to be enforced by the regulator. We also submit that there is no rationale for excluding either early stage companies or acquired financials of businesses.

4. **Are the figures in Annexure B7 representative for the regional MSOs? If not, what according to you are the correct representative figures? When providing representative figures, please provide figures for the category, and not of your company.**

   Same as given in point 3 above.

5. **Are the figures in Annexure B9 representative for the LCOs with > 500 subscribers? If not, what according to you are the correct representative figures? When providing representative figures, please provide figures for the category, and not of your company.**

   LCO profitability is grossly understated and the industry average is in the range of 70% EBITDA margin. This segment of the industry is characterized by lower declaration, chronic default and large scale tax evasion.

6. **Are the figures in Annexure B9 representative for the LCOs with =< 500 subscribers? If not, what according to you are the correct representative figures? When providing representative figures, please provide figures for the category, and not of your company.**

   Same as given in point 5 above.

7. **What according to you is the average analog monthly cable bill in your state or at an all India level?**

   The average analog cable bill in urban market is approximately Rs 160-170 per month and is approximately Rs.100-120 per month in the rural areas.

8. **Is the market for cable services in non-CAS characterized by the following issues:**

i. **Under-reporting of the analog cable subscriber base:**

When all business arrangement between the MSO and the Content providers are based on the principle of *'negotiated declaration', there is no linkage to the actual number of people watching a pay channel. The* pay channel fees are negotiated as a lump sum for full bouquet and customer base is derived based on standard card rate of broadcaster for each of the channel forming part of the bouquet. This artificial computation ignores the fact that MSO is forced to take complete bouquet while he intends to show only part of the bouquet. At present, declared interconnect price of all pay-channels per subscriber is approx Rs. 730 which is a basic impediment for any transparent near-actual declaration by the LCO.

To quote an example, if a bouquet consisting of 4 channels negotiated at a fee of Rs. 20 Lakhs per month with an MSO, MSO subscriber base is arrived at after dividing the total amount by total card rate of all channels within the bouquet, say Rs. 25 and thus, a fictional figure of 80000 customer base is derived and recorded in the agreement. However, MSO would have needed only one channel out of the bouquet costing Rs. 10 and in his internal calculation, the number of subscribers would be 2Lakhs.

Moreover, sports channels are typically viewed for thirty days in a year during a particular sports event, while MSOs are forced to pay for full year at the card rates and a similar computation method is applied to arrive at an illogical customer base for the purpose of recording in the agreement.

Therefore, present processes for determination of subscriber base greatly exaggerates the phenomenon of under-declaration in the industry.

ii. Lack of transparency in business and transaction models

Point no (i) as mentioned above leads to vicious circle of lack of transparency across all stakeholders.

iii. Differential pricing at the retail level

Inability to extract higher price from the ground while giving the entire content further aggravates industry's inability to derive value

iv. Incidence of carriage and placement fee

Directly proportionate correlation between pay-channel costs and carriage and placement fee creates structural imbalance in the cost base of MSO industry model.

v. Incidence of state and region based monopolies

Content monopoly is prevalent in the industry and there is some amount of cartelization by same group operating various platforms of distribution apart from exercising content monopoly

vi. **Frequent dispute and lack of collaboration among stakeholders**

Yes, Main causes of disputes in this business are due to unreasonable terms imposed by pay channels on MSOs leading to disputes. The Regulations /legislations have failed to protect business interest of stakeholders.

9. **Are these issues adversely impacting efficiency in the market and leading to market failure**

   Yes

10. **Which of the following methodology should be followed to regulate the wholesale tariff in the non-CAS areas and why?**

    i) Revenue share
    ii) Retail minus
    iii) Cost Plus
    iv) Any other method/approach you would like to suggest

Popular content is a natural monopoly. If not regulated, it can lead to a monopolistic or oligopolistic market. It is for this reason, regulators provide for safeguards such as i)delinking of ownership between content producers (and resellers or agents) on one side and content distributers (DTH, MSOs etc) on the other side and ii) a 'must connect' clause in favour of content distributers. However, without a fair and effective regulation of content pricing, 'must connect' clause will become a toothless provision. If we agree with this proposition, then there are probably the following alternatives:

(a) Price Control: herein the regulator fixes the price at which the content is available to all content distributers. In India, we have been following a hybrid price control system whereby the content owner is free to fix price in the first instance with subsequent escalations being controlled by the regulator.

(b) Declared price with Most Favoured Customer (MFC) clause: In this case the Content producer/ seller would be free to declare the price for content and will undertake the obligation of providing most favoured customer treatment to each one of the content distributers. In other words the content producers/sellers cannot give preferential treatment to any content distributer on terms of trade. The effective implementation of

MFC clause will have be supported by audits by the regulator and periodic returns by the broadcasters.

Our suggestion is as follows:

Keep the existing TV Channels exceeding a certain threshold of TRPs for each genre (defined as - dominant Channels – see infra) under price control as hitherto (option (a) above). All other channels and new channels should be allowed to declare their price after undertaking obligation of MFC clause (option (b) above).

- Based on the experience, and after plugging loopholes found during the actual implementation, all the channels should be allowed to move to option (b) in say 3 years with a firm commitment. However, the regulator should keep a watch on the pricing of dominant channels and intervene where the price premium of such channels is unreasonable with regard to that of other channels in the same genre.

- Going immediately for option (b) for existing TV Channels exceeding a certain threshold TRPs is not recommended on the consideration of practicability. In the immediate context, it may lead to unpredictable consequences including an increase in consumer prices leading to a potential backlash against this policy. A gradualism in movement from controlled pricing to free market is prudent and time tested.

- For an effective implementation of option (b) it is mandatory that the there is a separation in ownership of content producers/sellers on one side and content distributers on the other side.

- **However, to help unstructured and fragmented cable business to smoothly transition into competitive market place, 'CAS pricing' should be allowed as an option for the addressable cable platforms for a period of 3 years.**

11. **If the revenue share model is used to regulate the wholesale tariff, what should be the prescribed share of each stakeholder?**

    Similar principles of CAS based tariffs should be applicable, should this route be preferred.

12. If the cost plus model is used to regulate the wholesale tariff, should it be genre wise or channel wise?

While we strongly recommend that the cost plus model should not be used to regulate the wholesale tariff, in the unlikely event it should be broad-based at genre level to encourage efficiency frontiers.

13. Can forbearance be an option to regulate wholesale tariff? If yes, how to ensure that (i) broadcasters do not increase the price of popular channels arbitrarily and (ii) the consumers do not have to pay a higher price.

Please refer to our recommendation under Question No. 10

14. What is your view on the proposal that the broadcasters recover the content cost from the advertisement revenue and carriage cost from subscription revenue? If the broadcaster is to receive both, advertisement and subscription revenue, what according to you should be the ratio between the two? Please indicate this ratio at the genre levels.

As practiced worldwide, content owner should have revenue streams either through subscription or through advertisement. In case of pay-channels, the source of income should only be subscription revenue and there should be no advertisement revenue. For example, BBC UK HBO far east. Similarly in case of channels deriving revenues through advertisement, no subscription revenue shall be allowed.

Dual streams of revenues to content owner are detrimental to the industry at large.

15. What is your view on continuing with the existing system of tariff regulation based on freezing of a-la-carte and bouquet rates as on 1.12.2007; and the rate of new channels based on the similarity principle at wholesale level?

The current tariff design is highly prejudicial to the industry at large, especially to the end consumer with the total bouquet cost of Rs. 730 (bouquet rate as declared by all leading pay channels assuming availability of all channels offered by them) should there be 100% declaration. We recommend to cap the existing total declared bouquet cost of all pay channels at a percentage of end subscription, to be determined by the regulator. Those broadcasters who do not opt for this model should offer their content only on addressable system.

16. Which of the following methodologies should be followed to regulate the retail tariff in non-CAS areas and why?
i) Cost Plus
ii) Consultative approach

iii) Affordability linked
iv) Any other method/approach you would like to suggest.

As per our response to Q no. 10 and 15.

17. In case the affordability linked approach is to be used for retail tariff then should the tariff ceilings be prescribed (i) single at national level or (ii) different ceilings at State level or (iii) A tiered ceiling (3tiers) as discussed in paragraph 5.3.23 or (iv) Any other

Not recommended due to difficulties in implementation.

18. In case of retail tariff ceiling, should a ratio between pay and FTA channels or a minimum number of FTA/pay channels be prescribed? If so, what should be the ratio/number?

Not applicable in view of our suggestion

19. Should the broadcasters be mandated to offer their channels on a-la-carte basis to MSOs/LCOs? If yes, should the existing system continue or should there be any modification to the existing condition associated with it?

Yes, broadcasters be mandated to offer their channels on a-la-carte basis to MSOs/LCOs. Current lopsided ala carte pricing should be annulled and a la carte pricing should be same that of bouquet split declared by the broadcaster to TRAI. This will encourage consumer choice at an affordable cost.

20. How can it be ensured that the benefit of a-la-carte provisioning is passed on the subscribers?

By aggressively encouraging addressable platforms for pay channels and by enforcing subscription or advertisement based content pricing as mentioned in Q no. 14

21. Are the MSOs opting for a-la-carte after it was mandated for the broadcasters to offer their channels on a-la-carte basis by the 8th tariff amendment order dated 4.10.2007. If not, why?

Current a la carte pricing is lop-sided and goes against the basic premise of a la carte pricing. Unless the la carte pricing is same as current bouquet pricing (per channel), the basic intent of encouraging choice is defeated.

22. **Should the carriage and placement fee be regulated? If yes, how should it be regulated?**

Primary reason why carriage exists is because of inadequate capacity of analog system to carry TV channels. This can be addressed only by rapid increase in addressable system. However the question arises if there should be a price regulation in the short term. Unfortunately in absence of any effective 'must carry', no price regulation is implementable. In any case the economic rationale for price regulation on carriage goes away once TV channel content pricing is freed as suggested above.

One of the easy but highly effective long term solutions for this is for the content owner to put in content on the web from where it can be streamed to computers, laptops and TVs. 'Direct from Web' can free the content provider from tyranny of chasing the limited distribution capacity that exists today. However, to make 'Direct from Web' successful, no channel should be allowed to deny its access on this platform

23. **Should the quantum of carriage and placement fee be linked to some parameters? If so, what are these parameters and how can they be linked?**

Consistent with the view expressed in our response to the previous question, it is not possible to regulate or control quantum of carriage and placement fee in absence of any effective 'must carry' provision.

24. **Can a cap be placed on the quantum of carriage and placement fee? If so,how should the cap be fixed?**

Same as given in 23 above

25. **Is there a need for a separate definition of commercial subscriber in the tariff order?**

Television viewing experience should be non-discriminatory in nature and the end subscriber tariff shall be applicable in similar manner as that of a non-commercial subscriber.

26. **If the commercial subscriber is to be defined in the tariff order, then does the existing definition of 'commercial subscriber' need to be revised? If yes, then what should be the new definition for the commercial subscriber?**

Not applicable in view of our response to Q no 25

27. **In case the commercial subscriber is defined separately, then does the present categorization of identified commercial subscribers, who are not treated at par with the ordinary subscriber for tariff dispensation need to be revised? If yes, how should it be revised?**

Not applicable in view of our response to Q no 25

28. **Should the cable television tariff for these identified commercial subscribers be regulated? If yes, then what is your suggestion for fixing the tariff?**

Not applicable in view of our response to Q no 25

29. **Do you agree that complete digitization with addressability (a box in every household) is the way forward?**

All developed countries have discontinued analogue platforms. We strongly recommend all addressable platforms for complete digitization be encouraged and supported by regulator with an aggressive time line for complete phase out of analogue platforms.

30. **While addressability is the way forward, cable platform needs an appropriate policy framework to make the transition over next few years.**

We recommend complete digitization of all state capitals in the next 12 months and for all B category cities in next 24 months with transient mechanism as articulated in the preceding responses.

31. **What according to you would be an appropriate date for analog switch off? Please also give the key milestones with time lines.**

We recommend complete digitization of all state capitals in the next 12 months and for all B category cities in next 24 months with transient mechanism as articulated in the preceding responses. Complete analogue switch off should be targeted in the next three years.

32. **What is the order of investment required for achieving digitization with addressability, at various stakeholder levels (MSOs, LCOs and Customers)?**

Given the fragmentation of LCO segment, it is recommended that MSO takes the lead to digitize on the basis of pay channel content being available only on the digital platform.

33. **Is there a need to prescribe the technology/standards for digitization, if so, what should be the standard and why?**

ITTU standards to be followed.

34. What could be the possible incentives that can be offered to various stakeholders to implement digitization with addressability in the shortest possible time or make a sustainable transition?

Capital subsidy on the CPE along with aggressive mandate to launch all new channels in addressable platforms with fiscal incentives. Regulator to mandate a phased switch over of content owners from Analog to Digital in the next 24 months. These proposals eventually will result in revenue neutrality as the service tax compliance offsets any possible revenue impact.

35. What is your view on the structure of license where MSOs are licensed and LCOs are franchises or agents of MSOs?

It is recommended that CAS guidelines in this regard be followed

36. What would be the best disclosure scheme that can ensure transparency at all levels?

Transparency through addressable platform coupled with mandated analog phase out

37. Should there be a 'basic service' (group of channels) available to all subscribers? What should constitute the 'basic service' that is available to all subscribers?

Competition should be encouraged through value chain to protect end subscriber interests.

38. Do you think there is a need for a communication programme to educate LCOs and customers on digitization and addressability to ensure effective participation? If so, what do you suggest?

Given the fragmented and highly profitable LCO segment of the industry, it is recommended that a mandated switch over to Digital, as had been the case in developed countries, with appropriate incentives to the value chain stakeholders will pave the way for complete digitization.

Thanking You,

Yours Sincerely,

For Kable First India Private Limited.

Authorised Signatory

KABLE FIRST INDIA PVT. LTD.