

Tatas – Acquirer or Administrator of VSNL?

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The Ministry of Telecommunications has raised a hullabaloo over VSNL's proposed investment of Rs12bn in Tata Teleservices over 4 years for a 20 to 26 per cent stake. Some of the quotable quotes emanating from the ministry are – “mockery of disinvestment and would be stopped”, “breach of trust”, “money invested is part of old management and does not belong to strategic partner”, “I will keep this in mind for future disinvestment proposals related to companies under my ministry”.

The Tata group had acquired a 25 per cent stake in VSNL for Rs14.39bn. It will have additional 20 per cent through an open offer amounting to Rs11.51bn. The ministry is peeved that VSNL's Rs12bn investment in Tata Teleservices would effectively cut the Tata's acquisition cost for VSNL by 46 per cent.

Tata Teleservices is a basic services operator in Andhra Pradesh with about 150,000 customers. It has licences to operate in Delhi, Tamil Nadu, Karnataka and Gujarat. The proposed project cost of Rs82.47bn is to be funded by Tatas (Rs25.52bn), VSNL (Rs12bn), non-Tata companies (Rs5.73bn) and debt (Rs39.22bn). The company is reviewing its options in Kerala, Punjab and Haryana. It is also in discussions with Hughes Telecom, which offers basic services in Maharashtra and Goa.

Role of Government

The divestment process entailed handing over management control to the Tatas. Indeed, that was the basis on which the Tatas agreed to commit over Rs25bn for 45 per cent stake. The shareholders' agreement provided for certain safeguards. For instance, the government's interests would be protected by its two nominees on the Board. Further, (physical) asset stripping required positive approval from the government nominees on the Board.

The government thus was left with two forums to influence decisions –

1. As a shareholder in general meetings of the company.
2. Through its directors in meetings of the Board.

Further, as a shareholder it has safeguards under the Companies Act, 1956 for prevention of oppression.

If the government flexes its muscle outside of these legally available forums, and threatens to use its discretionary powers in future to the detriment of any group, then we cannot claim to be a democracy. *Arm-twisting by the government is normally a characteristic of dictatorships.*

It was not too far back that the Government mopped up close to Rs20bn from VSNL through a 750% special dividend and 500% annual dividend. VSNL was valued on the basis of what remained. So there can be no differentiation between money that belongs to “old management” and money created by new management. When management control is passed on, the new management has to have the flexibility to run the company. There is no justification for backseat driving by the Government.

If the government cannot agree to this principle, then it should not divest businesses. It should appoint administrators, who will manage the companies in the interests of the government. But in such transactions, the government will not earn divestment proceeds to support the budget. *The Government cannot eat its cake and have it too.*

Conduct of Meeting

The actual events related to the Board meeting are fuzzy. While VSNL claims to have given one week's notice, a government nominee director disagrees. Similarly, the government nominee claims to have dissented from the decision to invest, while VSNL says the decision was unanimous.

It is not difficult to establish whether the notice for the meeting was given in time. Further, under section 193 of the Companies Act, 1956, the minutes of the Board Meetings would need to mention the names of directors dissenting from or not concurring with any resolution.

VSNL as well as the nominee directors however agree that the notice for the board meeting had a mention about proposed investment by VSNL, without mentioning Tata Teleservices specifically. Proposed investments in public companies are often shrouded in secrecy on account of likely impact on stock prices of the investee company – particularly if the investment does not go through. Tata Teleservices being a closely-held company, there was perhaps no need for the secrecy. The notice for the meeting could have made it clear that investment was being considered in Tata Teleservices.

Clearly, there was scope for greater transparency in the notice. But that does not become the basis to cancel a decision – particularly if, as VSNL claims, the notice was given on time and the resolution was passed unanimously.

The Decision

A few months back, VSNL was keen on entering basic services in Maharashtra and Delhi. It was not permitted because the law provided for only two government players – slots that were taken up by MTNL and BSNL. VSNL therefore remains primarily an international long distance (ILD) company, earning nearly 90% of its revenues from this business.

VSNL has justified its decision to invest in Tata Teleservices on the basis that it needs access to customers. Investment in a basic services operation will ensure this access. MTNL and BSNL have tied up with VSNL for ILD services. If they shift to say, IndiaOne of Bharti Telesonic, then VSNL will be left high and dry.

What needs to be considered is the emerging scenario. Soon, subscribers will be able to choose their ILD carrier. When that happens, the role of the basic services operator in routing calls to any specific ILD will be considerably reduced. Only default calls (where the subscriber has not dialled the carrier access code (CAC) of any specific ILD service provider) would go through the ILD service provider preferred by the basic services operator.

VSNL, by creating a strong ILD brand can ensure that subscribers would prefer its services. This would obviate the need to invest in basic or cellular services operation – and probably ensure better return on capital employed in the business.

The merits of the investment decision can be debated. Business models can be questioned. For instance, it can be argued that subscribers will not be inclined to enter the CAC, thus increasing the default calls, and therefore the role of the basic / cellular services provider. But what is not debatable is the "hands off" role expected of government, if the divestment program is to succeed.