

Annex - 1

Position Paper from the Telecommunications Regulatory Authority of the Kingdom of Bahrain on the treatment of intra-group revenues in relation to licence fees

Introduction

- 1 The purpose of this paper is to clarify and affirm the position of the Telecommunications Regulatory Authority of the Kingdom of Bahrain (“**the Authority**”) on the treatment of intra-group revenues in relation to licence fees.
- 2 It is intended to provide guidance to licensees when reporting financial information to the Authority to enable the Authority to calculate the applicable annual licence fees.
- 3 Where a licensee earns revenue from intra-group transactions, this revenue should be valued in accordance with the principles set out in this paper and included for the purposes of calculating licence fees.

Background and relevant legal basis

- 4 Pursuant to Article 3(c)(6) of the Legislative Decree No. 48 of 2002 promulgating the Telecommunications Law (“**the Law**”), the Authority has the power to set and collect fees under any licence.
- 5 Pursuant to Article 18(a)(2) of the Law, the Authority is to be funded from sources including annual licence fees, based (in the case of an individual licence) on the gross annual turnover of the licensee.
- 6 Pursuant to the Revenue Reporting Regulation dated 19 February 2020 (“**the Revenue Reporting Regulation**”), licensees are required to submit by 1st of April of each calendar year an Annual Audited Financial Statement and Revenue Reporting Declaration to the Authority, in order to enable the Authority to calculate the applicable annual licence fees.

Intra-group revenues

- 7 Intra-group revenues arise where a licensee provides services to another part of its corporate group. For example, a licensee may provide wholesale services to another company in its group, which uses those wholesale services to provide retail services to end customers.
- 8 In the Bahrain context, intra-group revenues may occur in the context of purely domestic arrangements e.g. where Bnet B.S.C. provides wholesale services to Batelco in Bahrain. They may also arise where an international operator holding a licence in Bahrain provides services in Bahrain to another part of its operations which is outside Bahrain (e.g. call termination).

- 9 In addition, intra-group revenues may arise where a multinational operator is providing telecommunications services to a customer covering a number of jurisdictions and its group licensee company in Bahrain is providing services in relation to the Bahrain element. In this scenario, typically the bundle of different services are provided under a single framework agreement concluded between the multinational operator and the customer.
- 10 In such a case, a reasonable proportion of the revenues arising under the framework agreement (or other such arrangement) should be allocated to the group licensee company, in accordance with the services provided in Bahrain, and reported to the Authority as revenue of that licensee. For these purposes, the proportion allocated should reflect the actual value of the services provided in Bahrain, which may differ from the revenue allocated to those services under the relevant contractual arrangements. This is to ensure that the actual business transactions undertaken between companies in the same group are appropriately identified, reflecting the economic reality of the situation.

Attributing a value to intra-group revenues

- 11 In certain situations, it may be that a market value has already been attributed to intra-group revenues.
- 12 Where this is not the case, a reasonable value should be attributed to such revenues, to ensure that the licensee's revenues are not understated for the purposes of calculating the applicable licence fee. For these purposes, the value attributed should reflect the economic reality of the situation, which may differ from the value attributed under any contractual arrangements that are in place. In particular, in attributing a value, the licensee should (i) identify accurately the actual commercial or financial transactions with the other part of its corporate group and (ii) where relevant, compare the valuation of those transactions with the valuation of comparable transactions with third parties.
- 13 In relation to identifying the actual transaction, an intra-group service arises where an activity is performed for another member of the group, which has provided that other member with economic or commercial value to enhance or maintain its business position. One means of seeking to determine this is whether an independent third party would have been willing to pay for the relevant service (or would have provided the service in-house for itself). If so, the relevant activity is likely to constitute an intra-group service.
- 14 In relation to comparing the valuation of the transaction with the valuation of comparable transactions with third parties, it will be important to understand the basis that has been used to value the transaction. This might be on the basis of a specific direct charge for the relevant service or on the basis of cost allocation and

- apportionment methods. Once this is established, the valuation should be compared with how much a third party would be prepared to pay for the relevant service in comparable circumstances, taking into account the value of the service to the third party and the costs of providing the service. If there is a material difference between the two, the valuation will need to be adjusted to reflect what the third party would be prepared to pay.
- 15 Particular considerations arise in relation to transactions involving intangibles (ie non-physical assets, such as intellectual property). In such circumstances, it is important to identify the nature of the intangibles and the rights that are transferred, including any limitation imposed on those rights. As regards comparing the valuation of transactions involving intangibles with comparable transactions with third parties, it is important to consider the options realistically available to each of the parties in determining a price that would both be acceptable to the transferor and allow the third party transferee to earn a profit.
- 16 The Authority notes that there are international initiatives being undertaken in order to resolve issues arising from base erosion and profit shifting strategies adopted by multinational companies. These strategies seek to exploit differences in tax rules between jurisdictions to shift profits artificially to low or no-tax locations where there is little or no economic activity or to erode tax bases through deductible payments such as interest or royalties. The Authority expects licensees not to engage in such strategies and to ensure that their transactions are accounted for in a way that reflects economic reality and that revenues actually earned in Bahrain are appropriately recorded and reported as such.

Appointment of auditor

- 17 Upon finding an apparent discrepancy in the treatment of intra-group revenues by a licensee, the Authority shall, after undertaking a preliminary assessment, have the right to engage a firm of independent auditors, pursuant to Article 13 of the Revenue Reporting Regulation, to carry out a detailed audit of the accounting records of the licensee in question. Following the audit, the Authority may, by means of a decision, adopt the valuation which is determined by the auditors to be the fair valuation of an intra-group transaction for the purposes of the calculation and payment of the relevant licensee's annual licence fees.

Retention of financial records

- 18 Licensees must retain financial records of their intra-group revenues for a minimum period of ten years in accordance with Article 5 of the Revenue Reporting Regulation.

Conclusion

- 19 The Authority believes that this Position Paper clearly confirms how the treatment of intra-group revenues should be applied by licensees (and their respective external auditors) for the calculation of licence fees. Where a licensee earns revenue from intra-group transactions, this revenue should be valued in accordance with the principles set out in this paper and included as revenue for the purposes of calculating licence fees.
- 20 The Authority requires that the contents of this Position Paper are drawn to the attention of each licensee's auditors by the licensee.
- 21 A process map is attached at Schedule 1 to assist licensees in applying the principles set out in this paper.

Schedule 1 – Process Map

Step 1	Has a licensee provided a service to another part of its corporate group (“ intra-group transaction ”)? If so, proceed to step 2.
Step 2	Revenue attributable to the intra-group transaction must be included when reporting the licensee’s revenue to the Authority for the purposes of calculating the licensee’s annual licence fees. Proceed to step 3.
Step 3	Has a market value been attributed to the intra-group transaction? If so, proceed to step 5. If not, proceed to step 4.
Step 4	The licensee should attribute a reasonable value to the intra-group transaction which reflects the economic reality of the situation and in accordance with the principles set out in this position paper. Proceed to step 5.
Step 5	Include the relevant value of the intra-group transaction when reporting the licensee’s revenue to the Authority for the purposes of calculating the licensee’s annual licence fees.
Step 6	The Authority may appoint independent auditors to carry out a detailed audit.
Step 7	Issue annual licence fees.