Passive infrastructure sharing
Why sharing?

Passive infrastructure sharing started with mobile phone towers. Mobile network operators allowed each other to hang antennas on their mast sites, resulting in consolidation of existing estates and lower capex for network rollouts. This required operators to calculate that financial benefits outweighed any loss of competitive advantage from network coverage at premium sites. Passive infrastructure sharing has developed into emerging markets, into parts of infrastructure beyond the basic “steel” of the tower, and with different financial models, including specialist “Towerco” companies that do not operate networks. Passive network sharing is primarily driven by:

Opex reduction – sharing costs of shared infrastructure between multiple operators, sometimes via an intermediary. This is a driver in more penetrated and mature markets where price competition and margin pressure are big features of the market.

Capex reduction for network rollouts. This is a driver for new entrants, for rollout in under-penetrated markets and rural areas, and where a new technology (e.g. 3G) requires more extensive sites.

Capital raising – monetising real estate assets by a sale-and-leaseback with a specialist tower company. This is a way of raising capital for investment in other markets, or for new technologies. It has higher transaction costs than accessing debt and capital markets.

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How are tower sharing deals structured?

Tower sharing between operators

Operators permit each other to install active equipment on their respective towers under a bilateral agreement. This is what Telefonica O2 and Vodafone did in 2009 for their operations in the UK, Ireland, Spain and Germany. The commercial deal is typically cash neutral but may include a rental payment by one party, depending on the relative value of the towers and the number of sites each uses. These were some of the earliest tower deals. They required competitors to see the benefit of cooperating, but then paved the way for Towerco businesses. There is a view among some industry players that inter-operator sharing can be a “dead-end”, because once a portfolio is shared between operators, the different timing, strategy and financing needs of the operators make it more difficult to take it further by monetising through a sale-and-leaseback, or deeper sharing of active elements. Sharing is also of more use to established operators than new entrants.

Sale-and-leaseback structures

Sale-and-leaseback structures can be used to establish tower sharing between operators, or between an operator and an existing Towerco. Towers are transferred to a specialist Towerco and space on them is “leased” back to the party that contributed them (and, in order to generate returns for the Towerco, to other operator parties to the deal and/or third party operators). The capital value of the real estate is released by its sale to the Towerco. If it is set up as a new share between operators, this is typically a “clean” joint venture company and can therefore be used to raise third party investment, or potentially be transferred entirely as part of a subsequent tower sharing deal. Such deals have been especially popular in emerging markets, particularly where passive infrastructure was not already extensively rolled out. Perhaps unsurprisingly, this model is especially popular with new entrants who need to roll out a network. Examples include the establishment of Indus Towers in India (a joint venture between Vodafone Essar, Bharti Group and Idea Cellular) and the sale by South African operator Cell C of its towers to a local subsidiary of American Tower.

Sale-and-leaseback deals are typically structured using the following agreements (in addition to any joint venture agreement relating to the newly-established Towerco):

– An Asset Sale Agreement, under which the relevant towers/assets are transferred. This may provide for a series of phased transactions to account for the process of transferring a large numbers of sites.

– A Master Lease Agreement, under which the Towerco agrees to grant the operator rights to co-locate equipment on the towers that are the subject of the deal. This is technically a licence-to-occupy, rather than a lease, depending on the property law of the jurisdiction involved. An anchor-tenant will normally negotiate preferential rights as a result of providing the anchor revenue for the Towerco. Rights may include prime position on the relevant towers, rights of first refusal on any future sites acquired by the Towerco, as well as pricing preferences (although, if the deal is with an independent Towerco, it will resist attempts to apply pricing preferences to additional sites beyond those contributed by the operator).

– A Master Services Agreement, under which the Towerco commits to provide varying “inputs”, such as periodic and emergency maintenance and the supply of power services, in respect of the transferred towers (and, potentially, towers added to the scope in the future). The Towerco may provide service level commitments (sometimes linked to capped service credits), but as it normally only provides the “steel”, rather than active
equipment, these do not typically extend to commitments about availability of equipment at the site.

– A Build-To-Suit Agreement (sometimes called a “Site Acquisition Agreement”) under which the Towerco undertakes to find appropriate sites for future network rollout (or upgrades to future generations of equipment, which may require a denser network).

**Outsourcing**

An operator may outsource the operation and maintenance of its towers to a Towerco, and/or install equipment on towers owned and operated by the Towerco. Towerco fees are lower than an operator’s equivalent opex for its own towers, due to the Towerco’s pooled resources.
Key issues in tower sharing deals

Due diligence

All tower sharing deals are likely to involve some level of due diligence process in respect of the relevant tower portfolio(s). The process is likely to be more extensive if the contributor of the sites will not retain a significant stake in their ownership (e.g. through its shareholding in a joint venture Towerco), or where it resists giving extensive warranty protection in the relevant asset transfer agreement.

The importance of this issue must not be underestimated by a mobile network operator considering undertaking a tower deal. If the operator invests time in preparing a thorough database of sites (according to GIS location, configuration of the tower, occupancy of antennas, access to power, security of tenure of property rights, and other factors relevant to local market conditions), the operator will be able to conduct an efficient transaction, and ideally a form of auction.

Financial motivations

If the primary purpose of a tower deal for an operator is to monetise infrastructure, consider whether there is a more efficient way to raise capital. Tower deals are complex, requiring extensive information gathering and negotiation on commercial issues. They may also require extensive engagement with government authorities, especially in emerging markets. On the other hand, a tower deal in which multiple operators are willing to share infrastructure is currently seen as one of the most effective means of capex and opex reduction available to the mobile industry.

Valuation

Valuation methodologies can be more developed in mature markets where comparable deals may have recently been completed. Each tower site’s valuation may be based upon its capability to accommodate multiple operators and an “urban/rural/remote” categorisation.

Jurisdiction specific legal issues

Local legal advice is needed on the laws of the towers’ jurisdiction, taking into account issues such as statutory rights to access tower sites, mandatory environmental and health and safety requirements for tower sites.

It may also be a requirement in the relevant jurisdiction to be locally incorporated and/or wholly or partially locally owned to construct, own or operate towers. Although in most countries telecom towers are not seen as a sensitive industry and do not attract foreign ownership or regulation, some countries require a Towerco to hold a licence, but allow foreign investment in licensees (e.g. Ghana, or India, which has proposed an FDI limit of 74%), but
others impose more stringent requirements (e.g. Indonesia, which requires 100% local ownership).

For joint venture deals in emerging markets, which may require financial participation by a local partner and often involve dealing with government officials (e.g. for transfer of ownership of the portfolio), the parties should also consider anti-bribery legislation that applies to jurisdictions relevant to the holding structure of the investor group (such as the US Foreign Corrupt Practices Act or the UK Bribery Act).

Third party rights/agreements

Third party rights relating to towers can affect the parties’ flexibility to transfer towers and to enter into subsequent deals relating to them. Parties should consider landlord consents relating to tower sites (noting that sites may be government owned for towers built on public land, and therefore subject to a statutory regime), or rights granted to other operators or Towercos as part of any previous tower sharing arrangements. The parties may or may not wish to keep in place third party “input” agreements relating to the towers, or may seek to renegotiate them to obtain preferential terms as part of the deal.

Regulatory approvals

Local telecommunications regulator approval may be required, but regulators are generally encouraged to approve infrastructure sharing arrangements (and some even mandate them, as is the case in New Zealand and China). Issues relating to local anti-competition/anti-trust regulations may also be relevant, depending on local law and the market position of the parties.

Tax

The jurisdiction of the company that will own the towers and any intermediate holding company (or companies) will be influenced by local tax laws, and any double taxation agreements where multiple jurisdictions are relevant. Taxes on transfers of interests in property can be especially difficult in tower deals. In emerging markets, telecom network infrastructure may have been imported with reduced customs duties (to encourage network build), and a disposal of infrastructure by the operator may trigger a claw-back of these customs concessions.

Accounting

From an accounting perspective, the party contributing the towers may wish to retain the assets on its books, derecognise the assets (i.e. transfer them to a third party or joint venture company), or partially derecognise them. The operator’s accountants will need to advise on what needs to be done to achieve this.
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