INDIA – REGULATORY UPDATE

Could the CCI's determination to take down E- Commerce Marketplaces really be counter-productive?

Rarely does a day go by, without the Confederation of All India Traders (CAIT) or the All India Online Vendors Association (AIOVA), both powerful trader lobbies, accusing foreign owned e-commerce entities (such as Amazon and Flipkart) of having used underhanded means to circumvent the intent of India's Competition Act and Foreign Direct Investment policy. The accusations themselves come with such frequency, that it is surprising that they continue to be taken seriously by news agencies, as well as the Indian Government. This speaks to the serious political muscle that these associations enjoy as a large vote bank, which must be kept happy.

Is it at all possible that in this instance, the focus on these e-commerce giants is doing the opposite of encouraging free and fair competition? Does the CCI's continued concentration on these e-commerce giants have the propensity to force these already squeezed businesses to shut shop? Where will this leave the Indian consumer that has greatly benefited from the marketplace model during the pandemic? Will it be to the detriment of small businesses that online e-commerce has purportedly saved during the pandemic by providing them an outlet to their wares?

Let us consider some of the claims and consequences:

1. **Predatory Pricing**

One allegation is that these foreign owned ecommerce entities ensure that goods are priced below cost, with the intention of bleeding out competitors. Once these competitors have been pushed out, these e-commerce entities would then raise their prices to monopoly levels to recoup their losses. There are a few problems with this assertion:

- For predatory pricing to be an offence, it is necessary for it to be established that the entity in question is 'dominant'. Dominance is the ability of an entity to act independently of market forces. Here, clearly, one can see the likes of Flipkart and Amazon compete vigorously with each other, particularly in terms of the offers available during sale festivals. If either of them is indeed pricing below cost, it is doing so to meet competition from their biggest rival, rather than risk becoming irrelevant.

- The roundabout argument that pricing below cost is unto itself an indication that an entity is dominant has previously been rejected by the CCI in the OLA case.[1]

- There are multiple instances of new e-commerce entities entering the market, Nykaa and AJIO spring to mind immediately.
- E-Commerce entities with Foreign Direct Investment (FDI) cannot price products on the marketplace, nor can they sell directly to consumers. This is something that was ensured by way of India's FDI Policy, specifically by Press Note 2 of 2018 amending India's FDI Policy (PN2).

[1] Refer to paragraph 97 of *Fast Track Call Cab Pvt. Ltd and Anr. Vs. ANI Technologies Pvt. Ltd. (6 of 2015)*

- While not a legal argument, but an emotional one - mom and pop stores have had complete freedom to price how they like, often where markets are physically delineated. It is no wonder that these stores are complaining about their margins through trade associations when prices are lower on online marketplaces.

Overall, the breaking of the monopoly of mom-and-pop stores in their limited geographies, providing lower prices, a wider range, while also enabling the convenience of not having to leave the house during a pandemic in terms of customer benefit should be seen as far outweighing the need to protect the bottom line of these stores that have had it all their own way so far.

The claim from trade associations that foreign owned e-commerce entities are putting small retailers out of business is obviously a self-defeating one, because it means that they compete, necessarily making the market not restricted only to e-commerce marketplaces, and greatly reducing the likelihood that they are dominant in a market where the vast majority of sales are still made directly from a local store.

2. Use of Third-Party Seller Data

While the CCI decided not to pursue this in March of 2022 against Amazon, there have been repeated claims/concerns and news reports raised about the use of third-party seller data to reverse engineer goods of leading brands and small businesses, thereafter undercutting them to put them out of business through the entity's own 'private brands'.

This again is a claim that would require 'dominance' to be established. It is understandable if the brands have no choice but to sell on the marketplace, which is for all practical purposes an essential facility, but this is clearly not the case. Other than there being multiple online marketplaces, these brands can, and often do sell their goods through brick-and-mortar stores, as well as their own websites.

If it can indeed be established that no dominance exists in favor of the e-commerce marketplace giants we have mentioned before, one cannot help but come to the conclusion that the outcome of the use of data is clearly pro-competitive. These private brands usually offer a cheaper alternative to branded goods, often aping the market leader. Consumers then have a choice of buying an established product at a slightly higher price, or a cheaper substitute that is designed to do the same job.

Should the branded product have a suitably superior quality, be suitably differentiated, or be priced suitably reasonably, it is certain to survive. This is essentially the kind of competition that the free market predicates.

3. Differential Treatment

This is another area where the lines are extremely blurred between Competition Law and FDI Policy. Section 4(2) of the Competition Act 2002 states that a 'dominant' party cannot impose unfair or discriminatory conditions in the sale of services, here to be read as access to the marketplace. Needless to state here that the establishment of dominance would be a necessary criteria for this to even begin to be considered as something that could potentially fall foul of the Act.

Press Note 2, however requires the e-commerce entity to maintain a level playing field for its sellers on the platform.

It is notable that Press Note 2 also establishes that an ecommerce entity with FDI cannot have an ownership interest in sellers, and cannot dictate prices. Logically thus, what interest would a marketplace that survives on commissions have to discriminate against a seller, but based on performance or customer satisfaction?

It is interesting to note that the Enforcement Directorate, one of India's most powerful enforcement agencies, responsible for enforcing economic laws and a part of the Department of Revenue, only chose to send a notice to Flipkart and not Amazon for purported violation of FEMA, asking why a fine to the tune of USD 1.35 Billion should not be imposed. [2]

It appears that another way to bell the cat has been found here, where the antitrust challenge was destined to fail.

Analysis

There is little doubt that the overall impact of having Amazon and Flipkart operate and compete with each other, as well as disrupt existing supply chains is greatly pro-competitive when viewed from afar. Availability and customer choice have greatly improved. Prices and delivery times have nosedived.

Add to this the fact that both provide jobs, either directly or indirectly to thousands of people, which goes up significantly during Big Billion Days and the Great India Sale festivals. There are also multiple instances that can be found on the internet, whereby Amazon and Flipkart claim to have taken steps such as waiving listing and onboarding fees and providing working capital loans to enable small businesses to keep afloat during the pandemic.

Not for a minute can it be claimed that these organizations act solely altruistically. Positive media coverage and attention are nothing but attempts to drive up stock prices and profits. But where really are these profits? Both Amazon and Flipkart have reportedly made losses of over 500 and 300 million USD respectively[3]. This is without accounting for wholesale arms of both entities which also make massive losses.

Walmart procured a 77% stake in Flipkart in May of 2018 for USD 16 Billion. This was surely done with the hope that Flipkart would become profitable at some point in the future, or at least that Walmart would be able to sell its stake down the line profitably. Unfortunately for them, later that year, PN2 would come into play that would cut off one of the avenues to be able to make revenue, i.e. by selling directly to the customer.

It appears increasingly unlikely that Amazon or Flipkart will ever be able to turn it around to become profitable, particularly with mounting legal expenses and the threat of millions being imposed upon them as a fine.

[2] Refer to https://economictimes.indiatimes.com/industry/services/retail/enforcement-directorate-threatens-flipkart-its-founders-with-1-35-billion-fine-say-sources/articleshow/85056916.cms
[3] Refer to https://www.business-standard.com/article/companies/flipkart-clocks-25-growth-in-fy21-revenue-at-rs-43-357-cr-losses-drop-23-122010401221_1.html

It will be unfortunate if the myopic protectionist measures to protect Indian companies leads to a withdrawal of these established global e-commerce giants.

While active outreach programs that ensure you stay in the news for all the right reasons e.g. providing jobs, enabling cottage industries and small Indian businesses succeed will certainly help stem the tide of popular opinion against the 'outsiders', the importance of visibly and obviously being in compliance cannot be overstated particularly when it comes to FDI norms and the Competition Act. Some of the top most priorities should be:

1. Training your representatives on what to say, and what to avoid saying, such as ill-advised boasts about being beyond competition, including on social media. A tactless statement may seem innocent enough as mere puffery, but can, and often is used by regulators against you, and can be quite difficult to overcome. Train representatives not to publish unsubstantiated reports about your company on their own personal social media.

2. Keep in mind that regulatory and enforcement bodies in India are becoming increasingly sophisticated and cooperative (with each other). It is important to have a well thought out dawn raid policy in place, have a process in place to inform suitably appointed in-house and outside counsel in place to deal with investigation to ensure investigating authorities have suitable authorization in place, and do not collect data and information which is beyond their purview.

3. Establishing a culture of compliance, ensuring that new business activities, sales, discounts, exclusivity arrangements, pricing decisions and advertisements and publicity have been looked over specifically by counsel from the POV of eliminating what could be seen as a potential FDI or Competition Act non-compliance. Having a strong compliance program, and being able to prove a will to comply with FDI norms and the Competition Act will certainly go in a company's favor, and may even be an important factor to be considered for leniency or clemency.

4. Staying ahead of the curve may help, e.g. by ensuring your search algorithms are transparent, putting policies in place that ensure sellers are treated alike, and that decisions on prices are taken by sellers alone. It is also extremely important that records be kept to be able to show these actions in the event of being questioned by a regulator.

Admittedly, there is no bullet proof solution for safeguarding investments in an economy where ad-hoc decisions are unfortunately commonplace. The 4 steps mentioned above however, should go some way is providing some security to businesses.

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