

The State and the Digital Giants*

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The NDA government has decided to further tighten its regulation of e-commerce, taking on in particular foreign giants like Amazon and Flipkart-Walmart, with implications for domestic organized retail majors like Reliance. The Department of Consumer Affairs in the Ministry of Consumer Affairs, Food and Public Distribution has called for comments on an amended version of the Consumer Protection (E-Commerce) Rules, 2020, which it posted on its website in late June 2021. The amendments, conveniently highlighted using track changes, go beyond strengthening consumer protection per se. The intent seems to be to rein in dominant players in an area.

Among the many objectives that possibly motivate the government's interventions in the e-commerce space there are at least three that visibly matter here. The first is to preempt the possible abuse of market power to swindle customers financially or otherwise. The second, is to prevent use of such market power to crush the competition, consisting of a multitude of small and medium vendors and retailers. And the third is to exert control on how the large volume of data on suppliers and customers that e-commerce entities gather is used.

Consumer protection rules are not the only means available to pursue these objectives. In fact, the principal instrument the government has used thus far to rein in foreign e-commerce giants like Amazon and Walmart (which acquired Flipkart) is the set of regulations governing foreign direct investment (FDI) in the sector. FDI with 100 per cent foreign equity holding is permitted in e-commerce activities through the automatic route. But a review of the policy released in December 2018 had clarified that foreign direct invested e-commerce entities are only allowed to engage in Business to Business (B2B) and not Business to Consumer (B2C) transactions. Specifically, the guidelines noted that 100 per cent FDI under automatic route is permitted only in a marketplace model of e-commerce, where the platform merely was a place where suppliers and consumers discovered each other and transacted, and not in the inventory-based model, where the platform hosts companies that use it as their dominant or sole market or the e-commerce entity directly or through a subsidiary acquires and holds inventory of particular brands of popular to sell through its own channel. The latter could include sale through its marketplace of goods carrying the platform's unique private labels.

Firms like Amazon and Flipkart not only had exclusive marketplace agreements with some leading brands, especially in the electronics and mobile phones area, but had invested in vendors who are important sellers in their own marketplace. Amazon has, for example invested in Cloudtail India (which is owned by Prione Business Services that is held by Infosys founder Narayana Murthy's Catamaran Ventures with a 51 per cent stake, Amazon Asia Pacific Resources with 48 per cent and Amazon Eurasia Holdings with 1 per cent) and Appario Retail (which is a subsidiary of Frontizo Business Services that is held by Amazon Asia Pacific Holdings with a 48 per cent stake, Zodiac Wealth Advisors with 51 per cent and Zafre LLC with 1 per cent). Similarly, Flipkart was reportedly hosting sales by its subsidiary RetailNet. These entities were important vendors on the respective marketplaces.

The policy review effectively barred such firms from the ‘parent’ e-commerce platform, stating that the e-commerce entity providing a marketplace cannot exercise either ownership or control over the ‘inventory’ or the goods that are being sold through the marketplace. Control in this context had been defined as exercised when the combined sale by a vendor through the marketplace of an FDI-invested e-commerce entity and through its subsidiaries exceeds 25 per cent of its total sales. This would mean that if one or more FDI-invested e-commerce entities and its subsidiaries become the preferred marketplace of a substantial number of buyers of particular products, it would be seen as violating the FDI policy and invite penal action. This amounted to using the FDI policy also as an instrument to counter foreign investor oligopolisation of the retail trade. The principal objective, according to the policy review, was to ensure that foreign e-commerce entities “will not directly or indirectly influence the sale price of goods or services” and to maintain a level playing field. For that, services provided by the e-commerce entity to vendors on the platform must be delivered “at arm’s length and in a fair and non-discriminatory manner.”

According to a Reuters report from earlier this year, a leaked internal document of Amazon points to its strategic use of related firms Cloudtail and Appario to enhance profits earned in the Indian market through the e-commerce entity. The document allegedly reveals that sales by these related entities were ramped up to 47 per cent of total sales on the platform by 2016, through a process that was allegedly not all fair. With the government issuing new FDI rules in 2016 that capped sales by group companies at 25 per cent of the total, this had to stop. But soon Amazon found a way out, by diluting its stake in these related firms to below 26 per cent. Initially Amazon-owned companies such as Cloudtail withdrew from the platform. Amazon sold 25 per cent of its shares to Prione Business Services Pvt, a company run by Catamaran Advisors, to take Prione’s stake to 76 per cent from 51 per cent. The remaining 24 per cent was held by a non-Indian arm of Amazon.

Recently the Confederation of All India Traders (CAIT) had reportedly written to Commerce Minister Piyush Goyal calling for an investigation into the role of Cloudtail India and other similar players, on the ground that they were making a mockery of the law. CAIT alleged that Cloudtail India (P) Limited, Appario Retail (P) Limited, and other related firms together controlled a very large share of the business on the Amazon marketplace. Even though equity ownership does not indicate this, there was according to CAIT evidence of a close relationship and control by Amazon of these ventures. "In Cloudtail and its holding company, Prione Business Services, it is no coincidence that the managing directors, CFOs, key persons are (so-called) former employees of Amazon. Even the majority of board members of Cloudtail are (so-called) former employees of Amazon." This showed that share ownership notwithstanding, Cloudtail and Prione are managed and operated by Amazon through (so-called) former employees, the CAIT letter circulated on Twitter said.

The amendment to the Consumer Protection Rules may have partly responded to such demands. One amendment is an addition to the rules that states that: “Every marketplace e-commerce entity shall: (a) ensure that it does not use any information collected through its platform for unfair advantage of its related parties and associated enterprises; (b) ensure that none of its related parties and associated enterprises are enlisted as sellers for sale to consumers directly; (c) ensure that nothing is done by

related parties or associated enterprises which the e-commerce entity cannot do itself.” The term related parties is to have the same meaning as in section 2(76) of the Companies Act, 2013, under which enterprises shall be deemed to be associated, if “(a) enterprises are related to each other through a common chain of directors or managing partners; (b) enterprises are related to each other through a common chain of shareholders, where such shareholders hold not less than 5 per cent of the shareholding in the related enterprises; (c) enterprises having 10 per cent or more common ultimate beneficial ownership; and (d) where one enterprise can exercise a right to veto any decision, appoint one or more director(s) or in any other manner influence other entity’s decision making on any matter either through its shareholding or through an agreement including a shareholders’ agreement;.” With such a broad definition of relatedness, the likes of Cloutail and Appario would find it difficult to restructure themselves to remain within the law.

The amendments to the Consumer Protection Rules also seek to explicitly ban deep discounting. To start with the amended rules state that “no e-commerce entity shall organize a flash sale of goods or services,” where a flash sale is defined as sale “at significantly reduced prices, high discounts or any other such promotions or attractive offers for a predetermined period of time on selective goods and services or otherwise with an intent to draw large number of consumers offered on its platform.” Such sales, supported with discounts that involved large losses, were routine means adopted by e-commerce giants to attract consumers to their marketplace and to products and brands in which they had a special interest.

The proposed amendments to the rules also seek to regulate the use of data acquired by e-commerce entities through their operations. If notified, the rules requires every marketplace e-commerce entity to not make available any information pertaining to a consumer to any person other than the consumer without the express and affirmative consent of that consumer; not record such consent automatically, including in the form of pre-ticked checkboxes; not use information collected for sale of goods bearing a brand or name which is common with that of the marketplace e-commerce entity ... if such practices amount to unfair trade practice and impinges on the interests of consumers.

While the intent here seems to be to protect privacy and prevent unfair competition using information collected through e-commerce operations, the rules provide preferential access to the government to data. It requires that “every e-commerce entity shall, as soon as possible, but not later than seventy two hours of the receipt of an order, provide information under its control or possession, or assistance to the Government agency which is lawfully authorised for investigative or protective or cyber security activities, for the purposes of verification of identity, or for the prevention, detection, investigation, or prosecution, of offences under any law for the time being in force, or for cyber security incidents”. As in the case of the IT rules aimed at reining in social media majors like Facebook, Twitter and WhatsApp, as well as digital news portals like The Wire, Scroll and Quint, the objective here is surveillance. Clearly, there are multiple motivations underlying the government’s interventions in the digital sphere. And some of the stated motivations may be mere means to deflect attention from the government’s primary concerns.

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