

Online Retailers vs. Electronic Manufacturers: Competition Wars

Can a manufacturer of electronics that puts up a disclaimer on its website stating that it will not guarantee products from Online Retailers a contravention the Competition Act?

The present issue in hand seems to stem from the order dated 29.12.2014 passed by the Competition Commission initiating investigation into the conduct of the manufacturer namely Kaff Appliances (India) P. Ltd. in a case brought by M/s Jasper Infotech P. Ltd. (Snapdeal), hereinafter referred to as The Kaff Appliances¹ matter.

The Kaff Appliances matter was brought before the CCI, in light of a caution notice (disclaimer) that was issued by the manufacturers of Kaff appliances, wherein they had stated that any products that are purchased from Snapdeal.com are counterfeit and therefore the warranties on products so procured shall not be honored. Kaff had earlier vide an email wrote to Snapdeal, advising them not to sell their products below Market Operating Price (MOP).

Snapdeal filed a complaint before the Commission, stating that by issuing the aforementioned disclaimer, KAFF is attempting to limit its authorized distributor from selling their products through the e-commerce channel. Furthermore, it was contended that KAFF was imposing anti-competitive conditions on the authorized distributors by not allowing them to sell the products at a discounted price without prior permission of the manufacturers, thereby violating the provision under Section 3(4)(e)² of the Act. The Commission *prima facie* observed that the manufacturer cannot dictate the prices at which its products are to be sold by the authorized distributor, as that would hinder competition and the distributors would not be able to compete with the authorized distributors of other manufacturers in the market.

In light of the Kaff Appliances Judgment, a leading Online Retailer recently issued a notice to a leading Electronics Manufacturer accusing its caution notice to be “patently misleading, illegal, anti competitive and per se disparaging in nature.” The Electronics Manufacturer has also been accused of contravening various provisions of the Competition Act 2002 (The Act) along with conspiring to deny warranty to products sold through e-commerce to maintain a Market Operating Price (MOP) and restricting sale through e-commerce, the sole basis for which is the Kaff Appliances Judgment.

For the Kaff Appliances Judgment to apply, MOP needs to be proved as per the requirements given in Section 3 of the Act, which deals with vertical agreements. The entire onus of proving an agreement of this nature lies on the person who brings such a complaint. Such an accusation will have to be proved at four levels-

1. Existence of such an agreement which contravenes Section 3(e) of the Act;
2. Is competition affected in the relevant market³ [as per Section 19(5) of the Act];

¹ <http://www.cci.gov.in/May2011/OrderOfCommission/261/612014.pdf>

² Section 3. (4). Any agreement amongst enterprises or persons at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or price of, or trade in goods or provision of services, including— (6) (a) tie-in arrangement; (b) exclusive supply agreement; (c) exclusive distribution agreement; (d) refusal to deal; (e) resale price maintenance,

³ Section 19.(5) For determining whether a market constitutes a “relevant market” for the purposes of this Act, the Commission shall have due regard to the “relevant geographic market” and “relevant product market”.

3. Is there any Appreciable Adverse Effect on Competition⁴ (AAEC) [as per Section 19(3) of the Act];
4. Is insistence of LG that its products be brought from 'authorized dealers only' in contravention of the Act?

Existence of Agreement contravening Section 3 of the Act

The observations of the CCI in the Kaff Appliances Order were as follows:

"Para 13. The Commission also finds substance in the argument advanced by the informant wherein it has been contended that the existence of an agreement can be inferred from the conduct considered to be coercive when the level of coercion exerted to impose an apparent unilateral policy in combination with the number of distributors that are actually implementing the unilateral policy of the supplier would, in practice point to tacit acquiescence by the other party or parties."

"Para 18. The opposite party through an email informed the Informant that sale of its product below the MOP shall not be permitted which shows that the opposite party was having a minimum price maintenance agreement with its dealers also. Further, in a legal notice to the Informant dated 18.10.2014 the Opposite Party has stated that the goods manufactured by it are sold at its exclusive chain of authorized retail outlets and at the listed price only and any discounted schemes introduced and launched in the market is with the prior approval of the opposite party. Such an agreement hinders the ability of dealers/distributors to compete on the price of the product. The Commission feels that such prescription of MOP by the Opposite Party to its dealers and insistence to follow MOP pricing regime prima facie seems to be in contravention of Section 3(4)(e) read with Section 3(1)⁵ of the Act. "

In contravention to the facts of the above case, if the Manufacturer has sent no such correspondence to the Online Retailer in contravention of the aforementioned sections and thus, the onus of proving such an agreement lies entirely on Online Retailer it has to make out a prima facie case for the Commission to take cognizance which is unlikely.

⁴ Section 19.(3) The Commission shall, while determining whether an agreement has an appreciable adverse effect on competition under section 3, have due regard to all or any of the following factors, namely:— (a) creation of barriers to new entrants in the market; (b) driving existing competitors out of the market; (c) foreclosure of competition by hindering entry into the market; (d) accrual of benefits to consumers; (e) improvements in production or distribution of goods or provision of services; (f) promotion of technical, scientific and economic development by means of production or distribution of goods or provision of services. (4) The Commission shall, while inquiring whether an enterprise enjoys a dominant position or not under section 4, have due regard to all or any of the following factors, namely:— (a) market share of the enterprise; (b) size and resources of the enterprise; (c) size and importance of the competitors; (d) economic power of the enterprise including commercial advantages over competitors; (e) vertical integration of the enterprises or sale or service network of such enterprises; (f) dependence of consumers on the enterprise; (g) monopoly or dominant position whether acquired as a result of any statute or by virtue of being a Government company or a public sector undertaking or otherwise; (h) entry barriers including barriers such as regulatory barriers, financial risk, high capital cost of entry, marketing entry barriers, technical entry barriers, economies of scale, high cost of substitutable goods or service for consumers; (i) countervailing buying power; (j) market structure and size of market; (k) social obligations and social costs; (l) relative advantage, by way of the contribution to the economic development, by the enterprise enjoying a dominant position having or likely to have an appreciable adverse effect on competition; (m) any other factor which the Commission may consider relevant for the inquiry.

⁵ 3. (1) No enterprise or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition within India.

Competition affected in the relevant market⁶ of the person

The Commission noted in the San Disk Case⁷ of 2014 that-

“Para 15. The Commission is of the view that relevant product market in the present case is the market for portable small-sized consumer storage devices that includes USB pen drives, SD Memory Cards and Micro SD Cards, Based on factors such as intended use and price, both pen drives and memory cards can be considered as substitutes.”

“Para 16. The Commission is of the view that these two markets (online and offline) are different channels of distribution of the same product and are not two different relevant markets.”

Thus it is clear that the Commission believes that any products which exercise a sufficient price constraint on other products would form part of the same market. This means the relevant market for Electronics constitutes all major manufacturers of the substitutable products such as LG, Samsung, Panasonic, Sony etc. This also means that online and offline retail do not constitute separate relevant markets as they are merely different channels of distribution which are substitutable. In light of this knowledge, the Electronic Manufacturer would have to be in a position to really move the market with a large market share in order to create conditions as given in Section 3(1) of the Act which it doesn't. In the Kaff Appliances Case, CCI relied on the fact that the market share of the opposite Party was 28% which may not only harm the consumers but also likely to have an adverse effect on competition.

A normal Electronic Manufacturer doesn't fulfill this requirement given its big list of competitors and close substitutes and thus a prima facie case cannot be made out.

Is there any Appreciable Adverse Effect on Competition

CCI noted in the Mohit Manglani Case of 2014⁸-

“Para 15. That “Section 3(1) of the act unequivocally condemns only such agreement/arrangement/understanding which has or is likely to have an AAEC in the market. Vertical agreements/arrangements under section 3(4) and other agreements/arrangements which do not fall under section 3(3) are anti-competitive only when AAEC is proved. Therefore, the Commission has to consider various factors as laid down under Section 19(3) of the act to assess the effect of such exclusive arrangements between manufacturers and e-portals.”

It is clear from the market share argument and the wordings of Section 19(3) and (5) that LG does not in any way cause AAEC in the markets and far from a prima facie case being made out.

Insistence of the Electronic Manufacturer that its products be brought from authorized dealers in contravention of the Act?

⁶ Section 19.(5) For determining whether a market constitutes a “relevant market” for the purposes of this Act, the Commission shall have due regard to the “relevant geographic market” and “relevant product market”.

⁷ <http://www.cci.gov.in/May2011/OrderOfCommission/262/172014.pdf>

⁸ <http://www.cci.gov.in/May2011/OrderOfCommission/262/802014.pdf>

As observed in the San Disk Case-

“Para 19. Insistence by San Disk that the storage devices sold through online portals should be bought from authorized distributors by itself cannot be considered as abusive as it is within its rights to protect the sanctity of its distribution channel. In a quality driven market, brand image and goodwill are important concerns and it appears a prudent business policy that sale of products emanating from unknown / unverified / unauthorized sources are not encouraged/ allowed.”

“Para 20. The conduct of SanDisk in issuing such a circular can only be considered as part of normal business practice and cannot be termed as abuse of dominance.”

It is clear from the CCI order that the Electronic Manufacturer’s disclaimer against entities reselling its products purchased from unverified sources is merely Manufacturer protecting its own interest and goodwill and a prudent business policy.

Conclusion

The onus of establishing anti-competitive practice on the part of Electronic Manufacturer is entirely on the person who brings forward the complaint as a prima-facie case cannot be made out on the basis of the abovementioned principles supported by legislation and precedence.

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