

PRIMER 1

THE WHY AND HOW OF EX-ANTE COMPETITION PROPOSALS IN INDIA

UNPACKING THE PARLIAMENTARY STANDING
COMMITTEE ON FINANCE'S RECOMMENDATIONS ON
BIG TECH AND COMPETITION

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Recommendations on Big Tech and Competition

INTRODUCTION

The 53rd Report of the Parliamentary Standing Committee on Finance (**PSCF Report**) recommends framing a dedicated ex-ante (pre-emptive) regulatory framework for addressing competition issues in digital markets. This primer unpacks the “why” and “how” of the PSCF’s recommendations and tests the underlying assumptions through counterfactuals.

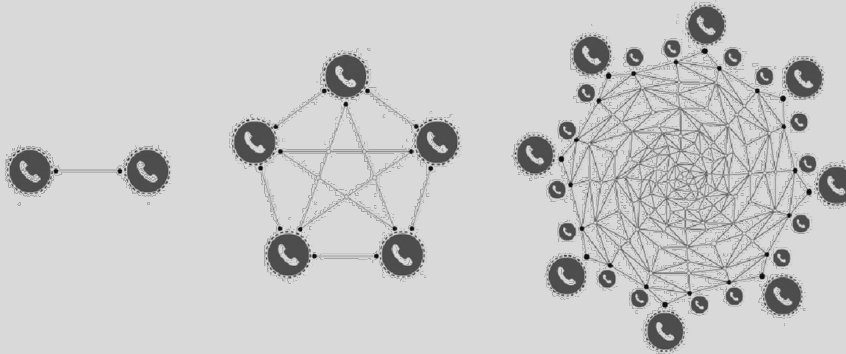
What Was Recommended?

- A set of pre-emptive rules governing the conduct of certain digital business with their customers and competitors.
- The pre-emptive rules would be over and above existing rules governing competition (i.e., the Competition Act) and rules governing other operational aspects of digital businesses (e.g., the Information Technology (Intermediaries Guidelines) Rules, the Consumer Protection (e-Commerce) Rules, etc.).
- The rules would apply to digital business of a certain size, determined based on the number of users, revenue or market capitalization.¹

Why Did the PSCF Recommend a Pre-Emptive Set of Rules for Digital Market?

Assumption 1: Digital Markets Favour Monopolies by Design

The PSCF noted that digital markets are susceptible to “tipping” owing to “network effects”. In its most basic form, “network effects” can be observed in telephone networks. A telephone network consisting of only two phones, will be of certain value to its users, since each phone can only communicate with one other phone.



However, the value of the telephone network would increase if it connected to more phones, since it enables more communication. A similar phenomenon is observed in digital markets, where the value of a service (e.g., social network) increases with additional users – thereby attracting more users to adopt the service.

The PSCF notes that at when a network has the greatest number of users amongst competing platforms – users would tend to flock to the largest network, reinforcing its market position (i.e., the market would “tip” in favour of the largest network).

¹ The Report recommends the term “Systemically Important Digital Intermediaries” (SIDIs) to refer to companies which are large enough to influence competitive conduct in the digital ecosystem. The Report proposes to identify SIDIs based on the size of their user base/ revenues/ market capitalization.

Counterfactual 1: Digital Markets Can Self-Correct to a Large Extent

The number of users, and therefore potential number of transactions between such users – can help a network grow to a certain extent. However, the quality of services offered by the network continue to be a key driver of value for consumers.

For instance, if a telephone network suffers from too many call drops, users would eventually be prompted to move to other networks. If a network cannot remedy this, it would lead to a vicious cycle where it would fall behind its competitors in terms of users.

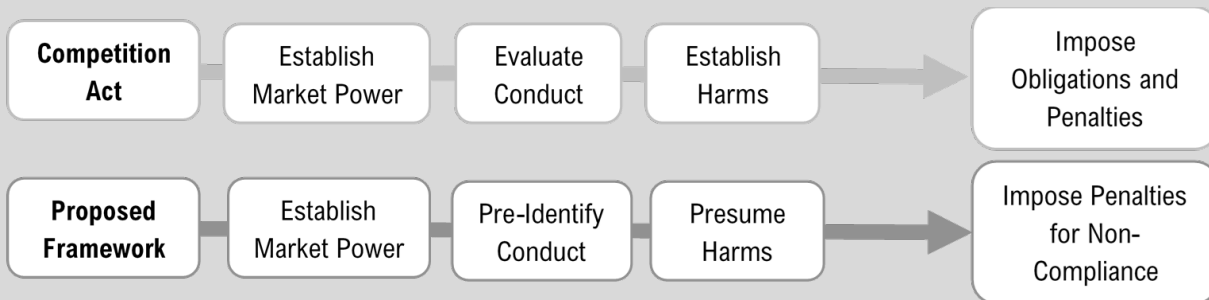
A similar phenomenon has played out repeatedly in digital markets, especially in the case of social networks and content sharing platforms. Platforms such as MySpace which failed to maintain quality of service, lost out to players such as Facebook. More recently, Facebook has seen a depletion of user base, in favour of newer more innovative, customized, and in certain instance more privacy friendly networks.

Creating a rigid set of rules, which presumes that digital markets cannot self-correct, could therefore be premature and lead to undesirable outcomes for Indian digital markets.

Assumption 2: Current Laws Cannot Prevent the Creation of Monopolies in Digital Markets

Since the number of users on a platform is a critical factor for a platform’s success, platforms have incentives to scale fast. Resultantly, a lot of technology companies focus their efforts on building a user base.

Based on the first assumption, that digital markets cannot self-correct owing to “network effects”, the PSCF recommends an approach where the regulator (the Competition Commission of India; **CCI**) can intervene at a stage where a technology company is yet to gain market power.



Under the current law, an intervention by the CCI needs to be based on evidence of (a) a company enjoying a certain level of market power (determined by market share, revenues, etc.); and (b) harms to competition and/or consumers, arising from a company’s conduct.

The PSCF observed that the time involved in gathering and evaluating the necessary evidence, can lead to the creation of a digital monopoly, and resultantly, unaddressed harms. Accordingly, the PSCF recommended a pre-emptive set of rules that could prevent the creation of monopoly position.

Counterfactual 2: The Competition Act Already Enables Prevention of Monopolies

The Competition Act already contains a set of pre-emptive rules to prevent attempts to monopolize a market through mergers and acquisitions. Any merger or acquisition between parties of a certain size (determined through their revenues) needs to be pre-notified to the CCI. With the Competition (Amendment) Act, 2023, the CCI will now have the power to review transactions valued at more than INR 2000 Crores, irrespective of the size of the companies. This can enable the CCI to review and/or block strategic acquisitions that seek to end the potential for future competition, by acquiring new entrants.

However, unlike its predecessor the Monopolies and Restrictive Trade Practices Act, 1986 (**MRTP Act**) which sought to prevent businesses from growing in any manner, the Competition Act does not prevent organic growth (i.e., growth in the ordinary course of business). This was a conscious move brought about by the Raghavan Committee (2000), which recommended shifting the focus of competition law from the size of a company, to the harms arising from its conduct. Therefore, the PSCF's recommendation could bring back the consciously abandoned MRTP approach, and in the process harm start-ups and other digital businesses from adopting legitimate business strategies for their growth.

HOW WOULD THE PROPOSED FRAMEWORK LOOK?

It Will Address Consumer Choice: The PSCF recommends prohibiting practices like pre-installation of applications, and bundling of services/products, since they impact consumer choice.

Factors Not Considered

- Practices such as bundling of products, discounting, etc. are beneficial to consumer, and do not decrease choices available to consumers. In any event, given that a consumer bears negligible/no costs for switching to other digital platforms, consumer choice is unlikely to get impacted by the practices identified by the PSCF.

It Will Address Data Usage Practices: The PSCF recommends placing restrictions on data usage by platforms, since access to extensive user data can be used as a strategic lever to exclude competitors and new entrants.

Factors Not Considered

- Data is not a finite resource. It can, and indeed is gathered with minimal costs by new entrants. Government frameworks like the Account Aggregator (AA) framework can bring down the costs of acquiring data further.
- Consensual data processing can lead to consumer benefit, since it enables personalization and improved user experiences. Similarly, data-driven decision-making allows companies to optimize resource allocation, and drive business growth.

It Will Address Platform Neutrality: The PSCF noted that platforms which acted as intermediaries, should refrain from practices such as self-preferencing (i.e., a business providing a favourable treatment to its own services, on its own platform) and anti-steering (i.e., preventing users from conducting transactions outside a business's platform).

Factors Not Considered

- Certain sector specific laws already require platforms to behave in a neutral manner (e.g., the FDI Policy on Ecommerce).
- Some of the identified practices, including self-preferencing and anti-steering, can benefit consumers. For instance, anti-steering could be crucial in ensuring integrity and security of transactions.

It Will Address Rise in Market Power: The PSCF recommends that certain large companies should mandatorily notify any intended acquisition irrespective of whether it is notifiable to the CCI or not.

Factors Not Considered

- The current law intentionally excludes non-problematic acquisitions, in order to better channel the limited resources available to the CCI.
- Some acquisitions may involve an acquisition of a non-controlling stake, intended to infuse additional capital to early-stage companies. Investments from digital companies has been a key driver of India's start-up growth. The proposed rule may negatively impact such investments.
- Recent amendments to the Competition Act, enable the CCI to review and/or block strategic acquisitions that could lead to lessening of competition in the market.

KEY TAKEAWAYS

- While intuitive at first glance, the PSCF's recommendations are based on certain untested assumptions about the nature of digital markets, and the sufficiency of existing laws.
- The PSCF's recommendations fail to undertake a wholistic evaluation of the effects of digital businesses' conduct, especially benefits accrued to consumers.
- Before implementing a new law to regulate digital markets, it will be prudent for policy makers including the Committee on Digital Competition Law to re-assess the assumptions and assessments made by the PSCF in its Report.

