



CHALLENGES AND EFFECTS OF DIPP'S REVISED FDI POLICY ON E-COMMERCE MARKETPLACE ENTITIES

❖ INTRODUCTION

The Department of Industrial Policy and Promotion (“DIPP”) under the Ministry of Commerce introduced Press Note¹ dated 26 December 2018 (“Press Note”) to bring in certain changes to the conditions applicable to e-commerce entities under the Consolidated Foreign Direct Investment Policy of 2017 with effect from 1st February, 2019. The main objective of amending the existing Foreign Direct Investment Policy (“FDI Policy”) relating to e-commerce activities is to protect the interests of the small time offline and online retailers in the Indian market from the deep discounting and predatory pricing strategies adopted by big online e-commerce players such as Amazon and Flipkart.

❖ CHANGES INTRODUCED THROUGH THE PRESS NOTE

The Press Note has introduced some major changes which will have a huge impact on the e-commerce in India and the same have been discussed below, however this policy does not operate in other sectors such as entertainment, service sector, etc., which shall continue to be governed by their specific provisions.

Control of Inventory

Per the position under the Press Note 3² of 2016, an e-commerce entity providing a marketplace was barred from exercising ownership over the inventory as the same would render the business into an inventory based model.

The Press Note has widened the definition of inventory based model to include e-commerce marketplace entities exercising control over inventory and hence prohibiting Foreign Direct Investment (“FDI”) in the same.

An e-commerce marketplace entity was previously restricted from having more than 25% of the sales value generated through its marketplace platform from one vendor or a vendor's group companies by virtue of the Press Note 3 of 2016. This restriction has been removed by the Press Note. Also, as per the provisions of the Press Note, a marketplace entity will be deemed to control the inventory of a vendor if more than 25% of purchases of such a vendor are from the marketplace entity or its group companies.

Services by the Marketplace Entity

The position prior to the Press Note was that e-commerce marketplace entities shall not directly or indirectly influence the sale price of goods or services and shall maintain a level playing field.

The Press Note has stated and further clarified that services may be provided to vendors on an e-commerce marketplace, only at arm's length and in a fair and non-discriminatory manner by: (a) marketplace entities; or (b) other entities in which a marketplace entity has *direct or indirect equity participation* or *common control*. These services include, among other things, logistics, warehousing, advertising, marketing, payments and financing.

Interestingly, the Press Note also specifically sets out that *cashback* provided to buyers by group companies of a marketplace entity shall be fair and non-discriminatory. However, a marketplace entity providing services to a vendor on terms which are not made available to other vendors in *similar circumstances* will be deemed unfair and discriminatory. The Press Note is silent on what will be considered as *similar circumstances*.

Restriction on Sale

¹https://dipp.gov.in/sites/default/files/pn2_2018.pdf

²https://dipp.gov.in/sites/default/files/pn3_2016_0.pdf



The Press Note has introduced new restrictions which state that a vendor will not be allowed to sell on a marketplace entity's platform if (a) such marketplace entity or its group companies holds any stake or has equity participation in the vendor or (b) the control of the vendor's inventory is deemed to be with such marketplace entity or its group companies. However, marketplace e-commerce entities will be permitted to enter into transactions with sellers registered on its platform on B2B basis.

Exclusivity

The Press Note states that the e-commerce marketplace entity shall not *mandate* any vendor to sell any product *exclusively* on such marketplace entity's platform. This can be considered as a restriction only if the marketplace entity is exclusively imposing this restriction. However, this is a welcome move for the vendors/manufacturers as they are not prohibited from selling their product exclusively on their own platforms.

Annual Submission to the Reserve Bank of India

The Press Note has introduced a new requirement for marketplace entities to provide a certificate, along with a report of a statutory auditor, to the Reserve Bank of India, confirming compliance with the prescribed guidelines, by the 30th of September every year, for the preceding financial year. Therefore, the first set of documents, post the Press Note, will have to be submitted to the RBI by 30th September 2019, for the financial year 2018-2019.

❖ CHALLENGES FOR E-COMMERCE MARKETPLACE ENTITIES

The new policy's restriction on sales and discounts by vendors, joint ventures and group entities of marketplaces as well as the exclusivity restriction has forced not only the e-commerce platforms from revisiting their business models (except for their own private labels such as of Mynta, Flipkart, etc) in order

to accommodate smaller businesses (offline and online) but will also make the products expensive for customers.

Also, considering services are to be provided at an arm's length, small vendors shall now have the opportunity to sell on big platforms. DIPP officials have stated that the provisions are not against the interests of consumers, and that only fair, competitive and transparent business practices will better protect consumers in the short as well as long term³.

❖ CONCLUSION

The restrictions that have been brought out by the Press Note tackle few of the common practices followed by the major e-commerce market players.

Needless to mention this has come in as an unpleasant close to 2018 for most of the major e-commerce players in India, whilst the DIPP is expected to issue some interpretational clarifications on some of the issues. It has certainly forced e-commerce players to go back to the drawing board to (re)consider their business models in order to minimize the unavoidable loss brought about by these changes.

³ <https://economictimes.indiatimes.com/news/economy/policy/no-ban-on-private-labels-fdi-policy-not-against-consumer-government/articleshow/67374862.cms>



OVERVIEW OF NEW EXTERNAL COMMERCIAL BORROWING (ECB) FRAMEWORK BY RESERVE BANK OF INDIA

On 16th January 2019, the Reserve Bank of India (“RBI”) vide its Notification no. RBI/2018-19/109, A.P. (DIR Series) Circular No. 17 brought out a new External Commercial Borrowings Policy (“**ECB Policy**”) with the intention to liberalize and rationalize the extant framework for External Commercial Borrowings (“**ECB**”) and Rupee Denominated Bonds (also known as ‘*Masala Bonds*’)⁴. This circular is in continuation of RBI’s principle regulation on Foreign Exchange Management (Borrowing and Lending) Regulations, 2018.⁵

❖ SALIENT FEATURES OF THE REVISED FRAMEWORK

Merging & Reclassification of Tracks

The preceding framework for raising loans through ECB consisted of three tracks and a regime for Rupee Denominated Bonds listed on foreign debt exchanges. In particular, the said framework essentially provided for⁶:

Track I - Medium term foreign currency denominated ECB with minimum average maturity of 3 to 5 years, except in the case of manufacturing sector companies which could raise foreign currency denominated ECBs with a minimum average maturity period of only 1 year;

Track II - Long term foreign currency denominated ECB with minimum average maturity of 10 years;

Track III - Rupee denominated ECB with minimum average maturity of 3 to 5 years, except in the case of manufacturing sector companies which could raise INR

denominated ECBs with a minimum average maturity period of only 1 year in accordance with Track I; and

Rupee Denominated Bonds or Masala Bonds – Rupee Denominated Bonds / Masala Bonds are the bonds issued by an Indian entity in foreign markets of which the interest payments and principal reimbursements are denominated in Rupees (“**INR**”).

By virtue of new ECB Policy, the above classification has been merged and reclassified into the two following options for raising loans –

- (a) **Foreign Currency denominated ECB** which consists merging of Track I and II.
- (b) **Rupee denominated ECB** which consists merging of Track III and Rupee Denominated Bonds/Masala Bonds.

Expansion of Eligible Borrowers

Easing the classification to make it more compatible with the provisions made for new entries in borrowers and as a part of the rupee denominated ECB, the list of eligible borrowers is expanded to include all entities which are eligible to receive Foreign Direct Investment (“**FDI**”). In terms of Clause 2.1(iii) of the new ECB Policy, apart from all the entities being eligible to receive FDI, the ‘*Eligible Borrowers*’ now also include:

- (a) Port Trusts,
- (b) Units in SEZ,
- (c) SIDBI,
- (d) EXIM Bank,
- (e) Registered entities engaged in Micro- finance activities, viz., registered for not for profit companies, registered societies/trusts/cooperatives and non-government organizations;
- (f) Service and trading entities.

⁴ RBI circular dated January 16, 2019 on External Commercial Borrowings (ECB) Policy – New ECB Framework.

⁵ Notification No. FEMA.3R/2018-RB dated December 17, 2018, vide G.S.R. 1213(E) dated December 17, 2018.

⁶Master Direction No. 5 dated January 01, 2016.



Recognized Lenders

(a) Entity as Lender:

In terms of new ECB Policy, for being qualified as recognized lender, the lender should be resident of Financial Action Task Force (“FATF”) or International Organization of Securities Commission (“IOSCO”) Compliant Country, including transfer of ECB.

However, earlier framework limited the lenders to International Banks, Capital Markets, Multilateral Financial Institutions, Export Credit Agencies etc. but now any entity of a country, being a member of FATF or IOSCO is also a recognized lender.

(b) Individual as Lender:

Individuals can only be lender if they are foreign equity holders or have subscribed to bonds/debentures listed abroad.

(c) Foreign branches of Indian Banks as lender:

Foreign branches/subsidiaries of Indian Banks are permitted as recognized lenders only for Foreign Currency denominated ECB (except Foreign Currency Convertible Bonds and Foreign Currency Exchangeable Bonds)⁷.

Minimum Average Maturity Period (MAMP)

The previous framework provided for multiple Minimum Average Maturity Period (“MAMP”), depending upon the amount of borrowing as specified below:

- (i) **Track I** (Medium Term ECB) - MAMP of 1, 3 and 5 years.
- (ii) **Track II** (Long Term ECB) - MAMP of 10 years
- (iii) **Track III** (INR denominated ECB) - MAMP of 3-5 years in accordance with Track I

However, under the new ECB Policy, the RBI has kept MAMP at 3 years for all ECBs, irrespective of the amount borrowed.

Exception to the above, manufacturing sector companies may raise ECBs with MAMP of 1 year for ECB up to USD 50 million or its equivalent per financial year.

End- Uses (Negative List)

In view of the Clause 2.1(viii) of the earlier ECB framework, for the following activities, ECB proceeds were not allowed to be utilized:

- (a) Real estate activities
- (b) Investment in capital market
- (c) Equity investment
- (d) Working capital purposes except from foreign equity holder
- (e) General corporate purposes except from foreign equity holder
- (f) Repayment of Rupee loans except from foreign equity holder
- (g) On lending to entities mentioned in (a) to (f) above

In addition to the above, the FDI Policy of 2017 prohibits the utilization of ECB proceeds for the following activities:

- (i) A chit fund business or Nidhi company;
- (ii) Agricultural or plantation activities; and
- (iii) Trading in Transferable Development Rights.

Hedging Provisions

With the enforcement of new ECB framework, new hedging provision under Clause 2.1(x) has been introduced in terms of which the entities raising ECB are required to follow the guidelines for hedging issued (if any) by the concerned sectoral or prudential regulator in respect of foreign currency exposure.

Also, infrastructure space companies shall have a board approved risk management policy. Further, such companies are required to mandatorily hedge 70 per cent of their ECB exposure in case average maturity of ECB

⁷https://rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=11456



is less than 5 years. The designated AD Category-I bank shall verify that 70 per cent hedging requirement is complied with during the currency of ECB and report the position to RBI through Form ECB 2 returns.

The following operational aspects with respect to hedging should be ensured:

- a. Coverage
- b. Tenor and rollover
- c. Natural Hedge.

Special Dispensation

a. ECB facility for oil marketing companies

Under Clause 8.1 of new ECB Framework, ECB can be raised by public sector oil marketing companies with MAMP of three years from all recognized lenders without mandatory hedging and individual limit requirements. All other provisions will be applicable as such.

b. ECB facility for startups

As per Clause 8.2 of new ECB framework, AD Category-I Banks are permitted to allow startups, as recognized by the Central Government to raise ECB under automatic route upto USD 3 Million and MAMP will be of 3 years. Overseas lenders in case of INR denominated ECB will be eligible to hedge its INR exposure through permitted derivative products.

❖ CONCLUSION

This is the second time in two years that RBI has overhauled the ECB framework to quench the liquidity concerns of the borrowers. Considering the wider lenders and borrowers' definition pool, these changes are hoped to result in increase the inflow foreign currency and tackle diminishing value of rupee against the dollar and also improve the ease of doing business.

However, the ECB Policy is not without faults. Certain industries like renewable energy developers,

infrastructure companies and such allied and affiliated companies may face some serious problems as the End-Uses (Negative List) mentions that repayment of rupee denominated loans cannot be made from ECB proceeds. On a similar track, the National Solar Energy Federation of India (NSEFI) has also argued that infrastructure projects like wind and energy require long term financing of about 20-25 years and companies borrow from domestic lenders and at high cost and pay them back with lost cost ECBs. Such kind of financing helps companies assail through liquidity crunch.⁸

⁸ Ksenia Kondratieva, *Infrastructure companies concerned about refinancing rupee loans under new ECB framework*, THE HINDU BUSINESS LINE, January 22, 2019, <https://www.thehindubusinessline.com/money-and-banking/infrastructure-companies-worried-over-refinancing-rupee-loans-under-rbis-new-ecb-framework/article26058580.ece>



LEX REVISORS

1. The Companies (Amendment) Ordinance, 2019

The Companies (Amendment) Ordinance, 2019 was promulgated on January 12, 2019. It repeals and replaces the Companies (Amendment) Ordinance, 2018 promulgated on November 2, 2018. The 2019 Ordinance amends several provisions in the Companies Act, 2013 relating to penalties, re-categorization of certain offences, among others. The Companies (Amendment) Bill, 2019 (to replace the 2018 Ordinance) was passed by Lok Sabha on January 4, 2019 and is currently pending in Rajya Sabha.

Read More at: http://www.mca.gov.in/Ministry/pdf/NotificationCAO2019_15012019.pdf

2. Companies (Acceptance of Deposits) Amendment Rules, 2019

The Ministry of Corporate Affairs (“MCA”), vide its notification dated 22nd January 2019, has amended the Companies (Acceptance of Deposits) Rules, 2014, through the Companies (Acceptance of Deposits) Amendment Rules, 2019. One of the key changes brought in by this amendment was the substitution of the Form DPT – 3, amongst others.

Read more at: http://www.mca.gov.in/Ministry/pdf/AcceptanceDepositsAmendmentRule_22012019.pdf

3. Specified Companies (Furnishing of information about payment to micro and small enterprise suppliers) Order, 2019.

The Specified Companies (Furnishing of Information about Payment to Micro and Small Enterprise Suppliers) Order, 2019 vide Notification no. S.O. 368(E) dated 22nd January 2019 is passed to enforce the Government Order vide notification number S.O. 5622(E), dated 2nd November 2018 which mandates that the companies getting supplies of goods and services from micro and small enterprises and whose payment to suppliers exceed to 45 days from the date of acceptance or the date of deemed acceptance of the goods or services shall submit dues recording reasons for delay.

Further, the order mentions that a company shall file MSME Form I as annexed in the order mentioning details of dues and return.

Read more at: http://www.mca.gov.in/Ministry/pdf/MSMESpecifiedCompanies_22012019.pdf

4. Companies (Prospectus and Allotment of Securities) Amendment Rules, 2019.

The MCA vide its Notification no. G.S.R. 43(E) dated 22nd January 2019 introduced Companies (Prospectus and Allotment of Securities) Amendment Rules, 2019. By virtue of the aforesaid rules, sub-rule 11 is inserted to further amend Rule 9A of Companies (Prospectus and Allotment of Securities) Rules, 2014. Rule 9A mentions Issues of Securities in dematerialized form by unlisted public companies.

In terms of sub-rule 11 of Rule 9A, it is provided that Rule 9A shall not apply to an unlisted company which is:

- (a) A Nidhi Company
- (b) A Government Company



(c) A wholly owned subsidiary

Read more at: http://www.mca.gov.in/Ministry/pdf/CompaniesProspectusAllotmentRule_23012019.pdf

5. **Goods and Services Tax (GST): Composition scheme for small taxpayers extended to Rs. 1.5 crore**

Under Section 10 of the Central GST (Amendment) Act, 2018 which will come into effect from 1st February 2019, as according to the GST Council meeting, it has been decided to increase the threshold limit for the composition suppliers from INR 1 crore to INR 1.5 crores and further to enable registered manufacturers and traders to opt for composition scheme u/s 10(1) of the Central GST Act even if they supply services of value not exceeding 10% of the turnover in a State/Union territory in the preceding Financial year or INR 5 lakhs, whichever is higher. Presently, registered persons engaged in the supply of services (other than restaurant services) are not eligible for the composition scheme. The amendment also allows supply of services to the extent of above specified limits, apart from services referred in Para 6(b) of Schedule II i.e. restaurant services. This change seems to be inserted in view of clause (b) of Section 10.

Read more at: <http://www.egazette.nic.in/WriteReadData/2018/188986.pdf>

6. **Foreign Exchange Management (Establishment in India of a Branch Office or a Liaison Office or a Project Office or any other Place of Business) (Amendment) Regulations, 2019**

In order to improve the ease of doing business, the Reserve Bank of India (“RBI”) has introduced Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) (Amendment) Regulations, 2019 vide Notification no. FEMA 22 (R)/ (2)/2019-RB dated 21st January 2019. By virtue of the amendment regulations, RBI has relaxed the norms for opening of branch and liaison and project offices by foreign companies. With effect to this, if a foreign company is dealing in defence, telecom, information and broadcasting and private security sectors has obtained an approval of the regulator and ministry concerned then the approval of RBI is no longer required.

Read More at: <http://egazette.nic.in/WriteReadData/2019/195706.pdf>

7. **Securities and Exchange Board of India (Prohibition of Insider Trading) (Amendment) Regulations, 2019**

The Securities and Exchange Board of India through a gazette notification published the Securities and Exchange Board of India (Prohibition of Insider Trading) (Amendment) Regulations, 2018 (“Amendment Regulation”) to amend the existing Securities and Exchange Board of India (Prohibition of Insider Trading) Regulation, 2015 in effect from April 1, 2019. Key highlights include addition of new terms such as ‘Financial Literate’ to mean a person who has the ability to read and understand basic financial statements i.e. balance sheet, profit and loss account, and statement of cash flows. Further, the Amendment Regulation mandated the maintenance of a digital database of the names persons/entities along with their PAN details or other such identifiers as prescribed under law with him unpublished price sensitive information is shared. Such digital database needs to be audited from time to time to ensure that there is no instance tampering.

Read more at: <https://www.sebi.gov.in/legal/regulations/jan-2019/securities-and-exchange-board-of-india-prohibition-of-insider-trading-regulations-2015-last-amended-on-january-21-2019-41717.html>



8. **Mutation of land in the Revenue Records does not create or extinguish the title over land nor does it have any presumptive value on the title**

On 31st January 2019, a division bench comprising of Justice Abhay Manohar Sapre and Justice R Subhash Reddy, the Supreme Court in the judgement of 'Smt. Bhimbai Mahedeo Kambekar (D) through LR versus Arthur Import and Export Company & Ors.' has reiterated that mutation of land in the revenue records does not create or extinguish the title over such land nor it has any presumptive value on the title. It only enables the person in whose favour mutation is ordered to pay the land revenue in question.

Read more at: https://www.sci.gov.in/supremecourt/2012/7024/7024_2012_Judgement_31-Jan-2019.pdf

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