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FOREIGN DIRECT INVESTMENT (FDI) IN E-COMMERCE

The Department of Industrial Policy and Promotion, Government of India ("**DIPP**"), *vide* Press Note 3 (2016 Series) dated March 29, 2016 ("**PN 3/2016**") has issued guidelines for foreign direct investment ("**FDI**") in E-commerce.

As per the Consolidated FDI Policy Circular of 2015[1] ("**2015 FDI Policy**"), FDI up to 100% was permitted in Business to Business ("**B2B**") e-commerce, under the automatic route[2]. However, FDI in Business to Consumer ("**B2C**") e-commerce was permitted only under specific circumstances, being (i) a manufacturer of products in India could sell through e-commerce, and (ii) a single brand retail entity could sell products online as a means of supplementing its brick and mortar sales. However, pure-play B2C trading activities were not permitted in e-commerce.[3]

In order to overcome these restrictions, various e-commerce companies began carrying out retail trading through the marketplace model whereby the companies would only provide a technology platform to enable trades to take place between various sellers and purchasers of goods. However, the confusion persisted as to whether the market place model used by the e-commerce companies was recognised under the 2015 FDI Policy or not.

The issuance of PN 3/2016 clarifies the position on FDI in e-commerce, and legitimizes the marketplace model, but with some significant riders. PN 3/2016 provides that while 100% FDI shall be permitted under the automatic route in the marketplace model of e-commerce, no FDI shall be permitted in the inventory based model of e-commerce. The inventory based model has been defined as an e-commerce activity where inventory of goods and services is owned by the e-commerce entity and is sold to the consumers directly as opposed to the marketplace model where an e-commerce entity provides an information technology platform on a digital and electronic network where such entity acts as a facilitator between buyer and seller.

Other Sectoral Conditions laid down under PN 3/2016 for FDI in E-commerce:

FDI in marketplace model of e-commerce is permitted subject *inter alia* to the following conditions:

(i) A marketplace e-commerce entity shall be permitted to enter into transactions with sellers registered on its platform on a B2B basis;

(ii) A marketplace e-commerce entity shall be permitted to provide support services to its sellers such as warehousing, logistics, call centre, etc.;

(iii) A marketplace e-commerce entity shall not be permitted to exercise ownership over the inventory as the same will render it to be an inventory e-commerce entity, in which FDI is not permitted;

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[1] dated May 12, 2015

[2] Without prior governmental approval for FDI

[3] Refer Press Note 12 of 2015 dated November 24, 2015

(iv) An e-commerce entity will not permit more than 25% (twenty five per cent) of its sales to be effected through one vendor or its group companies[4];

(v) The goods and services made available for sale electronically through the website by a marketplace e-commerce entity shall clearly provide the details of the seller on its website. All post sales services such as delivery of goods, customer satisfaction, any guarantee or warranty, etc. shall be the responsibility of the seller;

(vi) Payments for sale in the marketplace based model may be facilitated by the e-commerce entity in conformity with the guidelines of the Reserve Bank of India;

(vii) Marketplace e-commerce entities shall not, directly or indirectly, influence the sale price of goods or services and maintain level playing field;

(viii) Guidelines on cash and carry wholesale trading shall apply to B2B e-commerce; and

(ix) Subject to the conditions under the 2015 FDI policy with respect to the services sector and other applicable laws/regulations security and other conditionalities, sale of services by e-commerce entities shall be under the automatic route.

Conclusion

On the whole, PN 3/2016 is a commendable step towards clarifying the position on FDI in e-commerce by clarifying that FDI in marketplace e-commerce entities is permitted up to 100%, which would help bolster more investments in the said sector. The significance of PN 3/2016 also lies in the impact of the restriction of not effecting more than 25% of the sales from any single vendor and its group companies and the obligation to maintain a level playing field with regard to pricing of goods/services, on the current business model adopted by the e-commerce.

Activities in the form of the marketplace model that were being carried out under the uncertain regime prior to issuance of PN 3/2016 have now been legitimized, subject to compliance with certain conditions specified thereunder.

In case of any clarifications, please feel free to contact:

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[4] "Group companies" under the FDI policy have been defined as follows: (a) Where one enterprise is in a position to exercise at least 26% voting rights in the other enterprise; and (b) Where one enterprise can appoint more than 50% of the Board of Directors in the other enterprise