FDI IN E-COMMERCE: PROS & CONS

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ABSTRACT

The department of industrial policy and promotion (DIPP) has recently invited comments on allowing foreign direct investment (FDI) in e-commerce, indicating the government intent to open up this segment.

The current policy in India does not allow foreign investment in the business of selling via online to consumers. There are no restrictions on FDI in the business-to-business (B2B) e-commerce transactions in goods. The DIPP is therefore considering going beyond B2C retails of goods to other transaction, such as consumer-to-government (C2B), business-to-government (B2G) and consumer-to-business (C2B) transaction.

The present paper would examine the pros & cons of FDI in e-commerce. The paper is woven as a conceptual paper and can be used to effectively resolve some of the major issue confronting FDI in e-commerce.

Key words: e-commerce, FDI.

1. INTRODUCTION

Electronic commerce may no longer be the explosive buzz word that it was in late 1990’s, but as it becomes more mature, many of the questions that we have been asking about increasing consumer response to electronic commerce or e-commerce.

The Indian e-commerce market grows at 88% and amounted to $16 billion in 2013 according to the recent ASSOCHAM (The Associated Chambers of Commerce and Industry of India) report. Increasing internet penetration and availability of more payment options boosted the e-commerce industry in 2013. The size India’s fast expanding e-commerce market is estimated to be Rs. 50,000 crore.

ASSOCHAM estimates that India’s e-commerce market will reach $56 billion by 2023, driven by rising online retail. It stood at $2.5 billion in 2009, amounted to $8.5 billion in 2012 and raise 88% to touch $16 billion in 2013.
Global retailer’s interest in expanding in India comes at a time when local start-ups such as Flipkart Internet Pvt. Ltd. and Snapdeal.com are taking off in the competition gaming online retail market, the broad range of products that these retailers offer with discounted prices and their easy payment options have made them huge hits in India, especially with young consumers.

US-based e-commerce companies Amazon and E-bay operate in India through the market place model, and these companies are pushing Indian government to open up the e-commerce sector further so that they can sell their products directly to consumers.

1.1 FDI in E-commerce Regulation in India:

The current policy in India does not allow foreign investment in the business of selling via online to consumers i.e. the existing policy does not allow FDI in business-to-consumer (B2C) e-commerce activities, but 100% FDI is allowed in business-to-business (B2B) e-commerce and in the market place model under which the e-retailer does not sell directly to consumers, but provides a platform to other sellers. US based e-commerce companies Amazon and e-bay operate in India through the market place model.

2. PROBLEMS WITH THE ISSUE OF FDI IN E-COMMERCE

A deep divide is emerging in the e-commerce industry over the issue of Foreign Direct Investment in online retail firms, on the one side are global multinationals, such as Amazon, which favours 100% FDI in this sector, and on the other are the large Indian players who are seeking only a partial opening-up of the sector.

The contentions issues are:

a) Whether 100% FDI should be allowed in e-commerce.

b) Whether it should be only for non-strategic investors.

c) Whether offline retailers should be allowed to bypass retail norms via e-commerce.

d) Whether there should be limit for local sourcing.

e) Should FDI be allowed in B2C e-commerce

f) Should it open for all products or only for non-foods products.

3. FDI Boiling Point

Along with the belief that FDI in e-commerce with lesser restrictions can do wonders for this sector, there are others who have expressed deep concerns for the same.

Let us have a look at some of those concerns:-

a) Extinction factor: One of the primary fears of allowing FDI in e-commerce would seriously impair small time trading of bricks and mortar stores. Small shopkeepers are not highly qualified and will not be able to compete with sound e-retail business. The massive reach of e-commerce companies which have the capacity to reach far-flung areas. Displacement of small stores is big challenge.
b) Geographic Restrictions: Another important concern is the geographic restriction for e-commerce, as applicable in the FDI policy for MBRT (Multi-Brand Retail Trading). According to the policy for MBRT, states have been empowered to take decision on notification of towns and cities with population of more than 10 lakhs as per 2011 census.

c) Local Sourcing: At present, e-retailers including Amazon works on inventory based model which can adversely impact the SMEs, and therefore the question of local sourcing arises as in the case of FDI in multi brand.

d) Unemployment: Another serious issue of small time businesses and kirana stores being the largest source of employment in the country and opening the business to consumer (B2C) e-commerce on inventory based model is likely to seriously impact these shopkeepers, leading to large scale unemployment.

Along with FDI, taxation is a key consideration impacting e-retailers’ business model, operational strategy and future growth. Lack of physical boundaries and the intangible nature of operations create several income-tax and indirect tax issues at each stage of the value chain.

e) Server management: In e-commerce, the company owning and operating the server is likely to be different from the e-commerce entity hosting the Web site. When the server is located outside India, and leased and operated by the e-commerce entity, there could be taxation issues.

f) Advertisement and promotion: E-commerce companies provide customers various incentives such as credit points, cash back, cash rollover, re-purchase discounts, buy one–get one free, combo-pack discounts and so on. The valuation of products and services for indirect taxes are, in general, based on the stream of considerations received, and an incorrect valuation could expose the e-commerce companies to higher taxes, interest and penalties.

g) Order processing: If e-commerce companies source products based on customer orders, it may result in a ‘predetermined’ sale, which, in turn, could be considered an inter-State/ CST transaction leading to loss of tax credits.

h) Stock procurement and management: E-commerce companies engage in activities such as branding, repacking, labeling, re-affixation of MRP, gift wrapping and so on for shipping products to customers. Based on the activity and the value addition to the final product, it may qualify as ‘deemed manufacture’, under the Central Excise Legislation, chargeable to excise duty.

i) Dispatch and delivery: The supply chain of e-commerce companies is usually thin and hence they use drop shipment, wherein the vendor of the e-commerce company directly delivers the product to customers. The vendor, the e-commerce company and the customer could be in different States and the place of taxation could vary based on the transaction. Further, registration and compliance management in the respective States would pose significant challenges to the e-commerce company.

j) Invoicing and collection: The USP of e-commerce companies is the timely delivery of products. The transactions could be so structured between the vendor, e-commerce companies and the customer that the issue of invoice, which is a document for transfer of ownership, happens at a later date. The time for issuance of invoice and the time and place of ownership transfer are usually regulated by the State VAT/CST legislation; deviation from compliance and ownership aspects could expose the company to the risk of taxes, interest and penalties.
4. ADVANTAGES OF FDI IN E-COMMERCE

Internet has made our lives easier in more than one ways and has touched our routine life as well. India has 137 million internet users with penetration of 11%. 71% of the transaction of consumer e-commerce industry relates to travel. Expected contribution of e-commerce to GDP by 2020 would be around 4%. If we analyse why people prefer buying product and services through online as compared to the shopping from traditional store, there are many advantages of permitting foreign direct investment (FDI) in business-to-consumer segment, the Department of Industrial Policy and Promotion’s (DIPP) paper said that it would also improve customer service.

a) **Boost to the infrastructural development:** Increased capital will help to establish supply chain, distribution system and warehousing.

b) **Impetus to manufacturing sector:** Growth in retail sector will have cascading effect in the manufacturing sector which will positively contribute to overall growth of economy and job creation.

c) **More efficient supply chain management:** Will reduce the need for middlemen leading to lower transaction costs, reduced overhead and reduced inventory and labour costs.

d) **Adopting best global business practices:** Will lead to better work culture and customer service.

e) **Increased outreach:** Will provide increased access to buyers/sellers; allow MSMEs and artisans to reach out to customers far beyond their immediate location, both locally within India and abroad.

f) **Traceability and transparency:** Will not only empower consumers with information and data but also help in better compliance of regulatory framework.

g) **Reduced costs:** On marketing and distribution, travel, materials and supplies will benefit businesses

h) **Improved customer service:** providing more responsive order taking and after-sales service to customers and competitive pricing

i) **Positive spillover effect:** It also said the growing e-commerce industry can have a positive spillover effect on associated industries such as logistics, online advertising, media and IT/ITES. Currently e-commerce accounts for 15-20 percent of the total revenues for some of the big logistics companies.

j) Other than foreign players like Amazon and eBay, opening up of FDI in this sector is likely to benefit existing local companies who need more capital to expand their business in a rapidly growing market. It could also lead to a better work culture, information data and improved customer service by providing more responsive order-taking and after-sales service to customers, along with competitive pricing.

5. CONCLUSION

Overall, ecommerce including online retail in India constitutes a small fraction of total sales, but is set to grow to a substantial amount owing to a lot of factors such as rising disposable incomes, rapid urbanization, increasing adoption and penetration of technology such as the internet and
mobiles, rising youth population as well as increasing cost of running offline stores across the country.

US-based e-commerce companies Amazon and E-bay have been pushing the Indian government to open up the e-commerce sector further so that it can sell its products directly to consumers.

Traders have dismissed the proposed policy to allow Foreign Direct Investment in e-commerce, but the views expressed by the global and domestic e-commerce companies are mixed. India’s retailer association is also divided on the issue of FDI in e-commerce.

FDI in e-commerce will boost infrastructure development and spur manufacturing, but it could also lead to large scale job losses. Finally the government is still waiting for views of all stakeholders before allowing FDI in e-commerce and further all depends upon which Political party is going to form the government at the centre.

REFERENCES

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