Ch1
Prologue--An Overview

In his very first year as Prime Minister of India in 2004, Dr Manmohan Singh wrote a signed frontpage editorial in *The Economic Times*. In it he said: "*I do hope that in the New Year we can all work together to build a more equitable, competitive and humane India"*. This report by CUTS *inter alia* takes stock of how we have moved forward since in promoting growth and equity through regulatory reforms and better management, and what still needs to be done.

Dr Singh's exhortation has its roots in the first days of the new government, which announced its intention of making competition policy a serious issue, drawing from the National Common Minimum Programme of May, 2004, which says the government "will not support the emergence of any monopoly that only restricts competition. All regulatory institutions will be strengthened to ensure that competition is free and fair. These institutions will be run professionally". This was reinforced in the President's address to the parliament on June 7, 2005:

> "Revival of industrial growth is of paramount importance. Incentives for boosting private investment will be introduced. Foreign Direct Investment will continue to be encouraged. Indian industry will be given every support to become productive and competitive. *Competition, both domestic and external, will be deepened across industry with professionally run regulatory institutions in place to ensure that competition is free and fair.*
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> "The Government will establish a National Manufacturing Competitiveness Council to provide a continuing forum for policy interactions to energise and sustain the growth of the manufacturing industry.
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> "The Government is committed to a strong and effective public sector, whose social objectives are met by its commercial functioning. But for this, there is need for selectivity and a strategic focus. My government will devolve full managerial and commercial autonomy to successful, profit-making companies operating in a competitive environment.
>
> "My government believes that privatisation should increase competition, not decrease it".

These statements provide the *raison d'etre* for this report, which examines what has happened – and what has not – on these commitments. In other words, it seeks to provide a status report on the state of competition and regulation in India. The appropriate definition of competition is a situation which ensures that markets always remain open to potential new entrants and that enterprises operate fairly under the pressure of competition. Regulation, in this context, is defined as an instrument to tackle market failures in regulated sectors, particularly infrastructural areas like electric power, which due to their natural monopolies are not amenable to competition.

How will competition help us?

Broadly speaking competition can help us, first, by ensuring that there are a large number of suppliers, so that there is healthy rivalry. Second, where there are natural monopolies,

we require better regulation and price capping, so that consumers are not exploited. For example, there is huge competition in the telecoms sector, which is improving with new technologies available every day. Yet, the sector needs regulation. Rivals can collude, and thus negate the benefits of competition. Or, tariff plans can be devised and presented in such a way that consumers cannot decipher them. Thus, there is the Telecom Regulatory Authority of India (TRAI) at New Delhi, which governs the performance standards and commercial behaviour of the telecom sector.

TRAI is engaged in another area of regulation, which is also quite close to consumers, namely cable TV. In this sector, there are a large number of suppliers – the last mile operators – who are serving a large population of consumers. Yet there is no perfect competition. Here we are stuck with natural monopolies, because they divide the territories among themselves. They too charge exploitative prices. Consumers cannot even change their cable TV operator for fear of being left with no service at all. In 2003**,** CUTS carried out a nationwide survey on consumer satisfaction, the results of which show a high level of dissatisfaction. The study highlighted that despite the existence of relatively strong consumer awareness in the country, the cable TV sector remains a seller's market. The consumer is no more than a puppet in the hands of the operators, without any say in the types of channels they want to watch or in choosing their cable operator. Consumers pay for channels they do not watch, and many may not receive channels they would like to watch and pay for. There are many other sectors, such as electricity to name only one, where too natural monopolies reign.

In most cases, the capacity of regulators is either limited or non-existent. This is made worse by the fact that most regulatory agencies are run by retired bureaucrats or judges, whose working lives have been spent under a command and control regime. Not surprisingly, their understanding of law and economics in the area of independent regulation is minimal. Some do learn on the job and perform well, but by the time they have learnt the ropes, it is usually time for them to go. In addition, the salary levels of staff are quite low, so the regulators don't attract good professionals. As a result the quality of regulation suffers. Clearly, we have miles to go.

What is fortunate is that the new government at the centre is very serious about improving competition in the market place, and to reform the regulatory structure. Currently, the Planning Commission is engaged in looking at the regulatory framework in infrastructure and considering how we can bring in international best practices to improve it. Thus, there is intent – the challenge is to turn it into reality.

How to promote competitiveness through competition

Competition policy has a significant role to play in promoting competitiveness and growth. The term 'competitiveness' appears to have aroused considerable controversy in recent years. On the one hand, the word has become a kind of catch-all term for a wide-ranging set of policies. On the other hand, it evokes an analogy suggesting nations compete in the same way as firms. While nations may not always compete, they can – and should – help firms compete more effectively by following a set of macro policies

that can create an enabling environment for competition. A simple example is length of time it takes to issue clearances to set up a business.

A study conducted by the World Bank[1] reveals that in India, it takes 35 days to set up a business. In 2006, however, it took 71 days to start a business in India. In a sample of 175 countries, India was placed 134th.

What is perhaps worse is the difficulties faced by businesses *after* they have started – an unhelpful and obdurate bureaucracy, brought up with an attitude problem, is just one of many hurdles darkening our business landscape.

There are lessons for India in how other countries deal with similar problems. Faced with declining competitiveness, the European Union published a white paper in 1993[2], which highlighted four areas for priority action:

- The promotion of investment in intangible assets;
- The development of co-operation between firms;
- Ensuring fair competition; and
- The modernisation of public authorities

Thus we see that the EU white paper on competitiveness emphasises the need for ensuring fair competition in the market as an essential ingredient for enhancement and maintenance of competitiveness in the economy. These prescriptions apply to India as well. The government has thus created the National Manufacturing Competitiveness Council, but its work has been uninspiring, marked by an inability to think out of the box, which is so essential to change things.

Empirical evidence, though focusing mainly on the experience of developed countries, has confirmed that barriers to competition within an economy, whether due to governmental or private restraints, leads to losses in income and welfare. On the other hand, a well-designed and implemented competition policy promotes economic growth by ensuring a better allocation of resources, as highlighted by the following examples:

> *A study carried out for the Australian economy estimates the expected benefits from a package of competition promoting and deregulatory reforms (including improvements in the competition rules) to lead to an annual gain in real GDP of about 5.5 percent, or A$23 billion, where consumers would gain by almost A$9 billion besides seeing increases in real wages, employment and government revenue.*[3]
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> *A report released by the McKinsey Global Institute (MGI)*4*, based on research on the economies of 13 nations, argues that the key to reducing economic inequalities between rich and poor countries is productivity and its links to competition and consumption. MGI studied national economies from the ground up, and points out that global economic agencies underestimate the significance of a level playing field. Competition is more important than education or greater access to capital markets in*

[1] Doing Business in 2007: How to Reform, The World Bank

[2] Growth Competitiveness, employment: The Challenges and Way Forward into the 21st Century (1993) http://aei.pitt.edu/1139/01/growth_wp_COM_93_700_Parts_A_B.pdf

[3] http://www.unctad.org/en/docs//c2em_d10.en.pdf

[4] William W. Lewis, 'The Power of Productivity', McKinsey Global Institute, The University of Chicago Press, 2004

lifting a country's gross domestic product. To reduce barriers to competition, policy makers must stand up to business special interests and focus more on the welfare of consumers.

In the context of developing countries, including India, there is a shortage of systematic analyses of the benefits of adopting a competition law regime. In India, there was never an effective law. However, a relevant study of the Peruvian competition agency, Indecopi, found that in the first seven years of its operation, the economic benefits due to the competition authority's operations amounted to $120m against operating costs of $20m, or a six-fold 'profit'.[5] Similarly, a study by the Korean Fair Trade Commission in 2003 found that benefits (consumer welfare increase and income transfer effect) outweighed costs (the KFTC's budget) of competition law enforcement in 2000 and 2001 by 34 times[6].

Under the 7Up (the first in a series of similar projects which have carried out comparative studies of competition regimes in several developing countries) project[7], we found that the Indian government in the 1980s and 1990s did not appear to be serious about the competition law regime, as the budgetary allocation to the MRTP Commission was just about 0.0009% of the total government budget in 2000, when the ideal allocation in other developing and developed countries was in the range of 0.0013%. Even a small poor country like Zambia had provided 0.005% of its total budget to its Competition Commission.

How does competition policy ensure pro-poor development?

An issue that is often raised in discussions about competition policy in the context of a developing country is the role of such a policy in the country's economic development. Arguably, the biggest challenge before the developing world today is to rid itself of the abject poverty that deprives a large section of its population of the opportunity to lead a dignified life. An important approach to poverty reduction is to empower the poor, provide them with productive employment and increase their access to land, capital and other productive resources. But this approach may not be successful unless the poor are linked to the markets and markets are made to work for the benefit of the poor.

The World Development Report 2000-01 says:

"Markets work for the poor because poor people rely on formal and informal markets to sell their labour and products, to finance investment, and to insure against risks. Well-functioning markets are important in generating growth and expanding opportunities for poor people."

"Well-functioning" implies markets that work efficiently and without distortions. However, competition is often distorted by players, and it is essential that governments

[5] See Caceres, A (2000), 'Indecopi's first seven years' in Beatriz Boza, ed., *The Role of the State in Competition and IP Policy in Latin America: towards an academic audit of Indecopi*, Lima.
[6] CUTS (2005), 'Citizens' Report on the State of Competition Laws in the World', CUTS/INCSOC, Jaipur
[7] CUTS (2003), 'Pulling Up Our Socks – A Study of Competition Regimes of Seven Developing Countries of Africa and Asia: The 7-Up Project', CUTS, Jaipur.

enact competition laws to regulate distortions. What is often ignored is the fact that the prevalence of anti-competitive practices in markets hurt the poor more than the rich. A rich person would not mind paying a rupee more for a product or service, but for people living with less than Rs 20 a day getting value for money – for every *paisa* they spend – is vital to survival. This is the 'consumption' side.

If we look at the 'ability to pay' angle or the 'income' side, a sector that immediately comes to mind is agriculture. Of the 1.2bn people of the globe who live in extreme poverty, approximately 75 percent live and work in rural areas and about two-thirds of them draw their livelihood directly from agriculture[8].

The market in agricultural products is very often considered to be an example of a perfectly competitive market. However, there is a huge gap between the prices consumers pay and the prices farmers actually receive. This is because of the chain of intermediaries between consumers and farmers that do not always work in a competitive manner. These intermediaries abuse their monopolistic dominance in the market for final products, while in the markets for primary products, they abuse their monopsonistic dominance. In a country like India, where two-thirds of the population draw their livelihood directly from agriculture, the linkage between market imperfections in agricultural goods and poverty is manifest.

Competition law is not a luxury of the developed world, but an indispensable tool for developing countries in their fight against poverty. Developing countries should not be dogmatic about withdrawing from the markets, as distortions and failures in markets are ubiquitous, necessitating state intervention to promote a fair and orderly market.

Competition policy maximises consumer welfare by ensuring that goods and services of the best possible quality are offered at the lowest prices and available in adequate quantities. Furthermore, competition policy also leads to business welfare, by ensuring, for instance, that intermediate goods and services consumed by businesses are available through a competitive process.

Promoting effective markets through competition

Competition, though seen as a means of attaining efficiency and fairness, may not necessarily promote these objectives. A perfectly competitive market with many small firms may achieve equality of opportunity (fairness) but may not achieve efficiency, as the existence of too many firms means that they may not be able to achieve economies of scale.

Obviously, competition policy must deal with trade-offs in its objectives and instruments. This concern has led to a shift from a structural to a behavioural approach in enforcing competition. After all, in a fiercely competitive market, even a duopoly can produce an outcome that a perfectly competitive market generates. Thus, it may not be necessary to

[8] International Fund for Agricultural Development (IFAD), 'Rural Poverty Report 2001: The Challenge of Ending Rural Poverty', New York, OUP, 2001.

have a highly-competitive market structure provided appropriate rules of the game can be designed and enforced so that the behaviour of the market players remains competitive.

This approach may, however, become ineffective when there are natural monopolies and competition cannot be ensured as such. Situations could also arise where there may be a number of players in the market but the market itself is so segmented that the individual players become monopolists. The only way to get 'competitive outcomes' in such markets is to put in place effective regulation. Thus, regulation in different sectors becomes an integral component of competition policy.

As is evident, competition policy is a complex issue. Unfortunately, there has not been much research on competition issues in India. Currently, Department for International Development, UK, supports the Competition Commission of India (CCI) through the World Bank's Foreign Investment Advisory Service to undertake studies in various sectors, which can be accessed at www.competitioncommission.gov.in. The CCI project resulted mainly from a landmark study by CUTS, *Towards A Functional Competition Policy for India*, conducted in 2005 and supported by DfID. The study was a comprehensive one, which looked at both systemic issues and some sectoral issues.

As the country is poised to implement a new competition law, a lack of understanding of the nature and extent of prevalence of different types of anti-competitive practices in India will pose a major challenge. This Status Report is aimed at giving stakeholders a better understanding of the competition scenario in India. It will help:

- the government to integrate a national competition policy;
- the competition and regulatory authorities to set priorities; and
- other stakeholders to understand the complexities and make appropriate interventions.

The Report

This chapter gives an overview of competition and its relationship with various dimensions of economic governance. It also recalls our previous work in the area of competition and regulation in India since the year 2000. This report is the fourth major research project undertaken by CUTS in India in this exciting and challenging field.

Perhaps for the first time in India, an effort has been made here to gauge the popular perception to competition and regulation by developing an index. A carefully selected sample of about 660 respondents was achieved. Chapter 2, *How do people perceive the situation?*, carries the results of this exercise. The purpose was to assess the perceptions of stakeholders on the competition and regulation scenario along the following lines:

- Competition law or competition issues in competitive industries;
- Sector regulation or competition/regulation issues in regulated industries; and
- Government policy/measures/other legislation

What comes out clearly in this exercise, is that although the need for a competition policy, competition law, and rules that encourage competition is clearly recognised, progress has been slow and haphazard. Evidence of anti-competitive behaviour is found in virtually every sector of the Indian economy.

The reforms of 1991 gave a fresh impetus to markets, which had been in a near-dormant state since the late 1960s. These reforms were undertaken to instil dynamism in the industrial economy through competition. Competitive forces were expected to pull the Indian industry out of its state of inertia and place it on a dynamic growth path. In this context, it is generally believed that economic liberalisation and globalisation have succeeded in changing the market structure so as to allow more competitive free play. Market competition is in turn expected to have a positive influence on the performance of industry.

Industrial growth has improved the supply of various goods and services in the market. The availability of better and cheaper goods and services to consumers has certainly enlarged and is set to increase further with the rise in competition in the market. The availability of a larger basket of goods and services certainly enhances consumer welfare but it is limited only to those who have the necessary purchasing power.. One of the basic objectives of competition in any economy is that the gains of competition be distributed equally among different segments of society. But the trickle-down effect of economic growth is not visible in the Indian market and the poor among the consumers do not have the opportunity to reap the benefits of competition. Obviously, to access the benefits of competition, firstly s/he has to become a part of the market, which means they must be given the opportunities to generate purchasing power.

Do all the consumers have the ability to pay, even if competition has increased the availability of goods and services in the market, and thus access? There are cases where, in spite of the availability of goods and services paying capacity the market is characterised by a lack of access due to skewed and uneven distribution of goods and services in the market. These problems are often compounded by mal-governance. Growth has to be accompanied by reduced disparity, good governance and, even more importantly, dispersed benefits.

There has been substantial growth and expansion in various goods and services with relaxation in control and new technologies. The telecoms sector, for instance, is a success story in terms of its widening access. With the rise in access to various goods and services and competition in the market, various anticompetitive practices are also expected to arise. As a result, while competition has increased, the task of regulating their conduct has not diminished – hence the need to develop a stated competition policy to promote efficiency and consumer welfare. Further, competition policy is needed to create a healthy business environment, which leads to efficient resource allocation, and to curb the abuse of market power.

In India, although the need for a competition policy and competition rules that encourage competition has been recognised, progress has been slow and haphazard. There has been

a tendency, in spite of the commitment to reforms, to frame policies, laws and rules without acknowledging the market process. Often, the approach has not been consistent.

Many of the government policies and practices have not been in line with market principles, mainly because of a lack of awareness, but also due to other reasons. These have been analysed in Chapter 3, *Policy Induced Anticompetitive Outcomes*. Even when the government is committed to introducing competition based on market principles, the outcome is often the very opposite. Mostly, this happens because of futile and ignorant efforts to reconcile too many conflicting objectives. Too many good intentions often result in bad outcomes. But, increasingly, cronyism has also been responsible for such policies. For furthering competition as a fair process and as an impulse to shape equitable outcomes, it is important to ensure that the design and operation of policy instruments do not frustrate the market process.

However, a large overhang and backlog from the past persist in attitudes and laws, preventing the government from both construing and constructing policies that are structured to work in sympathy with the market processes. The design and operation of several policies and practices of the government are such that they distort the market process and competition – most often in the name of public interest, which invariably means some entrenched/vested interests. Market distortions also exist at the state/local level. In a word, several policies and rules adopted by governments are obsolete in the present economic environment and are adversely affecting the competitive forces and competition culture in the country.

There is mounting concern that this state of affairs is affecting the welfare of both consumers and businesses. For example, the manner in which privatisation and deregulation policies have been introduced in some cases has simply transferred monopoly power from the public to the private sector.

Indian law provides for regulatory mechanisms under several Acts. These have been discussed in some detail in this report. Regulation in the manufacture and trading of goods is governed by several laws, such as standards and food safety laws. To promote fair play alone, there is the MRTPA, the Consumer Protection Act, 1986 and several IPR laws. Then there are the traditional laws such as the Contracts Act and the Sale of Goods Act – and an effective, though inefficient, judicial system to resolve disputes.

As far as specific infrastructural industries are concerned, there is, for example, the Electricity Act of 2003, which aims to create a liberal policy environment to facilitate the entry of new players into the business of electricity generation. The Act vests the power of determining tariffs to the appropriate regulator (State and Central Electricity Regulatory Commissions) and not the generating company. The State Electricity Regulatory Commissions are expected to regulate prices that final consumers pay and to foster competition. However, political interference overshadows good regulation in the states. Telecom is a central subject, hence state-level interference is ruled out. The Telecom Regulatory Authority of India (TRAI) Act, amended in 2000, empowers the

regulator of this sector but stops short of giving it teeth. It does have a lashing tongue though.

In order to enable healthy competition in the market place, there are set principles which the government has to imbibe and incorporate in the policy rubric. The report has listed such principles in Chapter 4, *The Nine Principles of Competition Policy*. An important finding on a broad basis is that competitive neutrality is at a premium. This requires the separation of policymaking, ownership and regulation. For example, in the telecoms sector, the ministry of communication sets the policy; it owns and operates two large public sector companies – BSNL and MTNL – and also oversees the regulator, Telecom Regulatory Authority of India. In such a scenario, can telecom regulation be really neutral? These and several other dimensions have been dealt with in the chapter.

Chapter 5, *Need for Competition Policy & Law* and distinguishes between the terms competition policy; competition law and competitiveness, as many often confuse one with the other. It goes on to address some popular misconceptions through a Myth vs. Reality matrix. It examines and queries certain fundamental aspects of the issues at stake: for example, have we adopted a competition law under external pressure to enable market access for foreign multinationals? And do we need a competition law at all?

India does not have a comprehensive national competition policy. Interestingly, two arms of the government have initiated the process after successful advocacy by CUTS[9] through a research report. The Department of Corporate Affairs (formerly Company Affairs) directed the Competition Commission of India (CCI) to form an advisory committee, headed by eminent economist, Dr. Vijay Kelkar on 17th January, 2006, for developing a consultation paper on a national competition policy. The committee has met on several occasions, but is yet to complete its assignment.

Overtaking the above process, the Planning Commission established a working group to develop a national competition policy on 5th June, 2006, with V. K. Dhall, Member, Competition Commission of India, as its chair. The working group delivered its report in February, 2007. The report is to be integrated into the 11th five-year Plan Document, which is expected to be ready by the end of 2007. The same has to be adopted by the National Development Council and then put into action. Our work will continue.

The main features of its recommendations include the establishment of a Competition Policy Oversight Council which will oversee the implementation of the policy, to broadly cover the following principles:

1) Effective control of anticompetitive practices;
2) Competitive neutrality, i.e. a level playing field;
3) Rule-bound procedures with transparency and non-discrimination;
4) Institutional separation between policy making, operations and regulation;
5) Third party access to essential facilities on fair terms; and

[9] Kirit Parikh, Member, Planning Commission's pronouncements at CUTS event on release of report: 'Towards a Functional Competition Policy for India,' February 1, 2005

6) Deviations from policy on social or other grounds should be clearly defined, transparent, non-discriminatory and having the least anticompetitive effect.

Emanating from the first of the nine principles mentioned above, Chapter 6, *India's competition law regime: past and the present*, takes the reader through the history of competition law in India – from the Monopolies and Restrictive Trade Practices Act of 1969 to the Competition Act of 2002 and an amended one in 2007. Work on the new law began in 1999, when the then Finance Minister, Yashwant Sinha, announced the government's resolve to bring in a modern law. This came about for two cognate reasons: a) lobbying by the consumer movement led by CUTS[10] from the mid-1990s and b) the government's realisation that the archaic MRTPA, having worked more as a licensing law rather than a competition law, had outlived its utility. The whole approach was to turn the law on its head – while the MRTPA was a structural law, the Competition Act, 2002 would be a behavioural law. Big was no longer to be considered bad, but if 'big' misbehaved it would invite punishment. The new law is yet to be notified fully because of several problems with its structure, but hopefully it will be operational soon.

The delay of nearly eight years was due to several reasons. First, there was opposition from business, which is often the case in many developing countries. Businesses believe that such a law will suffocate their growth due to its very nature or prevent them from making profits, and that overzealous regulators will use a heavy hand. Another reason for the delay centred around the quality of regulators. Regulatory authorities are mostly headed by retired civil servants, who have been weaned in a command-and-control economy, and have

Box: 1 - Finding the going tough

Between July 2003 and September 2005, the upstream polyester producers, including Reliance and Indo Rama Synthetics, had increased the price of Polyester Staple Fibre (PSF) by approximately 26 per cent. According to reports, PSF was available at Rs. 71.5/kg in the domestic market. As against this, through imports, PSF was available at around US$1.2 (CIF) or Rs 56/kg. However, with 20% import duty on import price and 16% countervailing duty, the effective import duty on PSF came to around 39.2%. Thus, the cost of imported PSF for the domestic users worked out to Rs 77.8/kg. The domestic PSF producers have been pegging their prices to landed cost of imports, and taking advantage of the tariff protection.

With Reliance producing about 85% of the Polyester Staple Fibre (PSF), and Indo Rama producing the rest, this man-made fibre segment, like others, is known to be a highly concentrated sector. Over the years, the duo have conspired to ensure very limited competition by manipulating trade policy to maintain a high tariff barrier, and grown rather fat on profits from their exploitative pricing policy.

Consequently, the Indian Cotton Mills Federation (ICMF), now the Confederation of Indian Textile Industry (CITI) called for a lowering of customs duty on synthetic yarn to check exploitative pricing by domestic suppliers as it would check arbitrary pricing by the manufacturers. It demanded that import duties on all man-made fibres be reduced from 20% to 10%, while excise duty on domestic manufacture be cut down from 16% to 8%, if the textile sector was to become competitive.

The apex body of the textile industry had reportedly also threatened to call its textile affiliates to boycott polyester fabric and switch to cotton fabric if its concerns remained unresolved. CITI held that the country's synthetic yarn production had stagnated at 600,000 tonnes per annum since 1997 due to the PSF duopoly of Reliance and Indo Rama. Various industry associations of the domestic mills sector had repeatedly pointed out that rather than squeezing more profits from the stagnating market, the polyester producers should look at their prices and try to expand the market. (Source: ET, 20.09.04 & BL, 22.12.04)

[10] Acknowledged by Yashwant Sinha, MP in a personal communication to CUTS on 29th June, 2007

little understanding of law and economics. The same happened in this case too, and it was challenged in the Supreme Court. The court took umbrage on some other grounds, mainly that such quasi-judicial authorities with the power to impose fines can only be dealt with by judges, and not by civil servants under the doctrine of separation of powers between the executive and judiciary. There is more about this in the report.

Predictable and effective regulatory regimes create confidence among businesses, and thus help to promote investment. If telecom and electricity rates come down it is not only consumers who benefit but also business as customers of the input. Similarly in the area of intermediates, it is business which gains from low cost inputs to become competitive. For example, in two synthetic chemical inputs the consumers – textile and garment manufacturers – suffer because of duopolies (see box above). Again, where there are cartels, the immediate sufferer is businesses, as most cartels operate in the area of intermediates such as chemicals, cement and equipment, which are purchased by other businesses to produce goods and services. One of the most important benefits for business in a competition law is its ability to take action against entry barriers to setting up a business or supplying goods or service.

Both consumers and businesses urgently need a competition law, because of the existence of unchecked anticompetitive practices, such as cartels, across the country. Chapter 7, *Cartels, the major challenge,* traces the history of the pathology of cartels in India.

Cartels plague every sector in India. In one case to do with the contraceptive device, Copper-T, even a public sector undertaking, Hindustan Latex Ltd., has been named as a colluder[11]. The cartel was never investigated in spite of a complaint by us to the MRTP Commission. In another case involving a well-known and widely-prosecuted international cartel in vitamins, the MRTPC dismissed our complaint summarily, without even a speaking order.

Cartels can operate without fear of prosecution because there is no competition law worth its name. The MRTP Act, which can crack down on cartels, is toothless, as can be seen from a reading of cases handled by it since its inception. Further, the commission has little resources. An additional problem centres around the lack of a definition for cartels. But this problem will hopefully be resolved under the new law – it not only lays down clear definitions, but also offers amnesty to whistleblowers, a tool that has been used successfully by competition authorities in advanced countries. As this report is being written, a cement cartel is in the news, often occupying the front and editorial pages of business newspapers.

Cement cartels highlight another type of anticompetitive practice – abuse of dominance. Cement companies are breathing down the necks of dealers to operate as exclusive distributors of their brands, and they risk losing supplies if they sell another company's brand. In the parlance of competition law such type of behaviour is termed as 'exclusionary' abuse of dominance. This will be another crucial area of enforcement for the new competition authority. As already noted, the thrust of the new law is to regulate

[11] Indian Express, 'Copper-T Cartel? Govt Wants PSU to Explain', August 6, 2004

bad behaviour by big firms, rather than be inhibited by considerations of size. Besides that, the political economy of the country will enable big to become bigger over time, and thus regulating combinations (mergers, etc.) will involve striking a balance. Analyses of combination cases will also need a high level of skills and understanding, and will therefore take time to build up. Pay-scales offered by the authority are too low to attract skilled professionals, so there will be some limitations in capacity. This is not to suggest that regulation of combinations should be ignored but only to point out some practical difficulties.

Chapter 8, *Abuse of dominance, another serious issue,* takes the reader through the various definitions of the term. There are two types of abuses of dominance. One is exclusionary, which has been discussed above. The other is exploitative and its menu of abuses is longer than that of exclusionary. Mainly the conduct leads to a form of price gouging or rent extracting by a dominant business because either the customer has no choice or cannot access substitutes easily. One important contemporary case in India relates to an abuse of an intellectual property right. The ongoing case of price gouging by Monsanto Mahyco in its marketing strategy on Bt cotton seeds, over which the company has a global patent, is described in the chapter.

The MRTPA did not specifically cover IPRs, but it did test some cases under the provision of monopolistic and restrictive practices. Under various court judgments, European courts have held that IPRs by themselves are not bad – it is their abuse which is bad. The Competition Act is rather weak in this respect, and hence any action against IPR-related abuse will have to be dealt with under this provision. This would also require strong capacity in the authority.

One problem that we have seen in the past with the MRTPA was that it could not really oversee the whole country because of constraints on resources, low capacity and the sheer size of the country. On the other hand, there are increasing numbers of anti-competitive and unfair competition practices which happen at the grassroots level without any recourse to justice. To give just one example from the CUTS dossier, a hosiery sale organiser, Bal Krishna Khurana[12], used the media to advertise the sale of cheap hosiery goods (claiming, for instance that a saree worth Rs.1,000 is available for Rs.150) necessitated by the factory closing down and/or ships sinking. In fact, the goods were of a poor quality, many customers could not find the particular good advertised, and there was no opportunity to complain against bad goods, as these sales organisers had no regular office.

The sales were always held for 3-5 days in hired exhibition halls or hotels. This was and is a standard practice in all our cities. Khurana was thus carrying on business at Jaipur through both unfair trade practices and switch-and-bait. A complaint was filed against him at the MRTP Commission, which issued cease and desist orders. Copies of the orders were sent to the newspapers which were carrying these misleading ads. The practice stopped for many years and newspapers desisted from carrying these types of ads. Alas,

[12] CUTS and Competition Issues: Dossier, May 2005, http://www.cuts-international.org/documents/C-CIER-Dossier.doc

the same practice has begun again and there is no action. Consumer courts are there to provide relief to unsatisfied consumers, but they hardly take any preventive action.

This is why we need competition and regulatory agencies at the local level. In a comparable large federal country like the US, there are state competition laws and agencies to deal with local problems. Chapter 9, *Local problems need local solutions,* argues the case for local-level authorities which can work in conjunction with central authorities. The telecoms regulator, which also oversees cable TV, is on record saying that sitting in Delhi it is unable to police the actions of a large number of cable operators, and that these should be handled at the local level.

In the area of telecoms, India has witnessed a stunning success in terms of creating huge competitive networks and offering the lowest tariffs in the world. However, this doesn't mean that one can be complacent about it. Chapter 10, *Telecom and electricity* takes us through the situation of competition and regulation in both these crucial infrastructure sectors through case studies. While telecom has been a success, electricity has been a failure in terms of promoting competition. Common factors to both sectors include the establishment of universal supply obligations and a fund to assist companies to serve the poor and disadvantaged people/areas. It is operating in the telecom sector but not in the electricity sector as yet., On the same lines, private sector airline and petroleum retail companies are required to mandatorily service less profitable and remote areas. The telecom USO Fund is currently being used to create a rural infrastructure.

In the electricity sector there is very little private enterprise as the old electricity boards continue to function in their new avatars as generation, transmission and distribution companies. They continue to operate under a lethargic system and even the state electricity regulators have little control over them. Politicians often compete to deliver free power to rural consumers, rather than offer subsidy to the distribution company to do so. The central government has tried to stop these unhealthy practices and to offer incentives to states to improve their power situations, but the matter drags along. The electricity sector can be competitive by allowing private producers to sell power directly to consumers using the existing grid and distribution network, but apathy only prevents anything from happening in concrete terms. In the mobile telephony sector, one thing which is happening is separating infra from the ownership of operations. A similar approach will be required in the electricity sector to promote competition.

Finally, in terms of promoting growth, it is equally important to see how we deliver education and health care to our people. Both these areas are crucial for steady economic development too. Chapter 11, *Social sector regulation,* examines these two areas as case studies. Too much attention is being given to pharma prices in the country through the Drug Price Control Orders and the National Pharmaceutical Pricing Authority, while the issue of competition lies elsewhere. Consumers do not decide which brand of drug to buy or which laboratory to go to for a diagnostic test – rather, it is their doctor or the hospital who decides. Many of the doctors prescribe under the influence of pharmaceutical companies and seek extra income from pharma retailers and diagnostic labs. In the area of education, the quality of regulation is equally poor. Little attention is paid to the course

curriculum or the pedagogy or even standards. On the other hand, the education regulators – the University Grants Commission and the All India Council for Technical Education – set standards on the basis of the number of faculties or size of facility. These benchmarks cannot promote quality, and the National Knowledge Commission has argued for an education regulator in the area of higher education[13].

Postscript

The record on infrastructural regulatory institutions is also poor, affecting both businesses and consumers. For business it affects investment decisions, while for consumers it means that things will be business as usual. We need about $450bn during the 11th Plan period to create a strong infrastructure, so that we can maintain our growth rate at 9 percent or even go higher, and to create more jobs and raise the living standards of the poor.

The Prime Minister announced in mid-2004 that the Planning Commission would prepare a policy paper on a sound regulatory architecture for India, taking into account best practices from around the world. He announced a deadline of six months. This was also an item in the agenda for the newly-established Committee on Infrastructure, which was headed by him. The paper is yet to be completed.

The first draft, on 'Approach to Infrastructure Regulation: Issues and Options', was prepared and placed on the Planning Commission's website on August 18, 2006, two years after the announcement. A round table was organised on September 25, 2006 to discuss the draft paper, and participants were drawn from the government, regulatory agencies and consumer groups among others.

Box 2: Regulatory malfunction

The regulatory system for the efficient functioning of sector markets was meant to supplant a political system that is usually unable to take the required pricing decisions in various infrastructure sectors like electricity, or weighs in favour of special interest groups. However, as is common knowledge, the regulatory system has not worked perfectly, and some might argue in favour of rule-based contracts that do away with the need for periodic decisions by fallible regulators. But it should not be too much to ask that, so long as a regulatory system is in place, it works smoothly. That, unfortunately, is not the case.

The selection of the chairman of the Central Electricity Regulatory Commission (CERC), due since late last year, has once again been held up. The situation becomes worse with the Telecom Dispute Settlement and Appellate Tribunal (TDSAT) set to stop functioning for all practical purposes in three weeks' time because the posts of a second member (out of three) will have fallen vacant. The government has to make the appointments, and it is clear that people in the government are playing games. If the selection process is so politicized, it raises the question as to how independent the regulatory system is in practice.

In the case of the CERC, a selection panel short-listed two candidates, but one of them dropped out. Another name that was not in the original list was inserted and, even more extraordinarily, this Maharashtra-cadre IAS official was placed at the top of the list of two. In the case of the TDSAT, it gets worse. A candidate for one of the two posts was chosen by a panel, and the name approved by the Chief Justice of India. Then an unexplained problem was discovered, as a result of which the post was not filled. Later, the communications ministry decided to recommend the name of the outgoing chairman of the government-owned telecom firm, Bharat Sanchar Nigam Ltd. (BSNL), which the Chief Justice rightly rejected on the grounds that 90 per cent of the cases before the TDSAT are against BSNL. Undeterred, the ministry has sent the same name once again. The selection process for the second member has just begun.

Matters do not improve after appointments are made. In the case of the Telecom Regulatory Authority of India (TRAI), it is well known that there was a difference of opinion between the TRAI Chairman and the telecom minister. So, for months the ministry refused to act on TRAI's recommendations – it did not help that the recommendations themselves were not well thought-out, and were changed in one critical case once TRAI had a new chief. None of this points to the regulatory system in the country functioning satisfactorily. A systemic review is in order. (*Business Standard, 27th August, 2007)*

[13] 'New Regulator for Higher Education Says Pitroda', *The Hindustan Times*, December 18, 2006

Expectedly, the discussions were contentious, because the paper had floated new ideas such as a framework law on regulatory regimes in order to promote cohesion among ministries in how each of them drafts laws for regulators in the sectors that they control. Another idea was to create truly independent regulators by making them directly accountable to the parliament rather than line ministries. The draft paper suggested that regulators be pulled out of the control of ministries so that they could perform better and in an independent manner. An idea to create a department of regulation was also floated. But these suggestions met with severe resistance, as the line ministries would lose control.

At a second consultation on June 4, 2007, exclusively with consumer groups, the Deputy Chairman, Montek Singh Ahluwalia, observed that the final paper would be part of the 11th Plan Document to be debated at the National Development Council, before adoption. This may take another 3-4 months. However, for the recommendations to be accepted in full, it might take 4-5 years.

It is however also true that in some areas like telecom, civil aviation, insurance, railway container traffic and gas distribution, government monopolies have been curbed by allowing the private sector to enter. However, if one examines each sector in detail we find that principles of competitive neutrality (providing a level playing field) have been given short shrift. In the airline sector or oil exploration sector, the reverse has also been observed, where private players were given undue advantage over the public sector.

On goal setting, the government's record is mixed. Reforms have lead to growth, but competition in its true sense and equity are still missing. Critics within the ruling establishment allege that reforms are propelling growth that benefits big industry, leaving the vast majority of Indians and the small scale industry in a state of neglect and deprivation[14].

At this point, it is not clear when the implementation of the Competition Act of 2002 will begin in earnest. The amended law has been adopted by the parliament in this year. The Parliamentary Standing Committee had gone through the amendment bill. Among its recommendations is one which has agitated the business community – that of making it mandatory for all combinations (mergers etc) to be notified. This has been accepted by the government.

This is a classic case of the never-ending debate on industrial policy vs. competition policy. Many in India feel that we need large enterprises to be able to compete with big enterprises from abroad in both the domestic and overseas markets. Korea and Japan, through a protectionist regime, prospered in the 1960s/1970s because they did not have a bias against bigness. But thanks to many factors, all of which have driven countries to adopt highly-advanced competition laws, the situation today is very different from what it used to be even a decade ago. Today both the Korean and Japanese competition laws have been strengthened to deal with abusive behaviour of big firms, who find their *laissez faire* freedoms curbed.

[14] *Economic Times*, 2nd May, 2007

One way to promote competition against entrenched/dominant domestic businesses is to allow imports at tariffs which would create a level playing field for imports. Thus, trade policy instruments are used to ease tariffs and generally lead to increased choice for the consumer both in terms of price and quality. But import competition can be thwarted (see Chapter 7 *Cartels, a serious challenge*) by the affected parties manipulating tariffs in such a way that the landed cost of a cheaper product is ultimately higher than the rent-seeking prices at which they are selling their own goods in India.

Similarly, for industry, policy measures such as delicensing, and removal of capacity expansion restrictions and protection (reservation of products) to small-scale industries would allow firms to expand strategically. This will facilitate economies of scale and scope, which can result in better prices and quality for consumers. Of course one will need to take care that products being manufactured by many small units does not result in the creation of a few large units in the sector, but many medium-size units which can be competitive.

Privatisation and disinvestment should seek to replace public sector monopolies with a thriving, competitive environment, while at the same time providing for efficient, well-structured regulatory bodies to govern them. The creation of effective regulation is surely beneficial to the market and the consumer.

As discussed in the report, while a more appropriate umbrella competition legislation has been designed, its implementation will take some time, as the amended law is operationalised over time. The amendments have done away with regional benches which would mean fewer checks on anti-competitive practices at regional or local levels. Two better ways are for the CCI to meet regularly in regional centres and to establish regional offices to act as windows. Nor is there a formal mechanism for an interface between the competition authority and the consumer courts mechanism born out of the Consumer Protection Act, 1986 (COPRA which often deal with grassroots competition abuses). This is essential if the two systems are to work in tandem for the protection of the consumer.

Also, as mentioned before, there is a need for wider civil society involvement in the issue of competition and consumer protection – something that the new economic governance framework will hopefully foster. The civil society movement needs to be resourced institutionally and their capacity built up to maintain a healthy demand side dimension to a healthy economy.

This chapter began with what the Prime Minister had to say and concludes by quoting him once again, on the crucial issue of economic democracy. Speaking at a function in New Delhi on 1st May, 2007, he observed:

"I was struck by a comment in the media that most of the billionaires among India's top business leaders operate in oligopolistic markets, and in sectors where the government has conferred special privileges on a few. This sounds like crony capitalism.

Are we encouraging crony capitalism? Is this a necessary but transient phase in the development of modern capitalism in our country? Are we doing enough to protect consumers and small businesses from the consequences of crony capitalism? [Have] we, in the name of protecting them [big industry] encouraged crony capitalism?

Do we have a genuine level playing field for all businesses? What should be done to inject a greater degree of competitiveness in the industrial sector?"