



# **Grim Fate of Third-Party Vendors Who Sell on Online Platforms**

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## **A. INTRODUCTION**

The digital age has seen the rise of many online platforms that provide opportunities for third-party vendors to offer products to customers. One persistent narrative that has been made about these platforms in recent years is that they help vendors in developing countries to export their products to consumers in distant parts of the world. This narrative is evident not only in academic research and research emanating from some inter-governmental organisations, but also in statements of world leaders. For instance, the 2020 G20 Leaders' Declaration (at Riyadh) endorsed high level policy guidelines<sup>1</sup> which claim that "SMEs are globally benefiting from the collaborative economy in several ways, especially thanks to their collaboration with digital platforms."<sup>2</sup> Similarly, the 2016 G20 Leaders' Summit (at Hangzhou) resulted in the creation of a Digital Economy Development and Cooperation Initiative, which encouraged MSMEs to participate in global value chains<sup>3</sup>. Since MSMEs lack the resources to do so on their own, the natural assumption would be that they would seek help of digital platforms to access these global value chains. The UNCTAD Digital Economy Report of 2019<sup>4</sup>, while noting the asymmetric rise of these platforms (which have mostly emerged, with a few exceptions, in developed countries) nevertheless claims that "e-commerce platforms may provide export opportunities for MSMEs, enabling them to reach beyond small domestic markets."<sup>5</sup> It further goes on to say that "in the

right circumstances, digital platforms can expand the opportunities for small enterprises in developing countries to reach new customers.”<sup>6</sup> Beyond the claims of access to the larger world market, the UNCTAD report also mentions that the platforms can reduce transaction costs that exist in the analog world, and create new opportunities for MSMEs in both domestic and foreign markets.<sup>7</sup>

What is missing in these claims and assertions is the voice of the third-party vendors who are actually conducting business on these platforms. Thus, the supposed benefits of e-commerce on digital platforms need to be examined in light of the real-world experiences of vendors who sell on online platforms. In gathering these experiences, and the behaviour of major online platforms, this policy brief relies extensively on two notable reports – ‘Amazon’s Stranglehold: How the Company’s Tightening Grip Is Stifling Competition, Eroding Jobs, and Threatening Communities’ by Stacy Mitchell and Olivia LaVecchia, and ‘Investigation of Competition in Digital Markets’, the Majority Staff Report by the Subcommittee on Antitrust, Commercial and Administrative Law of the Committee on the Judiciary of the United States (hereinafter referred to as “the Sub-Committee report”). The problems highlighted in these reports relate to third-party vendors of all sizes, whether they be MSMEs or big brands and manufacturers. The compelling evidence provided by these reports challenges the narrative that third-party vendors, especially MSMEs, can benefit their business by gainfully linking to online platforms. The next section provides illustrations of how, through the different practices adopted by online platforms, their commercial interests get significantly enhanced at the expense of the third-party vendors.

## **B. THE PROBLEMS OF THIRD-PARTY VENDORS ON ONLINE PLATFORMS**

Two important reasons explain the contrasting fortunes of the platform owners and the third-party vendors: first, the platform owner has asymmetric access to the data of vendors and consumers, which it is able to leverage to its advantage; and second, the platform owner also becomes a vendor on its

platform. This section identifies specific practices of online platform owners, which hurt the commercial interests of third-party vendors.

**Platform owners appear to appropriate for themselves a large share of the sales made by the vendors on their platform:** Many platforms take 30% or more of the sale value made by third-party vendors on their platforms. To illustrate, Apple<sup>8</sup> and Google<sup>9</sup> both charge a 30% commission on downloads of paid apps, as well as a 30% fee for in-app purchases (IAPs) made on their app stores. Amazon<sup>10</sup> charges a varying rate that ranges between 15% to 50% of the product value, depending on the item. The actual costs of running these platforms, however, do not appear to justify this practice. In this regard, the following observation in the Sub-committee report is extremely relevant: “Apple’s former Senior Director of App Store Review, estimated that Apple’s costs for running the App Store are less than \$100 million. Other analysts estimate that the App Store has significantly higher profits. A gaming developer explained that the fees it pays Apple’s add up to millions of dollars—or even tens or hundreds of millions of dollars for some developers—far in excess of the developer’s estimate of Apple’s costs of reviewing and hosting those apps.”<sup>11</sup>

The high rents which these platforms extract from third-party vendors is likely to compel these vendors to reduce their investments into innovative new products and services, and hampers their ability to compete on the platform.

While both Google and Apple have recently reduced their app store commissions to 15% for certain classes of developers (for example, developers who make less than \$1 million in an year from the app store)<sup>12</sup> after close scrutiny from government regulators<sup>13</sup>, a 15% cut still represents an outsized profit untethered to the cost of running these platforms.

Some of these platforms also frequently make aggressive demands for discounts, surprise fees and payments from the vendors and publishers on their platforms, and force them to agree to these demands by threatening to

either remove the buy-button from their product pages, or remove their products from their recommendation algorithms<sup>14</sup>.

**Third-party vendors may get induced into buying additional services from the platform owner:** A number of e-commerce companies offer packaging, warehousing and shipping services in addition to their core business as a platform for vendors. These companies “encourage” vendors to use the platform’s fulfilment services over their own by giving vendors who use the company’s services a much better chance at winning the “buy box”- which means being selected by the platform’s opaque algorithms as the default seller on a product page<sup>15</sup>. According to the Subcommittee report “Industry experts estimate that about 80% of Amazon sales go through the Buy Box, and the percentage is even higher for mobile purchases.”<sup>16</sup> Thus, losing the buy box can be catastrophic for a vendor. Further, the dominant e-commerce platforms are in the habit of raising the fees for their fulfilment services without warning, thereby destabilizing the carefully balanced business models of third-party vendors<sup>17</sup>.

The online platforms also offer advertising services to allow vendors to claim a prominent spot in search results on the marketplace. But these services often end up being more of a requirement than an option if a vendor wishes to compete on the storefront<sup>18</sup>. Through these practices, online platform owners exercise absolute control over what the customers discover on their platforms, and losing the advertisement war can condemn a vendor’s products to obscurity.

**Platform owners seem to undermine third-party vendors by copying their products and competing with them:** The long-term business model for certain online platforms is far more insidious than simply squeezing third-party vendors for high fees. By virtue of being owners of the online platforms, they have access to the data of consumers and vendors. The owners use this data to identify the popular products on their platforms. Thereafter, the

platforms create competing private-label products that copy the features of these third-party products, and finally cut out the original third-party vendors<sup>19</sup>. Dominant platforms with near-monopoly status in their respective markets are particularly notorious when it comes to this practice. As per the authors of ‘Amazon’s Stranglehold’, “Once Amazon brings a seller’s most popular products into its own inventory, it can lower its price so that it becomes the default seller, or simply award itself the buy-box anyway.”<sup>20</sup> In fact, the Subcommittee report remarks that “underlying Amazon’s public-facing rhetoric is the reality that it views many of the sellers on its platform as competitors. In its internal documents, Amazon refers to third-party sellers as “internal competitors.” ”<sup>21</sup>

Similarly, companies that run popular app store platforms collect and analyse information about popular apps on their app store, and then build competing apps with similar functionality, and offer them to customers as the default apps on that platform<sup>22</sup>. For example, the Subcommittee report notes that “The Apple Developer Agreement, which Apple requires every app developer to agree to, appears to warn developers that in exchange for access to the App Store, Apple is free to build apps that “perform the same or similar functions as, or otherwise compete with” apps in the App Store.”<sup>23</sup>

Once these platforms have developed competing products and appropriated the product knowledge and seller expertise from third-party vendors, they either eject the original vendors from their platforms or push their products away from the eyes of customers, essentially killing their business<sup>24</sup>.

**Platforms may place their products higher in searches than the products of third-party vendors:** The fact that the online platforms also operate as vendors on their online marketplaces presents an obvious conflict of interest. They can and do give preferential treatment to their own products over competing products of third-party vendors. The Subcommittee report cites the investigations by a couple of popular American newspapers in this regard: “In 2019, the Wall Street Journal and The New York Times both conducted extensive investigations and reported that Apple appeared to be favoring its

apps in the App Store search results. The Wall Street Journal explained that “Apple’s mobile apps routinely appear first in search results ahead of competitors in its App Store, a powerful advantage that skirts some of the company’s rules on search rankings.” The New York Times reported that six years of analysis of App Store search rankings found Apple-owned apps ranked first for at least 700 common search terms. Searches for the app titles of competing apps even resulted in Apple’s apps ranked first.”<sup>25</sup>

**The rules and guidelines on these platforms appear to be arbitrary and opaque, and often may not apply to their own products:** The policies of online marketplaces run by e-commerce giants create an atmosphere of uncertainty for third-party vendors, where their accounts can be suspended or shut down for unclear reasons, and the process to get these decisions reverted is prolonged and arduous. The following extract from the Subcommittee report describes the experiences of a number of developers with these rules: “One developer that spoke with the Subcommittee described Google’s Play Store policies as an “opaque system [that] threatens the ability of app developers to develop and compete in the market for consumers, who should ultimately determine which apps they use.” Another developer explained, “When apps allegedly violate Google Play Store standards, Google does not ever explain how, other than to quote the policy above and attach pictures of the allegedly violating image. When the imagery does not fit the above definitions, app publishers such as [third party] are put in a position of having to guess how to apply these standards.”<sup>26</sup> Further, the problems are not limited to one platform, as the following observation of the Subcommittee report reveals: “Among the most egregious examples of Amazon’s arbitrary treatment of sellers are its abrupt suspensions of their accounts, frequently made without explanation.”<sup>27</sup>

Some of the online platforms have also been known to use violations of their rules as a pretext for retaliatory behaviour against third-party vendors<sup>28</sup>, or use the threat of suspensions to force the vendors to agree to ever higher discounts and concessions<sup>29</sup>. It is also relevant that certain dominant app

store platforms have been accused by developers of changing their app store guidelines over time so as to benefit their own apps<sup>30</sup>. The Subcommittee report provides the following pertinent example: “While the Apple Developer Agreement provides Apple the right to replicate third-party apps, Apple’s Guidelines direct developers not to “copy another developer’s work” and threaten removal of apps and expulsion from the Developer Program for those that do.”<sup>31</sup>

**MFN clauses are likely to prevent third-party vendors from selling their products cheaper outside the platform:** Some platforms enforce Most-Favoured-Nation (MFN) or price parity clauses on third-party vendors, which prevents them from offering lower prices on competing online marketplaces. It appears that platforms haven’t shied away from misusing these clauses. As the Subcommittee report points out - “Amazon has a history of using MFN clauses to ensure that none of its suppliers or third-party sellers can collaborate with an existing or potential competitor to make lower-priced or innovative product offerings available to consumers.”<sup>32</sup> As a specific example, the report mentions the following: “a former third-party seller explained that Amazon uses “Buy Box Suppression,” where Amazon will remove a seller’s ability to win the Buy Box, as a way to penalize sellers that offer products at a lower price on competing sites.”<sup>33</sup>

**Platform owners seem to create information asymmetry by limiting the access of third-party vendors to their customers:** Many online platforms only allow vendors to communicate with customers through their own, heavily-monitored system, and prohibit them from including links to their websites, among other things, on the platform<sup>34</sup>. On this practice, the Subcommittee report notes the following: “Amazon generally forbids sellers from contacting their customers. The packaging and even the order confirmation email for third-party sales feature the Amazon brand prominently and do not reference the seller. A typical Amazon customer is unaware of the source of the sale.”<sup>35</sup> As a result vendors cannot build loyalty

with customers who don't know them. Instead, this customer loyalty is built towards the e-commerce platforms. App platforms are no strangers to this behaviour either, as evident from the following observation in the Subcommittee report: "Developers have also detailed that Apple attempts to lock in its fees by preventing apps from communicating with customers about alternatives. Under the App Store Guidelines, apps may not provide any information "that direct[s] customers to purchasing mechanisms other than in-app purchase." They also cannot communicate with iOS app customers about purchasing methods other than IAP."<sup>36</sup>

**The need to win the Buy Box appears to reduce pricing to a race to the bottom:** On most online e-commerce platforms, the combination of all the above factors results in a situation where, for the customer, the only meaningful differentiation between competing products offered by vendors is the price. The algorithm that selects the winner of the Buy Box on certain dominant e-commerce sites partly depends on price<sup>37</sup>, and as such, the need to win the Buy Box often compels vendors to engage in a race to the bottom, with ever-diminishing margins<sup>38</sup>. Some vendors have even started using paid software that adjusts the prices of their products every few minutes to undercut competitors in the Buy Box race<sup>39</sup>.

**The platforms seem to weaponize counterfeiters to force third-party vendors to comply with the terms and conditions mandated by the platform:** Unauthorized resellers and counterfeiters have sprung up on numerous ecommerce platforms, and the policing of these sellers, who eat into the profits of the legitimate vendors and harm the customers, has unfortunately been inconsistent on these platforms.<sup>40</sup> Some of these platforms, in fact, have often used their ability to selectively police these counterfeit sellers as a negotiating tactic in their dealings with third-party vendors. If a vendor chooses to leave the platform, the platform will allow these counterfeiters and unauthorized resellers of the vendor's goods to run rampant in the marketplace without any policing. The damage caused to the

original third-party vendor in terms of both the profits and reputation might convince them to either rejoin the platform or not leave in the first place.<sup>41</sup> Beyond that, the platform will often use the same threat to force third-party vendors to agree to onerous terms, or to pressurize them to give discounts on the platform.

**Certain brand manufacturers may be forced to be wholesalers by platforms and might not be allowed to sell directly to customers:** The largest e-commerce giants leverage their dominance and near-monopoly status in the market by forcing certain brand manufacturers who would prefer to be third-party vendors into being wholesalers instead<sup>42</sup>. This allows the company to act as a middleman between the brand and the customer, further enriching itself.

**Certain platforms appear to have degraded their seller services and instead make third-party vendors pay for better service:** Vendors rely on effective communication with the platform holder to resolve their issues with the platform, whether it be removal of counterfeit products or appealing against account suspensions. But as the Subcommittee report shows, certain dominant platforms have completely dropped any pretence of being responsive to the issues raised by the vendors: “Sellers shared with Subcommittee staff that communications to Amazon’s Seller Support Central generally prompt automated, unhelpful responses, which may be entirely unrelated to the specific case, question, or concern raised by the seller.”<sup>43</sup> But the problem in this particular example goes far beyond merely degraded service. The Subcommittee report observes that “Amazon has recently monetized the degradation of its seller services, rolling out a program where sellers can pay an extra fee for a dedicated account representative. Sellers are supposed to pay for representatives to help them solve the very problems that Amazon created in the first place.”<sup>44</sup>

**Some platforms appear to require third-party vendors to sign a forced arbitration clause to give up their rights to go to court:** To point to a specific example, the Subcommittee report notes that “all of Amazon’s third-party sellers and most of its vendors are subject to a pre-dispute, binding (“forced”) arbitration clause, requiring them to sign away the right to their day in court if a dispute with Amazon arises. Subcommittee staff heard from sellers who said that if it were not for Amazon’s market power over them, they would not agree to this term.”<sup>45</sup> Such clauses force the vendors into an arbitration where the wildly unfair status and bargaining power of the two parties essentially allows the platform to control the outcome.

**Dominant app-store companies may be forcing apps to add In-App Purchases(IAPs) to stay on the platform:** In-app purchases, which involve any transactions performed inside the app (except purchase of physical goods), allow app-store platforms to extract tremendous profits from their app stores, and dominant companies have been known to force developers to implement IAP in their apps or risk being removed from their stores. Again, the Subcommittee report is rich with specific examples, for instance – “As Apple has emphasized growing its Services business, app developers and technology writers have observed Apple is increasingly insistent that apps implement IAP—cutting Apple in on revenue from more developers—and threatening apps that do not comply with expulsion from the App Store.”<sup>46</sup>, and “several market participants have informed the Subcommittee that Google has begun insisting that a broader category of apps will be required to use Google IAP exclusively, no longer allowing the option of a third-party payment processor.”<sup>47</sup>

**Platforms appear to be exploiting the COVID-19 crisis to disadvantage third-party vendors further:** The COVID-19 crisis has seen certain platforms squeeze and discriminate against third-party vendors in an even more blatant manner. To quote an example from the Subcommittee report, “In response to the COVID-19 pandemic, some businesses moved physical

events online, often booking through an app and holding the event through a video chat application. Educators have also shifted resources online, including through apps. The New York Times reported that Apple demanded a 30% commission from these virtual class offerings. As a result, one company stopped offering virtual classes to users of its iOS app.”<sup>48</sup> E-commerce giants aren’t shy to take advantage of the pandemic either. As the Subcommittee report states: “Amazon initially responded to the sudden surge in sales by refusing to accept or deliver non-essential supplies from its third-party sellers—a stance that would seem reasonable except that Amazon continued to ship its own non-essential products while restricting third-party sellers’ ability to use alternative distribution channels to continue selling through Prime.”<sup>49</sup>

## **C. CONCLUSIONS AND POLICY RECOMMENDATIONS**

It’s evident from the above compilation and analysis that if digital platforms are to be truly beneficial to third-party vendors, they must be regulated and monitored to prevent exploitation of vendors at the hands of the major companies that run these platforms. The fact that the issues highlighted above aren’t limited to a certain subset of vendors, but affect big brands and manufacturers as well, paints a dismal picture of the impact of these problems on MSMEs and small vendors. This brief makes the following suggestions to address the practices surrounding the treatment of third-party vendors on these platforms:

- a) Comprehensive regulations that prohibit online platforms from acting as vendors themselves, whether directly or indirectly, must be implemented. Further, the monitoring of the proper implementation of these regulations should be as important as their creation. In this context, the experience of India, which permits marketplace model of online retail, is extremely relevant. While the Government of India introduced new e-commerce rules in 2018 that prohibit e-commerce platforms from selling products from companies they have an equity interest in, platforms have proven adept at circumventing these regulations. Subsequent to the new e-commerce

rules, Amazon divested its stake in Cloudbtail and Appario, the two major merchants on its platforms that it created as Joint Ventures.<sup>50</sup> However, Amazon Asia-Pacific Resources, a non-Indian unit of Amazon, still owns a 24% stake in Cloudbtail.<sup>51</sup>

The Competition Commission of India(CCI) has ordered a probe against Amazon and Flipkart, and in the case filed by the two companies in the Karnataka High Court for the quashing of this probe, the CCI claimed that Cloudbtail and Appario continue to be related to Amazon, and are given preferential treatment by the company compared to third-party vendors.<sup>52</sup> A Reuters report in February 2021 found internal Amazon documents revealing that in 2019, just 35 vendors accounted for two-thirds of all sales on Amazon's India e-commerce platform, and Cloudbtail and Appario, vendors in which Amazon continues to hold indirect equity, made up about 35% of the platform's revenue.<sup>53</sup>

- b) There should be regulatory restrictions on the type of vendor and consumer data that could be accessible to the platforms. Further, to enforce these restrictions, there should be a requirement for strong IT systems audit, so as to ensure that measures are actually in place in these companies to prevent sensitive consumer and vendor data from being accessed by the platform.
- c) It is desirable for governments to promote online platforms owned by MSME associations, as a counterpoint to giant e-commerce platforms, whose interests do not align with those of MSMEs, and who exercise considerable asymmetric bargaining power in dealings with MSMEs on their platform.
- d) Regulations to hold the platform responsible for removal of counterfeit products in a timely manner at the instance of the original vendor are required to prevent certain platforms from profiting from the theft of the intellectual property of original manufacturers, who may or may not have their products on that platform.

e) Lastly, it must be examined whether government monitoring bodies that watch out for anti-competitive conduct have enough teeth to be able to successfully bring e-commerce giants flouting national laws and regulations to heel. In absence of close, continued scrutiny and decisive action, there's an imminent danger of some of the online platforms swallowing third-party vendors, especially MSMEs, and irretrievably wrecking local business and entrepreneurship, particularly in developing countries.

**(Disclaimer: The assertions and conclusions expressed in this brief rely exclusively on the facts, investigations, and reports cited in the brief).**

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