India Competition & Regulation Report (ICRR)
Report of 3rd National Reference Group Meeting
Saturday, 17 March 2007, New Delhi

Background and Introduction

CUTS International has undertaken a research project to prepare the first of its kind 'India Competition and Regulation Report (ICRR)'. The project, supported by the British High Commission, New Delhi, has been undertaken against the background that while India has embraced market-oriented economic reforms for the past 15 years, there is, as yet, no periodic review to assess competition and regulation scenario in the country. ICRR is an attempt to fill this vacuum. The report would be prepared on a biennial basis and provide inputs to policy community and other stakeholders to take necessary actions to promote well-functioning markets. For more on the project, please visit www.cuts-international.org/icrr.htm

This third meeting of the National Reference Group was organised to review drafts of various sections of the report. Nitin Desai (ND), Chairman ICRR NRG, welcomed all participants. Following sections of the report were discussed in the meeting:

- Competition Issues in Pharmaceuticals
- Competition Regime and Business Welfare
- Theme Section: Competition Regime and Enhancing Access

Follows a brief report of the proceedings with key outcomes.

1. Competition Issues in Pharmaceuticals

Draft of chapter is available at
http://www.cuts-international.org/pdf/ICRR07_%20Pharma.pdf

1.1 The chapter has been written against the background `that the competition aspects of the pharmaceutical industry are very distinct from those in most markets. The very essentiality of the product being sold, namely medicines, is facilitative to distortion in competition in the pharmaceutical market. Consumption patterns in this industry are not affected by prices and therefore, firms do not have any incentive to keep prices low. Another issue is that the consumers are very often not the decision-makers. They are for the most part guided by instructions from their doctors and pharmacists. The significant role assumed by the doctors and pharmacists in influencing drug sales, leads to manipulation of the system. This vitiated guidance on the part of the doctor deprives patients from availing the best possible products at the lowest possible prices, which is a basic competition principle.

1.2 Following issues from the chapter were highlighted in the presentation:

1.2.1 Notwithstanding all the encouraging indicators and the substantial promise of the pharmaceutical industry in India, the sector is today in a state of flux. Many domestic companies are being confronted by the very issue of survival in face of the sweeping changes introduced in the patent regime and the increasingly de-regulated environment. Especially threatened is the issue of access to medicines by the poor.

1.2.2 In the western world, Government is the major buyer of medicines and Government being monopolist can regulate the price by bargaining with the manufacturers. Even if not so consumer does not bear the burden of medicines as the Government provides these. In India, situation is reverse as consumer pays for the medicine and bears the burden of price rise.

1.2.3 The competition concern is that patents confer monopoly status to pharmaceutical companies and often monopoly rights are misused to the detriment of consumers, with companies abusing their dominant position by pricing their patented products at monopolistic profit-maximising levels, thereby severely circumscribing access to affordable medicine. India Competition Act 2002 does not provide any power to regulate these monopolies.

1.2.4 The most common medicines, which can be produced easily, are selling at very low prices but in decontrolled regime the prices of these medicines have gone up heavily as the market is segmented along doses line etc. Producers are able to sell higher priced product more as the doctor is willing to prescribe that medicine due to higher commission he gets. The abuse of dominance, which was almost non-existent earlier, may become quite frequent in the new patent regime in India. Another concern is the nexus between the manufacturer of medicine and the doctors. Some States offer companies exemption from excise duty and the companies are migrating to these States, however their production units remains in the existing state. The companies are coming to Excise Exemption State for packaging of their products. The companies keep higher MRP, as they don't have to pay excise on this. Doctor prescribes the higher priced medicines as they get higher commission.

1.2.5 In India, we are talking of controlling the medicine prices but we are concentrating more on regulating the doctors/ hospitals. Consumer organisation can create some pressure for self-regulation. Till now self-regulation has not been seen.

1.2.6 There is a need to strike a balance because total control may be harmful for industry but total decontrol is also not the solution. Supreme Court has given the verdict that essential medicines and life saving drugs do not fall out of price control regime. There are concerns being raised that the government is hard on manufacturers and too soft on doctors and pharmacists. However, with decontrol mechanism, we are not hard on manufacturers but certainly we are too soft on doctors and pharmacists.

1.2.7 As in the case of Bangladesh, the doctors have to write the generic name in place of the brand name so that consumer can find out which brands are cheaper within that generic name. With this practice in Bangladesh, prices of medicine have come down and the industry is also growing at a faster rate. Import competition can also be seen as solution.

1.2.8 Another concern is of spurious medicine and quality control of diagnostic centres. Doctor advise patients to go to a particular diagnostic centre to undertake various

tests in the name quality and there are cases when doctor send patients to more than one centre and get commission from all the centres.

1.2.9 Pricing of patented medicines is also an important issue however foreign companies operating in India are resisting the price control.

1.2.10 Keeping in mind, all the various concerns that have raised with relation to the India Competition Act, 2002, the Competition Commission of India could be empowered to tackle concerns once it is operationalised.

1.3 Following comments/suggestions were made on this chapter:

1.3.1 Data on the health delivery system perhaps need to be checked. There is non specialty also towards dispense medicine, especially over the counter medicines. That constitutes a very large segment of regular medicines such as saridon, coldarin, etc. Thus if we take such medicines in account, then perhaps the data on number of outlets as mentioned in the slides, perhaps would be much larger.

1.3.2 There are 2 fundamental features of pharmaceutical industry i.e. affordability versus market determined practices. This is always a dilemma for any policy maker. But not for CCI as they would advocating that everything should be determined by market forces. But in a country like India where very large population lives at less than a dollar a day, then the issue of affordability comes. This particular paper should focus on whether the affordability should be through the mechanism of price control or through a mechanism of for example a health voucher, which could be used to provide medicine to poor people, maybe through directly giving subsidy to people living below the poverty line.

1.3.3 Another issues that need to be addressed are that lower prices in drugs bring in lower quality in services.

1.3.4 The very concept of MRP, which was designed for the governments to be able to get their tax revenues in non-debatable forms. From the consumer perspective, if anyone goes to any market in India, the moment you buy the drug, the pharmacist would look at the MRP and sell the drug at that price. However, MRP is not the retail price determent, its only a maximum recommended price. MRP is a seal, so there is absolutely no competition for any drug that one can buy anywhere in India, as because it is all sold at MRP. So MRP can be a competition concern. One can say that they are colluding between so many markets across the whole country, but sadly it has become a standard business practice.

1.3.5 Issue of VAT, which is chargeable on the discounted prices and only at after setting of the prices already paid by the retailer. The consumers are being asked to pay VAT on MRP, which is wrong. As because the retailers, are charging the price which is already been collected and paid into the VAT. The retailer, the pharmacists are not at all depositing the VAT, which charged from the consumers. This is a serious issue, which needs to be looked into.

1.3.6 The issue of abuse of dominance, in case of IPRs. There is a need to build capacity and experience to deal with this issue. So the important issue here is that, if you are giving the IPR exemptions, then how should competition authority deal with such exemptions, is the important issue?

1.3.7 The issue of prescription audit needs to be emphasised in the study. It was stated that may years ago, CUTS had taken this issue and had undertaken a campaign.

However, the campaign lost its steam, as it is a State Subject, so there is a need to deal with all the individual State Governments through India and because o budget constraints the campaign was lost. In Saudi Arabia, CUTS came across a study, which showed that 40% of price fall had taken place as soon as prescription audit was announced. The fear of stick often works far better than the stick itself.

1.3.8 On the issue of tied selling, another point is that, at the retail level is their evidence of tied selling?

1.3.9 There is also need to look at political economy dimensions. The issue of parallel imports also needs to be mentioned. For ex. Hindustan Lever brought a case against a company importing lux soaps from Indonesia. The Bombay High court granted a stay, this is a clear case of competition. The IPR regime is very clear, i.e. once you have put a product in the market, then your rights are exhausted only rights that remains is that somebody does not make a spurious lux soap. In Indonesia, the economy had a down turn and the rupiah became, then some importers found that importing lux soap from Indonesia makes a better sense, but HL moved the Bombay HC to get a stay. The stay was granted. Another issue which is important is of exportability i.e. when you have licensing conditions i.e. you can only sell in India market, then if you sell that product in Africa market, then do those African countries have provisions for parallel imports? As a concept, this needs to be mentioned in the paper.

1.3.10 There is also important issue that needs to be touched, is the issue of access to doctors. In villages, people don't have access to doctors. First comes accessibility to services, such as hospitals, doctors and then comes the issue of accessibility to medicines.

1.3.11 The paper does not really discuss the health care delivery system in place pharmaceutical industry. Regulating pharmaceutical industry is one issue and regulating medical profession is separate issue. It tries to find out the barriers to competition that prevent consumer to have the access to the complete knowledge about the product i.e. the right price& availability, its side effects etc.

1.3.12 Mapping of the regulatory structure, (what are their roles, if there is any anti competitive practice where to go, in case of abuse where to address, is there overlapping jurisdiction between different regulatory bodies) in terms of entry barriers, competition and regulation related issues. As there are multiple regulatory bodies, consumers as well as producer get confused.

2. Competition Regimes and Business Welfare

Draft of chapter is available at
http://www.cuts-international.org/pdf/ICRR07_CompetitionRegimeBWelfare.pdf

2.1 The chapter has been written against the background that competition is necessary for the existence of firms. More than one firm can often do a number of things together to enhance value that a single firm cannot do alone. Competition is necessary for increasing productivity, adoption of new technology, improvement in business practices and enhancement of value by delivering more to buyers. Competition also increases value through improvement in factor markets (better

trained work force and more efficient suppliers). It can also help firms garner resources from the environment through lobbying and joint action.

2.2 Following issues from the chapter were highlighted in the presentation:

2.2.1 People often say competition is good for business. Now at some level it seems to be a very strange idea, as to why competition would benefit business houses? In standard common understanding business should be wary of competition for ex. monopoly does benefit businesses.

2.2.2 However, in business one benefits from the action of the rival. For ex. in telecom, if there is new entry into the market and if there are more players, you as a competitor benefit. As because the value of a telephone connection that you provide, that value goes up. Thus in network industries, there are benefits from competition. Thus the only way businesses can benefit from competition is because of the presence of externalities.

2.2.3 So first thing to be explained is what is competition? In economics sense, it means paradigm of perfect competition i.e. large no of players, homogeneous products, free entry and exit from market and perfect information.

2.2.4 One may say homogeneity is bad, leads to comodification of ones product and as a result one faces extremely tough competition. But again standardisation helps, particularly in the case of new products. If one has a new product that the common problem is that who would buy the product in the market?

2.2.5 The real problem lies in entry and exit. One could argue that the possibility of entry makes the market contestable, that it would lead to lower prices being charged by players in the market and that could lead to problem. There is a need to look at entry and exit together. Entry is restricted either through government restrictions or because of capital market imperfections. If firms were not allowed to exit, then the inefficient firms would be allowed to operate, which would not benefit the market.

2.2.6 Perfect or better information is good for businessmen. Now because of Internet one can reach out to larger audience. Better information helps the producers in the market and it also leads to more intense competition.

2.2.7 Competition is necessary for existence of firms, several firms can often do a number of things together, competition is necessary for increasing productivity at option of new tech, and competition results in improved factor markets for ex. Better trained workforce, efficient supplies and finally only inefficient firms fear competition.

2.2.8 Finally, there is a need to identify case studies to substantiate what is being dealt in the paper.

2.3 Following comments/suggestions were made on this chapter:

2.3.1 There is a need to differentiate between standards and standardisation. In the sense that, the economics of standards for example the CDMA technology or GSM could actual be good for competition in the long run, there could be

competition between differing standards. Once if you establish a standard, there may be a possibility of exercising some amount of monopoly.

2.3.2 There is a need to distinguish two levels of argument in the paper i.e. one level of argument is about, would I rather work in a policy environment, where competition policy is effectively enforced or would I rather work in a policy environment, where business and government can get together and I have a country with a series of segmented monopolies running everything. The question is about where the preference of any businessmen would be? 2nd level of question is that can we say that there are certain aspects of competition, which are good for businesses bottom line? The real challenge lies in the 3rd question, is competition the contestability of the market that I serve good for my bottom line?

2.3.3 Contestability of market or contestability in market. Contestability of markets does not necessary translates into classical perfect competition. Ex. Infotech and Internet sector. The great thing about Internet is the cost of barriers to delivery services are so limited i.e. winner's takes all environment. With Internet there is no barrier to access to market. It is a contestable market. Need to look into contestability.

3. Theme Section: Competition Regime and Enhancing Access

Draft of chapter is available at
http://www.cuts-international.org/pdf/ICRR07_CompetitionRegimeWAccess.pdf

3.1 The idea behind this chapter is that we should take some attribute of competition and try to see how competition regime has affected that attribute. There is a need to look at the environment in which we are looking at the attribute. That's why this raises the question what are the political economy environments within which we are talking about widening access?

3.2 Following issues from the chapter were highlighted in the presentation:

3.2.1 There is a need to see that the State should play the role of a facilitator or regulator to see that the markets are working, to offer wider choice, consumer choice are safeguarded and no windfall profits to the providers. From this realisation the idea came that enhancing or widening access, safeguarding consumers interest, these are some of the objectives that are important to be analysed in the political economy context we are talking about. To what extent has this intention of the government been put into practice? There is a need to look at the environment we are talking about to analyse the extent to which these objectives have been put into practice. This lead to the need to analyse the market reforms that were initiated and what came out was that the political economy situation that when market regulatory reforms are initiated by way of implementation of regulatory or competition laws, there are always apprehensions among various constituencies about such market regulatory reforms, including consumers as they are not aware of impact of such reforms, they are ignorant and unorganized. Business groups are against such reforms as because they perceive

such reforms as a situation where the state plays the role of interventionist by being a regulator.

3.2.2 Thus there are roadblocks in implementation of market reforms by various constituencies ex. Consumers, business houses, etc. The opposition by all such stakeholders could result in the competition regime being captured by powerful vested interests. For example, the enactment of competition law was in a way captured by business houses as far as the merger provision is concerned. The competition law had to be redesigned to suit their interests.

3.2.3 Thus in a situation, where economic decision making are being manipulated by various constituencies for their own interests, then what happens to the whole issue of enhancing access of safeguarding consumer interests. Thus the objectives may be sidelined and could be captured by business interests as has happened in various countries.

3.2.4 To analyse various issues, as mentioned above, the study of the telecom market was undertaken. The telecom market has been quite successful as far as widening access, is concerned, with the growth in the number of subscribers over the years, and lowering of tariffs. Given the political economic situation, the study of the telecom sector was undertaken to see as to what extent widening access or increase access in telecom sector was the direct result of the governments action or whether it was a result of another policy action of the Government?

3.2.5 In 1992, the Government allowed the private sector to enter the market and provide value added services. Then the Telecom Policy allowed the private players to provide all the services. The idea behind allowing the private sector to enter the market was to meet the need of investment in the sector. But in that policy statement there was no acknowledgment per se of need for competition, in bringing down prices, in providing services with better quality, in expanding of the market. This implied that increasing telephony target was the sole objective, other attributes of access, quality, price they were all sidelined. The widening of the market through national telecom policy was only a halfhearted objective.

3.2.6 Earlier the market in the telephone sector was divided; the fixed line telephony was reserved for public sector, the mobile phone telephony was reserved only for the private sector. Later on, the public sector incumbents realised that they made a fault by keeping out of the mobile telephony, which was turning out to be a lucrative market. So the public sector played a spoilt sport and that lead to turf war between TRAI and the Government, between private operators and DOT, etc. These disputes occurred because the government's objective through the National Telecom Policy was to increase the telephony targets. At the same time, when DOT and MTNL started to play spoil sport, the objective turned out to enhance the interest of the public sector incumbents rather than increasing the telephony targets. So the objective turned to be something else, it was different to what was mentioned in the NTP.

3.2.7 In order to tackle the disputes, the Government introduced a New Telecom Policy. The Government allowed the public sector incumbents to enter into the mobile telephony. So when both the public and private sector were allowed in the market, competition started to appear in the market. So the question that could be asked is why did this not happened earlier? What comes out is that the competition that

was allowed in the sector was not the deliberate move by the government but rather the motive of the government was to have a truce between the public and private players rather than having competition or widening access in the market.

3.2.8 So what emerges from this case study is that, the widening access appears to be a bye product of the disputes between the public and private players and that widening access was an accidental bye product.

3.2.9 Thus the hypothesis that *widening access was an accidental bye product* shall be put to test in other sectors such as electricity, water, transport, etc. Other dimension of the paper shall be that subsidy is often used by the government to ensure widening access of certain goods and services. But due to fiscal problems, the government is looking at other means to achieve these objectives. Such as educational vouchers to widen access to elementary education. Here one question could be asked, that are educational vouchers are being used to actually widen access or is it to take care of the fiscal problem of the government and widening access is once again a bye product. The reason is because it's easy to say that educational vouchers would provide easy access to students but this is possible in urban areas. In rural areas, it is not possible as there is no choice available to decide on schools. In urban areas, neighbourhood schools are being promoted, which also restricts the choice to select a school. Then again the point comes that when ever we talk about widening access, then these ground realities are not being considered. Rather some other implicit objectives are being achieved.

3.3 <u>Following comments/suggestions were made on this chapter</u>:

3.3.1 How do you fit in Universal Service Obligations, etc into the said thesis? There is a need to address the same, as USO is a part of the policy of the government.

3.3.2 There were concerns about the title of the paper and as to what was presented. The correlation was missing. Referring to the title, providing access it came across that it meant that people, who were previously shut out of the market system, would now enter the market. We often forget the need to have a large number of buyers in the market when we talk about market and competition. We don't think about the market mechanism as price discovery mechanism. So for the market to function well, for the price to reflect the true value of the product, there is a need of larger number of people in the market.

3.3.3 There is a need to change the approach of the paper. Rather saying that the widening access is the bye product of governments action, it would be better to mention that competition is a better way to promote widening access than government policies.

3.3.4 It was re-iterated that the title and content of the paper i.e. "competition regime and widening access" did not have any co-relation. There are two dimensions to the title, one that government policies impede access to the market, this has to be addressed separately and whether competition has resulted in a larger market, needs to be addressed separately. There is no need to put two things together i.e. government and competition policies as the linkage and focus is missing.

3.3.5 Competition law and competition policy needs to be differentiated. Competition policy is being looked in larger dimension in the said chapter.

3.3.6 There is a need to define widening access in the said chapter.

3.3.7 There is a need to change the title of the said chapter i.e. from Competition Regime and Enhancing Access to Competition Regime and Widening Access.

List of Participants

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