COMPETITION COMMISSION OF INDIA

Explosive Manufacturers Welfare Association  

Coal India Limited and its Officers

Order under Section 27 of the Competition Act

As per R. Prasad, Member (dissenting):

In this case, the Commission had directed investigation by the Director General under Section 26(1) of the Competition Act, 2002. The D.G. investigated the case and found contravention of Sections 3 & 4 of the Competition Act. The informant in this case, an association of Explosive Manufacturers, probably because of the economic strength of Coal India Ltd. withdrew its complaint. As withdrawal of information is not permitted, the Commission gave a hearing to the parties concerned after giving them a copy of the DG’s report. The information provider did not appear but the opposite party, Coal India Ltd. appeared and argued its case. The majority of the Commission held that no contravention of the Competition Act was established and therefore the case should be closed. I do not agree with this view and there I am passing a separate order for reasons given below:

2. This is a case of public procurement. Coal India Ltd. is a public sector undertaking having a near monopoly of production of coal in India. For the production of coal, purchase of explosives is necessary. This case is of procurement of explosives by Coal India Ltd. Incidentally Coal India consumes 60% of the total of all the explosives consumed in India. The
information provider (I.P.) in its complaint contended that the opposite party (OP) entered into a five year contract with Indian Oil Corp. (IOC) and Indo Burma Petroleum (IBP) on nomination basis and without calling tender for the supply of explosives amounting to 20% of the total explosives consumed by the O.P. It was also alleged that the OP unilaterally amended the rate contract after the issuance of the tender. It was also alleged that the security deposit at 10% of the contract value was not returned even after the expiry of the contract. The I.P. also objected to the reverse auction process for the process of the award of contract. It was further alleged that though the contracts were for three years the O.P. unilaterally changed it one year. The I.P. also stated that the O.P. was pressurising its members to lower the prefixed prices of the explosives. The association has also alleged that the O.P. had arbitrarily terminated the contracts entered into thus causing loss to its members. The information provider therefore stated that the O.P. had contravened Sections 3(1), 3(3)(a) and 3(3)(b) of the Act.

3. The D.G. investigated the case and came to the conclusion that it is a case of abuse of dominance. According to him, the relevant product market is the consumption of bulk and cartridge explosives and the relevant geographical market is India. He also found that the O.P. consumes 65% of the total consumption of explosives in India. Thus, the O.P. was a dominant player and the dominance had come due to the Coal Mines Nationalisation Act of 1973. The D.G. also found that the contracts were entered into by the O.P. with its suppliers for one year only and not for three years. As far as the revision of prices is concerned, the revision of prices was part of the contract and therefore no error/abuse was committed by the O.P. Regarding reverse auction and e-procurement the D.G. found no merit in the allegations. Regarding the allegation regarding the quality of procured articles, the D.G. found no fault in the conduct of the O.P. Regarding the agreement with IOC-IBP, the DG found that the O.P. had entered into contract with the said consortium for five years
against one year with the other parties. No security deposit was taken from this consortium and that the contract on nomination basis was to ensure regular supply of explosives. Incidentally the supplies in the first year of the contract was only 14.5% of the total consumption of explosives against 20% contracted for. The D.G. found that the disruption in supplies from the other suppliers was only on 2-3 occasions in the last 6-7 years. The D.G. held that the agreement with IOCL-IBP restricted the market for the other competitors and this constituted a violation of section 4(2)(b)(i) of the Act. The D.G. also recorded a finding that the agreement with IOCL-IBP denied market access to the competitors and therefore it violated sections 4(2)(c) of the Act. The D.G. did not find any violation of Section 3(3) of the Act but in respect of the exclusive supply agreement with IOCL-IBP he found a violation of Section 3(4)(b) of the Act. He was also of the view that the agreement with IOCL-IBP led to refusal to deal and therefore held that even the contravention of Section 3(4)(d) was established.

4. On the other hand, it was argued on behalf of the O.P. that the O.P. is not a dominant player and therefore is not hit by the provisions of Section 4(1) of the Act. Further it had not resorted to any abusive conduct. It was stated that the other suppliers had formed a cartel which was disrupting supplies, increasing prices and had abusive conduct. It was argued that as 80% of the market was left for the other suppliers, there was no exclusive supply agreement and that there was no refusal to deal. It was therefore stated that the provisions of Section 4 and Section 3(4) were not attracted. It was argued that if it was held that there was contravention of the Act, it would mean that no enterprise could enter into directly negotiated contracts with its suppliers. It was stated that due to cartelisation by the suppliers and boycott by them it was necessary to give orders on nomination basis. This helped the O.P. in maintaining buffer stock and defeat the cartelisation by the other suppliers.
5. In view of the information, investigation and the agreements of the O.P., the issue has got to be decided. There is no doubt that it is a case of public procurement. On public procurement, the Supreme Court in two decisions has laid down the law. The first case is Nagar Nigam vs. Al Faheem Meat Exports Pvt. Ltd. & Ors. SLP(Civil) NO. 10174 of 2006. The findings of the Supreme Court are as under:-

"This Court time and again has emphasized the need to maintain transparency in grant of public contract. Ordinarily, maintenance of transparency as also compliance of Article 14 of the Constitution would inter alia be ensured by holding public auction upon issuance of advertisement in the well known newspaper. That has not been done in this case. Although the Nagar Nigam had advertised the contract, the High Court has directed that it should not be given for 10 years to a particular party (respondent No. 1). This was clearly illegal. It is well settled that ordinarily the State or its instrumentalities should not give contracts by private negotiation has been carried out by the High Court itself, which is impermissible. We have no doubt that in rare and exceptional cases, having regard to the nature of the trade or largesse or for some other good reason, a contract may have to be granted by private negotiation, but normally that should not be done as it shakes the public confidence. The law is well-settled that contracts by the State, its corporations, instrumentalities and agencies must be normally granted through public auction/public tender by inviting tenders from eligible persons and the notification of the public-auction or inviting tenders should be advertised in well known dailies having wide circulation in the locality with all relevant details such as date, time and place of auction, subject-matter of auction, technical specifications, estimated cost, earnest money Deposit, etc. The award of Government contracts through public-auction/public tender is to ensure transparency in the public procurement, to maximize economy and efficiency in
Government procurement, to promote healthy competition among the tenderers, to provide for fair and equitable treatment of all tenderers, and to eliminate irregularities, interference and corrupt practices by the authorities concerned. This is required by Article 14 of the Constitution. However, in rare and exceptional cases, for instance during natural calamities and emergencies declared by the Government; where the procurement is possible from a single source only; where the supplier or contractor has exclusive rights in respect of the goods or services and no reasonable alternative or substitute exists; where the auction was held on several dates but there were no bidders or the bids offered were too low, etc., this normal rule may be departed from and such contracts may be awarded through 'private negotiations'. (See Ram and Shyam Company vs. State of Haryana and Ors. MANU/SC/0017/1985 AIR1985SC1147).

In the second case i.e. Sachidanand Pandey vs. State of West Bengal 2SCR223, Justice O. Chinnappa Reddy after considering various decisions of the apex court summarised the legal propositions in the following terms:-

On a consideration of the relevant cases cited at the bar the following propositions may be taken as well established: State owned or public owned property is not to be dealt with at the absolute discretion of the executive. Certain precepts and principles have to be observed. Public interest is the paramount consideration. One of the methods of securing the public interest when it is considered necessary to dispose of a property by public auction or by inviting tenders. Though that is the ordinary rule, it is not an invariable rule. There may be situations where there are compelling reasons necessitating departure from the rule but then the reasons for the departure must be rational and should not be suggestive of discrimination. Appearance of public justice is as important as doing justice. Noting should be done which gives an
appearance of bias, jobbery or nepotism. The public property owned by the State or by an instrumentality of the State should be generally sold by public auction or by inviting tenders. This Court has been insisting upon that rule, not only to get the highest price for the property but also to ensure fairness in the activities of the State and public authorities. They should undoubtedly act fairly. Their actions should be legitimate. Their dealings should be above board. Their transactions should be without aversion or affection. Nothing should be suggestive of discrimination. Nothing should be done by them which gives an impression of bias, favouritism or nepotism. Ordinarily, these factors would be absent if the matter is brought to public auction or sale by tenders. That is why the Court repeatedly stated and reiterated that the State owned properties are required to be disposed of publicly.

He also observed as follows:-

"That though that is the ordinary rule, it is not an invariable rule". There may be situations necessitating departure from the rule, but then such instances must be justified by compulsions and not be compromise. It must be justified by compelling reasons and not by just convenience.

In the case of Nagar Nigam (Supra), the Court further observed:-

The law is, thus, clear that ordinarily all contracts by the Government or by an instrumentality of the State should be granted only by public auction or by inviting tenders, after advertising the same in well known newspapers having wide circulation, so that all eligible persons will have opportunity to bid in the bid, and there is total transparency. In our opinion this is an essential requirement in a democracy, where the people are supreme, and all official acts must be actuated by the public interest, and should inspire public confidence.
The law laid down the Supreme Court is the law of the land and has got to be followed in all government contracts and procurement.

6. An argument may be raised that though it may be the law of the land, unless it is violative of the competition Act, no notice can be taken by the Commission. In this connection it is necessary to examine the preamble to the Competition Act which reads as under:-

An Act to provide, keeping in view of the economic development of the country, for the establishment of a Commission to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interest of consumers and to ensure freedom of trade carried on by other participants in markets, in India, and for matters connected therewith or incidental thereto.

In India, public procurement by Central and State governments, corporations and other instrumentalities account for 30% of the G.D.P. of India. As India’s GDP is around 2 trillion dollars, the expenditure on public procurement is very high. This large public procurement leads to competition effects. The procurement by the Govt. and its instrumentalities leads to economic development and creation of jobs. The public sector can promote competition by sourcing requirements from a range of suppliers. It can also restrict competition by restricting participation in tenders and it can also discriminate against particular types of firms. The public sector can also contribute towards an improvement of competitive conditions. In fact, public sector enjoys buyers power. Buyer power is related to the size of demand relative to total demand in a relevant market. It also enjoys power because it is strategically important customer for its suppliers. There are differences between public procurement and private procurement. There are legal and regulatory requirements for public procurement which do not exist for private procurement. Transparency and non discrimination are necessary
for public procurement. Decision to purchase is different for a public sector as compared to private procurement. Public Sector is more risk averse and therefore failure is normally avoided. Public Sector purchases are not with a desire to maximise profits. There are other policy objectives which binds a public sector such as employee’s welfare, govt. policies etc.

7. When tendering process is adopted in public procurement it leads to breaking entry barriers. It results in lower prices and better quality and savings which leads to surplus for investment. It also increases competition in the market and more contracts can be given to large number of firms/persons. Public procurement can lead to significant effects on investment and innovation. In fact large public sector demand leads to increase in productive capacity and employment. In fact, public sector demand can create a market. For these reasons, the Supreme Court came up with the decisions as reproduced above.

8. Incidentally, the Competition Act has constitutional sanction. This is evident from the Preamble of the Constitution which is reproduced as under:

THE PEOPLE of India, having solemnly resolved to constitute India into a [SOVEREIGN SOCIALIST SECULAR DEMOCRATIC REPUBLIC] and to secure to all its citizens:

JUSTICE, social, economic and political;

LIBERTY of thought, expression, belief, faith and worship;

EQUALITY of status and of opportunity; and to promote among them all

FRATERNITY assuring the dignity of the individual and the [unity and integrity of the Nation]
IN OUR CONSTITUTENT ASSEMBLY this twenty-sixth day of November, 1949, do HEREBY ADOPT, ENACT AND GIVE TO OURSELVES THIS CONSTITUTION.

The Preamble talks about economic justice and the equality of opportunity. In accordance with equality of opportunity and economic justice in the market, there is a necessity to prevent practices resulting in an adverse effect on competition and to protect the interest of consumers and also to ensure freedom of trade carried out by participants in the markets. For this purpose, if someone enters into an agreement which would have adverse effect on competition then such an agreement is a void agreement. Similarly the effort to fix prices, limit or control production, supply development and provision of services or allocating markets is presumed to have appreciable adverse effect on competition. Even exclusive distribution agreement etc. or the discriminatory practices in sale or purchase of goods or even having conditions in purchase or sale of goods, denial of market access infringe on the economic freedom and equality before law. Therefore, any public procurement which has anti competitive elements is hit by the provisions of Competition Act.

9. In this particular case 20% of the supply was given to IOCL and IBP on nomination basis without calling for tenders. This is against the law as laid down by the Supreme Court. This also shows exclusionary conduct on the part of Coal India Ltd. because for 20% of the supply of explosives was given to the consortium of IOCL-IBP.

10. The issue to be decided here is as to whether the procurement of explosives, to the extent of 20% of the total consumption of explosives, on nomination basis from IOCL-IBP is justified. Coal India Ltd. i.e. the O.P. has justified it on the ground that due to the disruption of supplies and to maintain a large inventory of explosives so that production does not suffer, it was necessary to outsource the procurement on nomination basis. It has been justified that this procurement was done with the
approval of the Ministry. On the other hand, the D.G. has recorded a finding that in the last 6-7 years, there was a disruption of supplies only on 2-3 occasions and never for more than two days at a time. This finding of the D.G. has not been controverted when the hearing took place. Therefore, as laid down by the Supreme Court no compelling reasons have been given by the O.P. which would justify non-tendering of the procurement requirements. There could be other reasons for taking the procurement decisions to the extent of 20% on nomination basis and not business exigencies.

11. Coal India consumes 65% of all the explosives consumed in the country. By not tendering purchase of 20% of the explosives consumed by it shows anti-competitive behaviour of Coal India Ltd. Many persons who had invested in manufacturing capacity of explosives would thus be debarred from the supply of explosives to Coal India. Further the behaviour of Coal India by taking supplies without any security deposits is also discriminatory because in the case of other suppliers’ security deposits at 10% of the contracted value was taken as a deposit. It is also seen that though the contract with IOCL-IBP was for a period of 5 years, as far as other suppliers are concerned, the contract is only for a period of one year. Incidentally IOCL is not a manufacturer of explosives and therefore IOCL could not have produced the goods and supplied to Coal India Ltd. There is therefore reason to have a prima facie belief that there was an abuse of dominant position by Coal India in the public procurement of explosives.

12. The majority has agreed with the finding of the D.G. regarding the relevant market and dominance of the O.P. in that market. But no abuse of dominance was found by the majority. In the view of the majority, 20% of the total procurement on nomination basis constituted a small quantity and the suppliers were not debarred from supplying to other procurers. It was further held that there were justifiable reasons for procuring on nomination basis. It has also been held that the choice of
supplier does not fall within the ambit of Competition Act. It is also view
of the majority that once a selection of a supplier is made, the other
suppliers cannot claim that their supply is restricted. It has also been
observed that 80% of the market has been left to the other suppliers,
there was no harm to competition in India. It is also the view of the
majority that the selection of choice of supplier, unless it falls foul of
competition law is not an issues which should be brought before a
competition agency. For these reasons, it has been held by the majority
that as no limit or restriction is placed on the production of services or
market by the action of the O.P., there is no denial of market access. For
this reason it was held that the contravention of Sections 4(2)(b)(i) and
4(2)(c) of the Competition Act has not been established.

13. Regarding the applicability of Sections 3(4)(b) and 3(4)(d) of the
Competition Act, the majority of the Commission after examining the
provisions of Section 19(3) of the Act found that as no entry barrier in the
market had been created by the action of the O.P. Further sourcing of
20% of the supplies on nomination basis did not drive other competitors
from the market. It was also the view of the majority that as there was
no material to hold that the action of the O.P. had resulted in creating an
adverse effect on competition in India, the contravention of Section
3(4)(b) and 3(4)(d) of the Act is not established.

14. The majority view is that an arrangement of continued supply of a
small quantity of explosives so as to have a secured supply of coal did not
foreclose the market. The majority felt that an interruption in the supply
of coal would lead to decrease in the production of coal to the detriment
of other industries dependent on coal. Regarding the allegation in respect
of delay in the refund of security deposits, shortening the period of
contract, reduction in price etc. the majority held that these related to
contractual obligations and do not fall within the ambit of competition. As
according to the majority, contravention of Section 3 and 4 of the Act, the
case is required to be closed.
15. The practices followed by Coal India Ltd. for the supply of explosives without calling for tender 20% of supply causes appreciable adverse effect on competition in respect of Section 3(1) of the Act read with Section 3(4) of the Act. Section 3(4)(c) talks of exclusive supply agreement which includes any agreement to limit or restrict or supply of goods. In this particular case as supply to 20% of the goods was limited to only one party, behaviour of Coal India showed anti competitive behaviour which creates an appreciable adverse effect on competition. The question which arises as to whether the agreement entered with IOCL-IBP could be termed as violative and therefore void in terms of Section 3(1) and 3(2) of the Competition Act.

16. Whenever public procurement is made without calling for tenders and on nomination basis, it excludes large number of persons who could have participated and got orders. Public procurement by nomination is not only against the law of the land but it is also exclusionary in nature. It kills competition in the market and leads to lower investment, lower development and may be higher expenditure for the public procurer. The agreement for procurement on nomination basis therefore leads to appreciable adverse effect on competition in India. Therefore there is a violation of not only Section 3(1) of the Act and consequently Section 3(2) of the Act.

17. Section 3(4) reads as under:

Any agreement amongst enterprises or person at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or price of, or trade in goods or provision of services, including –

(a) tie-in arrangement,
(b) exclusive supply agreement,
(c) exclusive distribution agreement,
(d) refusal to deal;
(e) resale price maintenance, shall be an agreement in contravention of sub-section (1) if such agreement causes or is likely to cause an appreciable adverse effect on competition in India.

D.G. has made out of case under Sections 3(4)(b) and 3(4)(d) of the Act. A reading of the above provisions show that there is no reason to hold that there was a refusal to deal. There was nothing on record to hold that Coal India Ltd. refused to deal with the members of the explosive manufacturers. Therefore the provisions of Section 3(4)(d) are not attracted in this case. Section 3(4)(b) like Section 3(4)(d) is an inclusive definition. It is settled law that whenever a definition is inclusive, a wide meaning has to be given to the provisions. Section 3(4)(b) talks of an exclusive supply agreement which is any manner restricts the supply of goods to a procurer from any seller. In this case as far as 20% of the goods (explosives) are concerned, there is an exclusive supply agreement. But the provisions of Section 19(3) have to be seen before any conclusion of contravention of Section 3(4)(b) can be established. I have already held that if procurement is made on nomination basis without tendering, it is exclusionary. In fact 20% of the market in this case of procurement is closed to all competition. Thus, the facts of this case are hit by the provisions of 19(3)(c) of the Act. By reserving 20% of the market, the market gets reduced and this can act as a barrier to new entrants in the market. Thus, the provisions of Section 19(3)(a) are also attracted. I do not agree with the majority view that there was no foreclosure of competition in this case. Thus in my view, there is a contravention of Section 3(4)(b) of the Act in this case.

18. Regarding abuse of dominance, it is an accepted fact that the O.P. is a dominant player in the procurement of explosives. There is no dispute in respect of the relevant market. The issue to be decided as to whether there is an abuse of dominance. The D.G. has made out a case of violation of Section 4(2)(b)(i) and 4(2)(c) of the Act. Section 4(2)(b)(i)
talks of limiting or restricting a market and Section 4(2)(c) is about the denial of market access. On the other hand, the majority view is that there was no contravention of these two Sections. There is no doubt that Coal India Ltd. is a dominant player in the purchase of explosives as it consumes 65% of the explosives consumed in India. Its dominance comes due to the Coal Mines Nationalisation Act. In fact, it can act independently of competitive concerns in the market. It is in a position to affect its suppliers in its favour. Thus, Coal India Ltd. is hit by the explanation to Section 4 of the Act and it is a dominant player. The other issues to be examined are as to whether its behaviour is abusive in terms of the provisions of Section 4 of the Act. The D.G. has correctly held that by not calling tender for 20% of the procurement of explosives the market has not only been limited but it has also been restricted. Thus in this case there is a violation of Section 4(2)(b)(i) of the Act. Further, as far as 20% of the procurement is concerned, there is a denial of market access to the other suppliers. Therefore there is a contravention of Section 4(2)(c) of the Act.

19. The D.G. has not examined the discriminative behaviour of Coal India Ltd. As far as the members of the information providers are concerned, they used to get a contract for one year whereas the contract given to IOCL-IBP is for a period of five years. This is discriminatory behaviour on the part of Coal India Ltd. Further, no security deposit has been asked for from IOCL-IPL though the other parties have to give a security deposit at 10% of the contract value. If this is not discrimination, it is not clear as to what would be discrimination. Abusive behaviour of Coal India Ltd. is also established by the fact that the refund of the security deposits is not given by Coal India to its suppliers. Thus, there is a contravention of Section 4(2)(a)(i) of the Act.

20. Before invoking the provisions of Section 4, it is necessary to consider the factors mentioned in Section 19(4) of the Act. Coal India has
acquired its dominant position as a result of Coal Mines Nationalisation Act. Therefore the provisions of 19(4)(g) are attracted. Taking into account the predominant position of Coal India Ltd., the provisions of clauses (a), (b), (c) and (d) of Section 19(4) are also brought in play. Even clause (f) of Section 19(4) is applicable in this case as the suppliers are dependent on the orders of Coal India Ltd. because it is the dominant buyer in the explosives market. By its action of closing 20% of the supply, Coal India Ltd. has created entry barriers to other suppliers. By not calling for tender, entry barriers are also created. Therefore, Section 19(4)(h) is also attracted. The action of Coal India in this case is opposed to social obligations and social costs. This happened as there was no equality for the suppliers at the time of procurement. Even the concept of opportunity was not given to the other suppliers. Further the tender was not called in this case of supply in accordance with the law laid down by the Supreme Court. Thus, there is a contravention of Section 19(4)(k) of the Act. As discussed above such an action by a major buyer can lead to a slower economic development. Thus, even Section 19(4)(l) is attracted.

21. There is another issue to be discussed that freedom of a buyer to choose its suppliers and product. In the Competition Act, freedom of trade is mentioned only in the Preamble to the Act and Section 18 and nowhere else. But the other aspects in the Preamble have to be considered and freedom of trade cannot be considered in isolation. The other factors are:-

(i) prevent practices having adverse effect on competition
(ii) to promote and sustain competition in markets
(iii) to protect the interest of consumers.
(iv) economic development of the country.

Similar view is expressed in Section 18 of the Commission. The question is whether the choice of supplier even if it leads to anticompetitive behaviour comes under the head freedom of trade. The next question is whether any purchases by the State / sale of assets of the State i.e. in
broad terms public procurement would come within the ambit of freedom to make a choice and hence freedom of trade. The State and its instrumentalities are not a living persons. The purchases/sale of assets of such a person cannot be equated with private purchases where a person has the option to make his own choice. As already discussed, public procurement can lead to make anticompetitive infringements. No general rule can be framed and the facts have to be examined on case to case basis. But in any case the state looks towards the welfare of its citizen. It not only protects the freedom of speech and trade but also sees that there is equality before law, equality of opportunity and economic justice. No minion of the State or its instrumentalities can forget the laudable ideas for which the State exists, and take shelter behind the maxim 'freedom of choice'. Freedom of choice does not work in public procurement because many factors come into play when a decision of procurement is made. Further freedom of choice comes from freedom of trade. There has to be a restriction on freedom of trade when the other factors mentioned in the preamble and the Competition Act are considered. Otherwise the Competition Act will be negated and become otiose. In such a case, any violator of competition law can take the plea of freedom of trade and freedom of choice. That cannot be the aim of the Parliament and the citizens of the State.

22. Considering all these factors, it is established that Coal India Ltd. had contravened the provisions of Section 3(1), 3(2), 3(4)(c), 4(2)(a)(i), 4(2)(b)(i) and 4(2)(c) of the Act.

23. Considering the contraventions, Coal India Ltd. is directed
(i) to cease and desist from procuring goods without calling in tenders for procurement except in exceptional circumstances.
(ii) to refund the security deposits of suppliers.
(iii) not to discriminate between suppliers.
(iv) As there has been a contravention of Competition Law as discussed above and it is the first contravention by Coal India Ltd., a penalty of Rs. One Crore is levied on Coal India Ltd. which is much below 10% of the average turnover of Coal India Ltd.

The Secretary is directed to serve this order on Coal India Ltd.

Certified True Copy

Assistant Director
Competition Commission of India
Govt. of India,
New Delhi

(R. Prasad)
Member, CCI