



February 27, 2023

# OPEN NETWORK FOR DIGITAL COMMERCE

## - ISSUES AND CHALLENGES FOR PAYMENT AGGREGATORS

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## INTRODUCTION

Digital commerce, over decades, has grown exponentially and reshaped the global business environment and the manner in which buyers and sellers across the globe transact with each other, leading to a fairer marketplace for all businesses, including small businesses, across the globe. This exponential increase in digital commerce was further fueled by the advent of the COVID-19 Pandemic. During the Pandemic, with the whole world being home bound, while there was a decline of digital commerce in the travel services, digital commerce in the retail space sky-rocketed. People flogged online to purchase medicines and medical supplies, household supplies and groceries, leading to an increase in business-to-consumer (B2C) sales. India did not remain untouched by the impact the COVID-19 Pandemic had on the online retail space and consequently, all the shortcomings of the Indian digital commerce ecosystem were exposed since most parts of the retail chain were found to be digitally absent and there was a complete breakdown of the supply chain. Local grocery stores or 'Kirana' stores as they are colloquially called, while being just round the corner from the consumer and having the requisite supply, were not digitally present, leading to a simultaneous loss to both the consumer and the owner of the 'Kirana' stores.

In view of the weaknesses in the digital commerce space exposed by the COVID-19 Pandemic, the dominance of e-commerce giants such as Amazon and Flipkart and in order to democratize the e-commerce space and to not have buyers and sellers restricted to one e-commerce platform, the Department for Promotion of Industry and Internal Trade ("DPIIT"), Government of India ("GoI"), created the Open Network for Digital Commerce ("ONDC").

The ONDC entity was incorporated on December 30, 2021, as a not-for-profit Company, under Section 8 of the Companies Act, 2013, with limited liability and a majority ownership of private sector institutions. The GoI, on September 30, 2022, released ONDC on a beta testing basis in Bengaluru, Karnataka.

## WHAT IS THE ONDC?

The DPIIT, while introducing ONDC, released its Strategy Paper<sup>1</sup> on January 25, 2022 ("Strategy Paper"), threw light on the new e-commerce sphere sought to be created by the DPIIT. In the Strategy Paper, the DPIIT recognized the importance of a facilitator driven and interoperable decentralized network such as ONDC. In the ONDC, as long as the platforms/applications are interoperable, buyers and sellers can transact, no matter what platform/application they use to be digitally visible/available. The Strategy Paper describes ONDC as a network that enables location aware, local digital commerce stores across industries to be discovered and engaged by any network enabled applications. The Strategy Paper further clarifies that ONDC is neither a super aggregator application nor a hosting platform and all existing digital commerce applications and platforms can voluntarily choose to adopt and be a part of the ONDC network. The responsibility of onboarding sellers and buyers and the management of the end-to-end order cycle would also continue to reside with such network-enabled applications.

The ONDC, thereafter released the ONDC Network Policy<sup>2</sup> ("ONDC Network Policy"), whereunder it defined "ONDC Network"<sup>3</sup> as the open, interoperable network established, facilitated, managed, made available and owned by ONDC for enabling digital commerce.

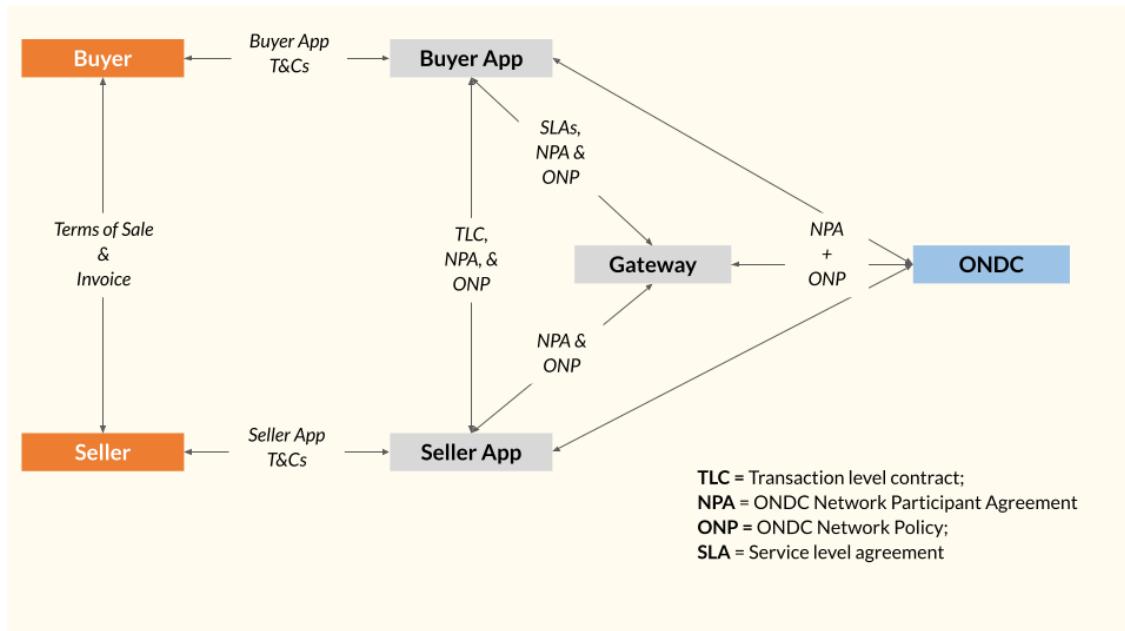
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<sup>1</sup>[https://ondc-static-website-media.s3.ap-south-1.amazonaws.com/res/daea2fs3n/image/upload/ondc-website/files/ONDCStrategyPaper\\_ucvfjm/1659889490.pdf](https://ondc-static-website-media.s3.ap-south-1.amazonaws.com/res/daea2fs3n/image/upload/ondc-website/files/ONDCStrategyPaper_ucvfjm/1659889490.pdf)

<sup>2</sup><https://ondc.org/governance-and-policies/>

<sup>3</sup><https://ondc-static-website-media.s3.ap-south-1.amazonaws.com/ondc-website-media/downloads/governance-and-policies/Definitions.pdf>

The operation of the ONDC Network, in terms of the ONDC Network Policy can be depicted as under:



## PARTICIPANTS OF THE ONDC NETWORK

Clause 3.2.1 of the Strategy Paper, clearly stated that the “*Network Participants*” (“**NPs**”) within the ONDC could be broadly categorized into the following 2 (two) categories<sup>4</sup>, the definition of which NPs has also been laid down under the “*Technology Components*” of the ONDC in the Strategy Paper<sup>5</sup>:

- i. **Buyer-Side Application:** Any application that will interact with the buyers i.e., the demand side of any transaction, where the transaction originates. These can include different types of applications including User Experience (UX) based applications, voice assistants, chat-bots, etc. depicting the demand layer for the good or service.
- ii. **Seller-Side Application:** Any application which will interact with the sellers, i.e. the supply side of any transaction. These can be any applications that receive buyer requests and, in response, publish their catalog of goods and services and fulfill buyer orders.

The Strategy Paper further, in Clause 3.2.4, states that NPs will be responsible for managing the order life cycle depending on their roles in the network—including but not limited to customer/seller onboarding, catalogue management, order management, invoicing & reconciliation, warehousing and inventory management, logistics, customer support, returns management, payments, etc.

In furtherance of the above and subsequent to the Strategy Paper, the DPIIT, also released a Public Consultation Paper on September 29, 2022<sup>6</sup> (“**Consultation Paper**”), providing a

<sup>4</sup> Clause 3.2.1 of the Strategy Paper released on January 25, 2022.

<sup>5</sup> Clause 3.1.5 of the Strategy Paper released on January 25, 2022.

<sup>6</sup>[https://ondc-static-website-media.s3.ap-south-1.amazonaws.com/res/daea2fs3n/image/upload/ondc-website/files/ONDC\\_Building\\_Trust\\_Consultation\\_Vf\\_utbodw/1664541553.pdf](https://ondc-static-website-media.s3.ap-south-1.amazonaws.com/res/daea2fs3n/image/upload/ondc-website/files/ONDC_Building_Trust_Consultation_Vf_utbodw/1664541553.pdf).

detailed insight into the ONDC and invited suggestions from the general public to the same. The Consultation Paper, with reference to NPs, lists and defines the NPs on the ONDC as under<sup>7</sup>:

- i. **Buyer Apps (Also known as Buyer Nodes):** Buyer Apps are NPs that handle the buyer-side operations such as buyer acquisition, search and discovery and also provide a functionality to the buyer to place orders on ONDC.
- ii. **Seller Apps:** Seller Apps manage the seller-side of the operations and can be further categorized into 2 (two) categories:
  - a. Market Seller Nodes (MSNs): MSNs are essentially aggregators that allow market sellers (who, themselves, are not network participants) to transact on the ONDC. MSNs hold no inventory, but rather function as purely marketplaces.
  - b. Inventory Seller Nodes (ISNs): ISNs are sellers themselves, who are also participants in the ONDC.
- iii. **Gateways:** Gateways purely function as nodes for multicasting search queries and collecting results.

The ONDC Network Policy, defines NPs/Participants as participants on the ONDC Network, including Gateways, Buyer Side Application, Seller Side Applications, NP-ISN, NP-MSN and NP-BN. The NPs within the ONDC, in terms of the ONDC Network Policy, are defined as under:

- i. **Network Participant- Inventory Seller Node (NP-ISN)** is an entity who is registered on the ONDC network and acts as the “seller on record” with respect to the goods and services offered by them to any buyer accessing the Network from any NP-BN from their own inventory which is either from their own production or obtained procured from other merchants/service providers.
- ii. **Network Participant- Market Place Seller Node (NP-MSN)** is an entity who is registered on the ONDC network and represents itself and acts as the marketplace with respect to the goods and services offered by third party merchants/service providers to any buyer accessing the Network from any NP-BN. In this case, the NP-MSN will not be “seller on record” but the third party merchants/service providers will be the “seller on record”.
- iii. **Network Participant-Buyer Node (NP-BN)** is an entity registered in the ONDC network and enables any person to search for and buy products or services on the ONDC network from any NP-ISN/NP-MSN.
- iv. **Gateway** shall mean the technology provider that will ensure discoverability of all Sellers in the ONDC Network by multicasting the search request received from Buyer App to all Seller Apps and vice-verse, based on criteria, including but not limited to, location, availability, and other customer preferences as provided for in the Network Policies of ONDC.

Other important definitions under the ONDC Network Policy are as under:

- i. **Consumer** has the same meaning as under the Consumer Protection Act, 2019

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<sup>7</sup> Clause 1/Internal Pg. 9 of the Consultation Paper dated September 29, 2022.

- ii. **Buyer Side Applications/Buyer Apps** means all platforms and applications which enable the Consumer to purchase any goods or avail any service on the ONDC Network.
- iii. **Seller** shall mean any seller registered with a Seller Side Network Participant to offer products or services through the ONDC network, including service provider as defined under the Consumer Protection Act, which can be searched for, discovered and procured by Buyers registered with Buyer Side Applications.
- iv. **Seller Side Applications/Seller App** means all platforms or applications of Network Participant NP-ISN/MSN, which allows sellers to publish their product/service inventory, pricing, and other terms of transaction and enables the sellers or any other service providers, including but not limited to logistics service provider, to transact on the ONDC Network.

### **PAYMENT AGGREGATORS AS BUYERS AND SELLERS ON THE ONDC**

The Reserve Bank of India (“**RBI**”) introduced the “*Guidelines on Regulation of Payment Aggregators and Payment Gateways*” dated March 17, 2020 (updated as on November 17, 2020)<sup>8</sup> (“**PA-PG Guidelines**”) and the subsequent “*Guidelines on Regulation of Payment Aggregators and Payment Gateways*” dated March 31, 2021, in order to regulate Payment Aggregators (“**PAs**”) and Payment Gateways (“**PGs**”), which had earlier remained unregulated. While issuing the PA-PG Guidelines, the RBI defined PAs as under:

*“PAs are entities that facilitate e-commerce sites and merchants to accept various payment instruments from the customers for completion of their payment obligations without the need for merchants to create a separate payment integration system of their own. PAs facilitate merchants to connect with acquirers. In the process, they receive payments from customers, pool and transfer them on to the merchants after a time period.”*

Clause 3.6 of the PA-PG Guidelines clearly state that the e-commerce marketplaces providing PA services shall not continue this activity beyond the timeline prescribed by the RBI. Further, if such entities wish to continue such an activity, it shall be separated from the marketplace business. The PA-PG Guidelines further provide that the settlement of funds with merchants shall not be co-mingled with any other business, if any, handled by the PA.<sup>9</sup>

It is also pertinent to highlight that the Strategy Paper, made a reference to “*entities providing payment platforms or digital wallets or even mobile services*” and states as under:

*“2.4.3 Unbundling **will** also open up opportunities for innovation and the advent of new players in the areas of logistics, warehousing, etc. Further, it **will** also encourage players who are were hitherto providing certain specialized services to buyers and sellers (for example entities offering accounting software solutions to manufacturers and traders or entities providing payment platforms or digital wallets or even mobile services) to extend digital commerce interfaces to sellers or buyers, taking advantage of their existing strength without worrying about establishing complete and integrated digital commerce platforms.”*

*(Emphasis Supplied)*

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<sup>8</sup> RBI/DPSS/2019-20/174.

DPSS.CO.PD.No. 1810/02.14.008/2019-20.

<sup>9</sup> Clause 8.12 of the Guidelines on Regulation of Payment Aggregators and Payment Gateways dated March 17, 2020.

The Strategy Paper, under the aforesaid Clause 2.4.3, while making a reference to “*entities providing payment platforms or digital wallets*”, only laid down the prospective action/outcome of the ONDC and the consequential “*unbundling*” that is sought to be achieved through the ONDC. The same is evident from the language used in the aforementioned Clause, wherein the reference being made is that of what “*unbundling*” would lead to.

While the Strategy Paper stated the above, in Clause 3.2.1 of the Strategy Paper, it is clearly stated that the NPs within the ONDC could be broadly categorized into Buyer Side Application and Seller Side Applications, as described hereinabove.

Further, the Strategy Paper made a short reference to “*entities providing payment platforms or digital wallets or even mobile services*”<sup>10</sup> on the aspect of what “*unbundling*” would lead to and categorized and defined “*Buyer Applications*” and “*Seller Applications*”. The Consultation Paper laid down a more specified process with respect to the flow of transactions on the ONDC and clearly listed down and further defined and sub-divided the NPs within the ONDC, which specificity was not contained in the Strategy Paper. The Consultation Paper also made no reference of digital wallets such as payment aggregators being an NP on the ONDC, which reference was earlier made in the Strategy Paper.

It is pertinent to state here that the Consultation Paper categorically stated that Buyer Nodes and MSNs fall within the definition of “*Marketplace E-Commerce Entities*” as defined under the “*Consumer Protection E-Commerce Rules, 2020*” issued by the Ministry of Consumer Affairs, Food and Public Distribution on July 23, 2020 (“**E-commerce Rules**”). Further, ISNs fall within the definition of “*Inventory E-Commerce Entities*” as defined under the E-commerce Rules and Gateways fall within the general definition of “*e-commerce entities*” under the E-commerce Rules. The Consultation Paper also laid down the framework and the transactional flow under the ONDC, including the broad heads of the ONDC Network Policy<sup>11</sup> and the Transaction Level Contract<sup>12</sup> between the Buyer-Apps and the Seller-Apps.

In view of the definitions laid down in the Consultation Paper, it is pertinent to consider the definition of a “*marketplace e-commerce entity*” as defined under the E-commerce Rules. A “*marketplace e-commerce entity*”<sup>13</sup> is an e-commerce entity providing an information technology platform on a digital or electronic network to facilitate transactions between buyers and sellers.

A conjoined reading of the definitions laid down in the Consultation Paper, would clearly establish that an entity seeking to be either a Buyer Node and/or an MSN or both on the ONDC Platform, would be deemed to be an “*e-commerce entity*”.

Thereafter, upon the release of the Consultation Paper and the response received from the public at large, the ONDC has now released the ONDC Network Policy, which removed the specific reference of the Buyers Apps and Seller Apps being an “*e-commerce entity*” under the E-commerce Rules and limited the definition of the same.

While the ONDC Network Policy removed the specificity of NP-ISNs and NP-MSNs being e-commerce entities under the E-commerce Rules, a closer look at the definition of NP-ISNs and NP-MSNs, would clearly establish that despite the removal of the reference of the E-commerce Rules, an NP-ISN and NP-MSN would continue to be considered as an entity

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<sup>10</sup> Clause 2.4.3 of the Strategy Paper released on January 25, 2022.

<sup>11</sup> Appendix A of the Consultation Paper dated September 29, 2022.

<sup>12</sup> Appendix B of the Consultation Paper dated September 29, 2022.

<sup>13</sup> Section 3 (1) (g) of the “*Consumer Protection E-Commerce Rules, 2020*” issued by the Ministry of Consumer Affairs, Food and Public Distribution on July 23, 2020.

undertaking e-commerce activity since an NP-ISN is the “seller on record” on the ONDC network and NP-MSNs in the ONDC network Policy, represent themselves and acts as the marketplace with respect to the goods and services offered by third party merchants/service. Whether Seller Side Applications/Seller Apps, not being NP-ISNs and/or NP-MSNs, would be considered as e-commerce marketplaces under the E-commerce Rules, would be determined by the function discharged by such Seller Side Applications/Seller Apps since the definition of Seller Side Applications/Seller Apps includes platforms and applications which allow sellers to publish their product/service inventory and other information such as pricing, etc. to transact on the ONDC network.

Under the ONDC Network Policy, Buyer Side Apps, however, may not be considered as e-commerce entities under the E-commerce Rules since there is no reference of the same being marketplaces of any kind. The above is further strengthened by Clause 2.3.4 of the ONDC Network Policy, which makes a special reference to Buyer Side Applications being marketplace entities and the specific obligations to be complied with by such Buyer Side Apps, while there are no such specific obligations to be complied with by Seller Side Apps.

As already stated hereinabove, the PA-PG Guidelines mandate the separation of the PA business of an entity with the e-commerce marketplace business, if any, of such an entity. Further, the PA-PG Guidelines also clearly state that there can be no co-mingling of the funds of the PA with any other business carried out by the PA entity.

## **MARKET TREND**

It is in view of the above, e-commerce entities, such as Paytm E-commerce Private Limited, the parent of Paytm Mall, has gone live on the ONDC Platform beta testing currently being undertaken in Bengaluru, Karnataka.

There are banks such as HDFC Bank, Kotak Mahindra Bank and IDFC Bank that have also onboarded themselves on the ONDC. Under Section 6 of the Banking Regulation Act, 1949, as amended by The National Bank for Financing Infrastructure and Development Act, 2021 (17 of 2021) (w.e.f.19-4-2021), banks are not permitted to undertake e-commerce activities and are only permitted to undertake ancillary banking activities. It is for this reason that banks such as Kotak Mahindra Bank’s “*KayMall*” App only reflects the different products sold by Amazon, Flipkart, Big Basket, etc. and provides hyperlinks to the merchant apps onboarded on *KayMall*, with the merchants providing cashbacks and/or other benefits to the customers if they used Kotak Mahindra Bank’s credit cards/debt cards to undertake the transactions, while Kotak Mahindra Bank earning no commission/fees on the same. Similarly, HDFC Bank, while displaying products on its “*SmartBuy*” App, has merely provided a platform to its already existing customers to view different products on the platform, while giving clear disclaimers that HDFC Bank shall not be earning any commission, fees, etc. qua the transaction and has also no liability with respect to the products displayed on the platform and/or any alleged grievance qua the same, which liability vests only with the seller of the product. Banks such as IDFC Bank, has partnered with an app registered on ONDC and is onboarding small merchants onto ONDC through the said app. YES Bank has also partnered with ‘SellerApp’ to integrate itself onto ONDC.

Thus, in view of the ONDC Network Policy read with the PA-PG Guidelines and in the absence of any specific guidelines/policy, etc. to the contrary as on date, it can be concluded that an NP-ISN and an NP-MSN on the ONDC network, would be considered as marketplaces undertaking e-commerce activities and thus, in terms of the PA-PG Guidelines, a PA cannot be onboarded as an NP-ISN and/or an NP-MSN on the ONDC network. In case the Seller Side Applications/Seller Apps, not being NP-ISN and NP-MSNs, merely provides a platform to sellers to merely publish their product inventory and other relevant information, the same

may not be deemed to be an e-commerce activity and a PA can thus, undertake such activity. A PA, may also onboard itself on the ONDC network as a Buyer Side Application, so long as there is no e-commerce is being undertaken through such Buyer Side Application and the PA is merely providing a platform. It is however to be borne in mind that in case a PA is onboarding itself on the ONDC network, the funds received from its ONDC activity, is not co-mingled with the funds received by the PA from its primary PA activity.

The ONDC network is still in its nascent stage, with the same only being beta tested in various markets. Thus, with the wide usage of the network with time, its governance policies may also evolve alongwith it. The ONDC Network, seems to be fulfilling of democratizing e-commerce space and breaking the monopoly held by giants such as Flipkart, Amazon, etc.

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