

# How Amazon Exploits and Undermines Small Businesses, and Why Breaking It Up Would Revive American Entrepreneurship

By Stacy Mitchell and Ron Knox, June 2021

Most Americans believe that Amazon's outsized power is dangerous and must be reined in. A recent poll found that nearly 80 percent of voters believe Amazon should be subject to greater regulation, and more than half support breaking it up.<sup>1</sup>

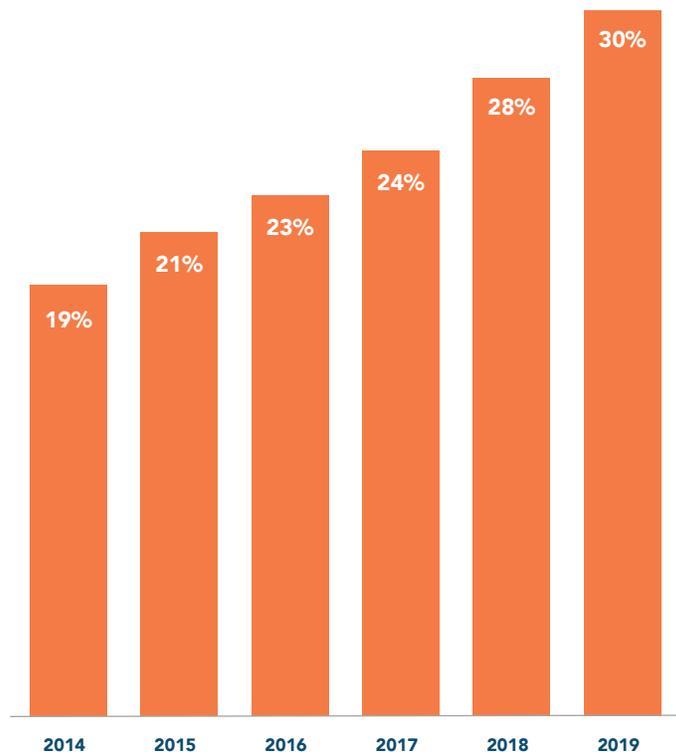
A growing number of lawmakers are moving to do just that.<sup>2</sup> A 15-month investigation by the House Judiciary Committee concluded that Amazon "has monopoly power over many small- and medium-sized businesses."<sup>3</sup> It called for breaking up the company by separating its major business lines into stand-alone firms and regulating its online marketplace to ensure that sellers are treated fairly. Both Democrats and Republicans have voiced support for these measures.<sup>4</sup>

As lawmakers have grown increasingly serious about addressing Amazon's harms, Amazon has sought to portray itself as beneficial to independent small businesses.<sup>5</sup> In splashy campaigns, press releases, and lobbying at the Capitol, Amazon contends that it has "a mutually beneficial relationship" with the small businesses that depend on its platform, that these businesses are "thriving," and that "our interests are well aligned."<sup>6</sup>

Small business owners themselves tell a very different story. In a 2019 survey, three-quarters of independent retailers ranked Amazon's dominance as a major threat to their survival, and only 11 percent of those selling on its site described their experience as successful.<sup>7</sup> It's not only retailers; small consumer product manufacturers, book publishers, and other creators are also imperiled. All of

## Amazon's Cut of Sellers' Revenue

For every \$100 sellers earn in sales, Amazon is keeping \$30 in fees, up from \$19 five years ago.



Notes: Amazon's financials break out revenue from third-party seller fees, but do not include seller payments for product advertising. ILSR has estimated those fees and included them here. The estimates are based on data from eMarketer and information from Amazon's financials. Sources: Amazon's 10-K filings; eMarketer.

these small businesses are trapped in Amazon's monopoly gambit: the tech giant controls access to the online market, which leaves them little choice but to sell on its platform. Yet doing so allows Amazon, also their competitor, to exploit and undermine them.

As Amazon has grown, the number of independent businesses has fallen. Between 2007 and 2017, the number of small retailers fell by 65,000.<sup>8</sup> About 40 percent of the nation's small apparel, toy, and sporting goods makers disappeared, along with about one-third of small book publishers.<sup>9</sup> (Small is defined here as under 500 employees.)

This factsheet details the specific ways in which Amazon abuses its market dominance to hurt smaller competitors.

→ **Amazon has cornered the online market, impeding the ability of small businesses to operate independently and blocking them from having direct relationships with their customers.**

A majority of shoppers looking to buy something online begin their search on Amazon, and its site captures about 50 percent of online spending in the U.S.<sup>10</sup> This dominance allows Amazon to function as a gatekeeper: retailers and brands must sell on its site to reach much of the online market. This dependence is risky and leaves many businesses living in fear. Changes to Amazon's search algorithms or selling terms can cause their sales to evaporate overnight. Amazon also makes it hard for sellers to reduce their dependence on its platform, in part by making their brand identity almost invisible to shoppers and preventing them from building relationships with their customers. Amazon strictly limits contact between sellers and customers.<sup>11</sup> In April 2021, it implemented a new policy that blocks most sellers from even seeing the names and addresses of the people buying their products.<sup>12</sup>

**"If the customer is on Amazon, as a small business you have to say, 'That is where I have to go.' Otherwise, we are going to close our doors."**

– CHRIS LAMPEN-CROWELL, OWNER OF  
GAZELLE SPORTS IN GRAND RAPIDS, MICHIGAN<sup>13</sup>



**"When you are small, someone else that is bigger can always come along and take away what you have."**

– JEFF BEZOS, FOUNDER AND CEO OF AMAZON<sup>14</sup>

→ **Amazon steals independent businesses' best ideas and innovations.**

While Amazon touts sellers as "partners" in public, within the company, it refers to them as "internal competitors."<sup>15</sup> Both the House investigation and reporting by the *Wall Street Journal* have found that Amazon has spied on sellers and appropriated data about their sales, costs, and suppliers. It's then used this information to create its own competing versions of their products, often giving its versions superior placement in the search results.<sup>16</sup> Amazon has also been caught using its venture capital fund to invest in startups, only to steal those startups' ideas and create rival products and services. In some cases, "Amazon's decision to launch a competing product devastated the business in which it invested."<sup>17</sup>

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**“It’s not a comfortable feeling knowing that [Amazon has] people internally specifically looking at us to compete with us.”**

– TRAVIS KILLIAN, CEO OF UPPER ECHELON, A HOME GOODS MANUFACTURER IN AUSTIN, TEXAS, THAT SELLS ON AMAZON’S SITE<sup>18</sup>

→ **Amazon compels sellers to buy its warehousing and shipping services, even though many would get a better deal from other delivery providers.**

Amazon has made a seller’s ability to generate sales on its site largely contingent on purchasing its warehousing and shipping services (“Fulfillment By Amazon” or FBA). Sellers who subscribe to FBA are favored by Amazon in two ways: they’re allowed to add the Prime badge to their products and they’re significantly more likely to be chosen by the site’s algorithm as the default seller of a product (known as “winning the buy box”).<sup>19</sup> Both are crucial to generating sales. By making FBA all but mandatory, Amazon has built a massive logistics business on the backs of independent businesses who would, in many cases, prefer to use another carrier. “I’d recommend Amazon if they were really good on price, but they’re not. If it weren’t for the algorithm... FBA wouldn’t be attractive,” according to Matthew White, a logistics consultant for e-commerce companies.<sup>20</sup>

**If you “actually add up all the ways Amazon nickels and dimes you... you can’t make money.”**

– DOUG MRDEZA, FOUNDER OF TOP SHELF BRANDS, AN E-COMMERCE SELLER IN MICHIGAN<sup>21</sup>

→ **Amazon imposes high fees on sellers, putting them at risk of going under.**

Through the fees it charges sellers, Amazon keeps an average of 30 percent of each sale independent businesses make on its site, up from 19 percent in 2014.<sup>22</sup> Amazon has extracted more from sellers in part by making it harder for them to generate sales unless they purchase additional Amazon services, including shipping and advertising. Amazon’s revenue from seller fees soared to \$60 billion in 2019 and has grown so large that “sellers are effectively cross-subsidizing Amazon’s retail division.”<sup>23</sup> These high fees make it nearly impossible to sustain a profitable business. Because of the rising cost of these monopoly tolls, “the vast majority of those who start selling on Amazon’s site fail within a few years.”<sup>24</sup>

→ **Amazon blocks independent businesses from offering lower prices on other sites.**

Under scrutiny from members of Congress, Amazon in 2019 eliminated clauses in its contracts that barred third-party sellers from offering their goods for less on rival shopping sites.<sup>25</sup> But Amazon continues to indirectly enforce this rule through its “Fair Pricing Policy.”<sup>26</sup> If Amazon’s pricing bots detect that a seller is offering a lower price elsewhere, Amazon suppresses the seller’s sales by demoting the item in search results, so that customers are unlikely to see it, or making the seller ineligible to win the buy box.<sup>27</sup> These actions invariably cause sales to crater. As a result, even though it may cost less to sell on competing sites, sellers can’t lower their prices below Amazon’s, on any platform. This insulates Amazon from competition and preserves its dominance.

→ **Amazon shuts down small businesses without due process.**

Despite small businesses’ reliance on Amazon’s platform to reach customers, Amazon routinely suspends sellers’ accounts and seizes their inventory and cash balances.<sup>28</sup> These actions are often abrupt and arbitrary, and can be catastrophic, costing sellers enormous sums in lost merchandise and receivables. Sellers have little recourse. It can take weeks or months for Amazon to respond to complaints of mistaken or inappropriate suspensions.<sup>29</sup> Sellers who attempt to recover their losses or get their accounts reinstated must go through an arbitration process;



Credit: Marie Donahue

Amazon's standard contract bars them from pursuing legal action. As the House Judiciary Committee's investigation found, "the [arbitration] process is unfair and unlikely to result in a meaningful remedy."<sup>30</sup> Evidence collected during the investigation showed that "Amazon's poor treatment of sellers is far from an isolated incident."<sup>31</sup>

**"I paid that bribe [to Amazon] and the books reappeared."**

– DENNIS JOHNSON, CO-OWNER OF MELVILLE HOUSE,  
A BOOK PUBLISHER IN BROOKLYN, N.Y.<sup>32</sup>

→ **Amazon sells goods and services below cost to harm rivals and take market share.**

Amazon has consistently engaged in predatory pricing – selling products and services below cost to kill off competitors and expand its market share.<sup>33</sup> During its first six years, Amazon lost billions of dollars selling books below cost, a strategy that drove many bookstores out of business.<sup>34</sup> Amazon has also used predatory pricing to eliminate e-commerce rivals. It reportedly lost \$150 million selling shoes below cost in a successful bid to compel Zappos to agree to a merger.<sup>35</sup> Similarly, it clocked hundreds of millions of dollars in losses selling diapers below cost to destabilize Diapers.com and force it into a merger.<sup>36</sup> Amazon has also incurred strategic losses to keep customers locked into Prime and thus wed to its shopping platform. It has lost as much as \$700 million a year on Prime Video, for example.<sup>37</sup> Amazon initially financed its predatory pricing schemes through a tacit agreement with investors, who accepted little or no profit in exchange for rapid market share growth.<sup>38</sup> More recently, it's been able to

cross-subsidize losses by tapping into the high profits of its cloud division, Amazon Web Services. In 2020, 59 percent of Amazon's operating income came from AWS.<sup>39</sup>

→ **Amazon strong-arms small brands, destabilizing their businesses and making it harder for them to grow and develop new products.**

As Amazon muscled competing retailers out of the market, small manufacturers are left with fewer channels through which to market and sell their products. This gives Amazon even more leverage to extract price concessions and special terms from them. Those who do not comply can face ruinous retaliation. When the book publisher Melville House declined Amazon's demand for steeper discounts, for example, Amazon removed the buy button from all of its titles, causing a devastating drop in sales.<sup>40</sup> Similarly, the phone accessory-maker PopSockets reported having to buy nearly \$2 million in advertising from Amazon before the tech giant would rid its platform of counterfeit versions of PopSockets' products.<sup>41</sup> As Amazon fleeces producers, these companies are left with less revenue to invest in developing new products and growing their businesses. "If you can't make any money, it takes away invention and innovation," an executive at a sporting goods company explained.<sup>42</sup>

**"There's a whole class of businesses out there who live in fear of going out of business as a result of the fiat of Amazon and their algorithms."**

– AN ANONYMOUS THIRD-PARTY SELLER IN AN  
INTERVIEW WITH THE SEATTLE TIMES<sup>43</sup>

## Congress Needs to Break Up Amazon Along Business Lines and Set Standards of Fair Dealing for Its Marketplace

Congress shouldn't let Amazon dictate whether and how small businesses can compete online. If policymakers do not act to check Amazon's outsized power, they're effectively allowing Amazon to be a private regulator of the online market, deciding which businesses may reach customers and the price they must pay to do so.

### To restore an open, competitive online market, policymakers must:

#### 1. Break up Amazon along its major lines of business.

Amazon derives much of its power to bully and exploit independent businesses from its integration across business lines and the fact that it plays multiple roles in markets. This allows it to leverage its dominance in one area to gain an advantage in others: It uses its power as an online marketplace to grow its logistics business, force concessions from suppliers to its retail division, and appropriate seller data to inform development of its own products. "Market participants that depend on Amazon's retail platform are effectively forced to accept its demands – even in markets where Amazon would otherwise lack the power to set the terms of commerce," the House Judiciary Committee's investigation concluded.<sup>44</sup> In its report, the committee called for breaking up the dominant tech firms along business lines. By separating Amazon's third-party marketplace from its retail division, and spinning off its cloud services and other major divisions into stand-alone companies, policymakers could remove the incentive and ability for Amazon to exploit its gatekeeper status to favor its own interests and harm competition.

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#### 2. Require dominant digital platforms to deal fairly with the independent businesses that rely on them.

Breaking up Amazon and separating its major divisions into new companies is essential to removing the underlying conflicts of interest and incentives to self-deal that drive its anti-competitive and abusive behavior. But even as stand-alone companies, dominant digital platforms, such as Amazon's retail marketplace, will still serve as critical infrastructure for other businesses, much like railroad and telephone lines. As such, these platforms should be regulated in a similar fashion. Congress should enact legislation requiring them to treat all sellers fairly and on equal terms. Congress should also nullify contract provisions that force sellers to accept mandatory arbitration or other coercive terms for adjudicating disputes.

#### 3. Block Amazon from engaging in abusive tactics by making our antitrust laws stronger and easier to enforce.

In the 1980s, federal antitrust enforcement agencies and the courts began to radically reinterpret our antitrust laws. Judges set aside the concerns about outsized power that had led Congress to pass these laws in the first place and instead oriented antitrust enforcement around the goal of maximizing efficiency. Under this framework, the courts began to look favorably on consolidation and, through a series of misguided rulings, made many antitrust violations very difficult to prove. This fundamental shift allowed Amazon to amass market power by engaging in anti-competitive tactics, such as predatory pricing, that would have been blocked in an earlier period. Congress should restore the antitrust laws to their original strength and purpose by enacting legislation that clarifies the intent of these laws and sets clear, bright-line rules that prohibit anti-competitive behavior and don't allow judges to rewrite the law. Doing so will make antitrust enforcement simpler, less expensive, and more effective. ■

## Notes

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