SPOTIFY'S RESPONSE TO THE CMA'S DIGITAL MARKETS TASKFORCE

CALL FOR INFORMATION

A. INTRODUCTION

Spotify AB ("**Spotify**") welcomes the opportunity to respond to the Digital Markets Taskforce's ("**DMT**") Call for Information on the proposed pro-competition approach. The views expressed in this paper are consistent with Spotify's views in response to the European Commission's two consultations on the Digital Services Act and the New Competition Tool, in which Spotify is also participating.[1]

Key characteristics of the digital economy, such as network effects, intense economies of scale and scope and the significant role of data, create an increasing need for swift enforcement of competition law combined with effective remedies. Traditional *ex post* competition enforcement has, thus far, proven versatile in capturing new theories of harm in digital markets. Nevertheless, as digital markets evolve at internet speed, traditional enforcement mechanisms can often come too late to remedy serious harm to competition and consumers. Spotify, therefore, agrees that the need arises to consider how the UK competition law toolkit will best evolve to fit the digital economy now and in the future. Spotify believes that any amendments to UK competition law, such as the pro-competition approach, should prioritise the principles of speed of enforcement and effectiveness of remedies. The pro-competition approach could also incorporate the recurring themes that have been emerging in UK and EU competition law enforcement in the past several decades (*i.e.*, types of behaviour that, when conducted by companies with market power, are almost certain to cause anti-competitive harm, such as self-preferencing or leveraging market power into adjacent markets through means that do not constitute competition on the merits). These themes have been emerging repeatedly, with slight variations and in different markets from the Microsoft cases of the early 2000s through to the recent cases against Google.

1 *See* https://ec.europa.eu/commission/presscorner/detail/en/IP_20_977

Spotify believes that ex ante regulation such as the pro-competition approach should be limited to "gatekeeper platforms" (a concept that Spotify perceives as being adjacent to that of platforms with Strategic Market Status ("**SMS**")). These gatekeeper platforms hold a unique position in the marketplace and have a unique ability to control and thwart innovation and competition to the detriment of consumers. Applying the pro-competitive approach to gatekeeper platforms would avoid a regime the scope of which would be overinclusive and which, therefore, unnecessarily impedes innovation by smaller entrants, while addressing the harm generated by a small subset of platforms.

In Spotify's experience, app stores are a prominent example of platforms that can exhibit all the characteristics of a gatekeeper. For the past few years, Spotify has been raising awareness of antitrust risk from the conduct of app store owners, including submitting a complaint before the European Commission ("**EC**") against Apple for app store restrictions that violate EU competition law, which the EC is now formally investigating.[2] In the interest of providing additional context to the DMT, **Section B** provides an overview of the key competitive dynamics in app store markets and examples of how app store owners can (and do) abuse their position. **Section C** provides answers to the DMT's Call for Information.

B. APP STORE MARKETS

Competitive dynamics in app store markets

The smartphone is the most ubiquitous digital device amongst UK adults and is expected to remain so for many years. In fact, the smartphone is likely to consolidate its primacy over the coming years, and become even more vital.[3] Consumers worldwide increasingly use their smartphones to access services and content, and these interactions are overwhelmingly conducted through the use of mobile applications ("**apps**").

App stores are critical for users and developers

To download, update and (sometimes) discover apps for the two major mobile Operating Systems ("**OS**"), Android and iOS, consumers depend on the app stores present on each OS,

2 See Spotify's dedicated microsite, *available at:* https://www.timetoplayfair.com/

3 Deloitte report "*Global Mobile Consumer Survey: UK cut | Plateauing at the peak | The state of the smartphone*", *available at:* https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/technology-media-telecommunications/deloitte-uk-plateauing-at-the-peak-the-state-of-the-smartphone.pdf

i.e., Google's Google Play store ("**Google Play**") and other app stores for Android as well as Apple's App Store (the "**App Store**"), the only app store Apple allows to operate on iOS. Google Play and the App Store distribute apps developed by the app store / platform owner (Google and Apple, respectively) alongside third-party apps. Thus, Google and Apple are simultaneously owners of the mobile OS, operators of the main (or in Apple's case the only) app store on that OS, and suppliers of apps in competition with third parties.

For commercial users/developers, there are no viable alternatives to app stores for reaching customers on Android and iOS.[4] Inviting third-party apps onto an app store is a mutually beneficial arrangement for developers and the platform owner: developers benefit from being able to distribute services to mobile users, and the app store owner benefits from the presence of third-party apps (particularly ones with considerable brand recognition) which make the platform more attractive to users.

To reach the broadest possible audience, app developers must be present on both Google Play and the App Store (*i.e.*, they must multi-home). This is because mobile users tend to single-home *i.e.*, typically use only one mobile ecosystem at a time (Android or iOS) due primarily to high switching costs and brand loyalty.[5] In *Google Android*, the EC found Google Play to be dominant in a distinct relevant market for Android app stores, which is not constrained by Apple's App Store.[6] There are good arguments to support the App Store as being also dominant in a separate relevant market for app distribution on iOS.

App stores have considerable bargaining power over developers

Given their critical nature for app distribution, app stores have considerable bargaining power over developers. This bargaining power is most evident in the app approval process. To be eligible to distribute apps on app stores, developers must agree to the app store owner's

4 Browser-based apps are not generally viewed as a sufficient substitute for mobile apps as key functionality that mobile apps offer cannot be replicated on a browser-based app (*e.g.*, offline functionality).

5 In *Google Android*, the EC cites research estimating that, in 2015, 82% of Google Android smartphone users purchasing a new smartphone decided to purchase a Google Android device. The equivalent figure for iOS users was 78%. *See* EC decision in Case AT.40099 – *Google/Android,* paragraphs 500 and 533 *et seq* ("***Google Android***").

6 *Google/Android,* paragraphs 268 and 306.

standard, non-negotiable contract terms, including app approval protocols.[7] Both the App Store and Google Play have app review protocols in place whereby they approve or reject third-party apps for inclusion in the app store. Every update to third-party apps (*e.g.*, bug fixes or service improvements) also needs to be approved by the app store owner.

App store owners have broad discretion in designing their app approval processes. For instance, Apple artificially distinguishes between different types of apps in its app approvals process, imposing heavy obligations on apps providing digital content that do not apply to apps supplying physical products or services. More specifically, digital content apps are required exclusively to use Apple's in-app payment mechanism, In-App Purchase ("**IAP**") for all in-app sales to users, at the exclusion of other payment mechanisms, and to pay Apple a 30% fee on every in-app transaction.[8] Apple has thus far not offered a convincing objective justification for this difference in treatment. As a digital content app, Spotify has experienced these restrictions first hand and these are at the heart of the EC's recently launched investigation against Apple.[9]

App stores are in a position not only to *set* app approval terms unilaterally, but also to give themselves the discretion unilaterally to *amend* app approval rules (or their *interpretation*), leaving developers no option but to adapt their own commercial conduct, even when materially disadvantageous to them. For instance, Apple deems its App Store Review Guidelines ("**Guidelines**") a "*living document*", further intensifying the ambiguity faced by third-party developers as to whether their app will reach users through the App Store, and if so in what shape. Apple states explicitly that the Guidelines are subject to change without notice at Apple's sole discretion (*see* rule 3.2 which states that "*the lists below are not exhaustive, and your submission may trigger a change or update to our policies*").

Spotify's experience illustrates this: since 2011, Apple has developed a pattern of moving the goalposts of developers' compliance with its Guidelines: (i) by amending the Guidelines to tighten restrictions on developers' ability to advertise to users on iOS; and (ii) by enforcing the Guidelines in a capricious and inconsistent manner, depriving developers of certainty on

7 For Apple, these are the terms included in the Developer Program License Agreement and the App Store Review Guidelines *available at:* https://developer.apple.com/app-store/review/guidelines/ For Google, these are the Google Developer Programme Policies, and the Google Play Developer Distribution Agreement.

8 The 30% fee becomes 15% in the second consecutive year of a subscription.

9 EC Case AT.40437 – *Apple – App Store Practices (music streaming)* launched formally on 16 June 2020.

whether their app / app updates will be approved. This is often done despite explicit assurances or previous practice to the opposite effect. Given the focus on digital content apps, it is no wonder that Apple's conduct has disproportionately affected apps that compete with Apple's own apps on the App Store.

Sources of antitrust risk in app stores

In Spotify's experience, under specific circumstances, app stores can become a vehicle for anti-competitive conduct. Vertically integrated platforms with native app stores, which also sell downstream apps, have the ability and often the incentive to self-favour: they are in a position to abuse the privilege of being both referee and player to give their own apps an unmerited competitive advantage.

App store owners are able to restrict the operation of competing third-party apps by imposing on them exploitative or exclusionary conditions for accessing the app store to which the app store owner's own apps are not subjected, such as:

a. **Making access to the app store conditional on the acceptance by third-party developers of supplementary obligations unrelated to the app distribution contract.** Such unrelated supplementary obligation can include requiring developers exclusively to use the app store owner's in-app payment mechanism to make in-app sales (and pay a fee per in-app transaction), as Apple does with IAP on the App Store. This is often accompanied by prohibiting developers from informing users through the app of alternative (often cheaper) purchasing options for the same service.

b. **Artificially raising third-party apps developers' costs of doing business.** A significant proportion of developers seek to sell services via their app. The effectiveness of the in-app channel in driving customer conversions is easy to appreciate: the user is being presented with in-app advertising and the ability to purchase while engaged with the developer's service, and is thus more receptive to the advertising message. In-app conversion tools provide users with an excellent means to convert to a developer's paid service while they are focused on the service and their intent and desire to convert are highest. Restrictions on a developer's ability to sell in-app (such as the one described above under (a)) often render it commercially unviable for the developer to continue making such sales. These therefore deprive developers of a critical conversion channel and force them to increase spending towards more expensive and less effective

marketing methods (*e.g.*, social media advertising). As such, third-party developers are weakened in their ability to compete with the app store owner's own apps.

c. **Restrictions on developers' freedom to communicate with their users.** App store owners are able to put limits on developers' freedom to communicate with their users via the app. Examples from Spotify's experience include restrictions imposed by Apple on Spotify using its iOS app to inform users of in-app discounts and promotions; out-of-app purchasing options for the same service; and bundles of services (often at an attractive price for the user).

d. **Intervening in the relationship between the developer and its users.** Platform owners are intermediaries between the developer and its users / customers and is in a position to potentially abuse that privilege. For instance, when a user purchases digital content (*e.g.*, a Spotify subscription) using Apple's IAP[10], Apple becomes the merchant of record for the transaction instead of the app developer. Thus, the developer is forced to relinquish control of communications with its own customers concerning the subscription / billing to Apple. In addition, this allows Apple to obtain data and sensitive insights into aspects of the developer's business, performance and customers, which in the case of competing apps can give competitively sensitive insights to Apple. This creates an artificial opacity in the consumer relationship for the developer. For instance, at the time, Spotify was unaware of the status of communications around billing and had little information about the reasons for, *e.g.*, cancelled subscriptions. This limited Spotify's ability to adopt pro-competitive initiatives to win over customers. For example, if a customer failed to pay his subscription fee on time, the user's subscription was terminated, with Spotify being prevented from offering any flexibility by either waiving the fee or allowing the customer to pay later.

Effects of this behaviour on developers and consumers

Anti-competitive behaviour by an app store owner can negatively affect consumers and third-party developers by:

10 This was the case, for instance, for Spotify while it had enabled in-app purchases of Spotify Premium subscriptions on the App Store between May/June 2014 and May/June 2016 through Apple's IAP.

a. **Reducing consumer choice** as third-party developers who compete with the app store owner's own apps are excluded or weakened in their ability to compete.
b. **Increasing prices for consumers** as it can leave developers with no viable choice but to pass on the restrictions imposed by app store owners (*e.g.*, discriminatory commission fees) to consumers in the form of higher prices.
c. **Reducing incentives and ability to innovate and the overall level of innovation on the market** due to third-party developers' financial losses and loss of scale.

Left unchecked, such anti-competitive behaviour risks being cemented into industry practice with app store owners engaging in a 'race to the bottom', with detrimental effects for consumers, businesses and future foreign investment in digital technologies in the UK market.

C. SPOTIFY'S RESPONSE TO THE DMT'S CALL FOR INFORMATION

Scope of a new approach

1. What are the appropriate criteria to use when assessing whether a firm has Strategic Market Status (SMS) and why? In particular:

• The Furman Review refers to 'significant market power,' 'strategic bottleneck', 'gateway', 'relative market power' and 'economic dependence':

– How should these terms be interpreted?

– How do they relate to each other?

– What role, if any, should each concept play in the SMS criteria?

• Which, if any, existing or proposed legal and regulatory regimes, such as the significant market power regime in telecoms, could be used as a starting point for these criteria?

• What evidence could be used when assessing whether the criteria have been met?

A platform with SMS / "gatekeeper platform" could potentially be defined as a platform:

a. Whose core market is protected by high barriers to entry (*e.g.*, large economies of scale, and strong direct and indirect network effects); and

b. Which holds the only access to critical online services for a large population of consumers, who single-home (*i.e.*, who use only one platform, not multiple), hence allowing it to act without constraint when it sets the rules to have access to its platform. Platforms which operate as "gateways", "bottlenecks" or benefit from others' "economic dependency" would be caught under this criterion; and
c. Which is able to leverage unique assets (*e.g.*, large volumes of data, large customer base, unique technological assets &c.) into adjacent markets and exclude rivals in those markets.

To avoid an overinclusive definition, the criteria listed above should be **cumulative**.

In sum, it would be preferable for the pro-competitive approach regime to apply to a small subset of platforms that engage in behaviours that, because of their unique position of strength, pose a significant threat to competition and innovation, and that require swift remedies to prevent such harm before it occurs. It is also important to preserve the consumer benefits that innovation by gatekeeper platforms can bring when they choose to invest and compete. Thus, the pro-competition approach should not prohibit competition amongst gatekeepers or between gatekeepers and the app developers that rely on their platforms, but rather ensure that competition occurs on a level playing field. Innovation can come from both large and small companies. The pro-competition approach regulation must preserve the ability of the large companies to compete and innovate, while ensuring that smaller innovators are not foreclosed.

2. What implications should follow when a firm is designated as having SMS? For example:

• Should an SMS designation enable remedies beyond a code of conduct to be deployed?

• Should SMS status apply to the corporate group as a whole?

• Should the implications of SMS status be confined to a subset of a firm's activities (in line with the market study's recommendation regarding core and adjacent markets)?

In Spotify's view, designation of a firm as having SMS should be accompanied by a set of obligations (affirmative duties) and prohibitions to provide a degree of certainty to the marketplace and improve the speed and efficacy that competition law investigations sometimes fail to deliver.

This would not exclude the possible need for tailor-made remedies in certain cases, knowing that this approach should be framed in such a way that it does not run into the problems of lack of speed and efficacy that the pro-competition approach is intended, *inter alia*, to solve. As gatekeeper platforms regularly devise new ways of using their gatekeeper status to distort competition and thwart rivals, tailor-made might inevitably become necessary in some cases. When remedies are needed, they should be adopted swiftly, and measures should be taken to ensure that gatekeeper platforms implement them correctly.

As to the set of obligations and prohibitions to be imposed by regulation, the focus should be on the experience of competition and regulatory authorities over the past decades and the types of conduct they have found to be distortive and exclusionary when engaged in by large digital platforms.

There would be a number of behaviours that meet this test and that, if codified in legislation, would clearly define the bounds of acceptable behaviour for gatekeeper platforms and enable the CMA to act with sufficient speed to stop such conduct in an effective manner to preserve competition. Such behaviours would include duties to operate in a fair, reasonable and non-discriminatory manner towards all services on the gatekeeper's platform and respective user choice, and prohibitions against imposing unfair terms and conditions, engaging in self-preferencing behaviour, restricting commercial users' communications with their users, misusing data relating to third-party services, and inconsistently applying rules that govern commercial users' access to a platform.

The SMS standing could potentially apply to all entities belonging to a corporate group, but only in relation to activities belonging in a clearly identified relevant product and geographic market.

3. What should be the scope of a new pro-competition approach, in terms of the activities covered? In particular:

• What are the criteria that should define which activities fall within the remit of this regime?

• Views on the solution outlined by the Furman Review (paragraph 2.13) are welcome.

In Spotify's view, the pro-competition approach should capture at least the digital sector (and potentially be broader). Spotify, however, recognises the practical difficulties in trying to limit the scope of the pro-competition approach to markets "based upon digital platforms" (as para 2.13 of the Furman Review suggests). Attempting to define markets "based upon digital platforms" by reference, for instance, to certain economic characteristics such as network-based or data-driven business models might cause more legal uncertainty and confusion as few, if any, industries could arguably be described as not "based upon digital platforms" and this will certainly continue to be the case in the future as the economy becomes increasingly digitised.

4. What future developments in digital technology or markets are most relevant for the Taskforce's work? Can you provide evidence as to the possible implications of the COVID-19 pandemic for digital markets both in the short and long term?

The pro-competition approach has the potential to become a paradigm shifting change to UK competition law – it is therefore important to ensure it is future-proof. The economy's increasing dependency on the digital sector and digital platforms in particular is one of the most relevant factors to take into account when designing the pro-competition regime, which therefore needs to be sufficiently versatile and able to encompass new issues.

Another important development relevant to the DMT's work is the emergence of increasingly advanced consumer products and services linked to the Internet of Things ("**IoT**") (*e.g.*, wearable devices), which have at their core intelligent voice assistants. IoT applications have the potential to provide enormous value to consumers and businesses globally. It is therefore important to ensure a level competitive playing field for commercial users on IoT devices and services to allow the full benefits from this innovation to flow to consumers. The lessons learned in other markets (*e.g.*, regarding the risks of self-preferencing, discriminatory treatment by platform-owners, or abuse of data advantages) should be a helpful guide for ensuring the competitiveness of the IoT space.

The COVID-19 pandemic emphasised the dependency of commercial users and consumers on the digital sector (and app stores in particular) and the ease with which this dependency can be exploited. A pertinent example comes from Apple's behaviour:

Businesses offering services in the analogue world (*e.g.*, cooking classes) have, for a long time, allowed customers to make reservations through iOS apps and pay using the business's own

payment processing system. Apple had not previously required such apps to use IAP. Due to the COVIDd-19 crisis, many of them started using videoconferencing services to hold engagements digitally and restore a portion of their quickly declining revenue. Apple began to demand a 30% cut of the reservations, insisting that these must also be offered for purchase through IAP (under rule 3.1.3 of Apple's App Store Review Guidelines).

Apple's response to businesses on the verge of financial ruin was to again move the goalposts of compliance with the Guidelines and demand to be paid the IAP 'tax' for services offered outside the App Store or even outside the iOS platform. Apple's demand is also inconsistent with its own attempted justification as to why physical goods and services consumed outside of the iOS app were exempt from IAP. In its reply to Spotify's complaint, Apple had claimed that the exemption was due to it being unable to verify the delivery of physical goods and services to users. This, however, remained the case for the above services even after the switch to videoconferencing – they continued to be consumed outside the app and Apple was not in a position to validate fulfilment. Apple once again moved the App Store goalposts, this time to profit from the global pandemic.

Remedies for addressing harm

5. What are the anti-competitive effects that can arise from the exercise of market power by digital platforms, in particular those platforms not considered by the market study?

Please see the Introduction to this note, discussing the potential harmful effects arising from anti-competitive behaviour by app store owners.

6. In relation to the code of conduct:

• Would a code structure like that proposed by the market study incorporating high-level objectives, principles and supporting guidance work well across other digital markets?

• To what extent would the proposals for a code of conduct put forward by the market study, based on the objectives of 'Fair trading', 'Open choices' and 'Trust and transparency', be able to tackle these effects? How, if at all, would they need to differ and why?

Please see above response to Question 2.

7. Should there be heightened scrutiny of acquisitions by SMS firms through a separate merger control regime? What should be the jurisdictional and substantive components of such a regime?

Strategic acquisitions by vertically integrated digital giants in recent years (*e.g.*, Facebook's acquisitions of WhatsApp and Instagram, Apple's acquisition of Shazam, Google's acquisition of DoubleClick) have come into the spotlight again. Valid concerns have been expressed about the ability of merger control regimes globally to capture such deals effectively and consistently, and protect competition and consumers from their negative consequences, especially when nascent competitors are involved.

Spotify agrees with the principle that acquisitions by companies designated as having SMS should come under heightened scrutiny, including by amending the applicable jurisdictional thresholds, which are often too high to capture acquisitions of promising new entrants / killer acquisitions.

Potentially, greater emphasis would need to be placed on the effects of such mergers beyond actual competition – on potential competition (*e.g.*, are potential competitors eliminated?), dynamic competition and the level of innovation in the future – taking into account, in particular, effects arising from the combination of valuable acquired assets (*e.g.*, data or technology) with owned assets. Such substantive considerations could be incorporated in the revision of the CMA's Merger Assessment Guidelines that is currently in progress.

8. What remedies are required to address the sources of market power held by digital platforms?

• What are the most beneficial uses to which remedies involving data access and data interoperability could be put in digital markets? How do we ensure these remedies can effectively promote competition whilst respecting data protection and privacy rights?

• Should remedies such as structural intervention be available as part of a new pro-competition approach? Under what circumstances should they be considered?

Please see above response to Question 2.

In choosing the appropriate remedies, the most components are (i) speed of imposition and implementation and (ii) effectiveness *i.e.*, a true change in market behaviour. Spotify cannot exclude that structural remedies might, in some cases, be the fastest and most effective way to fix issues caused by companies abusing their SMS. However, the use of structural remedies should be carefully considered as they alter the competitive structure of the market on a lasting basis and, in most cases, cannot be reversed. They are also onerous for the parties involved, as any forced divestment is likely to be at distress prices. Such remedies should only be imposed only where proportionate *i.e.*, either where there is no equally effective behavioural remedy (*i.e.*, there is substantial risk of a lasting or repeated infringement that derives from the very structure of the company with SMS) or where any equally effective behavioural remedy would be more burdensome for the undertaking concerned than the structural remedy.

9. Are tools required to tackle competition problems which relate to a wider group of platforms, including those that have not been found to have SMS?

• Should a pro-competition regime enable pre-emptive action (for example where there is a risk of the market tipping)?

• What measures, if any, are needed to address information asymmetries and imbalances of power between businesses (such as third-party sellers on marketplaces and providers of apps) and platforms?

• What measures, if any, are needed to enable consumers to exert more control over use of their data?

• What role (if any) is there for open or common standards or interoperability to promote competition and innovation across digital markets? In which markets or types of markets? What form should these take?

Please see above response to Question 1.

<u>Procedure and structure of a new pro-competition approach</u>

10. Are the proposed key characteristics of speed, flexibility, clarity and legal certainty the right ones for a new approach to deliver effective outcomes?

Spotify agrees that seeking to modernise UK competition law through the lens of speed, flexibility, clarity and legal certainty is the correct approach. In Spotify's view, speed should take precedence amongst these characteristics, as the risk of irreparable harm to the digital economy is real and ever-present.

Please also see above Introduction and the response to Question 1.

11. What factors should the Taskforce consider when assessing the detailed design of the procedural framework – both for designating firms and for imposing a code of conduct and any other remedies – including timeframes and frequency of review, evidentiary thresholds, rights of appeal etc.?

The more serious the potentially negative implications of designating a firm as having SMS, the greater the need to establish appropriate procedural safeguards, such as defence rights and rights of appeal. Nevertheless, the fundamental tension between procedural fairness and timeliness of proceedings should not be ignored. Procedural safeguards introduced to guarantee rights of defence add time and are often abused by parties seeking to protract investigations and delay remedial action. The pro-competition approach should maintain the right balance between these two conflicting goals.

In addition, consistent with prioritising speed of competition law enforcement in the digital economy, the DMT could consider the strategic use of statutory time limits for the completion of key procedural steps in the pro-competition approach, similar to the time limits applicable in the UK market investigations regime as well as strict time frames for parties' co-operation with the CMA's investigative tools (*e.g.*, providing responses to information requests).

12. What are the key areas of interaction between any new pro-competitive approach and existing and proposed regulatory regimes (such as online harms, data protection and privacy); and how can we best ensure complementarity (both at the initial design and implementation stage, and in the longer term)?

The pro-competitive approach will not exist in a policy vacuum but will coexist with other regulatory regimes seeking to address different challenges posed by the digital economy. This is not a new phenomenon. Competition regulations in the UK and globally have coexisted with sectoral / specialised regulations for decades. At a high level, to ensure complementarity, it is fundamental to delineate the scope of each regulatory regime with precision, and eliminate

overlaps between them to the extent possible. It is critical that legal certainty be provided to companies and consumers as to their rights and obligations, and how these are enforced.

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