



Legatum Institute response to the Competition and Markets Authority consultation on the digital markets competition regime guidance—

TO: Competition and Markets Authority

CC:

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How to ensure that the Digital Markets Unit encourages and increases prosperity

The United Kingdom has one of the most impressive and dynamic tech economies in the world. Today, the UK is the world's third-largest destination for venture capital investment, attracting more investment than France, Germany and Spain combined. This has not happened by accident. Thanks to a welcoming regulatory environment, generally attractive taxes, and deep pools of talent, London, Cambridge and the south-east of England have developed one of the world's leading clusters of technological innovation.

This benefits the entire country. The digital economy is a source of economic output, innovation, employment, foreign investment, and tax revenue. It sits at the heart of many of the Government's stated ambitions for the economy, to increase innovation, to establish the UK as a global leader in artificial intelligence (AI), and to foster economic growth. Importantly, this has not just been the work of companies native to Britain, but also some of the world's largest tech giants. Indeed, the investments made by companies like Google, Amazon and Microsoft in the British economy have helped to foster dynamism, innovation, and economic growth in this country.

Considering the UK's ageing population, decades-long slump in productivity, and struggles with administrative efficiency, the Government would be right to consider technological innovation the primary problem-solver and a route to sustained economic growth. This should be reflected in the guidance issued to the Digital Markets Unit. Officials at the Competition and Markets Authority should ensure that any intervention they take in this regime is to the benefit of British consumers first and foremost, and does not harm economic growth.

When the Digital Markets, Competition and Consumers Act was making its way through Parliament, the Bill was amended to take more of these principles into account. It is therefore important that the intentions of Parliament are reflected in this guidance, and that a democratic check is added to the regulatory regime.

Proposed principles to adopt

This response is inspired by the research and recommendations from Legatum Institute's 2023 paper on the digital markets act when it was a bill in parliament: https://li.com/wp-content/uploads/2023/12/4543_LI_DMCC_Main_AW-Web.pdf

This paper argued in favour of amending the bill to include safeguards on the operation of the Digital Markets Unit, which has been given statutory powers by this law. These recommendations included:

- Ensuring all CMA interventions are implemented on the basis of a rigorous evidence base
- Enshrining the principle of consumer benefit when it comes to interventions and regulatory action
- Allowing companies sanctioned by the regime to challenge the CMA on the merits of its case, rather than process grounds only, as originally envisaged
- Increasing democratic oversight over the Digital Markets Unit by ensure parliament and/or ministers can approve guidance to the Unit and the CMA

There were other recommendations in the paper, but the four above were all accepted to various degrees by Parliament, who amended the bill accordingly.

Most important, for the purpose of this consultation, is the final recommendation around democratic oversight. The government partially accepted Legatum Institute's recommendations around democratic oversight by deciding that the Secretary of State should approve the guidance to the DMU. While this does not meet the full request for more expansive parliamentary scrutiny and oversight of the DMU, either by Select Committee, or parliamentary scrutiny of DMU appointments, it is a welcome and important step.

The CMA's actions in digital markets could have a transformative effect on the British economy. The powers it has been vested are sweeping. The regulator has the ability veto new products and services offered by companies which have been designated as having "Strategic Market Status". It will be able to extract information from designated companies, change their products, and issue fines of up to 10 percent of their global turnover. These are huge powers and must be scrutinised.

Our response will primarily focus on the designation of firms as having Strategic Market Status, and the CMA's approach to Conduct Requirements and Pro-competition interventions.

Strategic Market Status

The CMA should avoid hasty designations, and take into account the fact that digital markets have a tendency to change radically. Market power is much less entrenched than is often assumed. For example, in 2019, the CMA found that Facebook and Google, the two biggest tech giants at the time, enjoyed an "unassailable" duopoly in the online advertising market.¹ However the tech economy has seen extraordinary changes since

¹ Andrea Coscelli, 'Digital Markets: using our existing tools and emerging thoughts on a new regime' (Fordham Competition Law Institute conference, 9 October 2020)

then. Post-Covid 19 pandemic shifts in consumer behaviour have fundamentally altered the digital economy, and evidence is growing that the supposedly “unassailable” duopoly enjoyed by Google and Facebook is actually a thing of the past.²

- The duopoly was already past its peak when the Furman Review was published.³ Since then, Amazon has gained significant market share in online advertising, along with e-commerce in general. This reflects changing consumer habits in the Covid-19 pandemic, many of which have remained, such as the expansion of online retail, which now accounts for nearly 30 percent of British retail sales.⁴
- The social media market is also fundamentally different today to that of 2019. The rise of TikTok and Snapchat has transformed the market in ways not predicted in 2019.
- The advent of more advanced AI chatbots in 2022 and 2023, just as this Bill was being introduced, also shows how technology has moved on. The chatbot developed by Microsoft-funded OpenAI, ChatGPT, is already changing the way people discover information online, and challenging online search in a way nobody predicted.⁵

In this respect, the Digital Markets regime is based on a law designed for a tech economy which no longer exists. While guidance can only do so much to mitigate against this, it will be important for officials in the CMA to take into account the fact that digital markets undergo seismic change in short periods of time, and that regulatory intervention can harm consumers by limiting choice and protecting certain incumbents.

Particular points of attention in the Strategic Market Status designation section are:

2.49:

- Regarding (a), the CMA should pay close attention to wider market dynamics and consumer behaviour before making a designation. Importantly, the CMA should think about consumer welfare – as the law states – and not just act in the interest of smaller competitor companies to the firms facing SMS designation.
- Regarding (b), the CMA should pay attention to the way in which competitors to SMS firms may be helped or hindered by the wider regulatory environment. For example, AI-powered chatbots, like ChatGPT might well threaten Google’s dominance in search from an unexpected angle. However, these chatbots and their underlying AI models are being constrained by government policy on access to data for copyright reasons.⁶ Seeing as a viable competitor to Google Search

<www.gov.uk/government/speeches/digital-markets-using-our-existing-tools-and-emerging-thoughts-on-a-new-regime> accessed 23 October 2023.

² Tamar Terell, ‘The Google-Meta Ad Duopoly is Ending: What Now?’ *Invest is Digital* (26 January 2023) <www.investisdigital.com/blog/paid-media/google-meta-ad-duopoly-ending-what-now/> accessed 23 October 2023.

³ Ibid.

⁴ Office for National Statistics, ‘Internet sales as a percentage of total retail sales (ratio) (%)’ (20 October 2023) <www.ons.gov.uk/businessindustryandtrade/retailindustry/timeseries/j4mc/drsi> accessed 20 October 2023.

⁵ Liam Tung, ‘Google is feeling the ChatGPT threat, and here’s its response’ *ZDNet* (3 February 2023) <www.zdnet.com/article/google-is-feeling-the-chatgpt-threat-and-heres-its-response/> accessed 23 October 2023.

⁶ Herbert Smith Freehills, UK withdraws plans for broader Text and Data Mining (TDM) copyright and database right exemption, March 2023, <https://www.herbertsmithfreehills.com/notes/ip/2023->

has been undermined by government policy, it would be unwise for the CMA to designate a company as having SMS in such circumstances, as existing government regulation is contributing to the status quo.

2.55-59:

- This is a reasonable list of conditions to cover to assess SMS designation, but they should be analysed in light of consumer welfare concerns. The fundamental principle of competition law that consumer benefit should come first must not be ignored here, and Parliament explicitly amended this law in passage to ensure it pays heed to consumer benefit. Otherwise, this allows the CMA to designate a large firm as having SMS by virtue of it being larger than its rivals.
- It is welcome that the CMA is taking a contextual approach to this, and will have greater flexibility than the European Union's digital markets regime, it will be important to give an indication of what kind of conditions carry greatest weight, in the interests of transparency.

2.60-61:

- There is a great danger that these two paragraphs could be used to prevent all manner of new products being launched, if they are being launched by a large company. This will harm consumers, and will erode market dynamism. For example, Google has postponed launching its AI chatbot, Bard, in the EU, following concerns from the EU's regulators. While this was largely around data privacy instead of antitrust concerns, it highlights the huge effects that regulatory decisions have on consumers. European consumers are now left with a much less competitive generative-AI tools market because of this decision (which in turn might create a false sense that Microsoft is wielding entrenched market power with OpenAI).⁷
- Competition between large companies over new products yields huge benefits to consumers. This is the case in Amazon's emergence in e-commerce to challenge the Meta and Google duopoly, or Google's purchase of Android to compete with Apple in the smartphone market. The CMA should consider acting if there is evidence of consumer harm, not just based on an analysis of market power.

2.62:

- If not applied intelligently, this could lead to consumer and businesses losing out from the benefits of the platform economy. There is clearly a balance to be struck between the way in which a platform operator sets standards for users, and how those affect the interests of the platform and the users, but the CMA should consider the consumer benefits derived from these platforms, and whether designation would reduce such benefits. Does punishing a large platform, like an app store, benefit consumers? Does a new app store immediately open up which is able to better serve its customers? Does regulatory action really benefit consumers here?

03/uk-withdraws-plans-for-broader-text-and-data-mining-tdm-copyright-and-database-right-exception

⁷ Clothilde Goujard, Google forced to postpone Bard chatbot's EU launch over privacy concerns, Politico, 13 June 2023, <https://www.politico.eu/article/google-postpone-bard-chatbot-eu-launch-privacy-concern/>

2.109:

- This section is interesting and deserves support. It implicitly acknowledges the possibility of leapfrog competition in digital markets, the 'creative destruction' described by Schumpeter.
- Subsection (b) notes that former giants can collapse in market power in a short period of time, and this has been seen with companies like MySpace and Yahoo in recent years. Therefore, the possibility of leapfrog competition, as highlighted in this section, should be considered when making decisions around designation, not just reassessments.

Conduct Requirements

It is vital that all decisions on conduct requirements are made following an analysis of the effect this will have on economic growth and consumer welfare. The section devoted to Conduction Requirements on non-designated activities could have a negative effect on consumer welfare as it could prevent companies from launching new products which will benefit consumers.

3.13-15:

- This section is an attempt to walk back the provisions in the law to prove market power before taking action. The CMA should only decide to enact a Conduct Requirement on an SMS firm after assessing the level of consumer benefit and harm from the status quo, and the level of harm of benefit that might change after a CR is imposed.
- Self-preferencing is not in its nature wrong, and in many cases it improves consumer welfare and user experience. Regulatory attacks on self-preferencing must avoid amounting to interventions on large companies for the sake of being large.
- The EU's Digital Markets Act offers a cautionary tale in this area. Google Maps and Google Flights are no longer integrated into Google Search in the European Union. This is to consumers' detriment, increasing the time it takes for them to find locations, destinations or flights, and acts in the interest of medium-sized companies which compete with Google. It also harms the many small businesses who use Google Maps as a form of advertisement and promotion, as it makes it harder for users to find their company profiles. This is exactly the sort of outcome that should be avoided, and this should be reflected in the guidance.

Pro-competition interventions

The CMA should commit to a higher standard of evidence gathering before implementing pro-competitive interventions.

4.09-15:

- The CMA should be clear about which list of indicators it considers most important to mitigate against the possibility of finding an adverse effect on competition. For example, 4.12 (e) notes the importance of SMS firms continuing to innovate to supply the products that their users and customers want. This is welcome, but the CMA should be clear that innovation is being rewarded, not punished. Many other aspects of this regime punish innovation by SMS firms, as they may face sanction for introducing new products to entrench their market power. The guidance should give additional weight against intervention if there is evidence of innovation.

4.19:

- While it is narrowly understandable that the CMA does not want to produce a prescriptive list of evidence that it will take into account when assessing whether there is an adverse effect on competition in digital markets, and prefers a more contextual approach, the CMA would be wise to offer a more transparent and open approach to this assessment.
- The entire guidance document avoids offering clarity on the sort of evidence the CMA will take into account when making decisions. This is unwise and dilutes trust in the integrity of the regime, and highlights the downside of flexibility for the companies who are subject to these regulations.
- The CMA should explicitly consider consumer welfare concerns in this section, and ensure that any action it takes enhances, rather than reduces, consumer welfare, and that this is backed up by evidence to show that this is not an theoretical assumption.

Conclusion

The DMCC regime is going to be one of the most important regulatory regimes in the UK in the next decade. It updates over two decades' worth of competition law practice, and will have huge impact on the entire economy. As such, the Secretary of State should pay close attention to the operation of this regime, and ensure the CMA is a agent of prosperity, rather than a threat to it.

It was welcome that the law was amended by Parliament to explicitly refer to the importance of consumer welfare in this regime, whereas previously it was overwhelmingly focused on protecting the interests of one group of businesses over that of another. Ultimately, consumer welfare is the only thing that matters, and focusing on this is the best guarantor of economic growth, increased dynamism, and improved living standards. By taking into account the analysis and recommendations in this document, the Secretary of State and the CMA will be able to ensure that the DMCC regime nurtures innovation and prosperity in the UK, and ensures Britain remains one of the best places in the world to develop, sell and operate digital products and services.

