2020 vision

THREE THEMES FOR THE COMPETITION YEAR AHEAD

January brings our annual look ahead to topics that are likely to dominate the competition law agenda in the coming year. In this bulletin we identify three themes for the year ahead: 1) Digital markets, and how to apply competition law to them; 2) Potential competition, and how competition authorities should analyse the future; and 3) The wider view, or, should the scope of competition enforcement be limited to its current parameters?

From talk to (the beginnings of) action

The most important competition law topic of the late 2010s was the appropriate competition law response to the rise of the digital economy. 2019 might be characterised as "the year of debate": reports were issued in several jurisdictions raising potential competition concerns, identifying gaps in current competition law frameworks and/or enforcement approaches, and floating potential remedies.[1] 2020, in contrast, looks as if it might be the year in which some of these ideas start to be turned into concrete steps.

Intriguingly, recent developments seem to reflect a concern that national (and supranational) competition authorities (collectively NCAs) are unable to constrain the behaviour of large digital firms using conventional competition law tools. The Australian Competition and Consumer Commission (ACCC) has recommended that a digital platforms branch be set up within the ACCC.Designated digital firms would be subject to a code of conduct relating to their relationships with news media businesses, and be subject to ex ante regulation of various forms.[2] In Germany, the draft 10th Amendment to the Act against Restraints of Competition (the draft Act on Digitalisation of German Competition Law ("*GWB-Digitalisierungsgesetz*")) proposes to restrict the behaviour of "companies with overwhelming importance for competition across multiple markets". This will entail wider ex ante powers against potential abuses, such as preventing self-preferencing, impeding inter-operability, and vertical (or horizontal) leveraging strategies, with a particular focus on the use of data to achieve these aims.[3] In the UK, the Furman report recommended the creation of a Digital Markets Unit with ex ante regulatory powers applied to digital firms with strategic market status. Following this lead, the UK Competition and Markets Authority recently proposed the introduction of a code of conduct (i.e. ex ante regulation) applying to such firms, with particular emphasis on the high level principles of "fair trading", "open choices", and "trust and transparency".

These proposals raise several challenging questions that policy makers and legislators will have to grapple with. For instance:

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1 For instance: the Crémer/Montjoye/Schweitzer report of April 2019 for the European Commission; the Furman review **of** March 2019 in the UK; the Stigler Committee on Digital Platforms of September 2019 in the US**,** the Bundeskartellamt's report into "Competition 4.0" in Germany; the Bundeskartellamt and Autorité de la Concurrence's joint study on the implications for competition law of algorithms of November 2019.

2 https://www.accc.gov.au/system/files/Digital%20Platforms%20Inquiry%20-%20Final%20report%20-%20part%201.pdf

3 An official version of the draft Act is not yet publicly available, but an unofficial version, which has been the focus of a consultation process between government departments, was leaked in October 2019 and is available at d-kart.de/wp-content/uploads/2019/10/GWB-Digitalisierungsgesetz-Fassung-Ressortabstimmung.pdf.

- **Who to target?** There are several definitions being debated, and as yet no clarity on exactly how one would identify the relevant firms that fall under whatever definition is decided upon. A definition based on broad criteria could potentially capture a large number of firms, which may become unmanageable. A definition based on narrow criteria could potentially run into concerns that it is individual firms that are being targeted rather than principles, and may not be fit for purpose in the future as markets develop.
- **What markets?** Competition law in most countries is founded on the concept of market definition. The definitions of "strong digital firms" typically imply or rely on some assessment of market power for which market definition is a requirement. However, current approaches to market definition assessment in two-sided digital markets are still hotly debated. For instance, the European Commission has used a one-sided "functional characteristics" approach in *Google Shopping* and *Google Android*. If replicated elsewhere, many firms could potentially be found to have strong market positions depending on exactly which characteristics and combinations of characteristics are determined to be important. Elsewhere commentators have highlighted the importance of looking at both sides of a two-sided market. This was discussed extensively in the US Supreme Court judgment in *American Express*, which - while not a digital market - has many similar features.
- **What are the gaps?** Several of the issues identified appear to fall within the scope of existing competition law. For instance, the German proposals for rules against self-preferencing would seem to be captured by existing competition law, as this is the basis of the *Google Shopping* decision. Vertical leveraging is similarly reviewable under existing laws (as *Google Android* demonstrates). It may be that NCAs feel that the time taken to make these decisions and the burden of evidence required to make a watertight case is too great. If so, it will be interesting to see whether legislators agree that the appropriate approach is to make it easier for NCAs (or the European Commission) to bring cases by reducing the time and evidential burden required.

It is likely that 2020 will bring the beginnings of action in this area. But given the challenges we have identified, this may be the beginning of several years of activity.

The protection of competition yet to come

The second theme that we expect to grow in importance is an increased desire of competition authorities to protect future competition through more restrictive merger control. The debate has occurred primarily in relation to digital markets, but there is also some read across to non-digital markets.

This will require authorities to develop and enhance their techniques for assessing future competitive developments. Some initial thinking has been done in these areas, but the challenges are substantial and there are several issues to overcome that competition authorities are currently grappling with.

- **Internal documents.** The UK CMA seems to have taken the approach that mentions in internal documents (that two firms are competitive threats to each other in the future) is sufficient to demonstrate a loss of potential competition from a merger (e.g. *Experian/Clearscore*). While there is clearly some weight that can be placed on internal documents, it would be concerning if this were considered to outweigh robust quantitative evidence. If actual market outcomes were to contradict statements in internal documents, it would seem more sensible to rely on the actual data, rather than on documents which may themselves be based on less reliable evidence or "gut feel". It will be interesting to see the extent to which competition authorities seek to rely on evidence from internal documents in the future. Certainly there is a trend towards ever-greater internal document requests in mergers and in other competition investigations, both at the EU and national level.
- **Killer acquisitions.** There has been substantial recent commentary around the idea of "killer acquisitions" – acquisitions by a large firm of a small firm in that market or a related market, to reduce the future competitive threat the large firm faces. This idea originally arose in the pharmaceutical sector, with the idea being that incumbents would acquire firms seeking to develop the next generation of a particular product. The reports on digital markets mentioned above have

applied this analysis to acquisitions by large digital firms.[4] However, the read-across from the pharmaceutical sector is far from clear.

- Pharmaceutical markets are typically characterised by clear and lengthy innovation pathways. Initial investment in a particular innovation space, if successful, is likely to lead to a product in that space, and innovation in a different innovation space is unlikely to lead to a competing product. Acquisitions in the same innovation space are likely to lead to a reduction in potential competition (see *Dow/DuPont* for an example in the context of pesticides, which share many innovation characteristics with pharmaceuticals).
- Digital innovation does not typically proceed on the same lines. There might be many firms that are currently innovating to develop new attention-grabbing products with different characteristics to existing firms. Each may potentially be a strong competitor for the existing firms in the future, depending on how attractive their product ultimately is to consumers. It is perhaps for this reason that the Crémer/Montjoye/Schweitzer report for the European Commission was cautious about casting the net wide in relation to identifying firms that might compete closely with each other in the future. Taking a wider approach to identifying firms that might have overlapping products in the future, if viewed consistently, might allow more mergers to proceed rather than less.

The "killer acquisitions" hypothesis does not therefore provide competition authorities with a silver bullet for preventing acquisitions.

- **Counter-arguments.** The flipside of a focus on potential reductions in competition in the future would appear to be an equal need to assess the potential dynamic counter-arguments that might apply. In recent years NCAs have considerably developed their techniques for assessing static competition, largely to the exclusion of dynamic arguments. As a result, two areas in particular will need to be considered:
  - **Entry.** If the acquired party might develop into a strong competitor even in the absence of existing evidence, then potentially so might other firms with similar capabilities, given the profit opportunity that is available. This might require competition authorities to return to analysis focused more around barriers to entry and whether these would restrict the prospects of potential entry to restore the current level of competition. An approach of concentrating on barriers to entry was common in Europe prior to the revision of the EU merger regulation, and the subsequent focus on static assessments of competition, in 2004. This issue has recently arisen in conventional mergers: a key issue in *Siemens/Alstom* was whether potential competition from Chinese producers was sufficient to overcome any loss of competition between the parties arising from the transaction. It may be that the European Commission could more easily accommodate the desire from some member states to allow more transactions between large EU firms by placing greater weight on potential entry arguments (rather than allowing a "national champions" exemption).
  - **Efficiencies.** It would also seem incumbent on competition authorities to take more seriously the idea that mergers could give rise to efficiencies, in a world where the only potential competition concern arises in the future. The current static approach has led largely to a neglect of the efficiencies that could arise from a merger. Recent analysis of previous digital mergers by LEAR has highlighted that there appear to have been substantial merger efficiencies arising from some digital mergers under review (and which were not captured in the original analysis).[5] However, NCAs have typically been sceptical as to the existence of merger efficiencies, so may be unlikely to take these into account as part of the dynamic merger calculus even if they would seem to be highly relevant.

[4] In France, the Autorité de la Concurrence has requested powers for ex-post review of mergers, in order to give itself the freedom to review killer acquisitions that fall below the relevant jurisdictional thresholds.

[5] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/803576/CMA_past_digital_mergers_GOV.UK_version.pdf

These issues have primarily been considered in a merger context thus far. However, there may be similar pressures in an Article 102 context. The proposed (draft) revision of the German competition regulation includes provisions to deal with abuses that are designed to tip a market in favour of an incumbent, for instance in markets that are characterised by strong network effects. This is likely to raise the question of whether particular business practices are pro- or anti-competitive. If a firm developing a new product seeks to charge a zero price to consumers (as is common in many digital markets), in order to establish a sizeable user base, which is ultimately funded through advertising would this be pro-competitive or anti-competitive? During the start-up period, the firm will be making losses, particularly if there is competition between multiple firms all of whom are seeking to develop the same product and recognising that there is a winner-takes-all or winner-takes-most character to the market. Is this predatory pricing or anti-competitive investment? Or is it the natural expression of competition in such markets? If such behaviour is condemned on the part of incumbents in other markets, but allowed by new entrants, does this implicitly result in a ban on new product developments by large digital firms? And if so, is this good or bad for competition?

We can expect further efforts by competition authorities to develop techniques for assessing the dynamic effects of competitive behaviour, both in an abuse context and a merger context, in the coming months and years.

More could be done – but should it be done?

Competition authorities and wider commentators have expressed frustration with the limits to the scope of competition law powers, or with the way that these powers are sometimes expressed. For instance:

- The Chair of the UK CMA, Lord Tyrie, has asked the UK Government for a revision of its market study powers to be based on a test of an "adverse effect on *consumers*" rather than an "adverse effect on *competition"*.
- The Bundeskartellamt's case against Facebook for abuse of a dominant position through accessing data from users who login using Facebook on third party websites (which was rejected on appeal by the Oberlandesgericht Duesseldorf) was based on a view by the Bundeskartellamt that Facebook was in violation of the General Data Protection Regulation.
- The French and German governments have requested a review of EU merger control to allow for the creation of national champions.
- Commentators have identified competition law as a potential hindrance to businesses developing solutions to environmental issues such as recycling, climate change and air pollution.[6]

However, in other contexts competition authorities have sought to retain limits to their scope of activities. The CMA has come out against the Furman review proposal for a balance of harms test, on the basis that this would be difficult to operationalise in practice given the challenges with identifying precise probabilities for particular future outcomes. The European Commission has sought to push back against proposals to allow national champions and – whilst recognising that environmental issues may well result in adverse effects on consumers – has identified there would be concerns if environmental issues were to be a fig leaf for anti-competitive behaviour.

Pressures for an expanded role for competition authorities – both resulting from wider political and social pressures, and from an internal motivation to be seen to be relevant and effective in tackling the public's concerns – may well grow. This creates both opportunities and challenges for competition authorities. On the one hand, public choice theory would suggest that state bodies will generally welcome an increase in their powers. On the other hand, moving away from hard competition principles will allow wider scope for lobbying, and could result in challenging balancing acts for the competition authorities. For instance, suppose that energy firms got together (hypothetically) to agree to raise the cost of petrol and diesel to consumers. This might be justified on consumer grounds and hence may provide an objective justification under an "adverse effect on consumers" test. The basis for this would be that it would lead to a reduction in journeys and so air pollution, and a likely increase in the rate of take-up of electric vehicles with benefits for meeting CO_2 reduction targets. In such a situation the competition authority would need to balance off adverse price effects with potentially beneficial health, environmental or macro-economic effects, perhaps with a distributional overlay. At present this wider balancing is an issue for central government.

[6] https://www.law.ox.ac.uk/sites/files/oxlaw/simon_holmes.pdf

So a further area to look for over the next 12 months is the fundamental issue of how the scope of competition law develops, and with it the role of competition authorities.

Conclusion

As with many recent years, 2020 seems likely to be a year of great interest to the competition community, with many active and challenging policy debates. Frontier will continue to contribute to these debates, both in our project work and in our wider thought leadership activities. And with the opening of our new larger office in Brussels this year, our presence at the heart of the conversation will be greater than ever before.

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