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High-Level Working Dinner

Market Dynamics and Competition in the Digital Economy

Special Guest

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Online Platforms and Antitrust: Challenges and Opportunities



Plan

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- **Tying practices in digital markets:** a comparison between *Microsoft I* and *II* and *Android*
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Definition of online platforms

What are “online platforms”?

- **Online platforms** are **systems** that **allow users to interact with content, services and functionalities over the internet**
- A platform may be a **service** (search engines, social networks, e-commerce sites), a **software** (web browsers, operating systems) or even a **device** (smartphones and tablets)
- The **benefits of online platforms** over the past few years have been enormous for social welfare

Online platforms as multi-sided markets

- Online platforms are **multi-sided markets**
- **Rochet and Tirole**
 - “A two-sided market [is defined] as [a market] in which the **volume of transactions between end-users depends on the structure and not only on the overall level of the fees charged by the platform**”
 - Important to focus on the structure of the platform: a market is two-sided when the total volume traded on the platform does not depend only by total price charged to users overall but by how much each group of users is charged
- Key insight is therefore that a platform must be allowed to fine tune its business model so that it can charge less on one side of the market (up to zero or even a negative price) and more on the other side of the market
- Furthermore, the platform’s pricing structure on one side of the market must deal with externalities on the other side of the market – “**attracting one side by lowering price is particularly profitable for the platform if this side creates substantial externalities on the other side**”
- Various business models
 - giving away a product for free in order to maximise profits on complementary products (e.g. applications)
 - investing heavily on quality on one service to maximise revenue on other services (e.g. search engines)
- **Multi-sided strategies, bundles, product design, and product integration** are key to innovation in these markets
- **Platform structure, business model, and product design** in multi-sided platforms are key

Antitrust analysis of online platforms

The multi-sided nature of the platform matters

- Case C-67/13 P *Cartes Bancaires*
 - Commission had concluded that the Groupement des Cartes Bancaires (CB) had infringed Article 101(1) TFEU by applying fees on issuing banks designed to increase the costs of cards to the benefit of the larger banks and to the detriment of consumers – the restriction was a restriction by object
 - CB argued that the purpose of the measures was twofold: (i) to encourage those members of the Groupement that are issuers rather than acquirers to develop their acquiring activities, and (ii) to give financial recognition to the efforts of the ‘founding members’
 - GC upheld the Commission decision
 - Court of Justice set aside the judgment of the GC
 - **Court of Justice held that the GC had been wrong to conclude that an analysis of the balancing requirements between issuing and acquisition activities could not be carried out in the context of Article 101(1) (because the purported restriction took place in the market for issuing only) : the GC had confused two issues: (i) that of the definition of the relevant market; and (ii) that of the context to be taken into account to ascertain whether the content of an agreement reveals the existence of a restriction by object. Since the GC had found issuing and acquiring activities to be essential for the operation of a card payment system it could not ignore this simply because the act of acquiring did not occur in the issuing market**
- The “object” test under EU law is the test where the least market analysis is required in order to conclude that a practice restricts competition. Thus analysis of the two-sidedness of the market is **always** necessary to determine whether any practice is restrictive of competition

Market definition

- **Not an end** in itself **but a tool** to assess market power and anti-competitive effects
- Application of the **SSNIP test** when a service is provided for free
 - **competition** among platforms may be competition **for the attention of the consumer, his usage of the platform, or his personal data**
 - key parameter may be **quality** but how to apply market definition tests traditionally developed with price in mind?
 - defining the market based on the qualitative features of a service may be misleading in markets with differentiated but potentially competing products – does Facebook compete with Snapchat? And Snapchat with Whatsapp? And Whatsapp with mobile and fixed telephony services? When does differentiation become a separate market and how to assess this with any reasonable degree of certainty?
- **Multi-sided markets**
 - if a hypothetical monopolist raised its price on one-side of the market, this could have a **feedback effect on the other side of the market** so that the price increase would not be profitable. If market definition does not fully consider this feedback effect, the market may be defined too narrowly
 - example: if a social network started charging its users or degraded its quality by a small but significant non-transitory measure, it could lose enough advertisement on the other side of the market because advertisers would move to advertising on a search engine – does it mean that the market should not be limited to social networks but include also search engines? Or perhaps market definition as we know it is not particularly meaningful and we should move towards focusing directly on **market power** and **anti-competitive effects**?

Market definition revisited

- Is it really necessary to continue to define the market?
 - given that market definition is only a tool to understand the competitive constraints on products/services and the likely effect on competition of the conduct under review, if other evidence/methods are available to do just that, **market definition could be dispensed with, or**
 - **continue to define markets but**
 - **consider all plausible market definitions**
 - **analyse the competitive pressure** on the platform under investigation regardless of formal market definition and market shares
 - **verify whether the evidence of anti-competitive effects is consistent with the existence of substantial and durable market power** by the platform

Market shares \neq market power

- **Market shares** are **not a reliable indicator of market power** or a **dominant position**
 - market shares are **difficult to calculate**
 - they do not take into account the **constraints exercised by users on both sides of the markets**
 - they do not take into account the competitive pressure exercised by **potential competition**
 - also bear in mind **costs of erroneous intervention**
- *Facebook/Whatsapp*, para 99: “the Commission notes that **the consumer communications sector is a recent and fast-growing sector which is characterised by frequent market entry and short innovation cycles in which large market shares may turn out to be ephemeral.** In such a dynamic context, the Commission takes the view that in this market high market shares are not necessarily indicative of market power and, therefore, of lasting damage to competition”
- Can a platform be dominant on one side of the market without being dominant of the other side of the market?
- Dynamic competition and competition for the market
- Evidence suggests that barriers to entry on online markets are not necessarily significant, e.g. success of **Whatsapp** in messaging services, **Facebook’s success over MySpace** in social networks, **Google’s success over Yahoo!** and AltaVista in search
- Online markets have opened up significant opportunities for rapid and effective entry and expansion, e.g. **Pokémon Go** apparently reached 40 million users within weeks of launch and in July 2016 iPhone users were spending more time on Pokémon Go than on Facebook

Facebook/Whatsapp

- **Market definition**
 - the EEA-wide or global market for consumer communication apps for smartphones while noting that
 - traditional electronic communication services could be in the same market (eg mobile telephony and text messaging)
 - services offered on other devices could be part of the same market
 - no segmentation based on functionality (pictures, text, voice) was appropriate
 - EEA-wide or global market for social networking services, while noting that
 - consumer communication services could be part of the same market
 - national online advertising services, while noting that
 - there could be separate markets for online search and non-search advertising and even a separate market for social networks advertising
- **Market shares** on the consumer communication apps market
 - Facebook's proposal: app reach (percentage of users on a representative panel who used the app over a 30 day period)
 - market participants' proposal: monthly minutes of use
 - no reliable data could be collected, e.g. in relation to messages sent, messages received, individual vs. group messages, etc.

Data as a barrier to entry

- *Bazaarvoice/Power-Reviews* merger in the USA → merger was blocked on application by the DoJ because it would have created a monopoly in “rating and review platforms”- network connecting retailers and brands and data were not replicable by competitors either organically or by M&A
- However, note approach in the EU when a merger combines important sets of data or sets of data with vertically related services (e.g. data analytics)
 - *Google/Double Click*: merged entity would obtain data sets from Google and Double Click thus becoming able to match data from both data sets. However, **there were several competitors that ran both a search engine and ad serving and, furthermore, data could be purchased from third parties**
 - *Facebook/WhatsApp*: merged entity could collect data from WhatsApp in order to improve targeting of advertising on Facebook. However, incentives were mixed (WhatsApp users could have switched to other consumer communications apps) and the **amount of data available to competitors remained considerable**
 - *Microsoft/Yahoo!*: **combining data from both search engines would improve services and allow the merged entity better to compete with Google**

Different policies for different objectives!

- Important not to confuse competition policy with other policies and not to use competition law for purposes other than its long-term consumer welfare/productivity growth objective
- Case C-238/05 *Asnef-Equifax, Servicios de Información sobre Solvencia y Crédito, SL v Asociación de Usuarios de Servicios Bancarios*
- Reference involved a register run by Asnef-Equifax whereby a group of financial organisations exchanged solvency and credit information about their customers in order to evaluate the risks undertaken when engaging in credit or lending activities
- Para 63 “Furthermore, since, as the Advocate General observed, in substance, at point 56 of his Opinion, **any possible issues relating to the sensitivity of personal data are not, as such, a matter for competition law, they may be resolved on the basis of the relevant provisions governing data protection.** In the main proceedings, it is apparent from the documents before the Court that, under the rules applicable to the register, affected consumers may, in accordance with the Spanish legislation, check the information concerning them and, where necessary, have it corrected, or indeed deleted”

Network effects

- **Direct and indirect network effects**
 - direct network effects: user's valuation of the product increases as the number of users of the same product increases
 - indirect network effects: user's valuation of the product increases as the number of users of complementary products increases
- *Facebook/Whatsapp*, para 130: **“The existence of network effects as such does not a priori indicate a competition problem in the market affected by a merger.** Such effects may however raise competition concerns in particular if they allow the merged entity to foreclose competitors and make more difficult for competing providers to expand their customer base. **Network effects have to be assessed on a case-by-case basis”**
- Paras 131 -141: **network effects not a problem when**
 - **sector is fast moving**
 - **low barriers to entry**
 - **consumers multi-home**
 - **parties do not control any essential element of the network**

Disruptive innovation

- Schumpeterian competition – innovation cycles – competition for the market
- *Facebook/Whatsapp*, para 116: “The consumer communications apps market has been characterised by **disruptive innovation**. For example, BlackBerry launched the first successful smartphones with integrated consumer communications app and had a very significant market position. However BlackBerry Messenger was available only for BlackBerry smartphones and lost importance with the emergence of multi-platform apps once Android and iOS devices gained a larger part of the smartphone market ... WhatsApp itself was launched in 2009, when the shift of users of consumer communications services from PC to smartphone started, and today it has approximately 600 million active users. Similar market dynamics can be found with respect to LINE and WeChat, which were both launched in 2011 and each of which has now more than 400 million active users worldwide”
- Para 117: “the Commission has found in its market investigation that **there are no significant ‘traditional’ barriers for a new consumer communications app to enter the market**, that is, to be offered to users for download”

Switching costs and multi-homing

- As the digital economy develops, **switching costs become lower and lower** and **multi-homing more and more common**
- *Microsoft I* [2007] OJ L32/23 – tying of Windows with Windows Media Player
 - consumers had no or low incentives to obtain a second media player providing similar functionality
 - downloading was not an efficient distribution practice because of many users’ reluctance to download a second media player from the Internet (slow internet connection + worries about downloading software from the internet)
- Consider **downloading** today in **2017**
 - eg by the beginning of 2016, Dropbox was downloaded more than **half a billion times** on Android even if Android had the file-sharing app Drive pre-installed: B King Jr, ‘Dropbox Android App Passes 500 Million Installs On Google Play’ (25 January 2016), available at <http://www.androidpolice.com/2016/01/25/dropbox-android-app-passes-500-million-installs-on-google-play/> (accessed on 12 January 2016) and <https://play.google.com/store/apps/details?id=com.dropbox.android&hl=en> (accessed on 18 April 2017).
- Canadian Competition Bureau, ‘Competition Bureau Statement Regarding its Investigation into Alleged Anti-Competitive Conduct by Google’ (Ottawa, 19 April 2016), available at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/04066.html> (accessed on 12 January 2017): **“consumers can and do change the default search engine on their desktop and mobile devices if they prefer a different one to the pre-loaded default”**

**Tying on digital markets:
A comparison between
Microsoft I and II and
*Android***

Tying in online markets

- Combining different services and functionalities together as **key feature** of digital economy
- Tying **cannot be a *per se/object* abuse**
 - General Court in *Microsoft I* and Commission Guidance on Art 102
 - dominant position on tying market
 - tying and tied product must be separate products
 - coercion
 - foreclosure
 - consumer harm
 - objective justification
 - possible refinement of the test
 - **structural features of tied market** - already inherent in foreclosure analysis but to make it explicit would guard against the risk of false positives
 - **consumer harm** could be acquisition, maintenance, or strengthening of market power on the tying market, the tied market, or a related emerging market, to the detriment of consumers
 - note consumer harm test ensures that market power is not of a transient nature so that it may be eroded by entry and expansion
 - separate product and coercion tests less important if thorough foreclosure + consumer harm analysis is performed

Dominant position on tying market

<i>Microsoft I and Microsoft II</i>	<i>Android (Play Store)</i>	<i>Android (Google Search)</i>
Tying product = Microsoft Windows → World-wide market for PC operating systems	Tying product = Play Store → EEA-wide or national markets for app stores for the Android operating system	Tying product = Google Search → EEA-wide or national markets for general internet search services
Strong network effects in that developers writing applications for Windows had no or little incentives to write applications for other operating systems	No network effects in that developers can write apps that would run on any Android device and could be downloaded from any app store	Query the extent of network effects in search
No-multi-homing	More than one app store can be used on Android	More than one search app can be used on Android
Lack of interoperability	Interoperability	Interoperability

Features of the tied market

<i>Microsoft I</i>	<i>Microsoft II</i>	<i>Android (Google Chrome)</i>	<i>Android (Google Search)</i>	<i>Android (licensable mobile operating system)</i>
Tied product = Microsoft Media Player	Tied product = Internet Explorer	Tied product = Google Chrome	Tied product = Google Search	Tied product = Android complying with minimum compatibility standards
Strong network effects in that developers and content providers had no or little incentives to write applications and provide content for other media players	Strong network effects in that developers and content providers had no or little incentives to write applications and provide content for other web browsers	Query the extent of network effects in search	Query the extent of network effect in search	No or weak network effects as developers can and do write apps for both Android and iPhone and apps written for AFA-compliant versions of Android can also run on other versions of Android
No-multi-homing	No multi-homing (?)	More than one web browser can be used on Android	More than one search app can be used on Android and search can be performed other than by a search app	AFA-compliant versions of Android not supplied by Google can be used – note also Android is open source
Lack of interoperability	Lack of interoperability	Interoperability	Interoperability	Interoperability

Foreclosure

<i>Microsoft I</i>	<i>Microsoft II</i>	<i>Android (search)</i>	<i>Android (licensable mobile operating system)</i>
Consumers have no or low incentives to obtain a second media player	OEMs have no incentive to install a second media player providing same functionality	Incentives to obtain second browser app or web browser + additional ways in which users can search the Internet	Obviously only one operating system can run on each device but note AFA-compliant versions of Android not supplied by Google are allowed
Downloading was not an efficient distributional practice	Downloading not an efficient distributional practice due to users' inertia or lack of technical skills	Downloading today	Downloading not relevant
Data does not point to a comparative advantage in terms of quality of Microsoft's media player	IE was not superior to its competitors	Possible to say that Google search services are used notwithstanding they are of inferior or not superior quality?	Possible to say that AFA-compliant Android does not have benefits (mainly anti-fragmentation)?
Bundling media players with other Internet services or software was less efficient than Microsoft's tying (no guaranteed market share that was key for developers and software providers)	No discussion of alternative distribution methods other than deals with OEMs and downloading	Could competitors deploy equally effective distributional strategies, i.e. by providing valuable products for free, by making upfront payments or by entering into revenue-sharing agreements?	No obstacle to OEMs using competing versions of Android as AFA is optional
Indirect network effects	Indirect network effects	Query extent to network effects in search	No or weak network effects as developers can and do write apps for both Android and iPhone and apps written for AFA-compliant versions of Android can also run on other versions of Android

Consumer harm

Microsoft I	Microsoft II	Android (search)	Android (licensable mobile operating system)
Monopolisation of media player market	Preservation of dominant position on client PC operating system market	Monopolisation of search market requiring proof that either (1) consumers would not react to a degradation of the quality of search services or (2) there are no adequate actual or potential alternatives to Google search services on the market for internet search services	Android is licensed for free, therefore the incentive to foreclose could not consist in the acquisition, maintenance or strengthening of market power on the tied market
Protection of dominant position on PC operating systems	Lack of interoperability locked users into IE	Incentive is monopolisation of advertising market on the theory that search advertising is not a substitute for other forms of online advertising	Preventing emergence of Android forks in order to preserve role of Play Store as tying product to foreclose search market
Increasing barriers to entry on the PC operating system by forcing entrants to offer a Microsoft-compatible media player	If IE was only available on, or compatible with, Windows, users would be locked into Windows	Is lock-in realistic?	Preventing emergence of Android forks as they could carry alternative web browsers or search apps
Gaining 'significant advantage in other business areas such as those for content encoding software, format licensing, wireless information device software, DRM solutions and online music delivery'	Possible leveraging of dominant position into Web 2.0 service markets such as banking, social networking, information sharing, etc.	Leveraging into other markets?	Leveraging into other markets?

Innovation as a safe harbour

- **Firms must be able to innovate even if innovation excludes competitors**
- But how to define “innovation”?
- Are there exceptions, that is, **could innovation be detrimental to competition?**
- A possible exception to a “non prohibition rule” is **when innovation is not genuine innovation but has no other purpose than to exclude rivals**
- Important to note that the **test cannot be only “intention to exclude rivals”** – all innovation is carried out with the “intention to exclude rivals” in one way or another
- Necessary limb of the test is that **conduct is not “genuine innovation”** – this should require proof that the conduct is not of any material benefit to consumers and that it is therefore only aimed at excluding competitors
- Classic objection is that competition authorities should not “second-guess” the market on innovation – however, this cannot mean that it is sufficient for a dominant undertaking to state that something is innovation to escape any antitrust liability – **competition authorities must be able to verify whether the safe harbour applies in the first place which means that they must be able to verify whether the conditions for the application of the “safe harbour” are met**

Innovation as objective justification

- **Dynamic efficiency** is an **objective justification** under Article 102 TFEU as well as under Article 101 TFEU
- Case T-201/04 *Microsoft Corp v Commission*, para 709: test is whether the refusal to supply was detrimental to Microsoft's incentives to innovate
- *Streetmap.eu Ltd v Google Inc* [2016] EWHC 253 (Ch), paras 142 – 176 (Roth J)
 - **technical improvements in the quality of the goods can be a defence to an abuse case**
 - where the efficiency is a technical improvement, **proportionality does not require adoption of an alternative that is much less efficient in terms of greatly increased cost or which imposes an unreasonable burden** (at the very least in a case where there is no suggestion that the conduct impugned was likely to *eliminate* competition)
- **Difference between dynamic efficiency as a safe harbour or as an objective justification** may be **somewhat academic** – it is obviously for the allegedly dominant firm to plead that the conduct is dynamically efficient and adduce sufficient evidence to substantiate its defence but burden/standard of proof/of adducing evidence should not be so high that it cannot reasonably be met
 - costs of false convictions
 - businesses cannot be expected to have knowledge that goes beyond a reasonable assessment of own demand/consumers' preferences/own opportunities for growth and profit maximisation
 - businesses cannot be expected to incur additional burdens or choose less efficient alternatives for the purpose of helping/not damaging rivals

Thank you

Comments and questions

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