

# Antitrust Chronicle

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## THE 2017 ANTITRUST HORIZON

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# LETTER FROM THE EDITOR

## Dear Readers,

On January 27, 2017, European Competition Commissioner Margrethe Vestager said that putting “faith in barriers and fences” instead of open markets are going about it the wrong way. She went on to say that “[t]hose defenses will not help. They’ll only weaken our economies and increase prices for consumers, without giving people any more control over their own lives.”

Meanwhile, on May 16, 2016, then candidate Trump said that Jeff Bezos and Amazon “have a huge antitrust problem” and that “Amazon is getting away with murder, tax-wise.”

With Commissioner Vestager’s and President Trump’s recent statements as a backdrop, we are proud to offer our subscribers this year’s second edition of the CPI Antitrust Chronicle for February: “**The 2017 Antitrust Horizon.**”

This edition focuses on what’s next for antitrust in the U.S. and the EU for the coming year. Antitrust policy and enforcement faces uncertainties on both sides of the Atlantic in the near future. The antitrust times...they are a-changin’. But how far reaching will these changes potentially be?

In the U.S., things may become a bit clearer once the Trump administration appoints leadership positions at the DOJ and FTC and new Justice of the Supreme Court is confirmed. In Europe, the pending Brexit looms large on the horizon of antitrust enforcement.

We are featuring a “**Digital Markets Update**” in this month’s Chronicle with three great articles from leading minds in the field.

In our CPI Talks section, we hear from Frederic Jenny and get his thoughts on what could be ahead for antitrust in 2017. A must read interview!

Thank you to our great panel of authors this month.

We hope you enjoy reading our February edition of the CPI Antitrust Chronicle.

Sincerely,  
**CPI Team**

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## Changing Times? The Outlook For Antitrust Enforcement In The EU And The U.S.

By Rachel Brandenburger, Logan Breed, Helen Bignall & Paul Castlo

This article considers the outlook for antitrust enforcement in the EU and the U.S. in the next few years, and how Brexit and the new U.S. administration under President Trump could impact that outlook. Antitrust policy and enforcement faces extraordinary challenges and uncertainties in the EU and the U.S. in the coming few years. These are indeed changing times, but to what extent and in what direction or directions is less easy to forecast.

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## America-First Antitrust

By Eleanor M. Fox and Harry First

What is America-First antitrust? America First means nationalism, which of course extends beyond America. Nationalism is the watchword of Brexit and of any number of political parties in Europe that might soon come to power. "From this moment on, it's going to be America First." So spoke Donald J. Trump in his inaugural address as President of the United States. The new Administration appears to embrace these nationalistic trends, while at the same time criticizing what it sees as nationalistic policies of our trading partners, particularly China, but Japan and Korea as well. This article puts forward possible ways in which America-First antitrust could play out in the years to come.

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## Brexit And Its Impact On English Antitrust Claims

By Kenny Henderson

In Theresa May's memorable words, "Brexit means Brexit." But what does this mean for England's status as a favored jurisdiction for antitrust damages claims? The impact of Brexit on antitrust litigation in England will be influenced by the form of Brexit that the UK eventually adopts. Post hard Brexit, the cause of action for breach of Articles 101 and 102 TFEU may become unavailable, leaving claimants to file under the domestic analogues of Chapters I and II Competition Act 1998. This may narrow the territorial scope for such claims. These changes notwithstanding, even a hard Brexit will not remove many of the features that make England an attractive jurisdiction to claimants. In fact, England could become more attractive in some ways.

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## U.S. Antitrust Under The Trump Administration - A Fearless And Perhaps Accurate Prediction

By Kent Bernard

The vast majority of experts predicted both that Trump would lose, and that the stock market would crash if he won: he did; it didn't. When you have gotten the big prediction very wrong, it is hard to claim with a straight face that you are going to get the follow on predictions right. In making predictions as to what antitrust policy will be under the President Trump Administration, this article first looks to the makeup of the Trump's transition team, and what do these choices tell us. Next, the author, with the help of his crystal ball, looks at a couple of key antitrust areas and what is more likely than not to happen to them under a new administration.

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## U.S. / EU Antitrust Friction In The Time Of Brexit: Toward A Rosier Scenario?

By Tad Lipsky

Although U.S. and EU antitrust rules share many elements, their historical roots are distinct and a variety of important tensions and inconsistencies persist between the two systems. Firms with operations in both jurisdictions are typically required to follow different legal advice and to operate differently in each. In many circumstances such firms can tolerate the added expense and business limitations without significant effects on their fundamental business models. Where there are important complementarities and cross-influences between U.S. and EU business conduct, however, the clash in antitrust rules can alter the fate of a business enterprise or an entire industry.

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## Digitalization Revolutionizes The Economy – And The Work Of Competition Authorities

By Andreas Mundt

Digitalization is revolutionizing all sectors of the economy. This is a challenging development not only for the business community but also for competition authorities. Digitalization and the competitive assessment of the global Internet giants are currently one of the most important issues for competition authorities around the world. There are many new questions on how competition law should be enforced in these days of digital revolution.

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## The Emerging High-Court Jurisprudence On The Antitrust Analysis Of Multisided Platforms

By David S. Evans

Between September 2014 and September 2016 high courts in multiple jurisdictions released five decisions that address applying competition law to matchmakers that operate virtual or physical platforms for connecting multiple groups of customers. The decisions rely, directly or indirectly, on the economic literature on multisided platforms that commenced around 2000. The high courts all recognize that it is necessary to consider the several distinct groups of customers and their interactions in evaluating whether business practices are anti-competitive.

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## Coordinating Policies To Realize Benefits From The Digital Economy: The Case Of Mexico

By Martin E. Cave & Ernesto Flores-Roux

The degree to which digitization has penetrated most sectors of the economy makes it extremely difficult to quantify its reach. Can we clearly separate brick and mortar business and digital activity? Can we isolate digital advances in typical technological industries from those that apply in less affected industries? This article aims to describe the benefits which Mexico might gain by taking advantage of the opportunities of digitization, and to identify ways in which that performance might be improved by various public policy interventions.

# REACHING OUT IN 2017

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CPI wants to hear from you, our subscribers. In the coming months of 2017, we will be reaching out to members of our community for your feedback and ideas. Let us know what you want (or don't want) to see, at [antitrustchronicle@competitionpolicyinternational.com](mailto:antitrustchronicle@competitionpolicyinternational.com).

## CPI ANTITRUST CHRONICLE APRIL 2017

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The April 2017 Antitrust Chronicle will address issues related to **IP, Patent Holdup and Royalty Stacking in IT**. This edition will be presented in cooperation with Qualcomm and based in part on the Leadership Conference to be held in Washington, DC on March 27th, co-sponsored by CPI.

As a reminder to potential authors, our tentative topic for the May 2017 Antitrust Chronicle is **Antitrust and the Algorithm-Driven Economy**.

Contributions to the Antitrust Chronicle are about 2,500 – 4,000 words long. They should be lightly cited (follow bluebook style for footnotes) and not be written as long ponderous law-review articles with many in-depth footnotes. As with all CPI publications, articles for the CPI Antitrust Chronicle should be written clearly and with the reader always in mind.

Interested authors should send their contributions for the April edition by March 20, 2017 to Sam Sadden ([ssadden@competitionpolicyinternational.com](mailto:ssadden@competitionpolicyinternational.com)) with the subject line "Antitrust Chronicle," a short bio and picture(s) of the author(s).

The CPI Editorial Team will evaluate all submissions and will publish the best papers. Authors can submit papers in any topic related to competition and regulation, however, for the April and May issues, priority will be given to articles addressing the above-mentioned topic. Co-authors are always welcome.

## WHAT'S NEXT?

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This section is dedicated to those who want to know what CPI is preparing for the next month. Spoiler alert!

We look forward to bringing our subscribers the March Antitrust Chronicle of 2017 which will address **Recent Antitrust Developments in China**. This special issue will cover various topics including MOFCOM, SAIC and NDRC enforcement as well as private litigation in China.



## WITH FREDERIC JENNY



Thank you, Professor Jenny, for granting this interview to CPI.

### 1. In your view, what are some hot button issues or developments that will potentially shape the antitrust landscape in 2017?

The development of the digital economy and the growing importance of disruptive innovations create a challenge for competition authorities. As the rate of innovation accelerates, competitors may be using vastly different business models and be on different markets, markets may be multi-sided, etc... Hence there is a need for competition authorities to fine tune their enforcement instruments (to define markets, assess market power, evaluate pricing behaviors, anticipate disruptive innovations, etc...) to make them more relevant in the complex environment in which we live today. This is an urgent task as we already know that there are diverging approaches on the same cases across jurisdictions. The *Booking.com* case in Europe is an excellent example of a situation where different European competition authorities have had different views about the business model of online booking accommodations services which has led them to different conclusions about parity pricing mechanisms. This creates a legal uncertainty for firms and exposes the competition community to a risk of incoherence. While, the autonomy of each national competition authority should be protected, collective thinking about the challenges we face and exchanging experiences among competition authorities and economists could be helpful to promote a much desired soft convergence in enforcement.

The OECD has a vast program on the digital economy and as part of this large program, the OECD Competition Committee, with the help of academic economists and chief economists of competition authorities, will be investigating the ways in which traditional instruments used in enforcement can be adapted.

At the European level, I believe that the upcoming judgment on the *Intel* case by the European Court of Justice will be of great importance for the future of competition law enforcement in Europe. What is at stake is the relevance of economic analysis in European competition law enforcement.

### 2. The European Commission recently announced the final elements of its long-awaited Digital Single Market strategy for Europe (and May 2017 will mark the two-year anniversary of the initiative). Moving forward, how do you see the Digital Single Market strategy playing out? Any potential pitfalls?

Given the rapid development of the digital sector, one can only support the goals and ambitions of the Commission's digital single market agenda. However, one should not forget that the digital world is not only expanding rapidly but that it is also a sector characterized by innovations and rapidly changing services, products and business models. At any one time there is a wide diversity of actors competing with one other. Thus there is tension between the desire to adopt *ex-ante* regulations which will accelerate the achievement of the single market and the burden imposed by those regulations on platforms, online intermediaries, data and cloud computing and the collaborative economy players with a risk of thwarting innovative developments which may benefit consumers. It is not clear whether the Commission has sufficiently considered this tradeoff in its proposals and there is some concern that it may err on the side of too restrictive "one-size fits all" *ex-ante* regulations either where there is no discernible market failure or where market mechanisms could have developed innovative solutions to protect consumers. The issue of geo-blocking is, for example, clearly an issue where the desire to achieve the unique market may clash with perfectly legitimate reasons for service providers to price discriminate (such as differences in costs). The issue then is whether an *ex-ante* regulation is preferable to the use of competition law instruments to eliminate illegitimate geo-blocking.

### 3. Antitrust authorities are increasingly focusing on big data and its effects on competition and consumer choice. We have been talking about big data for almost two years, where do we stand now? Any progress?

There is indeed some pressure on competition authorities to tackle the possible competition issues related to big data. Part of this pressure arises from competition among competition authorities themselves because they want to be seen as innovative and relevant. But part of the pressure for competition authorities to intervene comes from public opinion, legislators, etc...

A number of approaches are being explored. Big data as an asset and the risks that the ownership of this asset or the conditions of access to this asset may constitute barriers to entry, privacy as an element of the quality of internet service which risks being degraded as the result of increased market power, big data as a vehicle for price discrimination, big data and artificial intelligence leading to the creation of pricing algorithms which are exploring profit maximizing strategies and may choose collusion, etc... The variety of approaches testifies to the fact that we are still struggling with the issue (or issues) of how to treat big data issues in competition law.

There are further questions about the legitimacy of considering privacy issues in the context of competition law and the proper interface between privacy laws and competition laws. We are still missing a unified intellectual framework to consider the interaction between big data and competition. We are also missing some of the tools which may be necessary to deal with quality as an element of economic performance in antitrust matters. Overall more questions are raised than answers provided.

**4. With the arrival of the President Trump Administration and the expected “Hard Brexit” looming, what are your initial thoughts on the outlook for antitrust enforcement in the U.S. and the EU? For instance, merger enforcement may not be as vigorous under the Trump Administration.**

I would not want to speculate on what the merger or antitrust enforcements are likely to be in the U.S. But I do think that the British have played a particularly important role on the EU competition scene and that there is a risk that Brexit will have a negative impact on competition law enforcement in the EU. Not only have the British consistently argued within the Commission for a more economic approach to competition law enforcement in the EU, but it is also noticeable that British judges in Luxemburg have played a particularly important role at the level of the European Court in promoting a better fit between legal and economic considerations in the jurisprudence on competition. Thus Brexit and the subsequent disappearance of British civil servants in the Commission and British judges on the European courts runs the risk of slowing down the modernization of competition law in Europe and of strengthening the camp of those who think that the promotion of consumer welfare was never intended to be the goal of European competition law enforcement and that the interpretation of European competition law should be informed by the goal of promoting the internal market.

**5. The OECD, as well as the ICN, plays an important role in promoting international cooperation in antitrust enforcement and best practices. On January 13, 2017, the DOJ and FTC issued their revised Antitrust Guidelines for International Enforcement and Cooperation. Where do you see room for improvement in the year ahead and where have international antitrust authorities made significant progress towards convergence, with particular focus on the U.S. and EU antitrust authorities? How do you see Donald Trump’s proposed policy of “America First” fitting in with this?**

First, I think that everybody would agree with the fact that competition laws throughout the world have significantly converged over the last decade and that international cooperation on antitrust (for example on cartel enforcement) or on merger enforcement has also developed considerably both among competition authorities of countries which have a long experience in antitrust or competition law and between those agencies and relative newcomers.

As a consequence, there is less tension between competition authorities than used to be the case in the 1990s. As the revised Antitrust Guidelines for International Cooperation on Enforcement indicate, the U.S. Antitrust agencies expect that conflicts of law will be “rare” as “more jurisdictions have adopted and enforce antitrust laws that are compatible with” U.S. law.

There is a great appetite for more cooperation between competition agencies and work on the ways to deepen international cooperation figures high on the agenda of both the ICN and the OECD. What we are looking for are new instruments to facilitate cooperation.

International cooperation on competition is always voluntary. Each national competition authority can decline to cooperate on a specific case but what we have witnessed a collective realization that cooperation is a positive sum game in the long run for the cooperating agencies. International cooperation is based on mutual trust and assistance among competition agencies. So Donald Trump’s policy of “America First” should not necessarily contradict the idea of pursuing international cooperation in the field of antitrust. By cooperating with other competition agencies, U.S. agencies will ensure that when the interests of U.S. consumers are threatened by foreign firms they will be in a better position to get those foreign authorities to cooperate.

**6. American and European regulators have set the path for other countries’ competition policies. Do you see the rising tide of nationalism personified in “America First,” Brexit and the far right movements across Europe influencing or antagonizing the antitrust agencies of BRICS (especially China) and other developing countries to the detriment of consumer welfare?**

One should be careful about asserting that American and European competition regulators have set the path for other countries’ competition policies.

First, a number of countries adopted a competition law because it was a requirement for the country to be able to enter into a bilateral trade agreement with the U.S. or the European Union or to join the WTO. In other words, trade policy rather than the experience of North American or European competition authorities has been the leading force behind the proliferation of competition laws.

Second, when adopting competition laws, developing countries have, for the most part, not copied U.S. and European laws but have adapted the instrument to their own needs, or their history or their strategic interests. China, for example, has adopted an Anti-Monopoly Law which, among other more classical goals, aims to promote the healthy development of the socialist market economy. In South Africa, one of the purposes of the Competition Act is the promotion of employment and the advancement of the social and economic welfare of South Africans. The competition law in Russia aims at curbing the economic power of administrative monopolies (which is a much wider concept than state owned enterprises).



Third, when it comes to enforcement, it is true that there is a great deal of convergence among competition authorities, thanks to the work done at the OECD and in the ICN, both on some procedural issues (for example on merger control) and on substantial issues (such as the importance of the fight against international cartels or the necessity to have a robust, economically based theory of harm in competition cases). However, there is less convergence on the enforcement of monopolization or abuse of dominance or dependency or even on vertical agreements provisions.

Finally, some countries, China in particular, aim at combining standard analysis and innovative remedies. So developing countries' competition authorities cannot be described as mere "followers" of the North Atlantic competition authorities.

America First, Brexit and the far right movements across Europe have less to do with competition law enforcement than with a concern about the destructive effect of international trade on the fabric of societies in the North Atlantic industrialized nations. But economic globalization and international trade are, in general, seen more positively in developing countries because there is a perception in those countries that they can contribute to economic development and poverty reduction.

International trade is based on mutual concessions since each nation state has the power to exclude or restrict foreign products or services competing with domestic products. So one can expect that in response to protectionist tendencies in some countries there will be retaliations in the form of further international trade restrictions by the targeted countries. This may well weaken competition in some markets. But I do not believe that it will have a lasting effect or that it will impact competition law enforcement. If a country wants to limit international trade it has much more direct and effective ways to do it than using competition law strategically. Furthermore, I am skeptical of the value of the evidence regarding the alleged strategic use of competition law enforcement in some developing countries. Just because most of the cartels sanctioned by the U.S. Department of Justice are foreign based does not mean that the U.S. DoJ strategically targets foreigners and ignores domestic cartels. I think that the same logic applies to the activities of competition authorities in the BRICS countries. The fact that the GAFAs or other powerful pharmaceutical firms of North American or European origin are the subject of competition investigations does not necessarily reflect a protectionist bias by the national competition authorities of the countries which investigate them.

What is most important to avoid deviant tendencies is to keep building up the consensus of competition authorities on the proper way to investigate mergers and alleged antitrust violations and to promote the idea that competition authorities should be independent and should act in a transparent manner. This is where international organizations such as the OECD, the ICN and UNCTAD have a crucial role to play.

# CHANGING TIMES? THE OUT LOOK FOR ANTITRUST ENFORCEMENT IN THE EU AND THE U.S.

BY RACHEL BRANDENBURGER<sup>1</sup>,  
LOGAN BREED<sup>2</sup>, HELEN BIGNALL<sup>3</sup>  
& PAUL CASTLO<sup>4</sup>



## I. INTRODUCTION

This article considers the outlook for antitrust enforcement in the EU and the U.S. in the next few years, and how Brexit and the new U.S. administration under President Trump could impact that outlook.

<sup>1</sup> Senior Advisor & Foreign Legal Consultant to Hogan Lovells U.S. LLP (Admitted in England & Wales).

<sup>2</sup> Logan Breed is a partner at Hogan Lovells in Washington, DC.

<sup>3</sup> Helen Bignall and Paul Castlo are both Counsel at Hogan Lovells in London.

<sup>4</sup> Following the judgment of the UK Supreme Court in *R (Miller) v. Secretary of State for Exiting the European Union*, handed down on January 24, 2016, the UK Parliament must first pass an Act authorizing the Government to give notice under Article 50.

## II. THE EU – THE POTENTIAL IMPACT OF BREXIT

Like many aspects of life in Europe, antitrust enforcement in 2017 to 2020 will take place against the backdrop of the UK's exit from the EU ("Brexit"). It is impossible to discuss developments in EU competition law enforcement over the next few years and beyond, as this article seeks to do, without taking account of the impact that Brexit could have.

### A. The UK's Negotiating Aims

The UK Government intends to trigger the Article 50 procedure under the Treaty on the Functioning of the European Union before the end of March 2017, beginning a two year period of negotiations.

Precisely what relationship the UK will have with the EU after Brexit will not be known for some time. But on January 17, 2017, the UK Prime Minister said that the UK would not be seeking continued membership of the EU:

European leaders have said many times that membership means accepting the '4 freedoms' of goods, capital, services and people. And being out of the EU but a member of the single market would mean complying with the EU's rules and regulations that implement those freedoms, without having a vote on what those rules and regulations are. It would mean accepting a role for the European Court of Justice that would see it still having direct legal authority in our country.  
[...]

So we do not seek membership of the single market. Instead we seek the greatest possible access to it through a new, comprehensive, bold and ambitious free trade agreement.<sup>5</sup>

In addition, she said that the EU Courts would not have jurisdiction in the UK after Brexit but that the substance of EU law would apply until specifically amended or repealed:

... we will convert the 'acquis' – the body of existing EU law – into British law.

This will give the country maximum certainty as we leave the EU. The same rules and laws will apply on the day after Brexit

<sup>5</sup> The government's negotiating objectives for exiting the EU: PM speech, January 17, 2017, retrieved from: <https://www.gov.uk/government/speeches/the-governments-negotiating-objectives-for-exiting-the-eu-pm-speech>.

as they did before. And it will be for the British Parliament to decide on any changes to that law after full scrutiny and proper Parliamentary debate.<sup>6</sup>

If the UK Prime Minister is successful in achieving this aim, Brexit could have a significant impact on competition law enforcement in the EU.

### **B. Antitrust Investigations**

In relation to antitrust (i.e. cartel and conduct) investigations, one significant change would be that the UK competition agencies<sup>7</sup> would be able to conduct their own investigations in parallel with those carried out by the European Commission (“Commission”).

This could complicate matters for both companies subject to investigations and agencies. Of course, parallel investigations of the same conduct by multiple antitrust agencies are not unusual. But post-Brexit, the UK will be an additional jurisdiction, and a UK antitrust investigation an additional investigation, in the multi-national world of enforcement.

The scale of this potential doubling-up is demonstrated by looking at the 28 cartel decisions adopted by the Commission since 2012: seven related to conduct expressly affecting the UK; and 17 related to conduct stated to be EEA or worldwide in scope – so including the UK.<sup>8</sup> In the last four years alone, the Commission has reached a decision in 24 cartel cases that, after Brexit, the UK agencies could have jurisdiction to consider in whole or in part.

In any event, just because the UK competition agencies may have jurisdiction to investigate conduct, that does not mean they will choose to exercise that jurisdiction or have the resources to be able to do so. As a result, although there may be parallel investigations in some cases, this may not happen in all cases.

### **C. On-going Commission Cases**

What about the Commission’s pipeline of cases? There are likely to be antitrust investigations with a UK nexus already underway that are not completed before Brexit. Also, ahead of Brexit, the Commission may have to decide whether to start any new cases where the main focus of the anti-competitive activity is the UK. There are a number of possibilities, including:

- The Commission could decide to continue on-going investigations after Brexit on the basis that it had jurisdiction when the relevant

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<sup>6</sup> Ibid.

<sup>7</sup> In addition to the main UK competition agency, the Competition and Markets Authority, certain sectoral regulators have competition law enforcement functions in the UK.

<sup>8</sup> The European Economic Area comprises the 28 Member States of the EU plus Iceland, Lichtenstein and Norway.

conduct took place. In other words, it may assert jurisdiction even where the conduct would not have affected trade between EU Member States after Brexit because the UK is no longer an EU Member State.

- Where a Commission investigation is on-going, in the absence of transitional arrangements to the contrary, the UK competition agencies could start a parallel investigation the day after Brexit.

### **D. Impact on Leniency**

A further element of uncertainty may result from the interplay between leniency, enforcement and damages claims. Post Brexit, a court in the UK may take a less sympathetic view to parties seeking to withhold Commission leniency documents from disclosure – on the basis that the effectiveness of the Commission’s leniency regime may no longer be a concern to courts as they would no longer have a duty of sincere co-operation.<sup>9</sup> This could affect current Commission investigations on-going after Brexit, as well as those initiated post-Brexit.

All of this creates the conditions for potential confusion, uncertainty and jurisdictional turf wars in European competition law enforcement over the coming years. Much will depend on the nature and extent of co-operation between the UK competition agencies, the Commission and other agencies around the world where more than one agency is investigating the same matter. However, there is no reason to believe that such co-operation will work any less well than it has in very many cases over the past several years between, for example, the Commission and the U.S. Department of Justice (“DOJ”) and Federal Trade Commission (“FTC”).

### **E. Merger Control**

As to merger control, the biggest practical impact is likely to be on the “one-stop shop” because the arrangement whereby the national competition agencies of EU Member States do not review a transaction being reviewed by the Commission in Brussels would no longer apply in the UK.

Also no longer applicable to the UK would be a number of mechanisms designed to ensure that the best-placed authority in the EU reviews mergers, including the ability of the Commission to refer cases to the UK and *vice versa*, and the “two-thirds rule” which provides that in cases where all of the parties to the merger derive two-thirds or more of their EU-wide revenues from the same EU Member State the merger does not have to be notified to Brussels.

In broad terms, post-Brexit:

- Some mergers which are reviewable by the Commission may also be reviewable, and reviewed, in the UK as well as in Brussels.

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<sup>9</sup> Article 4(3) Treaty on European Union.

- Some mergers involving UK parties or markets may fall below the EU thresholds for review and therefore not need to be reviewed in Brussels, given that UK turnover would not count towards the EU thresholds. This could result in more notifications in individual EU Member States, or maybe more references to Brussels by parties to mergers that are notifiable in three or more remaining EU Member States. In other words, the impact may not be limited to the UK and Brussels – and there may be somewhat of a rebalancing of the national and supranational regimes across the EU. It could also trigger a reassessment of the thresholds under the EU Merger Regulation.

- Conversely, some mergers that would not today be notified to the Commission because the parties' UK revenues trigger the "two-thirds rule" may become reviewable in Brussels.

This may give rise to some practical difficulties. The EU and UK merger control regimes are not designed to be run in parallel and doing pan-European deals may take longer and become more expensive. As with antitrust investigations, much will depend on the extent of co-operation between the agencies. Again, there is no reason to believe that such co-operation will work any less well than co-operation between, for example, the Commission and the U.S. antitrust agencies.

Another way in which Brexit could have an impact on the outlook for merger control in the EU is on the role of the public interest in merger reviews. There has been some speculation that the UK may move towards a regime where the public interest plays a greater role in merger review.<sup>10</sup> It seems other EU Member States may also want to give a greater role to public interest considerations, either at the EU-wide or individual Member State level. For example, President Hollande of France has reportedly said that the EU's competition laws should be "adapted" to enable Europe to produce "global leaders" and "support both... public and private investments."<sup>11</sup> Thus, the way ahead may be influenced by the outcome of the French election in May 2017, and maybe also by other elections due in EU Member States this year, and not only by the outcome of the UK referendum last year.<sup>12</sup>

### III. MEANWHILE IN THE EU...

The next few years will not only be about Brexit.

In the first part of her term, Commissioner Vestager has shown that she does not shy away from investigations involving "big name" companies including Google and Gazprom. There has also been a

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10 See House of Commons Library Briefing Paper Number 05374, Mergers & takeovers: the public interest test, September 1, 2016.

11 MLex, Hollande says competition rules need "adapting" under post-Brexit priorities, June 29, 2016

12 In addition to the French Presidential election, there are pending national elections in Germany and the Netherlands in 2017.

string of high profile State aid decisions finding that EU Member States have made illegal tax benefits available to a number of large U.S. and other companies which the Commission requires be repaid.

There is nothing to suggest that the rest of Commissioner Vestager's term will be less eventful. Indeed, the Commission's Work Programme for 2017 emphasizes that the Commission will continue to focus on the "big things."<sup>13</sup>

#### A. Damages Directive

The deadline to implement the 2014 Damages Directive by December 27, 2016 was met by only a handful of Member States despite Commissioner Vestager's call in November for a "final push" to meet it. In practice, the Commission is unlikely to initiate lengthy court proceedings against the "late" Member States, although it could threaten to do so to speed things up.

The proposal for a Directive was part of Vice President Almunia's legacy, an objective which he said he "did not spare any efforts to achieve" and which would "establish a higher and more level legal ground in the EU" to facilitate private damages actions by the victims of competition law infringements.<sup>14</sup>

Will the Directive reduce the amount of forum-shopping seen today? In the short to medium-term at least, a dramatic shift in cases away from the UK, Germany and the Netherlands is unlikely. These have developed reputations as the go-to jurisdictions for private damages actions to date. Judges and lawyers have developed expertise and, most importantly, there is a body of case law that provides some predictability on certain issues – something that is important to a would-be claimant.

Although the Directive has clarified the law in some respects, it also creates new uncertainties. There is an expectation that some Member States will seek guidance on how to interpret certain aspects of the Directive from the Court of Justice of the European Union ("CJEU"). The number of CJEU references may depend on the level of detail the Commission chooses to include in the guidelines that it is required to publish (although without a specified deadline, it is not clear when). Therefore, there could be some further delay before the realization of what Vice President Almunia described as a "milestone in the evolution of competition law enforcement in the EU."<sup>15</sup>

It will also be interesting to see whether the Commission will take further action in the context of facilitating collective redress

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13 Commission Communication – Commission Work Programme 2017, Delivering a Europe that protects, empowers and defends, COM (2016) 710 final, 10.25.2016.

14 Speech by Joaquín Almunia on Antitrust damages in EU law and policy at the College of Europe GCLC annual conference, November 7, 2013.

15 Speech by Joaquín Almunia on Antitrust damages in EU law and policy at the College of Europe GCLC annual conference, November 7, 2013.

schemes. In its 2013 Recommendation, the Commission invited Member States to introduce collective redress mechanisms. The Commission has stated that it will assess the implementation of the Recommendation and, if appropriate, propose further measures by the end of July 2017.<sup>16</sup>

## ***B. Effective Enforcement at Member State Level***

The results of the Commission's consultation (initiated by Commissioner Vestager last year) on the effectiveness of competition authorities' enforcement powers at Member State level are likely to be published shortly. The Commission is considering framework legislation to be proposed in June 2017 (likely another Directive).<sup>17</sup> Issues for consideration include whether leniency material is sufficiently well protected and whether whistleblowers should be protected from criminal sanctions in certain Member States.

## ***C. An Increasingly Digital World***

One of the key themes in the rest of Commissioner Vestager's term will be the role of competition law in the context of e-commerce.

### *1. E-commerce*

The Commission's final report following its e-commerce sector inquiry is due in the first half of this year.

In September last year, the Commission published its provisional findings highlighting business practices that could limit online competition. In relation to distribution agreements, the Commission received responses indicating that retailers were subject to various restrictions in the context of online sales, including being restricted from selling online at all. According to the Commission, these restrictions "may, under certain circumstances, make cross-border shopping or online shopping in general more difficult and ultimately harm consumers by preventing them from benefiting from greater choice and lower prices in e-commerce."<sup>18</sup>

The EU official leading the e-commerce inquiry, is reported to have said that once the sector inquiry final report has been published, "the Commission 'will take more interest' in restrictions imposed in distribution agreements, 'especially when it comes to cross-border' commerce."<sup>19</sup> The Commission has already opened a

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16 Commission Recommendation on common principles for injunctive and compensatory collective redress mechanisms in the Member States concerning violations of rights granted under Union law – June 11, 2013 (2013/396/EU).

17 Commission Communication – Commission Work Programme 2017, Delivering a Europe that protects, empowers and defends, COM(2016) 710 final, 10.25.2016, page 8 and Annex 1, page 3.

18 European Commission press release, IP/16/3017, September 15, 2016.

19 Thomas Kramler speaking at a conference in Brussels on November 29, 2016, as reported by MLex on the same day.

new investigation into whether consumer electronics manufacturers have restricted the ability of online retailers from setting their own prices for widely used consumer electronics products.<sup>20</sup> More cases may follow at both Commission and Member State levels.

Businesses should keep in mind Commissioner Vestager's comments at a stakeholder conference last year. She said she does not "want to tell businesses how to distribute their products. It just means that however they choose to do it, it shouldn't harm competition, and deny consumers the benefits they expect. The idea of this inquiry is to make sure we get that balance right."<sup>21</sup>

### *2. Geo-blocking*

The Commission has also focused its e-commerce inquiry on the issue of geo-blocking (attempts to restrict cross-border sales, for example by restricting sales based on a consumer's address or credit card details) which it has said could restrict competition.<sup>22</sup> This follows the Commission's issues paper published on March 18, 2016 which found that the practice was widespread in the EU. The Commission already has a pending investigation against Sky UK and six major U.S. film studios, a case which Commissioner Vestager recently described as being "about a fundamental principle of the European Union – that businesses must not sign contracts that recreate unjustified barriers between European countries."<sup>23</sup> The Commission has also just opened two new investigations. One relates to whether consumers are restricted on the basis of their location or country of residence in relation to their online purchase of video games. The other concerns agreements between hotels and tour operators which may discriminate between customers based on their nationality or country of residence.<sup>24</sup>

As part of its Digital Single Market Strategy, the Commission adopted a proposal in May 2016 for a Regulation to address unjustified geo-blocking as part of a package of reforms to facilitate e-commerce across the EU. Legislation in this area therefore seems likely.

### *3. Third Party Platforms*

As part of its e-commerce sector inquiry, the Commission has also considered whether online marketplace restrictions (for example when a manufacturer restricts a retailer from selling on third party

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20 European Commission press release – Commission opens three investigations into suspected anticompetitive practices in e-commerce, February 2, 2017.

21 Speech by Margrethe Vestager on October 6, 2016: E-commerce: A Fair Deal for Consumers Online.

22 European Commission press release, IP/16/3017, September 15, 2016.

23 Speech by Commissioner Vestager – Celebrating European Culture, An Evening with Nordic Drama, Brussels, January 24, 2017.

24 European Commission press release – Commission opens three investigations into suspected anticompetitive practices in e-commerce, February 2, 2017.

platforms such as Amazon and eBay) are acceptable. In its provisional assessment, the Commission refers to the interpretation of its own guidelines on the issue as well as the debate at Member State level. Its preliminary findings are that marketplace bans do not amount to a *de facto* prohibition to sell via the Internet and that their impact together with the potential justifications and efficiencies for them vary according to the type of product as well as the particular features of a marketplace.

The Higher Regional Court in Frankfurt has referred several questions to the CJEU in the Coty case regarding third party platform restrictions in the context of a selective distribution system. The CJEU's preliminary ruling may provide clarity on this increasingly important area of law in due course.

#### 4. Parity Clauses

The Commission has also focused its e-commerce sector inquiry on parity clauses (or most-favored-nation clauses) in agreements between retailers and marketplaces. These typically require the retailer to sell on the marketplace (or list on a price comparison tool) at the lowest price and/or on the best terms offered either on the retailer's own website or on other marketplaces. This kind of clause has been under the spotlight at EU level (the e-book cases) and at national level where there have been divergent approaches (online hotel booking cases). The Commission has provisionally concluded that these clauses need to be analyzed on a case-by-case basis, but hopefully its final report will provide some clarity.

#### 5. Merger Control Thresholds

The Commission is considering whether to make changes to its jurisdictional thresholds to capture important mergers in sectors like digital services and pharmaceuticals, where the relevant businesses' turnover is not yet sufficiently high to trigger an EU level review. This proposal stems in part from the *Facebook/WhatsApp* merger which did not meet the EU Merger Regulation thresholds (even though the Commission did ultimately review it following a referral request). The consultation period closed on January 13, 2017.

#### D. Google

The Commission has three open investigations against Google:

- Comparison shopping: Google received a supplementary Statement of Objections in July last year (having received the initial Statement of Objections in April 2015) setting out allegations that Google is abusing its dominant position by favoring its own shopping comparison services through its search results. There is speculation that the Commission could issue a decision this year following a five year investigation.
- Mobile devices: In April 2016, the Commission sent a statement of objections to Google alleging that it has imposed restric-

tions on Android device manufacturers and mobile network operators to protect and strengthen its dominant position in relation to Internet searching.

- Search advertisements (the *AdSense* case): In July 2016, the Commission issued a Statement of Objections alleging that Google is protecting its dominant position by restricting the ability of third party website providers to display search advertisements from Google's competitors.

Commissioner Vestager has cited the Google investigations as examples of the need for the Commission to take evidence-based decisions: "The reason why we're investigating Google is very simple. It's because the evidence has led us to the initial view that its actions may have harmed competition. So we'd be failing in our duty if we didn't take a very close look."<sup>25</sup>

#### E. Gazprom

Commissioner Vestager made a similar point soon after she assumed office when the Commission issued a statement of objections against Gazprom in 2015 alleging it had abused its dominant position by restricting the flow of gas, partitioning the Central and Eastern European upstream gas markets and using unfair pricing. Commissioner Vestager is reported as having said that "the decision to bring charges was an independent one based purely on law enforcement, which treats Gazprom the same as any other company..."<sup>26</sup> It has been reported that settlement discussions with the Commission are underway.<sup>27</sup> So a resolution may be forthcoming in the next year or so.

#### F. State Aid

Commissioner Vestager has also emphasized the need for impartiality in the context of the recent State aid decisions: "The same goes for all the companies . . . If they've received illegal State aid from an EU country, they need to pay it back, no matter where the company comes from. It's the only way to enforce our rules impartially."<sup>28</sup>

These cases are politically charged: in its August 2016 White Paper, the U.S. Treasury Department stated that "The Commission's new interpretation of State-Aid doctrine threatens to undermine the well-established basis of mutual cooperation and respect that many countries have worked hard to develop and preserve." The pending appeals in several of these cases, which argue that the Commission

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25 Speech by Margrethe Vestager at the UCL Jevons Institute Conference, June 3, 2016.

26 Financial Times – Brussels risks Russian ire with Gazprom antitrust case, April 21, 2015.

27 Mlex – Gazprom submits offer to settle EU antitrust probe, December 27, 2016.

28 Speech by Margrethe Vestager at the UCL Jevons Institute Conference, June 3, 2016.

has deviated from well-established case law, will be closely followed over the coming years.

### G. Intel

The CJEU's judgment in the *Intel* case is likely to be handed down this year. Intel will have been buoyed by Advocate General Wahl's opinion that the EU General Court was wrong to uphold the Commission's decision that Intel abused its dominant position by offering rebates to computer manufacturers for its semiconductors.<sup>29</sup> If the CJEU were to follow the AG's opinion, it would mark a major shift in the EU Courts' position on rebates.

### H. Mega-mergers

At the end of last year, the Commission's Deputy Director General for mergers emphasized the risks associated with concentration in globalized markets. He said merger case handlers need to be "particularly vigilant" regarding transactions that result in "restructurings of global industries that lead to divestitures to eliminate overlaps in different jurisdictions."<sup>30</sup> These comments followed the Commission's review of the *AB InBev/SABMiller* merger last year and were made while the Commission is currently investigating three global mergers in the agri-chemicals sector: *Dow/Dupont*, *ChemChina/Syngenta* and *Bayer/Monsanto*.

The nature and extent of cooperation between the competition authorities in different jurisdictions is particularly important in this context. Commissioner Vestager recognizes this. In the middle of last year, she commented that competition authorities "do not have magic solutions," but that "we can do our bit: to help create fair conditions in markets," whether through merger control or the enforcement of the antitrust rules in the context of cartels and companies which have abused their market power. And the "secret weapon?" "... cooperation and enforcement on a global scale."<sup>31</sup>

## IV. THE U.S.

### A. Cartel Enforcement

No matter who President Trump selects to head the DOJ Antitrust Division, cartel enforcement will likely remain vigorous over the next few years. Both Democratic and Republican administrations have supported aggressive cartel prosecution for the past several decades, including frequent substantial prison sentences for individu-

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29 Opinion of Advocate General Wahl in Case C-413/14 P *Intel Corporation Inc. v. Commission*, October 20, 2016; Judgment of the EU General Court - Case T-286/09 *Intel Corporation Inc. v. European Commission*, June 12, 2014, Commission Decision COMP/C-3/37.990 - *Intel*, May 13, 2009.

30 Carles Esteva Mosso speaking at a conference in Brussels on December 7, 2016, as reported in MLex the same day.

31 Speech by Margrethe Vestager at the UCL Jevons Institute Conference, June 3, 2016.

als and increasingly large fines for corporations. President Trump's transition team appointments, David Higbee and Joshua Wright, indicate this trend is likely to continue. During Higbee's time at DOJ, the agency consistently emphasized cartel enforcement as its highest priority. Wright wrote a letter to the U.S. Sentencing Commission in 2014 advocating for the "Commission to consider increasing the prescribed range of jail sentences and to consider as well other individual sanctions, including enhanced individual fines and, insofar as the law allows, disqualification from holding fiduciary positions for a period of years."<sup>32</sup> President Trump's nominee for Attorney General, Alabama Senator Jeff Sessions, also has demonstrated an interest in cartel enforcement. During his time in the Senate, he supported legislation to enhance DOJ's leniency program for companies that self-report cartel activity to DOJ.

### B. Merger Control

The Trump administration's likely approach to merger control is much less clear. While President Trump has raised the possibility of antitrust enforcement against deals such as *AT&T/Time Warner* and *Comcast/NBCU*, Republican antitrust enforcement of the prohibition on mergers that may tend to substantially lessen competition, Clayton Act Section 7, has traditionally been somewhat less aggressive than under Democratic administrations.

As an FTC Commissioner, Wright was more willing to accept merging parties' efficiencies arguments in some cases than his Democratic colleagues, and he did not support the FTC litigating or imposing remedies in merger cases where the harm to consumers was not abundantly transparent. For example, in his dissenting statement regarding the *Nielsen/Arbitron* transaction, Wright wrote that "when the Commission's antitrust analysis comes unmoored from ... fact-based inquiry, tethered tightly to robust economic theory, there is a more significant risk that non-economic considerations, intuition, and policy preferences influence the outcome of cases."<sup>33</sup> The new administration may also be less likely to challenge transactions involving claims such as loss of potential competition or harm to innovation. In any event, the new leaders of DOJ and FTC will assume their positions with several significant merger cases pending, including the *Anthem/Cigna* health insurance deal, a possible appeal of the *Aetna/Humana* case, and multiple hospital mergers, as well as looming decisions on high-profile transactions such as *AT&T/Time Warner*, *Monsanto/Bayer*, *ChemChina/Syngenta* and *Dow/Dupont*, so it will quickly be seen how aggressively the new administration intends to enforce Section 7.

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32 See: [http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-comment/20140729/Ginsburg\\_Wright.pdf](http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-comment/20140729/Ginsburg_Wright.pdf).

33 See: [https://www.ftc.gov/sites/default/files/documents/public\\_statements/dissenting-statement-commissioner-joshua-d.wright/130920nielsenarbitron-jdwstmt.pdf](https://www.ftc.gov/sites/default/files/documents/public_statements/dissenting-statement-commissioner-joshua-d.wright/130920nielsenarbitron-jdwstmt.pdf).

### C. Unilateral Conduct

Republican antitrust enforcers have tended not to focus aggressively on unilateral conduct because of the difficulty in distinguishing between legitimate vigorous competition and anticompetitive exclusionary conduct. The previous Republican administration under George W. Bush issued a report raising the bar for DOJ unilateral conduct cases. The Obama administration rescinded the report on taking office in 2009, but the new administration could restore it. Trump advisor Wright generally expressed more skepticism on unilateral enforcement cases than his Democratic colleagues, particularly in the context of the use of FTC Act Section 5. Another Trump administration advisor who is reportedly playing a role in vetting candidates for the next leaders of the FTC and DOJ Antitrust Division, billionaire venture capitalist Peter Thiel, penned an essay in the Wall Street Journal in 2014 titled “Competition is for Losers” in which he extolled the benefits of monopolies, claiming that they are “not a pathology or an exception. Monopoly is the condition of every successful business.”<sup>34</sup>

One case that will be interesting to see develop in the next year or so is the FTC’s complaint against Qualcomm. This was filed in federal district court just days before President Trump’s inauguration. The FTC alleged that Qualcomm “used its dominant position as a supplier of certain baseband processors to impose onerous and anticompetitive supply and licensing terms on cell phone manufacturers and to weaken competitors.”<sup>35</sup> Specifically, the FTC alleged that Qualcomm (1) maintained a “no license, no chips” policy under which it supplies its baseband processors only to cell phone manufacturers that agree to Qualcomm’s preferred license terms; (2) refused to license standard-essential patents to competitors; (3) extracted exclusivity from Apple in exchange for reduced patent royalties. The FTC claimed that these activities violated Section 5 of the FTC Act, which prohibits unfair methods of competition. It is highly unusual for the FTC to make a “standalone” Section 5 claim (i.e. a Section 5 case that does not also involve a violation of Sherman Act Section 1 or 2) in a competition case. Commissioner Ohlhausen, who has been named the acting FTC Chairwoman by the Trump administration, dissented and stated that this was “an enforcement action based on a flawed legal theory (including a standalone Section 5 count) that lacks economic and evidentiary support, that was brought on the eve of a new presidential administration, and that, by its mere issuance, will undermine U.S. intellectual property rights in Asia and worldwide.”<sup>36</sup> The suit was filed in federal district court in California, rather than in an administrative proceeding at the FTC, which will make it more difficult for the incoming Trump adminis-

tration to withdraw the action, although Commissioner Ohlhausen reportedly is considering whether to press the FTC to drop the suit.<sup>37</sup>

### D. Other Considerations

Another consideration that could become significant over the next four years is the opportunity the Trump administration will have to appoint at least one – and possibly more – Supreme Court justices, as well as a significant number of lower court appointments. There are no antitrust cases pending at the Supreme Court in the current Term, but future Terms may decide cases involving important issues such as “reverse payment” patent settlements, extraterritorial application of U.S. antitrust law and class certification in antitrust cases. Republican Supreme Court appointees have generally been more deferential to defendants in antitrust cases, with a series of cases over the last twenty years making it more difficult for antitrust plaintiffs to win antitrust judgments.<sup>38</sup>

Finally, it is not clear how the Trump administration will approach international antitrust cooperation and competition advocacy abroad over the next four years. Trump’s campaign rhetoric and his post-election comments have frequently eschewed traditional foreign policy positions. His positions on numerous issues have implied a retreat from international cooperation with traditional allies and organizations such as NATO as well as international trade agreements such as NAFTA. These comments raise the possibility that the Trump administration may adopt an isolationist posture rather than continuing the United States’ traditional role as a strong advocate for the view that the antitrust laws should be used only to protect consumers from conduct that threatens to stifle competition and innovation, with the DOJ and FTC being active participants in the global antitrust policy and enforcement dialogue.

## V. CONCLUSION

Antitrust policy and enforcement faces extraordinary challenges and uncertainties in the EU and the U.S. in the coming few years. These are indeed changing times, but to what extent and in what direction or directions is less easy to forecast.

34 Peter Thiel, “Competition is for Losers,” Wall Street Journal, Sept. 12, 2014, available at: <https://www.wsj.com/articles/peter-thiel-competition-is-for-losers-1410535536>.

35 See: <https://www.ftc.gov/news-events/press-releases/2017/01/ftc-charges-qualcomm-monopolizing-key-semiconductor-device-used>.

36 See: [https://www.ftc.gov/system/files/documents/cases/170117qualcomm\\_mko\\_dissenting\\_statement\\_17-1-17a.pdf](https://www.ftc.gov/system/files/documents/cases/170117qualcomm_mko_dissenting_statement_17-1-17a.pdf).

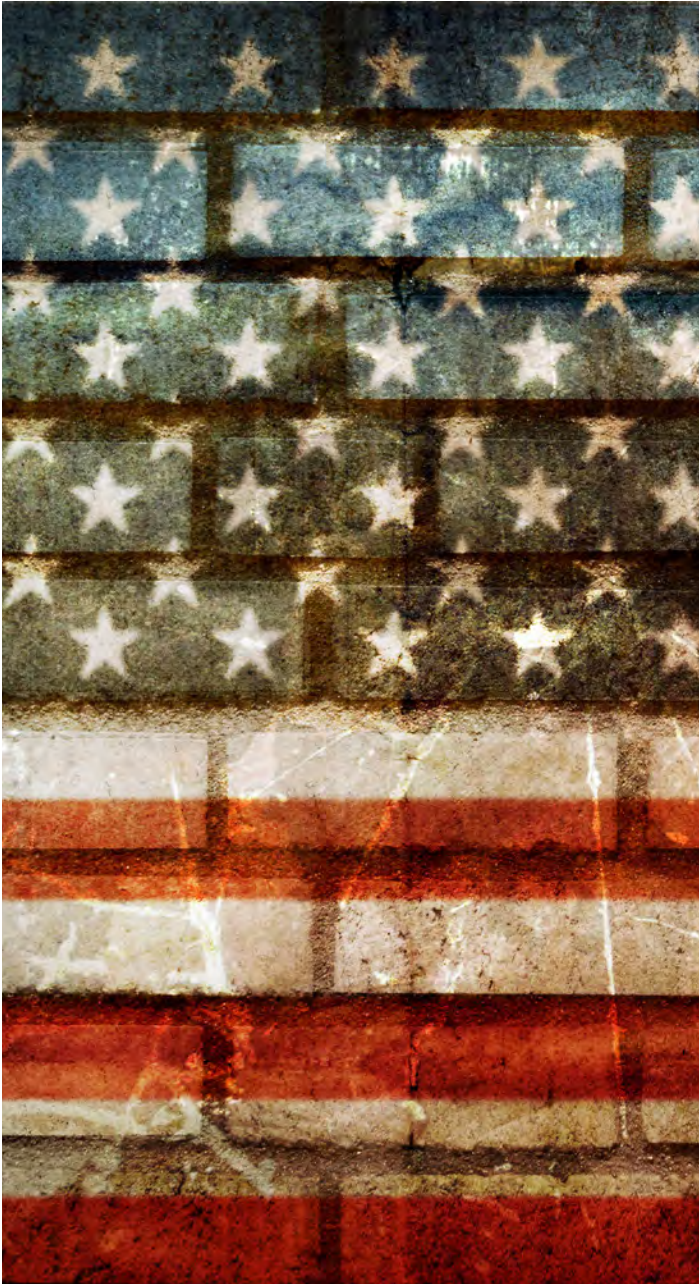
37 See: <http://www.mlex.com/GlobalAntitrust/DetailView.aspx?cid=860400&siteid=191&rdir=1>.

38 See, e.g. *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007) (creating a new, stricter standard of specificity required to plead a proper Sherman Act conspiracy).



# AMERICA-FIRST ANTITRUST

BY ELEANOR M. FOX AND HARRY FIRST<sup>1</sup>



## I. INTRODUCTION

“From this moment on, it’s going to be America First.” So spoke Donald J. Trump in his inaugural address as President of the United States.

What is America-First antitrust? America First means nationalism, which of course extends beyond America. Nationalism is the watchword of Brexit and of any number of political parties in Europe that might soon come to power. The new Administration appears to embrace these trends, while at the same time criticizing what it sees as nationalistic policies of our trading partners, particularly China, but Japan and Korea as well.

We see America-First antitrust playing out in the following ways:

1. Making deals: forgoing good antitrust in exchange for promises to invest in America;
2. Applying U.S. antitrust laws more aggressively against foreigners or applying them in disregard of foreign sovereigns’ legitimate interests;
3. Allowing antitrust transgressions by American firms that hurt only foreigners;
4. Using antitrust enforcement as a hook to get concessions from foreign firms that will help America; and
5. Fighting, at the highest levels, foreign use of antitrust that hurts American firms, and broadly accusing the foreign antitrust agencies of misapplication and discrimination.

## II. FLESH ON THE BONES OF AMERICA-FIRST ANTITRUST

America-First antitrust can produce some mixed results; but the principle compromises antitrust and the results are mostly bad.

*Making deals:* Making deals is about process. It means that the Executive as businessman cuts through the facts and makes trade-offs he thinks are good for America. Results matter, principles do not. Even before Donald Trump took the oath of office, he met with the CEOs of Bayer and Monsanto, hopeful partners to the biggest ever agribusiness merger, to strike a deal on jobs and investment in the United States at the same time that the Department of Justice was reviewing their merger. The press speculated that favorable treatment of the merger was implied in return.

<sup>1</sup> Eleanor M. Fox is Walter J. Derenberg Professor of Trade Regulation at New York University School of Law. Harry First is Charles L. Denison Professor of Law at New York University School of Law. The reader may note some resemblance of fact situations to actual cases. We have drawn fact patterns from real cases but have sometimes taken the liberty to alter the facts, so all fact situations should be regarded as hypothetical.

*More aggressive enforcement against the foreigners.* Under America-First antitrust, we can imagine a world in which the Department of Justice sues the Chinese solar panel manufacturers in antitrust for their low American prices, alleging a conspiracy even if there is no evidence of one, and threatens them until they raise their prices. We can imagine a world in which the Department of Justice sues Samsung or Huawei for refusing to license patents at reasonable prices to American manufacturers, while asserting when tables are turned that price levels are a matter for the market and contract, not antitrust.

These cases involve the substance of the law. Other scenarios involve the geographic reach of the law. Firms in Japan and Korea fix prices of liquid crystal display panels, which they sell to Chinese subsidiaries of Motorola Mobility; the Chinese subsidiaries incorporate the panels into smart phones and sell the finished products to Motorola Mobility U.S. and the world at large. Can U.S. antitrust reach the price-fixers? America-First antitrust would have no doubt that it can.

*Enforcement when sovereigns claim their interests are at stake.* State-involved restraints suggest another application. Would America-First antitrust challenge OPEC? The OPEC nations and their oil firms have been protected from the market for almost 60 years by the most open notorious cartel in the world. The NOPEC bills (“No Oil Producing Export Cartels”) would have authorized the Executive to sue to enjoin OPEC. The OPEC nations clung to assertions of sovereignty. America-First antitrust (and Donald Trump before he was president) support the bill.

Would America-First antitrust bow to China’s attempt to shield Chinese manufacturers’ price-fixing into America? Chinese vitamin C producers admittedly fixed prices into the United States, allegedly raising prices by more than 100 percent. The Chinese Ministry averred in the U.S. court proceedings that it ordered the companies to set their export price, and thus that the companies should have the benefit of the foreign sovereign compulsion defense. The same Ministry averred in the WTO – wherein it undertook not to distort export trade – that it gave no such order. America-First antitrust would disregard the Ministry’s claim, preferring to protect American buyers rather than to defer to China’s assertions of sovereignty.

*Allowing antitrust transgressions by Americans that hurt only or especially the foreigners.* Suppose American alkali companies fix export prices. The behavior is the worst antitrust restraint, by international consensus – but it hurts only foreigners. America-First antitrust does not care about foreigners. In fact, that strategy is good; American companies profit.

Or suppose a big merger creates a U.S. national champion in passenger jet aircraft. The merger might create market power and ultimately raise the cost of air travel, but U.S. antitrust authorities approve it because America and its champion win (in profits and power) more than American consumers lose.

*Antitrust as a hook to get concessions that will help America.* China may already have written the playbook. There is a merger that requires U.S. clearance. It is a rich deal, and the companies will do what is necessary to get clearance. The merging companies are foreign and they hold less than 10 percent of any market – but they have something the U.S. wants – important natural resources. The U.S. enforcers bargain for a promise that the firms will sell a mineral plant abroad to a U.S. buyer and will promise to supply the needs of U.S. buyers of the mineral for 20 years.

*Fighting foreign suits against U.S. firms, especially high tech and big data firms and firms that own important intellectual property.* Perhaps suits are brought by the competition authorities in China, Korea or Europe. America-First antitrust will attack and discredit the suits, and charge the foreign competition authorities with discriminating against U.S. firms and illegitimately pursuing industrial policy, not antitrust.

### III. WHAT WOULD NATION-BLIND ANTITRUST DO?

As we have signaled, America-First antitrust outcomes are not 100 percent bad. They sometimes map on to principled antitrust; but not usually. When they do, it is just by chance. This happy convergence occurs when the enforcement is against foreign firms that have harmed U.S. competition but firms might, under current principles, successfully argue for exemption. It may occur also when U.S. firms are in fact the targets of discrimination and excessive unprincipled application of foreign antitrust law. In this section we revisit our list of America-First applications.

Making deals without transparency or process is all bad. Anti-competitive mergers might get approved in return for promises of jobs and investment, and procompetitive deals might be disfavored. CEOs who stand by their rights to get cheaper production abroad (and their firms and customers) might get punished. The Executive is likely to make big decisions without critical facts and without the advice of technical experts. Cronyism and private interests might creep in undetected. The rule of law will be compromised. Even if one should believe in trading off competition for jobs, who will know if jobs will really be saved, and who will calculate the costs of saving them?.

The double standard (more aggressive antitrust against foreigners) is all bad. It compromises the rule of law. It sells American consumers short. It is a lightning rod for retaliation, perhaps in the form of tit for tat. And it teaches the wrong lesson to competition enforcers abroad who are fighting for competitive markets and see U.S. process and standards as an example.

On the other hand, extraterritorial reach to condemn foreign actors who hurt American competition is not in essence bad, nor is action against foreign state-supported offenses. Trade and competition are global, and there is every reason for a harmed nation to

reach out to protect itself. If a harmed nation has no power to do so, especially where the most directly affected jurisdictions are unlikely to enforce their own laws, the whole competition system gets compromised. Moreover, the OPEC cartel is a persistent problem that invites cynicism with regard to antitrust itself. If producers of one of the most important resources of the world can legitimately fix prices and allocate quotas, how can it be that price fixing is essentially evil? The NOPEC bills were narrowly drawn; only the Department of Justice could sue, and only for an injunction, and the Executive could decide not to sue if it would harm foreign relations. Similarly for use of foreign sovereign compulsion and/or elastic uses of comity to let foreign sovereigns shield “their” firms from American antitrust. Good antitrust requires at the least a healthy skepticism of foreign sovereign attempts to shield their firms from the price-fixing offense. Thus, just because a policy happens to correspond with the America-First agenda does not mean it is bad. But beware the shoe that did not fall. What is a good principle for America when our competition is harmed by firms abroad, even under a gauzy cloak of sovereign support, is also a good principle against America when American firms harm competition abroad. We suspect America-First is not on board for reciprocity.

This leaves our last three applications of America-First antitrust. These are: relaxing antitrust when American firms hurt mostly foreigners, using antitrust against foreign defendants to extract non-competition concessions, and fighting foreign uses of antitrust against American firms by exaggerating or imagining discrimination or excessiveness. All of these applications involve the double standard problem. They bend process and the rule of law. They impose costs on consumers or on foreign firms or systems of law. And they fail to give appropriate respect to our trading partners to develop their own competition rules of law.

Two nuances are important. First, under common antitrust jurisprudence, nationals may hurt foreigners as long as the predatory actors do not hurt competition in their own markets. The assumption is that the harmed jurisdiction can and will sue (even if the assumption is wrong). Second, the United States has the right to stand up for its firms when other jurisdictions are applying their laws in nationalistic and discriminatory ways that harm the competitiveness of American firms.

## IV. CONCLUSION: WHY AMERICA-FIRST ANTITRUST IS BAD FOR AMERICA

We have reviewed an America-First antitrust agenda. We have shown why this agenda lacks legitimacy, undermines the rule of law, and usually (although not always) harms competition and consumers. Moreover, the agenda is dangerous in the world marketplace. Just as many Americans fight a China-first antitrust agenda, China and the world will be incentivized to fight an American one. An America-First agenda would lower the discourse to tit for tat, inspire trade friction and trade wars, and in addition, bear the high opportunity cost of unraveling the cosmopolitan antitrust consensus that, among other things, aims at improving competitiveness and minimizing systems friction in the world. In antitrust, as in many other areas, the United States is a teacher to the world. We should not teach parochial lessons. America-First antitrust is bad for America and bad for the world.



# BREXIT AND ITS IMPACT ON ENGLISH ANTITRUST CLAIMS

BY KENNY HENDERSON<sup>1</sup>



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## I. INTRODUCTION

In Theresa May’s memorable words, “Brexit means Brexit.” But what does this mean for England’s status as a favored jurisdiction for antitrust damages claims?

For complex claims with a cross border element, claimants frequently have a choice of where to file proceedings. At present, England, the Netherlands and Germany are, by a considerable margin, the claimants’ jurisdictions of choice. Should a “hard” Brexit occur and should this make England a less attractive forum, then one would expect fewer claims to be filed in England, with a corresponding increase in the Netherlands and Germany.<sup>2</sup>

The impact of Brexit on antitrust litigation in England will, of course, be influenced by the form of Brexit that the UK eventually adopts. If, for example, the UK joins EFTA and the EEA, then we can expect limited change to antitrust litigation as Articles 53 and 54 of the EEA Agreement proscribe the same conduct as Articles 101 and 102 of the Treaty on the Functioning of the European Union (“TFEU”). This eventuality would not require much commentary, and so this piece considers the impact if the UK adopts a hard Brexit model.

Post hard Brexit, the cause of action for breach of Articles 101 and 102 TFEU may become unavailable, leaving claimants to file under the domestic analogues of Chapters I and II Competition Act 1998 (“CA 1998”). This may narrow the territorial scope for such claims. Also, if Commission infringement decisions are no longer binding on English courts, then claimants will need to prove liability. For claimants there are potential workarounds for these issues and, in any event, the UK is unlikely to make any material adjustments for the short to medium term.

These changes notwithstanding, even a hard Brexit will not remove many of the features that make England an attractive jurisdiction to claimants, such as the English approach to disclosure, the relative speed of procedure and the strength of the antitrust bar. In fact, England could become more attractive in some ways. In particular, as English courts may no longer have to wait until exhaustion of

<sup>2</sup> This article therefore assumes that at least one European jurisdiction, in addition to England, could take jurisdiction over the relevant dispute. The rules applied by the English courts to assessing jurisdiction may change post Brexit. There is insufficient space to examine these changes in detail, but possible outcomes include the Recast Brussels Regulation ceasing to be applied and instead for the English courts to apply the Brussels Convention or for the UK to accede to the Lugano Convention. If there is no replacement to the Recast Brussels Regulation then the English courts may apply the common law rules on jurisdiction in its place.

rights to appeal before the European Courts, proceedings in England may be able to march ahead of those commenced in the national courts of EU Member States, allowing claimants to progress towards trial and/or push for settlement even more quickly.

## II. THE PROCESS FOR “BREXITING”

“Brexiting” will have an impact both at the treaty level and also at the level of domestic law.

As to the former, the newly-famous Article 50 of the Treaty on European Union (“TEU”) provides for a two-year period during which the EU and the withdrawing Member State can negotiate and conclude an agreement on the State’s withdrawal.<sup>3</sup> If no agreement is reached to extend the negotiation period, then both the TEU and the TFEU will automatically cease to apply to the withdrawing State at the expiry of the two-year period.<sup>4</sup>

As to the latter, the position is less clear. On October 2, 2016, Theresa May announced that the Government would introduce a “Great Repeal Bill” to repeal the 1972 European Communities Act (the “ECA”), with the Great Repeal Act coming into force on the day of Brexit.

The Government has provided little detail on the mechanics of the Great Repeal Act, but it appears that much of extant European Law will be transposed into the domestic legal systems of the UK.<sup>5</sup> In the months and years that follow Brexit, the UK can progress the mammoth task of identifying and removing selected elements of European law from domestic law.

## III. IMPACT OF BREXIT ON THE CAUSE OF ACTION

At present, most damages claims for international cartels are pleaded as a breach of the statutory duty imposed by the ECA to comply with Article 101 TFEU. Post hard Brexit, the TFEU will no longer apply to the UK at treaty level. Furthermore, as the Great Repeal Act will repeal the ECA, the statute underpinning the statutory duty will fall away.

Before considering the effects of the above, it is worth examining two preliminary matters. First, it seems likely that any changes to the cause of action will not take place for the short and possibly

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3 In light of the ruling of the Supreme Court ruling of January 24, 2017, it is now clear that the UK can only trigger Article 50 following authorization by an Act of Parliament, *Miller & Anor, R (on the application of) v. Secretary of State for Exiting the European Union* [2017] UKSC 5.

4 TEU, Article 50(3).

5 In a statement to Parliament, Brexit Secretary David Davis said, “The great repeal Act will convert existing European law into domestic law, wherever practical.” October 10, 2016 (Hansard Vol 615).

also the medium term. This is because the UK government would be cautious to remove any cause of action for claims that have already vested. Legislating in such a manner would be highly controversial as a matter of domestic law,<sup>6</sup> it would potentially infringe the doctrine of acquired rights set out in Protocol 1 of the European Convention of Human Rights and in addition it could expose the UK to liability in investment treaty arbitrations.

More likely is that we would have a transitional regime, whereby Article 101/102 TFEU remain available for claims where the underlying acts took place pre-Brexit. Given that most Article 101 TFEU activity is concealed, there can be a very long tail between infringing behavior and filing of claims. Thus, the effect of any transitional arrangements could last for many years, with business as usual for claimants. Any transitional arrangements will also need to consider infringing behavior that overlaps Brexit-date and whether the totality of a single continuous infringement could be telescoped into a transitional regime that permits claims under Articles 101/102 TFEU.

Second, the UK Government will need to amend national legislation if it wishes to avoid claims under Articles 101 and 102 TFEU being brought in by the back door as a matter of domestic law. Article 1 of Regulation 1/2003<sup>7</sup> proscribes infringement of Articles 101 and 102 TFEU. Thus, transposition of Regulation 1/2003 into domestic law by the Great Repeal Act would lead to the curious position whereby the TFEU no longer applies to the UK at treaty level, but Articles 101 and 102 TFEU form part of UK domestic law. A claimant may even argue that the Great Repeal Act embraces the same statutory duty as the ECA, thereby introducing a cause of action of the same scope as Articles 101 and 102 TFEU. This said it would be straightforward for the UK to choose against importing Regulation 1/2003 into domestic law either at the time of Brexit or shortly thereafter.

Relatedly, section 47A of the CA 1998 imparts a statutory cause of action for breach of Articles 101 and 102 TFEU (as well as Chapters I and II of the CA 1998) before the CAT. Thus, unless the UK Government amends or repeals section 47A, the cause of action for breach of Articles 101 and 102 TFEU will remain available, albeit only before the CAT.

Although not relevant to a cause of action, the UK Government may also amend or repeal sections 58A and 60 of the CA 1998. The former provides that Commission infringement decisions are binding on the High Court and the CAT. The latter currently requires the English Courts to interpret questions arising out of the CA 1998 con-

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6 Retroactive laws are “contrary to the general principle that legislation by which the conduct of mankind is to be regulated [and] ought. . . to deal with future acts and ought not to change the character of past transactions carried on upon the faith of the then existing law. . .” *Phillips v. Eyre* (1870) LR 6 QB 1, 23.

7 Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (2003) OJ L 1/1.

sistently with the treatment of corresponding questions arising under EU law in relation to competition within the European Community.

#### A. What if Claims Can No Longer be Brought Under Articles 101 and 102 TFEU?

Chapters I and II of CA 1998 are the domestic analogues to Articles 101 and 102 TFEU, but the former have narrower “territorial scope.”

Article 101 TFEU proscribes anticompetitive behavior between undertakings: which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market.” Article 102 TFEU proscribes abuse of dominance “within the internal market or in a substantial part of it... in so far as it may affect trade between Member States.

Chapter I CA 1998 proscribes collusive anticompetitive behavior which “may affect trade within the UK, and ... have as their object or effect the prevention or distortion of competition within the UK.”<sup>8</sup> Chapter II CA 1998 proscribes abuse of dominance “if it may affect trade within the UK.”<sup>9</sup> Thus, the territorial scope of Chapters I and II are restricted to the UK, whereas the territorial scope of Articles 101 and 102 TFEU extend to the internal market.

In two recent judgements,<sup>10</sup> the High Court has confirmed that restrictions on the territoriality of Article 101 TFEU apply to antitrust damages claims. For the majority of the pleaded purchases in these cases, the sales by the defendants were first made in Asia to distributors and/or direct to OEMs. The goods were then incorporated into finished products before being sold to claimant entities in Asia, who then transferred the finished goods to other claimant entities in Europe. In *iiyama CRT*, on the basis of the pleaded supply chain, the Court ruled that Article 101 TFEU has not been infringed, either on the implementation test,<sup>11</sup> or on the “immediacy” element of the qualified effects test.<sup>12</sup> Similarly, in *iiyama LCD*, the Court ruled that the claim for overcharges based on indirect purchases originating in Asia did not breach Article 101 TFEU.<sup>13</sup>

If a post-Brexit English Court only applies Chapter I CA 1998, the scope of damages that are recoverable potentially narrows. Thus,

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8 CA 1998, Section 2(1).

9 *Ibid*, Section 18(1).

10 *iiyama Benelux BV & Ors v. Schott AG & Ors* [2016] EWHC 1207 (Ch) (“*iiyama CRT*”) and *iiyama LCD*.

11 *Ahlström Osakeyhtiö v. Commission*, (“*Woodpulp I*”) [1988] ECR I-5913.

12 *Gencor Ltd v. Commission* (“*Gencor*”) [1999] E.C.R. II-753.

13 In *iiyama LCD* the Court ruled that an alternate theory of harm was capable of being pleaded. Namely, that had the cartel not been implemented in Europe, the claimants could have purchased LCDs at non-cartelized prices. While this way of putting the claim was capable of pleading to the strike-out standard, it raises significant hurdles on causation.

where a corporate group buys cartelized products via different European subsidiaries, European losses may fall within the scope of Article 101 TFEU which would no longer be available in England. In contrast, UK losses would lie outside the scope of Article 101 TFEU but may be recoverable under Chapter I CA 1998.

#### B. Potential Workarounds

Most torts do not have a territorial scope, and so the causes of action dependent on Articles 101 and 102 TFEU are unusual in this regard.<sup>14</sup> Accordingly, claimants may try to identify other tortious causes of action without limitations on territoriality. The Court of Appeal’s ruling in *Air Cargo*<sup>15</sup> effectively forecloses unlawful means conspiracy for cartel claims. The specific difficulty flows from the “intent” requirement of the tort. In *OBG v. Allen*<sup>16</sup> Lord Nicholls identified “the defendant’s intention to harm the claimant” as a “key ingredient of the tort.”<sup>17</sup> Lord Nicholls explained that the intention must be both specifically directed to the claimant and must also be the motivation behind the defendant’s behavior.<sup>18</sup> The Court of Appeal noted that in cartels it is foreseeable that “someone” will be harmed, but on account of pass-on and the unpredictability of whom in the distribution chain will be harmed,<sup>19</sup> the intent element of the tort will be very difficult to meet.

Unlawful means conspiracy may however be viable for certain abuse of dominance claims. Abusive behavior performed by companies within the same corporate group may be specifically directed at an identified competitor, satisfying the intent element of the tort. This claim theory would be unlikely to work in the U.S., where the Intracorporate Conspiracy Doctrine holds that companies in the same corporate group are incapable of forming a conspiracy. However, this doctrine does not form part of English law.<sup>20</sup>

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14 Unusual but not unique. Territoriality is also a concept of copyright law. Section 96 of the Copyright Designs and Patents Act 1988 (“CDPA”) imparts a cause of action on copyright owners whose rights have been infringed. The CDPA sets out numerous behaviors that comprise “infringement” including, “[importing] into the UK, otherwise than for... private and domestic use, an article which is, and which he knows or has reason to believe is, an infringing copy...” CDPA, Section 22. (Emphasis added.)

15 *Air Canada & Ors v. Emerald Supplies Limited & Ors* [2015] EWCA Civ 1024.

16 *OBG v. Allen* [2007] UKHL 21.

17 *Ibid*, Paragraph 164.

18 “The defendant’s conduct in relation to the loss must be deliberate. In particular, a defendant’s foresight that his unlawful conduct may or will probably damage the claimant cannot be equated with intention for this purpose. The defendant must intend to injure the claimant. This intent must be a cause of the defendant’s conduct,” *Ibid*, at Paragraph 166.

19 A class of victims which may include “anyone in the chain down to the ultimate consumer... opens up an unknown and unknowable range of potential claimants.” *Ibid*, at Paragraph 169.

20 *Peterson Farms v. C&M Farming* [2004] EWHC 121 (Comm), Paragraph 62.

Another potential workaround for claimants is to argue that Article 101 or 102 TFEU is invoked on account of the applicable law for the dispute. If, on an applicable law analysis, the English court determines that the domestic law of a rump EU Member State is the applicable law, then Article 101/102 TFEU will be reintroduced.

The regime for determining the applicable law turns on when the underlying conduct took place. For conduct between May 1, 1996 and January 10, 2009, the Private International Law (Miscellaneous Provisions) Act 1995 (“PILMPA”) applies.<sup>21</sup> The starting position under PILMPA is *lex loci delicti*; that the applicable law is the law of the country in which the events, or the events’ most significant elements, constituting the tort in question occurred.<sup>22</sup> There is an exception for where there is a more substantial connection to a different country.<sup>23</sup>

In *Iiyama LCD*, after commenting that damage resulting from a tort is a necessary part of the cause of action, Mr. Justice Morgan “provisionally concluded” that such harm was suffered in the claimant’s country of incorporation, and such national law would apply to the claim. Taking our example from above, a claim by a French subsidiary buying cartelized goods will be subject to French law, and will reintroduce Article 101 TFEU. On this basis, claims will be able to recover damages before an English court<sup>24</sup> for breach of Article 101 TFEU.

## IV. SIGNIFICANCE OF EUROPEAN COMMISSION INFRINGEMENT DECISIONS POST-BREXIT

Post hard Brexit, it seems likely that infringement rulings by the Commission would no longer be binding on the English courts.<sup>25</sup> On the face of it, this would be bad news for claimants who would face new burdens of proving liability. After Brexit, only the findings of the CMA would be directly binding on the English courts.

However, in many situations, the fact that a Commission decision is not formally binding on the English court may have little substantive effect. Findings of fact by the Commission will likely be highly influential and a defendant who takes issue with such findings risks

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21 Where the conduct was prior to May 1, 1996, the common law rules apply. Where the conduct post-dated January 11, 2009, the Rome II Regulation applies. As noted, the Great Repeal Act may incorporate Rome II into domestic law, but this is uncertain. If Rome II ceases to apply, then PILMPA will apply even for events after January 11, 2009.

22 PILMPA, Sections 11(1), 11(2)(c).

23 *Ibid*, Section 12.

24 Subject, of course, to the English court taking jurisdiction.

25 Provided that section 58A CA 1998 is amended and that the UK and EU do not enter a mutual recognition arrangement for the rulings of competition regulators.

being given short shrift by an English court. The position that the defendant took during a Commission investigation will also be important and a leniency applicant will not realistically be able to deny underlying conduct that it admitted before the Commission.<sup>26</sup> Similarly, companies that participated in the settlement process with the Commission will thereby have admitted liability. An English court may however be more circumspect for defendants that are appealing the Commission’s decision.

While there may be questions on whether a Commission ruling is formally admissible in evidence before an English court, claimants frequently make allusions to findings of foreign antitrust regulators in witness evidence. Even if not formally admissible, it will be difficult for judges to put such findings fully out of their minds.

In summary, although post-Brexit, Commission decisions may cease to be formally binding on English courts, this may have little practical impact. By analogy, in the U.S., although the findings of the Department of Justice (“DoJ”) are not binding in civil damages proceedings, defendants that make guilty pleas to the DoJ do not typically deny liability.

## V. MANY FEATURES THAT MAKE ENGLAND ATTRACTIVE TO CLAIMANTS WILL REMAIN

Many of the features that attract claimants to file their claims in England will remain, even if a hard Brexit model is adopted.

England is perceived as a relatively speedy jurisdiction for resolving damages claims. In this respect, England’s competitive advantage may actually increase post-Brexit. At present, and in common with other EU Member State courts, pursuant to Regulation 1/2003<sup>27</sup> an English court cannot try a claim against a defendant whose conduct is under investigation by the European Commission. Not only must the national court wait for the Commission to complete its investigation,<sup>28</sup> but, pursuant to the pre-Brexit duty of sincere cooperation,<sup>29</sup> it must wait until the exhaustion of appeals against the Commission findings by any defendants before proceeding to trial.<sup>30</sup> Relatedly, the means for making a preliminary reference to the ECJ

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26 Leniency applicants must provide, “A detailed description of the alleged cartel arrangement, including for instance its aims, activities and functioning... [and] the specific dates, locations, content of and participants in alleged cartel contacts...” Commission Notice on Immunity from fines and reductions of fines in cartel cases, 2006.

27 Council Regulation (EC) No 1/2003 of December 16, 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (2003) OJ L 1/1.

28 *Ibid*, Article 16.

29 TEU, Article 4(3).

30 “[The English Courts will] avoid any decision running counter to that of the Commission or the community courts,” *National Grid Electricity Transmission Plc v. ABB Ltd* [2009] EWHC 1326 (Ch) at Paragraph 24.

on questions of EU law via Article 267 TFEU would be removed. Although references are used fairly infrequently in follow-on claims, their use can slow progress to trial. Post-Brexit, trials before the English Courts could proceed significantly in advance of those in the remaining EU Member States.

The English Court's approach to disclosure is also popular with claimants. Disclosure can be important even in follow-on claims. Sometimes a publicly available infringement decision is heavily redacted and/or may not give a digestible account of the wrongdoing, and so disclosure is required for visibility on the underlying events.<sup>31</sup> Disclosure is also very helpful in arguing quantum. Although the Damages Directive<sup>32</sup> requires that national courts must be "empowered...to estimate harm,"<sup>33</sup> economic models that are built and tested by reference to underlying data specific to the case are more defensible than those that overly rely on proxies or generalized sector data. Thus, while economic models that rely on proxies may be expressly permissible under the Damages Directive, those that rely on hard data can carry more weight, and disclosure can assist in this process.

One of the aims of the Damages Directive is to encourage broader disclosure in the national courts of Continental EU Member States, where disclosure is traditionally limited. This may reduce the competitive advantage that disclosure has given England in the past, but it remains to be seen how the Continental courts will interpret and apply their newfound powers of disclosure. To butcher an expression: it is one thing to change the law but another to change the cultural behavior of national courts.

Indeed, broad English disclosure can allow English claims to be a "can-opener," facilitating claims in other jurisdictions. Although the collateral undertaking<sup>34</sup> precludes the use of documents obtained in English disclosure for purposes other than such extant proceedings, this does not give defendants complete protection. Once a claimant has learned of the existence of documents through English proceedings, it is better positioned to specifically request the same documents in related proceedings elsewhere. This can-opening effect could be expedited if the pace of claims in England is accelerated post-Brexit.

Also, England will remain the only forum for certain categories of claim and claimant. English antitrust litigation received much attention following introduction of the opt-out claim mechanism in the Consumer Rights Act 2015 ("CRA"). Although certain other European jurisdictions such as Belgium and Portugal have opt-out mechanics,

those jurisdictions are not popular for antitrust claims. Importantly, opt-out mechanisms are the only practicable way to bring a claim where individualized losses are low but aggregate losses are significant.<sup>35</sup> This will not change post-Brexit and, subject to resolving teething issues on the mechanism,<sup>36</sup> the collective redress mechanism will remain attractive for suitable claims.

England is also an attractive regime on account of its sophisticated antitrust bar and relatively specialized judiciary, both in the CAT and in the Chancery Division. There is no reason to think that these features will change post-Brexit.

## VI. CONCLUSION

In summary, Brexit will be a long path and will have many uncertainties. However, even on a hard-Brexit, the features that make England so attractive to claimants are unlikely to change. While there could be changes to the territoriality of the cause of action, such changes may not take effect for many years and could leave claimants room for workarounds.

31 For complex infringements such as bilateral information sharing, it can be difficult to understand the underlying events even with disclosure of contemporaneous documents.

32 Directive 201/14/EU of the European Parliament and of the Council of November 26, 2014.

33 Ibid, Article 17(1).

34 Civil Procedure Rule, Part 31.22.

35 The mechanism is only available on an opt-out basis to claimants domiciled in the UK.

36 To date, only two claims have been filed using the new collective redress mechanism in the CRA. If these claims are certified by the CAT, it is likely that further claims will follow.



# U.S. ANTITRUST UNDER THE TRUMP ADMINISTRATION - A FEARLESS AND PERHAPS ACCURATE PREDICTION

BY KENT BERNARD<sup>1</sup>



I would feel much more confident about trying to predict what is likely to happen in a Trump antitrust administration if my crystal ball had correctly predicted the Trump election victory. When you have gotten the big prediction very wrong, it is hard to claim with a straight face that you are going to get the follow on predictions right. Of course, if ignorance and a terrible track record disqualified pundits, very little would get written. I would only caution the reader to keep his or her hand firmly on his or her wallet when reading any predictions (including mine). Recall that the vast majority of experts predicted both that Trump would lose, and that the stock market would crash if he won: he did; it didn't.

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No administration comes into power for the first time with a track record in antitrust enforcement, for the simple reason that you can't enforce anything until you are in office. We really don't have much to go on here. But having accepted the assignment to do some antitrust prognostication, it is time to uncover that crystal ball and see what it can tell us.

At the start, the ball tells us that changes will be less than people hope/think/fear they will be. One of the few benefits of getting older is to have seen administrations come and go, and the world not ended. The influence of economics has blended with, and largely supplanted, the original populist strain in antitrust. And what we have today is neither the extreme wing of the Chicago School argument that "anything goes, because the market will self-correct in due course" of the 1980s, nor the "block everything" mood of the 1960s.<sup>2</sup> Things will change. But anyone hoping for repeal of Section 2 of the Sherman Act or an expansion of the Robinson-Patman Act is likely to be seriously disappointed.

In making more specific predictions as to what policy will be in specific areas, the first thing that we can look to is the makeup of the Trump's transition team. As of this writing, the two people on Trump's team with backgrounds in antitrust are Joshua Wright and David Higbee. These are not newcomers to antitrust.

I hope that Wright would not be offended if I described him as a seriously smart academic, with a passion for efficiency arguments. He has a great deal of enthusiasm for free markets, and has produced an extensive paper trail of articles, speeches and opinions. FTC Commissioners (and heads of the Antitrust Division) all pledge allegiance to the idea of free markets. Wright actually walks the walk. He served as a Commissioner at the FTC from 2013-2015. Wright's return to the FTC as a Commissioner marked his fourth stint at the agency. In simple terms, he knows the Agency, and antitrust is his gig.

David Higbee comes from the law firm side, but also with significant government experience. He served at the Department of Justice as Deputy Assistant Attorney General and Chief of Staff of the Antitrust Division. Higbee also served as Deputy Associate Attorney General and as Counsel to the U.S. Attorney General and White House Liaison. To simplify again, he knows the Antitrust Division and he knows the way Washington DC operates.

<sup>2</sup> Who can forget such gems as [United States v. Von's Grocery Co.](#) 384 US 702 (1966)? A merger between the third and seventh largest grocery chain a geographic market, with a whopping combined 7.5 percent of total sales, was enjoined, and the people cheered in the streets (yes, that is sarcasm).

So what do these choices tell us? First, they tell us that Trump has reached out for experienced antitrust lawyers, with practical experience at the antitrust agencies. Second, they suggest that while Trump may have personal views about antitrust issues, he has not gone to extreme doctrinaire people for his transition team. Yes, Wright favors efficiency arguments, and can be provocative. But he is still within the antitrust mainstream.

While surely some things will change under the new administration (they always do), and both Trump and his advisors tend to favor free markets over regulated ones, getting from there to a prediction as to a specific matter or case requires a leap of faith more than analysis. Trump doesn't come to us with a fully formed public view of the function of antitrust in the 21st century. There is a strong urge to fill in the blanks in Trump's views for him. For example, he has spoken about wanting to rebuild American industry. Surely he will want to "unshackle" U.S. corporations to compete with foreign entities, remove unnecessary regulation and require proof of bad effects from conduct before the agencies condemn it. Therefore, if we follow this trail, we can predict that mergers will be allowed and that single firm dominance will go unchallenged. I have no such confidence, however.

That line of analysis opens the door to a very old logical trap: the fallacy of the excluded middle. It is very easy to go from "Trump says he wants to revive American industry" to "I want to revive industry" and then to "Therefore Trump will/should adopt the policies X, Y and Z that I favor." The rest of the article can then be whatever the author favors or wishes that the law was.<sup>3</sup> While we may all agree on the goal that does not mean that we agree on the best way to get there. And what Trump himself has said on these issues is not totally consistent. For example, Trump is a big fan of job preservation, but cutting workers is often the primary "efficiency" driving a merger. So are mergers favored, or disfavored?

Yes, Trump's appointees are likely to want to change certain policies and practices at the FTC and the Antitrust Division.<sup>4</sup> Every administration does that. But even assuming that we actually know what Trump wants or favors doesn't really tell you what his appointees are going to do. This is especially true of FTC Commissioners, who do not serve at the pleasure of the President.

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3 Another example would be: "*Kent is late for work. Either he has overslept or he has been abducted by Martians. We went to his house and learned that Kent isn't at home, so he must have been abducted by Martians.*" This argument is a fallacy, because there are many other reasons why I may have been late for work that day. For example, the New Haven Railroad might have broken down (the odds on favorite), or I might have decided to take the day off to go bungee jumping off the Brooklyn Bridge.

4 For a good overview of areas of potential change, at least at the FTC, see Bilal Sayyed, President-Elect Trump Has Once-in-a-Century Opportunity to Substantially Revise the FTC's Law Enforcement and Regulatory Agenda (December 2016), available at: <http://viewer.zmags.com/publication/ccd79339#/ccd79339/1>. The conclusion is that Trump will have to choose his appointees carefully. On that we can all agree.

With that as our foundation, let us look at a couple of key anti-trust areas, and what is more likely than not to happen to them under a new administration.

1. There will be pressure to use antitrust for broader policy issues than merely competition law. To the man with a hammer, everything looks like a nail. To an antitrust lawyer/scholar, every issue is a potential antitrust issue. While I personally do not see evidence that a Trump administration will fall prey to such anti-trust mission creep, it could happen.

2. Horizontal cartels will still be prosecuted. The rules regarding the core offenses of antitrust evolve slowly, and likely will not change much under President Trump. Cartels are bad. We get it. The rules governing concerted activity will remain relatively constant. This certainly applies to horizontal conduct, and may well apply to vertical restraints. Revolutionary change is not likely in these areas. Even if Trump had a burning desire to alter basic antitrust learning, it is not that simple for even a President to do that unilaterally.<sup>5</sup>

3. In the area of single firm conduct, a new administration may well make an impact. The U.S. rules are considerably more accommodating of hard competition than are those in the EU.<sup>6</sup> However, Trump has spoken as if he sees certain companies – such as Amazon/Washington Post – as wielding too much power.<sup>7</sup> The fact that certain media companies and media owners seemed to go on a crusade to have Trump lose the election, may have sharpened that perception. There also should be some concern among the Silicon Valley tech giants and their potential to shape the information flow, especially given the over the top hysteria when Peter Thiel endorsed Trump.<sup>8</sup>

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5 Recall what happened with the 1985 Vertical Restraints Guidelines; U.S. Department of Justice, Vertical Distribution Restraints Guidelines, 50 Fed. Reg. 6263 (1985), and the reaction to them. The Guidelines were perceived as an attempt to change the law and make it more permissive towards vertical restraints. An uproar ensued. A good description of the Guidelines themselves may be found at Fisher, Johnson, & Lande, *Do the DOJ Vertical Restraints Guidelines provide guidance?* 32 ANTITRUST BULL. 609 (1987). As for the reaction, as a later head of the Antitrust Division noted "The rescinded Vertical Restraints Guidelines, promulgated in 1985, were controversial from the outset. They were criticized by Congress and the National Association of Attorneys General...." Anne K. Bingaman, *Change and Continuity in Antitrust Enforcement*, Fordham Corporate Law Institute 1993, available at: <http://www.justice.gov/atr/public/speeches/0107.htm> page 13.

6 See, e.g. Bernard, Is Full Transatlantic Competition Law Convergence Realistic, or Even Desirable? CPI Antitrust Chronicle, December 2015 (1).

7 See Geyer, Will President Trump Revive Section 2 of the Sherman Act? (November 15, 2016), available at: [http://antitrustconnect.com/2016/11/15/will-president-trump-revive-section-2-of-the-herman-act/?utm\\_source=CPI+Subscribers&utm\\_campaign=a12037c784-EMAIL\\_CAMPAIGN\\_2016\\_12\\_08&utm\\_medium=email&utm\\_term=0\\_0ea61134a5-a12037c784-234820525](http://antitrustconnect.com/2016/11/15/will-president-trump-revive-section-2-of-the-herman-act/?utm_source=CPI+Subscribers&utm_campaign=a12037c784-EMAIL_CAMPAIGN_2016_12_08&utm_medium=email&utm_term=0_0ea61134a5-a12037c784-234820525)

8 There were cries to boycott companies with which Thiel was involved, de-

4. Mergers – Horizontal mergers (i.e. of competitors) will continue to be in the cross-hairs of the antitrust agencies. In my view, the agencies have sometimes taken an overly restrictive view of the market in which to judge the potential effects of a merger.<sup>9</sup> But the real excitement may well be in vertical cases. The big case now is *AT&T/Time Warner*. During the campaign Trump said that he was opposed to the merger.<sup>10</sup> More recently, the parties have said that they have been “reassured” by the Trump team’s statements that the merger will be “scrutinized without prejudice.” Apparently that reassurance is based on Trump’s appointment of Higbee and Wright to the transition team. Sources attributed to AT&T described the men as having a “hands-off record on antitrust enforcement.”<sup>11</sup> Yes, but...“hands off” generally, and a bland statement that a matter will be reviewed without prejudice, doesn’t exactly tell you anything about a specific, very high profile case. And the most recent reading of tea leaves reports that Trump is still opposed to the deal because he believes it would concentrate too much power in the media industry. This is allegedly according to people close to the president-elect, who has been publicly silent about the transaction for months.<sup>12</sup> Are you really willing to bet money on the outcome based on that?

So, here we are. We have a lot of unknowns. President Trump will get to appoint or nominate a lot of people, but it is unclear what he would like those people to do. Our track record in predictions about Trump should give us pause before we get too authoritative in predicting antitrust strategy. Perhaps we can take some comfort in the required disclosure in those ads for mutual funds and trial lawyers: past performance is no guarantee of future results. We shall see.

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mands to throw him off the board of other companies see: <http://www.dailymail.co.uk/news/article-3848206/Peter-Thiel-faces-Silicon-Valley-backlash-Donald-Trump-donation.html>. I would not be shocked if someone had suggested burning him at the stake for his heresy.

9 See Bernard, *An Integrative Approach to Evaluating Healthcare Provider Mergers in the Era of The ACA*, *Antitrust*, Vol. 30, No. 3, Summer 2016.

10 The quotes are collected in Geyer, *supra* note 6.

11 See: <http://arstechnica.com/tech-policy/2016/12/att--on-time-warner-merger-after-talking-to-trump-team/>

12 Smith and Green, *Trump Tells Confidant He Still Opposes AT&T – Time Warner*, available at: <https://www.bloomberg.com/news/articles/2017-01-05/trump-said-to-tell-confidant-he-still-opposes-at-t-time-warner>.

# U.S./EU ANTITRUST FRICTION IN THE TIME OF BREXIT: TOWARD A ROSIER SCENARIO?

BY TAD LIPSKY<sup>1</sup>



## I. INTRODUCTION

Although U.S. and EU antitrust rules share many elements, their historical roots are distinct and a variety of important tensions and inconsistencies persist between the two systems. Firms with operations in both jurisdictions are typically required to follow different legal advice and to operate differently in each. In many circumstances such firms can tolerate the added expense and business limitations without significant effects on their fundamental business models. Where there are important complementarities and cross-influences between U.S. and EU business conduct, however, the clash in antitrust rules can alter the fate of a business enterprise or an entire industry.

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EU rejection of the proposed General Electric/Honeywell International combination – cleared by the U.S. following antitrust review – is a famous example. Nine- and ten-figure EU antitrust fines imposed on Microsoft and Intel, and a \$14.5 billion “fine” against Apple (technically an EU command under its State Aid rules that Ireland assess additional taxes), plus threats of equally serious fines against Google and Qualcomm, raise questions on the U.S. side about the true content and objectives of the EU system. Looking back from the EU side of the Atlantic, U.S. assertions of jurisdiction over foreign parties and activities, when combined with U.S. criminal and civil remedies of great severity (incarceration, opt-out class-action treble-damage proceedings), are probably alarming to EU firms considering the antitrust risk inherent in U.S. operations following cases such as *Hartford Fire Ins. v. California*.<sup>2</sup>

As explained below, important differences between the two regimes have persisted for a half century, despite a variety of ongoing bilateral and multilateral efforts to harmonize international antitrust enforcement. Is this tension likely to continue? Two recent developments may disturb the current balance – Brexit, and the inauguration of an American President focused on international arrangements perceived to disadvantage U.S. economic prospects. Although it is impossible to predict which of many future scenarios seems most likely to play out, there is still cause for optimism that a Pareto improvement would result from the present configuration of forces on the field of international antitrust policy. This short article briefly speculates how the current picture could evolve into a rosier scenario – mutual U.S./EU progress toward shared antitrust objectives, standards, procedures and institutions.

## II. U.S./EU ANTITRUST TENSIONS

The more serious differences in the antitrust rules adopted in the two jurisdictions are reasonably well identified at this point.

### A. Collective Conduct

The EU has come a long way since 1962 when its institutional ancestor the EEC, implemented a formalistic and precautionary approach to potentially anticompetitive agreements. That approach required tens of thousands of agreements containing even minor and/or procompetitive restrictions to go through a lengthy and highly

<sup>2</sup> 509 U.S. 764 (1993). The decision was noteworthy (and controversial) for its strong suggestion that U.S. antitrust liability attaches to conduct that is both legal and even encouraged by government policy in the home jurisdiction of the affected parties – i.e. that the doctrine of international comity was not even implicated where compliance in both jurisdictions was technically possible for the accused firms.

bureaucratic process of notification and (in some cases) exemption to determine their legality. Despite significant improvements since then, today's EU law and practice remain more opaque and less tractable than the U.S. where collective conduct is concerned.

1. The EU concept of “concerted practices” – conduct that can violate TFEU<sup>3</sup> Article 101 (the EU cognate of Sherman Act Section 1), but without distinct proof of “agreement” – creates a fuzzy edge to the legality of certain forms of conduct that remain clearly outside the reach of U.S. antitrust (e.g. unilateral business information disclosures, which in some cases are being treated by the EU as illegal “by object” – that is, without regard to analysis of competitive effect). Liability for collective conduct in the U.S. requires proof of “agreement” full stop.

2. Because EU rules embody a market-integration objective, territorial limitations that coincide with EU Member State borders are decreed illegal “by object.” Recently it appears the EU is seeking to apply the “by object” classification to restrictions on internet sales, based on the sanctity of cross-border trade. By contrast, aside from classic “cartel” restraints, in the U.S. all territorial restrictions, vertical or horizontal, are lawful absent demonstrable anticompetitive effect.

3. EU antitrust law on vertical agreements bears noticeably greater skepticism than the U.S. toward exclusive arrangements and other intrabrand restrictions. U.S. antitrust law attends only to the horizontal effects of such restrictions, and has no concern with preservation of intrabrand competition as such.

4. Minimum vertical price agreements are still considered illegal “by object” in the EU. In the U.S. all vertical agreements – including those involving minimum price – are assessed according to proof of their competitive effect (despite lingering use of *per se* analysis of minimum vertical price agreements in some state antitrust rules).

## **B. Abuse of Dominance**

Substantive differences are even more pronounced between TFEU Art. 102 and Section 2 of the Sherman Act.

1. The EU may (and does) prohibit a wide variety of pricing conduct by dominant firms without proof of individual exclusionary effects. This is the problem of the so-called “exploitative abuse” – a species of antitrust violation not recognized under U.S. antitrust rules governing unilateral conduct.

2. The EU recognizes “joint dominance,” which (like the concept of “concerted practice”) can obscure the boundary between unilateral and collective conduct. No “joint dominance” allegation is admissible under U.S. monopolization law, as distinct from “conspiracy to monopolize” where the element of agreement is explicit.

3. The formulation of comprehensible standards for unilateral conduct gives rise to difficult problems in any system of antitrust law. The U.S. has made some valuable progress in the explicit use of empirically based economic analysis to refine rules governing predatory pricing, “mandatory access” cases and a few other areas, although many ambiguities remain. The EU – and most notably its judiciary – lags the U.S. in this regard, preserving opportunities to challenge various forms of unilateral conduct under EU competition rules that are generally more readily defensible under U.S. standards.

## **C. Enforcement Institutions**

Aside from the substance of antitrust rules, there are enormous practical differences in the U.S. and EU enforcement systems.

EU enforcement is conducted within a much less formalized or detailed legal framework compared to the U.S. In the U.S. – with limited exceptions (mostly cases subject to an on-the-record administrative hearing before the FTC) – contested antitrust allegations ultimately come down to the judgment of an Article III court, with two opportunities for review by higher Article III courts. Federal courts in the U.S. follow elaborate and strictly enforced safeguards to prevent any form of intrusion into the application of law to a clearly identified record composed under strict protections of litigants’ rights of defense. There can be no intervention by any legislative and/or political authorities, government prosecutors are treated like other parties (i.e. no *ex-parte* contact is permissible by any party) and extensive rules of evidence and procedure (at trial and appellate level) protect against intervention by untested evidence and other influences, including political influences.

By contrast EU antitrust decisions are technically the province of its senior administrative body, the College of Commissioners, where there are far less clear rules of evidence and procedure, rendering the EU process more akin to legislative “lobbying.” The process of investigation, “statement of objections,” and composition and assessment of the record can be highly discretionary and separation of investigative/prosecutorial vs. adjudicative/decision making/remedial powers is observed minimally if at all. Even after the 2011 judgment of the European Court of Human Rights in *Meranini*, judicial review is heavily deferential to the Commission both as to fact assessment and application of law to fact, and so slow as to be of limited utility at all events.

As a result, those outside the Commission – litigants and the public – have far less opportunity to verify and test the basis for decisions. Compounding the doubts created by these weak procedural protections, the EU overtly promotes important non-competition values such as market integration within its competition rules and institutions. This adds to the difficulties of monitoring or assessing EU deviations from output-maximization objectives that are central to U.S. antitrust.

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3 Treaty on the Functioning of the European Union.

### III. THE FIFTY-YEARS' TIFF: PERSISTENCE OF U.S./EU ANTITRUST FRICTION

The differences outlined above have persisted over many decades, despite long-standing multilateral and bilateral efforts to achieve greater approximation between U.S. and EU standards and procedures. The OECD – a Paris-based economic policy organization comprising 35 leading developed nations (descended from the committee that handed out Marshall Plan aid following World War II) – created “Working Party 3,” predecessor to the current Competition Committee, in 1964, to “enhance the effectiveness of competition law enforcement, through measures that include the development of best practices and the promotion of co-operation among competition authorities of member countries.”<sup>4</sup> Similarly, the International Competition Network is a “virtual organization” created in 2001 and now including every antitrust enforcement agency in the world (other than the three main Chinese agencies) aimed broadly at the same objectives as the original OECD WP3 mandate quoted above. Over the years since inception both organizations have produced a great number of thoughtful studies, surveys, guidance documents and “best practices” recommendations.

The U.S. and EU<sup>5</sup> (and EU Member States) are not only among the most prominent sponsors of and participants in OECD and ICN efforts, their antitrust agencies also have a long record of extensive formal and informal bilateral contacts. Their antitrust agencies have a variety of written cooperation agreements and a history of close and regular contact at many levels. Such cooperation occurs in the context of specific cases – e.g. coordinated “dawn raids” in international cartel matters, accommodation of remedies for mergers and acquisitions subject to review in both jurisdictions – and also on policy questions raised during the course of participation in bilateral and multilateral fora. Yet these extensive cooperative efforts – no doubt productive and in many ways valuable and even essential – have not produced harmonization in the areas discussed above.

The reasons for these limitations on the decades-old process of ironing out the key differences are many, and would themselves merit a lengthy analysis. The focus here, however, is on whether recent and predictable future developments could produce a shift in the present equilibrium. As described in the next section, the possibility certainly exists. The alternative paths are numerous, and the likelihood that any will be taken is liable to be affected by other forces now on the loose in the field of international economic policy, which has assumed an attention-grabbing dynamism in recent months. But the situation is far from hopeless.

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4 OECD, International Co-operation in Competition Law Enforcement p. 7n.6 C/MIN(2014)17.

5 Technically the EU does not have full OECD membership, but it is an active participant in proceedings of the OECD and its Competition Committee.

### IV. U.S./EU ANTITRUST: CAN WE REDUCE THE GRATING?

Two major new elements (arguably traceable to similar political undercurrents – but that isn’t the subject here either) inhabit the world of U.S./EU economic relations. First, the UK is leaving the EU, although there is little clarity about the end-game result. Second, there is a new U.S. Administration intent upon renovating America’s international economic relationships (*inter alia*). Both Brexit and the Trump Administration remain novelties – the one not even formally initiated, strictly speaking, and the other less than a month old at this writing. So, predictions as to their future course and how they might ultimately come to bear upon a topic so discrete and technical as antitrust enforcement is extremely hazardous. The following thoughts are offered in the full appreciation of the current obscurity of the road ahead.

Historically the UK has played a leavening role in EU antitrust enforcement. In general, the UK is seen as a force for improvement in and more pervasive application of economics in antitrust enforcement. Possibly the UK’s departure from the EU will dim hopes for further reconciliation of EU and U.S. antitrust models through these instruments, on the theory that if the UK is not “present” in EU antitrust debates, its views are unlikely to be of much effect. But one can foresee many complexities and related developments that might negate or overwhelm this simple logic as Brexit develops in practice.

The advent of the Trump Administration has already produced an apparent reversal in one very important policy aspect directly relevant to Brexit. Specifically, President Trump has reversed President Obama’s “end-of-the-queue” threat to the prospect of a U.S./UK trade arrangement. As a result, there are plausible suggestions (reinforced in a broad sense by UK Prime Minister May’s parlay with President Trump as his first state visitor) of an early focus on a U.S./UK bilateral trade agreement to revitalize the frayed “special relationship.” The U.S. has sought to include a competition chapter in many key trade agreements discussed or concluded in recent years: U.S./Chile (2004), U.S./Australia (2005), U.S./Korea (2012), the Trans Pacific Partnership (the U.S. has withdrawn at this writing), and the Transatlantic Trade and Investment Partnership (the U.S. has also withdrawn at this writing).

The notion of improving trade agreements by incorporating protections from the misapplication of antitrust (through unsupportable substantive rules, the mixture of industrial policy or other non-economic goals with antitrust enforcement and/or failure to adopt procedures that provide adequate opportunities for defense against antitrust allegations) should fit comfortably within the Administration’s broad rubric of vindicating U.S. interests in international trade. This allows some hope that negotiation of a U.S./UK trade bilateral agreement might consider inclusion of a competition chapter enshrining consensus on fundamental antitrust objectives, rules and processes. The U.S. and UK have similar antitrust traditions (even considering the accumulated influence of UK membership in the EU, which en-

couraged numerous forms of compliance with EU antitrust models). They also share common-law heritage and other fundamental notions of legal practice (e.g. attorney-client privilege) and procedure. Of course this is unsurprising given that the United States evolved from a collection of British colonies.

If an agreement were achievable, it might serve as a model for additional bilateral competition agreements involving each jurisdiction with others. What would be the EU reaction? The EU might turn inward, strengthening the unique pillars of its Ordoliberal antitrust tradition (a strong belief that the state must provide clear rules to guide economic operators while protecting the social market economy), pursuit of non-economic objectives such as market integration, special protections for SME's and workers and special support for technology-based industry or other favored sectors. But there is a chance that a U.S./UK collaboration based on limitation of antitrust enforcement to economic objectives and formalized procedures providing greater accountability – if successful – might inspire the EU to follow an Anglo/U.S. approach.

## V. CONCLUSION

The notion of a U.S./UK competition collaboration is of course a highly speculative proposition that would face numerous complexities and obstacles. How would the many areas of substantive difference be hammered out? How would the political institutions of both jurisdictions be persuaded to accept such a model for an operative set of legal rules and institutions – presumably in substitution for existing rules and institutions? Would such a regime apply only to U.S. and UK nationals, or would it extend to others? Even if such an agreement could be successfully negotiated and adopted, how would it be enforced? International dispute-settlement mechanisms receive no enthusiasm in U.S. trade and legal circles these days, yet it seems doubtful that such an agreement could have much impact without some way of resolving differences.

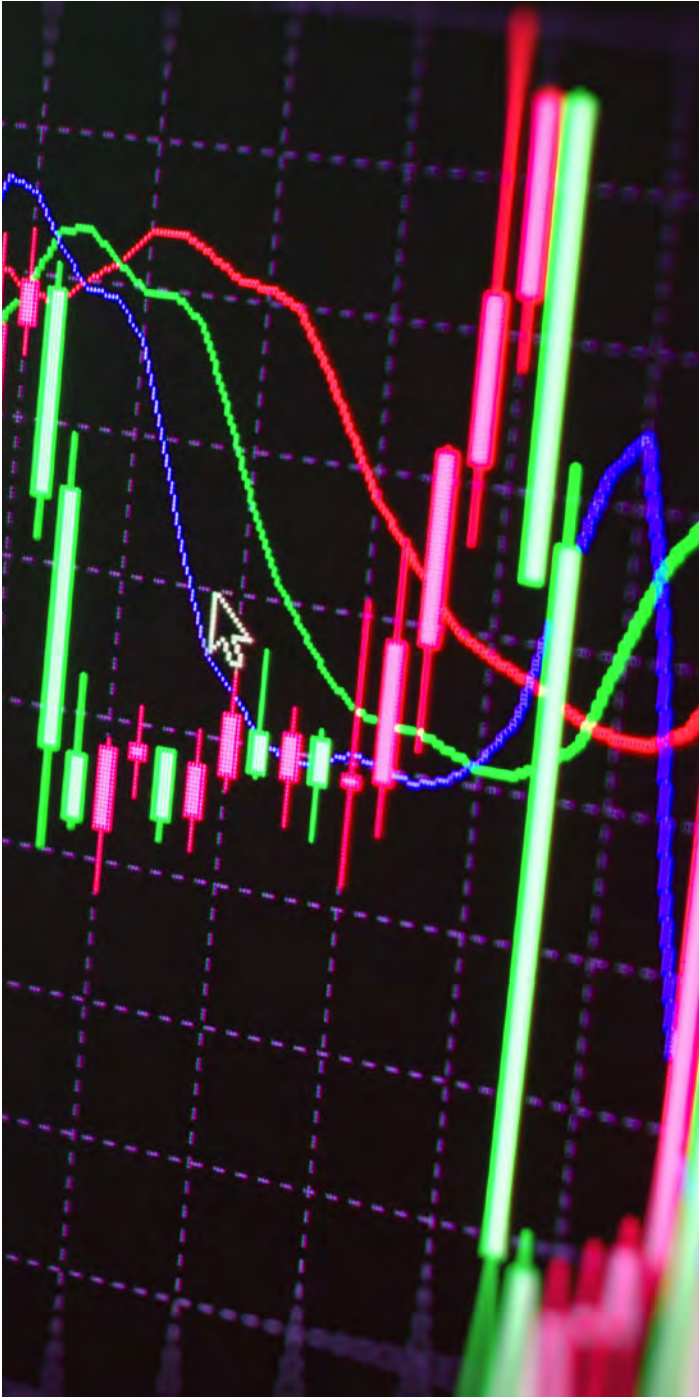
It is far too early to imagine how the current circumstances will evolve over coming months and years, and what effect they will have on U.S./UK and U.S./EU antitrust. But it is worth picturing what might be done to improve our antitrust systems, reduce the impact of multinational antitrust frictions, all to the ultimate point of enhancing the productivity of the global economy to the mutual benefit of the international community. It would be a great legacy of the current generation of antitrust enforcers, policy-makers, scholars and practitioners to outline a vision in which international conflict is reduced and economic growth prospects are enhanced. No harm in trying.

# DIGITAL MARKETS UPDATE



# DIGITALIZATION REVOLUTIONIZES THE ECONOMY - AND THE WORK OF COMPETITION AUTHORITIES

BY ANDREAS MUNDT<sup>1</sup>



## I. INTRODUCTION

Digitalization is revolutionizing all sectors of the economy. This is a challenging development not only for the business community but also for competition authorities. Digitalization and the competitive assessment of the global Internet giants is currently one of the most important issues for competition authorities around the world. There are many new questions on how competition law should be enforced in these days of digital revolution.

## II. THE TOPIC

Digitalization has changed existing business models in many areas. There are innumerable examples: retailers have to recognize that more and more people want to buy products online; publishers struggle with E-books or self-publishing on the Internet; newspapers face new competitors in the form of news sites or the further distribution of news on social networks. The telecommunications companies are recording a sharp decline in the use of SMS and fixed-line telephony while the data traffic via WhatsApp, social networks and Skype explodes.

This enormous transformation process is challenging for the economy and, of course, for competition authorities. We have to deal with new markets, new players and new business models and we do not have many precedents for our decisions. There is hardly any jurisprudence – let alone from higher or supreme courts. Therefore, competition authorities are under the spotlight and have to pave the way. Another thing we are seeing is that, on the one hand, the Internet markets are often highly dynamic and business and consumers benefit from digitalization, innovative business models and high market dynamics. We are usually reluctant to intervene on highly dynamic markets. On the other hand, digital markets are often characterized by direct and indirect network effects and strong economies of scale. Therefore, they are often highly concentrated. Often, competition is rather “for the market” than “on the market.” But sometimes even competition for the market is limited and high market concentration is persistent over long periods of time. That would speak in favor of intervening. Given this trade-off, it is not easy for us to judge whether or not to intervene.

In addition, digital markets have certain characteristics that make their competitive analysis more complex. Digital business models are often organized as networks or multi-sided platforms with direct and indirect network effects. To fully capture the competitive effects on such markets, several interrelated markets have to be analyzed. Additionally, products and services are often financed by advertising

<sup>1</sup> President of the Bundeskartellamt.

and provided as zero-priced products. The standard tools of market analysis have to be adjusted to such effects.

Furthermore, in digital business models, data is often a highly relevant parameter of competition. Data – usually known as “Big Data” – often has many positive effects such as improving existing products and services and creating new ones. Nevertheless, it can also be a factor which contributes to market power and to competition concerns that are not seen in other markets. But concerns can also go beyond competition law and affect consumer, data protection and privacy rights.

Finally, in public debate the market power of some digital companies has reached a politically relevant dimension. Some of these companies are even starting to get actively involved in politics. Therefore, today we also have to take care that economic power does not turn into political influence.

### III. EFFECTIVE ENFORCEMENT IN DIGITAL MARKETS

This is the context in which the competition authorities are acting today. The competitive challenges of digitalization call for effective competition law enforcement. If companies break the competition rules, we need to intervene. What does all this mean for our work? It means that our daily work and our approach to cases is also changing and that competition authorities have to adapt to this new economic environment. Our task is not changing, but our focus is. One focus of our case work will be to keep markets open *vis-à-vis* powerful or dominant companies. In this respect, and due to the internal growth of some digital players, the control of abusive practices – the “Mount Everest” of competition law – will probably become an increasingly important topic. Another focus is merger control. Here we need to assess effects on digital and data-driven markets. Moreover, we all have to consider if competition law is flexible enough or if new legislative measures necessary.

The Bundeskartellamt has addressed these challenges in conceptual projects and in its case work. As regards conceptual work, it was one of the first competition authorities to answer questions on how to deal with the digital economy. We have established a working group – internally labelled as a “Think Tank” – to develop concepts and tools, which developed a key policy paper on the market power of Internet platforms published by the Bundeskartellamt in June 2016. Also, we conducted, together with our colleagues from the French competition authority, a study on the interrelation between “Big Data” and competition law which was published in May 2016. Furthermore, we have successfully concluded a large number of proceedings in the digital economy dealing with the questions laid out in our various reports. All this aims to further develop existing examination concepts and, where necessary, develop new ones to enable the Bundeskartellamt to quickly and efficiently assess cases involving the digital economy.

As regards enforcement activities in digital markets, the Bundeskartellamt became active early and is an active enforcer in digital markets in Europe. The Bundeskartellamt and the former OFT in the UK were among the first authorities to initiate proceedings in cases of so called “Best Price Clauses” (“BPCs”). This was the case with hotel booking platforms in cases like *HRS* and *Booking*. Another example of effective intervention was the “Price Parity Clause” (“PPC”) of Amazon with regard to suppliers who made use of the Amazon Market Place. Best Price Clauses are a wide spread instrument in the Online Economy. While BPCs, at first view, suggest to be beneficial for consumers – they seem to benefit from the “best price” without search cost – in fact they are often the opposite. They often restrict competition and lead to higher prices. They reduce incentives for competitors to engage in price competition, they eliminate consumers’ incentive to search for better offers and they can make the market entry of new platforms considerably more difficult. In the *Hotel Booking* cases, these BPCs ultimately prevented the offer of lower hotel prices elsewhere and thus restricted competition between existing online portals. Moreover, they made the market entry of new platforms considerably more difficult because they prevented new platforms from offering hotel rooms at lower prices.

A similar example of what a National Competition Authority can achieve in the digital economy was the proceeding against Amazon with respect to the PPCs of the Amazon Market Place. Price Parity Clauses can have similar effects as BPCs. They prevent competitors from offering lower prices. Under Amazon’s PPC, sellers were prohibited from selling products they offer on Amazon cheaper through any other sales channel. Suppliers who made use of the Amazon Market Place were not allowed to sell their goods cheaper on other platforms. Again, the Bundeskartellamt initiated proceedings – in close cooperation with the OFT. Finally Amazon decided to abandon the PPC not only for Germany and the UK but for all of Europe. This case illustrates the role of national competition authorities in applying European Competition Law and setting standards in these markets.

An example for close co-operation of a National Competition Authority and the European Commission in digital markets are proceedings against *Audible/Amazon* and *Apple*. These proceedings relate to exclusivity agreements in the supply of digital audio books. The German Publisher and Bookseller Association had lodged a complaint at the Bundeskartellamt and the European Commission. The complaint was about an exclusivity arrangement between the two companies. Following the investigation of the Bundeskartellamt and the Commission, the parties abandoned these exclusivity clauses in a long term agreement on digital audiobooks. With the removal of the exclusivity agreement, Apple will now have the opportunity to purchase digital audiobooks from other suppliers. And Audible can supply other purchasers as well. This will enable a wider range of offers and lower prices for consumers. After conducting intensive market investigations and due to the close cooperation with the European Commission in this case, we were able to close these proceedings without a formal decision.

The specific characteristics of digital markets also change the assessment of merger cases. While in traditional markets market share is often a good proxy for market power, it can be a less reliable proxy in digital markets. Direct and indirect network effects, multi- or single-homing, market tipping and access to data can be relevant factors and can change the results of the analysis compared to traditional markets. For example, recent merger cases between large Internet platforms in the area of real estate or partnership platforms were cleared despite high market share on the basis of the criteria mentioned above.

## IV. BIG DATA AND COMPETITION LAW ENFORCEMENT

The increasing collection, processing and commercial use of data in digital markets has prompted a broad debate about the role of data in corporate strategies and the application of competition law to such strategies. The Bundeskartellamt has not only done conceptual work on the interrelation of Big Data, data protection and competition law. Data and data protection issues also play a vital role in cases.

In this context, the Bundeskartellamt has recently initiated a proceeding against Facebook. This case could serve as an example of how competition law and data protection law can be interrelated. We are investigating whether Facebook has abused its alleged dominant position in the market for social networks. Facebook's terms and conditions on the use of user data may constitute an exploitative abuse. Facebook's terms and conditions violate German data protection rules and German law on general terms and conditions. According to German competition case law, the use of unfair contract terms by a dominant undertaking can constitute an abuse. This could be a promising way forward in dealing with infringements of law by companies with a dominant position in digital markets.

## V. REFINING THE LEGAL TOOLBOX

Adapting the case practice is important. But just as important is reassessing the respective competition law provisions and to look for ways to improve the instruments and tools. We know from our experience that tackling threats to competition in digital markets needs a particularly thorough but at the same time speedy analysis. This is because products and services are often complex and markets are new and rapidly evolving.

That requires us to develop concepts and tools that are workable in practice to deal with Internet cases in a fast and efficient way. For exactly that purpose, we work intensively on legal and economic concepts to deal with digital platforms and networks, as those are the typical business models in digital markets.

Legal provisions need to allow us to apply these new concepts. In Germany, with the upcoming amendment to the German Competition Act (Act against Restraints of Competition, "GWB") criteria like

network effects, access to data, multi- and single-homing are explicitly mentioned as important factors in assessing market power in the German law. The amendment will also clarify that a market may also be assumed where no monetary payments occur. This conclusion is – especially in two-sided markets – already part of the competition authorities' practice, but one which until now was not clearly provided by the German competition law. Alternatively we could have gone forward striving for confirmation by court, which may have taken too long in such a dynamic environment.

Furthermore, the amendment will contain important adjustments with regard to the notification of merger cases that do not meet the established turnover thresholds. A new transaction volume threshold is to be introduced into German competition law, a consequence of the takeover of WhatsApp by Facebook for more than \$19 billion USD as one example. There were only three jurisdictions in the entire EU that were competent to review this merger due to WhatsApp's extremely low turnovers. This was in obvious contrast to WhatsApp's market position in the EU. It is not unusual in the digital economy for important companies to start with a very low turnover. The transaction volume threshold will allow the Bundeskartellamt to look at such important deals.

## VI. NO "ONE-SIZE-FITS-ALL" REGULATORY SOLUTION

However, even if the legislators make these adjustments to the amendment of the GWB, competition law still is not likely to solve every problem in the digital economy. There are plenty of examples of infringements of consumer rights on the Internet where thousands or even millions of consumers are affected. Consumer protection in Germany is a civil law matter. But in such cases it is often not likely that individual consumers sue for injunction or claim for compensation. The damages suffered are often relatively small for the individual person. Especially in new and fast-moving markets, legal uncertainty prevails.

Competition authorities principally have the tools to address many of these problems. But competition law, as it stands today, addresses a certain behavior by dominant companies. Establishing dominance – in particular in digital markets – usually is complex and requires time consuming investigations. In addition, especially in the Internet economy, thousands or millions of consumers might be harmed by a certain behavior of companies that are not dominant. To address these manifold problems prevailing within the digital economy, some call for the establishment of a special regulatory agency for digital markets. But when it comes to regulatory oversight, it will hardly be possible to develop a standardized set of rules, which would capture the specific problems raised by complex, highly differentiated and quickly changing business models. Therefore, there is no "one-size-fits-all" solution that can be applied by a single "super authority" – as it is sometimes discussed in the political debate.

While there might not be need and room for a regulatory “super authority” for the digital economy, a micro-invasive, targeted public enforcement of consumer rights in digital markets appears useful. We have to acknowledge that there can be difficulties for individuals to enforce their rights. If private enforcement reaches its limits, a certain degree of public consumer rights enforcement could be a useful supplement. It is currently being discussed whether the Bundeskartellamt should be given additional competences in the future to enforce consumer protection in the digital economy. The aim of introducing public enforcement in this area is to take up widespread violations and to focus on fast-moving areas of the digital economy. It should be a supplement to the well-established private enforcement system in Germany, which is working well in most cases. In our view, the examples of many other countries which have extended the powers of their competition authorities to include comparable competences show that competition authorities are well placed to deal with consumer protection issues.



# THE EMERGING HIGH-COURT JURISPRUDENCE ON THE ANTITRUST ANALYSIS OF MULTISIDED PLATFORMS

BY DAVID S. EVANS



## I. INTRODUCTION

Matchmakers help two or more different kinds of customers, such as drivers and riders in the case of ride-sharing apps, find each other and engage in mutually beneficial interactions.<sup>1</sup> They typically operate a physical or virtual place, which we call a platform, to help these customers find each other and interact. The different groups are called “sides” of the platform. Shopping malls, for example, operate physical platforms where retail stores and shoppers can find each other and do business. Search engines operate virtual platforms where users looking for information, websites that want to make their content available to users, and advertisers looking to reach users can get together.

Several modern technologies, particularly the Internet, have drastically reduced the cost of creating and running platforms resulting in the global proliferation of this type of business. Matchmakers now account for many of the most valuable companies. Three of them — Apple, Google and Microsoft — are regularly in the top five companies by market cap. Matchmakers are also the source of significant disruptive innovations. Seven of the largest startups in the world, such as Airbnb, operate multisided platforms. Matchmakers are behind what’s been called the sharing economy, the gig economy and the app economy.

Economists, following pioneering work by Rochet and Tirole, have developed significant theoretical and empirical work that has deepened our understanding of matchmakers.<sup>2</sup> The new economics of multisided platforms shows that there are material differences between businesses that facilitate matches among several interdependent groups of customers and traditional businesses that transform inputs into outputs. These distinctions are often relevant to the analysis of competition, regulatory and other public policy issues involving platform-based businesses.<sup>3</sup>

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1 David S. Evans and Richard Schmalensee, *Matchmakers: The New Economics of Multisided Platforms* (Boston: Harvard Business Review Press, 2016). (“*Matchmakers*”).

2 Jean-Charles Rochet and Jean Tirole, “Platform Competition in Two-Sided Markets,” *Journal of the European Economic Association*, 1(4) 990-1029, June 2003. For an overview of the literature and an extensive bibliography see David S. Evans and Richard Schmalensee, “Antitrust Analysis of Multisided Platforms,” in Roger Blair and Daniel Sokol, eds., *Oxford Handbook on International Antitrust Economics* (Oxford: Oxford University Press, 2015) and in particular the bibliography in the appendix available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2214252](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2214252).

3 David S. Evans, *Antitrust Economics of Multi-Sided Platforms*, *Yale Journal of Regulation*, Summer 2003, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=363160](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=363160) and Evans and Schmalensee, *Antitrust Economics of Multi-Sided Platforms*, *Yale Journal of Regulation*, Summer 2003, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=363160](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=363160).

Between September 2014 and September 2016 high courts in China, the European Union, France and the United States have issued decisions that examine particular issues concerning how to apply competition law to matters involving matchmakers.<sup>4</sup> These decisions recognize, at least implicitly, the new economics of multisided platforms. The emerging jurisprudence shows that the courts realize the need to adapt traditional antitrust analysis to matchmakers in light of the differences in the economics of these businesses and how they compete. Although high courts have just begun to touch on several complex issues involving these businesses, it is apparent that parties involved in matters involving matchmakers should pay close attention to the new economics of multisided platforms and its implications for conducting sound antitrust analysis.

After summarizing the key differences between matchmakers and traditional businesses, this article reviews the recent high court decisions and their implications for antitrust analysis of matters involving multisided platforms.

## II. WHAT MAKES MATCHMAKERS DIFFERENT?

Matchmakers create value for participants in a variety of ways. Most simply, the platform provides a way for two parties to enter into mutually beneficial exchange.<sup>5</sup> Participants are often more likely to find a good match if there are many potential trading partners.<sup>6</sup> Matchmakers can increase these chances by encouraging more participants to join their platforms. In fact, the main challenge for new platforms is securing enough participants on one side to make the platform valuable enough to participants on the other side. Matchmakers also create value by discouraging participants from engaging in bad behavior that could harm other participants.<sup>7</sup>

BlaBlaCar illustrates these methods of creating value. Consider a driver who is traveling from Paris to Barcelona and would appreciate a passenger to help share the cost and a person who would like to get a ride. BlaBlaCar's ride-sharing platform makes it much easier for them to find each other, ensure they are comfortable traveling together, and making an agreement. By encouraging more people

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titrust Analysis of Multi-Sided Platforms, above.

4 These are all situations in which a decision by a court of first instance was appealed and there was a ruling by an appeals court or a supreme court. I focus on the decisions by the highest court in the jurisdiction to address multisided platforms. On January 30, 2017, as paper was being prepared for publication the High Court of Justice in the UK issued a judgment, which I also discuss briefly.

5 Rochet and Tirole (2003) refer to this as a usage externality.

6 Rochet and Tirole (2003) refer to this as a membership externality; it is an example of what economists refer to more generally as positive indirect externality.

7 In *Matchmakers* Evans and Schmalensee examine the case of behavioral externalities for platforms.

to join the platform, particularly between heavily trafficked city pairs, it also increases the odds that a driver and passenger will find a good match for a particular time and destination. BlaBlaCar also discourages bad behavior on the platform through a rating system for participants and through disabling accounts for people who violate community rules.<sup>8</sup>

Economists have developed significant theoretical and empirical work that has deepened our understanding of matchmakers. That work shows that there are material differences between businesses that operate platforms and those who don't.

The firms are different. A traditional firm buys inputs, such as capital, material and labor, transforms those inputs into products or services, and sells them to distributors or end consumers. BMW makes cars and sells them to people. A matchmaker recruits one type of customer, and makes those customers available to another type of customers. Uber gives drivers and riders access to each other. This difference between selling products and selling access is fundamental.

The economics are different. The demand by one side of the platform depends on the interest, and therefore the demand, of the other side of the platform. The demand by buyers to patronize online marketplaces depends on the volume of sellers on these marketplaces, and the demand by sellers depends on the volume of buyers on the marketplaces. The existence of multiple distinct, and interdependent, types of customers results in fundamental differences between the economics of businesses that have multisided platforms and those that don't. Traditional firms don't have multiple interdependent customers.

The math is different. Economic models of platforms have terms that account for multiple customer groups with interdependent demand. For traditional firms, profit depends on the demand for the product; demand for the product in turn depends on the price of that product and the prices of substitutes and complements. For platforms, profit depends on the demand for the products consumer by both sides and that the demand for each product depends on the demand for the other. Most economic models of firm behavior are built from conditions for profit maximization and therefore the math of these models is different for platforms than for traditional firms.

Profit-maximizing pricing is different. For traditional firms, long-run profit-maximizing prices generally exceed marginal costs. In practice, it is rare for traditional firms to charge less than marginal cost for long. For platforms, long-run profit-maximizing prices to one customer group can be less than marginal cost. In practice, it is common to see platforms charge less than marginal cost, to provide

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8 See David S. Evans et Richard Schmalensee, *De précieux intermédiaires: Comment BlaBlalaCar, Facebook, Paypal et Uber créent de la valeur* (Paris: Editions Odile Jacob, 2017) (French translation of *Matchmakers* with additional content) and BlaBlaCar, *Inside Stories* available at <https://www.blablacar.com/blog/inside-story/think-it-build-it-use-it>.

platform services for free, and to give customers rewards for joining or using the platform.

Competition is different. Traditional firms compete with each other for customers that buy their products. Platforms compete by increasing the value of each side to the other side. They typically must compete for customers simultaneously on all sides. Payment entities are competing to get consumers to use their wallets online and for merchants to offer those wallets as a payment method.

Governance is different. Platforms often require governance systems to harness externalities among members and, particularly, to prevent members from harming each other on the platform. Sometimes they have self-regulatory systems such as ratings. Other times they prohibit specific behavior, monitor behavior and punish violators. Online marketplaces such as eBay, for example, have rules for buyers and sellers and penalties for violating those rules. Traditional firms don't have similar institutions because customers are not interdependent. BMW's customers don't interact with each other and therefore there is no reason why BMW would have rules for how customers behave with respect to one another.

These distinctions between matchmakers and traditional businesses are important to antitrust analysis involving platform-based businesses and high courts have already highlighted several of these differences.

### III. HIGH COURT DECISIONS ON PLATFORMS

Courts have encountered matters involving platform-based businesses, such as newspapers, for much of the history of competition policy.<sup>9</sup> They didn't have, however, the benefit of the theoretical or empirical work conducted by economists since 2000 in analyzing the issues in these cases.<sup>10</sup> The courts and the other parties involved in these matters didn't recognize platforms as a class of businesses that had much in common. The high court decisions since September 2014 that have addressed platform issues have reflected evidence and arguments, presented by the parties involved, based on the new economics of multisided platforms. I discuss these decisions starting with the most recent one at the time this paper was completed, which is also the most comprehensive.

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9 See, for example, *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594 (1953).

10 The High Court in the United Kingdom declined to follow the Commission's analysis in part because it predated some of the relevant economic literature. See *Ada Stores et al. v. MasterCard*, High Court of Justice, Queen's Bench Division Commercial Court, United Kingdom. 2017 EWHC 93, January 2017. ("It is also the case that economic theory has developed over the relevant period in a way which was simply not considered by the Commission [in 1992-2007]" (*Mastercard UK*))

#### A. American Express

American Express issues credit and charge cards to consumers as well as corporate customers. It charges cardholders an annual fee and, in the case of credit cards, interest on outstanding balances. It also offers reward points based on the amount of transactions made on those cards. It enters into contracts with merchants to accept its cards and to reimburse the merchant for transactions made with its cards. It charges a "merchant discount fee" which is a percentage of the transaction amount.

Merchants that enter into contracts with American Express have to agree to "nondiscrimination provisions" that prohibit merchants from giving customers a discount, or other incentive, for using another card brand, express a preference for another card brand, or disclose information to consumers about the cost of accepting these cards. Visa and Mastercard have had similar provisions for their cards. The nondiscrimination provisions prevent merchants from steering consumers to use cards that have lower merchant fees.

The U.S. Department of Justice, joined by a number of states, sued the three card networks. MasterCard and Visa settled. A U.S. District Court found against American Express after a trial before the judge. The U.S. Court of Appeals for the Second Circuit reversed.<sup>11</sup> The Second Circuit decision is the only U.S. appeals court case that has specifically addressed the antitrust analysis of multisided platforms in light of the new literature. The Court relied extensively on the economic literature on multisided platforms, and on payment systems, in its decision.<sup>12</sup>

The Second Circuit Court of Appeals concluded that it was inappropriate to separate out the two interdependent sides of the platforms in defining a relevant product market. The District Court defined a separate market for acquiring merchants. The Second Circuit found that "[t]he District Court erred in declining to define the relevant product market to encompass the entire multi-sided platform ... because the price charged to merchants necessarily affects cardholder demand, which in turn has a feedback effect on merchant demand (and thus influences the price charged to merchants)."<sup>13</sup> The Court noted that separating the two markets results in penalizing legitimate competitive activities "no matter how output-expanding such activities may be."<sup>14</sup> The Court found that

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11 *United States et al. v. American Express Company, MasterCard International Inc, Visa, Inc.*, No. 15-1672 (2d Cir. 2016). The Second Circuit denied a petition by the U.S. Department of Justice to hear the case, which was decided by a three-judge panel, en banc. As of this writing it is not known whether the Justice Department will seek Supreme Court review.

12 Many of the citations are to articles I've authored, many with colleagues, on multisided platforms or on the payment industry. I was not involved as an expert economist in this particular matter for any of the parties.

13 *United States et al. v. American Express Company, MasterCard International Inc, Visa, Inc.*, No. 15-1672 (2d Cir. 2016), p. 43.

14 Id. p. 38.

evidence of demand interdependence between the two customer groups was sufficient to conclude that the relevant product market analysis must consider the platform as a whole.

The Second Circuit concluded that it was necessary to consider both sides in assessing market power. It rejected the lower court's market power analysis for failing to account for the interdependencies between the two sides of the platform.<sup>15</sup> The District Court failed to "acknowledge that increases in merchant fees are a concomitant of a successful investment in creating output and value." The Second Circuit rejected the lower court's decision to ignore price calculations "intended to capture the all-in price charged to merchants and consumers across [the] platform" because "the two sides of the platform cannot be considered in isolation."<sup>16</sup> The District Court had found that American Express had market power over merchants in part because of the desire on the part of its cardholders to use its cards. The Second Circuit concluded that desire was what makes it worthwhile for merchants to accept Amex cards and pay its fees.

The Second Circuit concluded that the analysis of competitive effects had to consider both sides of the platform. The lower court found that it was sufficient to show "anticompetitive harm to merchants" that constituted the market that it had found. The Second Circuit said that the lower court's "analysis erroneously elevated the interests of merchants above those of cardholders" and that "the market as a *whole* includes both cardholders and merchants, who comprise distinct yet equally important and interdependent sets of consumers sitting on either side of the payment-card platform." (emphasis in original).<sup>17</sup>

Throughout its analysis, the Second Circuit determined that it was necessary to account for the interdependent demand of the two sides of the platform in conducting each prong of an antitrust analysis.

## B. *Groupement des Cartes Bancaires*

Groupement des Cartes Bancaires ("CB Group") is a bank association that operates the domestic debit card and ATM networks in France.<sup>18</sup> Members can issue CB branded cards to their customers for payment at merchants and cash withdrawals from ATMs. They can also promote the acquisition of card transactions for those cards by signing up merchants and installing ATMs. The CB Group man-

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15 Id. p. 38.

16 Id. p. 49.

17 Id. p. 55.

18 For an analysis of the ECJ's judgment in *Cartes Bancaires*, and the related judgment in *Mastercard*, see Frederic Pradelles and Andreas Scordamaglia-Tousis, "The Two Sides of the *Cartes Bancaires* Ruling: Assessment of the Two-Sided Nature of Card Payment Systems Under Article 101(1) TFEU And Full Judicial Scrutiny of Underlying Economic Analysis," *Competition Policy International*, Volume 10, No. 2, Autumn 2014, pp. 139-156.

ages the network of these participating banks, consumers and merchants. Members can choose the extent to which they issue cards, install ATMs and acquire merchants. Members pay various membership fees to the CB Group to support the operation of the network.

In 2002, the CB Group decided to alter its fee schedule so that members that focused mainly on issuance rather than acquiring would pay higher fees.<sup>19</sup> The CB Group notified, under the procedures at the time, the schedule to the European Commission and decided to wait for approval before implementing the fees. The Commission examined the proposed rules under Article 101, which prohibits agreements that have as their "object or effect the prevention, restriction or distortion of competition within the internal market."<sup>20</sup> Restrictions by object are those that are "regarded, by their very nature, as being harmful to the proper functioning of normal competition."<sup>21</sup> It isn't necessary to examine whether the effect of a restriction is anti-competitive if it is a restriction by object. The Commission found that the proposed rule had a restrictive object — to restrict entry and raise card prices to the benefit of the major banks that belong to the association — and was therefore unlawful.

In 2012, following an appeal by the CB Group, the European General Court ("EGC") upheld the Commission's determination that the agreement involved a restrictive object. CB then took the matter up with the European Court of Justice ("ECJ"). In September 2014, the high court found that the EGC erred in concluding that the agreement had a restrictive object given the two-sided nature of CB and the role of the fees in balancing issuing and acquiring.

The EGC had recognized that CB was a two-sided payment system. It found that issuing and acquisition activities were "essential" to each other; that there were "interactions" between issuing and acquiring; and that those interactions gave rise to "indirect network effects." It also acknowledged that the rules sought to establish a balance between issuing and acquiring. The ECJ found that, given these findings, "the General Court could not, without erring in law, conclude that the measures had as their object the restriction of competition within the meaning of Article [101](1) EC."

The ECJ provided insights into the relationship between market definition and the analysis of anti-competitive behavior. The EGC had, following the Commission, found that there were distinct markets for issuing and acquiring despite the interdependencies it acknowledged. The EGC then concluded "the analysis of the requirements of balance between issuing and acquisition activities within

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19 Banks that were largely inactive would also have to pay a "wake-up" fee to remain in the association.

20 Article 101 TFEU. The case itself refers to Article 81, which became Article 101 under the Treaty on the Functioning of the European Union ("TFEU") came into force amending the previous treaties. For *Cartes Bancaires* and *MasterCard* I refer to the current numbering.

21 *Groupement des Cartes Bancaires (CB) v. European Commission*, Case C-67/13 P, September 11, 2014, para. 50, citing to the case law. ("*Cartes Bancaires*")



the payment system could not be carried out ... on the ground that the relevant market was not that of payment systems ... but the market, situated downstream for the issue of payment cards....”<sup>22</sup>

The ECJ found that the EGC had confused the market definition issue with the context for analyzing whether an agreement restricts competition. Therefore, when a platform competes in separate but interdependent markets it is necessary to consider both markets in analyzing restraints on competition.<sup>23</sup> This conclusion only applies, strictly speaking, to the analysis of whether an agreement is a restriction “by object” in the context of Article 101(1). The reasoning would appear to apply to an effects analysis under Article 101 EC — *MasterCard*, discussed next, confirms that — and to an analysis of abuse by object or effect under Article 102.<sup>24</sup>

### C. Mastercard

The ECJ released its decision in *MasterCard v. Commission* the same day as *Cartes Bancaires*. MasterCard, like *Cartes Bancaires*, is a four-party payment platform. It has two sides. The issuing side consists of banks that issue cards to consumers that they can use to make payments at merchants that accept the brand. The acquiring side consists of banks that sign up merchants and acquire their transactions when consumers use the brand for payment. When an issuing bank cardholder uses her card to pay for a transaction at a merchant, the acquiring bank for that merchant pays the issuing bank an interchange fee.

The Commission found that the interchange fee rule had been adopted by an agreement of banks, that it had the effect of restricting competition under Article 101(1), and that it did not have countervailing efficiencies that could save it under Article 101(3). It did not reach a conclusion on whether the object of the interchange fee rule was to restrict competition. Instead, it relied on an analysis of effects to support its finding that there was a restriction of competition. MasterCard appealed to the EGC, which sided with the Commission. The ECJ upheld the lower court but in the course of doing so provided guidance on the analysis of competitive effects and efficiencies.<sup>25</sup>

The ECJ concluded that there was no dispute that MasterCard is a “two-sided” platform, that issuing and acquiring are interdependent, and that there are indirect network effects between the two

sides.<sup>26</sup> In that case the “economic and legal context of the coordination concerned includes ... the two-sided nature of MasterCard’s open payment system, particularly since it is undisputed that there is interaction between the two sides of that system...” That economic and legal context must be considered in analyzing whether a practice restricts competition.<sup>27</sup> *Cartes Bancaires* and *MasterCard* therefore find that it is necessary to consider both sides of the platform, and their interactions, in determining whether coordinated behavior among firms has the object or effect of restricting competition under Article 101(1).

The ECJ also addressed the analysis of countervailing efficiencies. European competition law has a unique framework for doing so for coordinated practices provided under Article 101(3). Even if a practice has the object or effect of restricting competition, it may be lawful if it “contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit.”<sup>28</sup> The ECJ’s analysis was based on the finding, not subject to the appeal, that issuing and acquiring were two separate but linked markets. The ECJ found that the analysis of efficiencies in two-sided markets should account for the benefits obtained by customers in both markets and not just the benefits realized by the customers in the market subject to the restriction.<sup>29</sup> Therefore, just as it would be an error to analyze the object or effect of a restriction only in the market for one side of a two-sided platform, it would be an error to analyze efficiencies only in the market for one side of a two-sided platform.

The high court, however, imposed some limitations on the use of benefits in one market to save a restriction in a related market. The consumers in the market subject to the restriction have to secure an appreciable benefit in order to place any weight on the benefits obtained by consumers in the related market. As a result, if consumers in the market subject to the restriction don’t receive appreciable benefits, no amount of benefits in the other market could save the restriction. If consumers in the market subject to the restriction receive appreciable benefits then, even if those benefits aren’t enough by themselves to save the restriction, it is possible to consider the benefits in the other market and determine whether the benefits in both save the restriction. It is difficult to discern the logic, as a matter of economics or policy, behind this approach and perhaps it is an artifact of European case law.<sup>30</sup>

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22 *Id.* para. 76.

23 Market definition was not before the ECJ. Nevertheless, the ECJ noted the inconsistency in the EGC referring to a payment systems market with interdependent issuing and acquiring, and then defining separate issuing and acquiring markets.

24 The European General Court then considered the matter again given the ECJ’s guidance. My understanding is that it determined that the MasterCard agreement was a restriction by effect; as of this writing they have not published the judgment in English.

25 *MasterCard et al. v. Commission*, C-67/13 P, September 11, 2014.

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26 The ECJ noted that there “are certain forms of interaction between the ‘issuing’ and ‘acquiring’ sides, such as the complementary nature of the services, and the presence of indirect network effects, since the extent of merchants’ acceptance of cards and the number of cards in circulation each affects the other.” *Id.* para 177.

27 The ECJ did not delve into whether the Commission had failed to do so because it found that this issue was not raised in the appeal.

28 Article 101(3) goes on to say that the restrictions must be indispensable for achieving the objectives and must not eliminate competition.

29 *Id.* para. 237.

30 As noted above, as this paper was in press, a high court in the UK dismissed claims brought by retailers that Mastercard’s interchange fee rule

## D. Google Maps

Bottin Cartographes (“Bottin”), a Paris-based firm, and Google both provide mapping software that retailers can use for their websites to show location and provide directions. Bottin charges retailers for using its software. Google provides a basic version of its Google Maps API for free for a similar purpose; in this case Google makes money from selling advertising. It offers other versions, with more functionality and support, for a fee.

Bottin claimed that Google was engaging in predatory pricing. The Commercial Tribunal of Paris agreed in December 2012. It found that Google had abused its dominant position in maps to exclude competition and to exploit its dominant position in targeted advertising. Google appealed to the Paris Court of Appeals which, as required under French law, referred the matter to the French Competition Authority (“FCA”) for advice. The FCA found that Google was not engaging in predatory pricing because it was recouping its costs through the sale of advertising based on a number of cost-based tests it devised. In November 2015, the Paris Court of Appeals agreed with the FCA and overruled the lower court.<sup>31</sup>

For the purposes of assessing predatory pricing by a multisided platform, the appeals court found that it was appropriate to consider the recovery of costs in a related market:

[T]he irrationality of the economic model of Google Maps API is obviously not established. [T]he Authority has rightly observed that for operators on multisided markets ‘it may be rational . . . to provide free products or services in a market not to foreclose competitors but to increase the number of users on the other market [and that] the free business model is quite widespread in electronic markets.’<sup>32</sup>

As with the ECJ decisions, the Paris Court of Appeals decided that even if there were distinct markets defined for each side of a two-sided platform it was necessary, given the interrelationship between the multiple sides of the platform, to consider both sides in evaluating whether a practice — or at least a predatory practice — was anti-competitive.

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was a restriction by effect. It recognized following the ECJ that the analysis needed to consider the interactions between the two sides of the platform. It concluded that Mastercard would not be viable with a significantly lower interchange fee because issuers would have switched to Visa, which was not a party to this particular matter, and that the interchange fee was therefore necessary for it to compete. See *Mastercard UK*, above.

31 *Evermaps v. Google*, Paris Court of Appeals, November 25, 2015. Evermaps was formerly Bottin Cartographe.

32 *Id.* at 11.

## E. Tencent

*Qihoo 360 v. Tencent* is the first antitrust case decided under the Anti-Monopoly Law (“AML”) by the China’s Supreme People’s Court.<sup>33</sup> The high court presented extensive discussion concerning defining markets and assessing market power for online platforms.

Tencent is one of the largest online firms in China. Its major products include instant messaging (“QQ”), micro-blogging (“Weibo”), and online games (“QQ Games”). It provides many products for free to attract users. It makes money from selling premium versions of its products, online advertising, and artifacts for playing games. Qihoo 360 provides Internet security software and operates a gaming platform for third party developers. It makes money from selling online advertising, commissions from game developers and premium products.

In November 2010, there was a highly publicized scuffle between Qihoo 360 and Tencent. At the time Qihoo 360 was the leading provider of Internet security software and Tencent was the leading provider of instant messaging. Tencent introduced security software as a feature in one of its products. It also required QQ users to use Internet security software from a provider other than Qihoo 360 following claims that there were problems with Qihoo 360’s software. A few days later, following intervention by the Chinese government, Tencent reversed the policy and allowed QQ users to use Qihoo 360’s security product.

About a year later, Qihoo 360 filed an antitrust lawsuit against Tencent over this episode. The case was heard in the first instance by the Guangdong High People’s Court, which ruled against Qihoo 360 in March 2013.<sup>34</sup> Qihoo 360 appealed to the Supreme People’s Court, which upheld the decision in October 2014. The high court found Tencent did not have significant market power and therefore was not dominant under the AML. In the course of its decision, it provided extensive discussion concerning the analysis of market definition and market power for online platforms particularly where some products are provided for free.

The Supreme People’s Court recognized the importance of platform competition for evaluating the issues in the case. It noted that, “Internet providers compete not only for users but also for advertisers in order to gain profits in the advertising business and value-add-

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33 *Qihoo 360 v. Tencent*, Supreme People’s Court of People’s Republic of China, Civil Judgment No. Minsanzhongzi 4/2013, October 2014. For an English translation see: <https://www.competitionpolicyinternational.com/assets/Uploads/EvansetalMay-2.pdf>. I was an economic expert for Tencent in the lower court and high court proceedings and presented extensive written testimony to, and responded to written questions, from the Supreme People’s Court.

34 For citations and links to English translation of the decision see David S. Evans, Vanessa Yanhua Zhang, and Howard Chang, “Analyzing Competition among Internet Players: *Qihoo 360 v. Tencent*,” CPI Antitrust Chronicle May 2013 (1).

ed businesses.”<sup>35</sup> However, it decided that market definition should focus on the side in which the alleged anti-competitive practices were taking place. Instead, it concluded that platform competition should be considered “in order to recognize correctly the business’s market positions and its market control power.” In other words, it favored an approach where market definition is considered on each side of the platform but where the linkages between those two sides are considered in evaluating market power.

In analyzing whether Tencent had significant market power, the Supreme Court examined the interdependencies between the free and paid sides of the platform. “To gain profit from advertising business and value-added business,” the high court noted, “the instant messaging service proprietors have to attract a large number of users at the client end continually. In order to attract more users, the proprietors should constantly improve the quality of their service, constantly develop news services.” It concluded that, even though Tencent had a high share of the market for instant messaging and related services it had defined, Tencent lacked significant market power because it could not decrease quality, or raise price, significantly in that market given the loss of revenue for paid services.

## IV. CONCLUSIONS

As I noted earlier, multisided platforms are not a new type of business. They’ve been around for millennia. The courts have examined antitrust cases involving platforms for many years. In seeking a rehearing before the Second Circuit, for example, the U.S. Department of Justice emphasized that the Supreme Court had already examined two-sided platforms and decided that it was appropriate to just consider the market on one side.

In *Times-Picayune*, the Supreme Court addressed a tying restraint imposed by a newspaper — a classic two-sided platform. The Court recognized that ‘every newspaper is a dual trader in separate though interdependent markets,’ serving advertisers and readers. 345 U.S. at 610. Nonetheless, because ‘[t]his case concerns solely one of these markets,’ the Court defined the relevant market around just the competition for advertisers.<sup>36</sup>

The *Times-Picayune* case was decided, however, in 1953. That was almost half a century before Rochet and Tirole circulated their now classic paper on the economics of multisided platforms. Prior to the circulation of their paper, there wasn’t an economic theory of multisided platforms or systematic empirical studies on how these businesses behaved.

Competition authorities, courts and practitioners now benefit from the theoretical and empirical work that has been conducted

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<sup>35</sup> *Id.*

<sup>36</sup> See: <https://www.justice.gov/atr/case-document/file/910116/download>.

since 2000. It has taken time, or course, for the recent economic work to filter its way through decisions. Remarkably, between September 2014 and September 2016 — four high courts, in Luxembourg, Beijing, New York City and Paris, issued five decisions that relied on this new learning to address antitrust issues involving these matchmaker businesses. All five decisions recognize that matchmakers serve multiple interdependent groups of customers and that the interactions between these groups matter substantively for analyzing antitrust issues.

Four of those decisions find it is necessary to take the several sides of the platform into account in assessing whether a practice has an anti-competitive purpose of effect; the Chinese Supreme People’s Court did not address that issue but dismissed the competition concern finding a lack of market power. Two decisions addressed whether market definition should be conducted at the level of the overall platform or for the individual sides. The U.S. Second Circuit Court of Appeals concluded that it should be at the platform level while the Chinese Supreme People’s Court decided that it should be conducted for the individual sides with the two-sided constraints brought back in for market power assessment.

These cases are likely just the beginning of new jurisprudence on how to apply competition laws to a type of business that is increasingly important in economic life. Nevertheless they signal that the courts will expect that parties before them to have considered the economic characteristics of matchmakers and in particular the interactions between the groups served by them.



# COORDINATING POLICIES TO REALIZE BENEFITS FROM THE DIGITAL ECONOMY: THE CASE OF MEXICO

BY MARTIN E. CAVE  
& ERNESTO FLORES-ROUX<sup>1</sup>



## I. INTRODUCTION: THE IMPORTANCE OF THE DIGITAL TRANSFORMATION

The 2016 World Bank Development Report, *Digital Dividends* (“WBR 2016”), is a thoughtful review of the impact the “greatest information and communications revolution in human history” has had: the “poorest households are more likely to have access to mobile phones than to toilets or clean water.”<sup>2</sup>

Access to data, via smart phones and the Internet, comes from three sources. First, it reduces the cost of existing activities; second, it is inclusive by putting services, including basic ones such as education, within the reach of people who were previously deprived of them; and third, it permits new things to be done, such as interacting in real-time with virtual groups around the globe (think of social media).

The degree to which digitization has penetrated most sectors of the economy makes it extremely difficult to quantify its reach.<sup>3</sup> Can we clearly separate brick and mortar business and digital activity? Can we isolate digital advances in typical technological industries from those that apply in less affected industries? Digitization has, *de facto*, imbued our economic and social life.

Our study aims to describe the benefits which Mexico might gain by taking advantage of the opportunities of digitization, and to identify ways in which that performance might be improved by various public policy interventions. We do not, however, attempt to examine the impact that digitization has had on non-economic aspects of the life of a society, such as plurality of opinions and freedom of expression.

## II. WHERE MEXICO STANDS NOW WITH THE DIGITAL TRANSFORMATION

While the Internet has spread quickly in some countries, the rate of adoption of technologies that use the Internet has a wider variance. According to the WBR 2016, adoption of new technologies is closely related to the level of competition that firms face. To begin with a sense of how Mexico is doing internationally in terms of digitization, we use several measures, all of which point in the same direction:

<sup>1</sup> Martin E. Cave is Visiting Professor at Imperial College Business School, Ernesto Flores-Roux is an independent consultant and a member of IFT’s Advisory Board. We would like to acknowledge funding received for this research by the Consejo Ejecutivo de Empresas Globales (“CEEG”). The views expressed in this paper, however, are strictly ours, as are any mistakes.

<sup>2</sup> Page xiii. The report is available at: <http://www.worldbank.org/en/publication/wdr2016>.

<sup>3</sup> See OECD *Digital Economy Outlook 2015*, Ch. 3. The difficulty of measuring the “digital economy” can be contrasted with the relative ease of measuring the output of ICT-producing sectors.

Mexico is languishing in a lower place in the table than it should be, and that it would like.<sup>4</sup>

We illustrate such an approach with a “digitization index” developed by Katz et al. (2014),<sup>5</sup> which incorporates not only the development of basic infrastructure but also other aspects which affect appropriation and the capacity of a country to take advantage of information and communications technologies (“ICTs”). The “digitization index” is a weighted linear combination of six variables:

- “Affordability” is measured through the cost of ownership of a residential fixed line, of a mobile line and of fixed and mobile broadband accesses.
- “Infrastructure reliability” considers investment in mobile, broadband and fixed line networks.
- “Network access” considers broadband penetration (fixed and mobile), as well as personal computer penetration and mobile network coverage.
- “Capacity” refers to international Internet bandwidth per user and broadband speeds.
- “Usage” comprises Internet retail, e-government, Internet penetration, non-voice services as percent of wireless average revenue per user, social network visitors and short message service usage.
- “Human capital” incorporates two measures of education (engineers as a percentage of the population and the percentage of labor force with more than a secondary education).

Using this index as a measure of how digitized Mexico is, we can see that the index number has grown in the period 2004-2015 from 25.2 to 46.1, an average annual rate (“CAGR”)<sup>6</sup> of 5.6 percent. In contrast, during the same period the rest of the world has moved faster (from 18.4 to 41.2, a CAGR of 7.6 percent), driven by Africa (7.0 to 23.5, or 11.7 percent), Asia (15.9 to 39.5, or 8.6 percent), and even Latin America (21 to 47.4, or 7.7 percent). In fact, Mexico’s percentile relative to the rest of the world has decreased 16.7 percentage points, going from the 65th percentile to the 48th.<sup>7</sup> On

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4 See, for example, the World Bank Digital Adoption Index, the Network Readiness Index of the World Economic Forum, the ITU’s Digital Opportunity Index, and indices constructed by various consultancy firms such as the Boston Consultancy Group’s e-Intensity Index.

5 Katz, R. P. Kutroumpis & F. Callorda, Using a digitisation index to measure the economic and social impact of digital agendas, Info, vol. 16, n.1, 2014, pp- 32-44.

6 Compound annual growth rate.

7 For clarification purposes, this means that 67 percent scored worse than Mexico in 2004, but by 2015, only 48 percent did. That is, according to this index, Mexico’s position decreased substantially in the twelve years

the positive side, the “infrastructure reliability” and “capacity” components have improved on a relative basis (+9 and +2 percentage points), but the “network access” component, which mostly measures penetration, has lost 20 percentage points.

Although governments have invested heavily in digitization of public services, one of the principal criticisms that have been levied at them is that strategies tend to be isolated, uncoordinated and sometimes lack a comprehensive plan. The WBR 2016 notes that “digital technologies have helped *willing* and *able* governments better serve their citizens” [emphasis added]. A government’s capability, it notes, is strongly related with the strength of the underlying institutions, which in turn create incentives for politicians to deliver better outcomes.

For Mexico, this leads to several questions, namely whether the government has a clear digitization strategy and an effective implementation plan, particularly one that can measure progress and allows for accountability. Compared with other countries, Mexico is in the last position in the OECD’s measure of digitalization, and in the fifth position for Latin American countries for 2011. More recent numbers from the same source are not yet available, but the Katz’s Digitization Index shows that relevant but insufficient progress has been made. Mexico’s economy is not as “digital” as it deserves to be.

### III. THE KEY PRECONDITION: ENHANCED CONNECTIVITY

Dissatisfaction with the state of telecoms in Mexico became strong enough in 2011 to persuade the government to invite the OECD to carry out a review of the Mexican telecoms sector. The results, published in early 2012, highlighted a significant number of issues that hindered the sector from taking off to become an enabler of the digital economy. The OECD identified a number of barriers to entry – such as foreign direct investment restrictions, a complicated and non-transparent licensing framework and the creation of artificial scarcities (such as in spectrum) – which it recommended be eliminated. It also exemplified that the system tended to be non-transparent and discriminatory; regulation was not applied equally to all and its application was not effective; processes were cumbersome and slow, an aggravation, particularly in a fast changing sector.

It also addressed institutional considerations, such as a confusion of regulation and public policy, as well as overlapping responsibilities between different government entities (the “double window,” mostly between the Ministry of Communications and Transport (“SCT”) and the Telecommunications Federal Regulator (“COFETEL”). The report also diagnosed that regulation was not promoting competition. It recommended certain issues needed to be addressed *ex-ante* (e.g. quality of service, interconnection rates); the regulator had to be able to determine the existence of agents with significant market power and impose adequate asymmetric regulation quickly and in

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to 2015.

a coordinated fashion. To be effective, the never-ending injunction procedures needed to be simplified and limited.

The message was clear: an independent regulator and enforceable competition regulation were necessary conditions to help Mexico address its deficient telecoms sector.

### A. Mexico and the Rest of the World

With respect to basic telecoms services, Mexico has consistently shown lackluster performance. From a high-level perspective, average performance would rank Mexico roughly in line with its GDP per capita, which, in 2015, ranked 64th out of 185 (65th percentile); nevertheless, the historical evolution of most relevant telecoms indicators shows otherwise.

- **Fixed telephony:** Fixed telephony penetration, currently at 16 percent, puts Mexico at around the 54th percentile, or above 54 percent of other countries; accordingly, it is below not only developed countries but also behind the Latin American average.
- **Mobile telephony:** In terms of mobile telephony penetration (total number of access lines per 100 inhabitants), Mexico has never been able to catch up with what has been the trend worldwide – more than two thirds of countries have penetrations above 100 percent, whereas Mexico's currently stands at 89 percent.
- **Unique users:** Penetration is in line with Latin America, with 70 percent of the population actually having a mobile phone, only 9 and 17 percentage points lower than the rest of North America and Western Europe respectively. But individuals with more than one phone are much less common in Mexico than in the rest of the world, mostly due to pricing, low mobile termination rates, large areas with only one telecoms provider and the reduced need to own more than one SIM card given the large on-net community of the largest operator.

Broadband services so far show a marginally better performance when compared to the rest of the world. Mexico was the 50th country in the world to launch mobile broadband<sup>8</sup> (second half of 2005):

- **Fixed broadband:** Fixed broadband penetration, half of which is provided with DSL technology, 34 percent with cable modem, and 13 percent with fiber, has reached 12 percent. As 88 percent of connections are residential, household penetration currently stands at around 47 percent. These numbers are in line with the world's median, at around the 55th percentile.
- **Mobile broadband:** Mobile broadband is still growing at over 20 percent per year<sup>9</sup> and has already reached more than 69

million connections<sup>10</sup> (penetration of 53 percent), which, according to the GSM Association ("GSMA"), means that 44.7 percent of the population has a mobile broadband connection. Mexico's ranking, currently at 96 (57th percentile), is slightly better than for traditional services, but the country has started to recede mostly because many low penetration countries are still showing growth rates above 30 percent, thus quickly catching up.

- **Population using the Internet:** In Mexico, in 2015 more than 57 percent of the population 6 years and over accessed the Internet with certain frequency. Use is higher than the Latin American average. Mexico's relative standing – at the 60th percentile – is better than in any other telecoms-related statistic. This percentage, when compared to household and mobile broadband penetration, implies that many broadband connections are shared by several persons, many of which probably access the Internet through public connections.

With respect to estimating the population using the Internet, appropriation, defined as the process by which people adopt and adapt technologies, is extremely hard to measure. Given changing methodologies and in this measurement which prevents comparability, we can only say that it has consistently gone up, but little can be said of the recent evolution of appropriation of the Internet. Thus, there is still significant room for improvement. Realized demand does not seem adequate for a country with Mexico's development. Appropriation has arrived slowly.

### B. Trends in Investing and Pricing

In its 2012 report on Mexican telecoms,<sup>11</sup> the OECD mentions that investment in the country is the lowest among its members, at around USD \$35-45 per capita.<sup>12</sup> Accumulated per capita investment in the period 2000-2009 was USD \$346, while the OECD average was USD \$1,447. From 2010 to 2015, these figures have barely increased. Lack of incentives, low competition and a relatively uncertain regulatory framework most likely explain an important fraction of this gap.

Though the recent telecoms regulatory framework overhaul has only started to reverse past trends in service uptake, it has already created a significant discontinuity in pricing. For wireline communications, which include basic telephony and fixed broadband, prices had been slowly creeping down, decreasing 6 percent in nominal terms in the four years to December 2014. In 2015, the recently approved law prohibited charging for long distance services. This new rule immediately translated into a one-time 6.4 percent drop in the telecoms pricing index. Since then the upward trend has resumed, having increased almost 2 percent in the last years.

10 IFT, *Segundo Informe Trimestral Estadístico 2016*.

11 OECD, *Estudio de la OCDE sobre políticas y regulación de telecomunicaciones en México*, 2012, p. 40.

12 Amounts for 2008 and 2009.

8 Defined as allowing downloads at a speed of 256 kpbs or higher.

9 24 percent in 2015, 25 percent in the year to June 2016, IFT, *Segundo Informe Trimestral Estadístico 2016*.

For mobile telecoms, the trend is significantly different. From the publication of the reform until the enactment of the new law, prices fell at an historic rate. But in August 2014 with the entry into force of the new law, interconnection for the “preponderant agent”<sup>13</sup> was set at zero, effectively allowing all other telecoms companies to terminate traffic in América Móvil’s networks for free. Two years after this legal change, mobile prices, as measured by the CPI, have gone down on average 38.7 percent, for a total decrease of 42.8 percent since the reform came into effect.

As differentiation with bundles of minutes has become harder, companies have already started adding additional elements to their offers. Most bundles now include limited access to apps (WhatsApp) and other services (Facebook, Twitter), in an effort to attract customers while being competitive. Though positive for users, we believe this strategy might potentially bring different competition concerns going forward.

### C. The 2013 Regulatory Changes

The 2013 constitutional reform included the term “preponderance” used to describe any agent in the telecoms and broadcasting sector that had a market share above 50 percent, measured by at least one of several indicators.<sup>14</sup> It was included to be able to quickly label as “dominant players” two companies that, through legal injunctions, had avoided being declared as such in the past. Since then, the concept of “preponderance” has been adopted by other countries, among them Ecuador.

The constitutional text allows the regulator to impose asymmetric measures on those agents deemed preponderant. The Federal Telecommunications Institute (“IFT”) dictated its measures on March 2014. Most measures were reinforced by the Telecom and Broadcasting Law in July 2014, though new ones were added. These rules will go through a first evaluation period in the short term, somewhat behind the original two-year deadline. So far, IFT has not made any formal statement of the degree of compliance by the preponderant agent.

Nonetheless, the Mexican telecoms sector is still underperforming with respect to the rest of the world. Imposing the regulatory rules was no simple task; and evaluating – much less modifying them – is not easy either, as the period of asymmetry is short and follows decades of almost unrestricted dominance. Success will take time, and loosening regulatory intervention too early risks giving away progress already made.

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13 A “preponderant agent” is a corporation which holds more than 50 percent of the telecoms or broadcasting sectors in at least one of several metrics (subscribers, traffic, revenues, capacity, audiences). In March 2014, the regulator declared América Móvil as the “preponderant agent” in telecoms. “Preponderance” only applies to sectors; it does not apply to specific services or markets.

14 Subscribers, traffic, revenues, capacity, audiences.

## IV. OTHER IMPORTANT CONTRIBUTORY FACTORS

### A. Independence of Regulators

There is broad agreement that the substantial and sometimes risky investments required to create a digitized economy within a framework of regulation is more likely to be forthcoming when that regulatory framework is predictable and not subject to surprises. There is also a fair amount of agreement that having an independent regulator is the arrangement best placed to provide a stable background against which the investment can go ahead.<sup>15</sup>

This does not absolve the government from involvement in setting objectives and in making broad economic and social policy decisions. The government is also a major producer of public services, which it is likely to want to manage in an increasingly “digital” way. But it does imply a hands-off approach by government when detailed technical decisions (for example, standard setting or giving preference to technologically neutral solutions), or decisions which impinge on the relative positions of different operators, are being taken; the goal is to remove them from what may be a short-term or politicized arena.

In Mexico, the enforcement of competition in communications markets is being put in place simultaneously with the transitioning phase, and even in some sectors with the transforming phase of regulating the digital economy to level the playing field between incumbent and Internet firms. Moreover, the disruptive element brought about by the entry of Internet start-ups has involved the same incumbent players as those participating in infrastructure investment and product markets; namely, América Móvil — the preponderant agent in telecoms — with its entry into digital streaming services, Claro Video, and Televisa — the preponderant in broadcasting — with its video streaming service Blim. This introduces a novel and challenging element into the regulation of the sectors as vertical integration is rampant in Mexico. Given the very asymmetric market shares of the players, the IFT must be very alive to the possibility of vertical and horizontal leveraging of market power by dominant players, as well to the possibility of dominance being transferred to other markets.

The major role in regulation belongs to the IFT – and, like all other regulators, it still needs to fully develop its knowledge base of the sector. But other independent regulators are required. Where the service for sale or supply is not an information or communications service, the Mexican competition authority (“COFECE”) will be involved, as will regulators in other sectors. The digitization process will be advanced by a clear system of governance by independent regulatory agencies.

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15 See B. Levy and P. Spiller, *Regulations, Institutions and Commitment*, Cambridge University Press, 1996.

## B. Trust

The use of digital services requires acts of trust. A person buying goods on the Internet, and paying in advance will need confidence that the goods will arrive in the first place, and will be replaced if they turn out to be defective. In commercial processes and government and public services ones, personal information – for example, credit card details or information about health states – may be disclosed, and the risk of invasion of privacy is always there.

In a report by A.T. Kearney,<sup>16</sup> researchers concluded that willingness to trust when transacting online is often overlooked when developing complex systems, “more research is needed on how context can be defined more clearly and simply, and how it can be practically integrated into systems and interface designs that create meaningful user engagements. This understanding is essential to developing effective ecosystems and policies. Too often, the sociological and behavioral aspects are overlooked in favor of more technocratic approaches that have not worked when actually implemented.”

The implication is that whether the digital interaction is commercial or public sector in nature, careful thought must be given as to how to organize the interaction. Business incentives are likely to align strongly with a context-appropriate approach: that way revenue is maximized. But public service organizations may need constant reminding of this aspect of their digital activities. This lays out a very important role for, for example, competition advocacy, a role that IFT may need to more forcefully use in the coming years.

## C. The “App Economy”

Apps, especially mobile apps, now constitute a major and fast-moving component of the communications value chain. They are mostly supplied via two intermediaries: the Apple App Store and Google Play. It was only eight years ago that Apple decided to market (after appropriate vetting) other developers’ apps, and Google followed suit shortly afterwards with Android apps. This has had a major effect on how software for smartphones is distributed and is a development which is very profitable for the large mobile platforms.

It also has a big effect in countries outside the magic circle of 10 countries which are said to receive 95 percent of app revenues.<sup>17</sup> But this concentration not only disadvantages developers in other countries but may also skew markets more widely, promoting products and services from some countries but not from others. A recent international study on apps sheds some light on Mexico’s experience.<sup>18</sup> It shows Mexico punching well below its weight in several respects. The number of app developers in Mexico City is the same

as in Lima, half that in Buenos Aires and one third that in Sao Paolo.

This situation may arise from a number of factors, of which lack of training may be one. It may also be exacerbated by intense competition in the large number of apps written in Spanish. Apps are becoming the main interface of users within the digital economy, so significant local expertise will be required if the country is not to be left behind. Given the importance of the App Economy, it is important that the Mexican Government and business community understand these factors and seek to counteract them.

## V. PROGRESS AND PROSPECTS IN KEY SECTORS: THE CASE OF BANKING, FINANCE AND TAXATION

e-banking, understood as the performance of banking activities via the Internet, and e-finance, defined as any financial activity carried out electronically (more specifically, over the Internet) simply cannot exist without the support of reliable ubiquitous telecoms networks through which to carry out fast and secure transactions.

The availability of ICTs is a necessary condition, but it is not sufficient. e-banking requires the existence of rules that not only guarantee the quality, security and efficiency of transactions, but also foster a competitive environment. Trust in the system is essential. Basic ICT skills are needed. Underlying systems have to be simple for people to use, as complicated systems (e.g. not user friendly, too many steps, cumbersome registration processes) hinder potential users from appropriating e-banking.

e-banking, together with e-payments, is also highly correlated with financial inclusion, which is considered one of the most important levers to help people exit poverty. Financial inclusion in Mexico still has a long way to go. In 2014 (last number available), only 38.7 percent of adults had a bank account, compared to a world average of 53.7 percent,<sup>19</sup> positioning Mexico at the 38th percentile. Cash is still the preferred way for consumer transactions. According to IMCO,<sup>20</sup> in 2013 around 96 percent of these types of transactions, representing 47 percent of total value, were carried out with cash. Nevertheless, in spite of this low banking situation, electronic transfers have grown dramatically in the last decade, though absolute numbers are still low.

Financial inclusion, e-banking, formality, and direct taxation go hand in hand. For example, IMCO<sup>21</sup> estimates that by reducing one percent the number of cash transactions, which are largely related to the informal economy, GDP might grow between 0.4 and 0.5 ad-

16 World Economic Forum and A.T. Kearney, *Rethinking Personal Data: Trust and Context in User-Centred Data Ecosystems*, 2014.

17 Caribou Digital, *Winners & Losers in the Global App Economy* Farnham, Surrey, United Kingdom: Caribou Digital Publishing, 2016, p. 8

18 Ibid. p. 31-49.

19 Unweighted average.

20 IMCO, USAID, *Reducción de uso de efectivo e inclusión financiera*, 2016, citing MasterCard Advisors, “Measuring progress toward a cashless society,” 2013.

21 Id.



ditional percentage points. The Mexican government has pursued initiatives in many areas, three of which stand out:

- It has boosted its efforts to increase the taxpayer base. From December 2012 until October 2016, it increased from 38.5 to 55.2 million, an impressive 43.4 percent.
- Since 2009, it is mandatory to submit tax returns online (for those earning more than 400,000 pesos – USD \$20,000 – or receiving income from more than one source).
- Since 2004 it also introduced the possibility of billing and invoicing electronically (“factura electrónica”), which became mandatory in 2014. Overall, revenues from income tax have increased more than 107 percent since 2010.<sup>22</sup>

It is hard to isolate the effects of each one of these initiatives. Nevertheless, tax payments made over the Internet have barely budged in the last decade, which most likely is explained by lack of appropriation and difficulty for making payments online. The “factura electrónica” has taken off since it became mandatory as no tax deductions<sup>23</sup> can be made without an electronic invoice, thus creating the incentive to be requested by the payor. But given penetration statistics and the minimum requirements to submit a yearly tax return, the “factura electrónica” will most likely level off in the near future unless new incentives are put in place.

Given the link that exists between e-banking and taxation, Mexico could develop public policies to increase both simultaneously, entering into a virtuous growth cycle where one variable feeds into the other. This will only be successful if good reliable telecoms networks exist and penetration and coverage are high. In addition, trust in the system is essential – subject to antifraud measures, strict consumer protection regulations must ensure that complaints and problems are addressed quickly.<sup>24</sup> Today, problems abound, customer service processes are cumbersome and designed to deter the consumer and the taxpayer from complaining.

So far, the above description has focused primarily on online payments using the formal financial sector. But what about the remaining 60 percent of the population who remains unbanked?

One of the main setbacks for the development of non-banking alternatives for e-payments has been regulation. Over the last decade or so, Mexico’s banking regulators have placed emphasis and prioritized regulation to limit dubious transactions that can lead to

22 There was an overhaul of the tax system – mostly, an increase in taxes – in 2014, but the huge increase cannot be explained only by inflation and the tax increase. The tax authorities have been working on many fronts simultaneously.

23 With a few minor exceptions.

24 For example, a complaint about a transaction that went wrong, if it is not solved quickly – and, by default, in favor of the user – will only lower trust in the system. She will be reticent about using the system again.

money laundering. While this continues to be a priority, a new objective has been gaining prominence: fostering financial inclusion. Non-bank electronic payments are a clear means to achieve this.

There are two recent services that, although linked to banks, are now offering a hybrid to non-financial electronic payments: Saldazo<sup>®</sup> card and Transfer<sup>®</sup> service. Changes in the Law for Credit Institutions in 2008 and 2010 allowed third parties, not just banks, to establish contracts with banking institutions and act as their agents; the reform allowed these third parties to also include other parties to do so through the operation of mobile telephony. Further changes allowed for a simpler process to open an account.

Transfer<sup>®</sup> is a mobile payment service linked to a simplified account that is available to Telcel users. It allows for the opening of an account without identity documents (account 1), with only basic identity data but not keeping any of those documents (account 2) or with full identity documents but without keeping a copy of these (account 3).<sup>25</sup> Initially, Transfer<sup>®</sup> only offered operations using a mobile phone; later on a debit card was incorporated; by 2014 Banamex (the largest bank in Mexico), Femsa (the holding company of the largest Coca Cola bottler in Latin America, among other businesses) and Visa jointly launched the Saldazo<sup>®</sup> card for the largest convenience store chain, OXXO (also owned by Femsa) – about 18,000 points of sales and growing — that can be linked to the service.<sup>26</sup>

Around 30 percent of Mexicans who use bank correspondents instead of banks as their principal financial channel have benefited from Saldazo<sup>®</sup>. According to information from Banamex, the Saldazo<sup>®</sup> card generates 5,000 daily accounts of which 80 percent get associated with Transfer<sup>®</sup> and 95 percent of cardholders are new clients for the institution. It is telling, particularly about the importance of trust in these transactions, that face-to-face interactions, albeit with a convenience store, have been able to reach more Mexicans than a mobile transaction only did before, even if it was carried out by the largest incumbent operator.

## VI. A PROJECTION OF OVERALL BENEFITS

This report has identified progress and problems (such as low investment, slow appropriation, and insufficient competition) in achieving the digitization of the Mexican economy against the background of the pervasive benefits for the economy available from a successful implementation. This section discusses the scale of those benefits at a macro level, both achieved in the past and attainable in the medium term future.

At a high level, there appears globally to be a relationship between levels of digital intensity and GDP per capita. This is illustrated by the Boston Consulting Group (“BCG”), which compares its e-intensity index with the GDP per head of various countries. The

25 CNBV, *Libro Blanco de Inclusión Financiera*, 2012.

26 CONAIF, *Reporte de Inclusión Financiera 7*, 2016.

e-intensity index is based on the following:

- **Enablement** accounts for 50 percent of the total weighting. It measures various aspects of fixed and mobile infrastructure deployment.
- **Engagement**, which accounts for 25 percent, measures how actively businesses, governments and consumers are embracing the Internet.
- **Expenditure**, also accounting for 25 percent, measures the proportion of money spent on online retail and advertising.

The BCG scatter diagram showing the e-intensity index and GDP per capita exhibits a pronounced upward slope, with some outliers and with Mexico just about in the middle of the “middle income countries” pack.<sup>27</sup> But the problem with such correlations is that they risk confounding cause and effect. Does e-intensity cause the economy to grow, or do people make more use of e-intensive products and services as they grow richer?

Secondly, when examining the impact of digitization on the economy, we need to recognize that it has spill-over effects both between and within the various sectors of the economy and the universe of firms operating within it, and from household to household. For example, a connected consumer can benefit others, as a result of her better search capability and her suppliers’ response to it by offering lower prices to all customers. The ways in which these effects operate are various; they include:

- Better access to markets, as new firms can use the web to bring their products or services before a wider customer base spread over a broader geography – what is sometimes called the “death of distance”; in the labor market, better job matching;
- New business processes and organizational structures: better stock control, quicker contracting and “just in time” production. For example, a major U.S. grocery store reported that its logistics operation in the U.S. was quite different from the same function in Mexico, because Mexican stores were less well connected; and
- More innovation in general, made possible by new communications services, notably social media.

An indispensable driving force behind these processes is improved connectivity, and this suggests that a plausible causal factor is the availability and use of communications services.

When the OECD published its 2012 Review of Mexico, it looked at the performance of telecoms markets and sought to measure the detriment to the economy resulting from lack of competition on the

basis of the scale of excessive prices.<sup>28</sup> But this approach is too static and limited to capture the radical and expansive nature of the processes involved in the interaction of communications services with the rest of the economy. Accordingly, we are looking for a more dynamic method which seeks to pin down the effect of connectivity as a significant causal factor affecting Mexico’s growth prospects in the medium term.

With this in mind we have used a well-established methodology which focuses on connectivity, but it is designed to capture in a dynamic process the benefits to the Mexican economy as a whole. The focus of the method is on mobile connectivity, which is the major source of communication services for the majority of Mexican households and businesses. Thus we model the relationship between the spread of mobile connectivity and the level of a country’s GDP,<sup>29</sup> using a telecoms dataset of annual data from 48 countries for the fifteen-year period between 2001 and 2015.<sup>30</sup> The dataset includes six countries from Latin America. For most countries we have a breakdown of mobile take-up by generation – 2G, 3G and 4G.

Once estimated, the model allows us to identify a notional “baseline” penetration rate, which indicates for a specified value of GDP per head the level of mobile take-up which we would expect a country to have, based on the overall experience of the 48 countries. Our first result is that the penetration rate of mobile communications in Mexico is substantially lower than we observe in the “average country” in our panel. This shortfall could be attributable to various reasons, including competitive distortions in the mobile marketplace.

Secondly, the data indicate that the impact on GDP of what connectivity there was in Mexico is substantially less than the impact expected to be found on the basis of international experience, as reflected in the model. Thus Mexico appears to suffer both from a lower level of mobile penetration than international experience would indicate, and from a lower impact on GDP of what mobile connectivity there is, again as estimated by the model on the basis of international experience.

The cross-country analysis also suggests that the effect of mobile penetration on GDP varies with the level of mobile penetration. In particular, countries on average experience a 2.2 percent effect on the level of their GDP at a mobile penetration level of 60 percent; they get a 3.5 percent effect at 80% penetration; a jump at 4.6 percent for 100 percent penetration; and 5.2 percent for penetration in excess of 120 percent.

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28 OECD, *OECD Review of Telecommunications Policy and Regulation in Mexico*, 2012, Annex C.

29 For details of this model, please feel free to contact either author. All GDP data in this section are in real (constant prices) terms.

30 We use all the available information from GSMA which covers 48 countries and combine this information with data from the World Bank and DoTEcon.

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27 See The Boston Consulting Group, *The 2015 BCG e-Intensity Index*, 2015.

The first quality change in mobile telephony arose with the provision of 2G services, which allow, as well as voice, some basic data communications to be accomplished. The real revolution was the third generation with download-speeds exceeding 14 Mbps and directly competing with fixed line alternatives. The fourth generation brings a whole new level of applications to smartphone users, thus changing dramatically the capabilities of their users and potentially even reaching 100 Mbps in download speeds.

Turning to the effect of the different generations, we note that use of second generation devices in a country has the lowest impact on GDP reaching 0.39 percent for every 10 percentage point increase in adoption. The broadband effect is manifested in the results from third and fourth generation controls. Countries that introduced 3G enjoy an additional 0.09 percent increase in their GDP for every 10 percentage point increase in adoption over others with simpler technologies available. This effect jumps to 0.11 percent of GDP for an identical increase in adoption in cases where 4G has been introduced. The broadband dividend is thus identified in the model as a direct growth-promoting effect that is positive and significant over a relatively long period of time for our sample of countries.

The estimations we have made based on data for the period 2000-2015 allow us to project into the future. Given the announced plans of Mexican operators for increased investments in 4G technologies, the falling price of mobile broadband offerings and other changes in market structure discussed above, Mexico can aspire to catch up its past poor performance, reach the level of the “baseline” country in our sample by 2020 and even overtake it. This would depend on an increase in subscribers by approximately 5 percent of population on an annual basis and a progressive transition towards 4G mobile broadband by the majority of the subscriber base. This favorable outcome has the potential to add an additional 4 percent to GDP in the period from 2016 and 2021. While this maximum figure is an aspiration, in our view the calculation shows a realistic possibility for the economy to gain an appreciable benefit from the regulatory and other interventions described in this paper.

## VII. SUMMARY OF PUBLIC POLICY RECOMMENDATIONS

We began by noting that the digital revolution has touched upon production, transactions and consumption by reducing costs, bringing services closer to all consumers, old and new, and creating new categories of goods and services. It has also increased dramatically the way people communicate – from a simple voice call, to a video call, text messages and even increasingly large social and professional networks.

This paper has argued that Mexico has an opportunity to grasp the benefits of pursuing a coordinated policy for the digitization of the economy. We have suggested that there are “pull” factors for doing so, driven by the prospect over the next few years of “catching up” on past performance, as well as benefitting from future deepen-

ing of the digital economy. But there are also “push” factors in play: because economies in the neighborhood and globally are pursuing similar initiatives, Mexico cannot afford to be left behind.

We list here some public policy recommendations which are by no means exhaustive, nor a substitute for a more thorough and comprehensive policy analysis.

**Connectivity:** The most conspicuous outstanding task is to maintain pressure through competition in the market place to extend both the speed and the coverage of connectivity. Our measure of the potential of connectivity revolves around the roll-out of fast mobile broadband as a foundation for the digital economy. The status quo in Mexico has proved resilient to change, and this is an argument for stronger or more persistent intervention by the regulator to diminish the influence of the preponderant over the sector.

**Avoiding contradictory or overlapping regulatory responsibilities:** In relation to wider issues in the digital economy including sectors using communications services as well as supplying them, we recommend that the various regulators involved – notably IFT, COFECE, PROFECO and the financial regulators (CNBV, Banxico and CONDUSEF, most notably) establish clear rules as to which takes the lead in dealing with the different elements of the ecosystem. The creation of the IFT as an independent regulator has been a fundamental pillar of progress and as such, it should be allowed to mature and should be, if necessary, strengthened in its responsibilities.

**Trust:** Trust is a complex concept to define. In principle, it is the reliance on the integrity of whichever process is being supported by the network. Trust takes time to build but seconds to destroy. From a policy standpoint, it is hard to define rules that increase trust in the system, but it can be addressed through a series of measures. Consigning both personal data and payments to the Internet requires an act of courage. It is important that both public and private sector agents appreciate this fully, with the government taking a lead on cybersecurity, and giving a good example by the care and attention which it gives to maintaining it. If trying to solve a problem burdens the consumer with excessive costs – such as figuring out how to contact the provider, having to comply with a large number of unreasonable requests or spending significant time and effort – trust will be undermined. Antifraud measures without unnecessarily increasing the complexity of transactions – must be put in place. These issues most likely require policy intervention.

**Skills and appropriation:** Though basic communication services can easily be put to use (nobody by now needs to be taught the wonders of making a phone call), a somewhat more sophisticated use of communications requires the development of skills. Self-evidently, skills are essential to the successful digitization of the economy. It is generally assumed that rethinking the process of education and training should begin very early, possibly pre-school. One of the most efficient ways to build digital skills is to create the need for digital services. Policies that move in this direction create a

fertile ground for the development of skills. Some can be mandatory (such as requiring that tax returns be submitted online); others can be through negative incentives (such as imposing additional costs for performing certain activities off-line instead of online); and others through positive incentives (such as rewarding certain types of behavior, like asking for invoices even though they cannot be used for deductions). Public policy should incentivize all potential digital activities through such schemes.

**Promotion of innovation:** Software, and, more specifically, apps, are a fundamental element of the digital economy. Our research has shown that Mexico is weak in this area on the basis of the metric of the percentage of total app revenue attributed to Mexico generated apps. This might suggest a need for some public intervention, in terms of targeted promotion funds, fiscal incentives, legal processes simplification, and, most importantly, in the development of human capital, which should be an integral part of the education system.

**Public services:** These should play a key and fundamental role in any government and national digitization strategy, and should be coordinated among all public entities to increase effectiveness. The provision of public services through digital means creates the need for access, which becomes an important incentive for appropriation. While public services tend to be thought of as federal, state services form the bulk of day-to-day transactions with citizens. Trying to adopt a general standard for those services may help create a virtuous circle among the various states and create a race to improve these services.

This is by no means an exhaustive list of policy recommendations, but it provides a starting point to help the digital ecosystem permeate the Mexican economy.



