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CPI COMPETITION POLICY INTERNATIONAL

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LETTER FROM THE EDITOR

Dear Readers,

As per tradition, this August 2021 Antipasto edition of the Antitrust Chronicle features articles from members of the CPI Editorial Advisory Board.

This set of articles covers a variety of jurisdictions and a diversity of antitrust topics including, among other things, the treatment of innovation in merger analysis, consumer patterns in online markets, controlling market power in online ecosystems, the effectiveness of remedies in recent U.S. merger clearances, and failure to file under the Chinese merger control regime.

We are pleased to kick off this CPI Antitrust Antipasto edition with a CPI Talks… with Ioannis Lianos, President of the Greek Hellenic Competition Competition ("HCC"), who addresses the manner the HCC has dealt with the various challenges it faced during the COVID-19 pandemic, all of which are of relevance to enforcers and practitioners the world over.

Looking forward, our August and September Chronicles will feature contributions from U.S. State AGs, and deal with the pressing issue of the treatment of so-called "free" markets, and the evergreen question of tying & bundling analysis in antitrust law.

Lastly, please take the opportunity to visit the CPI website to watch CPI TV — our selection of exclusive video content, featuring interviews, roundtables, and fireside chats with such esteemed interlocutors as Joseph Stiglitz, UK CMA Chair Jonathan Scott, HCC President Ioannis Lianos, and many others. This is a convenient way for you, our readers, to keep up with cutting edge debate from the comfort of your homes.

As always, thank you to our great panel of authors.

Sincerely,

CPI Team

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CPI Talks…

With Ioannis Lianos

In this edition of CPI Talks we have the pleasure of speaking to Ioannis Lianos, president of the Hellenic Competition Commission ("HCC").

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Digital Markets: The Challenges of National Enforcement in a Global World

By Rachel Brandenburger & Christopher Hutton

The proliferation of measures across the globe designed to address concerns about the functioning of digital markets has been remarkable. In the last 18 months, a veritable patchwork of new regimes and measures has been introduced or canvassed; and more are likely. Although the measures are at different stages of design and implementation, they appear to have the same broad aims: to address a perceived gap in antitrust enforcement powers and concerns about digital platforms' exercise of market power. But very different approaches have been adopted to the nature of the measures being proposed or introduced and the methods and scale of enforcement. The absence of a single global approach will likely create considerable challenges for all concerned: the digital platforms, the users and others the new measures are intended to benefit, and those tasked with enforcing the new measures.

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Proposed New EU Competition Rules for Distribution Agreements – A Rebalancing for the Digital Age

By James Killick, Tilman Kuhn & Peter Citron

On July 9, 2021, the European Commission ("EC") published for public consultation a draft revised Vertical Block Exemption Regulation ("VBER") and draft revised guidelines on vertical restraints ("Vertical Guidelines"). The EC has made substantial revisions, in particular adjustments to the rules governing dual distribution, dual pricing, and parity obligations.

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Controlling Market Power in Digital Business Ecosystems: Incorporating Unique Economic and Business Characteristics in Competition Analysis and Remedies

By Diana L. Moss

Digital business ecosystems ("DBEs") reflect the culmination of progressive changes in business models over the last 40 years. Coupled with the unique economic characteristics of the DBEs, these features amplify concerns arounds their ubiquity and significant market power. This article argues that existing competition analysis and proposed remedial approaches miss important implications of the complex business model and unique economic characteristics of DBEs. These include pervasive market failures, economies of scale in cloud computing technology, and algorithmic preference-shaping, all of which have myriad implications for assessing and controlling market power. If unaccounted for, these features will likely lead to competition analysis and policy approaches that do not appropriately target the source of DBE market power and vast capacity for expansion and growth.

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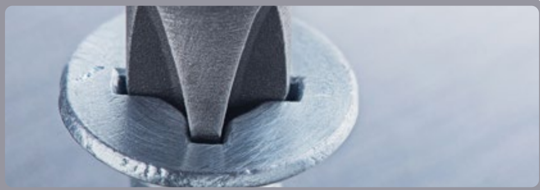

Fix It or Forget It: A "No-Remedies" Policy for Merger Enforcement

By John Kwoka & Spencer Weber Waller

The inherent limitations of remedies as a method of resolving competitive concerns with mergers have become more evident. The expansive use of remedies in actual practice has likely exceeded the capabilities of agencies and courts; and empirical evidence has increasingly cast doubt on their effectiveness. Accordingly, we propose a "no-remedies" policy under which the antitrust agency would not accept any conduct remedies and only limited divestitures. The agencies would only consider those structural changes that have been undertaken (or at least committed to) prior to the parties' filing their merger proposal and would not enter into negotiation with the parties during the review period. This "Fix It or Forget It" ("FIFI") policy would encourage merging parties to initiate the necessary competitive fixes and permit the agency to evaluate precisely what the parties file in their proposal. We believe this policy would strengthen merger enforcement by restoring the traditional roles of the agencies and the courts.

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"Something Is Happening Here but You Don't Know What It Is. Do You, Mrs. Jones?" Dark Patterns as an Antitrust Violation

By Jay L. Himes & Jon Crevier

Internet users surfing from one website to another, or using various web-enabled applications, regularly encounter "dark patterns" — web-design choices that trick users into unknowingly providing more time, money, or attention than they realize. Dark patterns thus manipulate users, impairing their ability to exercise free choice and to express their actual preferences. Their use on the web is pervasive. Moreover, as artificial intelligence develops and as the "internet of things" rolls out, the ability and opportunity to manipulate and exploit consumers via dark patters will, predictably, increase. This article discusses various dark pattern techniques and explains the conditions accounting for their frequency of use in the digital space. Legislation prohibiting dark patterns and litigation challenging them as deceptive acts or practices are becoming available. However, dark patterns also have anti-competitive consequences, as they shift surplus from customers to suppliers, while also raising rivals' costs to compete. Accordingly, antitrust enforcement should also be available to remedy these ubiquitous and pernicious online practices.

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Recapturing the Business Side of Innovation in Antitrust Merger Analysis

By Kent Bernard

The antitrust laws were not passed as an academic exercise. They were passed to break up the great Trusts, and to preserve competition. These were and are business issues. Our current debate over the impact of mergers on innovation seems to have left that business purpose and dimension out of the discussion. It is time to bring business reality back into the antitrust analysis. Innovation drives progress, and is a key factor in determining the success or failure of a business, an industry, and society overall. Innovation also is a concept with a rich heritage in business and social science. But our current legal discussions focus on only a part of what makes innovation important. We have set up a distinction between the idea of an innovation and the development of that idea into a successful product, and then downgraded or ignored that second part. But the transition from idea to product is a critical step in the process. After reviewing the ways in which innovation has been defined in the legal literature, we propose a definition arising out of the business world that captures the full meaning of innovation. It turns out that the current approach to evaluating the impact of mergers on innovation doesn't really have much to do with innovation at all.

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Failure To File Reportable Mergers – Update from China

By Jet Deng & Adrian Emch

Like many other jurisdictions, China has a system of compulsory pre-closing merger control. Like other jurisdictions, the Chinese antitrust authority – the State Administration for Market Regulation ("SAMR") – investigates and punishes companies for failing to file reportable transactions. Quite unique to China, in contrast, is that companies are queuing up before SAMR to get fined. Why? This paper will take a deep look at China's failure-to-file decisions and reply to this and other questions.

WHAT'S NEXT?

For September 2021, we will feature Chronicles focused on issues related to (1) **Tying & Bundling**; and (2) **Free Isn't Free?**

ANNOUNCEMENTS

CPI wants to hear from our subscribers. In 2022, 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.

CPI ANTITRUST CHRONICLES OCTOBER 2021

For October 2021, we will feature Chronicles focused on issues related to (1) **Imperfect Competition**; and (2) **Breaking Up Is Hard to Do?**

Contributions to the Antitrust Chronicle are about 2,500 – 4,000 words long. They should be lightly cited and not be written as long 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 to Sam Sadden (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 on any topic related to competition and regulation, however, priority will be given to articles addressing the abovementioned topics. Co-authors are always welcome.

…with Ioannis Lianos

In this edition of CPI Talks we have the pleasure of speaking to Ioannis Lianos, president of the Hellenic Competition Commission ("HCC").

Thank you, Mr. Lianos, for taking this time to talk to CPI.

1. How has the HCC dealt with the COVID-19 pandemic, and are there any learning experiences that you would like to share?

Definitely, the pandemic has been an important challenge. The first important issue that we had to consider was to maintain the functioning of the HCC during this difficult period.

First, we had to very quickly make the necessary investments to ensure that we could move to teleworking. I think we managed to do that very quickly, and we have been among the first public authorities in Greece, to put in place teleworking for almost all of our staff. That also included the meetings of the board of the HCC. We also had to put in place the necessary changes in our legislation and internal regulations so as to be able to have these meetings of the board, in particular for merger cases, but also for antitrust cases, through teleconferencing.

Also, we had to deal with the market situation, which was drastically changing with this supply and demand shock occurring. So, we had to devise mechanisms to somehow limit the competition law problems that this could create. We were the first authority that issued a recommendation with regards to maximum resale price maintenance, inspiring the rest of the ICN and other commissions to issue a joint statement that mentioned this as a possibility.

We also created a specific website that provided information to companies and citizens about the different competition law issues that emerged. It listed the various initiatives that competition authorities around the world were taking to deal with the crisis, as well as what companies around the world were doing to deal with the crisis. We put in place a helpdesk in order to provide information to anyone who wanted to see if they could cooperate, if the specific type of actions that they were envisioning were compatible with competition law.

To a certain extent, the pandemic provided us with the opportunity to somehow move to a more digital HCC. We put in place a system of digital services for consumers and citizens, so they could place a complaint through electronic means or follow their complaints and individual cases. We created an in-house platform – the HCC economic intelligence and data analytics platform – that is actually a quite unique system which collects and harvests information from all major supermarkets about the thousands of products every day, as well as other types of data that is available publicly.

For instance, this includes data from local markets in terms of fresh products, and data coming out of the e-fuels database, which includes the price of fuels across the country. So, all this data is now collected to the HCC's central platform, and this platform will have various dashboards that enable us to very quickly analyze this data and see market tendencies. Also, we put in place, in cooperation with a number of economists, screening tools to help us identify situations where we might need to have more information from the specific companies and where are somehow red flags about possible anti-competitive behavior.

This system has been in place for a few months, and it operates very well. It provides us with a very good understanding of market tendencies, and we are expanding it to include public procurements, so as to be able to screen for bid rigging type, as well as adding new products to take advantage of our interactions with price comparison websites, etc.

This also gave us the opportunity to put in place a whistleblower system through our platform, and we have seen quite considerable advantages to this system. The leniency policy in Greece hasn't really functioned very well, although it has been there for some time. Because the market is pretty small, everyone knows everyone so it's pretty difficult in this context for a leniency policy to work. The fact that we had the pandemic and the fact that we have been thinking more digitally enabled us to put in place this anonymous whistleblower information platform, and that has been in place for a few months now.

That has led us to some interesting cases that could open through information that was actually provided to us through this whistleblower platform. So, in a way, the crisis has been a major challenge for us, but also an opportunity to change. I think it created a culture of change with the staff at the authority, so some things that would have required more time for people to get acquainted to and organize had to be done very, very quickly. And we can now reap the benefits of this digitalization as our processes have been streamlined.

There is more transparency in the way the authority works, and we have a good basis to increase this reliance on digital means, in particular, in the context of the IT forensic type of work that authorities need to develop a bit further.

So, with regards to that, we put in place a IT forensic unit. We are now proceeding to the recruitment of a Chief Technology Officer and a team of data scientists that will help us use artificial intelligence tools, deep learning, and machine learning in our cases, and we have also procured software that we use.

It's a quite advanced software platform that we use to augment the capacity of our staff in analyzing big data, and quite important sources of information we collect in downgrades, for instance. Let me also add that the Greek authority has been one of the few that proceeded to downgrade during the periods of the crisis. Also, I mean, the last couple of months we have proceeded with a number of downgrades, and I think that's very important. I mean, always respecting having specific protocols and respecting actually the public health requirements that are needed for protection for both of our staff, but also of a company's staff that we are investigating.

I think this was extremely important for us to continue to pursue, because it's very important to keep a little bit of the deterrent effects of a competition authority during the period of crisis. It was part of the strategy that we developed for whenever we had a window of opportunity because we're not in lockdown. For instance, we already have organized a down rate that could help us progress an investigation, and also provide a message to the market that we're still here and we're taking our role very seriously. These were a summary of some of the challenges and opportunities that we had to deal with during the time of the pandemic and we're still dealing with them actually.

2. The HCC has clearly faced numerous challenges of late, yet these challenges also present opportunities for achievements. Are there any particular achievements you would like to mention?

One of the major achievements we had is that when I joined the authority, we had quite a lot of old cases. The average age of cases when I joined was around eight years, and we had cases that had been at the authority for almost 20 years. There was a huge backlog and this was a major problem.

Very quickly, we put in place a new organization with a specific task force or staff that focused on dealing with this backlog of cases. Now, the average age of our case is less than two years, so we managed to go from eight years to two years in basically 12 months. We finished more than 130 cases, some of which actually moved to a second stage and were investigated after by the board.

I think we managed very quickly in a year to become relevant again in terms of the timeliness of our enforcement. We are in the process of finalizing in terms of settlements or possible remedies and not fines. Obviously, this will be decided by the board, in cases that started basically a few months ago. This is really, I think, an achievement we're only able to have because of the work that has been done by the staff of the authority; the huge work that the staff of the authority with an important commitment to finalize old cases.

But, of course, there are not just old cases, but also new ones. I think we started a strategy of enforcing competition much more systematically and with a specific priority program. The authority, since 2020, every year there's a discussion based on information about the economics of the various sectors and the priorities of the authority, so we immediately prioritize some sectors of the economy and act by bringing cases.

We had a very important investigation that started with regards to banks. Almost a couple of months after I joined, we did the biggest downgrade ever of the authority to all the systemic banks. This investigation is still in process, so we are continuing, and obviously it will be finalized, I hope, soon. We invested hugely in staff as well as IT and software, specific software, to enable us to assess all the data that we're collecting in the context of that investigation.

We also finalized a sector inquiry for supermarkets. This sector inquiry started many years ago, I think it was in 2012. In 2019, we arrived, and it wasn't complete and actually not much had been done.

We moved very quickly to finalize this sector inquiry by structure, and also by the model of sector inquiries. A little bit like in the UK, we have the market investigation reference, by having an interim report and having a process of public consultation. This is very important for the authority to interact and to get this public consultation, and the final report was published and also included some proposals and remedies.

We then started a sector inquiry on e-commerce, and the interim report has been released. This is the first time that the e-commerce, or just digital commerce, was investigated by the competition authority, and the first time there's been such a quite broad analysis of e-commerce, in particular for products, by a public authority in Greece.

We also started two regulatory interventions, one in the context of the press distribution monopoly that we have, which raises quite interesting issues of obviously polycentric competition law. And secondly, in the context of the construction industry, which are to my knowledge, the first sector investigations which deal with the common ownership issue.

In that context, we also organized a conference on common ownership in cooperation with a journal in the competition law and economics. We adopted, most recently, a fine of 1.1 million euro for an abuse of dominance case in the gas appliances market. We have already dealt with some interesting practices, probably the first time these practices have been dealt with, by the company Diageo in the market for drinks in bars and in restaurants, etc.

We also commissioned a report in the context of our e-commerce market investigation. Preliminarily, it was in our investigation, a report on the situation of mobile data prices in Greece. It was the first time an authority had commissioned a report about this issue, because obviously there are problems in this market. Greece has quite high prices compared to other European countries, or also other OECD countries.

Most recently, we started a market investigation reference inquiry in the context of the healthcare sector and health insurance. Part of that inquiry is to analyze the changes that occur in this industry. Of course, there are local aspects in terms of concentration, but there are also very interestingly technological aspects. For instance, the use of data. The fact that we see now insurance and healthcare becoming part of the same value chain through this use of data and the development of personalized medicine. Aspects which, to my knowledge, haven't been investigated by another competition authority so far. We would like to somehow to develop this in the next few months in the context of a major structural change that we are seeing is happening in the Greek market.

In addition, I can announce that the authority will initiate another sector inquiry; a market investigation reference that has been decided by the board and it will be out next week. It is on waste management and recycling. We think this forms part of our major initiative on sustainable development and competition law. This has been a major issue that we have been investigating in cooperation also with other competition authorities like the Dutch competition authority. We published a discussion paper in September 2020, we organized a major international conference on this topic with participation of high officials from the European Commission and other national competition authorities. We commissioned, with the Dutch competition authority, a joint technical report by environmental economists and IO economists, so the first time that these two groups have been put together to think about the way sustainable development might be degraded, competition analysis, and the metrics that we can actually use.

Finally, most recently published a few days ago, the Sandbox Proposal for sustainable development that the HCC has put in place. This is a proposal that changes the way we conceive the role of competition authorities. We think that in the context of our advocacy efforts, in particular in small markets like Greece where we have a number of small and medium firms that face considerable problems to somehow get funding from banks, the banking system, or out of the investors for their green position.

We think it's very important to use any possible way to reduce the legal uncertainty that these may have in the context of engaging in a corporate initiative that might face problems from a competition perspective. So we think it's very important for competition authorities to clarify the situation, and to assist somehow these companies, in particular where they develop some innovative model, or project. We also think it's very important for competition authorities not to intervene after the fact where the market has tipped and actually, we cannot really do much, but before the fact so that we can avoid problems that might emerge in the future.

To a certain extent, by helping companies see the possible competition problems that might emerge, and providing them more clarity about our way of thinking, we help them projects in a way that could be compatible with competition law, but obviously promote sustainable development because it's obviously something we very much care about. I think these are some of the highlights of our enforcement and more generally actions in the last 21 months.

3. The HCC has adopted numerous initiatives in the past months. Can you advise other authorities on how to adapt more efficient processes and implement initiatives in a timely manner?

It's not an individual task, it's a joint task. I think the staff here were fantastic. They were very committed during the pandemic to the authority. Even if they have suffered because of the economic crisis and quite considerable pay cuts in the last two years, despite that fact, they have been very active. We have also been very lucky to cooperate with a number of experts, economists, lawyers, and technology experts from major universities in Greece, but also from abroad that believed in our efforts and helped us with very minimal cost compared to what we would pay in the market there.

They have been a little altruist in their way of helping us to develop these different projects, but I think, for us, it was very important to change the institutional structure of the authority. This is something I haven't mentioned. We changed completely the institutional structure of the authority, we moved from a system where we had the separation of lawyers and economists in different directories, to a mixed directory system where we have directories on the basis of sectors of the economy. Mixed directors where there's a lot of interaction and interdisciplinarity, we want really to focus on that. We put in place a very advanced program for training staff in data science, econometrics, and we brought very wonderful colleagues from the universities. Mostly recently, we had Richard Whish, we had Pablo Ibanez Colomo, and we had Alexandre de Streel who came actually and provided us with training, as well as Greek colleagues. And also, we have been at the same time working on a change of our legislation.

We submitted a new bill. The law proposal which has principally the objective first to transpose directive 2019/1 the ECN directive, but we took this as an opportunity to change more broadly competition in Greece. This is a bill that I hope the government will put to parliament. We have to see when this will be published, but in this bill we have some major changes; quite innovative ones. The first one concerns a new provision on abuse of ecosystem power, and this is really a major future innovation for this bill, as well as among other things. The possibility to adopt no action enforcement letters for the authority in case there are some important public interest objectives that require the authority to somehow clarify the position that they have upfront, and also in order to promote sustainable development. It's part of our effort to somehow develop more the right incentives for great firms to make this green transition as soon as possible. These are some of the changes that were part of this new law, and we hope that we'll see that passing in parliament very soon.

4. What are your views on the DMA? Are there other sectors that the HCC is focusing its attention on? Among other things, you mentioned construction, e-commerce, grocery, gas, healthcare, and waste management. Is there any other sector that you think deserves scrutiny that you didn't mention before?

Of course there is, but I cannot disclose that at this time. We have a program that we put in place for certain types, and we have different tools, and I think the Greek RICLO is very good with regards to that. We have already a mock investigation tool that we haven't use for many years. The last time it was used was 2009. We launched two last year, so we have made use of that tool. We issued an opinion as well in the press distribution area, so obviously we prefer to issue opinions, and obviously we have antitrust enforcement as well as merger control.

I think it's important to make a program of first the problems and then you know the tools that you have to deal with the problems. Some problems can be dealt with in Article 101 or 102, or an equivalent national investigation. Others needs a different type of sector inquiry, or even regulatory intervention. This is something that needs to be done after you've done some form of mapping. I think this is also one of the major changes in our new law because it gives competence to the authority to do the market mapping.

We will proceed, and for this reason, we are recruiting a chief economist and team of economists to start the process of mapping the Greek markets in the model of the UK having a state of competition report, to basically develop some indexes that we can use, some criteria we can use in order to see if the market is competitive or not. What is interesting is that we are trying to link this effort of mapping to the market and look into what is the situation in markets with the development of KPIs for the competition authority.

We are the first public authority in Greece that has somehow issued KPIs. We have the obligation to develop KPIs, and these are not developed by us, but actually by an independent commission of experts, members of which are appointed by the European Commission, as well as the governor of the Bank of Greece. We try to have independence to look at our work. On the basis of our performance in these KPIs, we have the possibility at the authority to gain a bonus in terms of extra resources automatically without that being subject to ministerial discretion.

That gives us an incentive also to improve ourselves, and what I'd like to do, and we have done in the process of organizing this, is to connect these KPIs at the authority level with the KPIs we're going to have at the staff level, and in particular, the bonus system that we would like to put in place. That's partly the ambition. We have been working with the OECD Gulf with regards to developing a system that might follow the best practices on how both systems can work in the context of the public administration.

But again, that needs a lot of work in terms of pushing for these reforms. Usually, the politicians are quite tough to convince, and we need always to make the case of the importance of competition in markets, the competition law enforcement. These are not always self-explanatory, and I think there's a lot of work to be done by our community, meaning the academics and the enforcers of competition law, to develop somehow tools and let's put it like communication strategies. To convince not just the public and the companies, but also the politicians that are investing in competition and promoting competition is something which very important for welfare, both consumer as well as for general welfare and wellbeing.

5. Thank you. The above summarizes well what you think could be the future direction of antitrust enforcement, both domestically and internationally. Is there anything else you want to add?

With regards to the last issue you mentioned, it's quite important to think more carefully about the way technology could be integrated in our proceedings, and in particular AI. This is really the most important challenge we will have, and that's why we have been very supportive of the development of this new work, and new research on competition law and economics. We actually drafted the report on the basis of what we have done here at the authority in terms of developing the platform and new tools on the basis of AI to help us in our work for the British Competition and Policy Center.

We drafted what was published on our website a few months ago. We also organized a conference, which is available to see on our web page, bringing in a number of scholars that have been doing a lot of work in this area of competition and competition economics. We are now thinking with our partners to develop a hackathon to somehow participate that could provide some form of incentive for programmers that are usually not thinking about competition law to somehow focus on that, and develop the tools that the competition authorities need.

We think that this is quite important in particular in small markets like ours where we don't have a number of upper-level specialists. I think it's very important also for jurisdictions that are proven jurisdictions in terms of staff and technical capacity to have these kinds of international efforts. We will be suggesting having it in the context of an international organization that focuses on competition and policy to somehow augment their capacities and being able to develop tools to better monitor their markets.

I think that's one of the major issues we'll develop in the future, this competition analysis and economics. And the second is the challenge of sustainable development and competition law. I think this is something that will occupy us for the foreseeable future, and of course, as competition is very marginal, in what it can do to avoid the climate change or to somehow limit the possible risks of environmental degradation, but I think it can contribute to that. I think that's really something that you should have in mind.

DIGITAL MARKETS: THE CHALLENGES OF NATIONAL ENFORCEMENT IN A GLOBAL WORLD

BY RACHEL BRANDENBURGER & CHRISTOPHER HUTTON[1]

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I. INTRODUCTION

The proliferation of measures across the globe designed to address concerns about the functioning of digital markets has been remarkable. Within the last 18 months alone, a veritable patchwork of regimes and measures have been introduced or canvassed.

Although the measures are at different stages of design and implementation, all have (on the face of it at least) the same broad aims: to address a perceived gap in antitrust enforcement powers and concerns about the exercise of market power by digital platforms. However, despite those common aims, very different approaches have been adopted. The differences in approach are manifested not just in the nature of the measures being proposed or introduced, but also in the methods and scale of enforcement.

This multiplicity of measures, and the absence of a single global approach, gives rise to considerable challenges. The need to navigate multiple regulatory regimes is not a new phenomenon, but the nature of digital platforms and the vast number and variety of businesses and customers that interact with them, heightens the challenges. Those challenges are not only for the digital platforms to navigate, but also for those who the new measures are intended to benefit, and those whose task it will be to enforce the new measures.

It is in the interests of all stakeholders that any measures aimed at digital platforms work effectively for all concerned, especially when legislation and enforcement occur at the national (or sometimes regional) level, whereas the digital marketplace is increasingly global in scope and reach.

II. DIGITAL MARKETS REGIMES

A Patchwork of New Regimes

Whatever your views are on the necessity or otherwise of the enhanced scrutiny that digital platforms now find themselves under, it is undeniably the case that the recent focus on digital platforms, and the multiplicity of measures that focus has given rise to, is one of the most remarkable developments in antitrust (or competition) law and enforcement in recent times.

One of the most noteworthy aspects of these developments is the fact that they are rooted in an acknowledgement of the apparent inadequacy of the current law and enforcement. As the Chief Economic Adviser of the UK Competition and Markets Authority said, when asked to comment on the different approaches to the regime changes being proposed in the UK and the European Union ("EU"): "*Both regimes respond to long-standing concerns that existing enforcement powers aren't sufficient to address competition concerns in fast-moving digital markets, nor have the requisite deterrent effect on the largest digital players*."[2]

The necessity or otherwise of new enforcement powers is an issue on which people have often strongly opposing views. The basic principles of antitrust law have hitherto generally been regarded as being sufficiently flexible and adaptable to serve their purpose even though the enforcement of those laws is often complex. This is reflected in the fact that, although there are differences in substance and enforcement across jurisdictions, the basic principles of antitrust law are common to many jurisdictions, and have remained unchanged for many decades. That many law-makers and antitrust enforcers, across the world, now consider existing antitrust laws and enforcement tools to be insufficient to meet the challenges arising in digital markets, is therefore noteworthy.

To a certain extent, the aims of the various new measures and regimes are common across jurisdictions: to limit the ability of digital platforms to exercise their market power at the expense of those who interact with, or depend on, those platforms, and to promote competition and consumer choice. However, alongside those aims is another noteworthy feature of the measures that are being proposed and adopted: the diversity of the different approaches that are being taken.

Such is the multiplicity and diversity of those measures, introduced or proposed, that a comprehensive survey of them is beyond the scope of this article. However, looking at just a few jurisdictions illustrates this:

- In the EU, the proposed Digital Markets Act will, if adopted as proposed, enable the European Commission to designate certain digital platforms as "gatekeepers," and impose an extensive list of antitrust-inspired obligations on those platforms.

2 Mike Walker speaking at Innovation Economics Conference for Antitrust Lawyers #2, Geopolitics of Platform Regulation webinar (28 April 2021). Available at https://www.concurrences.com/en/conferences/innovation-economics-conference-for-antitrust-lawyers-2-geopolitics-of-99064.

- In the UK, the proposed Digital Markets regime will, if implemented, see some digital platforms designated as having "strategic market status" and being the subject of binding codes of conduct "tailored to each firm."

The differences between the proposed EU and UK regimes in particular highlight the potential for conflict. The EU approach is to adopt a single set of rules across all "gatekeepers," whereas the UK approach is to adopt individual sets of rules for each digital platform to reflect the differences in the platforms and the ways in which they are used. There are advantages and disadvantages to each approach, but it is easy to envisage that a digital platform subject to both regimes could face having to comply with two sets of rules. Even if, for the most part, the rules were consistent, it is perhaps inevitable that some aspects of one set of rules may be stricter than the other set, or sufficiently divergent that they require different operational approaches by the affected digital platforms. In some instances, the rules could even be contradictory.

Across the Atlantic, the U.S. is seeing a plethora of legislative proposals focused on digital markets and in some cases also more broadly to introduce substantive and procedural changes to Federal and some State antitrust laws generally and to increase the funding of the Federal antitrust agencies. Prior to the introduction of these proposals, the Democratic members of the U.S. House of Representatives Judiciary Subcommittee on Antitrust, Commercial and Administrative Law issued a report[3] on competition in digital markets. The Report provided an overview of what the authors regarded as the limited effectiveness of the current US antitrust laws as applied to digital markets. The themes outlined in the Report laid the groundwork for the subsequent various legislative measures targeting digital platforms that were introduced by both the House and the Senate in early 2021.[4]

If passed into law, these measures would have a direct effect on the business practices of certain digital platforms. Four of the bills introduced into the House of Representatives in Spring 2021 are particularly noteworthy for the purposes of this article. They would apply to "covered platforms" and would 1) impose interoperability and data portability requirements intended to lower barriers to entry and switching costs for businesses and consumers[5]; 2) make it illegal for covered platforms to operate another line of business or leverage their control across multiple business lines to self-preference, disadvantage competitors, or create a conflict of interest[6]; 3) prohibit covered platforms from engaging in discriminatory conduct that "advantages the covered platform operator's own products, services, or lines of business" over its rivals[7]; and 4) prohibit covered platforms from acquiring nascent competitors.[8] At this stage, it is unclear whether there will be sufficient support to achieve legislation and, if so, on which measures.

Legislative changes directed at strengthening enforcement against digital platforms have also been adopted, or are being considered, elsewhere around the world, including Australia, China, Germany, Japan and South Korea.

B. Enforcement

It is not just the nature of the measures implemented that may differ from one jurisdiction to another. There may also be significant differences in the ways in which the measures will be enforced. As with many laws and regulations, the practical boundaries of individual regimes will be set by enforcement activity, which is, in turn, driven not only by overarching policy but also by complaints from third parties and the varying institutional frameworks within which the regimes operate. The role and influence of courts and judges, for example, differs significantly between prosecutorial regimes (such as the U.S.) and administrative regimes (such as the EU).

A large number of investigations have been opened, and litigation cases brought, against digital market players in the last two years (including by Federal and State enforcers in the U.S., the European Commission and EU Member States including France and Germany, as well as in Australia, China, India, Japan, Russia, South Korea and elsewhere). The number of investigations and cases continues to increase – sometimes, seemingly on a weekly basis. That many of the investigations and litigation cases have been launched using existing antitrust powers - and often ahead of the implementation of applicable digital markets regimes - is revealing, in terms of the importance agencies are placing on antitrust

3 U.S. House, Subcommittee on Antitrust, Commercial, and Administrative Law of the Committee on the Judiciary, Majority Staff Report and Recommendations, Investigation of Competition in Digital Markets (2020) (hereafter the "Report"). Available at https://judiciary.house.gov/uploadedfiles/competition_in_digital_markets.pdf?utm_campaign=4493-519.

4 See Office of Representative David Cicilline press release, Cicilline Statement on Big Tech Markup (24 June 2021); see also Competition and Antitrust Law Enforcement Reform Act, S.225, 117th Cong. (2021).

5 Augmenting Compatibility and Competition by Enabling Service Switching (ACCESS) Act, H.R. 3849, 117th Cong. (2021).

6 Ending Platform Monopolies Act, H.R. 3825, 117th Cong. (2021).

7 American Innovation and Choice Online Act, H.R. 3816, 117th Cong. (2021).

8 Platform Competition and Opportunity Act, H.R. 3826, 117th Cong. (2021).

enforcement in the context of digital markets. It seems that even if agencies consider their current enforcement tools need revision to match the challenges of digital markets, they also consider that they cannot wait to take action until new enforcement regimes are in place.

Although the number and scope of these opened investigations and cases indicates a direction of travel, and could (even without coming to conclusion) influence changes on a voluntary basis on the part of digital platforms, the full impact will only become clear if and when final decisions and judgments are reached.

Moreover, it is noteworthy in that regard that:

- Not all investigations that are opened may be pursued, and some may settle (with or without commitments). However, even those cases will be instructive in illustrating the practical impact of individual regimes, particularly where digital platforms voluntarily introduce changes to reflect concerns and settle investigations in place of litigating to an end result.
- A common theme across cases involving digital platforms is that they tend to be far from straightforward: the operational, factual and legal issues are often extremely complex and novel (as the perceived need by many regimes for new enforcement powers against digital platforms testifies). As a result, it will take some time, maybe years, before the outcomes of the current wave of investigations and cases is known. Indeed, given the pace of innovation and development in digital markets, the outcomes of some of the current investigations and cases could have limited practical impact by the time they come to a close.

III. THE CHALLENGES OF MULTIPLE NATIONAL REGIMES IN GLOBAL MARKETS

It would be foolhardy to predict the exact scope and focus of future enforcement. However, what is clear is that there is unlikely to be a single global approach adopted by either those regimes that are currently proposing changes to their laws or by those that do so in the future. Such an absence of a global approach will create challenges for all concerned: the digital platforms, those that interact with them, and enforcing agencies.

A. Challenges for Those Under Scrutiny

The need to navigate multiple regulatory environments is something that digital platforms have experience of. Similar challenges are also faced by other global corporations (particularly those in heavily regulated sectors – for example, pharmaceuticals). The challenges of navigating multiple regimes is inherent in the national nature of such regimes, and those subject to such multiple regimes may become more familiar with, and adept at, dealing with the situation over time.

However, the challenges are increased in relation to digital markets because, although there will be some "micro" regulations, the fundamental purposes behind the proposed digital markets regimes are broad in scope, and seek to go to the heart of the digital platforms' relationships with the companies and individuals that they interact with. Complexity is also added by the fact that many of the issues that digital markets raise extend beyond traditional antitrust considerations to privacy, consumer protection and other issues outside the scope of antitrust enforcement. This has been recognized by, for example, the novel initiative by the UK Competition and Markets Authority and the UK communications (OFCOM) and data protection (Information Commissioner's Office) agencies to establish a Digital Regulation Cooperation Forum to provide a "joined-up approach to digital regulation in the UK."[9]

As a result, digital platforms may be presented with new challenges to navigate, and may take various approaches to address them:

- A <u>global approach</u>, by taking the strictest regime, and applying the standards and rules of that regime globally. Although this might be simpler from a regulatory and compliance perspective – a single set of rules consistently applied brings certainty and clarity – it may not reflect commercial reality. This is not just a question of whether digital platforms should unnecessarily "straightjacket" themselves by applying stricter rules even in those markets or jurisdictions where the applicable regime is less restrictive. It may also be the case that digital platforms that may be considered to have market power in certain markets or jurisdictions do not necessarily hold that market power in others. The ability of a digital platform to grow and develop (and create competitive pressure) in new markets and jurisdictions could be impaired if it decided to apply globally the standards or rules of the most restrictive regime it operates in.

9 Competition and Markets Authority policy paper, Digital Regulation Cooperation Forum launch document (July 1, 2020). Available at https://www.gov.uk/government/publications/digital-regulation-cooperation-forum.

- A national approach, by applying national standards and rules to the digital platform's activities and relationships in the relevant jurisdictions. This would likely provide digital platforms with flexibility and greater commercial freedom in the least restrictive regimes. But it would not be without complexity: navigating multiple national rules in a global world may be additionally costly and may be impractical (particularly if the relationships between a digital platform and its users and others it does business with cross multiple jurisdictions).

- A mixed, issues-based approach, by applying a consistent cross-jurisdictional approach only in those jurisdictions of greatest perceived regulatory risk (or where such an approach is feasible and desirable), and applying a tailored approach in other contexts. This is an approach that many global businesses will recognize, and already adopt. It may enable digital platforms also to avoid unnecessary regulatory straightjackets. However, although this approach provides flexibility, it may also create confusion and the risk of inadvertent breaches of applicable laws, particularly in the context of global markets and relationships.

In all cases, a key consideration will be practicability: what can operationally be achieved, given the global nature of the markets? The answers to this question could drive important navigation decisions on the part of digital platforms – deciding where to invest, where to innovate, and where to challenge. In other words, the legal and regulatory landscape that emerges from the current proposed regime changes around the world may have an effect not only on the digital platforms subject to the regimes, but also on the wider digital ecosystem and beyond.

B. Challenges for Those the Regimes are Intended to Protect/Benefit

Looking at the likely patchwork of regimes from the perspective of those companies that hope to benefit from the regimes, they too will have to navigate the new regimes and their consequences.

A key point to note is that many businesses that interact with digital platforms are themselves global. It is therefore too simplistic to view the issue as one of whether and how to address the balance of power between global digital platforms on the one hand, and small national users, on the other.

As a result, the patchwork of digital regimes gives rise to a particular practical issue for those the regimes are intended to protect or benefit: different approaches across jurisdictions may mean that some of key relationships may have different flavors in different jurisdictions. For example, if a global business (A) relies on a global digital platform (B) to reach its customers, it too will have to decide whether to approach the legal and regulatory patchworks on a global or local basis. The fact that (A) is active in a jurisdiction where there is a stricter approach does not necessarily mean that it would be advisable for (A) to aggressively challenge (B) in that jurisdiction: the fact that it could make a complaint or take action against (B) in one jurisdiction may not assist it if that means it is then commercially exposed in another jurisdiction. Alternatively (A) might seek to use a threat of action in one jurisdiction to leverage an advantage in the context of its global relationship with (B). This may give rise to forum shopping (on the part of potential complainants and digital platforms), and companies may look to one jurisdiction to lead the way and bring about a global change.

C. Challenges for Regulators

The different regimes to regulate digital markets, both those that are currently in place and new ones that are under consideration, are generally designed to address and facilitate national enforcement priorities. (The regional EU regime is, of course, an exception.) The national focus reflects a practical reality: the powers of national agencies will (for the most part) be limited to challenging conduct that occurs within, or has an effect in, their jurisdiction.

A concern for national enforcement agencies is therefore whether the, necessarily national, limits of their powers could undermine the effectiveness of national laws or enforcement policies:

- Can a national agency bring about real change if its enforcement is limited to only one geography of the relationships between the digital platform and its users and others it does business with? In practical terms, national agencies may find it difficult to prevent an exercise of market power in their jurisdiction, or prevent the practical impact of such an exercise of market power, if the digital platform can exert commercial pressure outside of that jurisdiction in a way that is beyond the reach of national enforcement.

- A further question (which is not new) is also relevant: the extent to which agencies have the power to impose global remedies and, even if they do have such powers, whether they have the wherewithal to enforce such remedies in practice. Absent the enforcement of global remedies - which could be achievable by, for example, effective cooperation between agencies across different jurisdictions

- enforcement activity in one jurisdiction is unlikely to bring about the global change that may be required fully to achieve a national agency's enforcement objectives.

That is not to say that national enforcement can lack impact. It will obviously have a direct impact on national markets and relationships contained within the jurisdiction in question. But where the relationships between digital platforms and their users and others the platforms do business with is not so contained, there may be practical limitations to what agencies can achieve without cooperation with their counterparts in other jurisdictions. It is therefore not surprising that there has been considerable multilateral discussion about the regulation of digital markets, at political and agency levels. The discussions that led to the Ministerial Declaration following the G7 Digital and Technology Ministers' meeting earlier this year[10], the work of the Organization of Economic Cooperation and Development[11], and exercises such as the International Competition Network's Survey On Dominance/Substantial Market Power In Digital Markets,[12] are a few examples of fora in which policy discussions have taken place. There are many more.

Also, it is likely that enforcement agencies will increasingly cooperate with each other in relation to specific investigations as well as issuing joint statements highlighting the scope for cooperation and consistency of approach to enforcement in relation to digital markets. The recent statement of the UK Competition and Markets Authority, the Australian Competition and Consumer Authority and the German Bundeskartellamt on their common understanding about the need for rigorous and effective merger enforcement in relation to digital markets and more generally is an interesting example of cooperation between two non-EU and one EU jurisdiction.[13]

IV. CONCLUSION

As many jurisdictions introduce measures to address concerns about the functioning of digital markets, consistency of approach will be a key factor.

That does not mean that a global regime is desirable or necessary (even if it were achievable); nor does it mean that the multiplicity of national regimes will be ineffective. However, an absence of a consistent global approach presents challenges for all stakeholders, including enforcement agencies.

The balance that national agencies and lawmakers are trying to strike between the desire to encourage innovation and investment and the desire to limit potential risks to competition and consumers is particularly complex in digital markets. In addition, there may not be agreement between the stakeholders within a jurisdiction – let alone across jurisdictions - about exactly where the balance should be stuck

Whether or not a more coordinated approach develops over time, digital platforms, and those that interact with them, will need to continue to develop commercial and regulatory approaches to navigate the patchwork of regimes that they are likely to continue to face as the number of regimes that are reviewing and adapting their laws to address digital markets continues to increase.

10 Ministerial Declaration, G7 Digital and Technology Ministers' Meeting (April 28, 2021). Available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/981567/G7_Digital_and_Technology_Ministerial_Declaration.pdf.

11 OECD, Abuse of Dominance in Digital Markets (2020). Available at http://www.oecd.org/daf/competition/abuse-of-dominance-in-digital-markets-2020.pdf.

12 Unilateral Conduct Working Group, Report on the Results of the ICN Survey on Dominance/Substantial Market Power in Digital Markets (July 2020). Available at UCWG-Report-on-dominance-in-digital-markets.pdf (internationalcompetitionnetwork.org).

13 Competition and Markets Authority policy paper, Joint Statement on Merger Control Enforcement (20 April 2021). Available at Joint statement on merger control enforcement - GOV.UK (www.gov.uk).

PROPOSED NEW EU COMPETITION RULES FOR DISTRIBUTION AGREEMENTS – A REBALANCING FOR THE DIGITAL AGE

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On July 9, 2021, the European Commission ("EC") published for public consultation a draft revised Vertical Block Exemption Regulation ("VBER") and draft revised guidelines on vertical restraints ("Vertical Guidelines"). The EC has made substantial revisions, in particular adjustments to the rules governing dual distribution, dual pricing, and parity obligations.

The draft new rules aim to address the tectonic shifts over the last decade in the way business operates, in particular with the growth of e-commerce and online platforms. Emerging new distribution formats started challenging traditional brick-and-mortar shops long ago, but the industry has undergone radical change more recently with suppliers increasingly engaging in dual distribution (i.e. selling both through retailers and through their own stores, primarily online), price comparison websites offering direct purchase options, traditional online pure players opening brick-and-mortar shops, more online retailers offering sales opportunities for other retailers via online marketplaces, and the like. These new distribution formats have challenged suppliers to think about how to design their go-to-market strategy, and consider "steering measures," such as online sales restrictions, which have been scrutinized by a number of competition authorities.

At the time of the last review of the EU vertical regime 12 years ago, a key concern was to protect online sales and ensure that suppliers could not inhibit reseller development of online sales channels. The balance has changed with the explosion in online sales, growth of online platforms, and struggling brick-and-mortar shops – a trend that has been further accelerated by the COVID-19 pandemic. The EC now considers that "online sales have developed into a well-functioning sales channel and therefore no longer needs special protection."

I. THE VBER AND VERTICAL GUIDELINES

The VBER provides parties to vertical agreements (i.e. agreements entered into between businesses operating at different levels of the supply chain) with increased certainty about the compatibility of their agreements with Article 101(1) of the Treaty on the Functioning of the European Union ("TFEU"), by creating a safe harbor exemption.

If neither party's market share exceeds 30 percent, vertical agreements, which do not contain any so-called "hardcore restrictions" (including, for example, resale price maintenance or territorial/customer restrictions), de lege benefit from an exemption. Agreements, which do not satisfy the VBER conditions, may still be compatible with Article 101(1) TFEU, but these agreements require individual assessment pursuant to Article 101 (3) TFEU.

The Vertical Guidelines aim to help companies to self-assess whether their agreements are covered by the VBER or may qualify for an individual exemption pursuant to Article 101(3) TFEU.

The current VBER, which has been in force for 11 years, expires on May 31, 2022. The draft revised VBER and draft revised Vertical Guidelines follow an extensive evaluation exercise undertaken by the EC over several years, including a 2019 public consultation, stakeholder workshop, support studies, and a working paper. The EC's evaluation has, in particular, been focused on identifying the changes that are necessary to the EU regime as a result of the growth of online sales and new market players (such as online platforms).

II. DRAFT REVISED VBER AND VERTICAL GUIDELINES – WHAT IS NEW?

A. Dual Distribution

Dual distribution covers situations where a supplier not only sells its goods or services through independent distributors (such as retailers) but also directly to end customers in direct competition with its independent distributors. The rise of online sales – in particular through suppliers' own online shops – has resulted in a significant increase in such instances of dual distribution.

The current VBER exempts dual distribution arrangements – despite the fact that the supplier and the independent distributors are technically competitors at the retail level. The EC is concerned that this exception for dual distribution is likely to exempt vertical agreements where possible horizontal concerns are no longer negligible. While engaging in dual distribution itself is, of course, not prohibited, the way a supplier who has set up a dual distribution system operates in practice may trigger competition concerns, for example the extent to which the supplier exchanges competitively sensitive information (such as prices, customers, or sales volumes) with distribution partners, which are competitors on the retail level.

To address this concern, the EC is now proposing to make the following adjustments to the existing safe harbor for dual distribution:

- Exclude providers of online intermediation services from the benefit of the safe harbor if they have a hybrid function, namely when they sell goods or services in competition with enterprises to which they provide online intermediation services (Article 2 (7)).
- Limit the current safe harbor for dual distribution to instances where the parties' aggregated market share in the retail market does not exceed 10 percent, in line with the existing market share threshold for agreements between competitors used in the De Minimis Notice (Article 2 (4)).
- Create an additional but more limited safe harbor for dual distribution where the supplier and its distributors have an aggregated market share at retail level above 10% but still do not exceed the 30 percent market share threshold in Article 3 of the VBER. In such a scenario, all aspects of the vertical agreement remain exempted, except for information exchanges between the parties to the vertical agreement, which have to be assessed under the rules applicable to horizontal agreements (Article 2 (5)).

To benefit from the safe harbors listed in (b) and (c) above, the vertical agreements should include neither any "by object" restrictions under Article 101(1) TFEU, nor any hardcore restrictions under Article 4 of the revised VBER.

The EC has identified a potential gap because the current VBER does not extend to dual distribution by wholesalers and importers who often fulfil a similar role as suppliers. To remedy this gap, the EC now proposes to expand the scope of the dual distribution exception to include wholesalers and importers (Article 2(4)(a)).

The draft revised Vertical Guidelines do not contain any guidance on information exchange in dual distribution arrangements. This will be covered by the EC's new revised Horizontal Guidelines (which have not yet been published).

B. Parity Obligations ("MFNs")

Parity obligations – which have recently been the subject of a plethora of diverging national competition authority and court decisions concerning such clauses used by booking platforms – require an enterprise to offer its contracting party the same or better conditions as on other outlets (be it other platforms or any other sales channel). Parity clauses are generally exempted under the current VBER (provided the market share threshold is met and there are not hardcore restrictions).

The EC proposes to remove the benefit of the block exemption for across-platform retail parity obligations imposed by providers of online intermediation services.[2] Under this type of "wide" parity obligation, suppliers are prevented from offering better terms on other platforms. This type of parity obligation is now added to the list of so-called gray-listed clauses (or excluded restrictions - Article 5(d)) and, thus, will have to be assessed individually under Article 101 TFEU. The EC's concern is that "wide" parity obligations may make it more difficult for market entrants to establish a market presence, limit price competition, and restrict access to different sales channels.

The VBER continues to exempt retail parity obligations relating to direct sales or marketing channels (so-called "narrow" parity), e.g. where suppliers are prevented from offering better terms on their own websites. The exemption applies provided the general conditions for the application of the VBER are fulfilled, in particular the 30 percent market share threshold in Article 3.

C. Dual Pricing and Criteria for Online Shops

Dual pricing involves charging the same distributor a higher wholesale price for products intended to be sold online than for products to be sold offline. Many national competition authorities have investigated dual pricing cases affecting online selling, which have been resolved by the abandonment of the dual pricing provisions in question.

The current Vertical Guidelines specify that an agreement that the distributor shall pay a higher price for products intended to be resold online than for products intended to be resold offline constitutes a hardcore (passive sales) restriction. Hence, the only way for a supplier to support a buyer's offline sales efforts specifically was to pay a lump sum.[3]

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2 The EC is likely to have sought to establish clarity in this area as a result of the hotel bookings cases, where multiple national competition authorities adopted different views on the parity obligations at issue.

3 A supplier can also impose minimum offline sales requirements or offline sales targets which trigger discounts that then apply to all purchases.

The draft revised Vertical Guidelines (para. 195) now soften the stance and specify that the VBER allows suppliers to set different wholesale prices for online and offline sales by the same distributor, in so far as this is intended to incentivize or reward an appropriate level of investments and relates to the costs incurred for each channel.

In the context of a selective distribution system, the draft revised Vertical Guidelines (para. 221) state that the criteria imposed by suppliers in relation to online sales no longer have to be overall equivalent to the criteria imposed on brick-and-mortar shops, on the grounds that online and offline channels have different characteristics. By way of example, the draft revised Vertical Guidelines state that a supplier may establish specific requirements to ensure certain service quality standards for users purchasing online, such as the set-up and operation of an online after-sales help desk, a requirement to cover the costs of customers returning the product or the use of secure payment systems.

As with other online sales restrictions (see below), the draft revised VBER only block exempts dual pricing and the lack of equivalence (imposing criteria for online sales that are not overall equivalent to the criteria imposed on brick-and-mortar shops) if these restrictions do not, directly or indirectly, have as their object to prevent buyers or their customers from selling their goods or services online. This introduces effectively a requirement of individual assessment within the VBER (defeating the central purpose of a block exemption), and may lead to differences in interpretation by national competition authorities and national courts, with a possible strict approach taken by some.

D. Online Sales Restrictions

Restrictions that, directly or indirectly, in isolation or combination with other factors, have as their object to prevent the buyers or their customers from selling their goods or services online or from effectively using one or more online advertising channels, are defined as restrictions of active or passive sales, and thus as hardcore restrictions under Article 4 of the VBER.

The draft revised Vertical Guidelines provide additional examples of direct and indirect obligations that have the object of preventing distributors from selling online and also of restrictions that might be permitted.[4] They clarify the following:

- A restriction of the use of price comparison websites,[5] or paid referencing in search engines, amounts to a hardcore restriction under the VBER, as the ability to advertise allows a distributor to attract potential customers to its website, which is a prerequisite for being able to sell online.
- Online advertising restrictions that do not exclude specific online advertising channels are block exempted, for example, if such restrictions are linked to the content of online advertising or set certain quality standards.
- While the operation of a website is a form of passive selling, translating that website in a language not commonly used in the territory of the distributor is a form of active selling.

E. Active Sales Restrictions

Active sales restrictions are limitations of the buyer's ability to actively approach customers in a specific territory or customer groups defined by other criteria.

The current VBER does not foresee the use of shared exclusivities between two or more distributors in a particular territory which can be shielded from active sales by distributors outside of "their" territory, i.e. there can only be one exclusive distributor per territory/customer group. This makes it difficult for some suppliers to implement distribution networks that are tailored to their specific needs.

The draft revised VBER (Article 4 (b)) introduces the possibility of shared exclusivity, allowing a supplier to appoint more than one exclusive distributor in a particular territory or for a particular customer group. The draft revised Vertical Guidelines specify that the number of appointed distributors should be determined in proportion to the allocated territory or customer group in such a way as to secure a certain volume of business that preserves their investment efforts. At Para.102, they state that the number of exclusive distributors should be restricted to a "limited number," and should not be a "large number." They warn that exclusive distribution "shall not be used to shield a large number of distributors

4 There have been a number of recent cases at the EU and national level dealing with online sales restrictions, such as Case C-439/09 Pierre Fabre, Case C-230/16, Coty, the European Commission decision in Guess, and the German FCO decision in Asics.

5 This confirms the position taken in the EC's Final Report of its e-commerce sector inquiry, and follows the ruling of the German Federal Supreme Court in the Asics case that a restriction on the use of price comparison websites, which was not based on quality requirements, constitutes a hardcore restriction. These positions arguably conflicted with the ECJ's Coty ruling; see Kuhn/Rust, "Between Coty, Guess and the new V-BER—where do we stand on e-commerce restrictions?," ECLR 2019, 376 *et seq*.

from competition located outside the exclusive territory, as this would lead to partition of the internal market." It may prove challenging in practice to assess how many distributors are permissible in view of the volume of business in a particular territory, and there is a risk of different interpretations across Member States.

Further, the draft revised VBER now provides a clear position on a much-debated issue, namely that suppliers in exclusive distribution systems may oblige their buyers to pass on active sales restrictions to their customers. According to Article 4(b), such a pass-on is possible where the customer of the buyer has entered into a distribution agreement with the supplier or with a party that was given distribution rights by the supplier. The change aims to enhance the protection of the investment incentives of exclusive distributors.

The draft revised VBER grants substantially enhanced protection to selective distribution systems. It allows the restriction of all sales (active or passive) by an exclusive or open distributor (where a supplier operates neither an exclusive nor a selective distribution system) to unauthorized resellers in a territory where the supplier operates a selective distribution system.

F. Agency

Genuine agency agreements continue to fall outside the scope of Article 101 (1) TFEU.

The draft revised Vertical Guidelines include a new section on agency. The EC explains (para. 44) that:

Undertakings providing online intermediation services are categorized as suppliers under the draft revised VBER and can therefore in principle not qualify as agents for the purposes of applying Article 101 (1) TFEU.

Providers of online intermediation services generally act as independent economic operators and not as part of the undertakings of the sellers to which they provide online intermediation services.

III. WHAT STAYS IN?

The EC has decided to retain RPM as a hardcore restriction, resisting arguments made during the evaluation to take a more lenient approach. It is likely that RPM will continue to be the target of aggressive enforcement by the EC and national competition authorities.

The draft revised Vertical Guidelines provide expanded guidance on RPM, including in relation to price monitoring, Minimum Advertisement Pricing ("MAP") policies (which prohibit retailers from advertising prices below a certain amount set by the supplier), and fulfillment contracts (defined as an agreement between a supplier and a buyer that executes a prior agreement between the supplier and a specific end user). With respect to MAP policies, the revised Vertical Guidelines (para.174) specify that they may amount to RPM in cases where the suppliers sanction retailers for ultimately selling below the respective MAPs, require them not to offer discounts, or prevent them from communicating that the final price could differ from the respective MAP.

The EC has also decided to retain the gateway 30 percent market share for the VBER to be applicable.

Non-compete obligations continue not to be covered by the VBER if their duration is indefinite or exceeds five years. However, the draft revised Vertical Guidelines (para. 234) specify that non-compete obligations which are tacitly renewable beyond a period of five years are covered by the draft VBER if the buyer can effectively renegotiate or terminate the contract with a reasonable notice period and at a reasonable cost.

IV. NEW UK REGIME

On June 17, 2021, the UK Competition and Markets Authority ("CMA") published a consultation document setting out its proposed recommendations for the UK's post-Brexit approach to vertical agreements. Responses to the consultation will inform the CMA's final recommendation to the Secretary of State on whether to replace the retained VBER when it expires on May 31, 2022.

Unlike the EC, the CMA is not proposing to introduce an additional market share threshold for dual distribution, but recommends retaining the dual distribution exemption, as well as extending the exemption to wholesalers and/or importers. The CMA is considering providing guidance on information exchange in the context of dual distribution.

As opposed to the EC, which is proposing to treat them as "excluded restrictions," the CMA recommends that wide parity obligations be treated as hardcore restrictions.

If there emerges significant divergence from the EU system, there may be additional costs and restructuring burdens for businesses in the future, which currently structure their distribution arrangements on a pan-European (including the UK) basis.

V. NEXT STEPS AND TIMELINE

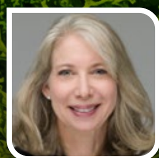
Date	Event
July 9, 2021	Publication of draft EU VBER and accompanying guidelines
July 22, 2021	Deadline for parties to submit comments on draft UK rules
September 17, 2021	Deadline for parties to submit comments on draft EU rules
June 1, 2022	New EU rules will enter into force until May 31, 2034 New UK rules will enter into force for 6 years

VI. CONCLUSION

The draft revisions do not seem like a big overhaul. The basic structure and themes of the VBER are being kept, but the EC is addressing individual lessons learned from the past decade, especially with respect to new digital business models. It seems slightly disappointing that the revision is not more economics-driven (e.g. economists tend to argue that vertical restraints can only be an issue where they have horizontal effects, and e.g. RPM without market power is not a problem). Still, while some of the changes may at first seem marginal, the devil is in the detail and some of them will have a significant effect in practice, for example the ability of a supplier to protect its selective distribution system from sales from outside the territory in which the system is operated. Further, additional issues will be addressed in other EC instruments, such as the revised Horizontal BERs and Guidelines, which will apparently address information exchange between a supplier and its re-sellers in dual distribution structures. Moreover, some of the changes seem to suggest an individual assessment in order to determine whether a clause is covered by the BER, which leads to a degree of legal uncertainty and conflicts with the very purpose of a block exemption. Therefore, the debate will continue both until the BER is adopted and probably beyond.

CONTROLLING MARKET POWER IN DIGITAL BUSINESS ECOSYSTEMS: INCORPORATING UNIQUE ECONOMIC AND BUSINESS CHARACTERISTICS IN COMPETITION ANALYSIS AND REMEDIES

BY DIANA L. MOSS[1]



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I. INTRODUCTION

Digital business ecosystems ("DBEs") reflect the culmination of progressive changes in business models and organizational structure over the last 40 years. DBEs feature collaborations of entities, primarily through digital architectures of information and communication technologies. Leading examples of large DBEs are Facebook (social networking), Google (search), and Amazon (e-commerce). Other powerful DBEs, however, are on the rise, including Zillow (real estate) and Optum (healthcare technology). The ubiquity and significant market power of large DBEs is troubling. But the DBE business model — which far surpasses other models in its scope, scale, and complexity — remains largely under-analyzed. This is a result of the speed with which the DBEs have developed, but also extant analysis that relies almost exclusively on a "law and economics" approach, without considering other important disciplinary perspectives.

This article encapsulates key results of a recent report by the American Antitrust Institute ("AAI"): Market Power and Digital Business Ecosystems: Assessing the Impact of Economic and Business Complexity on Competition Analysis and Remedies ("AAI Report").[2] The AAI Report argues that existing competition analysis and proposed remedial approaches miss important implications of the complex business model and unique economic characteristics of DBEs. These include a range of market failures such as positive network effects, information asymmetries around user data and privacy, and data externalities. As the engine of commerce and growth in DBEs, cloud computing technology, which displays significant economies of scale, adds further complexity. This is particularly true of data analytics, supported by artificial intelligence ("AI") and machine learning. All of these factors act to "supercharge" the DBE value proposition. That is, namely, to maximize user engagement across the interconnected set of markets in a DBE and monetize user data through advertising and infomediaries — all through the deployment of algorithmic recommendations.

These features have myriad implications for assessing and controlling market power. They increase the opacity of DBEs to consumers, competition enforcers, the courts, and lawmakers. If unaccounted for, the unique characteristics of DBEs will likely lead to policy approaches that do not appropriately target the source of their market power and vast capacity for growth. Enforcers and lawmakers are already behind in controlling the market power of large DBEs. U.S. merger enforcement in the sector is essentially nonexistent and monopolization cases are just getting off the ground. U.S. legislative proposals, while well-intended, miss the mark by tasking antitrust agencies with the job of "sector regulation," at the same time they target only the largest of the DBEs. This article explores major takeaways from the AAI Report in explaining the importance of new perspective for refocusing the lens on competition analysis and remedies for the digital technology sector.

II. GROWTH OF THE DIGITAL BUSINESS ECOSYSTEMS: THE ROLE OF CLOUD INFRASTRUCTURE IN FOSTERING EXPANSION

The DBE business model is particularly conducive to growth. Empirical evidence reveals that "growth through acquisition" is the major strategy for executing it. The five largest DBEs — Amazon, Apple, Facebook, Google, and Microsoft — have grown through the acquisition of almost 800 firms over the period 1987-2020, or an average annual rate of increase in acquisitions of almost 20 percent per year.[3] The average value of these acquisitions is much smaller than for similarly sized companies in non-digital sectors. The serial acquisitions made by the largest DBEs have reinforced the market position of the "platforms" that are often the hub of a DBE. Perhaps more important, acquisitions have expanded and diversified DBEs, with significant potential for further growth.

The major area of growth in the formative stages of development of the large DBEs was in core competencies. As part of the most recent cycle of acquisition beginning in 2010, most DBEs shifted their focus to the development of cloud infrastructure. Cloud infrastructure comprises the suite of technologies necessary to collect, aggregate, and enrich vast quantities of user data. The ability to use data has grown significantly through traditional statistical approaches, but also through the emergence of AI and machine learning. Economies of scale in cloud infrastructure allow for cost-effective gathering and processing of data that is essential to creating value by opening new routes to markets and supporting further DBE expansion.

The largest DBEs embarked on a build-out of cloud infrastructure that began in earnest in about 2013 and remains in an extended cycle. 2019 was a banner year, with an all-time high of 24 major cloud acquisitions. The average annual rate of growth in cloud acquisitions between 2013-2020 is about 26 percent, whereas the same rate for all acquisitions over the same period is -1.5 percent. This pattern reveals an intense

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2 Diana L. Moss, Gregory T. Gundlach & Riley Krotz, Market Power and Digital Business Ecosystems: Assessing the Impact of Economic and Business Complexity on Competition Analysis and Remedies, Am. Antitrust Inst. (June 1, 2021).

3 See Diana L. Moss, The Record of Weak U.S. Merger Enforcement in Big Tech, Am. Antitrust Inst., Jul. 8, 2019 (Moss (2019)); and Diana L. Moss; and Update on Digital Technology: The Failure of Merger Enforcement and Need for Reform, American Antitrust Inst., Mar. 3, 2021 (Moss (2021)).

focus on developing the cloud infrastructure that is central to fulfilling the DBE value proposition. The roughly 150 cloud acquisitions made by the five largest DBEs since 1998 have proceeded without opposition from antitrust enforcers. Four players now account for almost 65 percent of the cloud market: Amazon Web Services (31 percent in 2021), Microsoft Azure (percent), Google Cloud Platform (7 percent), and Alibaba Cloud (6 percent).[4] Two of those companies, Amazon and Microsoft, account for over 50 percent of the market. With ongoing investment in cloud infrastructure, DBEs are primed to enter further cycles of expansion, potentially creating even larger and more powerful entities.

III. UNIQUE FEATURES OF DIGITAL BUSINESS ECOSYSTEMS: SUPERCHARGING THE VALUE PROPOSITION AND ENHANCING MARKET POWER

The starting point for understanding market power in DBEs is the value proposition. The DBE business model is conducive to co-creating value. For example, most DBEs features a "platform," which serves as the hub of a star-like network. The platform is the digital infrastructure that provides the core functionality with which third-parties interoperate to provide complementary products and services. Platforms can serve as aggregators, marketplaces, or clearinghouses. Clusters of proprietary or rival businesses surround a platform, in horizontal, vertical, and "ecosystem" relationship to the platform, or each other. The operation and expansion of DBEs depends on this integration. For example, Facebook's acquisition of Instagram and Google's 2010 acquisition of ITA Software, Inc. reflect horizontal and vertical integration, respectively. Ecosystem integration does not involve assets that are in direct horizontal or vertical relationships. Rather, they capitalize on the DBE business model to co-create value by increasing connectivity across a series of markets. For example, Microsoft's 2016 acquisition of professional online networking service LinkedIn (2016) was designed to "recreate the connective tissue" for Microsoft's enterprises suite of functionality.[5]

Another key feature is the role of user data, where the unprecedented collection and commercial use of such data has resulted in the explosive growth of DBEs.[6] Data come from multiple sources, including given voluntarily in exchange for free services such as internet search and social networking; and collected from various user interactions through cookies, tracking, web surfing, and sensor data.[7] As DBEs enter further cycles of expansion, their expanding base of users will generate significantly more user data. And the larger the DBE, the more valuable is the value proposition. But it is well-known that raw user data do not offer much value. Data must be transformed to realize their full value by "map-p[ing] a given consumer's data into estimates of his values for products," to produce search results, personalized product recommendations, product ratings, and targeted advertisements.[8]

DBEs deploy sophisticated tools to harness the value of user data. Algorithms, generated by cloud-based data analytics and supported by AI and machine learning, "shape" consumer preferences by curating options based on past expressed preferences. This process occurs within a "fabricated informational sphere, built in a constant feedback loop," created and managed by the DBE.[9] This conduct generates a number of concerns such as algorithm overdependence, or when consumers "surrender to algorithm-generated recommendations even when the recommendations are inferior."[10]

Algorithmic preference-shaping, which operationalizes the DBE value proposition, creates strong incentives to exploit pervasive market failures and other economic anomalies. For example, social media and search platforms display positive network effects, a demand-side externality that make a network more valuable to all users when more users join it. This encourages users to divulge information they may not otherwise provide, promoting "tipping" to a dominant provider. Also consider information asymmetries around user data and privacy. Users provide their data and information in exchange for engagement and services. But while the firm has complete information about user data, the user has little to no information about how much data is collected, how it is used, and even DBE policies regarding its use.[11] One perverse outcome of this

4 Katy Stalcup, AWS vs Azure vs Google Cloud Market Share 2021: What the Latest Data Shows, ParkMyCloud.com, Feb. 10, 2021. Based on cloud infrastructure spending in 2020.

5 Microsoft to Acquire LinkedIn, Microsoft.com, Jun. 13, 2016. See also Grant Feller, This Is the Real Reason Microsoft Bought LinkedIn, Forbes.com, Jun. 14, 2016.

6 Dirk Bergemann, Alessandro Bonatti, & Gan Tan, The Economics of Social Data, Cowles Foundation Discussion Papers (2019), at 2.

7 Wolfgang Kerber, Digital Markets, Data, and Privacy: Competition Law, Consumer Law, and Data Protection, Gewerblicher Rechtsschutz und Urheberrecht. Internationaler Teil (2016), at 2.

8 Shota Ichihashi, *Online Privacy and Information Disclosure by Consumers, 110* Am. Econ. Rev. 569 (2020), at 2.

9 *Id.*

10 Sachin Banker & Salil Khetani, *Algorithm Overdependence: How the Use of Algorithmic Recommendation Systems Can Increase Risks to Consumer Well-Being*, 38 J. of Pub. Pol. & Mkting. 500 (2019), at 500.

11 Kerber, *supra* note 7, at 7.

information asymmetry is that even when consumers state certain preferences for privacy, when they are presented with scenarios where their data is shared, they behave counterintuitively, or rarely change their behavior.[12]

DBEs are also home to another market failure, powerful data externalities, which are revealed in the value of a small number of users' data in predicting the behavior of even larger groups of users. This includes how the privacy choices of a smaller number of users affect what sellers can learn about the privacy preferences of others. The power of data externalities, in conjunction with algorithmic preference-shaping, can induce DBEs to require users to provide even more detailed, personal information. DBEs can coerce this provision through lock-in or dependence on a particular platform or service,"[13] resulting in the collection of an excessive amounts of private data.[14] Taken together, the market failures that pervade DBEs foster not only anomalous user behavior but strong incentives for DBEs to acquire and exercise market power.

IV. WIDENING THE LENS ON COMPETITION ANALYSIS: HOW COMPLEXITY EXPANDS THE UNIVERSE OF POTENTIAL STRATEGIC CONDUCT

The unique economic and business features of DBEs directly affect how enforcers and policymakers frame competition problems in the digital technology sector. This includes how markets are conceptualized and defined, and the types of anticompetitive conduct for which redress is sought. For example, the market failure around user data and privacy, coupled with the algorithmic shaping of user preferences in DBEs, call into question whether consumers behave "rationally" — a critical assumption in competition analysis. This, in turn, creates a lack of clarity around how consumers will respond to the exercise of market power by switching (or not) to competing providers. These problems may mean the difference between a very narrowly defined market within a DBE in which there is suspected competitive harm and a larger "cluster" market, which could encompass a broader set of interconnected markets within a DBE.[15] Demand is the ultimate arbiter of market power, so any difficulty in evaluating it as the result of the unique features of DBEs will have a material impact on the ability of enforcers and policymakers to tackle competition problems.

The complexity and special characteristics of DBEs also give rise to a diverse set of potential anticompetitive strategies. Some outcomes are directly the result of key economic features, such as network effects and tipping, which can create barriers to entry for smaller DBEs and that might seek to challenge the position of an incumbent DBE. Other anticompetitive incentives result from ownership of a dominant platform, on which the DBE competes with third-party providers. For example, the 2020 state complaint against Facebook alleges the firm "selectively enforce[d] its policies to cut off API access to companies Facebook worried might one day threaten its monopoly."[16] Likewise, in 2012, the FTC investigated whether "Google unfairly promoted its own vertical properties through….the introduction of the 'Universal Search' box."[17] And in 2020, the EC investigated whether Amazon favored its proprietary products or preferred sellers that used Amazon's logistics and delivery services in calibrating which sellers are eligible to participate in its Prime loyalty program and appear in the "Buy Box."[18]

Analysis in the AAI Report reveals additional competitive concerns. One is the rapid expansion of the DBEs through ecosystem acquisitions. For example, the EC's concern in Google's acquisition of fitness wearables maker, Fitbit, was the potential extension of Google's enhanced market power in the market for health and fitness data to the broader ad-tech market.[19] Such acquisitions, which may be dismissed by enforcers as harmless "conglomerate" deals, pose significant competitive issues around leveraging of market power within a DBE. Novel analysis in the AAI Report also identifies additional forms of exclusionary conduct, particularly around cloud technology. For example, economies of scale in cloud infrastructure and high concentration in cloud markets raise barriers to entry to smaller firms seeking to gain a foothold within a DBE market(s).[20]

12 *Id.,* at *2* [noting "In the aftermath of Facebook's Cambridge Analytica scandal the social media company should have seen a higher number of consumers switching services or closing their accounts, but the outcome was the opposite."] See also, Thomas C. Redman & Robert M. Waitman, *Do You Care About Privacy as Much as Your Customers Do?* Har. Bus. Rev. (Jan. 28, 2020).

13 Nicholas Economides & Ioannis Lianos, Antitrust and Restrictions on Privacy in the Digital Economy, *2* Concurrences Review 22 (May 2020), at 23.

14 Kerber, *supra* note 7, at 7.

15 See e.g. Herbert Hovencamp, Digital Cluster Markets, Col. Bus. L. Rev. (2021) (forthcoming), at 6.

16 Complaint, *FTC v. Facebook,* No. 1:20-cv-03590 (D.D.C. filed Dec. 9, 2020).

17 See Statement of the Federal Trade Commission Regarding Google's Search Practices 3, n.2, In the Matter of Google Inc., FTC File No. 111-0163, Jan. 3, 2013.

18 Commission Sends Statement of Objections to Amazon for the Use of Non-Public Independent Seller Data and Opens Second Investigation into Its E-commerce Business Practices, European Commission, Nov. 10, 2020.

19 Mergers: Commission clears acquisition of Fitbit by Google, subject to conditions, European Commission, Dec. 17, 2020.

20 Emilio Calvano & Michele Polo, Market Power, Competition and Innovation in Digital Markets: A Survey, Info. Econ. & Pol., forthcoming, Dec. 1, 2019, at 27. See also Marc Bourreau, Some Economics of Digital Ecosystems, Hearing on Competition Economics of Digital Ecosystems, Directorate for Financial and Enterprise Affairs Competition Committee, OECD, Nov. 13, 2020, at 4.

A DBE can also engage in a variety of anticompetitive conduct involving cloud technology, such as denying rivals' access, granting access on discriminatory terms and conditions, or manipulating firewalls that cordon off rivals' cloud data. Even more troubling are scenarios where a DBE could deploy cloud technology to steer users to proprietary services (and away from rivals) using algorithmic recommendations. These strategies lock users into proprietary systems, limiting their ability to switch to a DBE that offers a similar cluster of services. But given the opacity of algorithmic recommendation systems, such conduct is likely to be difficult for rivals to detect. And switching also depends critically on competition, which may not be present in markets dominated by large DBEs.

V. REINING IN THE MARKET POWER OF THE DIGITAL BUSINESS ECOSYSTEMS: WHAT NEW ANALYSIS TELLS US ABOUT EFFECTIVE REMEDIES

Analysis of the DBE business model provides important insight into the effectiveness of various remedial approaches, a perspective that should inform current debate and legislative proposals to rein in the market power of the large DBEs. To date, proposals focus almost exclusively on two components of a regime that promotes access by both rivals and users. One is interoperability standards that ensure rivals' nondiscriminatory access to a platform and a second is data portability requirements that promote users' ability to switch between competing DBE services. These remedies, while important and necessary, do not address the unique economic and business features of DBEs that create strong incentives to exploit users and impede access by rivals. The following takeaways highlight a number of these, and related, issues.

Use of the antitrust laws to "quasi-regulate" the largest DBEs is not the most effective approach to addressing competitive concerns that arise more broadly in the digital technology sector. Tackling the market power problems raised by DBEs will require the coordination of multiple policy tools. Current proposals in the U.S., however, would require antitrust agencies to bear the vast burden of policing competition. This includes a new form of quasi-regulatory oversight involving structural separation of the largest firms, which would be added to traditional merger and monopolization enforcement performed by the DOJ and FTC. Aside from diverting scarce resources from the vital antitrust enforcement mission, burdening the agencies with quasi-regulation that is administered through the antitrust process would likely prove too slow, against the backdrop of a dynamic sector. The market power issues that are amplified by the market failures and complex business model that characterize the DBEs and would be better addressed through broader sector regulation. Sector regulation would work more efficiently and quickly to promote a system of universal nondiscriminatory access. This would also carry less risk of serious market distortions and a higher probability of success in preventing firms from growing to dominance. In sum, tasking the antitrust agencies with responsibilities for which law enforcement is not designed could impair the vital antitrust mission at a time when we need it the most, in digital technology and in other sectors.

Antitrust conduct remedies would be even less effective in the DBE context than they are in more traditional, non-digital sectors. Experience teaches that antitrust remedies designed to prescribe and proscribe certain activities of a defendant are the least effective at restoring competition. Antitrust conduct remedies do not reduce incentives to exercise market power and require oversight and monitoring, a task for which the courts are ill-suited. As applied in the DBE context, antitrust conduct remedies would be particularly ineffective. Complexity, market failures, and the opacity of complex technology systems make antitrust conduct remedies poor candidates for addressing the root problems that create anticompetitive incentives. A more comprehensive remedial framework is needed for DBEs, in the form of sector regulation.

Antitrust or legislated structural separations alone are unlikely to address the unique features of DBEs that give rise to market power. Structural remedies have been proposed to address a number of problems that arise in DBEs. Take privacy, where dominant DBEs have incentives to provide insufficient options to users.[21] Breakups will do little to eliminate incentives to exploit network effects and data externalities that compromise user data and privacy. And more competition could even promote more intense efforts to obtain personal data.[22] On another front, separation of affiliated businesses from a DBE platform could significantly weaken incentives to exclude rivals. A standalone platform would provide an essential network service where rivals operate out of the shadow of a DBE's affiliated businesses, and no longer be the target of discriminatory conduct. However, structural separations are only as effective as the ability of buyers of divested assets to fully restore competition. The growing record of failed antitrust divestitures in other sectors suggests that caution is needed in selecting viable buyers with a demonstrated ability to maintain divested DBE assets.

History teaches that reduced incentives to maintain a standalone platform will be a challenging issue in crafting remedial approaches. A DBE's incentive to maintain and invest in a platform is driven both by competition with third-party rivals on the platform *and* the risk of losing users to competing DBEs. Separating a platform from affiliated DBE businesses will weaken such incentives. This could lead to an overall decay

21 Daniel P. O'Brien & Doug Smith, Privacy in Online Markets: A Welfare Analysis of Demand Rotations, Federal Trade Commission, Bureau of Economics, Working Paper No. 323, Jul. 2014, at 26.

22 Eugene Kimmelman, Harold Feld, & Agustín Rossi, *The Limits of Antitrust in Privacy Protection*, 8 Int'l. Data Privacy L. 270 (2018).

in the quality of the platform, especially cloud infrastructure, access to which is essential for rivals to compete. These effects are illustrated by the spinoff of the British railway system to an independent operator in the 1990s, which was followed by safety problems and modifications to the original ownership and operation scheme.[23] Concerns over the sufficiency of investment in a network also arose in the U.S. electricity sector in the 1990s, where vertically integrated utilities were required to cede control of their transmission systems to regional organizations. Solutions to these concerns are largely absent from current policy approaches to controlling the market power of DBEs.

The stronger restrictions necessary to address the features of DBEs that foster the exercise of market power pose serious challenges for enforcers, courts, and regulators. Remedies that address the unique characteristics of DBEs that foster exploitative and anticompetitive conduct would focus on market failures, economies of scale, and algorithmic recommendation systems.[24] Such requirements pose serious challenges. For example, DBEs will invoke First Amendment protection to prevent outside access to algorithms[25] and it is not clear how enforcers or courts would ensure (and monitor for) unbiased results. Maintaining separate or firewalled datasets and cloud computing assets would eviscerate any benefits from data externalities and scale economies, and thus be strongly opposed by DBEs. Mandatory data-sharing raises questions about what and how much data should be shared between the DBE and rivals to reduce anticompetitive incentives. Moreover, it is not clear, as of yet, what changes to opt-out provisions would empower users to better align their preferences for privacy with their actual behavior. These questions require more thought and analysis, as part of a potential regulatory regime.

An effective regime for reining in the market power of the DBEs will require a comprehensive, hybrid approach. Analysis of the DBEs reveals the necessity of a hybrid approach that deploys a set of appropriate and complementary policy tools. Vigorous antitrust enforcement is a critical prong of a broader public policy approach to reining in the market power of the DBEs. Merger and monopolization law will remain critical in controlling the market power of DBEs, but constructive reforms are needed to clarify and strengthen their effectiveness across all sectors of the economy, including the digital technology sector. Structural remedies should be the approach "of choice" in antitrust consent decrees that emerge from successful enforcement actions. A complementary regulatory regime that governs potentially harmful conduct in the digital technology sector more broadly is essential. A regulatory framework should minimize the risk of gaming and ongoing legal challenges, at the same time it recognizes the characteristics of DBEs that create strong anticompetitive incentives. The complementarity between antitrust and regulation should be ensured through savings clauses in any legislative proposals, and full rein for antitrust authorities to pursue violations in the sector.

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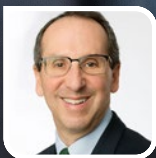
23 Russell Pittman, Structural Separation and Access Pricing in the Railways Sector: Sauce for the Goose Only? Oct. 15, 2004.

24 Diane Coyle, *Practical Competition Policy Implications of Digital Platforms*, 82 Antitrust Law J. 835 (2019), at 7. See also, In the matter of *Google/Double Click*, Dissenting Statement of Commissioner Pamela Jones Harbour (F.T.C. File No. 071-0170, Dec. 20, 2007). See also, Inge Graef, Blurring Boundaries of Consumer Welfare: How to Create Synergies between Competition, Consumer and Data Protection Law in Digital Markets, Dec. 7, 2016.

25 Randy M. Stutz, An Examination of the Antitrust Issues Posed by Google's Acquisition of ITA, Am. Antitrust Inst. (Feb. 18, 2011), at 22.

FIX IT OR FORGET IT: A "NO-REMEDIES" POLICY FOR MERGER ENFORCEMENT

BY JOHN KWOKA & SPENCER WEBER WALLER[1]



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I. INTRODUCTION

Over the past several years, merger remedies have come under ever closer scrutiny. Adverse experiences have exposed the difficulties of fashioning effective remedies while academic studies have documented the frequency with which remedies have failed. This is particularly true for conduct or behavioral remedies, which proscribe specified actions on the part of the merged firm, but it is also true that divestitures have failed with considerable frequency. In light of this mounting evidence, the U.S. antitrust agencies, the Antitrust Division of the Justice Department ("DOJ") and the Federal Trade Commission ("FTC"), have undertaken a number of actions. Starting in 2004, the DOJ has issued no fewer than three successive and somewhat different – guides or manuals setting out its policies, while the FTC has conducted two major studies of its own past remedies and used those as the basis for numerous recommendations.

This churn in policy reflects dissatisfaction with each iteration of policy, as well as persistent uncertainty about the best direction of reform. Moreover, agency practices have often deviated – and continue to deviate – from their own stated policies, approving mergers subject to remedies that are ill-conceived, too easy to evade, and ultimately unenforceable. As a result, many anticompetitive mergers continue to avoid the challenges that should be brought against them. Current remedies policy does not generally preserve or restore competition in affected markets.

We conclude that, despite the promise of merger remedies as a third way between outright rejection and unconditional approval of a merger, in practice there appears to be no viable and sustainable third way. The defects of remedies policies in principle, compounded by the misuse of remedies in practice, suggest that their problems are inherent and unfixable. Accordingly, the time has come for a radical rethinking of the current approach. We propose moving to a "no remedies" policy towards competitively problematic mergers.

Under our no-remedies policy, the competition agency's role would return to its statutory origin, namely, to simply decide "yea" or "nay" to each merger as it is filed under HSR and then evaluated for its competitive effects. The agency would make its determination based on the filed proposal. The parties could make no further changes and the agency would not negotiate, propose, or in any other way be drawn into a discussion with the prospective merging parties on what would or might be a satisfactory remedy. Nothing, of course, would or should prevent the merging parties from undertaking changes prior to their filing that would, in their estimation, resolve the competitive problems posed by their prospective merger. Any such changes would simply be a factual part of their HSR filing, not a proffer or trial balloon or agenda item for negotiation. Even here, however, there would be limitations. As will be discussed further below, no conduct remedies whatsoever would be allowed, and any divestitures must be targeted and represent a truly miniscule portion of the operation of the companies.

Our "no-remedies" policy might therefore more accurately be labeled a "no-negotiated-remedies" policy, or perhaps better yet as "Fix It or Forget It" — FIFI for short. It would provide merging parties with every incentive to undertaking their own fixes prior to making their HSR filing. If the agencies conclude that the divestitures — whether consummated or subject to binding commitment – are viable, fully cure competitive concerns, and involve a fully suitable buyer, such commitments would be embodied in a consent decree approving the merger. If not, the agency would proceed to challenge the proposed transaction in its entirety.

Under this plan, the parties would face the full burden of establishing that the proposed relief would fully preserve or restore competition in the relevant markets as well as the current public interest standard in the Tunney Act. Otherwise, the competitive impact of the transaction as a whole would be challenged for an up or down decision by the district court or administrative law judge. Once litigation commenced, remedies would be off the table, both substantively and as an evidentiary matter, and the court would be limited to a consideration of whether the transaction as a whole violated the provisions of the Clayton Act, FTC Act, or state law equivalent.

II. THE INHERENT DEFECTS OF REMEDIES... AND OF REMEDIES POLICY

In its 1961 decision affirming rejection of Dupont's attempted equity stake in General Motors, the Supreme Court made clear its preference for a divestiture remedy, rather than the conduct remedy proposed by the parties. The court said, "Divestiture has been called the most important of antitrust remedies. It is simple, relatively easy to administer, and sure." By contrast, in the view of the court, a conduct approach "would probably involve the courts and the Government in regulation of private business affairs more deeply than administration of a simple order of divestiture."[2]

Nothing in the intervening sixty years has challenged this wisdom: conduct remedies do indeed have fundamental, generally fatal, weaknesses. But in practice it is clear that the court did not go far enough since experience and evidence have now shown that divestiture remedies routinely fail to preserve or restore competition in affected markets as well. The problems with each type of remedy are different, and each deserves comment.

The defects of conduct remedies are by now reasonably well known. A conduct remedy is essentially an order by the competition agency that the merged firm not engage in certain anticompetitive actions as a condition for allowing the merger to proceed. The problem is that those prohibited acts are in the interest of the firm, which therefore can be predicted to seek workarounds and other methods to avoid or evade the intent of the remedy. The agency in turn labors under an informational disadvantage with respect to the firm's decisions and the intent of any action. This results in the likelihood that the firm will identify ways of minimizing the effect of the remedy, despite an agency's efforts at monitoring and overseeing the constraints it has imposed on the firm's behavior

For these reasons, most – but not quite all – of the remedies guides and manuals issued by the U.S agencies have stated their strong preference for divestitures instead of conduct remedies. The first of these – the 2004 Policy Guide to Merger Remedies issued by the Department of Justice Antitrust Division – echoed the Supreme Court. That guide described structural remedies as "clean and certain, and generally avoid costly government entanglement in the market," whereas conduct remedies were "more difficult to craft, more cumbersome and costly to administer, and easier...to circumvent."[3]

Despite this language, the DOJ employed conduct remedies in a number of major merger cases, and in 2011 issued a revised policy guide reflecting this policy shift endorsing some conduct remedies. Several years and many criticisms later, DOJ withdrew the revision and in 2020 issued a new Merger Remedies Manual restating its strong preference for structural rather than conduct remedies.[4]

The Federal Trade Commission has concurred in this stated preference for structural remedies. It also has conducted two studies of the effects of divestitures in actual merger cases. The first study, in 1999, assessed divestitures as successful if the divested assets remained in the market and were financially viable. Even by that weak standard, a sizeable fraction were failures.[5] A second FTC study, in 2017, suffered from a number of methodological flaws,[6] but nonetheless again found a similarly substantial fraction of studied divestitures to be failures.

These studies identified a number of defects and limitations of divestitures. Primary among them are the failure to divest an entire business operation rather than selected assets and the failure to ensure that the buyer has adequate financial and operational capabilities. Other divestitures have failed to recognize business issues affecting competition beyond the easily identified overlaps in operations, including so-called "portfolio effects." It was apparent that many failures simply resulted from the competition agency's informational disadvantage with respect to the technology, operations, marketing, and financial aspects of the businesses.

Divestitures have increasingly been used in novel ways that do not plausibly result in the preservation of competition. In a number of cases where it is apparent that the operations to be divested do not by themselves represent a fully capable business, the agencies have now sought to identify and assemble a package of assets from disparate sources in order to create the necessary replacement competitor. In this role the

2 *U.S. v. E.I. Dupont de Nemours & Co.*, 366 U.S. 316, 330-31 (1961).

3 Antitrust Division, U.S. Department of Justice, Antitrust Division Policy Guide to Merger Remedies (2004), https://www.justice.gov/atr/page/file/1175136/download.

4 Antitrust Division, U.S. Department of Justice, Merger Remedies Manual (Sept. 2020), https://www.justice.gov/atr/page/file/1312416/download. This Manual was issued shortly after approval of the *Sprint/T-Mobile* merger subject to only to a deeply flawed remedy (discussed below), illustrating the dichotomy between stated policy and actual practice.

5 A Study of the Commission's Divestiture Process, Prepared by the Staff of the Bureau of Competition of the Federal Trade Commission, William J. Baer, Director (August 1999), https://www.ftc.gov/reports/study-commissions-divestiture-process.

6 John Kwoka, *Controlling Mergers and Market Power* (CPI, 2020), Appendix, https://www.competitionpolicyinternational.com/controlling-mergers-and-market-power-a-program-for-reviving-antitrust-in-america/.

agencies have gone well beyond their law enforcement mission. Rather, they have entered into a three- or four-way bargaining process for which they are ill-suited,[7] acting more like a Wall Street investment bank determined to make a merger happen — a role altogether outside their writ.

Examples of the ineffective conduct and structural remedies and of overly expansive agency remedy practices abound. The difficulties of crafting a remedy and of fixing any possible loophole are illustrated by the resolution of the *Ticketmaster/Live Nation* merger in 2010. DOJ approved the merger subject to a conduct remedy that prohibited the company from several anticompetitive acts made possible by the merger. One key provision of the order stated that the merged firm must not condition or threaten to condition the provision of Live Nation Entertainment Events to a venue owner on whether the venue had contracted with another company for ticketing services. The merged company immediately did precisely that, arguing that the language only prohibited it from withholding *all* Live Nation events, not just one or a few events.

DOJ became aware of Live Nation's use of the prohibited conditioning almost immediately after the order went into effect, but it did not take action until 2020. At that time, it simply went to court to "clarify" the original language so as to prevent conditioning on one or more events, as opposed to all of them, but it did not charge Ticketmaster with contempt of court or even violating the order, nor did it seek rescission of the merger or any restitution or penalty from the company. As a result, customers were harmed for nearly a decade after the merger, in very much the same manner if the transaction had been approved unconditionally.

More recently, the DOJ approved the merger of Sprint and T-Mobile, two of the four national wireless carriers, subject to a remedy that illustrated many other problems with such orders. The agency acknowledged the need for four carriers in this industry, so that approval required constructing a fourth carrier to replace the one being extinguished. That fourth carrier is supposed to be Dish, a satellite TV operator with no relevant operations, infrastructure, or expertise in wireless telephony.[8] Dish is nonetheless supposed to become the necessary fourth carrier by 2026 by cobbling together Sprint's prepaid business; rights to acquire spectrum from Sprint; a phased 5-year divestiture plan for Sprint's retail locations, personnel, and licenses; all supported by interim use of T-Mobile's infrastructure and transitions services for a period of three years, while the new company builds out a national wireless infrastructure.

Many doubt the prospects of success for this remedy.[9] After all, success would require (1) the competition agency correctly identifying the necessary components of a new viable competitor, (2) a newcomer firm's ability to integrate those components into a new national network, (3) T-Mobile's willingness to divest suitable locations and infrastructure, and (4) providing crucial services to that newcomer to help it become a potent rival to itself. The entire deal was held together only as a result of the extraordinary — and likely inappropriate — intervention of the then-Assistant Attorney General for Antitrust who helped smooth tensions between Sprint and T-Mobile and coached them on their lobbying strategies with other regulators and with Congress.[10] Not surprisingly, it has quickly become clear that this remedy is already failing.

In the software sector, these limitations and problems are exacerbated by the fact that key assets are often software and other intellectual property, that the technology defies easy definition and is readily manipulated, and that the process confers enormous discretion on the parties, rendering oversight largely impossible. One of the most complicated examples came in the *Google/ITA* merger.[11] In July 2010, Google entered into a merger agreement to acquire ITA, the provider of the QPX software, which was the leading independent airfare pricing and shopping system. These systems provide pricing, schedule, and seat availability information to Internet travel sites such as Expedia and Travelocity, where consumers make on-line travel reservations, as well as so-called meta-search sites such as Kayak and TripAdvisor, which allow customers to view results from multiple travel sites. While Google was not then in the on-line travel space, it was the leading general use Internet search engine in the U.S., the leading seller of Internet advertising, and planned to launch an Internet travel aggregator site using the technology it would acquire from ITA.

The Justice Department's complaint focused on access as the likely harm resulting from the transaction. The complaint argued that the proposed merger would give Google the means and incentive to use its ownership of QPX to foreclose or disadvantage its prospective flight search rivals by degrading their access to QPX, or denying them access to QPX altogether. As a result, the proposed merger was likely to result in reduced quality, variety, and innovation for consumers of comparative flight search service.

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7 For an analysis of the hazards of agency negotiation over remedies, see Joseph Farrell, "Negotiation and Merger Remedies: Some Problems," *in Merger Remedies in American and European Union Competition Law*, (Francois Leveque & Howard Shelanski, eds., Edward Elgar, 2003).

8 The criterion that a buyer be suitable or even plausible has weakened to the point where it is unrecognizable. In addition to the *Sprint/T-Mobile* matter, see the FTC's resolution of the proposed merger of AbbVie and Allergan by drug divestitures to Nestle, a food and beverage company. Dissenting Statement of Commissioner Rohit Chopra In re *AbbVe, Inc./Allergan plc*, May 5, 2020, https://www.ftc.gov/public-statements/2020/05/dissenting-statement-commissioner-rohit-chopra-matter-abbvie-inc-allergan.

9 https://www.wired.com/story/opinion-the-terrible-t-mobilesprint-merger-must-be-undone/.

10 Katie Benner and Cecilia Kang. *How a Top Antitrust Official Helped T-Mobile and Sprint Merge,* N.Y. Times, (Dec. 19, 2019), https://www.nytimes.com/2019/12/19/technology/sprint-t-mobile-merger-antitrust-official.html.

11 For other examples see Spencer Weber Waller, *Access and Information Remedies in High Tech Antitrust*, 8 J. Comp. L. & Econ. 573 (2012).

The eventual consent decree imposed one of the most complicated access regimes of any merger case. The defendants were required to honor all existing QPX licensing agreements, negotiate extensions of such licenses with commercial terms "substantially similar" to the existing terms at the time of the consent decree, and negotiate other terms of the extension that are "fair, reasonable and non-discriminatory." New licenses must contain commercial terms that are "fair, reasonable and nondiscriminatory" as measured by both the specific terms under negotiation and the terms in effect between the defendants and similarly situated competitors. Defendants must provide upgrades at no more than fair, reasonable, and non-discriminatory prices. Furthermore, defendants must license a new software product called InstaSearch that was in development by ITA at the time of the merger on fair, reasonable, and non-discriminatory terms to all interested parties. Finally, the defendants agreed to devote at least as much annual resources as the average of the past two years for the continued research development and maintenance of both QPX and InstaSearch.

These cases are not isolated examples, but rather illustrations of the extraordinary efforts by the antitrust agencies to devise increasingly complex, but ultimately unenforceable, remedies as pretexts for merger approval. Not surprisingly, broader evidence confirms that they are not effective. One of us has conducted a meta-analysis (a structured summary of studies) of the effects of remedies in actual mergers and found that on average divestitures result in price increases of the same magnitude as cases not subject to remedies at all, while conduct remedies (many fewer in number) lead to more substantial price increases.[12]

Despite repeated efforts at reform, our merger remedies policy is broken. Even where policy guides set out sensible principles, the competition agencies have consistently misused their discretion, resulting in remedies too easily evaded and mergers too often anticompetitive. The time has come to confront the implications of these facts and act to prevent the agencies, and to a lesser extent, the courts from abusing their discretion over merger remedies.

III. FIX IT OR FORGET IT

We propose a Fix It or Forget It ("FIFI") system to replace our broken remedies system. Under FIFI, the agencies would challenge any transaction that may substantially harm competition in its entirety, unless — and only unless — the parties propose and implement before consummation to the satisfaction of the agencies a viable divestiture to a suitable buyer. The parties would be required to submit their commitments in their original HSR filing itself or in response to a second request from the Agencies, and these would become an integral part of their merger proposal.[13]

Conduct remedies would not be considered under any circumstances. Any merger seemingly "fixable" only with a conduct remedy would be treated as anticompetitive and challenged as such. Divestitures proposed by the parties would be considered under two circumstances. First, they must be *de minimis*. Divestitures involving more than a small fraction of a company — perhaps 5 to 10 percent of revenues, or $1 billion — would be judged as inherently unlikely to yield a satisfactory outcome, since they would constitute a change more akin to a restructuring of the company rather than a merger-related fix. Second, any divestiture would have to be proposed by the merging parties as an integral part of their merger filing. Ideally, the parties would complete the divestiture prior to consummation. In the event this is not possible, they would have to enter into a binding commitment to divest assuming agency approval of the merger-plus-divestiture that the parties file under HSR. In any event, the agency would have before it the full package for evaluation.

In response, the Agencies would evaluate the proposed merger-plus-divestiture plan and market test it as needed through the familiar process of seeking information and testimony from customers, suppliers, and competitors. In addition, the Agencies could seek more general feedback from the public through publication in the Federal Register and a notice and comment period. If the proposal is acceptable to the Agency, then the parties and the Agency would embody the agreement in a consent decree and share with the court both why and how the remedy fully cures all substantial potential competitive harms to the transaction as a whole.

What would *not* happen is an endless round of negotiations, modifications, brokering, and back and forth between the Agency and the parties over divestiture, access, and behavioral remedies. If the proposed remedy package truly cures the problem, the Agencies would accept it after appropriate review. If not, the proposal would be rejected, and the Agency would seek to prohibit the proposed transaction in its entirety under the Clayton or FTC Act. The court would then judge the legality of the proposed transaction in its entirety under the applicable law and not litigate the fix.

12 Kwoka, *supra* note 6.

13 Our FIFI proposal focuses on horizontal mergers. We do not here address vertical or other mergers, nor dual agency review.

Under FIFI, parties could not continually introduce new proposed remedies, or strategically introduce revisions late in the investigative process, as has sometimes been done. This limitation would create strong incentives for the parties to propose their best offers, sooner rather than later, to avoid a challenge on the merits to the transaction as a whole. It also creates incentives for the Agency to focus their resources on litigation, and not the evaluation of complex and often-changing offers that continue into the litigation phase of any merger challenge.

Parties could of course always withdraw a filing (as they can under the present system) for the purpose of refiling with an enhanced remedy package. While in principle they could do this repeatedly until the agency responded favorably, merging parties would face disincentives to that strategy. Each refiling would restart the HSR time clock and impose new filing fees. Given market realities and current legislative proposals for greater filing fees and longer time periods for investigation, merging parties would almost certainly wish to avoid such repetitions.

Under FIFI the parties propose, and the agency disposes, rather than initiating a bargaining process. FIFI would constrain the discretion of the courts as well as the agencies. All acceptable *de minimis* settlements with party commitments would go through enhanced Tunney Act review to satisfy the court and public that the proposed remedies are truly effective to eliminate the competitive problems with the transaction as a whole. The problems with the current limited Tunney Act review[14] would be addressed with greater standing and appeal rights for all affected parties and a higher burden on the merging parties and the agencies to demonstrate that the transaction as a whole poses no danger to competition.

The proposed divestiture remedy proposals normally should be completed on, or before, the approval of the consent decree by the court. If there were truly exceptional circumstances making that infeasible, the consent decree or closing statement would have to include monitoring and trustee provisions (with crown jewel provisions if necessary) on a tight time frame plus reporting obligations to provide the agency with the information if any further action – including undoing the merger agreement – is necessary. In all cases, the remedy would include the requirement that the parties report, on a regular basis, key performance data to the agency sufficient to permit assessment of the effectiveness of the remedy over a suitable period of time.

FIFI would also have the salutary effect of making merger law look more like the rest of antitrust law. In Section 1 and Section 2 cases, settlement is possible if the parties and the agencies reach agreement that cures the competitive harm at issue. But otherwise, the Agencies challenge the agreement or the unilateral conduct, rather than seeking to broker structural and behavioral remedies that are hard or impossible to monitor or evaluate.

Some version of a different, but similarly titled, policy of "fix it first" has been around since the 1980s.[15] But that policy was designed to enhance agency discretion to decline to challenge mergers, rather than eliminate flawed remedies and unchallenged mergers. The current version of the DOJ Merger Remedies Manual describes the general outlines of the government's fix it first policy over the past forty years as:

A fix-it-first remedy is a structural solution implemented by the parties that the Division accepts before a merger is consummated. An acceptable fix-it-first remedy eliminates the Division's anticipated (and yet to be determined) competitive concerns and therefore the need to file a case.[16]

This occasional practice is not embodied in statute or regulation but agency practice. It is not limited by size. It is an alternative to even filing a case or having to embody the parties' divestiture in a consent decree or seek judicial approval for that agreement. As currently constituted, fix it first is a tool that enhances, rather than limits, agency discretion over merger remedies.

Our FIFI proposal is not fix it first, but rather fix it or forget it (unless the parties convince the judge that no competitive harm is likely). The fix is further limited to *de minimis* divestitures that render the entire transaction competitively benign. If the defendants do not propose any commitments or do not propose commitments satisfactory to the Agencies, then the transaction in its entirety would be challenged in district court or before an administrative law judge. If the litigation is successful, the transaction is blocked. If not, it proceeds free from conditions, but remains subject to further challenge if actual (rather than predicted) harm ensues.

14 John J. Flynn & Darren Bush, *The Misuse and Abuse of the Tunney Act: The Adverse Consequences of the "Microsoft Fallacies,"* 34 Loy. U. Chi. L.J. 749 (2003).

15 Nathaniel C. Nash, *Business and the Law; U.S.'S 'Fix-it' Antitrust Policy*, N.Y. Times, Sept. 16, 1986, https://www.nytimes.com/1986/09/16/business/business-and-the-law-us-s-fix-it-antitrust-policy.html.

16 2020 Merger Remedies Manual, *supra* note 4, at 17.

IV. CONCLUDING OBSERVATIONS

Although this proposal might be viewed by some as radical, others may see it as quite modest. In some cases, sophisticated merging parties already do thing along these lines: they determine the likely antitrust issues with their merger and proceed to make a fix before initiating their HSR filing. The agencies then have a complete proposal from the parties and can evaluate it as such. To the extent the parties have indeed made the necessary fix — say, a minor divestiture or two — the prospects for a straightforward investigation, consent decree, and clearance are correspondingly enhanced.

That said, this proposal is fundamentally different from existing policy and practice in the U.S. It shifts the full responsibility for identifying an appropriate remedy to the parties. It creates an incentive for the parties to come forward with a sound remedy from the outset, rather than attempting to determine what they can get away with or introducing a new remedy well into the process. It relieves the agency of the burden of engaging in protracted negotiations with the parties as the latter seek the least constraining remedy. It also eliminates the risk of the agencies stepping outside their lane and acting as de facto business brokers or investment bankers in matching buyers and sellers. Finally, it brings more rigor to Tunney Act review of proposed *de minimis* divestitures and requires litigation of more troubling transactions. By focusing on the necessary remedy, the process would likely require less post-merger monitoring. And if no remedy is found acceptable, it will likely streamline the litigation that would follow a challenge.

This proposal, in short, "gets the incentives right," and thereby promises a more efficient and effective remedy policy: Simply put, the parties (and not the agencies) must fix it or forget it.

RECAPTURING THE BUSINESS SIDE OF INNOVATION IN ANTITRUST MERGER ANALYSIS

BY KENT BERNARD[1]

1 Adjunct Professor, Fordham University School of Law. I would like to thank Timothy Cornell, James Fishkin, Bill Kolasky and Mark Lemley for their comments and suggestions. They are absolved of any responsibility for any errors or omissions herein. A special thanks to the staff of the Fordham Law Library. In the midst of a pandemic, they remained helpful and responsive. They are much appreciated.

I. INTELLECTUAL ANTITRUST MEETS BUSINESS REALITY

The antitrust laws were not passed as an academic exercise. They were passed to break up the great Trusts, and to preserve competition. These were and are business issues. Our current debate over the impact of mergers on innovation seems to have left that business purpose and dimension by the side of the road. It is time to bring business back into the antitrust innovation debate.

We all seem to recognize that innovation is a key factor in determining the success or failure of a business, an industry, and society overall. Innovation drives progress. An antitrust policy that focused only on prices today but ignored a possible reduction in the rate of innovation "would be a calamity."[2]

Recently there has been considerable legal academic writing on whether and how mergers impact innovation.[3] But our current legal discussions focus on only a part of what makes innovation important. What we are omitting is exactly what we should be striving to protect and encourage. Innovation has a rich heritage in business and social science, a heritage that we are ignoring in our legal analysis.

Traditionally, we have looked to the impact of product overlaps in horizontal mergers; actual and potential competition. But the analysis now is going beyond products or even potential products. The argument is being made that a merger of two companies in the same market (or doing research in the same market) reduces "innovation" without regard to any product or even any potential product. In its strongest form, the thesis asserts that horizontal mergers *per se* always reduce innovation.[4] But to get to that point requires us to understand what "innovation" actually means, and what it requires. It turns out that what we have been measuring (and arguing about) doesn't actually correspond to innovation at all. The legal literature may be making a case over protecting some forms of competition, but it is not about protecting innovation, because we have been using a critically deficient definition of innovation.

We have set up a distinction between the idea of an innovation and the development of that idea into a successful product, and then set aside that second part. But the transition from idea to product is a critical step in the process. It is the result, the end product, that supports the importance of innovation and that we should be trying to protect. The current approach to evaluating the impact of mergers on innovation doesn't really have much to do with innovation at all.

II. WHAT IS INNOVATION?

One striking feature of the legal literature concerning the impact of mergers on innovation is that we confidently set out ways to measure innovation, without ever stopping to consider whether innovation actually is what we are measuring. Scholars outside of the legal field recognize that defining innovation presents some serious problems. After an overview of the literature, Baregheh, Rowley and Sambrook conclude that "there is no clear and authoritative definition of innovation."[5] Some legal scholars have made the same point. As Richard Gilbert noted, "[w]e remain far from a general theory of innovation competition."[6] But if we can't specify what innovation is with some confidence, how can we be confident that some action has an adverse (or a beneficial) impact on that innovation?

The ways in which the courts and agencies have tried to define innovation for the purposes of analyzing the impact of a merger, fall into a fairly consistent pattern. The analysis is done based on one or more research related factors that we can count on day one. We then assume or assert that what we have counted is "innovation" or determines innovation. But just because we can count something doesn't mean that it is the right, or the only, thing to count.

2 Frank Easterbrook, Ignorance and Antitrust, in Antitrust, Innovation, and Competitiveness 119, 122 (1992). See also Bernard and Tom, Antitrust Treatment of Pharmaceutical Patent Settlements, 15 Fed. Cir. Bar J. 617, 623 (2006).

3 See e.g. Federico, Giulio and Langus, Gregor and Valletti, Tommaso M., A Simple Model of Mergers and Innovation (June 29, 2017). CESifo Working Paper Series No. 6539. Available at SSRN: https://ssrn.com/abstract=3005163; Ioannis Kokkoris & Tommaso Valletti, Innovation Considerations in Horizontal Merger Control, *Journal of Competition Law & Economics* 1 (April 15, 2020); Mario Todino, Geoffroy van de Walle & Lucia Stoican, EU Merger Control and Harm to Innovation – A Long Walk to Freedom (from the Chains of Causation), The Antitrust Bulletin 1 (2018), available at https://www.jonesday.com/en/insights/2018/12/eu-merger-control-and-harm-to-innovationa-long-wal; L.I.M Suijkerbuijk, Innovation Competition In EU Merger Control, (2018), available at http://arno.uvt.nl/show.cgi?fid=145944.

4 Frederico et al., *supra* note 3; Justus Haucap & Joel Stiebale, Research: Innovation Suffers When Drug Companies Merge, Harvard Business Review, August 3, 2016.

5 Anahita Baregheh, Jennifer Rowley, Sally Sambrook, Towards a multidisciplinary definition of Innovation, Management Decision Vol.47 No.8 (2009) page 1323, 1324. Available at https://www.emerald.com/insight/content/doi/10.1108/00251740910984578/full/html?queryID=2%2F5414905.

6 Richard Gilbert, Looking for Mr. Schumpeter: Where are we in the Competition-Innovation Debate, 6 Innovation Policy and the Economy 159, 206 (2006).

If we take a broader view, the importance of innovation lies in the fact that it merges two separate actions. We measure the number or amount of inputs into the process - such things as the dollar amount invested in research, the number of compounds advanced in the FDA approval process - and in some cases (such as patents) the number of intermediate outputs from the process. But if we stop there, we are making a serious mistake. There also is an output dimension that links the idea and the execution of that idea into a successful product.

It is that execution component of innovation that is missing in our legal analyses, although it is a major point in the business and social science scholarship. *Innovation is important because it has real world effects* – better products, cures for diseases, explanations of natural phenomena. Meeting market needs (in the broad sense in which scientific advancement can be treated as part of the market) is a key parameter in determining whether something is a successful innovation, rather than simply an ingenious idea.

The Oslo Manual[7] published by the OECD, defines innovation as follows:"An innovation is the <u>implementation</u> of a new or significantly improved product (good or service), or process…."[8] That definition encompasses both the idea and the successful actualization of that idea. It is more than just R&D.[9]

"Successful innovation requires the coupling of the technical and the economic in ways that can be accommodated by the organization while also meeting market needs, and this implies close coupling and cooperating among many activities in the marketing, R&D, and production functions."[10]

The models used in the legal literature analyzing the impact of mergers on innovation never reach the question of meeting market needs. Partly, this may simply be a concession to the nature of models and the need to limit the number of variables at play at any one time. But the variable that is being excluded is a key one: the execution of the idea that takes it from just an idea to a successful product or process. This is what business cares about, and why antitrust is important. Business not only looks for that actualization of the idea, it measures it.[11] Our analysis has been simplified by eliminating perhaps the most important factor.

This concept of actualization – whether a good idea can be taken to a successful product, is enormously important. When one company is evaluating another as an acquisition candidate it looks at both the quantity and the value of the other company's research. Are there projects that the acquirer believes can succeed both in terms of being technically feasible, and being a success on the market? Those questions – technical feasibility and market value - drive decision making. Unless a proposed product is considered to be both something that both can be brought to market, and which is likely to earn back more than what it costs to bring it to market and to sell it, that proposed product is likely to be scrapped.[12]

7 The Oslo Manual is an internationally recognized methodology for collecting and using innovation statistics, assembled by the Organization for Economic Co-Operation and Development (the "OECD"). The Third Edition specifically treats the innovation process in some depth. Guidelines for Collecting and Interpreting Innovation Data (2005 Edition), available at https://ec.europa.eu/eurostat/web/products-manuals-and-guidelines/-/OSLO?inheritRedirect=true; see also https://unstats.un.org/unsd/EconStatKB/KnowledgebaseArticle10270.aspx.

8 Oslo Manual, Paragraph 146 (emphasis supplied).

9 Stephen J. Kline and Nathan Rosenberg, An Overview of Innovation, Studies on Science and the Innovation Process: Selected Works of Nathan Rosenberg, Chapter 9, pages 173-203 (2009), available at http://dec.ec.unipg.it/~fabrizio.pompei/KlineRosenberg(1986).pdf (pages 275 – 305).

10 *Id.* Pages 301-302 (emphasis supplied).

11 Nick Paul Taylor, Pfizer reports big jump in clinical trial success rate, Fierce Biotech February 2, 2021, available at https://www.fiercebiotech.com/biotech/pfizer-reports-big-jump-clinical-trial-success-rate (counting the compounds that that started out being tested in humans and ended up being approved for commercial sale).

12 This analysis and cull is done totally apart from any considerations of the structure of the acquisition or the status of the acquirer. It is simply part of the process of trying to be successful.

III. INPUT QUANTITY MEASUREMENTS AND THE AMOUNT OF INNOVATION

Most of the legal analyses of impact on innovation start by measuring inputs. Measures of such "innovation inputs" that have been used or proposed in this context include the number of companies doing R&D in a given market,[13] the number of R&D projects in that market, the amount of R&D Assets, the R&D capabilities of the parties,[14] the total R&D expenditures, and the amount of patenting that takes place.

With the exception of the number of patents, which will be discussed separately, these quantity measures share one key characteristic: they all assume that measuring inputs into the innovative process is the right way to measure innovation. That assumes not only that inputs alone can define innovation, but also that that a greater quantity of inputs into the innovation process correlates to greater innovation outputs. This second step is often glossed over as being obvious. But at the end of the day what is important is what comes out of the process, rather than what went into it. Inputs are simply tools to get us to the outputs that we desire. Input metrics measure if you are doing enough of the right activities. Output metrics measure whether you actually have achieved your goals.[15]

With those factors in mind, let us take a look at the various measures that have been proposed to determine if a merger has an adverse impact on innovation, and see if they capture both the conceptual and the actualization sides of innovation.

A. Companies in the Innovation Space

This is perhaps the highest level attempt to measure the impact of a merger on innovation – how many companies are doing something in your chosen field (broadly defined)? On this level, what we are looking for is what the European Commission in its 2010 Guidelines on Horizontal Cooperation called a "sufficient" number of R&D poles.[16] In the United States, the 2000 Antitrust Guidelines for Collaboration Among Competitors, at Section 4.3 state:

> "Absent extraordinary circumstances, the Agencies do not challenge a competitor collaboration on the basis of effects on competition in an innovation market where three or more independently controlled research efforts in addition to those of the collaboration possess the required specialized assets or characteristics and the incentive to engage in R&D that is a close substitute for the R&D activity of the collaboration."[17]

So how many companies or research poles is truly enough? In some innovation areas there are fewer than four players at the start of the relevant time. Does that mean that the parties should never be allowed to merge or collaborate? Should we simply ignore the Genzyme acquisition of Novazyme in 2001, bringing together the only two companies doing research into a treatment for Pompe disease, a rare and often fatal disease affecting infants and children for which there was no effective therapy at the time.[18] The question was which path promised to get an effective cure for Pompe disease approved and on the market faster – keeping the projects of the two companies separate, or allowing them to join forces?[19] The parties did merge and product did get developed and launched. Are we comfortable adopting an approach that tells us that the merger harmed innovation, despite its success in getting a treatment launched, because it led to one of the two projects being "killed"? Or did the merger increase innovation, by combining operations of the companies with the most knowledge in the field?[20] This would seem to be a highly fact dependent question. We can't support a broad claim that fewer companies in an innovation space means less innovation in that space. In Genzyme, the merger pretty clearly helped actualize the idea into a product.

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13 Petit, Innovation Competition, Unilateral Effects, and Merger Policy, 82 Antitrust Law Journal 873, 875 (2019). There is recognition that given the uncertainty that surrounds early research, the exit of one of the parties from an innovation space does not necessarily entail a loss of innovation output. *Id.* at note 113.

14 *Id.* page 874, citing cases.

15 Julia Kylliainen, Measuring Innovation – The Definitive Guide to Innovation Management KPIs (June 29, 2018), https://www.viima.com/blog/how-to-measure-innovation-kpis.

16 See the discussion in Bernard, Innovation Market Theory and Practice: An Analysis and Proposal for Reform, Competition Policy International, Spring 2011, Vol. 7, No.1 (2011), at text accompanying notes 105 and 106 and sources cited therein.

17 Available at https://www.ftc.gov/sites/default/files/documents/public_events/joint-venture-hearings-antitrust-guidelines-collaboration-among-competitors/ftcdojguidelines-2.pdf . But cf. Antitrust Guidelines for the Licensing of Intellectual Property (2017) at Section 4.3 stating that you need four or more independently controlled technologies in addition to the technologies controlled by the parties; https://www.justice.gov/atr/IPguidelines/download.

18 FTC Closes its Investigation of Genzyme Corporation's Acquisition of Novazyme Pharmaceuticals, Inc. (2004); available at http://www.ftc.gov/opa/2004/01/genzyme.htm.

19 Bernard, *supra* note 16, page 178.

20 See Grise, Burns & Giodano, The No Kill Zone: The Other Side of Pharma Acquisitions, CPI Antitrust Chronicle May 2020.

B. R&D Spending

The impact of the merger on combined R&D spending appears to be the most common way that we try to measure the impact of mergers on innovation.[21] The analysis usually proceeds based on two premises. First, if you put the two organizations together, the combined research and development spend will be less than the sum of the individual spends pre-merger. This is something that can be looked at and measured. Second, the less money spent on R&D equates to less innovation.[22] This is much more problematic.

The merged company may have substantial savings from combining facilities and streamlining the management structure. No one would seriously assert that either of those actions would have an adverse impact on innovation. In addition, as a matter of normal business practice, organizations rank research projects to determine funding and priority. When you combine two organizations, you can expect that there will be a review of the combined research pipeline. The result of that review may well be that some projects are discontinued. Some of the savings may be reallocated to more promising projects. How do those moves impact the amount of innovation? There is no a priori way to tell.

The use of R&D spending as a measure really just gives us our starting assumption (R&D spend equals innovation) enshrined in more complicated mathematical formulae. Reducing spending does not necessarily entail a reduction in innovation. You have to go much deeper into the specific details of the projects that were discontinued before you can establish that assertion. Would the project have succeeded in leading to a viable and profitable product but for the merger?

Furthermore, when you look beyond the legal literature, there is a substantial case that the whole argument rests on an unsound premise. Although it may seem counterintuitive, there is substantial evidence that the amount of R&D spending does not correlate with the amount of innovation very well, if at all.[23]

"Strategy & Business," a business unit within PriceWaterhouseCoopers, has been publishing an annual report of the top 1000 most innovative companies in the world for over 12 years now. In that time, it has found no statistically significant relationship between R&D spending and sustained financial performance. Its findings apply to total R&D spend, as well as R&D spending as a percent of revenues. Spending on R&D is not related to growth in sales or profits, increases in market capitalization or shareholder returns. In every single annual report that Strategy& has published, the top 10 most innovative companies are rarely the top 10 spenders on R&D."[24]

Financial performance is not the same as innovation *per se*. Still, one would expect the most innovative companies to show financial gains from that innovation. But these data argue that even if you show a reduction in R&D spending post-merger, the impact on innovation is unknown.[25] And as will be discussed further below, even a horizontal merger with actual overlapping programs does not necessarily entail that one or more of those programs will be killed. Before we can predict what will happen to a given research program we have to investigate patent protection, patent life, and the potential for successful product differentiation between the programs. You can't reliably predict the outcome without knowing the facts.

In light of this evidence, it is puzzling to see the European Commission concluding that if a horizontal merger will reduce spending on R&D, it therefore will reduce innovation. Innovation would seem to depend more on the effective use of R&D assets, rather than just the amount spent. And if we are looking for effective use of assets, sometimes a party already working in a field can better advance the work being done by the other party, than could someone outside the field.[26] Knowledge in a field learned on one project, can be used on another project. Rather than reducing innovation, a horizontal acquisition may actually increase the chances of a successful result.

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21 See e.g. Petit, *supra* note 13, page 874 and sources cited therein.

22 Kokkoris & Valletti, *supra* note 3, page 14; Haucap & Stiebale, *supra* note 4 (using money spent and R&D and number of patents produced as the measures of innovation).

23 The question is the effective use of resources resulting in a successful product, not just spending.

24 Tendayi Viki, Why R&D Spending Is Not A Measure Of Innovation (Forbes 2016), available at https://www.forbes.com/sites/tendayiviki/2016/08/21/why-rd-spending-is-not-a-measure-of-innovation/#2e2d5b4dc77d . The Strategy & report cited to is even more direct: "There is no long-term correlation between the amount of money a company spends on its innovation efforts and its overall financial performance." Jaruzelski, Chwalik, Goehle, What the Top Innovators Get Right, Strategy + Business Issue 93, Winter 2018 (October 30, 2018), available at https://www.strategyand.pwc.com/gx/en/insights/innovation1000.html; https://www.strategy-business.com/feature/What-the-Top-Innovators-Get-Right?gko=e7cf9.

25 This failure of proof has nothing to do with merger structure. If a private equity firm buys an operating company, we can expect cuts in R&D spending as part of an overall strategy to boost short term value and enable a resale of the company. See Bernard, Private Equity Meets Antitrust – Complications Ensue, CPI Antitrust Chronicle, January 2018.

26 Grise, Burns & Giodano, *supra* note 20, page 20.

A case study of this "use of knowledge" hypothesis was explored by the FTC in the matter of Genzyme's acquisition of Novazyme,[27] mentioned earlier. Only two companies were working in the field. The disease at issue affects a small number of people (i.e. the potential market for any end product is small), and the research was at the time preliminary, risky, and expensive. At the time of the case, there was no treatment for Pompe disease.[28] There was no evidence that anyone else was planning to enter into research on the treatment of the disease.

The issue for FTC Chairman Muris was whether the merger was likely to slow or reduce the progress towards and effective treatment for Pompe disease or whether it was likely to give the merged firm a greater ability to innovate and get an effective product launched more quickly. Two R&D programs had already failed. Genzyme and Novazyme had the remaining two programs. Both compounds were in the early pre-clinical stage. For drugs entered in Phase I testing (the first stage in which the drugs are given to people in the clinic); the failure rate is between about 75-85 percent.[29] The compounds in this case were not yet even in the clinic. It was by no means likely that either of these projects would make it to the finished drug stage at this point. Collaboration seemed scientifically the best way to get a

But what if two companies are both doing research that is more likely than not going to result in the near term in products that will directly compete? If they merge, will the merged company kill off one of those projects?[30] All we can say with any confidence is "perhaps."

The issue in that case isn't impact on *innovation*. It is a straight potential competition case, and can and should be analyzed that way.[31] It is a very different situation if the potential products are far from the market, or if we try to cut innovation from away from products entirely. If we are measuring whether or not drug compounds are likely to be advanced in the FDA approval process, without regard to whether they are more or less likely to reach the market (much less earn back their cost of capital), we have simply redefined innovation to be the number of drug compounds advanced one step in the approval process, regardless of whether the compounds ever became products. But in so doing we have hollowed out the definition of innovation. From a business and over all societal perspective, simply having candidates advance and fail at a higher step in the approval process cannot be the measure of innovation.

In *Dow/DuPont*,[32] the European Commission took a leap of faith into the unknown. The Commission gave us two separate analyses. The first is a classical one, looking at competition in markets for existing pesticides. The second is that the merger would reduce innovation. What is intriguing is that the Commission says that the merger would remove the parties' incentives to pursue ongoing parallel innovation efforts, without specifying what those efforts were.[33] Indeed, it could not really identify which projects, or even which lines of research, were likely to be discontinued.[34]

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27 FTC Closes its Investigation of Genzyme Corporation's 2001Acquisition of Novazyme Pharmaceuticals, Inc.(2004); https://www.ftc.gov/news-events/press-releases/2004/01/ftc-closes-its-investigation-genzyme-corporations-2001 What we had in that case was a debate over the decision to close (in 2004) the investigation of the merger which took place in 2001.

28 In 2006 the FDA approved the first such treatment, Genzyme's Myozyme. See https://www.biospace.com/article/releases/fda-approves-genzyme-corporation-s-myozyme-r-for-all-patients-with-pompe-disease-drug-to-carry-warning-/ (May 1, 2006).

29 Abrantes-Metz, Adams & Metz, Empirical Facts and Innovation Markets: Analysis of the Pharmaceutical Industry, The Antitrust Source, March 2005.

30 This is the premise behind Cunningham, Colleen and Ederer, Florian and Ma, Song, Killer Acquisitions (April 19, 2020). Available at SSRN: https://ssrn.com/abstract=3241707 or http://dx.doi.org/10.2139/ssrn.3241707 . The article makes predictions based on overall review of transactions and what products were advanced in the FDA approval process (but not necessarily reaching the market). The problem is that there is no factual analysis as to why a given compound failed, or was not developed further. Was there an Intellectual Property issue, a timing question, a royalty obligation, was the product simply a "me too" with minimal commercial prospects? Did the compound fail in clinical tests? All of these are key considerations, and ones that a company with a similar product in its own pipeline likely has more information about. We need to know what percentage of the "killed" products never really had good odds to reach the market at all. Otherwise we may be dealing with potential competition, but we are not dealing with innovation.

31 See Bernard, *supra* note 16, page 170 and notes 41 and 42.

32 Case M.7932 – Dow/DuPont, Comm'n Decision Paragraph 145 (March 27, 2017), non-confidential version available at https://ec.europa.eu/competition/mergers/cases/decisions/m7932_13668_3.pdf.

33 The EU Press Release makes this clear; Mergers: Commission clears merger between Dow and DuPont, subject to conditions 27 March 2017, available at https://ec.europa.eu/commission/presscorner/detail/en/IP_17_772.

34 See Petit, Innovation Competition and Merger Policy: New? Not Sure. Robust? Not Quite! (2018) available at https://medium.com/@CompetitionProf/innovation-competition-and-merger-policy-new-not-sure-robust-not-quite-19c8cec35494, page 4.

It is one thing to have a theory. It is quite another to say that your theory allows you to avoid identifying where there will be harm. The Commission's rationale is straightforward:

> "The merger between A and B will result in internalization by each merging party of the adverse effect of the R&D projects on the net revenues of the product lines of the other merging party; hence, in what this Annex called a merger-induced reduction in innovation competition, it will reduce investment in the competing R&D projects. The innovation competition effect follows the basic logic of unilateral effects, which is equally applicable to product market competition and to innovation competition."[35]

There is no real definition of innovation or innovation competition. And why the theory of unilateral effects should automatically apply to innovation competition, is left unsupported. But besides the theoretical problems it raises, the Commission's approach seems to be out of sync with what actually happens in many mergers. Where there are two paths, the merged company may well pursue both of them, especially if they take different approaches or could lead to differentiable products,[36] or have different levels of patent protection. We see this clearly with certain prescription drugs (e.g. Glaxo has Imitrex and Amerge, both are triptans indicated to treat migraine headaches. One is quick onset and strong, the other is slow acting but longer acting.).[37]

Only about 1 in about 4000 drugs proposed in preclinical testing actually ever makes it to market.[38] Once the drug gets to Phase I clinical trials, the probability of success increases substantially. Data show that about 26 percent of Phase I drugs eventually are launched on the market. For drugs that reach Phase II, the probability that the drug will get to market increases somewhat to 33 percent. For drugs that reach Phase III, the probability of success is 57 percent. But to predict the probability of success of an R&D project that has not yet entered clinical trials at all is just wild speculation.[39] And if it is too early to determine whether a pipeline product will ever become a marketed product, it seems unreasonable for the competition law agencies to intervene on the speculative ground that this potential overlap somehow harms innovation.[40] The analogy used is requiring a high school track coach to bless (or not) the engagement of a couple that may – one day – have a child, who may take to athletics and may become a champion sprinter.[41]

A final point is the assumption by some authors that the projected reduction in R&D spending is related to the structure of the transaction as a horizontal merger. But the motivation to reduce spending is inherent in just about every transaction, and is independent of deal structure. Even if the purchaser is a pure financial buyer with no other holding in the field at issue, we can expect cuts in R&D spending as part of an overall strategy to boost short term value and enable a resale of the company.[42]

C. R&D Headcount

The next measure proposed to determine impact on innovation is R&D headcount. But whether more bodies will lead to more innovation is unproven. The R&D headcount measure doesn't distinguish between the skills of the people involved, or how efficiently they operate. Throwing more people at a problem doesn't mean you have the right people, or that they are working on the right approach.[43] The purpose of spending on innovation is to get something valuable out the other end of the tube. Headcount doesn't tell us that. So can we measure innovation by output? And if so, output of what?

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35 Case M.7932 – Dow/DuPont, Comm'n Decision, Paragraph 145 (March 27, 2017), non-confidential version available at https://ec.europa.eu/competition/mergers/cases/decisions/m7932_13668_3.pdf.

36 See Denicolo and Polo, The innovation Theory of Harm: An Appraisal, 82 Antitrust Law Journal 921, 924 (2019).

37 See, e.g., Oliver & Taylor, Choosing the Right Triptan, Practical Pain Management, Volume 20, Issue 3 (forthcoming 2020), available at https://www.practicalpainmanagement.com/pain/headache/migraine/choosing-right-triptan.

38 Abrantes-Metz, *supra* note 29, pp. 3-4.

39 The actual chance of success for any given pre-clinical compound, based on the overall statistics, is 0.025%. That is twenty five one-thousandth of one percent.

40 Waisman and Hevia, Merger Control and Innovation: A Rights-Based Approach, Journal Of Economic Law and Practice (2021), page 3.

41 Id. Page 6 (citing Gavin Bushell, EU Merger Control and the Innovation Theory of Harm: Fake News? (2017) Kluwer Competition Law Blog, available at http://competitionlawblog.kluwercompetitionlaw.com/2017/03/03/eu-merger-control-and-the-innovation-theory-of-harm-fake-news/.

42 See Bernard, Private Equity Meets Antitrust – Complications Ensue, CPI Antitrust Chronicle, January 2018.

43 See e.g. Collison and Nielsen, Science Is Getting Less Bang for Its Buck, The Atlantic, November 16, 2018, available at https://www.theatlantic.com/science/archive/2018/11/diminishing-returns-science/575665/.

IV. OUTPUT QUANTITY MEASUREMENTS AND THE AMOUNT OF INNOVATION

"Innovation really has two parts, and this is what some people miss," [Jon Lauckner, Chief Technology officer, General Motors] explained. "The first part of innovation is the development, invention, patent or some other form of intellectual property. The second piece of innovation is the commercialization of that into products and services. *It's only when you commercialize that intellectual property, that know-how, that you transform an invention into an innovation.*"[44]

The analysis thus far has led us to consider that innovation is something that comes out of the process and that actualizes the invention. That is the "innovation" that we want to protect and nurture. With that caveat, let's look at a couple of measures that have been proposed as quantifying the output of innovation.

A. Patents

Correlating the amount of innovation with the number of patents has a certain intuitive charm. After all, two of the criteria for getting a patent in the United States are that the invention be novel and useful.[45] But assuming that the number of patents is a stable measure of innovation creates its own set of problems. There are a variety of factors that can affect patent counts.[46] People can apply for lots of patents without actually being very innovative. Other times, an industry can be exceptionally innovative without being patent dependent. That said, some commentators argue that patent numbers are a good measure of innovation,[47] and that patenting is closely related to other measures of innovative activity.[48] One author tried to balance the various factors and arguments:

> "But just how strong is the link between patent activity and innovation in an era of exponential technological progress?
>
> Just comparing the absolute number of patents on a company-by-company basis is misleading, to say the least. For example, consider the number of patents that companies have received thus far in 2015. According to this metric, IBM and Samsung are far and away the most innovative companies in the world, with 3,059 and 3,052 patents, respectively. Google ranks number five, with 1,083 patents, just ahead of Microsoft (No. 7), with 1,037. Apple, typically considered one of the most innovative companies in the world, comes in at only No. 11, with 780 patents. Facebook doesn't even crack the top 40.
> …
> However, just because you have a lot of highly cited patents … doesn't immediately mean that you can create valuable products from those patents. If you think about innovation as a process from first invention to final product, then patents only measure the front-end of that process — the actual invention — rather than the back-end of innovation: the launch of the commercialized product. If your research and development system is broken, you may be front-loading the system with a lot of patents, without very much to show for it."[49]

Following up on this point, Tim O'Reilly argues that neither patenting nor R&D spending give us a complete handle on innovation; that we need to take into account both the idea and the actualization of the idea into a product.[50]

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44 Joann Muller, How GM Lost – And Found The Path to Innovation, Forbes.Com (January 13, 2013) available at https://www.forbes.com/sites/joannmuller/2013/01/13/how-gm-lost-and-found-the-path-to-innovation/#554f4e584740 (emphasis supplied).

45 35 U.S.C. Section 101. See also https://www.justia.com/intellectual-property/patents/patentability-requirements/ .

46 Bronwyn H. Hall, Using Patent Data as Indicators, (2013), available at https://eml.berkeley.edu/~bhhall/papers/BHH13_using_patent_data.pdf.;' Erin Brown, Do Patents Invent Innovation?, Knowable Magazine (March 13, 2018), available at https://www.knowablemagazine.org/article/society/2018/do-patents-invent-innovation.

47 Carol Robbins, How Valuable are Patents as a Proxy for Innovation? Science and Engineering Indicators Perspective, Government-University-Industry Research Roundtable June 28, 2017, available at file:///C:/Users/Kent/Downloads/ecrobbinsjune%20guirr%20presentation_patents%20(5).pdf.; Riitta Katila, Using patent data to measure innovation performance; International Journal of Business Performance Management 2(1) · January 2000. But see Petra Moser, Patents and Innovation in Economic History, Annual Review of Economics, Vol. 8:241-258 (October 2016), available at https://www.annualreviews.org/doi/10.1146/annurev-economics-080315-015136.

48 See Jay Shambaugh, Ryan Nunn, and Becca Portman, Eleven Facts About Innovation and Patents, Brookings Institution, December 13, 2017, available at https://www.brookings.edu/research/eleven-facts-about-innovation-and-patents/.

49 Dominic Basulto, Patents are a Terrible Way to Measure Innovation, Washington Post July 14, 2015, available at https://www.washingtonpost.com/news/innovations/wp/2015/07/14/patents-are-a-terrible-way-to-measure-innovation/ See also Todino et al., *supra* note 3, page 11; Kokkoris, *supra* note 3, page 23.

50 Tim O'Reilly, How Do We Measure Innovation? Radar (March 26, 2010) available at http://radar.oreilly.com/2010/03/how-do-we-measure-innovation.html. He argues that there ought to be a way to measure the introduction of new products, and rank them by novelty and by widespread acceptance, in some way that reflects a more substantial measure of innovation and its impact on the economy.

In *Dow/DuPont*, the Commission actually created a hypothetical market of patent applications in a field, and then a market of the patent shares of companies for patents on herbicide new active ingredients, and then focused on the citations accumulated by a patent as indicative of the patent's innovative strength.[51] Looking at citations as a potential measure of the quality of the patent, is worth exploring, but ultimately doesn't bridge the disconnect between that patent and product that reaches the market. Can the success of a product really be tracked back to one or more specific patents?

Simply counting patents is a very rough way to try to measure innovation in general. But patenting is important, indeed crucial, on a related issue – the attempt to predict post-merger conduct of the parties. Any commercial advantage that may result from patent protection has a defined life and a defined end point. This life span needs to be a key part of any analysis of what parties are likely to do. If you don't have an estimate of how long an existing product will continue to generate significant revenues, how can you possibly predict how the company will treat a research project that may supplement or supplant that first product?[52]

Antitrust models may predict that a company will kill a potential product which threatens to upset its current "monopoly," but that is too blunt an approach to the issue of subsequent products. It is the time factor of revenue destruction that drives the business decisions.[53] Every seller needs either to continue its income stream, or replace it, in order to survive. A product (or compound) with weak patent protection, is less valuable than a product or compound with stronger patent protection.[54] A non-patented product that is not a prescription drug may survive quite well for many years. Listerine brand mouthwash was first launched in 1879 and is still going strong.[55] The models need to take this into account if they are going to give us valid prediction of what the parties are "likely" to do post-merger. Facts need to drive the analysis. Identifying key patents and their expiration dates, needs to be part of the merger analysis on the legal as well as on the business side.

B. Products

If the point of innovation is to get new or better products, then counting new products could be used to measure innovation. But there is a problem with that approach which mirrors the problem with counting patents. Launching two great products may be much more evidence of innovation than launching 20 mediocre ones. "It's usually not a great idea to sacrifice quality for quantity."[56] It is difficult to strike that balance between quantity and quality. This may have been one of the reasons that the European Commission explicitly cut its analysis of innovation free from any specific product or product line.

The data do not say that we should ignore the potential impact of any one factor. Cuts in R&D spending may or may not have an impact, depending on where the cuts are made and the value of the projects being no longer funded.[57] It all depends on the facts of the specific situation.

But finding, predicting, or assuming that a number of products will be cut does not entail finding that the merger will cause a decrease in innovation. The same critique applies to attempts to tie the amount of innovation to R&D spending, headcount, or patenting. They all give us quantity, but not quality. But there is one approach that deals with both sides of the innovation definition – the idea and the actualization of it.

51 See Suijkerbuijk, *supra* note 3, at text accompanying notes 259 – 271.

52 Cunningham et al., *supra* note 30, do not seem to take this into the analysis of their cannibalization assumption. The so-called replacement effect needs to recognize that a second product with strong patent protection can be very valuable to a company with an existing product whose protection is ending.

53 See Bernard, *supra* note 16 at pages 168-170.

54 This is what drives the strategy knows as "patent hopping," where a drug innovator, whose patent is expiring soon, tries to encourage or force doctors to prescribe a new version of the product that has longer patent protection. The law here is still evolving. I would predict that the general rule is likely to be that persuasion is fine, but coercion (say, by withdrawing the older product before it can be copied by generics) is illegal. See generally Tobin Klusty, A Legal Test for the Pharmaceutical Company Practice of "Product Hopping, (2015) *AMA J Ethics.* 2015;17(8):760-762. available at https://journalofethics.ama-assn.org/article/legal-test-pharmaceutical-company-practice-product-hopping/2015-08.

55 See Johnson & Johnson, History of LISTERINE®: From Surgery Antiseptic to Modern Mouthwash, available at https://www.listerine.com/about.

56 Julia Kylliainen, *supra* note 15, page 6.

57 This caution also would apply if a single player cut back on a particular line of inquiry. It may not be simple to link the potential harm here to a merger or acquisition.

V. A PROPOSED WAY TO DEFINE AND MEASURE INNOVATION

This analysis has tried to show that our current attempts to define and measure innovation suffer from a basic mistake. They divorce the idea of innovation from its implementation in a product.

When we look at various business and other non-legal attempts to define innovation, they have a common theme. Innovation can start out as an idea, a product or a process. What takes that initial idea to the level of an innovation is that it fills a perceived market need (taking market in the broadest sense to include the advancement of science). Pure science apart, an innovation needs to have a commercial dimension. It is this commercial dimension that ties the area back to the competition agencies, and to the purposes behind the antitrust laws. If the "innovation" is not commercial in some sense, it is difficult to see why competition law agencies should get involved in it. We need a definition that captures both the idea of a discovery and the subsequent execution of the idea such that it has a real world impact.

One promising approach to combining the quantitative and qualitative aspects of innovation was proposed by Brian Quinn, writing about how large organizations can innovate more effectively. After looking at various possible measures, he concludes that a measure used in business, the "hit rate," lets us measure innovation in a way that reunites the idea and the implementation dimensions.

"That said, measuring the organization's hit rate – <u>the percentage of innovations that create value by returning their cost of capital or other metric</u> – is one I'd recommend in almost any context, and keeping in the measurement system over time."[58]

Research has not revealed any merger cases where either party's hit rate for innovation has been used in the analysis. Looking at this metric would give us a way to compare the innovative effectiveness of the two companies proposing to merge. Without more, it wouldn't tell us the effect of the merger on innovation going forward. But it would be a starting point. We tend to do analyses based on overall R&D spending. But looking at the hit rate gives us an idea of R&D <u>effectiveness</u>, the quality of the innovation, which is much closer to what we should be caring about. Admittedly it is not easy to calculate whether an innovation does return its cost of capital. R&D is expensed, not capitalized into the overall cost of a specific product. Currently, businesses can choose to fully expense the costs of research and development (R&D); that is, they can deduct the costs of R&D from their taxable income in the year that those costs occur.[59]

But many companies keep track of expenses attributable to individual projects as a management tool, even if such calculations are not used for tax or reporting purposes. A business wants to know which projects generate a net profit. One measure which comes close to capturing the hit rate concept, is the clinical trials success rate: the percentage of compounds that enter clinical trials in people and go on to win approval to be marketed. In other words, ideas that becomes products. Companies are making those calculations right now.[60] It is time for the legal world to catch up.

To get from the clinical trials success rate to the hit rate is simply a matter of tracking the net sales and profits of the products, something that almost every company does routinely. Those data could be reached by a carefully targeted information request or civil investigative demand from a competition agency. These calculations are primarily backward looking, telling us which projects have met the hit rate test as being true innovations. Projecting what will (or is likely to) happen in the future as a result of a merger is difficult, but not impossible.

58 Brian Quinn, Why Measuring Innovation Matters, Forbes.com (November 5, 2015), available at https://www.forbes.com/sites/brianquinn/2015/11/05/why-measuring-innovation-matters/#59810f3e6cd8 (emphasis supplied).

59 Expensing is the proper tax treatment of investment and other business costs, as it prevents a firm's profits from being overstated in real terms. This lowers the cost of investment. Requiring a firm to amortize business costs over a number of years overstates the firm's taxable income, reducing business capital investment.
Starting in 2022, the Tax Cuts and Jobs Act (TCJA) will require companies to amortize their R&D costs over five years, instead of deducting them immediately each year. https://files.taxfoundation.org/20190204170826/Amortizing-Research-and-Development-Expenses-under-the-Tax-Cuts-and-Jobs-Act-FF635.pdf.

60 See e.g. Nick Paul Taylor, Pfizer reports big jump in clinical trial success rate, Fierce Biotech February 2, 2021, available at https://www.fiercebiotech.com/biotech/pfizer-reports-big-jump-clinical-trial-success-rate . A more detailed explanation, showing the success rate by clinical trial phase, and including the end to end success rate, is found in the Pfizer Earnings Report dated February 2, 2021, at page 10, available at https://s21.q4cdn.com/317678438/files/doc_financials/2020/q4/Q4-2020-PFE-Earnings-Release.pdf.

VI. SOME CONCLUDING THOUGHTS

This article has tried to deal with the problem of defining innovation so that we can more accurately see what kinds of actions or transactions are likely to help, or harm innovation in a real world context, where theory and commerce combine. So far, the legal arguments and analyses have left business on the sideline. It is time to invite it back into the antitrust game. If we are truly going to protect innovation, we need to use the fully loaded definition that includes both the idea and the result. Then we will have a solid foundation to investigate whether the impact of a given merger is likely to help, harm, or simply bypass innovation. Our current approaches don't actually let us determine the impact of mergers on innovation because they use a one-sided definition of innovation, a definition that is recognized as incomplete in business and social science. The hit rate concept provides us with an approach that includes both sides of innovation – idea and product. It is up to us to use it.

"SOMETHING IS HAPPENING HERE BUT YOU DON'T KNOW WHAT IT IS. DO YOU, MRS. JONES?" DARK PATTERNS AS AN ANTITRUST VIOLATION

BY JAY L. HIMES & JON CREVIER[1]

1 Title adapted from Bob Dylan, Ballad of a Thin Man (1965). Jay Himes is a former co-chair of Labaton Sucharow LLP's Antitrust Practice Group, and also a former Antitrust Bureau Chief, Office of the Attorney General of the State of New York. Jon Crevier is an associate at the Labaton firm.

As internet users surf from one website to another, or use web-enabled applications, they regularly — and unknowingly — encounter "dark patterns" — "the often unseen web-design choices that trick users into handing over more time, money, or attention than they realize."[2] Dark pattern techniques "make it difficult for users to express their actual preferences or . . . manipulate users into taking actions that do not comport with their preferences or expectations. Examples of dark patterns abound in privacy and security."[3] As Acting FTC Chair Rebecca Slaughter recently said in keynoting an agency workshop — Bringing Dark Patterns to Light — "[w]e increasingly see companies using dark patterns to manipulate people into giving up their data, which is then sold, aggregated, analyzed, and used to target advertising and manipulate future purchases and behavior . . . . We also see dark patterns used more directly to manipulate consumer behavior."[4]

This state of affairs is only likely to get worse: "[e]merging methods of big data present a new and vastly more efficient way to identify cognitive bias by attempting to pinpoint profitable anomalies."[5] As artificial intelligence develops apace and as the "internet of things" rolls out, the ability and opportunity to manipulate and exploit consumer biases will, predictably, increase — unless we take action to stop it.

Below, we first explain what dark patterns are and why they are used so frequently online. After that, we address the impact of dark patterns on user choice and online engagement. Finally, we discuss various approaches to attack dark patterns. Legal action grounded in prohibition of false or deceptive acts or practices, as well as legislation and regulatory intervention, are two approaches. Another, however, is antitrust enforcement, as dark patterns have competitive consequences. Dark patterns shift surplus from customers to suppliers and raise rivals' costs to persuade customers to switch to their platforms. Accordingly, existing antitrust law is nimble enough to tackle dark patterns.

I. WHAT ARE DARK PATTERNS?

Dark patterns "are not mistakes. They're carefully crafted with a solid understanding of human psychology, and they do not have the user's interests in mind."[6] Dark patterns draw on recognized human behavioral phenomena to "nudge" users in the direction sought by the online company even though this direction might not otherwise be preferred by the user or in the user's best interests. The "roach motel" technique is one example: "The design makes it very easy for you to get into a certain situation, but then makes it hard for you to get out of it (e.g. a subscription)."[7] For example, "Amazon makes it exceedingly easy for consumers to sign up for Prime, only requiring a couple of clicks on a prominent advertising banner. This stands in stark contrast to the process of ending the subscription."[8] Then, the prime member is "faced with a large number of hurdles, including complicated navigation menus, skewed wording, confusing choices, and repeated nudging," which "takes at least seven clicks to complete. . . ."[9]

Harry Brignull, a UK web designer who coined the expression "dark patterns," identifies other common techniques:[10]

- Trick questions: "When glanced upon quickly the question appears to ask one thing, but when read carefully it asks another thing entirely."

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2 Sidney Fussell, The Endless, Invisible Persuasion Tactics of the Internet, The Atlantic (Aug. 2, 2019), https://www.theatlantic.com/technology/archive/2019/08/how-dark-patterns-online-manipulate-shoppers/595360/.

3 Stigler Ctr., Stigler Comm. on Digital Platforms, Final Report, at 210 (2019), Stigler-Committee-on-Digital-Platforms-Final-Report.pdf (publicknowledge.org) (" Stigler Center Report"); see also *id.* at 12-13, 237-55.

4 FTC, Bringing Dark Patterns to Light, Workshop (Apr. 29, 2021), at 1-2, (transcript available at https:// www.ftc.gov/system/files/documents/public_events/ 1586943/ftc_darkpatterns_workshop_transcript.pdf.) (" FTC Workshop").

5 Ryan Calo, Digital Market Manipulation, 82 Geo. Wash. L. Rev. 996, 1010 (2014).

6 Harry Brignull, Dark Patterns: inside the interfaces designed to trick you, The Verge, (Aug. 29, 2013), https://www.theverge.com/2013/8/29/4640308/dark-patterns-inside-the-interfaces-designed-to-trick-you. See also Daniel Susser, Beate Roessler & Helen Nissenbaum, Technology, autonomy, and manipulation, 8 Internet Pol'y Rev. 1, 7 (Issue 2 2019) (dark patterns are "design strategies that exploit users' decision-making vulnerabilities to nudge them into acting against their interests (or, at least, acting in the interests of the website or app)"), https://policyreview.info/articles/analysis/technology-autonomy-and-manipulation.

7 Harry Brignull, Dark Patterns: Roach Motel, https://www.darkpatterns.org/types-of-dark-pattern/roach-motel.

8 Norwegian Consumer Council, You Can Log Out, But You Can Never Leave 29 (Jan. 14, 2021), https://fil.forbrukerradet.no/wp-content/uploads/2021/01/2021-01-14-you-can-log-out-but-you-can-never-leave-final.pdf.

9 *Id.* at 3, 11.

10 Harry Brignull, Dark Patterns: Types of Dark Patterns, https://www.darkpatterns.org/types-of-dark-pattern. See also Australian Competition & Consumer Commission (ACCC) Digital Platforms Inquiry: Final Report, at 422 et seq. (§7.7) (Dec. 2018) (discussing design choices and practices that nudge consumers away from less privacy invasive data collection, use, and disclosure) https://www.accc.gov.au/system/files/Digital%20platforms%20inquiry%20-%20final%20report.pdf ("ACCC Report"); Jamie Luguri & Lior Jacob Strahilevitz, Shining a Light on Dark Patterns, 13 J. Leg. Anal. 43, 53 (2021) ("Table 1: Summary of existing dark pattern taxonomies"), https://ssrn.com/abstract=3431205.

- Sneak into Basket: On your way to online checkout, an additional item is put into your basket, "often through the use of an opt-out radio button or checkbox on a prior page."

- Privacy Zuckering: Tricks that cause the user to share more information than really intended.

- Price Comparison Prevention: Design techniques that make it hard to compare the prices of items, "so you cannot make an informed decision."

- Misdirection: Design techniques that "purposefully focus[…] your attention on one thing in order to distract your attention from another."

- Hidden Costs: At the final checkout step, unexpected charges appear, such as delivery charges or taxes.

- Bait and Switch: "You set out to do one thing, but a different, undesirable thing happens instead."

- Confirmshaming: "[G]uilting the user into opting" in, by wording the opt-out option "in such a way as to shame the user into compliance." (For example, "No thanks, I'm not into savings"[11]).

- Disguised Ads: Camouflaging ads "as other kinds of content or navigation, in order to get you to click on them."

- Forced Continuity: Once a free trial ends, "your credit card silently starts getting charged without any warning. In some cases this is made even worse by making it difficult to cancel the membership."

- Friend Spam: You're asked for your email or social media permissions "under the pretense it will be used for a desirable outcome (e.g. finding friends), but then spams all your contacts in a message that claims to be from you."

FTC Commissioner Chopra has similarly noted that "[d]ark pattern tricks involve an online sleight of hand using visual misdirection, confusing language, hidden alternatives, or fake urgency to steer people toward or away from certain choices."[12] An online retailer who — to create a sense of urgency — reports to the potential customer that there is "one in inventory" for an item when that simply is untrue is illustrative.[13] A study of 11,000 online shopping websites identified 1818 instances of dark patterns, falling into 15 types — and, indeed, uncovered third-parties marketing their ability *to enable* dark patterns.[14]

In sum, while varying in form, dark patterns center on two themes: (1) some are deceptive or "information-hiding," thus "deceiving [users] or by delaying the necessary information to them," while others (2) "are asymmetric, covert, or deferentially treating of users, and restrictive."[15] Regardless of the theme, the effect is to "modify the decision space for users" so as to "ultimately influence how users make choices"[16] Notably, dark patterns can affect particular groups — indeed, even particular individuals — differently, and thus cause disparate, rather than uniform, harm.[17]

11 Numerous examples of confirmshaming can be seen at confirmshaming.tumblr.com.

12 F.T.C., Statement of Commissioner Rohit Chopra, Regarding Dark Patterns in the Matter of Age of Learning, Inc., (Sept. 2, 2020), https://www.ftc.gov/system/files/documents/public_statements/1579927/172_3086_abcmouse_-_rchopra_statement.pdf. See also Anastasia Kozyreva, Stephan Lewandowsky & Ralph Hertwig, 21 Psych. Sci. in the Pub. Int. 103, 111-14 (Issue 3 2020) (discussing persuasive and manipulative techniques, and identifying, as categories of dark patterns, sneaking, urgency, misdirection, social proof, scarcity, obstruction, and forced action), https://journals.sagepub.com/doi/pdf/10.1177/1529100620946707. See also FTC Workshop, *supra* n. 4, at 8-9 (remarks of Arunesh Mathur: identifying dark patterns by their attributes).

13 See generally Stigler Center Report, *supra* n. 3, at 241.

14 Arunesh Mathur, *et al.*, Dark Patterns at Scale: Findings from a Crawl of 11K Shopping Websites, The Atlantic (Sept. 2019), § 5.1 & Table 1, § 5.2 & Table 2, https://arxiv.org/pdf/1907.07032.pdf.

15 FTC Workshop, *supra* n. 4, at 8 (remarks of Arunesh Mathur).

16 *Id.* at 8. See also Stigler Center Report, *supra* n. 3, at 238 (dark patterns' "central unifying feature is that they are manipulative, rather than persuasive. More specifically, the design choices inherent in dark patterns push users towards specific actions without valid appeals to emotion or reason."). See generally *id.* at 238-42; Norwegian Consumer Council, Deceived By Design, 6-7 (§3.1), 12-39 (§4) (discussing dark patterns created by Facebook, Google, and Microsoft using (1) default settings, (2) cumbersome setting navigation paths, (3) framing, (4) rewards and punishments, (5) forced action and control, (5) illusion of user control) (June 27, 2018), https://fil.forbrukerradet.no/wp-content/uploads/2018/06/2018-06-27-deceived-by-design-final.pdf.

17 See e.g. FTC Workshop, *supra* n. 4, at 2 (remarks of FTC Acting Chair Rebecca Slaughter), 13 (remarks of Kat Zhou & Dr. Katharina Kopp), 25, 29 (remarks of Lior J. Strahilevitz), 44-45, 52 (remarks of Mutale Nkonde), 49-51 (remarks of Drs. Jasmine McNeely & Kelly Quinn), 53-65. (panel discussion of dark patterns directed to children and teens), 84 (remarks of Daniel Kaufman).

II. WHY ARE ONLINE DARK PATTERNS SO PREVALENT?

There is a commonsense intuition that probably accounts for the frequency of dark patterns in the online space: "the internal, proprietary research suggests dark patterns generate profits for the firms that employ them."[18] As web designer Brignull told those at the FTC's recent Dark Patterns Workshop:

Imagine if you ran a business and you could press a button to get your customers to spend 21 percent more, it's a no-brainer. Of course you'd press it. And that's the reason why dark patterns exist.[19]

In consequence, "[m]odern online environments are replete with smart, persuasive choice architectures that are designed primarily to maximize financial return for the platforms, capture and sustain users' attention, monetize user data, and predict and influence future behavior."[20] As web designers build dark patterns into their sites, these techniques "undermine consumers' ability to make free and informed choices by making us act against our own interests in favour of the interest of service providers."[21]

III. PERSUASION V.2.0 — OR NOT?

Advertiser persuasion — even deception — is, of course, nothing new. Are digital world dark patterns simply old wine in new wineskins? We, along with many others, think not. "Traditional brick-and-mortar stores and online platforms differ greatly in their advertising and personalization capabilities."[22] Several conditions in the online world coalesce to favor much enhanced resort to dark patterns:

- For one, while websites appear neutral, online companies "design every aspect of the interaction with the consumer."[23] These consumer-facing websites mask how the "interface shapes [the user's] interactions with, and perception of, online content" and cause them to "underappreciate the constructed nature of the information and choices presented . . . ."[24]

- At the same time, online companies are incented to cultivate in the user an "illusion of control" so that "deceptive design is unlikely to be questioned or even noticed."[25] Thus, users "routinely interact with the online environment in an efficient, task-focused, and habitual way," often acting reflexively "based on only a few visual cues" and ignoring "the rest of the screen."[26]

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18 Luguri, *supra* n. 10, at 45.

19 FTC Workshop, *supra* n. 4, at 7.

20 Kozyreva, *supra* n. 12, at 111 (citation omitted).

21 Norwegian Consumer Council, *supra* n. 8.

22 Stigler Center Report, *supra* n. 3, at 45. See also Margherita Colangelo & Mariateresa Maggiolino, Manipulation of Information as Antitrust Infringement, 26 Colum. J. Eur. L. 63, 64-65 (2020); Kozyreva, *supra* n. 13, at 106-11 (discussing systematic differences between online and offline environments); Luguri, *supra* n. 10, at 103 ("The online environment is different. It is perhaps only a difference of degree, but the degrees are very large. . . . What was once an art is now a science. As a result, consumers' ability to defend themselves has degraded."); FTC Workshop, *supra* n.4, at 35 (remarks of Finn Lutzow-Holm Myrstad: "The experience . . . from a brick and mortar stores . . . [is] taken up to another scale and can also do this in real time and really see how it works and how different consumer groups react to different types of dark patterns.").

23 Calo, *supra* n. 5, at 1004.

24 Lauren E. Willis, Deception by Design, 34 Harv. J. of Law & Tech. 116, 132 (2020).

25 *Id.* at 133; ACCC Report, *supra* n. 10, at 423 (§7.7.2); Kozyreva, , *supra* n. 12, at 104("the Internet is . . . , notwithstanding appearances, a highly controlled environment," in which user access "is regulated by algorithms and design choices made by corporations in pursuit of profits and with little transparency or public oversight.").

26 Willis, *supra* n. 24, at 132, 138; Susser, *supra* n. 6, at 7-8 (that digital technology has "become invisible to us — simply through frequent use and habituation — means the influences they facilitate are often hidden, and thus potentially manipulative. . . . And the more we become habituated to these systems, the less attention we pay to them.").

- Also, user activity online lends itself to "A/B testing," a technique in which slight website variants are delivered to subset user groups to determine that variant that results in "more" of the tester's desired response — "gaining more clicks, longer visits, more purchases."[27] "Online experiments allow designers to find the answers with just a few lines of code."[28] The variants can reflect subtle differences: "Yes, it's true that a team at Google couldn't decide between two blues, so they're testing 41 shades between each blue to see which one performs better."[29]

- Using A/B testing and applying computer analytics to massive amounts of data and real-time user activity, online companies can identify user vulnerabilities and exploit the interaction moment not only for groups, but also for individuals — and to deliver personalized ads systematically.[30]

Consequently, opportunities and techniques in the digital space, beyond those available in the brick and mortar world, enable dark patterns to drive decisions that the user otherwise would not make. Further, in the brick and mortar world, a customer can "just say no" to hype and walk away. By contrast, in the digital space, even when the user does not succumb to the dark patterns, the online company still collects valuable user data before the user eventually navigates her way out.[31]

IV. HOW BAD IS IT — REALLY?

In a recent study, researchers invited random participants to answer survey questions relating to their privacy views, after which they were offered a data protection plan.[32] A control group could decline the plan in a simple yes/no screen, while two other participant groups were subjected to either "mild" or "aggressive" dark patterns. Those subject to mild dark patterns accepted the protection plan 2.3 times more often than the control group, and those subject to aggressive dark patterns 3.7 times more often.[33] As these study results confirm, "we're seeing dark patterns proliferate because they're extremely effective."[34]

In a second study, these researchers probed more closely the impact of particular forms of dark patterns. Some "had a striking effect on consumer choice, others had little to no effect."[35] Of those exposed to a trick question, only half of those who in fact accepted the protection plan *believed* they had done so.[36] The trick worked: "not only were consumers manipulated into selecting acceptance, but they didn't understand that they had been manipulated and signed up for something that they didn't actually want to sign up for."[37] The researchers thus concluded: "*dark patterns are strikingly effective in getting consumers to do what they would not do when confronted with more neutral user interfaces.*"[38]

The 2020 House subcommittee report quoted from this research: "[dark patterns] are harming consumers by convincing them to surrender cash or personal data in deals that do not reflect consumers' actual preferences and may not serve their interests. There appears to be a substantial market failure where dark patterns are concerned — what is good for ecommerce profits is bad for consumers."[39] "Market

27 Brian Christian, The A/B Test: Inside the Technology That's Changing the Rules of Business, Wired (Apr. 25, 2012), https://www.wired.com/2012/04/ff-abtesting/. See generally Willis, *supra* n. 24, at 116, 127-28 & n. 52; Calo, *supra* n. 5, at 1015 & n. 114.

28 Arvind Narayanan, Arunesh Mathur, Marshini Chetty & Mihir Kshirsagar, Dark Patterns: Past, Present, and Future, 18 ACM Queue 67, 76 (Issue 2 2020).

29 Douglas Bowman, Goodbye, Google (Mar. 20, 2009), https://stopdesign.com/archive/2009/03/20/goodbye-google.html. See also FTC Workshop, *supra* n. 4, at 38 (remarks of Dr. Jonathan Mayer: company tested different shades of grey "to see how that changed user behavior with the consent notice.")

30 See generally Willis, *supra* n. 25, at 132, 142-45; Susser, *supra* n. 6, at 6-7; Calo, *supra* n. 5, at 1021-22; FTC Workshop, *supra* n. 4, at 13-14 (remarks of Dr. Katharina Kopp); Stigler Center Report, *supra* n. 3, at 242.

31 FTC Workshop, *supra* n. 4, at 45-46 & 46-47 (remarks of Drs. Jasmine McNeeley & Kelly Quinn).

32 Luguri, supra n. 10,. See generally FTC Workshop, supra n. 4, at 21-30 (remarks of Lior Jacob Strahilevitz: describing the study).

33 Luguri, *supra* n. 10, at 64.

34 FTC Workshop, supra n. 4, at 25 (remarks of Lior Jacob Strahilevitz).

35 Luguri, *supra* n. 10, at 75.

36 *Id.* at 78 (emphasis in original).

37 FTC Workshop, *supra* n. 4, at 28 (remarks of Lior Jacob Strahilevitz).

38 Luguri, *supra* n. 10, at 46.

39 House Subcommittee on Antitrust, Commercial and Administrative Law of the Committee on the Judiciary, Investigation of Competition in Digital Markets, Majority Staff Report and Recommendations 53 (2020) (footnote omitted) (quoting Luguri, *supra* n. 10, at 81-82).

failure" is both a consumer protection and an antitrust concern. Dark patterns are deployed to encourage continued user engagement with the online company, and user engagement equates to more data captured. For already dominant platforms, more data fortifies barriers to entry, thus perpetuating the feedback loop, driven by economies of scale and scope, that entrenches dominance.[40] But even for non-dominant players, by maintaining user site engagement, dark patterns dampen competition.

V. DECEPTIVE BY DESIGN

The dark patterns practiced on users today are akin to "subliminal" advertising used in television or radio broadcasts. "Subliminal" advertising is "any technique whereby an attempt is made to convey information to the viewer by transmitting messages below the threshold level of normal awareness."[41] Thus, subliminal ads "bypass the viewer's conscious mind entirely and lodge in the subconscious as fully formed and conclusory thoughts. They are, therefore, inconsistent with the goal of rational consumer choice and should be condemned as an unfair consumer practice."[42] Accordingly, in 1974, the Federal Communications Commission declared subliminal ads "contrary to the public interest. Whether effective or not, such broadcasts clearly are intended to be deceptive."[43] And although the case law is limited, courts have held that subliminal messages are "akin to false and misleading commercial speech" and thus subject to "little, if any, first amendment constitutional protection."[44]

Dark patterns are subliminal ads on steroids. Subliminal ads at least have to wait for viewer-groups before they can be used. By contrast, in the digital space, firms "choose when to approach consumers, rather than wait until the consumer has decided to enter a market context."[45] Dark patterns thus can be delivered whenever a user surfs the internet, and they can be adapted for individual users, specifically targeted to manipulate that particular user's decision-making process *at the very moment approached*.[46]

For example, digital companies have learned techniques to produce neuro-chemical responses in users, stimulating dopamine in the brain, to "hook" them on engaging the online site. Dopamine "is a neurotransmitter that rewards the body when a positive event occurs randomly."[47] As Sean Parker, Facebook's early president, has stated publicly, the company developed features such as the "like" button to give users "a little dopamine hit" that would help Facebook "consume as much of [the user's] time and conscious attention as possible."[48] Apple executive Eddie Cue similarly wrote internally: "[g]etting customers using our stores . . . is one of the best things we can do to get people hooked to the ecosystem."[49] Thus, "[t]ech companies understand what causes dopamine surges in the brain and they lace their products with 'hijacking techniques' that lure us in and create 'compulsion loops.'"[50] The more time the user spends on a company's website, the more data the company amasses, and the greater is its ability to target and manipulate.[51] "[P]ersonal data is the fuel of the manipulation process."[52]

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40 See FTC Workshop, *supra* n. 4, at 1 (remarks of Acting FTC Rebecca Slaughter).

41 Broadcast of Information by Means of 'Subliminal Perception' Techniques, 44 F.C.C. 2d 1016, 1017 (1974) (quoting the NAB Television Code).

42 Neil W. Averitt & Robert H. Lande, Consumer Sovereignty: A Unified Theory of Antitrust and Consumer Protection Law, 65 Antitrust L.J. 713, 740 (1997).

43 44 F.C.C. at 1017. See generally Marisa E. Main, Simply Irresistible: Neuromarketing and the Commercial Speech Doctrine, 50 Duq. L. Rev. 605, 615-16 (2012).

44 *Waller v. Osbourne*, 763 F. Supp. 1144, 1148 (M.D. Ga.1991), *aff'd without op.*, 958 F.2d 1084 (11th Cir.1992), *cert. denied*, 506 U.S. 916 (1992). See also *Vance v. Judas Priest*, 1990 WL 130920, at *25 (D.C. Nev. Aug. 24, 1990) ("not entitled to First Amendment protection") (appendix: summary judgment ruling). *Cf.* Ramsi A. Woodcock, The Obsolescence of Advertising in the Information Age, 127 Yale L. J. 2270, 2330 (2018) (footnote omitted) ("advertising that is purely persuasive, in the sense that it conveys no useful product information, is not protected by the First Amendment."); Calo, *supra* n. 5, at 1040 ("the collection of data for an unexpected purpose, the potential of digital market manipulation to mislead, or the possibility of undue influence" militate against First Amendment protection).

45 *Id.* at 1004.

46 See generally Susser, *supra* n. 6.

47 Gregory Day & Abbey Stemler, Are Dark Patterns Anticompetitive?, 72 Ala. L. Rev. 1, 12 (2020).

48 Olivia Solon, Ex-Facebook president Sean Parker: site made to exploit human 'vulnerability', The Guardian, (Nov. 9, 2017), https://www.theguardian.com/technology/2017/nov/09/facebook-sean-parker-vulnerability-brain-psychology. See generally *Stigler Center Report, supra n. 3, at 64-66 ("Online Exploitation and Addiction"); Day, supra* n. 47, at 21-22.

49 Dorothy Atkins, Apple Wanted App Users 'Hooked,' Exec's 2013 Email Reveals, Law360 (May 11, 2021), https://www.law360.com/articles/1383530/apple-wanted-app-users-hooked-exec-s-2013-email-reveals.

50 David Brooks, How Evil Is Tech? NY Times (Nov. 20, 2017), https://www.nytimes.com/2017/11/20/opinion/how-evil-is-tech.html. See also Simon Parkin, Has dopamine got us hooked on tech?, The Guardian (Mar. 4, 2018), https://www.theguardian.com/technology/2018/mar/04/has-dopamine-got-us-hooked-on-tech-facebook-apps-addiction.

51 Fiona M. Scott Morton & David C. Dinielli, Roadmap for an Antitrust Case Against Facebook (June 2020), at 4-5 ("Facebook Roadmap"). See also FTC Workshop, *supra* n. 4 , at 14 (remarks of Dr. Katharina Kopp: describing the objectives of dark patterns: (1) more "sales and revenue," (2) more user "engagement and attention, which may lead to harms of addiction," and (3) more "data use and collection.").

52 Tal Zarsky, Privacy and Manipulation in the Digital Age, 20 Theoretical Inquiries in Law 157, 186 (2019) (footnote omitted), https://din-online.info/pdf/th20-1-8.pdf.

Because data is so valuable, digital companies "are not incentivised to encourage consumers to opt out" of collection, use, or disclosure of their data; to the contrary, to avoid outward migration or product substitution, online companies seek "to convey an impression that they offer consumers significant control" over the data they're providing.[53] Moreover, companies are receptive to dark patterns "simply because a design that tricks users into doing something is likely to achieve more conversions [that is, user responses] than one that allows users to make an informed decision."[54] And on the user side, "[g]rowing reliance on digital tools in all parts of our lives — tools that constantly record, aggregate, and analyse information about us — means we are revealing more and more about our individual and shared vulnerabilities. . . . And the more we become habituated to these systems, the less attention we pay to them."[55]

Thus, dark patterns not only emerge, they also propagate to become "a regular part of the fabric of everyday experience."[56] They are particularly effective when used to nudge users to choose an offered default option. Users are disinclined to depart from a default they are offered or that they select (albeit through nudging).[57] This "default" or "status quo" bias is well-recognized: "individuals generally stick with the default choices they are presented with."[58] Dark patterns can themselves reinforce the bias. And this behavioral propensity means that nudging the user towards selecting the default offered entrenches the digital company's position.[59] By exploiting the user's default bias, "consumers make decisions they might not make with fuller consideration."[60]

VI. ZERO-PRICE EFFECTS

It is commonplace to hear talk of the many "free" services available on the internet. But, of course, nothing's "free." More accurately, many digital companies offer their products to users at a "zero-price" and thus must develop revenue from another source. In the digital space, online companies typically sell user access to advertisers and sometimes also deliver ads to content providers, referred to as "publishers," who offer "billboard" space on their website, from which a digital intermediary such as Google takes a cut of the payment to the publisher. This business model in turn requires the digital company to collect user data that can be analyzed to allow targeted advertising to be delivered to users, who pay for the zero-price product by providing their data. Further, as the user engages with an advertiser or publisher, the user's payment in data harvested increases. More user data permits more granular data analysis, leading to improved ad targeting. And improved ad targeting enables the company to charge more to its advertisers, as well as to publishers, for delivering ads. To enable ad dollars to flow at increasing rates, the digital company is incented to keep the user engaged on its website or on linked sites, thereby gathering as much data as it can.

Dark patterns can be used to maintain this user engagement and — equally important — to improve ad targeting that results in purchases users might not otherwise make.[61] Applying data analytics to large data sets, online businesses can "explore every nook and cranny of consumers' many behavioral shortcomings and biases in real time. Framing, nudges, and defaults can direct a consumer to the choice that is most profitable for the platform."[62]

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53 ACCC Report, *supra* n. 10, at 423 (§7.7.2).

54 Brignull, *supra* n. 6,. See also Brice Berdah, Dark patterns: submission by design?, UX Collective, Apr. 15, 2019, ("If you A/B test an honest, non-deceptive form versus a dark pattern filled one, the second one will certainly land more conversions."), https://uxdesign.cc/dark-patterns-submission-by-design-6f61b04e1c92.

55 Susser, *supra* n. 6.

56 *Id.*

57 See e.g. Jason Furman, Unlocking Digital Competition — Report of the Digital Competition Expert Panel 36 (Mar. 2019) (footnote omitted); ACCC Report, *supra* n. 10, at 431 (§7.7.5).

58 Competition & Markets Authority, Online Platforms and Digital Advertising: Market Study Final Report (July 1, 2020), at204 (¶ 4.205) ("CMA Final Report"); see also *id.* 13-15 (¶¶ 31-40) ("Consumer decision making and the power of defaults"). *See also* Stigler Center Report, *supra* n. 3, at 8 ("Consumers tend to stick with default options."); Furman, *supra* n. 57.

59 Stigler Center Report, *supra* n. 3, at 42. See also ACCC Report, *supra* n. 10, at 10 ("Consumer behaviour favours the use of incumbents, particularly those with strong brands. The operation of default settings further entrenches the market power of incumbents and increases the barriers to entering these markets."); CMA Final Report, *supra* n. 58, at 13-15 (¶¶ 31-40) ("Consumer decision making and the power of defaults").

60 *Id.* at 204 (¶ 4.205).

61 See generally Facebook Roadmap, *supra* n. 51, at 4-5 (discussing Facebook); Willis, *supra* n. 24, at 116, 121-23; Stigler Center Report, *supra* n. 3, at 11, 210-12, 246-48.

62 *Id.* at 30. See also FTC Workshop, supra n. 4, at (remarks of Ryan Calo: "the idea of persuasion profiling is . . . how do you find out what persuades a person, and then leverage that in real time"); Testimony of Gene Kimmelman Before the Senate Judiciary Committee, Subcommittee on Antitrust, Competition Policy and Consumer Rights 8 (Mar. 10, 2020) ("Powerful incumbent platforms may also make design choices to exacerbate this inclination [the default bias nudging people to stay put].") (footnote omitted) , https://www.judiciary.senate.gov/imo/media/doc/Kimmelman%20Testimony.pdf.

Offering online products at zero-price has another significant effect. It disables price as a signal for perceived product attractiveness: "[w]hen facing a zero-money price, and when quality is difficult to observe, consumers are not receiving salient signals about the social value of their consumption because the price they believe they face [that is, "zero"] does not reflect the economics of the transaction, and they are ignorant of those numbers."[63] Simply put, "there is no analogue to a 'price tag' for attention (or information) costs."[64] Moreover, while the company harvesting the user's data knows it's receiving something valuable, how valuable isn't all that clear because analytics need to be applied to add value and because harvested data may be used in ways not even apparent when collected.[65]

Digital companies are, therefore, incented to collect ever-increasing amounts of data. Dark patterns help achieve, maintain, and augment the user engagement that enables data collection.

VII. THE CURRENT LEGAL ENVIRONMENT

Deception is the core feature of dark patterns. Therefore, dark patterns should be actionable under federal and state law barring false, deceptive, or unfair practices.[66] A handful of FTC cases have addressed dark pattern techniques, albeit not using this terminology itself.[67] Ironically, however, "the proliferation and sheer variety of dark patterns on its own makes it more difficult for government enforcers to effectively identify the most severe offenders and to address these offenders through targeted enforcement actions."[68] Accordingly, there is a role for private enforcement, and many private cases that explicitly plead deceptive "dark patterns" are pending. All are in their early stages so that the court has not ruled on the claim's legal sufficiency.[69] Deception theory aside, contract law concepts could also be applied to void user agreements elicited using dark patterns.[70]

In addition, dark patterns have captured the attention of federal and state legislators. Perhaps not surprisingly, California is in the forefront. The California Consumer Privacy Act[71] provides that "dark pattern" means "a user interface designed or manipulated with the substantial effect of subverting or impairing user autonomy, decision-making, or choice, as further defined by regulation."[72] The law further provides that authorization on data use "obtained through use of dark patterns does not constitute consent."[73] Regulations issued under the law give Californians the right to opt-out of sale of their personal information by online companies that collect it, and include, as part of the new rules, provisions banning dark patterns that otherwise could impair exercise of the opt-out right. As the new regulations took effect, then-Attorney General Xavier Becerra

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63 Stigler Center Report, *supra* n. 3, at 67. See also CMA Final Report, *supra* n. 58, at 13 (¶ 32) ("default behaviour by consumers has had a profound impact on the shape of competition in both search and social media.") (emphasis deleted).

64 John Newman, Antitrust in Zero-Price Markets: Foundations, 164 U. Penn. L. Rev. 149, 179 (2015).

65 Katharine Kemp, Concealed data practices and competition law: why privacy matters, 16 Euro. Comp. J. 628, 642-43 (2020).

66 See e.g. Section 5 of the FTC Act, 15 U.S.C. § 45(a), which declares unlawful "unfair or deceptive acts or practices in or affecting commerce." The elements of deception are "[1] a representation, omission, or practice, that [2] is likely to mislead consumers acting reasonably under the circumstances, and [3], the representation, omission, or practice is material." *FTC v. LeadClick Media, LLC*, 838 F. 3d 158, 168 (2d Cir. 2016) (cleaned up). See also Luguri, *supra* n. 10, at 83-91.

67 *Federal Trade Commission v. LeadClick Media, LLC*, 838 F. 3d 15 (2d Cir. 2016) (finding deception where company created bogus customer reviews that it posted on fake online news sites); *Federal Trade Commission v. AMG Capital Management*, 910 F.3d 417 (9th Cir. 2018) (finding deception where company made rejecting automatic renewal onerous), *rev'd on other grounds*, ___U.S. ___, No. 19-508 (Apr. 22, 2021); *Fanning v. Federal Trade Commission*, 821 F. 3d 164 (1st Cir. 2016) (finding deception where the vast majority of online user profiles were generated by defendant, not by actual users). See also Complaint, *FTC v. FrostWire LLC*, No. 11-cv-23643-DLG (S.D. Fla. Oct. 12, 2021) (file-sharing set-up procedure, settings and interface were deceptive); Complaint, *Federal Trade Commission v. Age of Learning, Inc.*, 20-cv-07996 (C.D. Cal. Sept. 1, 2020) (membership interface, automatic renewal term, and cancellation process were deceptive); Complaint, *United States v. Facebook Inc.*, 19-cv-02184 (D.D.C. July 24, 2019) (action to enforce FTC consent decree based, in part, on deceptive collection of user data).

68 FTC Workshop, *supra* n. 4, at 72 (remarks of Jennifer Rimm). See also *id.* at 74 (remarks of Lauren E. Willis: proliferation of online marketing techniques, microtargeting, and automation of website display all can be a barrier to effective enforcement actions).

69 See e.g. Third Amended Complaint ¶¶ 44-45, *Nichols v. Noom Inc.*, Docket No. 1:20-cv-03677 (S.D.N.Y. Jan. 29, 2021), ECF 174 ("Noom's business model is predicated upon the 'Hidden Subscription Dark Pattern,' which "Noom augments . . . with numerous other Dark Pattern design techniques," including mental fatigue, trick wording, and roach motel.); Complaint at ¶ 21, *Mendez v. LinkedIn Corp.,* Docket No. 21CV378575 (Cal. Super. Ct. Mar 24, 2021) (LinkedIn uses "various types of dark patterns, including but not limited to 'interface interference' and 'preselection,' 'roach motel, 'misdirection,' and 'forced continuity' in order to prevent user unsubscription").

70 Luguri, *supra* n. 10, at 47-48, 92-97.

71 Cal. Civ. Code §§ 1798.100 to 1798.199 (CCPA).

72 *Id.* §1798.140(l).

73 *Id.* §1798.140(h).

said: “These protections ensure that consumers will not be confused or misled when seeking to exercise their data privacy rights.”[74] Proposed legislation in Washington State is virtually identical.[75]

Federal legislation may also be in the offing. During the last congressional term, Senators Warner and Fischer introduced the bipartisan Deceptive Experiences to Online Users Reduction (DETOUR) Act.[76] The Act sought to prohibit websites from using dark patterns that trick consumers into handing over their personal data. Among other things, the DETOUR Act would make it unlawful “to design, modify, or manipulate a user interface with the purpose or substantial effect of obscuring, subverting, or impairing user autonomy, decision-making, or choice to obtain consent or user data.”[77] The Act would also enable creation of a self-regulatory, professional standards body to “develop, on a continuing basis, guidance and bright-line rules” for platforms on dark patterns design practices,[78] and further would cement the FTC to act as a regulatory enforcer.[79] The bill died upon conclusion of the 116th Congress, However, the bill’s sponsors plan to reintroduce the DETOUR Act in the 117th Congress.”[80]

Antitrust enforcement is yet another means to rein in dark patterns.

74 Press Release, Attorney General Becerra Announces Approval of Additional Regulations That Empower Data Privacy Under the California Consumer Privacy Act (Mar. 15, 2021), https://oag.ca.gov/news/press-releases/attorney-general-becerra-announces-approval-additional-regulations-empower-data. See California Privacy Act Regulation §999.315(h).

75 Wash. S.5062-S2, §101 (6) & (10).

76 The Deceptive Experiences to Online Users Reduction Act (DETOUR), S.1084, 116th Cong., 1st Sess. §3(a)(1)(A) (Apr. 9, 2019). See also H.R.8975, 116th Cong., 2nd Sess. (Dec. 16, 2020).

77 *Id.* at §3(a)(1)(A).

78 *Id.* at §3(c)

79 *Id.* at §3(d)

80 FTC Workshop, *supra* n. 4, at 4 (remarks of Rep. Lisa Blunt Rochester). See also Sara Morrison, Dark patterns, the tricks websites use to make you say yes, explained, Vox (Apr. 1, 2021), https://www.vox.com/recode/22351108/dark-patterns-ui-web-design-privacy.

VIII. ANTITRUST ENFORCEMENT DIRECTED TO DARK PATTERNS

Dark patterns make the worst out of an already bad situation. "Dark patterns cause consumers to pay a higher data price than they would freely choose."[81] Essentially, users are tricked into overpaying with their data and attention. Further, dark patterns typically create other transaction costs, such as increased user on-site time or attention. Thus, they produce market waste and distortion.[82] By the same token, users pay a quality-adjusted price that is higher than it would be if they weren't deceived. A company's ability to over-charge users in this manner, without causing them to switch to substitutes, reflects company market power and reduces consumer surplus.[83]

In the U.S., if the company has a large enough market share, dark pattern use may constitute unlawful acquisition or maintenance of monopoly power. The anti-competitive conduct consists of secretly shaping, and thus exploiting, consumer choice — the very antithesis of competing on the basis of product merit.[84] In the EU and other jurisdictions, the company's conduct may constitute abuse of dominance or unlawful exploitive conduct.[85] For a Sherman Act §1 claim, the restraint must result from agreement by two or more participants, but conceivably the user itself could satisfy this plurality requirement, particularly when the website designer requires user adherence to terms of service or elicits a product purchase by the user.[86]

Moreover, actual and potential rivals face enhanced barriers to entry, caused by the first-mover's ability to exploit its user base. Where a digital company employs dark patterns to assure user attention and data-delivery, the result is better ad targeting, for which advertisers and content providers will pay the digital company more. Rivals will have to offer advertisers and content providers better terms than they would have to offer if dark patterns were not used to skew user choice and engagement. The first mover's position is reinforced not only by these network effects (often reflected in both economies of scale and scope), but also by the zero-price feature of many online products. When a product is offered at zero-price, to compete a rival must offer a demonstrably more attractive product — one providing identifiably better quality or more desirable product features.[87] Moreover, when, using dark patterns, a tech company captures user attention and increases their engagement with the company's site or on links offered to the user, the ability of rivals to contest the company's offerings is restrained.[88] More attention capture by one company means less opportunity to capture for rivals. Overcoming the asymmetry requires extra effort by the rival.

So, rivals seeking to counter the effects of a competitor's dark patterns on users will incur increased costs to compete. Through means other than competition on the merits of its product, the company raises its rivals' costs to persuade users to switch — anticompetitive conduct under Section 2.[89]

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81 Facebook Roadmap, *supra* n. 51, at 31; Calo, *supra* n. 5, at 1029-30.

82 Stigler Center Report, *supra* n. 3, at 239.

83 Kemp, supra n. 65, at 656-57; Note, Deception as an Antitrust Violation, 125 Harv. L. Rev. 1235, 1239 (2012).

84 *Cf.* Woodcock, *supra* n. 44, at 2332 (footnote omitted) (false and misleading advertising is denied First Amendment coverage in order "to protect the decision-making processes of consumers . . . by ensuring that consumers can accurately distinguish the attributes of different products and . . . can put their true preferences to work in selecting between those products.") & 2335 (manipulative advertising may be banned because it "interfer[es] with the decision-making process used by consumers to translate preferences into choices").

85 Kemp, *supra* n. 65, at 656-58.

86 See *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 n.9 (1984) (to establish an agreement between a supplier and a customer, "evidence must be presented both that the [customer] communicated its acquiescence or agreement, and that this was sought by the [supplier]"). *Cf. Spectators' Commc'n Network Inc. v. Colonial Country Club*, 253 F.3d 215, 222 (5th Cir. 2001) ("[T]here can be sufficient evidence of a combination or conspiracy when one conspirator . . . is enticed or coerced into knowingly curtailing competition by another conspirator who has an anticompetitive motive."); *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 463 n.8 (1992) (a sale offered only upon a condition is not unilateral conduct outside the scope of Section 1); *Isaksen v. Vermont Castings, Inc.*, 825 F.2d 1158 (7th Cir. 1987) ("The fact that [the plaintiff] may have been coerced into agreeing is of no moment"), *cert. denied*, 486 U.S. 1005 (1988); *Systemcare, Inc. v. Wang Laboratories Corp.*, 117 F.3d 1137, 1138, 1142–43 (10th Cir. 1997) (Section 1 is satisfied where "the seller coerces a buyer's acquiescence" in the transaction; "[t]he essence of section 1's contract, combination, or conspiracy requirement . . . is the agreement, however reluctant, of a buyer to purchase from a seller").

87 See CMA Final Report, *supra* n. 58, at §3.130, Box 2.2 ("The fact that consumers do not pay directly for the platform's services limits their incentives to switch, and means that new entrants must attract users through demonstrably better quality or innovative features, rather than being able to undercut on price.").

88 Colangelo, *supra* n. 22, at 64-65.

89 See e.g. Note, Deception as an Antitrust Violation, 125 Harv. L. Rev. 1235, 1238-39 (2012) (deception both raises rivals' costs directly and deprives them of economies of scale and thus creates inefficiency); Woodcock, *supra* n. 44, at 2313-15 (persuasive advertising can "lure consumers away from [rivals'] innovative products.") (footnote omitted). *Cf.* Facebook Roadmap, *supra* n. 51, at 29 (By offering users obscure privacy settings, Facebook "suppresses competition in quality.").

IX. PERSUASION V. COERCION VIA DARK PATTERNS

Persuasion "means attempting to influence someone by offering reasons they can think about and evaluate."[90] A product supplier may be expected to try to persuade potential customers to use its product. This is, after all, what advertising is supposed to be about. By contrast, "[c]oercion means influencing someone by constraining their options, such that their only rational course of action is the one the coercer intends. . . . [P]ersuading someone to do something is almost always acceptable, while coercing them almost always isn't."[91]

Commercial speech, such as product advertising, is protected by the First Amendment.[92] Accordingly, case law ends to skepticism of antitrust claims arising from representations about products, even when false or misleading. Although such commercial speech lacks redeeming pro-competitive benefits, marketplace counter-speech by rivals, rather than antitrust litigation, is said to be a preferable remedy.[93] This "marketplace of ideas" argument, however, posits that "[t]ruth is expected to outperform lies so long as people *are equipped* to choose it."[94] But this central assumption dissolves when applied to dark patterns — techniques designed and intended surreptitiously to over-ride rational individual decision-making. In these circumstances, dark patterns really amount to *hidden* coercion. And coercion is conduct courts recognize as relevant to establishing unlawful exclusionary conduct by a firm with monopoly, or to proving an unlawful restraint in a rule of reason case based on the totality of the facts.

New York ex rel. Schneiderman v. Actavis plc[95] is illustrative. Actavis, a drug manufacturer, sought to avoid generic competition for sales of its Namenda drug. As the patent for Namenda IR approached expiration, Actavis withdrew the drug from the market and replaced it with a near identical substitute called Namenda XR. Under federal and state pharmaceutical regulatory regimes, Actavis' conduct prevented substitution of a generic version of the drug, and thus required patients to switch from Namenda IR to Namenda ER. The Second Circuit held that Actavis' conduct violated Section 2:

> Defendants' hard switch crosses the line from persuasion to coercion and is anticompetitive. . . . Had Defendants allowed Namenda IR to remain available until generic entry, doctors and Alzheimer's patients could have decided whether the benefits of switching to once-daily Namenda XR would outweigh the benefits of adhering to twice-daily therapy using less-expensive generic IR (or perhaps lower-priced Namenda IR). By removing Namenda IR from the market prior to generic IR entry, Defendants sought to deprive consumers of that choice.[96]

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90 Susser, *supra* n. 6, at 4.

91 *Id.*

92 E.g. *Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council, Inc.*, 425 U.S. at 765 (1976).

93 See e.g. *Schachar v. Am. Acad. of Ophthalmology, Inc.*, 870 F.2d 397, 400 (7th Cir. 1989); *Retractable Tech., Inc. v. Becton Dickinson & Co.*, 842 F.3d 883, 893-97 (5th Cir. 2016) (discussing authorities); 3B Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law: An Analysis of Antitrust Principles and Their Application, ¶ 782b, at 326 (3d ed. 2008) ("There is no redeeming virtue in deception . . . ."). For a contrary view and case law, see Maurice E. Stucke, When a Monopolist Deceives, 76 Antitrust L.J. 823 (2010); *West Penn Allegheny Health System, Inc. v. UPMC*, 627 F.3d 85, 109 & n.14 (3d Cir. 2010) (citing authorities); *Nat. Ass'n of Pharmaceutical Mfrs. v. Ayerst Lab.*, 850 F.2d 904, 916-17 (2d Cir. 1988).

94 Ellen P. Goodman, Digital Information Fidelity and Friction, Knight First Amendment Institute (Feb. 26, 2020) (emphasis added), https://knightcolumbia.org/content/digital-fidelity-and-friction. See also Kozyreva, *supra* n. 12, at 127 ("Human-made, ubiquitous, persuasive, and manipulative designs, which rely on dark patterns and hidden defaults, challenge the human capacity to exercise autonomous and informed choice."); Colangelo, *supra* n. 22, at 65.

95 787 F.3d 638 (2d Cir. 2015). But see Luguri, *supra* n. 10, at 99-101 (suggesting that First Amendment protection may exist for some forms of dark patterns, such a nagging).

96 787 F.3d at 654-55.

Other cases are similar: conduct going beyond persuasion and into coercion can be unlawfully exclusionary.[97] When that coercion is itself covert, it amounts to manipulation and, indeed, where it plants false impressions, to affirmative deception — conduct that is even more pernicious: "we are directed, outside our conscious awareness, to act for reasons we can't recognise, and toward ends we may wish to avoid."[98] Antitrust law should not hesitate to intervene.[99]

The EC's *Google Shopping* case is also instructive. There, Google essentially used a dark pattern in the form of algorithmic bias against competitors.[100] Google's algorithmic bias favored its own comparison shopping sites, while disadvantaging rivals' sites. The company's conduct was "likely to lead to: an increase in the fees payable by retailers using Google Shopping; a consequential increase in the prices to be paid by their customers; a reduction in innovation incentives from both Google Shopping's competing comparison sites and Google Shopping itself; and a reduction of the ability of consumers to access the most relevant comparison shopping services."[101] Thus, Google corrupted the operations of the market by an algorithmic mechanism that favored display of its own sites while degrading placement of rival sites. Both rivals, online retailers, and customers were harmed.

In a similar vein, both U.S. and EU law recognize as anticompetitive collective, undisclosed manipulation of a benchmark used in marketplace pricing. Thus, in *Gelboim v. Bank of America Corp.*,[102] various banks allegedly suppressed the London Inter-Bank Offered Rate (LIBOR) by secretly submitting depressed borrowing rates that violated rate-setting rules. The plaintiffs, holders of various financial instruments affected by the LIBOR rate, "allege[d] that the Banks corrupted the LIBOR-setting process and exerted downward pressure on LIBOR to increase profits in individual financial transactions and to project financial health."[103] The Second Circuit held that the plaintiffs "plausibly alleged both antitrust violation and antitrust injury. . . ."[104] The EC similarly found an antitrust violation involving analogous corruption of the Euro Bond Inter-Bank Offered Rate.[105]

The very point of a benchmark price is to provide a reliable price signal for market participants. If participants knew the price signal lacked reliability, they would cease using the benchmark. So too, if online users knew that dark patterns were corrupting the settings they selected, the features delivered to them, or attractiveness of product displayed to them, they would lose confidence in the benefits of online surfing and purchase offerings.[106]

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97 See e.g. *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 287 (2d Cir. 1979) ("so long as [a monopolist's] success was not based on any form of coercion," product design changes are not actionable under section 2); *Mercatus Group, LLC v. Lake Forest Hosp.*, 641 F. 3d 834, 852 (7th Cir. 2011) ("absent an accompanying coercive enforcement mechanism of some kind, even demonstrably false commercial speech is not actionable under the antitrust laws") (cleaned up); *In re Suboxone*, 64 F. Supp. 3d 665, 682 (E.D. Penn. 2014) ("threatened removal" of drug in tablet form "from the market in conjunction with the alleged fabricated safety concerns could plausibly coerce patients and doctors to switch"); *In re Loestrin 24 Fe Antitrust Litig.*,13-md-02472-WES-PAS, slip op. at 97-98 (D.R.I. Aug. 8, 2018) (discussing authorities); *In re Asacol Antitrust Litig.*, No. 15-cv-12730-DJC (D. Mass. July 20, 2016).

98 Susser, *supra* n. 6, at 4.

99 *Cf.* Main, *supra* n. 43, at 629-30 ("the potential for neuromarketing to be overly persuasive, to the point of being coercive or misleading, is significant enough to justify a state's interest in regulating it in order to protect its citizens.").

100 Commission Decision 2017/4444/EC, Relating to proceedings under Article 102 of the Treaty on the Functioning of the European Union and Article 54 of the Agreement on the European Economic Area (AT.39740 - Google Search (Shopping)) (June 27, 2017).

101 Colangelo, *supra* n. 22, at 77-78 (citing Google Shopping Decision ¶¶ 589-96).

102 823 F.3d 759 (2d Cir. 2016).

103 *Id.* at 766.

104 *Id.* at 783.

105 Commission Decision, 2013/8512/EC, Relating to proceeding under Article 101 of the Treaty on the Functioning of the European Union and Article 53 of the EEA Agreement (AT.39914 - Euro Interest Rate Derivatives (EIRD) (Settlement)) (Dec. 4, 2013).

106 See generally Colangelo, *supra* n. 22, at 85-86 (in Google Shopping and LIBOR, marketplace actors relied on the integrity of the process that produced the search results and the benchmark without having the ability to determine its corruption).

Accordingly, whether viewed as coercion of users or corruption of marketplace operations, dark patterns are antithetical to competition on the merits. Market integrity presupposes rational decision-making by informed economic actors — rivals, suppliers, and customers. By surreptitiously manipulating actor decision-making processes, dark patterns undermine market integrity.[107]

These anticompetitive consequences are sufficiently clear that *per se* treatment should apply.[108] Secretly disabling informed and rational user or consumer choice has no redeeming social or economic value.[109] That is the underpinning of not only the denial of First Amendment protection to false or misleading advertising, but also the FCC's position on subliminal advertising. Nothing positive weighs in the balance.[110] To the contrary, failing to recognize the irredeemable quality of dark patterns itself encourages their continued use and expansion to manipulate and exploit online users. Creativity in developing dark patterns, however, is not "innovation" that should be incented.

While these cases do not involve dark patterns, they are instructive nonetheless because they provide an antitrust framework available to plead a claim. One recently filed lawsuit, however, alleges specifically that the defendant, Facebook, used dark patterns for anticompetitive purposes. In *Sherman v. Facebook, Inc.*, the plaintiffs contend that Facebook wrongfully acquired or maintained monopoly power in violation of the Sherman Act, in part, "by deploying dark patterns, skullduggery, and other misleading and fraudulent behavior" in its data collection efforts."[111] According to the plaintiffs, "[d]ark patterns cause consumers to pay a higher data price than they would freely choose. Framing and communication of privacy settings in a way that takes advantage of consumers' behavioral limitations causes them to give away more data and privacy than they otherwise would and represents a lower quality of the service."[112] The court has not yet ruled on the Sherman plaintiffs' claim, however.

X. CONCLUSION

Dark patterns aren't going away. They're getting worse. "[D]esign has been weaponized using behavioral research to serve the aims of the surveillance economy."[113] And as the "internet of things" continues to develop, the opportunities to abuse users and rivals will expand exponentially. Action needs to be taken before dark patterns move from computers, tablets, and mobile phones to heating systems, refrigerators, and all manner of consumer goods.[114]

Seeds of optimism are being planted, however. As the FTC's recent agency workshop and passage of the California Consumer Privacy Act demonstrate, there is now growing interest in fighting back against use of dark patterns. Enforcers, businesses, and consumers should challenge, dark patterns under the antitrust laws, which are well-equipped to tackle this activity. Potential treble damages antitrust liability and attorneys fee recoveries can deter a firm's continuing to resort to dark patterns to exploit users and hinder rivals.

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107 See *id.* at 65 ("[T]he idea that consumers select the best firms in the market on the basis of merit does not hold true when consumer opinions are manipulated by false or unduly persuasive information."); Guy Rolnik & Asher Schechter, How Can Antitrust Be Used to Protect Competition in the Digital Marketplace?, Promarket (Sept. 26, 2016) (interview of Ariel Ezrachi: "In the online world, the buyer's rational decision-making is often undermined by a controlled ecosystem in which transparency and choice can be distorted. Perhaps most striking, the targets of these practices — the buyers — are often unaware of the extent of the manipulation."), https://promarket.org/2016/09/26/digital-market-not-going-correct/; Woodcock, *supra* no. 44, at 2276 (footnote omitted) ("Tinkering with the decision-making processes of consumers prevents consumers from rewarding, through their purchase decisions, the innovators who best meet their needs, and thereby threatens the foundation of technological progress in a free market system.") (footnote omitted).

108 Main, *supra* n. 43, at 628-29 ("prohibiting coercive neuromarketing is essential to preserving a fair bargaining process, and therefore, the government could prohibit neuromarketing entirely").

109 See Stigler Center Report, *supra* n. 3, at 238 ("While dark patterns come in a variety of different forms, their central unifying feature is that they are manipulative, rather than persuasive. More specifically, the design choices inherent in dark patterns push users towards specific actions without valid appeals to emotion or reason.").

110 See Main, *supra* n. 43, at 627 ("The same rationale for denying protection to false or misleading speech in advertising also applies to unfairly effective neuromarketing, meaning that the government could constitutionally regulate the use of neuromarketing"). *Cf.* Woodcock, *supra* n. 44, at 2321 (footnote omitted) (persuasive advertising — that which manipulates consumer choice — as opposed to informative or complementary advertising (the former of which provides useful information and the latter of which enhances consumer enjoyment in product use) — should be unlawful *per se* under antitrust principles because, "like price fixing," persuasive advertising is "harmful to consumers in all cases," causing consumers "to pay more for the advertised product for reasons that . . . involve no gain in consumer welfare.").

111 Complaint at ¶79, *Sherman v. Facebook, Inc.*, Docket No. 5:20-cv-08721 (N.D. Cal. Dec 09, 2020).

112 *Id.* at ¶93.

113 Narayanan, *supra* n. 28, at 79.

114 See European Commission, Commission Staff Working Document Preliminary Report - Sector Inquiry into Consumer Internet of Things, SWD(2021) 144 final, ¶ 1.2(3), at 15 (June 9, 2021) ("It is expected that there will be more than 8 billion consumer internet and media devices worldwide by 2030, making this area by far the most common use case of the IoT as a whole") (footnote omitted).

FAILURE TO FILE REPORTABLE MERGERS – UPDATE FROM CHINA

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Like many other jurisdictions, China has a system of compulsory pre-closing merger control. Like other jurisdictions, the Chinese antitrust authority – the State Administration for Market Regulation ("SAMR") – investigates and punishes companies for failing to file reportable transactions.

Quite unique to China, in contrast, is that companies are queuing up before SAMR to get fined. Why?

This paper will take a deep look at China's failure-to-file decisions and reply to this and other questions.

I. INTRODUCTION

Chinese antitrust enforcement under the Anti-Monopoly Law ("AML") has visibly gained pace since the end of 2020. Some would even say Chinese antitrust has entered into a "new area."[2] A key reason for the increased antitrust enforcement was the high-level backing which top leaders voiced for antitrust enforcement. For example, on December 11, 2020, President Xi Jinping presided over a top-level meeting that indicated that the strengthening of anti-monopoly efforts is one of the key tasks for China in 2021.[3]

Not long after that, SAMR issued its decision against Alibaba for abuse of dominance – "from-two-choose-one," a form of exclusive dealing – with a record fine of over RMB 18 billion (around USD 2.9 billion).[4]

In the area of failure to file reportable transactions, too, enforcement levels increased dramatically. Since December 2020, 51 failure-to-file punishment decisions were adopted, of a total of 110 such decisions since 2014.[5] In other words, in the half-year since December 2020 around half of all such decisions were issued – while the other half of decisions were adopted over a period of six years before December 2020.

The statistics of failure-to-file decisions reveal other interesting points. For example, 63 of the 71 companies fined for failure to file since December 2020 were from the Internet sector or related industries. Equally interesting, SAMR and its predecessor did not impose the maximum possible fine in any case prior to December 2020, but did so in over 80 percent of cases (45 of 51 cases) since then.[6]

In this paper, we will first set out the law applicable to failure-to-file cases (section 2) and explain the procedure for investigating such cases (section 3). Then, in section 4, we will explain the content of the actual failure-to-file decisions. Section 5 concludes.

2 Sun Weiwei, *How to anti-monopolize in 2021: The Internet industry is the focus of law enforcement and the revision of the law may be completed*, January 7, 2021, https://www.yicai.com/news/100905831.html.

3 Xinhua Net, *The Meeting of the Political Bureau of the CPC Central Committee was held and presided by President Xi*, December 11, 2020, http://www.xinhuanet.com/politics/leaders/2020-12/11/c_1126850644.htm. Also see Xinhua Net, *The Central Economic Work Conference was held in Beijing with Xi Jinping and Li Keqiang delivering an important speech*, December 18, 2020, http://www.xinhuanet.com/politics/leaders/2020-12/18/c_1126879325.htm.

4 *Alibaba*, [2021] SAMR Notice No. 28, April 10, 2021.

5 From December 2014 to December 2020. Failure to file was not a priority at the beginning of China's modern antitrust era. SAMR's predecessor, the Ministry of Commerce, adopted the first failure-to-file decision in December 2014, over six years after the AML came into effect.

6 Since December 2020, the maximum fine was imposed in all of the Internet-related failure-to-file decisions (45 cases) and in one of six decisions against non-Internet companies.

II. LEGAL FRAMEWORK

The Chinese merger control regime is quite straight-forward. A filing with SAMR is required if (1) a transaction amounts to a "concentration between business operators" and (2) the relevant thresholds are met. The parties to a transaction are under a standstill obligation – the transaction cannot be closed before SAMR has issued clearance.[7]

The term "concentration between business operators" is explained in the AML: either a "merger" in the strict sense or an acquisition of a "controlling right" in one business operator by another (through acquisition of equity or assets, by contract or other means).[8]

In turn, the thresholds are not laid out in the AML but are set in a separate regulation adopted by the State Council. The thresholds are exclusively based on sales revenues.[9] Somewhat reformulated, the thresholds are:

1. the combined revenue of all parties to the concentration in the last financial year was above RMB 10 billion (around USD 1.6 billion) globally or RMB 2 billion (around USD 310 million) in China; and

2. the individual revenue of each party to the concentration in the last financial year was above RMB 400 million (around USD 62 million) in China.

In the case of failure to file a reportable transaction, the AML provides that SAMR

> "shall order the business operators to cease the implementation of the concentration, shall order the divestment of the shares or assets or the transfer of business operations within a given time limit, and shall take other measures necessary to restore the conditions prevailing before the concentration, and may impose fines of up to RMB 500,000."[10]

III. PROCEDURE FOR FAILURE-TO-FILE INVESTIGATIONS

A SAMR regulation, the Interim Regulation on the Review of Concentrations between Business Operators ("Review Regulation"), implements the procedure for a failure-to-file investigation (among other things) in more detail.[11]

In this section, we will first look at the Review Regulation's guidance on the failure-to-file investigation before SAMR. Then, we will examine an additional procedural point for listed companies (or companies about to list): disclosure obligations.

A. SAMR's Failure-to-file Investigation Procedure

The Review Regulation was released by SAMR and came into effect on December 1, 2020. It consolidated a number of prior rules and guidelines formulated by SAMR's predecessor responsible for merger control, the Ministry of Commerce ("MOFCOM").

The Review Regulation streamlined the procedure and timeline for SAMR's investigation into failure-to-file cases. SAMR expected the Review Regulation to "further improve the efficiency of case investigation, increase the predictability undertakings dealing transaction, and better serve the high-quality economic growth."[12]

One notable change by the Review Regulation (as compared to prior rules) is that SAMR conducts a shorter investigation: maximum 210 days (instead of 300 days under the prior rules). According to the new rules, SAMR's investigation now follows a "30+30+30+120 days" period, down from the "30+60+30+180 days" timeline under the prior rules.

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7 AML, art. 21.

8 AML, art. 20. Apart from a "controlling right," this provision also talks about the acquisition of the "ability to exercise decisive influence over another business operator." However, in the AML implementing rules and in SAMR practice, this concept is not given a separate meaning but instead subsumed in the concept of "controlling right."

9 State Council Regulation on the Notification Thresholds for Concentrations Between Business Operators, [2008] State Council Order No. 529, August 3, 2008.

10 AML, art. 48.

11 Interim Regulation on the Review of Concentrations between Business Operators, [2020] SAMR Order Nr. 30, October 23, 2020.

12 SAMR, *SAMR answers questions from the press regarding the release of the Interim Regulation on the Review of Concentrations between Business Operators*, October 27, 2020, http://gkml.samr.gov.cn/nsjg/xwxcs/202010/t20201027_322668.html.

If we look at past cases, we can see that most of the failure-to-file investigations (close to 90 percent) were completed within the 300-days period, and the majority of investigations (nearly 85 percent) since December 2020 lasted shorter than 210 days. Annex 1 to this paper contains a list of all failure-to-file decisions under the AML until today, including an indication of the timeline of the investigations.

Normally, SAMR initiates failure-to-file investigations on its own motion, after receipt of third-party complaints or (most frequently) following a self-report of parties having failed to file reportable transactions.

The procedure and timeline are generally as follows:

- Examination and verification. SAMR examines and verifies a complaint or self-report of suspected failure to file and decides whether or not to initiate a case (*i.e.*, accept the case on file and initiate a formal investigation).

- Preliminary investigation. After SAMR has initiated the investigation and issued a formal case acceptance notice, the parties under investigation have 30 days to submit information and documents to SAMR for the purpose of assessing whether the transaction was notifiable and has been implemented.

- Once the information/documents have been submitted, SAMR must decide on whether or not there was a violation of the filing obligation within 30 days. If so, SAMR must start a "further investigation" into the substance of the case and notify the parties accordingly.

- Further investigation. For this procedural phase, SAMR requires the parties to submit relevant merger filing documents within 30 days of receipt of the written notice.

SAMR then has 120 days to conduct its substantive review to determine whether the transaction has or may have anti-competitive effects.

B. Stock Exchange Information Disclosure Requirements

A listed company involved in a failure-to-file procedure will need to consider its information disclosure requirements under stock exchange rules. A similar issue exists for companies which are planning an initial public offering ("IPO").

We will briefly consider the rules of the two key stock exchanges in Mainland China – the Shanghai Stock Exchange ("SSE") and the Shenzhen Stock Exchange ("SZSE") – as well as the Hong Kong Stock Exchange.

The SSE and SZSE listing rules require listed companies to report material risks in a timely manner. A government investigation resulting in a decision finding a violation of law *and imposition of significant administrative or criminal penalties* would clearly qualify as a material risk.

Although the rules (e.g. the Rules Governing the Listing of Stocks on the Shanghai Stock Exchange) have not further defined "significant administrative penalties," they do provide some guidance by stating that where the matter involves a specific monetary amount, the provisions on transaction disclosure standards shall be applied.[13] One of the disclosure obligation-triggering standards involves "net profit related to the subject matter of the transaction for the most recent financial year accounts for more than 10 percent of the listed company's audited net profit for the same period, with the absolute amount of the net profit exceeding RMB 1 million."[14]

This means that the triggering amount for mandatory disclosure of a failure-to-file decision – or investigation – is typically RMB 1 million (or 10 percent of the company's audited net profit). Given the current cap of RMB 500,000 for failure-to-file fines under the AML, the imposition of a fine alone generally does not constitute a material risk requiring disclosure under current listing rules in Mainland China.

13 Rules Governing the Listing of Stocks on the Shanghai Stock Exchange, [2020] Shangzhengfa No. 100, December 31,2020.

14 *Id*. art. 9(2).

Not surprisingly, among the domestic listed companies fined for failure to file from 2019 to July 2021, only five disclosed the relevant penalties or decision to investigation in filings to the stock exchange. Three of these companies disclosed the penalty or investigation decisions immediately upon receiving them, by making standalone announcements to the stock exchange.[15] These announcements were made before SAMR published the failure-to-file decisions on its website.[16]

The other two companies disclosed the SAMR decisions in their IPO prospectus, restructuring progress announcement and other documents.[17] The subject of disclosure may be the punished entity and its parent company, or the target.

In Hong Kong, the Securities and Futures Ordinance has similar requirements for listed companies to disclose information not generally known to the public which is likely to have a material effect on the price of securities.[18] However, unlike the Mainland Chinese rules, the Hong Kong Stock Exchange rules do not explicitly mention an information disclosure obligation when a company has been imposed or faces significant administrative penalties. As the amount of a failure-to-file fine usually accounts for a (very) small proportion of companies' annual revenues and is not "likely to have a material effect on the share price," very few listed companies have chosen to disclose being subject to a failure-to-file investigation by SAMR or its predecessor under the Hong Kong rules.

In practice, if we look at the Hong Kong-listed companies fined for failure to file from 2019 to April 2021, we have only found one company which disclosed the information in its IPO prospectus in 2021: Baidu was fined RMB 500,000 for failing to notify its acquisition of Ainemo in 2020.[19]

IV. FAILURE-TO-FILE DECISIONS

All of the 110 failure-to-file decisions published by SAMR and its predecessor are very short. At most, they are four A4 pages long (in original). Most of them are quite "boring" in the sense that they do not discuss interesting details of the transactions or the procedure, or clarify the AML or implementing rules.

In particular, the absence of any meaningful discussion on (1) the key concept for a failure-to-file case – the acquisition of a "controlling right" – and (2) the substantive competition assessment is disappointing to the reader. In contrast, the text of a few decisions allows some (albeit limited) takeaways on the risks for multi-step transactions.

A. Controlling Right

As noted above, the acquisition of a "controlling right" is a prerequisite for any transaction to be deemed a "concentration between business operators" and therefore be notifiable under the AML (if the thresholds are met). Given the importance of the concept, one would expect in-depth discussions in the failure-to-file decision of whether a specific transaction gives rise to an acquisition of a controlling right.

Unfortunately, this is not the case. In none of the 110 failure-to-file decisions there is any meaningful discussion of whether a controlling right is acquired. The decisions only formulate the conclusion: the transaction leads to an acquisition of a controlling right, without any reasoning.

This is a missed opportunity – even more so, because the AML and its implementing rules provide very limited guidance on what the concept of a controlling right means. Article 3 of the Review Regulation sheds some light on controlling right, but the provision comes across as little operational, as it sets out high-level factors to be considered (not providing clear benchmarks).

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15 Soling, *Statement on Failure to File by its Controlling Shareholder*, March 2, 2021, http://www.cninfo.com.cn/new/disclosure/detail?plate=szse&orgId=9900023703&stockCode=002766&announcementId=1209317713&announcementTime=2021-03-02; Dewei Advanced Materials, *Statement on Receipt of SAMR's Pre-Notice of Penalty Decision on Failure to File*, January 23, 2019, http://www.cninfo.com.cn/new/disclosure/detail?orgId=9900015469&announcementId=1205796209&announcementTime=2019-01-23%2019:33, and Minmetals Development, *Statement on Receipt of SAMR'S Notice of Investigation of Suspected Failure to File*, April 20, 2021, http://www.cninfo.com.cn/new/disclosure/detail?orgId=gssh0600058&announcementId=1209726574&announcementTime=2021-04-20.

16 *Zhongshan Lexing Enterprise Management Consulting Co., Ltd./ Shenzhen Soling industrial Co. Ltd.*, [2021] SAMR Notice No. 5, February 23, 2021 (published by SAMR on its website on March 11, 2021); *Jiangsu Dewei Advanced Materials Co, Ltd./Jiangsu Heshili New Material Co., Ltd.*, [2019] SAMR Notice No. 1, February 14, 2019; and *Hangzhou Alibaba Venture Capital Management/ Minmetals E-Commerce*, [2021] SAMR Notice No. 56, July 6, 2021.

17 Sanhe Pipe, IPO Prospectus (August 12, 2020 version), http://www.csrc.gov.cn/pub/zjhpublic/G00306202/202008/t20200826_382213.htm; and Inly Media, Reply to Queries on the Private Placement, http://www.cninfo.com.cn/new/disclosure/detail?orgId=9900024134&announcementId=1206936863&announcementTime=2019-09-20, September 20, 2019.

18 Securities and Futures Ordinance (Cap 571), Part XV.

19 Baidu, Post Hearing Information Pack, March 9, 2021, https://www1.hkexnews.hk/listedco/listconews/sehk/2021/0323/sehk21030901053.pdf.

In the past, MOFCOM had circulated three (mostly unofficial) draft AML implementing rules where the concept of a controlling right was defined in a sp4ecific way, similar to European Union rules: a controlling right was construed as a veto right over budget, business plan, appointment/dismissal of senior management, and/or major investments. In addition, in the draft proposal for amendment to the AML published in January 2020, SAMR defined a "controlling right" – in some more detail but still very broadly – as the right or actual condition to directly or indirectly, alone or jointly, have or likely to have decisive influence over the target's production or operation activities or other major strategic decisions.[20]

Against this dearth of rules, the failure-to-file decisions would have provided the ideal opportunity to show through "case studies" what the controlling right concept could mean. There are a number of cases, specially in the last half-year where the acquisition of (very) low minority shareholdings were held to amount to a controlling right – for example, in *Chesheng/Skio Matrix* (3.23 percent),[21] *Hantao/Lingjian* (6.67 percent),[22] *Tencent/Kingsoft Internet Security Software* (10 percent),[23] *Tencent/Mogu* (11.7 percent),[24] *Cheering Venture Global/Yestock Rental Car* (11.77 percent),[25] *Meigengmei InformationTechnology/Wangjiahuan Agriculture Products Group* (11.9 percent),[26] *Tencent/Xingin* (13.19 percent),[27] *Suning/Pateo* (14.08 percent),[28] *Xiaoju New Energy/Hainan Transport Investment/Hainan Grid* (15 percent),[29] *Mitsubishi Heavy Industries/ Suning* (15 percent),[30] *Suning/Yiguo e-Commerce* (15.21 percent),[31] and *Tencent/Yuan* (15.41 percent).[32] These (and other) decisions did not provide any insights as to why these shareholdings gave the buyer a controlling right over the target.

As an exception of some sorts, the *Tencent/China Music Group* decision is a failure-to-file decision where SAMR provided language which may potentially give some, albeit limited, guidance on the concept of a "controlling right."[33] *Tencent/China Music Group* is the first and so far only case where SAMR and its predecessor have imposed remedies in a failure-to-file investigation. Like in the other 109 cases, SAMR did not engage in a detailed discussion as to why Tencent's acquisition of 61.64% of shares in China Music Group, agreed on in July 2016 and closed in December 2017, amounted to the acquisition of a "controlling right."

However, SAMR imposed a number of remedies, both substantive (essentially, prohibiting exclusive licensing of music rights) and procedural, in that transaction. Among the procedural remedies, SAMR required Tencent to notify "concentrations" below the filing thresholds, if they have anti-competitive effects. In addition, for transactions which do not amount to "concentrations," SAMR required Tencent not to participate in any commercial decision-making in the target (except for protecting its rights as a minority shareholder).[34] The term "commercial decision-making" used in *Tencent/China Music Group* is similar to the tems used in the three prior MOFCOM drafts and the SAMR draft proposal for amendment to the AML for defining a "controlling right." Against this background, the question now arises as to whether this requirement on Tencent not to participate in China Music Group's decision-making could be interpreted as a (perhaps indirect) definition of a "controlling right." If so, given that the benchmark is participation in decision-making, rather than deciding as such or vetoing decisions, such a definition would lower the threshold for a "controlling right" as compared to the MOFCOM drafts. Nonetheless, another interpretation is also possible, namely that SAMR wanted to subject Tencent to a different standard, hence the necessity for a remedy, so the *Tencent/China Music Group* benchmark would not be directly related to the definition of a "controlling right."

20 See SAMR draft proposal for amendment to the Anti-Monopoly Law of the People's Republic of China, see at http://www.samr.gov.cn/hd/zjdc/202001/t20200102_310120.html, art. 23(2).

21 *Beijing Chesheng Technology Co., Ltd./ Zhejiang Skio Matrix Co., Ltd./ JV*, [2021] SAMR Notice No. 51, July 6, 2021.

22 *Shanghai Hantao Information Consulting Co., Ltd./ Shanghai Lingjian Information Technology Co., Ltd.*, [2021] SAMR Notice No. 33, April 28, 2021.

23 *Tencent Holdings Limited/ Kingsoft Internet Security Software Holdings Limited*, [2021] SAMR Notice No. 60, July 6, 2021.

24 *Tencent Holdings Limited/ Mogu Inc.*, [2021] SAMR Notice No. 61, July 6, 2021.

25 *Cheering Venture Global Limited/ Yestock Rental Car Co., Ltd.*, [2021] SAMR Notice No. 35, April 28, 2021.

26 *Chengdu Meigengmei Information Technology Co., Ltd./ Wangjiahuan Agriculture Products Group Co., Ltd.*, [2021] SAMR Notice No. 14, March 12, 2021.

27 *Tencent Holdings Limited/ Xingin International Holding Limited*, [2021] SAMR Notice No. 59, July 6, 2021.

28 *Suning Rundong Share Investment Management Co., Ltd./ Shanghai Pateo Electronic Equipment Manufacturing Co., Ltd.*, [2021] SAMR Notice No. 17, March 12, 2021.

29 *Beijing Xiaoju New Energy Automobile Technology Co., Ltd./ Hainan Province Transport Investment Holding Co., Ltd./ Southern Power Grid Electric Vehicle Service Co., Ltd./ Hainan Power Grid Co., Ltd./ JV*, [2021] SAMR Notice No. 48, July 6, 2021.

30 *Mitsubishi Heavy Industries, Ltd./ Suning.com Co., Ltd./ JV*, [2021] SAMR Notice No. 63, July 6, 2021.

31 *Suning Rundong Share Investment Management/ Shanghai Yiguo e-Commerce Co., Ltd.*, [2021] SAMR Notice No. 37, April 28, 2021.

32 *Tencent Holdings Limited/ Yuan Inc*, [2021] SAMR Notice No. 13, March 12, 2021.

33 *Tencent Holdings Limited/ China Music Group*, [2021] SAMR Notice No. 67, July 24, 2021.

34 SAMR also required Tencent to submit an annual report to SAMR listing all such transactions for a period of three years.

B. Substantive Assessment

As noted, the Review Regulation mandates SAMR to examine in a failure-to-file investigation whether the given transaction has anti-competitive effects.

However, in none of the failure-to-file decisions there is any substantive discussion of the transaction's effect on competition – except for the *Tencent/China Music Group* decision.Apart from that decision, all other decisions only state that the authority has examined the substance of the case and then provides the conclusion: there are no negative effects on competition. There is no reasoning whatsoever.

Of course, the largest part of transactions does not pose competition problems. This is reflected in the fact that SAMR and its predecessor have only imposed remedies (or issued prohibitions) in a very small amount of cases, less than 2 percent of all notified transactions.[35] Only one transaction which was prohibited (and nonewhere remedies were imposed), among 110 failure-to-file decisions adopted so far, is not much beyond expectations.

However, apart from *Tencent/China Music Group*, there seem to have been other transactions with a sufficiently interesting background to at least deserve a more detailed substantive assessment to be shared in the public decision. By way of example, online reports suggest that the merging parties in *China Duty Free/Sunrise Duty Free* were two operators in a rather concentrated market (with potentially high market shares).[36] Similarly, reports indicate that the parties in the *Meinian Health/Ciming* case might have some, not negligible, market shares, even if not nation-wide so potentially at the city-level.[37]

Again, we do not argue that remedies should have been adopted in the failure-to-file cases, quite to the contrary. But we think that the Chinese antitrust enforcers could have been more transparent in some of the cases to share the details of their competitive assessment.

As for the *Tencent/China Music Group* case, SAMR did make a substantive assessment of the transaction's impact on the market. In particular, it found a high combined market share (70% in terms of revenues and higher on other metrics) in the relevant market post-transaction. SAMR further pointed to the high numbers on the Herfindahl-Hirschman Index, and the fact that the merging parties were close competitors. It found that the merged entity would be able to raise entry barriers through its large amount of exclusive music rights and by way of making high non-reimbursable royalty payments to music rights holders. In SAMR's view, Tencent's rich music right catalogue post-transaction would increase users' switching costs and prevent rivals from reaching a viable scale. The authority further found that market entry by competitors had significantly decreased after closing (as compared to the period between signing and closing and before). As a result of these findings, SAMR imposed a series of post-closing remedies on Tencent.

35 Since the AML came into force in 2008, over 3,000 transactions have been cleared; only three transactions were blocked, and 50 transactions were conditionally cleared. A simple calculation would show that over 98 percent transactions were cleared without conditions. See the statistics at, for example, *SAMR answers questions from the press regarding the release of the Interim Regulation on the Review of Concentrations between Business Operators*, October 27, 2020, http://gkml.samr.gov.cn/nsjg/xwxcs/202010/t20201027_322668.html.

36 *China Duty Free (Gorup) Co., Ltd./ Sunrise Duty Free (China) Co., Ltd.*, [2018] SAMR Notice No. 15, November 21, 2018. In 2019, the market share of China Duty Free reached 85 percent according to statistics. Qianzhan Industry Research Institute, *Analysis of the market status and competitive landscape of China's duty-free industry in 2020*, September 27, 2020, https://bg.qianzhan.com/report/detail/300/200927-02be30e0.html.

37 *Meinian Health (Group) Co., Ltd./ Shanghai Tianyi Asset Management Co., Ltd./ Shanghai Weitu Investment Center/ Ciming Health Checkup Management Group Co., Ltd.*, [2017] MOFCOM Notice No. 206, May 5, 2017. Meinian reportedly held a 20-30 percent market share in non-public physical examination in China. Finance China, *Meinian: Physical examination plus insurance expands the boundaries of health management*, April 16, 2020, http://finance.china.com.cn/industry/medicine/20200416/5250869.shtml. Another report cites Meinian and Ciming with a combined market share of 26 percent, nation-wide. Chuancai Securities, *Non-public physical examination giants set sail again*, May 31, 2020, https://pdf.dfcfw.com/pdf/H3_AP202005311381347761_1.pdf?1601215040000.pdf. It is possible that health check services could be defined as local markets, similar to other healthcare services, see for example, the public notices in the following cases: *Zhejiang Medical and Health Group/ Zhejiang Jolly Pharmaceutical*, April 24, 2020; *China Resources Medical Holdings/ Huaiyin Hospital of Huai'an City*, May 13, 2021; *Warburg Pincus/ DKSH (China)*, August 21, 2018; *CITIC Capital Holdings/ Beijing Century Hong Shui Hospital Management*, June 6, 2018.

C. Multi-step Transactions

Some transactions do not take place in "one go," but are parceled into two or more steps. Many times, companies pursue a multi-step transaction entirely for business reasons.

Other times, multi-step transactions may be perceived as a tool to get around merger filing obligations. As noted above, under the AML, companies cannot implement the transaction before securing SAMR's clearance. At times, facing a tight schedule, companies may sometimes be tempted to plan to restructure the transaction to allow them to partially proceed with the transaction while avoiding "gun-jumping" risks. One of the most debated plans would be to restructure the deal as a "multiple-step" transaction.

Over the six plus years of active failure-to-file enforcement, there have been a number of cases involving multi-step transactions. In most authority decisions on these transactions, there is not much guidance. But some decisions allow certain inferences.

A prior MOFCOM draft rule had indicated a seemingly straightforward rule for multi-step transactions: if the first step of the transaction confers a controlling right, there is a concentration between business operators and a filing is required; if the first step does not confer such right, a filing is not required. This idea is reflected in many of the failure-to-file cases.

In several transactions, the first step of a multi-step transaction was already found to give the buyer a "controlling right" over the target. This was the case in *Fujian Electronic Information Group/Chino-e Communication*,[38] *Fosun Pharmaceuticals/Erye Pharmaceuticals*,[39] *Zhuo'er Development/ Zhongnon Net*,[40] and *Suqian Hanbang Investment Management/Five Star Appliances*.[41]

In other transactions, in particular *Dade / Sichang Pharmaceuticals*,[42] *Paper Excellence/Eldorado*,[43] and *Alibaba Investment/Yingtai Commercial Group*[44] only the second step was found to confer a controlling right and trigger the notification obligation.

In a limited number of transactions, the authorities departed from the principle of checking each individual transaction step whether a controlling right is acquired.

In these transactions, the authorities looked at the entire transaction as a single "concentration between business operators." They focused on the interconnection between the various steps of the transaction, instead of examining which step individually gave rise to a controlling right. As such, in *OCI/Tokuyama Malaysia*, the buyer structured its acquisition of 100 percent of shares in the target in three parts, 16.5 percent, 34.2 percent and 49.3 percent. The buyer closed the first step within around a week of signing the transaction agreement. Before closing the second and third steps, planned for half a year later, the buyer self-reported to MOFCOM. MOFCOM found that the three steps were a "package deal" with a single transaction goal and interdependent transaction steps, amounting to a single concentration between business operators. As a result, MOFCOM held the updating of the target's business license after the first step to be a breach of the AML. With almost identical wording, MOFCOM found the *Meinian Health/Ciming* merger to be a "package deal" with a single transaction goal and interdependent transaction steps.[45]

One of the most remarkable examples of the "holistic" approach of considering several steps as a single concentration is *Canon/Toshiba Medical*.[46] In that case, Canon agreed to buy 100 percent of the shares in Toshiba Medical from Toshiba. Canon designed the transaction into two steps, implemented the first step and made a merger filing for the second step. MOFCOM held Canon to have jumped the gun.

38 *Fujian Electronic Information (Group) Co., Ltd./ Shenzhen Chino-eCommunications Co., Ltd.*, [2015] MOFCOM Notice No. 668, September 16, 2015.

39 *Shanghai Fosun Pharmaceutical Development Co., Ltd./ Suzhou Erye Pharmaceutical Co., Ltd.*, [2015] MOFCOM Notice No. 669, September 16, 2015.

40 *Zhuo'er Development Holding Limited/ Shenzhen Zhongnong Net Company Limited*, [2020] SAMR Notice No. 7, March 30, 2020. But first step of the transaction gave the buyer a shareholding above 50 percent.

41 The decision is not very clear whether the first step (46 percent of shares) or only the second step (the remaining 54 percent of shares) entailed the acquisition of a controlling right. In one part, the SAMR decision states that the acquisition of 100 percent of shares in the target amounted to a concentration between business operators. At another part, decision mentioned the dates of updating the business license for both steps, saying that this constitute a breach of the law.

42 *Dade Holdings Inc./ Jilin Sichang Pharmaceuticals Co., Ltd.*, [2016] MOFCOM Notice No. 173, April 21, 2016.

43 *Paper Excellence BV/ Eldorado Brasil Celulose S.A.*, [2018] SAMR Notice No. 4, July 30, 2018.

44 *Alibaba Investment Limited/ Yintai Retail (Group) Co., Ltd.*, [2020] SAMR Notice No. 26， December 14, 2020.

45 *Meinian Health (Group) Co., Ltd./ Shanghai Tianyi Asset Management Co., Ltd./ Shanghai Weitu Investment Center/ Ciming Health Checkup Management Group Co., Ltd.*, *supra* note 45.

46 *Canon Co., Ltd./ Toshiba Medical System Co., Ltd.*, [2016] MOFCOM Notice No. 965, December 16, 2016.

In that case, Canon used a so-called "warehousing" structure involving an interim buyer. In anticipation of the transaction, the seller (Toshiba) created three types of equity-related rights in relation to Toshiba Medical: 20 shares with voting rights; one share without voting rights; and 100 share options, allowing the owner to convert them into ordinary shares. In addition, a special purpose vehicle ("SPV") was established by three unidentified natural persons before the transaction.

As noted, the transaction was implemented in two steps. As a first step, the SPV acquired the voting shares in Toshiba Medical for close to JPY 100,000 (around USD 900), whereas Canon acquired the non-voting share and the share options for approximately JPY 665 billion (around USD 6 billion). As a second step, the plan was for Canon to exercise the share options and convert them into ordinary shares and for Toshiba Medical to buy the 20 shares with voting rights from the SPV and the non-voting share from Canon.

After closing of the first step but before implementation of the second step, Canon made a merger filing with MOFCOM.

However, MOFCOM considered that the two steps were closely connected and formed an indivisible part of Canon's acquisition of Toshiba Medical. Consequently, MOFCOM concluded that the closing of the first step was an implementation of the transaction in violation of the standstill obligation.

V. CONCLUSIONS

As noted in the introduction, a large part of the failure-to-file cases within the last half-year involves Internet companies.

To an extent, this is not a phenomenon limited to the failure-to-file area. The largest case this year, the *Alibaba* investigation, was followed by the publication of another penalty decision against an e-commerce player, Sherpa's.[47] Furthermore, in April 2021, SAMR called a meeting with online platforms and asked them to report back on their antitrust compliance and possible rectification measures.[48]

However, there is also a sector-specific driver behind the numerous recent failure-to-file cases against Internet companies. Due to certain regulatory phenomena, many transactions by Internet companies were not filed with SAMR and MOFCOM in the past. In that sense, the numerous failure-to-file penalty decisions against Internet companies since December 2020 show that the past is catching up for them.

But why are the Internet companies queuing up to self-report?

The reason is simple: the AML is currently in the legislative process for its first-ever amendment.[49] Both officially and unofficially circulated drafts of the to-be-amended AML contain a change in the fine level for failure-to-file cases – instead of RMB 500,000, the new fine would be up to 10 percent of the company's annual revenue in the previous year.

In other words, it makes a great deal of economic sense to file and get punished under the AML as it currently stands. According to China's administrative penalty rules, the amended AML would be applicable to transactions completed before the amendment's entry into force as long as the merged entities or JVs continue to exist – i.e., the violation may be deemed to be ongoing.

Generally speaking, multinationals have a better understanding of the merger control regime and higher compliance standard due to their experience in other jurisdictions with older merger control regimes than China. However, quite some of the past failure-to-file cases involved foreign companies, in particular JV projects with Chinese companies. Our experience is that this is partly due to the fact that some Chinese parties to the JV projects insist on not making merger filings in order to save time and costs, and some even promise to compensate the foreign parties in the event of fines being imposed for failure-to-file. Now that the amended AML is going to significantly change the landscape of China's merger control system, both foreign and Chinese companies need to realign and readjust their way of dealing with merger control issues in China.

47 *Sherpa's*, [2020] Shanghai AMR Notice No. 06201901001.

48 SAMR, *The Administration for Market Regulation, the Central Cyberspace Administration of China, and the State Administration of Taxation jointly convene an administrative guidance meeting for Internet platform enterprises*, April 13, 2021, http://www.samr.gov.cn/xw/zj/202104/t20210413_327785.html.

49 Currently, the Standing Committee of the National People's Congress has included the AML amendment in its legislative plan for 2021. Xinhua Net, *China will amend the Anti-Monopoly Law*, March 8, 2021, http://www.xinhuanet.com/politics/2021-03/08/c_1127184680.htm.

No.	Case	Time of decision	Duration of procedure (days)	Fine (RMB)
1	Tsinghua Unigroup Co., Ltd./ RDA Microelectronics Co., Ltd.	December 2, 2014	112	300,000
2	Fujian Electronic Information (Group) Co., Ltd./ Shenzhen Chino-e Communication Co., Ltd.	September 16, 2015	275	150,000
3	Shanghai Fosun Pharmaceutical Development Co., Ltd./ Suzhou Erye Pharmaceutical Co., Ltd.	September 16, 2015	184	200,000
4	Nanjing Nanche Puzhen Car Co., Ltd./ Bombardier Transportation Group Sweden Co., Ltd./ JV	September 16, 2015	197	150,000 each
5	BesTV New Media Co., Ltd./ Microsoft Corporation/ JV	September 16, 2015	253	200,000 each
6	Dade Holdings Inc/ Jilin Sichang Pharmaceuticals Co., Ltd.	April 21, 2016	/	150,000
7	New United Group Co., Ltd./ Bombardier Transportation Sweden AB	April 21, 2016	/	300,000 / 400,000
8	Beijing Beiche Investment Co., Ltd./ Hitachi, Ltd. / JV	April 21, 2016	/	150,000 each
9	Zhongshan Broad-Ocean Motor Co., Ltd./ Prestolite Electric (Beijing) Ltd.	August 31, 2016	/	150,000
10	Continental Holding China Co., Ltd./ Huayu Automotive Systems Company Limited/ JV	August 31, 2016	/	200,000 each
11	Canon Co., Ltd./Toshiba Medical System Co., Ltd.	December 16, 2016	56	300,000
12	Cummins (China) Investment Co., Ltd./ Xiangyang Kanghao Mechanical & Electricity Co., Ltd./ JV	January 9, 2017	355	150,000 each
13	OCI Company Ltd./ Tokuyama Malaysia Co., Ltd.	April 21, 2017	101	150,000
14	Guangdong Rising H.K. (Holding) Limited/ PNA Australia Co., Ltd.	May 5, 2017	465	150,000
15	Meinian Health (Group) Co., Ltd./ Shanghai Tianyi Asset Management Co., Ltd./ Shanghai Weitu Investment Center/ Ciming Health Checkup Management Group Co., Ltd.	May 5, 2017	284	300,000
16	Wuhu Construction Investment Co., Ltd./ Chery New Energy Automobile Co., Ltd./ Yaskawa Electric Corporation/ JV	July 11, 2017	235	150,000 each
17	Svitzer Asia Pte. Ltd./ Binhai Port Investment Development Co., Ltd./ JV	July 11, 2017	257	150,000 each

No.	Case	Time of decision	Duration of procedure (days)	Fine (RMB)
18	Grand Baoxin Auto Group Co., Ltd./ Beijing Yanbao Car Service Co., Ltd./ Sichuan Ganghong Investment Neoteric Stock Co., Ltd.	January 10, 2018	233	300,000 each
19	Yihai Kerry Investment Co., Ltd./ CJ Cheiljedang Co., Ltd./ JV	January 19, 2018	386	150,000 each
20	Shandong Sun Holding Group Co., Ltd./ International Paper & Sun Cartonboard Co., Ltd./ Shandong International Paper & Sun Coated Paperboard Co., Ltd./ Shandong Ip & Sun Food Packaging Co., Ltd.	January 19, 2018	336	300,000
21	Qingdao Port Merchants International Container Terminal Co., Ltd./ Qingdao Port (Group) Co., Ltd./ JV	April 4, 2018	238	200,000 each
22	Qingdao Port Merchants International Container Terminal Co., Ltd./ Qingdao Xinqianwan Container Terminal Co., Ltd./ JV	April 4, 2018	238	200,000 each
23	Yunnan Metropolitan Real Estate Development Co., Ltd./ Tianjin Yinrun Investment Co., Ltd./ Cangnan Yintai Property Co., Ltd./ Hangzhou Haiwei Real Estate Development Co., Ltd./ Pingyang Yintai Property Co., Ltd./ Hangzhou Lixiang Real Estate Co., Ltd./ Fenghua Yintai Real Estate Co., Ltd./ Chengdu Yincheng Real Estate Co., Ltd./ Ningbo Taiyue Co., Ltd.	April 26, 2018	260	150,000
24	Tianjin Haiguang Advanced Technology Investment Co., Ltd./ Advanced Micro Devices Inc./ JV	April 26, 2018	421	150,000 each
25	Paper Excellence BV/ Eldorado Brasil Celulose S.A.	July 30, 2018	124	300,000
26	Yunnan City Construction Investment Group Co., Ltd./ Chengdu Global Century Exhibition & Travel Group Co., Ltd.	August 22, 2018	176	300,000
27	GEM (Wuhan) City Urban Mineral Recycling Industrial Park Development Co., Ltd./ Wuhan GHM Auto Parts Remanufacturing Co., Ltd.	August 30, 2018	171	300,000
28	Linde Gas (H.K.) Limited/ Shanghai Huayi Energy Chemical Technology Co., Ltd./ JV	September 11, 2018	265	300,000 each
29	Linde Gas (H.K.) Limited/ Dahua Group Co., Ltd./ JV	October 10, 2018	300	300,000 each
30	China Duty Free (Group) Co., Ltd./ Sunrise Duty Free (China) Co., Ltd.	November 21, 2018	252	300,000

No.	Case	Time of decision	Duration of procedure (days)	Fine (RMB)
31	Linde Gas (H.K.) Limited/ Guangzhou Iron Holding Limited/ JV	December 4, 2018	230	300,000 each
32	Goji Medicine Co., Ltd./ Henan Baijiahao Yisheng Medicine Co., Ltd.	December 21, 2018	172	400,000
33	Jiangsu Dewei Advanced Materials Co., Ltd./ Jiangsu Heshili New Material Co., Ltd.	February 14, 2019	205	300,000
34	Inly Media Co., Ltd./ Shanghai Zhiqu Advertising Co., Ltd.	February 19, 2019	267	200,000
35	Overseas Hong Kong Investment Co., Ltd./ Weifang Sendamai Liquefied Product Terminal Co., Ltd.	February 19, 2019	333	300,000
36	Praxair (China) Investment Co., Ltd./ Nanjing Refinery Co., Ltd./ JV	April 28, 2019	275	300,000 each
37	Yageo Corporation/ Junyao Holding Limited	June 25, 2019	272	300,000
38	Tianneng Battery Group Co., Ltd./ Anhui Hongda Power Supply Co., Ltd.	August 16, 2019	94	300,000
39	Harbin Electric Co., Ltd. / GE (China) Co., Ltd./ JV	September 3, 2019	162	300,000 each
40	Speed Up Development Co., Ltd./ Harbin Dili Fresh Agricultural Products Enterprise Management Co., Ltd.	September 16, 2019	297	300,000
41	China Post Capital Co., Ltd./ Chengdu Wolaila Information Techology Co., Ltd.	September 16, 2019	418	400,000
42	Guangxi Liuzhou Iron and Steel Group Co., Ltd./ Guangxi Zhongjin Medal Technology Co., Ltd.	September 16, 2019	196	350,000
43	BAIC Motor Co., Ltd./ HCS Co., Ltd./ Hyundai Motor Group(China) Ltd./ JV	September 27, 2019	130	300,000 each
44	Tibet Dejin Enterprise Management Co., Ltd./ Shanghai Huitong Energy Co., Ltd.	September 29, 2019	173	300,000
45	Suzhou Quanyi Health Pharmacy Chain Co., Ltd./ Suzhou Jianshengyuan Yiyao Co., Ltd.	September 29, 2019	163	300,000
46	Pierburg Pump Technology Co., Ltd./ Shanghai Xingfu Motorcycle Co., Ltd./ JV	November 1, 2019	235	350,000 each
47	Guangzhou Port Co., Ltd./ Zhongshan Port Co., Ltd.	December 9, 2019	193	300,000
48	Liaoning Port Group Co., Ltd./ Yingkou Port Group Co., Ltd.	December 9, 2019	246	350,000

No.	Case	Time of decision	Duration of procedure (days)	Fine (RMB)
49	New Hope Investment Group Co., Ltd./ Xingyuan Environment Technology Co., Ltd.	December 13, 2019	193	400,000
50	MBK Partners, L.P. JC Fourth Limited Partnership/ Shanghai Siyanli Industrial Co., Ltd.	December 20, 2019	175	350,000
51	Zhuo'er Development Holding Limited/ Shenzhen Zhongnong Net Company Limited	March 30, 2020	215	300,000
52	Guangdong Sanhe Pipe Co., Ltd./ Guangdong Jianhua Pipe Co., Ltd./ JV (Guangdong Hejian)	June 9, 2020	473	300,000 each
53	Guangdong Sanhe Pipe Co., Ltd./ Guangdong Jianhua Pipe Co., Ltd./ JV (Guangdong Tuona)	June 9, 2020	473	300,000 each
54	Taiwan Cement Corporation/ Ordu Yardimlasma Kurumu/ JV	June 25, 2020	317	300,000 each
55	Jiangxi Jemincare Pharmaceutical Industry Investment Co., Ltd./ Nanjing Hencer Pharmaceutical Co., Ltd.	June 25, 2020	335	300,000
56	Ordos Junzheng Energy & Chemical Industry Co., Ltd./ Sinochem International Logistics Co., Ltd.	June 25, 2020	216	350,000
57	Zhejiang Infrastructure Investment Group Co., Ltd./ Dohia Group Co., Ltd.	September 3, 2020	184	350,000
58	ANE Fast Logistics (Hong Kong) Limited/ Changshan Giant Truck Supply Chain Management Limited	October 23, 2020	243	300,000
59	Jiangsu Yueda Investment Co., Ltd./ Beijing Changjiu Logistics Co., Ltd./ JV	November 6, 2020	292	300,000 each
60	Alibaba Investment Limited/ Yintai Retail (Group) Co., Ltd.	December 14, 2020	40	500,000
61	China Literature Limited/ New Classics Media Limited	December 14, 2020	40	500,000
62	Shenzhen HIVE Box Network Technology Co., Ltd./ China Post Zhidi Technology Co., Ltd.	December 14, 2020	174	500,000
63	Xinjiang Xuefeng Investment Holding Limited/ Yuxiang-Diversifous Poplar Chemical Co., Ltd.	December 30, 2020	204	300,000
64	Zhuhai Huafa Real Estate Management Service Co., Ltd./ Beijing Jones Lang LaSalle Property Management Services Co., Ltd./ JV	January 27, 2021	237	350,000 each
65	Baoneng Motor Group Co., Ltd./ Qoros Automotive Co., Ltd.	February 23, 2021	308	350,000

No.	Case	Time of decision	Duration of procedure (days)	Fine (RMB)
66	Zhongshan Lexing Enterprise Management Consulting Co., Ltd./ Shenzhen Soling industrial Co., Ltd.	February 23, 2021	240	300,000
67	Wuhan Jinyu Free Trade Development Co., Ltd./ Dhl Logistics (Beijing) Co., Ltd./ JV	February 24, 2021	670	150,000 each
68	Yintai Retail (Group) Co., Ltd./ Kaiyuan Commercial Co., Ltd.	March 12, 2021	46	500,000
69	Tencent Holdings Limited/ Yuan Inc	March 12, 2021	46	500,000
70	Chengdu Meigengmei Information Technology Co., Ltd./ Wangjiahuan Agriculture Products Group Co., Ltd.	March 12, 2021	46	500,000
71	Suqian Hanbang Investment Management Co., Ltd./ Jiangsu Five Star Appliance Co., Ltd.	March 12, 2021	46	500,000
72	Baidu Holdings Limited/ Ainemo Inc	March 12, 2021	46	500,000
73	Suning Rundong Share Investment Management Co., Ltd./ Shanghai Pateo Electronic Equipment Manufacturing Co., Ltd.	March 12, 2021	46	500,000
74	Didi Mobility Pte. Ltd./ SoftBank Corp./ JV	March 12, 2021	46	500,000 each
75	TAL Education Group/ DaDa Education Group	March 12, 2021	46	500,000
76	Shanghai Dongfang Newspaper Co., Ltd./ Beijing Quantum Jump Technology Co., Ltd./ JV	March 12, 2021	46	500,000 each
77	Beijing Nucarf Network Technology Co., Ltd./ Hebei Baoruitong Electronic Commerce Co., Ltd.	March 12, 2021	46	500,000
78	Hongyun Jiukang Data Technology Co., Ltd./ Shanghai Yunxin Venture Capital Management Co., Ltd./ JV	March 22, 2021	56	500,000 each
79	Tencent Holdings Limited/ Bitauto Holdings Limited	April 28, 2021	48	500,000
80	Tencent Holdings Limited/ Shanghai Lantu Information Technology Co., Ltd.	April 28, 2021	48	500,000
81	Linzhi Tencent Technology Co., Ltd./ Dalian Wanda Commercial Properties Co., Ltd./ JV	April 28, 2021	48	500,000 each
82	Shanghai Hantao Information Consulting Co., Ltd./ Shanghai Lingjian Information Technology Co., Ltd.	April 28, 2021	48	500,000
83	Cheering Venture Global Limited/ Toyota Motor Corporation/ JV	April 28, 2021	48	500,000 each

No.	Case	Time of decision	Duration of procedure (days)	Fine (RMB)
84	Cheering Venture Global Limited/ Yestock Rental Car Co., Ltd.	April 28, 2021	40	500,000
85	Didi Smart Transportation Technology Co., Ltd./ Jinan Inspur Intelligent Investment Technology Co., Ltd./ JV	April 28, 2021	48	500,000 each
86	Suning Rundong Share Investment Management Co., Ltd./ Shanghai Yiguo E-commerce Co., Ltd.	April 28, 2021	48	500,000
87	China Yintai Investment Co., Ltd./ Hangyin Consumer Finance Co., Ltd.	June 3, 2021	56	500,000
88	Huidi (Tianjin) Business Service Co., Ltd./ China FAW Group Corporation/ JV	July 6, 2021	112	500,000 each
89	Huaxia Trip Co., Ltd./ Huidi (Tianjin) Business Service Co., Ltd./ JV	July 6, 2021	109	500,000 each
90	Beijing Xiaoju Smart Car Technology Co., Ltd./ Beijing New Energy Automobile Co., Ltd./ JV	July 6, 2021	109	500,000 each
91	Huidi (Tianjin) Business Service Co., Ltd./ Teld New Energy Co., Ltd. / JV	July 6, 2021	85	500,000 each
92	Beijing Xiaoju New Energy Automobile Technology Co., Ltd./ Hainan Province Transport Investment Holding Co., Ltd./ Southern Power Grid Electric Vehicle Service Co., Ltd./ Hainan Power Grid Co., Ltd./ JV	July 6, 2021	117	500,000 each
93	Huidi (Tianjin) Business Service Co., Ltd./ Tibet Aotong Venture Investment Co., Ltd. (Zhejiang Dishi)/ JV	July 6, 2021	83	500,000 each
94	Huidi (Tianjin) Business Service Co., Ltd./ Tibet Aotong Venture Investment Co., Ltd. (Hangzhou Dishi)/ JV	July 6, 2021	83	500,000 each
95	Beijing Chesheng Technology Co., Ltd./ Zhejiang Skio Matrix Co., Ltd./ JV	July 6, 2021	85	500,000 each
96	Alibaba (China) Network Technology Co., Ltd./ Tianxianpei (Shanghai) Technology Co., Ltd.	July 6, 2021	117	500,000
97	Hangzhou Alibaba Venture Capital Management Co., Ltd./ Shanghai Commercial Investment Co., Ltd./ JV	July 6, 2021	109	500,000 each
98	Alibaba (China) Network Technology Co., Ltd./ Theland New Cloud (Shanghai) Digimart Co., Ltd.	July 6, 2021	109	500,000

No.	Case	Time of decision	Duration of procedure (days)	Fine (RMB)
99	Alibaba (China) Network Technology Co., Ltd./ Guangzhou Evergande Football Club Co., Ltd.	July 6, 2021	85	500,000
100	Haiyan Ali Venture Capital Co., Ltd./ Minmetals E-Commerce Co., Ltd.	July 6, 2021	43	500,000
101	Haiyan Ali Venture Capital Co., Ltd./ Zhejiang Province Chuangxin Fazhan Investment Co., Ltd./ JV	July 6, 2021	85	500,000 each
102	Tencent Mobility Limited/ 58 City	July 6, 2021	117	500,000
103	Tencent Holdings Limited/ Xingin International Holding Limited	July 6, 2021	117	500,000
104	Tencent Holdings Limited/ Kingsoft Internet Security Software Holdings Limited	July 6, 2021	85	500,000
105	Tencent Holdings Limited/ Mogu Inc.	July 6, 2021	85	500,000
106	Suning.com Co., Ltd./ Bank of Nanjing Co., Ltd. / JV	July 6, 2021	109	500,000 each
107	Mitsubishi Heavy Industries, Ltd./ Suning.com Co., Ltd./ JV	July 6, 2021	85	500,000 each
108	Beijing Sankuai Technology Co., Ltd./ Acewill Information Technology (Beijing) Co., Ltd.	July 6, 2021	83	500,000
109	Tencent Holdings Limited/ Sogou Co.	July 6, 2021	162	500,000
110	Tencent Holdings Limited/ China Music Group	July 24, 2021	180	500,000

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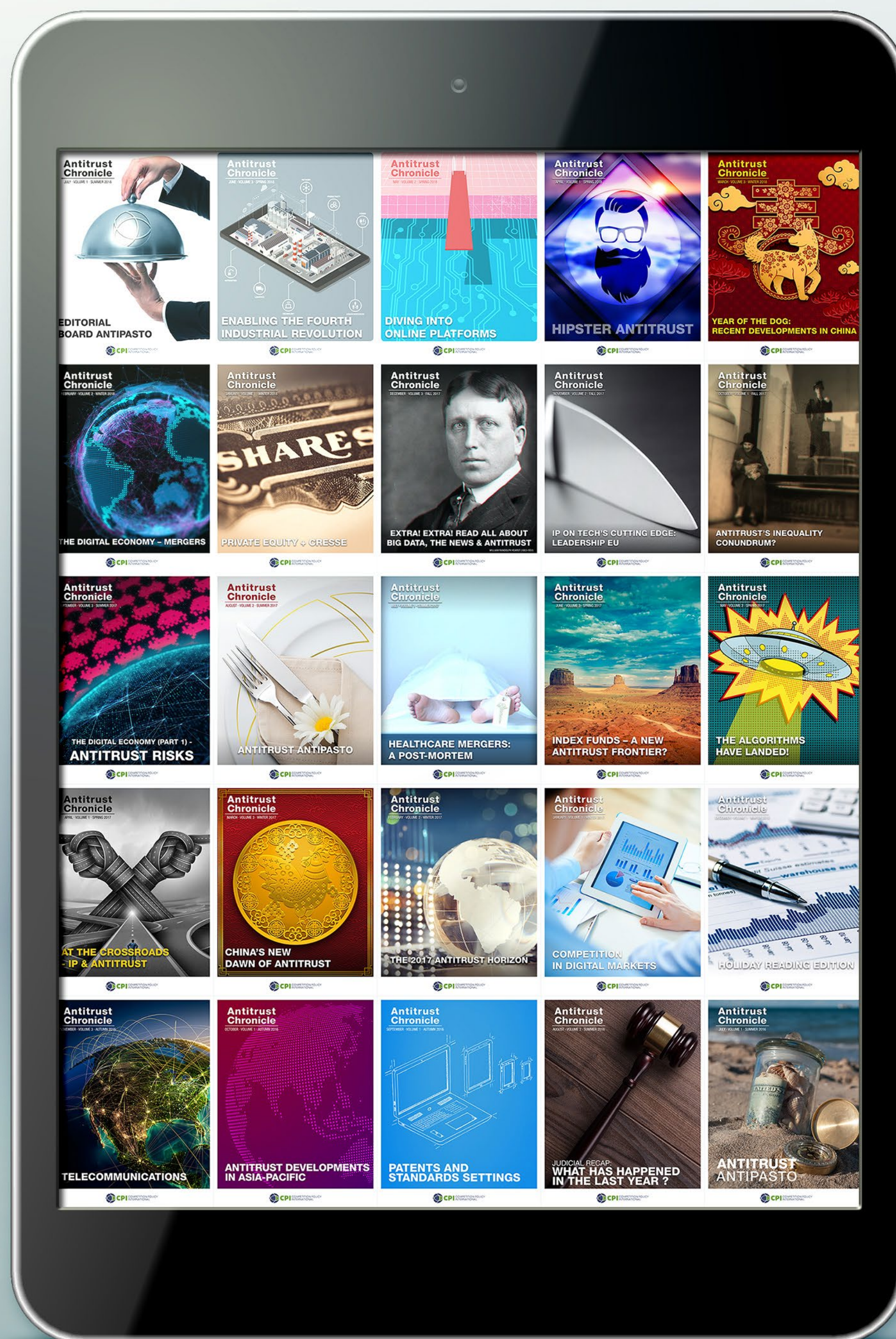

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