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## **USA and EU antitrust approaches to digital economy quizzes: forks and solutions**

This working paper represents the analytical survey of specific antitrust problems of the digital segment. The problems arise from considerable network effects, the active development of multi-sided markets with a strong information asymmetry and the important role of platforms with extensive opportunities to enhance their market power. The paper includes the analysis of several high-profile antitrust cases in the digital industries of the USA and the EU. The questions and solutions from those cases may be used for antitrust purposes throughout the world after their careful comparison and the analysis of their applicability to developing economies.

Digital economy has recently become one of the “hot topics” not only in a political rhetoric but also in the academic sphere. The term “digital economy” seems to represent an eclectic puzzle of new products, services, markets and industries, mainly with the considerable role of various modern information and communication technologies (ICT). Despite a strong presence of digital economy in the modern economic discourse, there is still a significant degree of controversy concerning the definition and the measurement of the digital economy.

The discussion on that problem is summarized, for instance, in (IMF, 2018) with the notable reservation on the absence of a single conventional definition of digital economy. The interpretations of digital economy vary from the narrowest “economy of platform-based activities” to the largest “economy with any use of digital data”. Of course, the latter probably covers almost the whole national economy. To avoid the ambiguity, IMF recommends to move from the confusing concept of “digital economy” to the instrumental definition of the digital sector: “online platforms, platform-enabled services, and suppliers of ICT goods and services” (IMF, 2018, p. 7). In this paper we follow that approach.

This narrow-defined digital sector is also very diverse but at least there is an opportunity to identify main factors affecting the applicability of this or that branch of economic policy.

When the antitrust rules are concerned there are several main peculiarities appearing in numerous cases / investigations in the digital sector – so, we can define the specific problems of antitrust in the digital sector through those factors:

- considerable network effects;
- development of two-sided and multi-sided markets;
- growth of platforms and aggregators.

*Network effects* reproduce the problem of the efficient over-concentration in the industry and, consequently, monopolistic trends in a market. There is nothing new in this problem itself: high economies of scale in natural monopolies lead to the same difficulty. However, the absence of usual physical network infrastructure in specific digital markets makes the necessity of regulation unclear. (Kimmelman, Cooper, 2015) and (Daly, 2017) suppose that digital markets antitrust in the USA and in the EU cannot go on without stronger and more precise regulation, especially in telecommunications.

Of course, there are some sensitive areas, such as the setting of standards and the access to essential facilities, which implies the strengthening of regulation in case of emerging necessity. However, now it is difficult even to imagine the direct regulation of all the industries with significant network effects. As such, common antitrust rules should be applied to the industries with network effects.

Then the following question appears: should network effects be regarded as an additional *excuse* or as an additional *guilt* for the company exploiting those effects?

This controversy could somehow be observed on the example of Microsoft cases on tying (bundling) different products in the EU and in the USA. The attitude of the European Commission was more hostile: network effects were considered as an instrument to extend a dominant position (Economides, Lianos, 2010, p. 356). The final US solutions on Microsoft policies expressed softer attitude to network effects, which are usually considered as a legal way to obtain market leadership (Gifford, Kudrle, 2015, p. 187), and then the court imposed behavioral remedies only.

The difference in American and European approaches in Microsoft cases, more or less clearly expressed, may be attributed to a more general matter of transatlantic discussion: do short-term consumer benefits brought by a potential monopolist with large network effects outweigh less competitive market structure in the long term? The presumable answer of the US antitrust regulators is positive, while the European Commission is more likely to give a negative answer (Devlin, Jacobs, 2010, supra note 25). A good summary is offered in (Page, 2010): "...markets are usually better than courts at restoring competition. Recent studies and the aftermath of Microsoft show that network effects do not fundamentally change this insight". Of course, the answer depends also on the existence of barriers of entry, which are considered below.

*Development of two-sided and multi-sided markets* is inherent to the digital sector, because the mere existence of those markets requires the supply of a good by both sides of the market, and the most obvious example of such a good is the information: articles, ads, software, consumer profiles, media content, etc. The information can be produced by a large and different sets of market players including households, SMEs, as well as by corporations, often without any needs in specific production capacities. Consequently, network effects are doubled, and relevant competition problems are multiplied due to crossing, mutual influence of network effects.

Antitrust policies in such markets face a variety of instrumental problems, but the most difficult task is generated by the existence of *platforms* – the entities integrating different sides of that market. Their existence is not indispensable for any multi-sided markets, if there is an independent ground for the interaction. Nevertheless, the existence of platforms is a powerful instrument of transaction costs minimization but the costs in terms of competition may be significant.

The combination of those factors can create a serious threat for the competition: the growth of market power (or the appropriation of dominance) of the biggest market players if they control the most important platforms and generate huge positive network externalities. One of possible answers to that challenge is the strengthening of antitrust policies on the ground of necessity to prevent the total dependence on one or two leading platforms, especially if they represent vertically integrated corporations and try to participate in the variety of markets (one of the examples is described in (Shastitko, Kurdin, 2017)).

This is the most outstanding, though not the single specific “digital” antitrust problem. Ezechia and Stucke (2016) identify 3 classes of such problems. One of them is a growth of platforms’ market power, which was already cited here.

The second problem is the large potential for price discrimination in markets with extensive information flows. The information asymmetry between different sides of the market and especially between platforms and the rest of the market provides a brilliant opportunity for the abuse of market power. This could be considered as another, informational aspect of the extensive platforms’ market power.

In addition, we should emphasize that the informational advantage of platforms may be also realized in a different manner: powerful platforms are able to monitor and even forecast the performance of newcomers in the same or adjacent markets in order to acquire them and to prevent the emergence of independent competitors. Here the informational advantage could serve as a strategic barrier to entry.

The third potential problem identified by Ezechia and Stucke (2016) is more artificial: it is the possible collusion between pricing algorithms, probably even without any human purposeful participation. An opportunity of “fully automatic cartelism” seems to be an exotic option, but in general pricing algorithms deserve to be an area of antitrust investigations.

Several recent cases demonstrate that there is significant degree of uncertainty towards the realization of antitrust instruments taking into the account the peculiarities and specific problems of competition in digital markets.

For instance, one of high profile investigations performed by the European Commission – the case of Google search and comparison shopping services – received a controversial reaction from the antitrust community. Google allegedly practiced the abuse of market power by manipulating its search results and promoting his own shopping comparison machine to the first places in response to clients’ queries. As a result, competing comparison machines suffered from the outflow of customers. In 2017, in order to change the situation, the EC prescribed

to change Google's policies (in addition to a \$2.7 bln fine), and Google introduced a new system of ranking search results based on the auction between all the market players. That step should guarantee the search neutrality. However, in practice, Google continued to prevail in his own search results despite the emergence of a new procedure<sup>1</sup>. As a result, the solution presented by Google and implicitly supported by the EC obtained his part of critique, although there were positive comments too<sup>2</sup>.

The core of the problem may be found in the information asymmetry: any measures undertaken by a dominant platform will be a "black box" for the regulator, as well as for the competitors, unless this platform shares its informational advantage. As such, the following question is applicable in the context of this investigation: should the antitrust authority regulate or control information flows inside a platform, or somehow intervene in them to prevent the abuse of those "big data" consolidated by a platform? Or, to be more precise, should special authorized bodies (regulators of ICT industries) accomplish such additional pro-competition tasks (in concert with antitrust bodies' efforts)? There are voices promoting that decision for Europe (Daly, 2017), as well as for the USA (Kimmelman, Cooper, 2015), in expectation that new conditions may contribute to a new stage of interrelation between competition policies and market regulations in the telecom industries.

This investigation was not a single antitrust problem faced by Google – another recent case with mobile applications may also involve significant consequences. Google was blamed by his competitors for an alleged imposing his own mobile applications to Android-based<sup>3</sup> mobile phone producers, which could harm other application developers. Russian Federal Antimonopoly Service successfully proceeded with this case in 2016-2017, and the European Commission is following the same path. That is the case of probable abuse of dominance based on the excessive market power (speaking in terms of the US antitrust) of a platform, which is simultaneously working as a provider of platform services and as a producer in adjacent markets (in this case – markets for mobile operating systems and markets for mobile applications respectively). However, even if we ignore the difficult technical question of market boundaries for that case, we face a fundamental question of effect-based antitrust rulings: is it possible to effectively perform functions of a platform without giving to a consumer any minimal guaranteed set of "bundled" products or services? And should the antitrust body punish a platform for such a "bundling"? This question is partially inherited from the Microsoft cases, as we can remember that EC-promoted "unbundled" version of Windows (without pre-installed media player) was ignored by consumers (Etro, 2007, p. 235).

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<sup>1</sup> <https://www.bloomberg.com/view/articles/2018-02-20/google-s-european-union-antitrust-troubles-are-a-lobbyists-war>

<sup>2</sup> <https://www.forbes.com/sites/washingtonbytes/2017/03/16/7-reasons-why-europes-antitrust-cases-against-google-are-a-big-deal/#1257a9031498>

<sup>3</sup> Android is a mobile operating system powered by Google.

Another resonant antitrust investigation of platforms' businesses is connected with an attempted merger between AT&T and Time Warner in the USA. AT&T is an ICT company providing internet and TV services, while Time Warner produces media content. The decision of the US Department of Justice (DoJ) in 2017 was unexpectedly negative, so the parties went to the court – and the decision was still pending as of May 2018. DoJ insisted that the merger could lead to a withholding of Time Warner content from other internet & TV providers and, consequently, to an increase in prices by a new conglomerate. According to the position of the companies concerned, the deal is intended to raise the efficiency of targeted ads. Here again we face the problem of a vertical integration between a platform (AT&T) and a market player from one side of multi-sided markets (including sales of media content to consumers, as well as sales of advertisement). The main question in this investigation is whether there exists a considerable specificity in platform businesses due to network effects, which could excuse probable anti-competitive effects or, on the contrary, antitrust decisions here should be more restrictive.

Active M&A policies of IT industry giants have been subject to criticism due to a negative effect on market entry and concentration. Facebook is a spectacular example of early-stage prospective purchases. In 2012 Facebook acquired his direct competitor in social networks – Instagram. In 2014 Facebook purchased one of now leading mobile messengers – What's App. Recently, in 2016, Facebook acquired a fast-growing internet surveys service TBH. Similar policies were conducted by Google with the purchase of video service Youtube, image organizer Picasa and dozens of smaller digital service and content providers. All these deals contributed to a current position of giants: together they receive about 60% of US net digital advertising revenue (data by eMarketer<sup>4</sup>).

If market leaders consistently buy prospective start-ups at early stages, then they could pass through antitrust restrictions because of a moderate scope of deals at the moment of purchase but in effect they undermine a possible redistribution of market shares by independent players. This problem of M&A policies in the digital segment comes from network effects, which entail an explosive growth of successful suppliers only after passing some quantitative threshold in their user network. As such, to prevent competition in the market it is sufficient to monitor the performance of newcomers, to “pick up” market entrants with prospective technologies and to develop them inside the own network of a market leader.

From here we can deduce the following question: is it reasonable to modify standards of M&A approval to take into account a potential competition and the informational advantage of market leaders giving them an opportunity to monitor and affect newcomers' strategies and results? (Economist, 2018).

Following the interpretation by (Stucke, Ezechia, 2017) and (Wessel, 2018), the set of such problems may become a reason for a substantial revision of the US antitrust policies, which are still relatively liberal, – and probably even lead to a

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<sup>4</sup> <https://www.economist.com/briefing/2018/01/20/the-teclash-against-amazon-facebook-and-google-and-what-they-can-do>

new cycle of antitrust “tightening”. On the other hand, it is important to accept that more expanded access to goods and services in several markets (due to platforms) contributes not only to the decrease of consumers’ costs but also to the development of competition in adjacent markets because of easier market entry (Ezrachi, Stucke, 2016).

Anyway, we can conclude that there is a set of new “forks” for antitrust authorities in the digital segment, including:

- the problem of information abuse prevention from the side of leading platforms controlling “big data” about the market;
- the problem of regulating platforms bundled with the suppliers acting in multi-sided markets and competing with non-bundled, “independent” suppliers;
- the problem of controlling M&A strategies intended to prevent market entry by prospective start-ups;
- the problem of general attitude to positive network effects through the lens of more restrictive or more tolerant antitrust standards.

The effective solution of those problems may contribute to a full realization of digital economy potential to the benefit of consumers and to the advantage of new technologies.

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