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Competition Law International

Call for submissions

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CLI Speedread

A brief overview of the articles in the December 2020 issue of Competition Law International

Competition implications of the transition to 5G

Dr Will Taylor and Adrien Cervera-Jackson

5G is the next generation of mobile technology. While it promises considerable increases in performance and functionality, it also requires significant investment. This need for new investment arrives at a time when mobile network operator (MNO) revenues and average revenue per user (ARPU) have been flat or declining, while connections and data usage by consumers have been increasing. These trends have put pressure on MNOs to combine (merge) or collaborate (share network assets) in order to achieve investment efficiencies. Both mergers and network sharing agreements (NSAs) have the potential to benefit consumers through increased investment and the dynamic competition benefits they bring, but may also reduce competitive tension, particularly in a more static sense, between MNOs. In this article, we set out the economic basis for this trade-off and discuss recent cases in which these issues have played out around the globe.

An economic perspective on the new South African buyer power provision and enforcement guidelines

Zoë van der Hoven, Paul Anderson and Kagiso Zwane

South Africa recently amended its Competition Act, introducing, among other amendments, a novel provision prohibiting the abuse of buyer power. The novelty of the provision stems from the combination of three features: a public interest focus, a dominance requirement and its application not only to trading terms but prices as well. To address this and provide further clarity, the South African Competition Commission released a set of guidelines outlining the factors or benchmarks for assessing a buyer power abuse. This paper considers the difficulties associated with each of the aforementioned features from an economic perspective, how the guidelines have dealt with each of these and what challenges are likely to remain.

Australia's draft News Media Bargaining Code

Katharine Kemp

Amid the tensions between leading digital platforms and traditional news businesses, the Australian government has produced a novel proposal to use competition law to require designated digital platforms – initially Google and Facebook – to compensate news media businesses for news content. This article explains the origins of the proposed News Media Bargaining Code and developments after the proposal, including reactions from digital platforms. It goes on to analyse crucial provisions of the draft Code in light of criticisms in Australia and approaches in other jurisdictions.

Systems competition – China's challenge to the competition order

Dr Thorsten Käseberg and Dr Sophie Gappa

Do we need new rules to protect a level playing field for competition with firms from non-European Union countries? Although there have been dry spells in international trade policy since the Second World War, there has been a long trajectory towards ever more trade and globalisation, which culminated in the accession of China to the World Trade Organization in 2001. The working assumption that the Chinese economic and social model would converge towards Western models has not materialised. Its model of state capitalism (as of today) raises serious challenges to the EU's order based on economic and personal freedom, competition and individual privacy.

Competition implications of the transition to 5G

Dr Will Taylor and Adrien Cervera-Jackson[1]

Introduction

5G is the next generation of mobile technology. While it promises a step-change increase in performance and functionality compared to 4G and is expected to give rise to a number of new use cases, it also requires significant investment from mobile network operators (MNOs).

However, the business case for 5G investment is unclear. The need for new capital expenditure arrives at a time when MNO revenues and average revenue per user (ARPU) have been flat or declining for several years, while connections and data usage by consumers have been increasing. This is putting pressure on current MNO business models. New use cases that would enable MNOs to monetise 5G are on the horizon, but it is unclear when they will arrive and provide new revenue streams. At this stage, it is also unclear whether the current Covid-19 pandemic will exacerbate these challenges.

These trends are putting pressure on MNOs to combine (merge) or collaborate (share network infrastructure) in order to achieve investment efficiencies, both

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The authors would like to thank Anca Cojoc, Hans Ihle, James Mellsop, Grant Saggers and Bruno Soria for their helpful comments. Valuable research assistance was provided by Kate Eyre and Barbara Kaleff. Any mistakes are the authors' own. The views expressed in this article are those of the authors and do not necessarily represent the views of NERA Economic Consulting or its clients.

of which may raise competition concerns. Both mergers and network sharing agreements (NSAs) have the potential to benefit consumers through increased investment but may also reduce competitive tension between MNOs.

Recent mergers between small MNOs have raised issues about the level of investment that would occur by the parties in the absence of the merger and the ability of the newly created firm to compete against the larger and better-resourced first and second players in each market. This was a key consideration of the courts in both the *Vodafone Hutchison Australia (VHA)/TPG Telecom (TPG)* (Australia) and *Sprint/T-Mobile* (United States) cases.

A frequently occurring consideration is whether alternative arrangements, such as infrastructure sharing, could allow MNOs to achieve similar efficiencies to a merger, but with less harmful effects on competition. NSAs generally benefit consumers in terms of faster rollout, cost savings and improved coverage but they may have a negative impact on competition in some circumstances.

From a competition perspective, infrastructure sharing has traditionally been viewed as more benign than a merger, particularly when it involves the sharing of passive, rather than active, infrastructure.[2] However, recent NSAs have involved more active sharing, which has heightened regulatory scrutiny of those arrangements given the greater risk that active sharing could reduce competition between MNOs – for example, the ongoing European Commission investigation into the NSA between O2 CZ/CETIN and T-Mobile CZ (Czech Republic).

Some mergers can also affect infrastructure sharing. In the proposed H3G/O2 transaction (UK), the Commission and the European General Court ('General Court') assessed the merger's impact on investment by examining its effects on two existing NSAs involving the merging parties.

Mergers and NSAs between MNOs have the potential to benefit consumers through increased investment and the dynamic competition benefits they bring. This increased investment occurs when mergers or NSAs relieve capital constraints and/or lower the per unit cost of expanding the network (due to network or spectrum synergies). In the latter case, this makes investments that are not profitable on a standalone basis profitable.

However, mergers and NSAs may also reduce competitive tension, particularly in a more static sense. The overall effect on investment and consumer welfare (ie, prices and quality) will depend on the specific facts and circumstances of each case. The cases discussed below highlight that for both mergers and NSAs, whether there is a positive impact on investment depends on various factors.

2 'Passive' refers to sharing passive physical infrastructure such as sites and towers, whereas 'active' refers to sharing the active electrical equipment such as the radio access network (RAN), which includes the antennas that transmit signals between a cell tower and a consumer's mobile phone.

With respect to NSAs, the competitive effects also depend on the nature of the sharing (active versus passive), the area covered by the shared network (urban versus rural) and the ownership structure of the network sharing (joint venture versus geo-split agreement).[3]

Economic analysis and evidence have an important role to play in evaluating the trade-off between efficiency gains and anti-competitive effects arising from consolidation and cooperation between MNOs and assessing the overall impact on investment and competition, as demonstrated in the General Court's recent *H3G/O2* judgment.

The remainder of this article is structured as follows. Section 2 explains the basics of mobile network economics and the properties of different spectrum bands, then describes the difference in performance between 5G and 4G. Section 3 sets out the challenges to MNO business models associated with 5G investment, which requires significant capital expenditure at a time when MNO revenues and ARPU have been flat or declining for several years. Section 4 describes the resulting rationale for MNOs to merge or collaborate to achieve investment efficiencies, sets out the trade-off between the potential efficiency gains and anti-competitive effects associated with mergers and NSAs, and discusses recent cases where these issues have been examined around the world. Section 5 concludes on the implications for investment of MNOs merging or collaborating.

What is 5G and how is it different from 4G?

To understand what 5G is, how it differs from 4G and why rolling it out involves large investment from operators requires an appreciation of the economics of mobile network capacity and some fundamentals on the capacity and coverage properties of different spectrum frequency bands.

Beginning with mobile network economics, MNOs have three primary means of increasing the capacity and performance of their network:

1. *More sites:* for a given demand for traffic by customers, increasing the number of 'base stations' decreases the number of customers using a given base station, thus reducing congestion at that base station.[4] To use a traffic analogy, building more cell towers is similar to building additional roads of the same size to enable more traffic to flow.

---

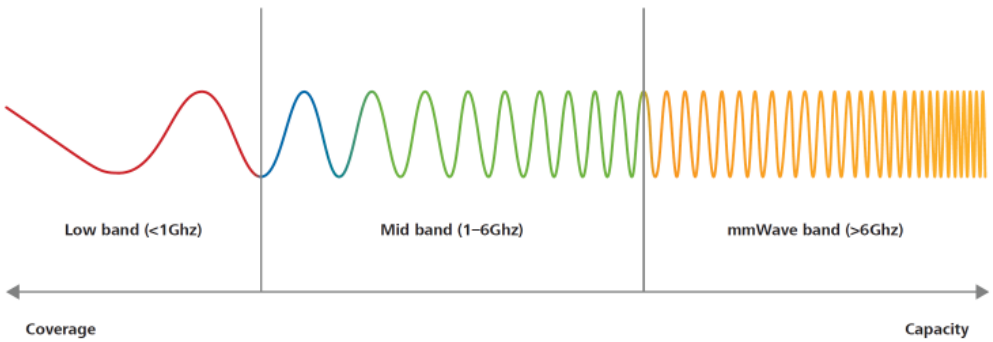
3 'Joint venture' refers to MNOs forming a joint venture company to operate the shared network assets and provide services to the sharing parties, whereas 'geo-split agreement' refers to the geographic separation of the shared network with each MNO operating the network in its respective area.

4 Eg, the towers or sites where equipment is installed and from which it broadcasts.

2. *More spectrum:* for a given base station and technology, the amount of traffic that can be carried is limited by the available spectrum. Therefore, increasing the amount of spectrum available to the MNO increases the capacity of a given base station. Continuing the traffic analogy, more spectrum is similar to widening an existing highway to add extra lanes.
3. *Increased spectral efficiency:* increased spectral efficiency refers to equipment being able to use a given amount of spectrum more efficiently by using another, higher performance modulation technology. Using the traffic analogy, a straight and flat road can carry more traffic at a higher speed than a winding road that travels over hills.

Regarding spectrum, different spectrum bands have different uses, which are broadly determined by the amount of spectrum available in a band (which determines the capacity available in a band) and its 'propagation' characteristics (ie, how far it can travel and the extent a signal is easily blocked by trees, walls, etc). Figure 1 illustrates the broad categorisation of spectrum bands and the purpose they serve.

Figure 1: Spectrum 101: different horses for different courses



Broadly, low-band spectrum (<1Ghz) is typically used for coverage, as the broad wavelengths can travel long distances and are not easily obstructed by walls, trees or other natural features. Because of its long reach, each base station in low band can cover a larger surface than other bands, and thus fewer base stations (and investment) are required to reach a given service coverage. However, in a low frequency band there is not a large amount of spectrum available. For example, in the 700MHz band, there is only 100MHz of spectrum available, which is not a

lot of capacity spread among operators. In Australia, Optus recently noted that there is only 130MHz of sub 1-GHz spectrum licensed for use in mobile services.[5]

By contrast, mmWave spectrum, which has a very narrow wavelength, has a far greater amount of spectrum available in a given band. For example, Verizon in the US acquired more than 1GHz of spectrum in the 39GHz band and holds 1.7GHz across three mmWave bands.[6] However, very high frequency spectrum does not propagate as well as low frequency spectrum, in that it is more likely to be obstructed by natural features of the environment (trees, buildings, hills, etc) and is less able to penetrate walls and windows. Therefore, it provides good capacity but poor coverage. As such, mmWave frequency is being touted as most useful for dense urban deployments.

In between these two extremes, 'mid-band' spectrum provides a balance of both coverage and capacity. As a result of these different characteristics and constraints on spectrum availability, the GSM Association (GSMA – originally Groupe Spécial Mobile) is recommending that regulators aim to make available 80–100MHz of spectrum per operator in 5G mid-bands (eg, the 3.5GHz band) and 1GHz per operator in mmWave bands.[7] The GSMA has also noted that there is a need to identify more spectrum below 1GHz so that rural areas (which are not densely populated and therefore are best economically served using low-band spectrum) benefit from 5G.[8]

5G differs from 4G in that it will increase the spectral efficiency of existing spectrum bands used to provide mobile services, but it will also use mmWave bands, which have not previously been used to provide mobile services. In pure technical performance terms, 5G is a step change compared to 4G (see Figure 2).

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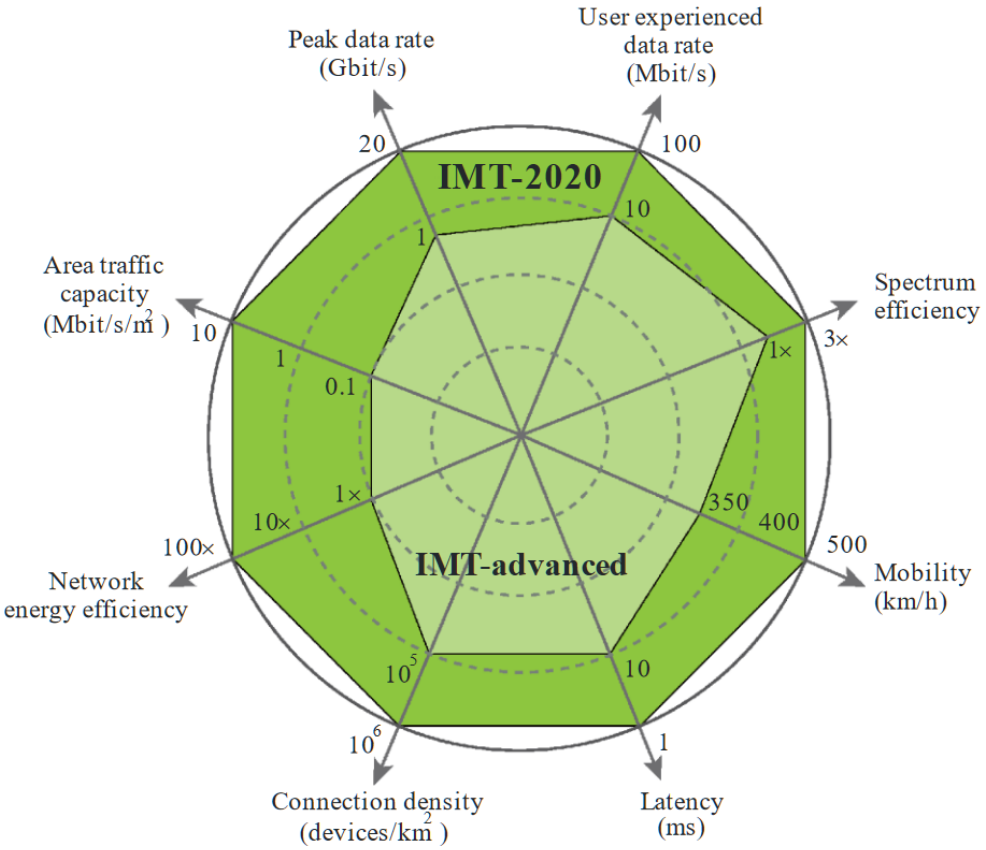
5 Optus owns just 20MHz of low band spectrum, while the other two main players, Telstra and VHA/TPG, own 60 and 50MHz respectively. See *Submission in response to ACCC Discussion Paper – Spectrum Allocation Limits – 26 GHz Band*, Public Version (Optus 2020) para 22.

6 Patrick Welsh, 'Verizon's Millimeter Wave Deployment Experiences' (Presentation at 15th European Spectrum Management Conference, 25 June 2020), available at: www.youtube.com/watch?v=MQ5u8guwPGA, accessed 2 October 2020.

7 GSMA, *5G Spectrum: GSMA Public Policy Position* (GSMA March 2020) p 2.

8 *Ibid*, p 6.

Figure 2: Technical performance of 5G (IMT-2020) versus 4G (IMT-Advanced)

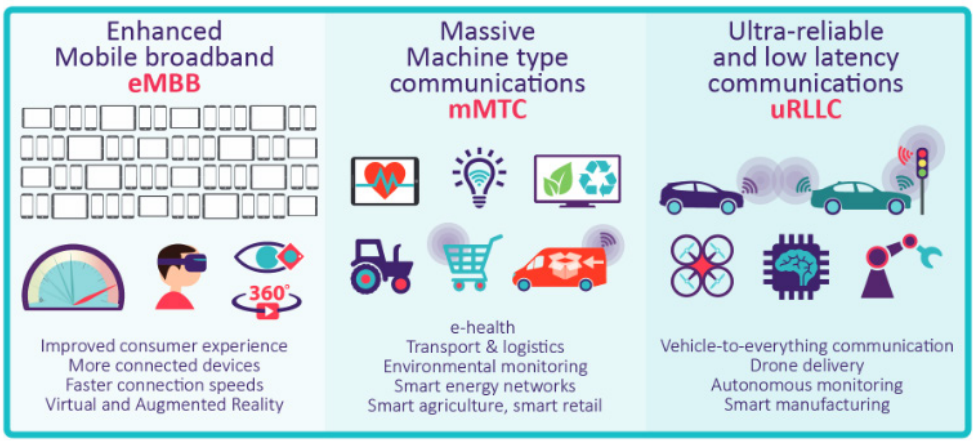


Source: 'Recommendation ITU-R M2083-0' (International Telecommunications Union 2015).

This raw technical performance is slated to do more than merely reduce buffering times or increase video-streaming resolution on consumers' phones. Reduced latency (the response time for two devices to communicate with each other), power efficiency and mobility are expected to give rise to various new use cases such as 'internet of things' (IoT) applications, driverless cars and telemedicine. By improving the capacity and speed of mobile networks, 5G may also make fixed wireless access a substitute for fixed broadband networks for some consumers.[9] Figure 3 from Ofcom (the UK telecommunications regulator) summarises some expected use cases for 5G.

9 Where fixed wireless access refers to providing a fixed broadband service using the mobile network.

Figure 3: 5G use cases



Source: 'Update on 5G spectrum in the UK' (Ofcom 2017).

5G will cost a lot, and the MNO business case isn't clear

While 5G promises much for consumers and the economy more generally, it is also likely to require significant capital expenditure from MNOs, over and above the normal costs that operators incur in upgrading equipment. Two key reasons for this include:[10]

1. the key spectrum bands for 5G (the 'C-band' and mmWave spectrum) are not currently owned or used by MNOs;[11] and
2. a much denser network of base stations is likely to be required to deliver true 5G speeds, due to the poor propagation characteristics of mmWave spectrum.[12]

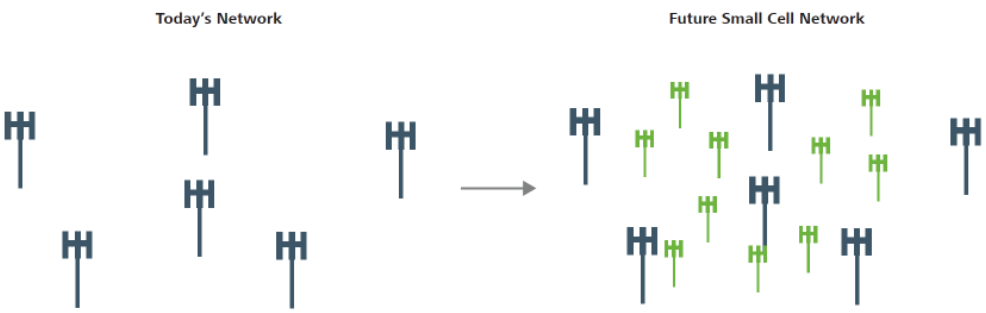
10 See Jeffrey A Eisenach and Robert B Kulick, 'Economic Impacts of Mobile Broadband Innovation: Evidence from the Transition to 4G' (2020) SSRN. According to Eisenach and Kulick, 5G will likely enhance the consumer-oriented mobile broadband use cases made possible by 4G and will extend commercial application of mobile wireless technology to business and industrial use cases not possible with previous technology, including enabling the IoT. They estimate that if 5G adoption follows the same path as 4G adoption, at its peak 5G will contribute approximately three million jobs and $635bn in GDP to the US economy. See also Majed Al Amine et al, 'Smart Cities: How 5G Can Help Municipalities Become Vibrant Smart Cities' (Accenture Strategy 2017) and 'Impacts of 5G on Productivity and Economic Growth' (Australian Bureau of Communications and Arts Research 2018).

11 The C-Band refers to 3.5GHz spectrum, which is expected to be the key international band for initial 5G roll outs.

12 Ferry Grijpink et al, 'The road to 5G: The inevitable growth of infrastructure cost' (McKinsey & Company, 23 February 2018).

The second point is illustrated in Figure 4, which shows stylistically how the topology of networks might change as mmWave spectrum is deployed.

Figure 4: Change in network topology from rolling out 5G mmWave technology

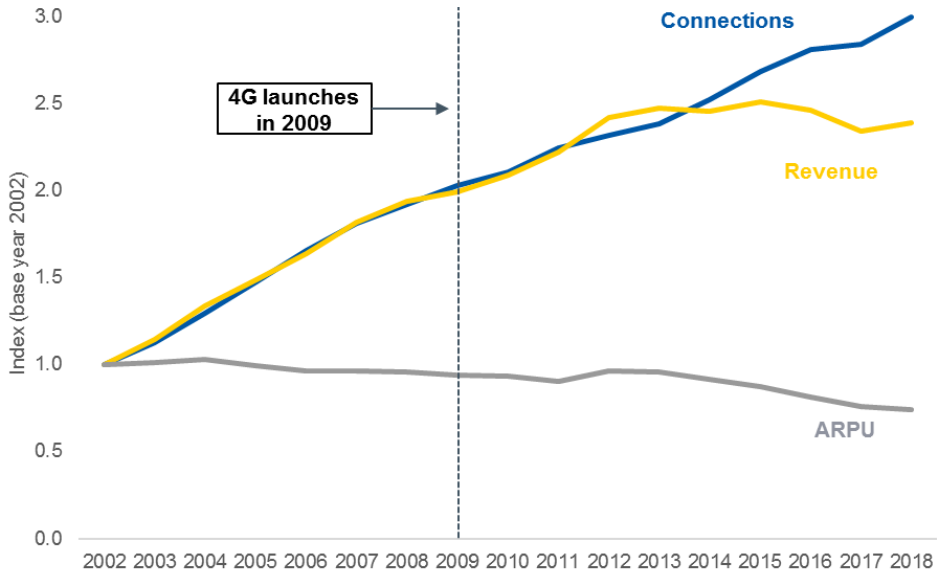


Therefore, operators will need to construct and operate a network with many more base stations than they presently operate. McKinsey estimates that the additional total cost of ownership (ie, opex and capex) could peak at between 60 per cent and 300 per cent of current spend, depending on data growth rates.[13] Clearly, the additional costs of 5G are substantial.

While operators are expected to incur large costs in rolling out a 5G network in the future, revenue and ARPU have been flat or falling in recent years. Figure 5 plots indexes for the number of connections, ARPU and revenue for wireless carriers in the US. Interestingly, mobile connections and revenue were closely correlated until around 2011, after which connections have continued to grow but mobile revenue has remained relatively flat. As a result, ARPU has been declining over the same period. A similar pattern holds for Europe, as demonstrated by Figure 6, which shows a similar fall in mobile ARPU since 2011, while fixed broadband ARPU has remained relatively stable.

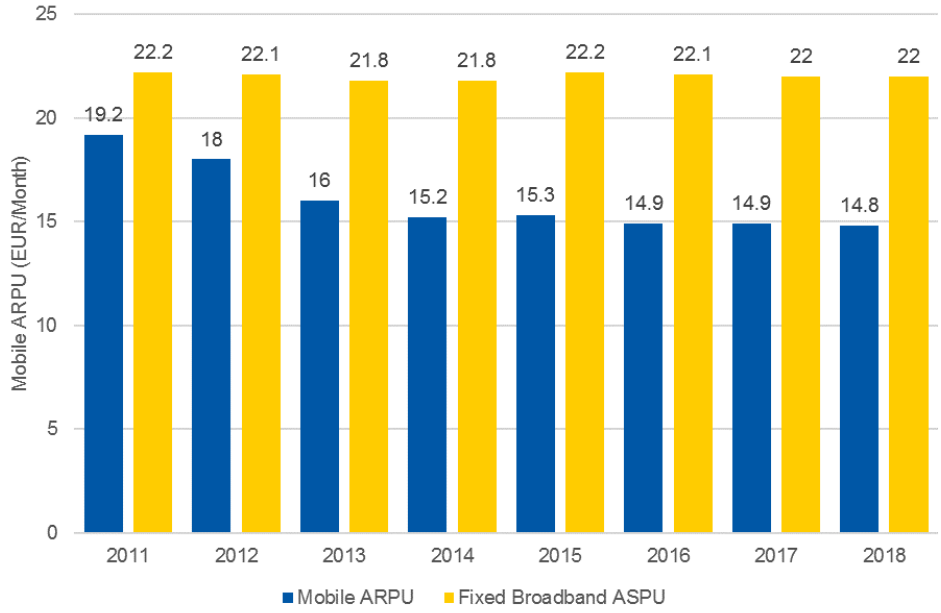
13 *Ibid.*

Figure 5: Mobile revenue has been relatively flat in the US, while mobile ARPU has been falling since 2012



Source: 'Topline results of the 2018 Cellular Telecommunications and Internet Association Wireless Industry Survey' (CTIA 2019).

Figure 6: Mobile ARPU has been falling in Europe, while fixed ARPU has remained stable

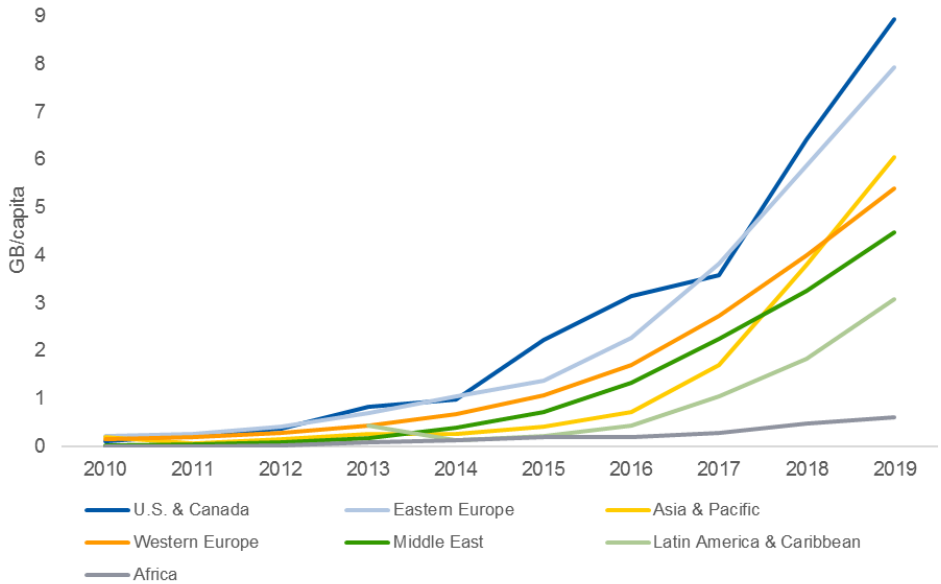


Source: 'The State of Digital Communications 2019' (ETNO Annual Economic Report 2019).

Falling ARPU, which likely reflects lower-quality adjusted prices, is not necessarily a bad thing from a societal perspective.[14] To the extent that competition is driving lower prices and higher-quality products, it is, in fact, a good thing. The exponential increases in data consumption, in conjunction with increased speeds as new technologies are rolled out (see Figures 7 and 8), suggests that consumers are benefiting greatly. Falling ARPU could also be the result of a change in connection mix. For example, an increase in low-revenue IoT and machine-to-machine connections could materialise as both a decrease in ARPU and an increase in total revenue since it represents a new revenue stream.

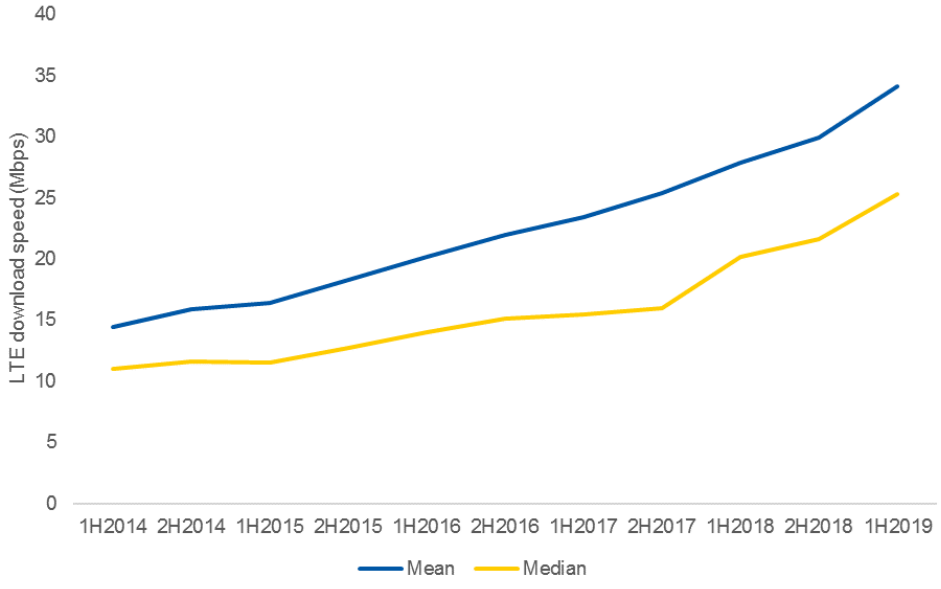
14 ARPU can fall either because consumers purchase lower-priced, lower-quality plans, or because prices for a given level of quality fall.

Figure 7: Average monthly mobile data traffic (GB per month per capita)



Source: Authors' analysis of Telegeography's GlobalComms database.

Figure 8: Mean and median total long-term evolution (LTE) download speeds in the US



Source: 'Communications Marketplace Report 2018: 20 February 2020 data update' (FCC 2020).

However, falling ARPU could also reflect that consumer willingness to pay for ever-increasing mobile speeds and capacity provided by new generations of technology has reached a ceiling. The increased expenditure requirement at a time when revenue is falling or flat is, therefore, putting pressure on existing MNO business models.

Of course, historic falling revenue is not a problem if consumers are willing to pay more for 5G, either by existing mobile users paying a premium or through developing new use cases that create new revenue streams. At this stage, it is unclear whether MNOs will be able to charge a material premium for 5G. For example, a number of operators are not charging a premium for 5G[15] and a 2018 survey found that fewer than one-third of Americans would be willing to pay a premium for 5G.[16] Of course, MNOs do not need to charge an explicit premium for 5G if they can achieve the same outcome by selling higher data allowance packages that are 5G-only (in effect, bundling 5G and large data caps) at a higher price. To the extent market practice moves towards plans with no data caps, this would be a difficult pricing strategy to implement.[17] However, more recent surveys by equipment vendors have found that consumers would be willing to pay a premium for 5G.[18] As previously noted, 5G promises new use cases, which should result in new revenue streams for operators, but it is not clear when these new use cases will arrive.

The impact of the current Covid-19 pandemic on MNOs is unclear. While fixed-line traffic appears to have increased dramatically as people spend more time at home,[19]

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15 Eg, when Vodafone launched 5G offers in the UK in 2018 and when T-Mobile launched its 5G offer, neither charged more for 5G. See John McCann, 'Vodafone 5G turned on in 7 cities and it's the same price as 4G' (TechRadar, 3 July 2019); 'T-Mobile 5G: It's On! America's First Nationwide 5G Network Is Here' (T-Mobile, 2 December 2019), at: www.t-mobile.com/news/press/americas-first-nationwide-5g-network, accessed 1 October 2020. Telstra in Australia recently reversed a planned decision to charge users more for 5G. See Chris Duckett, 'Telstra ditches 5G fee for users not on lowest tier plan' (ZDNet, 30 June 2020), at: www.zdnet.com/article/telstra-ditches-5g-fee-for-users-not-on-lowest-tier-plan, accessed 1 October 2020.

16 PwC, 'The promise of 5G: Consumers are intrigued, but will they pay?' (PwC 2018) p 8.

17 Eg, Spark, the largest MNO in New Zealand, has relaunched its mobile plans to have 'endless data', whereby there are no overage charges but the maximum speed reduces after a certain threshold. See 'Spark's Best Value Endless Mobile plans', at: www.spark.co.nz/shop/mobile-plans/endless-mobile#, accessed 1 October 2020.

18 A study by Ericsson notes that smartphone users say they are willing to pay a 20 per cent premium for 5G. See '5G consumer potential: Busting the myths around the value of 5G for consumers' (Ericsson 2019). Another study by Nokia found that around two-thirds of survey respondents said they would pay up to five per cent more for 5G, and just over half said they would even be willing to pay up to ten per cent more. See 'The value of 5G services: Consumer perceptions and the opportunity for CSPs' (Nokia 2020).

19 Eg, NBNco in Australia estimates Covid-19 has increased its traffic baseline levels by 75 per cent. See 'Network usage COVID-19' (NBN 2020), at: www.nbnco.com.au/corporate-information/about-nbn-co/updates/dashboard-may-2020, accessed 17 July 2020.

this could result in a reduction in mobile traffic as consumers spend more time connected to Wi-Fi.[20] However, while some operators are reporting declines in mobile traffic during the pandemic,[21] others are reporting increases.[22] Declines in mobile traffic may reduce the pressure on an operator to upgrade to 5G from a network capacity perspective. A recession may also place financial strain on operators, as some customers disconnect or downgrade their plans as a result of financial hardship.[23] However, if mobile traffic does increase, 5G may be a more cost-effective way of expanding network capacity. Therefore, the Covid-19 pandemic may exacerbate some of the pressures described earlier in this section, though the impact is presently unclear.

As a result, MNOs are combining and collaborating, with competition implications

The previous section describes the financial pressures MNOs are facing as a result of flat revenues, falling ARPU, increased consumer data demand and the impending investment required for 5G. As a result of these pressures, four broad trends are observed:

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20 Open Signal has found significant increases in the percentage of time smartphone users spend connected to Wi-Fi instead of their mobile networks. See Hardik Khatri and Sam Fenwick, 'Analyzing Mobile Experience during the coronavirus pandemic: Time on Wifi' (Open Signal, 30 March 2020), at: www.opensignal.com/2020/03/30/analyzing-mobile-experience-during-the-coronavirus-pandemic-time-on-wifi, accessed 1 October 2020.

21 Eg, AT&T in the US reports that '[m]obile data volume has slightly decreased during COVID-19 since people are able to connect to their home Wi-Fi throughout the day'. See Scott Mair, '6 Months In: Unyielding Connections in the Age of COVID-19' (AT&T, 16 September 2020), at: https://about.att.com/innovationblog/2020/09/fn_covid_19_six_months.html, accessed 1 October 2020.

22 Telecom Italia reported a traffic increase of ten per cent on its mobile network in the space of two weeks. Similarly, the five largest operators in Spain reported a 40 per cent increase in overall IP traffic, a 25 per cent increase in mobile traffic and a 50 per cent increase in mobile voice traffic since the start of the outbreak. See Rupert Wood, 'COVID-19: operators should be concerned about the robustness of networks rather than capacity' (Analysys Mason, 23 March 2020).

23 In Australia, Optus and Vodafone have implemented a range of customer support initiatives, including boosting mobile data allowances, bill waivers for health workers and three-month duration capped fee plans. See 'Optus continues to support customers affected by Covid-19' (Optus, 24 April 2020), at: www.optus.com.au/about/media-centre/media-releases/2020/04/optus-continues-to-support-customers-affected-by-covid-19, accessed 1 October 2020; 'Vodafone extending support for customers experiencing hardship' (Vodafone, 17 April 2020), at: www.vodafone.com.au/media/vodafone-extending-support-for-customers-experiencing-hardship, accessed 1 October 2020.

1. European MNOs have been spinning off their tower businesses to third parties to free up cash;[24]
2. open access/third-party neutral carriers have entered the market and begun to sell network capacity to MNOs;[25]
3. smaller MNOs have been merging and combining with larger rivals, including two recently litigated four-to-three mergers in the US and Australia and the 'four-to-three wave' that hit Europe in 2012 (ie, cleared acquisitions in Austria, Germany, Ireland, Italy and the Netherlands; a blocked transaction under appeal in the UK; and an abandoned deal in Denmark);[26] and
4. MNO infrastructure sharing, which traditionally involved only passive infrastructure, is moving up the value chain into active infrastructure.

The first two trends are expected to be largely pro-competitive and, therefore, aren't the focus of this article.[27] The remainder of this article considers the impact

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24 Telefonica has created a specialised subsidiary business unit, Telxius, better to utilise its tower business. Similarly, Vodafone has invited offers for a part-sale of its infrastructure arm, Vodafone Towers Europe. See Jamie Davies, 'Telefonica sells €1.5bn tower assets to Telxius in debt reduction mission' (Telecoms.com, 9 June 2020), at: https//:telecoms.com/504856/telefonica-sells-e1-5bn-tower-assets-to-telxius-in-debt-reduction-mission, accessed 1 October 2020; Joseph Purnell, 'Vodafone pushes ahead with tower IPO' (TelcoTitans, 23 June 2020), at: www.telcotitans.com/vodafonewatch/vodafone-pushes-ahead-with-tower-ipo/1793.article, accessed 1 October 2020.

25 Dense Air, an optimised network densification and network extension service that provides services on a 'Neutral Host' basis, has partnered with Spark to launch 5G services in New Zealand. See 'Dense Air Partners With Spark to Launch 5G Services' (Cision, 26 September 2019), at: www.prnewswire.com/news-releases/dense-air-partners-with-spark-to-launch-5g-services-300926129.html, accessed 1 October 2020.

26 Since 2012, the Commission has cleared five four-to-three mergers in the mobile sector (the first four subject to conditions and the latest unconditionally): (1) *Hutchison 3G Austria/Orange Austria* [2012] Case No COMP/M.6497; (2) *Hutchison 3G UK/Telefónica Ireland* [2014] Case No COMP/M.6992; (3) *Telefónica Deutschland/E-Plus* [2014] Case M.7018; (4) *Hutchison 3G Italy/WIND/JV* [2016] Case M.7758; and (5) *T-Mobile NL/Tele2 NL* [2018] Case M.8792. However, over the same period, the Commission prohibited the proposed four-to-three merger between Hutchison 3G UK (Three) and Telefónica UK (O2) in the UK in 2016 (subsequently overturned by the General Court in a May 2020 judgment, which the Commission has said it will appeal at the Court of Justice of the EU) and the proposed merger between TeliaSonera and Telenor's respective business units in Denmark was abandoned in 2015 after the parties were not able fully to address the Commission's competition concerns. See *Hutchison 3G UK/Telefónica UK* [2016] Case M.7612; *CK Telecoms UK Investments v European Commission* [2020] Case T-399/16 (General Court of the EU); and *TeliaSonera/Telenor/JV* [2015] Case M.7419.

27 To the extent that both involve the provision of open access wholesale infrastructure, they are unlikely to result in competition concerns. Consolidation in the tower sector might raise concerns if an acquisition of towers would create a near monopoly and it was determined that there are barriers to entry in the towers segment.

on investment of the latter two trends: MNOs merging and sharing infrastructure.[28] The prospect of gaining a first mover advantage may give some MNOs incentives independently to invest in 5G infrastructure (eg, Everything Everywhere launched the UK's first 5G service in six cities in May 2019). However, the scale of the investment required and the uncertainty associated with consumer willingness to pay for 5G mean the incentives might not be the same for all MNOs. There may be a benefit for some MNOs to wait for this demand uncertainty to be resolved (ie, a second mover advantage) by observing how successful the initial investment is before investing themselves, either independently or jointly with other MNOs.

The impact of two recent four-to-three mergers on 5G investment

Beginning with mergers, 5G network investment was at the heart of two recently litigated four-to-three mergers:

1. Sprint/T-Mobile: T-Mobile and Sprint were the third and fourth players respectively in the US mobile market. Following a settlement with the Department of Justice on 26 July 2019, subject to divestment undertakings, the merger was unsuccessfully challenged by state Attorneys General in the Southern District Court of New York;[29]
2. VHA/TPG: VHA and TPG were the third and fourth players respectively in the Australian mobile market. In the fixed market, TPG was the third player and VHA was the fourth. Following a statement on 8 May 2019 that the Australian Competition and Consumer Commission (ACCC) intended to oppose the merger,[30] VHA sought a court declaration that the proposed

28 A number of papers have empirically analysed the impact of MNO consolidation on investment in mobile markets. Eg, Genakos, Valletti and Verboven (2018) studied the dual relationship between market structure and prices and between market structure and investment in mobile markets, using a uniquely constructed panel of MNOs' prices and accounting information across 33 Organisation for Economic Co-operation and Development countries between 2002 and 2014. The authors found that more concentrated markets lead to higher end-user prices and to higher investment per mobile operator, though the impact on total industry investment is not conclusive. See Christos Genakos, Tommaso Valletti and Frank Verboven, 'Evaluating market consolidation in mobile communications' (2018) 33(93) *Economic Policy* 45–100. The GSMA has also published several papers assessing the impact of MNO consolidation on mobile market performance. Eg, the GSMA (2020) examined how European mobile markets performed during the 4G era, in particular how different market structures affected network quality, coverage and investment. The GSMA found that in this time, markets with more concentrated market structures were able to deploy 4G more quickly and were better at delivering higher performances. See Serafino Abate et al, *Mobile market structure and performance in Europe, Lessons from the 4G era* (GSMA 2020).

29 'Justice Department Settles with T-Mobile and Sprint in Their Proposed Merger by Requiring a Package of Divestitures to Dish' (US Department of Justice, 26 July 2019); Hilary Russ, 'New York drops fight against T-Mobile-Sprint merger' (Reuters, 17 February 2020), at: www.reuters.com/article/us-sprint-corp-m-a-t-mobile-appeal/new-york-drops-fight-against-t-mobile-sprint-merger-idUSKBN20A0MS, accessed 2 October 2020.

30 'ACCC opposes TPG VHA merger' (ACCC, 8 May 2019), at: www.accc.gov.au/media-release/accc-opposes-tpg-vha-merger, accessed 2 October 2020.

acquisition would not substantially lessen competition. The court found in VHA's favour on 13 February 2020.[31]

In both of these transactions, a key analytical question pertained to the level of investment that would be made by the parties in the absence of the merger and the ability of the newly created firm to compete against the larger and better-resourced first and second players in each market. In both situations, it was argued that the proposed merger between the third and fourth player would create a stronger third player that would provide a greater competitive constraint than the two firms would be able to provide separately.[32] This argument ultimately prevailed in both cases, though not without contentious litigation and, in the case of *Sprint/T-Mobile*, an undertaking to set up Dish as a fourth player.

There are a number of conceptual reasons why a merger might lead to increased investment, which are set out below, along with commentary from the *VHA/TPG* and *Sprint/T-Mobile* judgments:

Increased scale and scope improve the business case for investment in common/shared network assets

Many investments in telecommunications networks are lumpy and fixed costs are high. Combining two mobile networks or a fixed and a mobile network (as was the case with *VHA/TPG*) improves the business case for investment in shared infrastructure, since the same costs are spread over more customers. The *VHA/TPG* decision states that 'MergeCo will benefit financially from achieving scale. Scale is important for MNOs, as it enables the fixed costs of providing coverage to be recovered across a larger number of customers'.[33] Related to these cost savings, the decision states, 'Further, I do not consider that MergeCo would use its net profit after tax to pay dividends to its shareholders or to pay down debt, at the expense of using its financial firepower to invest in its network or compete for market share'.[34]

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31 *Vodafone Hutchison Australia Pty Limited v Australian Competition and Consumer Commission* [2020] FCA 117.

32 There is a nuance in *VHA/TPG*, in that one of the parties' arguments was that TPG was not actually going to roll out a full mobile network, given its investment plans had been disrupted by the government's decision to ban Huawei from supplying equipment to Australia's 5G networks. The court accepted this argument, noting 'The existing fact is that TPG has no business case for rolling out a mobile network, and has indicated it will not do so absent the merger.' See *ibid*, paras 471 and 897; see *New York v Deutsche Telekom AG* [2020] 19 Civ 5434 (VM) (SDNY 21 February 2020) 161.

33 See n 31 above, para 844.

34 *Ibid*, para 849.

Relieving capital constraints

In both *VHA/TPG* and *Sprint/T-Mobile*, a key issue was the ability of one of the players to finance investment absent the merger. In *VHA/TPG*, the evidence suggested that VHA was facing financial difficulties that wouldn't be resolved absent the merger, which impacted its ability to invest. The judge stated, 'it seems Vodafone faces financial difficulties that are unlikely to materially change absent the merger, and those financial difficulties will limit the extent to which Vodafone can invest in, and grow its business, in the counterfactual.'[35]

However, the merged entity would have an improved ability to fund network investment due to an improved balance sheet, improved access to debt and equity funding, cost synergies and financial benefits from economies of scale.[36] In relation to an improved balance sheet, the judge stated 'MergeCo would have a stronger balance sheet than either TPG or Vodafone separately. This would provide MergeCo with the capacity to invest strongly in its mobile assets, including by raising equity capital if necessary, and to roll-out 5G services and reduce network congestion more quickly.'[37]

The *VHA/TPG* decision also asserted that the increased ability to invest would allow a faster rollout of 5G, stating 'MergeCo's ability to invest additional capex in its network will enable it to offer high-quality 5G services to customers far sooner than Vodafone or TPG would be able to alone. In doing so, MergeCo will have the opportunity to become a more effective competitive constraint on Telstra and Optus.'[38]

Similarly, in *Sprint/T-Mobile*, the District Court was concerned with the viability of Sprint as a competitor given its financing issues, stating: 'The weight of the evidence at trial establishes that Sprint is caught in a vicious cycle caused by its inability to finance meaningful network investment, which perpetuates a low-quality network that drives away customers and limits Sprint's ability to generate the cash necessary to reduce its financial constraints.'[39]

Noting the narrow applicability of this 'weakened competitor' defence,[40] the District Court explored whether there were any competitive means other than

35 *Ibid*, para 677.
36 *Ibid*, paras 829–53.
37 *Ibid*, para 829.
38 *Ibid*, para 854.
39 *Deutsche Telekom* (see n 32 above) 101.
40 The 'weakened competitor' defence is the argument that a merging party will not be able to compete effectively on their own in the future and therefore the merger is less likely to have an anti-competitive effect. *Deutsche Telekom* (see n 32 above) 84.

the merger to resolve Sprint's competitiveness issues, ultimately concluding that there was not.[41]

COMBINING SCARCE SPECTRUM HOLDINGS INCREASES NETWORK CAPACITY AND LOWERS NETWORK BUILD COST

As noted above, network capacity can be increased by increasing the number of sites, investing in more efficient equipment (eg, upgrading to 5G) or increasing spectrum holdings. Increasing spectrum holdings increases the capacity of the existing network, but also means the capacity provided by any new investments also increases. In this sense, increased spectrum holdings reduce the incremental cost of expanding capacity. This was the case in *Sprint/T-Mobile*, with the judge stating:

> 'The undisputed evidence at trial reflects that combining Sprint and T-Mobile's low-band and mid-band spectrum on one network will not merely result in the sum of Sprint and T-Mobile's standalone capacities, but will instead multiply the combined network's capacity because a technological innovation referred to as "carrier aggregation" and certain physical properties governing the interaction of radios.'[42]

There is a further benefit if the spectrum holdings are contiguous, since this would also eliminate the need for 'guard bands' and thus increase the total amount of usable spectrum.[43] VHA and TPG had complementary spectrum holdings in a number of different bands. The decision noted that combining spectrum could lead to benefits, including the reduced need for 'overhead control'[44] and reduced congestion on the merged network.[45] The *VHA/TPG* decision explicitly recognised that the increased network capacity resulting from the merger would release funds which could then be redirected to accelerating the 5G rollout:

> 'The increase in the capacity of MergeCo's network will reduce the need to build additional sites or conduct "tactical" 4G upgrades to relieve immediate congestion issues, a substantial proportion of which is inefficient as it would need to be also replaced in the near future. That will release additional capex which can be directed towards accelerating MergeCo's 5G roll-out.'[46]

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41 *Deutsche Telekom* (see n 32 above) 86.

42 *Ibid,* 60.

43 To prevent interference, 'guard bands' of unused spectrum exist between adjacent bands used by different operators. If combined spectrum holdings are adjacent, guard bands are eliminated to create a contiguous block.

44 Some bandwidth is used to manage data flows, redundant with two separate networks. The overhead requirements are thus reduced with a single network.

45 See n 31 above, paras 795–800.

46 *Ibid,* para 859.

Combining spectrum in different bands allows an appropriate balance of coverage and capacity, reducing network build costs

As described above, different spectrum bands have different uses, with low-frequency spectrum providing superior coverage but low capacity and high-frequency spectrum providing poor coverage but high capacity. In *Sprint/T-Mobile*, T-Mobile had substantial low-band spectrum that Sprint lacked, while Sprint had substantial mid-band spectrum that complemented T-Mobile's holdings. The parties argued that having a broader spectrum portfolio would allow more efficient spectrum use (ie, using low-band in areas where mid-band could not reach), leading to cost efficiencies, since low-band spectrum can provide greater coverage with fewer sites:

> 'Apart from capacity and cost benefits, Defendants claim that New T-Mobile will provide better coverage than Sprint customers currently receive because T-Mobile's low-band spectrum covers a broader range and penetrates through buildings more effectively than Sprint's mid-band holdings can. Having a broad range of spectrum would allow New T-Mobile to dedicate each band of spectrum to its best use; it could prioritize the use of low-band in areas that mid-band and mmWave could not reach, while instead prioritizing the other two bands in areas correspondingly closer to the cell sites.'[47]

There are, of course, other impacts on competition besides the investment effects described above, including a reduction in competitive tension from having fewer players in the market (both at the network and retail level). Any pro-competitive effects of investment must be weighed against potential competitive detriments to determine whether, on balance, the merger is pro- or anti-competitive.

Another issue that could arise is whether the efficiencies described above are 'merger-specific'. Put another way, could the efficiencies be achieved by an alternative arrangement that does not involve a full merger? Indeed, in *VHA/TPG* the economic expert for the ACCC argued that the benefits described above were not merger-specific given they could be achieved outside of the merger by an NSA. This argument was rejected as it was raised as a hypothetical possibility, without consideration of the specifics of what an NSA might look like between VHA and TPG and whether it would replicate the benefits of the merger.[48]

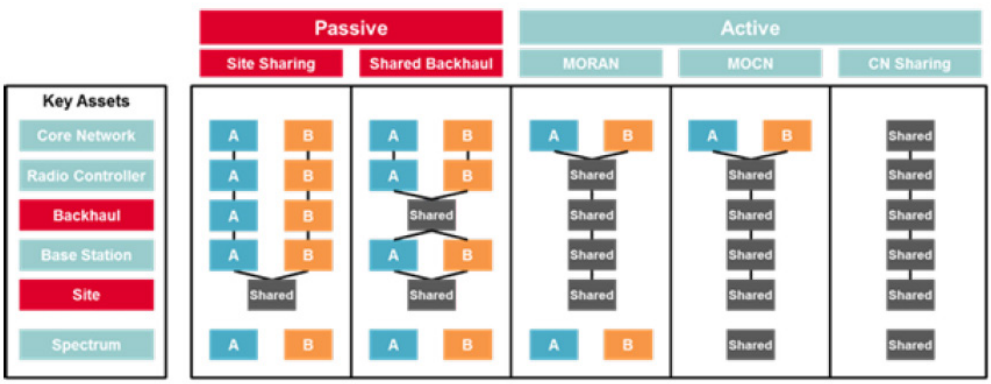
The potential effects of NSAs on 5G investment

It has been argued by regulators (including the European Commission) that NSAs could allow MNOs to achieve the same efficiencies as a merger, but with less harmful

47 *Deutsche Telekom* (see n 32 above) 62.
48 See n 31 above, para 704.

effects on competition at the retail level.[49] For this reason, NSAs have typically been considered less problematic from a competition perspective, particularly those that involve passive, rather than active, sharing of infrastructure. 'Passive' refers to sharing passive physical infrastructure (such as sites and towers), whereas 'active' refers to sharing the active electrical equipment (such as the radio access network (RAN), which includes the antennas that transmit signals between a cell tower and a consumer's mobile phone).[50] Within active and passive there are also different NSA models, which involve sharing different assets. Figure 9 provides an overview of models of sharing.

Figure 9: Overview of passive and active infrastructure sharing models



Notes: Site sharing is sharing of physical sites of base stations and shared backhaul is sharing of transport networks from radio controller to base stations. MORAN (Multi-Operator Radio Access Network) is where RANs are shared and dedicated spectrum is used by each sharing operator; MOCN (Multi-Operator Core Network) is sharing of RANs and spectrum; and CN Sharing (Core Network Sharing) is sharing of servers and core network functionalities.

Source: 'Infrastructure Sharing: An Overview' (GSMA 2019).

NSAs allow multiple MNOs to use the same physical infrastructure for the provision of mobile services. While such cooperation can generate efficiencies by lowering costs, and thus increasing coverage and/or speeding up network rollout, there may

49 *Hutchison 3G Italy/WIND/JV* (see n 26 above), paras 1417, 1422, 1426, 1508 and 1630.

50 GSMA defines passive and active infrastructure sharing as follows: 'passive' is sharing of non-electronic infrastructure at a cell site (eg, power supply and management system) and physical elements (eg, backhaul transport networks); 'active' is sharing of electronic infrastructure of the network, including the RAN (ie, antennas/transceivers, base station, backhaul networks and controllers) and the core network (servers and core network functionalities). See GSMA, 'Infrastructure Sharing: An Overview' (GSMA 2019).

be concerns that such cooperation softens competition by reducing the sharing parties' incentives to invest and their ability to compete, or raising the risk of tacit coordination between the sharing parties.[51] The net impact of NSAs on competition depends on the balancing of efficiencies and potential anti-competitive effects.

NSAs can generate pro-competitive effects

An NSA reduces the costs of infrastructure as it avoids duplication of some network elements. Depending on the degree of sharing, the sharing parties may only need to build out one set of sites to enable each other to provide coverage to their respective customers. As the unit cost of a higher-capacity shared site is lower than the cost of two standalone sites at half the capacity, there will be lower capex and opex from building one shared network rather than two fully independent networks.[52]

To the extent that the reduced costs of network infrastructure lower MNOs' marginal (ie, variable) costs, MNOs have greater incentives to pass cost savings on to consumers by lowering prices and/or improving quality.[53] Fixed cost savings can also benefit consumers if, for example, the additional cashflows result in more investment.[54]

The reduced costs of building and maintaining network infrastructure may also enable the sharing parties to increase quality of service by building a denser network than they otherwise would have found profitable to provide individually.

However, NSAs can also give rise to anti-competitive effects

An NSA may result in unilateral effects if it unduly restricts the ability of the sharing parties to differentiate their networks and offers at the retail level, or it may give rise to coordinated effects if the increased transparency and symmetry between the sharing parties facilitates tacit collusion in the retail market.

- *Unilateral effects:* Under certain circumstances, an NSA may restrict the ability and reduce the incentives of the sharing parties to differentiate their services (by hindering network quality improvements or delaying deployment of new technologies) compared to a counterfactual, where the parties roll out independent networks. The extent to which this may raise concerns will depend on the closeness of competition between the sharing parties and the

51 See, eg, 'BEREC Common Position on Mobile Infrastructure Sharing' (BEREC, 13 June 2019) pp 8–11.

52 Frank P Maier-Rigaud, Marc Ivaldi and C-Philipp Heller, 'Cooperation Among Competitors: Network Sharing Can Increase Consumer Welfare' (2020) SSRN 8–9, at: https://papers.ssrn.com/abstract=3571354, accessed 2 October 2020.

53 See n 51 above, p 9.

54 See n 31 above, para 893.

competitive constraints imposed by remaining MNOs. MNOs with an NSA may still be able to differentiate their services if there are differences in spectrum holdings between the parties and if they retain the operational freedom to deploy additional spectrum, technologies and sites on a standalone basis.[55] The degree of operational freedom depends on the model of network sharing adopted and the assets that are shared (see Figure 9 above). Even with network sharing at the wholesale level, MNOs can still differentiate their services at the retail level.

- *Coordinated effects:* Awareness of each other's investment plans (given the need to jointly plan common infrastructure) may increase the shared parties' ability to predict and respond to the other's competitive behaviour, which may facilitate tacit collusion. In addition, due to the joint operation of network infrastructure, there may be some commonality of costs, which may further enhance the ability of parties to tacitly collude.[56]

This trade-off between potential pro-competitive and anti-competitive effects was recognised by the General Court in its recent judgment annulling the European Commission's decision to block the proposed merger of Hutchison 3G UK and Telefónica UK in the UK:

> 'According to the Commission's decision-making practice relating to Article 101(1) and (3) TFEU, network-sharing agreements, which involve the pooling of certain infrastructures, present, from that point of view, competitive risks which vary according to the context and whether the type of sharing is active or passive. Depending on the method of cooperation chosen, the independence of operators and the risk of collusion are more or less prevalent and the risks of undermining competition are more or less significant. At the same time, network-sharing agreements may produce substantial economic benefits in terms of costs savings, improved coverage, and faster network roll-out.' [57]

As explained above, cost reduction is a driver for MNOs to engage in infrastructure sharing. The Body of European Regulators for Electronic Communications (BEREC) considers that the extent of cost savings from network sharing is likely to differ depending on the type of technology that is shared (ie, 5G versus 4G), the areas where sharing takes place (ie, urban versus rural) and when the sharing is implemented (ie, greenfield versus network consolidation).[58] The benefits of infrastructure sharing include potential cost savings and associated acceleration of coverage for areas where the coverage costs for a single operator deployment is high, which often applies to rural areas.[59] Indeed, the European Commission has

55 See n 52 above, p 11.
56 *Ibid*, p 9.
57 *CK Telecoms* (see n 26 above), para 339.
58 See n 51 above, p 9.
59 BEREC, 'BEREC Report on infrastructure sharing' (BEREC 2018) 15.

recognised that coverage in rural areas is a benefit of network sharing.[60] Because of this, regulators have typically considered that NSAs covering rural areas are more justified than those covering more densely populated urban areas. However, with the increased network density of base stations required for 5G, costs of rolling out a 5G network in urban areas are likely to increase and so the potential cost savings associated with network sharing in urban areas will likely be higher. Going forward, the investment costs associated with 5G are likely to result in more NSAs in urban areas.

It is often suggested that passive sharing is likely to be less problematic than active sharing, even though both have similar benefits in terms of reducing the sharing parties' costs (though there may be greater magnitude of cost savings in the case of active sharing).[61] The concern is that active sharing, which goes beyond the sharing of passive infrastructure (such as sites and masts) and includes active components of the RAN (such as antennas and base stations), may allow sharing parties to weaken competition if active sharing is more likely to restrict their ability to differentiate their networks and services.[62]

Concerns about an inability to differentiate services due to active NSAs may also decline under 5G. This is because under 5G, service characteristics and quality are likely to be determined more by software and the core network (which typically sits outside of NSAs – see Figure 9) than the radio equipment installed at towers.[63] Network slicing will also allow multiple virtual networks to operate over a single physical network.[64] This will allow MNOs using the same network to define different virtual networks with different quality characteristics targeted at different use cases and customers. Therefore, under 5G, parties to an NSA are likely to have more freedom to differentiate their products than would have been the case under previous generations of network technology.

The number of active NSAs globally has increased in recent years (see Figure 10). As NSAs have involved more active sharing elements, regulatory scrutiny of those arrangements has heightened given the greater risk of reduced infrastructure

60 'Antitrust: Commission sends Statement of Objections to O2 CZ, CETIN and T-Mobile CZ for their network sharing agreement' (European Commission, 7 August 2019), at: https://ec.europa.eu/commission/presscorner/detail/en/IP_19_5110, accessed 2 October 2020.

61 Per BEREC, national regulatory authorities indicated that active sharing (which typically includes passive sharing) can achieve greater cost savings than passive sharing. See n 51 above, p 9. In a separate BEREC report, some national regulatory authorities provided data on cost savings by type of sharing. See n 59 above, p 16.

62 See n 52 above, pp 2, 7, 9 and 11–12.

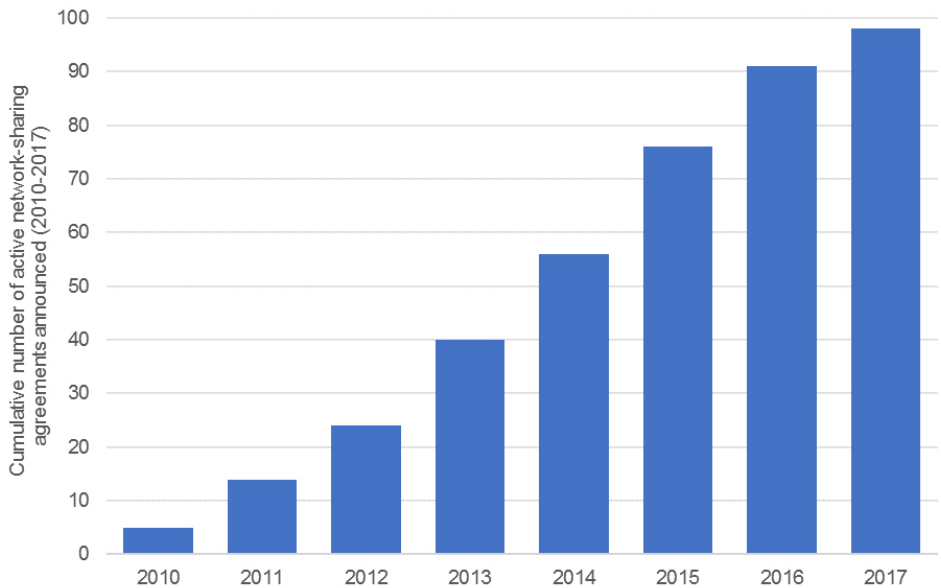
63 See GSMA, 'Road to 5G: Introduction and Migration' (GSMA 2018) 16; Massimo Condoluci and Toktam Mahmoodi, 'Softwarization and virtualization in 5G mobile networks: Benefits, trends and challenges' (2018) 146 *Computer Networks*, p 65.

64 For an overview of network slicing, see 'An Introduction to Network Slicing' (GSMA 2017).

competition between MNOs. Going forward, the pressures on MNOs to collaborate, given the substantial investment costs associated with 5G, are likely to result in active NSAs playing an even greater role in the mobile industry.

This also has implications for the assessment of merger proposals by antitrust authorities: if they consider active NSAs may be problematic from a competition perspective, they may not accept an NSA as a counterfactual for merger analysis.

Figure 10: Active network sharing has become more common worldwide



Source: Adapted from Grijpink et al (see n 12 above).

Competition and regulatory authorities across Europe have assessed the competitive impact of active NSAs.[65] A recent example of an active NSA attracting regulatory scrutiny is the network sharing cooperation in the Czech Republic between O2 CZ/CETIN and T-Mobile CZ.[66] The European Commission opened an antitrust

65 BEREC provides an overview of active NSA assessments by national competition and regulatory authorities in various EU countries. See n 59 above, annex 1.

66 O2 CZ's mobile infrastructure and wholesale business has been transferred to CETIN, a network infrastructure company belonging to the same corporate group. The network sharing cooperation between O2 CZ/CETIN and T-Mobile CZ began in 2011 and has since been increasing in scope. It currently covers all mobile technologies (ie, 2G, 3G and 4G) and the entirety of the Czech Republic excluding Prague and Brno, amounting to around 85 per cent of the population. See n 60 above.

investigation into this NSA in October 2016. In August 2019 the Commission issued a Statement of Objections to the parties, reaching the preliminary conclusion that their NSA restricts competition in breach of Article 101 of the Treaty on the Functioning of the European Union.[67] Of the three major MNOs in the Czech Republic, O2 CZ and T-Mobile CZ are the two largest, with their networks serving approximately three-quarters of subscribers.[68]

The European Commission acknowledged that '[o]perators sharing networks generally benefits consumers in terms of faster roll out, cost savings and coverage in rural areas'.[69] It added that network sharing is a widespread practice that can facilitate the rollout of networks by reducing costs and, in most cases, creating efficiencies, but in some circumstances, it may have a negative impact on competition.[70]

In this case, however, the Commission has taken the preliminary view that instead of leading to greater efficiencies and higher service quality, the NSA between O2 CZ/CETIN and T-Mobile CZ is likely to remove incentives for the two MNOs to improve their networks and services to the detriment of consumers.[71] However, a recent paper, 'Cooperation Among Competitors: Network Sharing Can Increase Consumer Welfare', found that this active NSA has generated consumer benefits through both lower prices and higher quality.[72] Another paper, 'Horizontal Cooperation on Investment: Evidence From Mobile Network Sharing', also found that the NSA generated cost savings for the sharing parties, which were passed on to consumers through lower prices and higher network quality.[73]

The impact on 5G investment of a four-to-three merger involving existing network sharing agreements

The proposed acquisition by H3G of O2 in the UK, which was notified to the Commission in 2015, is an example of a four-to-three mobile merger that involved both an assessment of the effects on competition and investment, as well as an evaluation of the impact of the deal on two existing NSAs involving the merging parties.

The merger would have combined the fourth player (H3G) with the first player by subscribers (if O2's share in the Tesco Mobile joint venture is included), and the second player by revenues. The four MNOs currently in the UK are parties

67 See n 60 above; 'Antitrust: Commission opens formal investigation into mobile telephone network sharing in Czech Republic' (European Commission, 25 October 2016), at: https://ec.europa.eu/commission/presscorner/detail/en/IP_16_3539, accessed 2 October 2020.

68 See n 60 above.

69 *Ibid.*

70 *Ibid.*

71 *Ibid.*

72 See n 52 above, pp 1 and 25.

73 Anca Cojoc et al, 'Horizontal Cooperation on Investment: Evidence From Mobile Network Sharing' (2020) SSRN 1 and 43, at: https://papers.ssrn.com/abstract=3593732, accessed 2 October 2020.

to two NSAs, which enable them to share the costs of rolling out their networks while continuing to compete at the retail level: EE and H3G have shared their networks under the Mobile Broadband Network Limited (MBNL) joint venture; and Vodafone and O2 have brought together their networks to create Beacon.

On 28 May 2020, the General Court annulled the European Commission's 2016 decision to block the proposed H3G/O2 merger, ruling that the Commission had not proven the transaction would generate non-coordinated (ie, unilateral) effects capable of constituting a significant impediment to effective competition (SIEC).[74] The Commission has since indicated that it will appeal the General Court's judgment at the Court of Justice of the EU.[75]

One of the three theories of harm identified by the Commission was that the merged entity would have been part of both existing NSAs (MBNL and Beacon) and would have had full overview of the network plans of both network sharing partners (Vodafone and EE – also the two remaining competitors), which would have weakened them and hampered the future development of UK mobile infrastructure, including 5G rollout.[76] In particular, the Commission considered that one of the ways of weakening the competitive position of a given NSA partner (eg, EE) would be to increase the costs of maintaining and improving the network or degrade the network quality of that NSA (eg, MBNL), which would be particularly relevant for the partner in the NSA uninvolved with the merged entity's consolidated network.

The Commission had argued that while, pre-merger, the partners of each of the two NSAs had an incentive to jointly develop the shared elements of their networks to achieve a better network than the other NSA, this competitive dynamic would be lost post-merger as the merged entity would be party to both NSAs and Vodafone and EE would no longer have a fully committed partner in Beacon and MBNL.[77] After examining the merging parties' network consolidation plans, the Commission concluded that the merger could: (1) weaken the competitive position of Vodafone

74 *CK Telecoms* (see n 26 above).

75 Foo Yun Chee, 'EU to take Hutchison, O2 case to top court after tribunal ruling' (Reuters, 29 July 2020), at: https//:uk.reuters.com/article/uk-telefonica-m-a-ckh-holdings-eu/eu-to-take-hutchison-o2-case-to-top-court-after-tribunal-ruling-idUKKCN24U2GT, accessed 2 October 2020.

76 The Commission also identified two other theories of harm: (1) the transaction would have eliminated competition between two strong players in the UK mobile market and the merged entity would have had much less incentive to compete, leading to reduced choice and quality of service and higher retail prices for UK consumers; and (2) the transaction would have reduced the number of MNOs effectively willing to host mobile virtual network operators. See 'Mergers: Commission prohibits Hutchison's proposed acquisition of Telefónica UK' (European Commission, 11 May 2016), at: https://ec.europa.eu/commission/presscorner/detail/en/IP_16_1704, accessed 2 October 2020.

77 *CK Telecoms* (see n 26 above) para 296.

and EE and, thus, reduce their competitive pressure; and (2) reduce industry-wide investments in network infrastructure.

In its judgment, the General Court made three broad sets of observations about the Commission's NSA-related theory of harm and its assessment of the effects of the disruption to the NSAs that would have resulted from the proposed merger.

Alignment of interests between the parties to the NSAs

Firstly, the General Court examined the Commission's analysis of the need for (and extent of) alignment of interests between the parties to each NSA in order to have a shared network that allows each partner to compete effectively. The General Court noted that the non-merging parties' (EE and Vodafone) ability to compete and incentives to invest would not depend decisively on the merged entity's investment decisions or on cost increases, but instead on the level of competition that these competitors would face, their financial resources and their strategies.[78]

In the General Court's view, the fact that an NSA may result in pro-competitive effects, thus counteracting the restrictions it contains, does not necessarily mean that its termination, renegotiation or each subsequent alteration to its balance following a merger may necessarily be characterised as an SIEC.[79] Thus, the General Court ruled:

> 'Therefore, it must be held that a possible misalignment of the interests of the partners in a network-sharing agreement, a disruption of the pre-existing network-sharing arrangements the duration of which was extended for the benefit of Three, or even the termination of those agreements does not constitute, in the present case, and as such, a significant impediment to effective competition in the context of a theory of harm based on non-coordinated effects.'[80]

Effects of the merger on the competitors that are partners in the NSAs

Secondly, the General Court examined the European Commission's assessment of the effects of the merger on the two competitors and NSA partners, EE and Vodafone, in light of the merged entity's network consolidation plans. The General Court ruled that the Commission had failed to prove to the requisite legal standard that the alleged increase in EE and Vodafone's fixed and incremental costs would lead to lower investments, a deterioration in the quality of services or, if the higher costs were passed on to consumers as higher prices, a decrease in competitive

78 *Ibid,* para 342.
79 *Ibid,* para 340.
80 *Ibid,* para 347.

pressure exerted by EE and Vodafone.[81] The General Court also found that a reduction in the competitive pressure that EE or Vodafone were capable of exerting is not, in itself, sufficient to establish an SIEC.[82]

Effects of increased transparency on overall network investments

Finally, the General Court examined the European Commission's concern that the resulting increased transparency of each MNO's investment strategy would reduce EE and Vodafone's unilateral incentives to invest proactively in new technology (before any initiative by the merged entity to invest first) and hence reduce their competitive pressure. The General Court ruled that, by failing to set out the appropriate timeframe for establishing the existence of an SIEC, the Commission had erred in law in finding that the increased transparency of MNOs' overall investments brought about by the NSAs would reduce MNOs' incentives to invest in their networks.[83]

The Commission analysed: (1) the merger's short- and medium-term effects in light of the temporary overlap of the two NSAs; and (2) the merger's medium- and long-term effects in light of the merged entity's network consolidation plans.[84] However, in the General Court's view, the Commission did not take into account that the merging parties would not maintain two separate networks in the long term.[85] Therefore, the General Court rejected the Commission's finding on the effect of increased transparency on overall network investments, which was based on the assumption of the existence of two separate networks.[86]

In addition, the Commission did not appear to consider the long term as the appropriate timeframe for assessing the effects of the merger.[87] The General Court, however, disagreed:

> 'The Court finds that the analysis of the effects of a concentration on an oligopolistic market in the telecommunications sector which requires long-term investment and where consumers are often tied by contracts over several years is a dynamic prospective analysis which requires account to be taken of any coordinated or unilateral effects over a relatively long period of time in the future.' [88]

81 *Ibid*, para 367.
82 *Ibid*, paras 370 and 381.
83 *Ibid*, para 408.
84 *Ibid*, para 408.
85 *Ibid*, para 410.
86 *Ibid*, para 416.
87 *Ibid*, para 410.
88 *Ibid*, para 415.

Conclusion

Both mergers and NSAs between MNOs have the potential to benefit consumers through increased investment and the dynamic competition benefits they bring. In particular, by improving the economics of 5G investment, they may increase the magnitude of investment and the speed with which 5G is rolled out. However, they may also reduce competitive tension, particularly in a more static sense, between MNOs. The overall effect on investment and consumer welfare will depend on the specific facts and circumstances of each case.

The cases we have discussed highlight that for both mergers and NSAs, whether there is a positive impact on investment depends on (among other things):

- the merging or sharing parties' financial position and ability to invest; and
- the extent of the synergies created by combining spectrum and network assets.

For NSAs, the degree of cost savings achieved (and potential for increased investment) will depend on the type of network sharing arrangement, in particular: the type of infrastructure that is shared (ie, passive versus active), the type of technology (ie, 5G versus 4G), the areas where sharing takes place (ie, urban versus rural) and when the sharing is implemented (ie, greenfield versus network consolidation).

Given the substantial investment costs associated with 5G, and the resulting pressures on MNOs to collaborate, active NSAs and NSAs covering urban areas are likely to play an increasingly important role in MNO plans for rolling out 5G networks. This is likely to attract greater regulatory scrutiny given the potential competition concerns raised by these types of NSAs. Counterbalancing this, the technical characteristics of 5G (virtualisation and network slicing) may lessen concerns that NSAs will limit the ability of MNOs to differentiate their services.

Economic analysis and evidence have an important role to play in evaluating this trade-off between efficiency gains and anti-competitive effects arising from consolidation and cooperation between MNOs, and assessing the overall impact on investment and competition, as demonstrated in the General Court's recent *H3G/O2* judgment.

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An economic perspective on the new South African buyer power provision and enforcement guidelines

Zoë van der Hoven, Paul Anderson and Kagiso Zwane

Introduction

On 13 February 2019, the South African Competition Amendment Act 18 of 2018 (the 'Amendment Act') was signed into law by President Cyril Ramaphosa. This legislation amended the Competition Act No 89 of 1998 by, among other changes, inserting a buyer power provision (contained in section 8(4)). This provision prohibits a dominant buyer in a designated sector from requiring or imposing unfair prices or trading conditions on small and medium businesses (SMEs) and firms controlled or owned by historically disadvantaged persons ('HDP firms').

Although the notion of buyer power and the ability of firms to abuse such power is by no means a new concept in competition economics, the South African buyer power provision presents a novel way of thinking about such an abuse. This is largely due to the combination of three features:

- first, it considers buyer power in the context of protecting the public interest rather than the traditional consumer welfare framework;
- second, the provision is included under section 8, which deals with abuse of dominance; and
- third, it is expansive in that it covers not only unfair trading terms but also unfair prices.

The unusual combination of these factors has raised a number of questions as to how the provisions should be applied from an economic perspective. To address this, the Amendment Act was followed by the publication of the Buyer Power Regulations (2020) (the 'Regulations')[1] as well as a set of Buyer Power Enforcement Guidelines (2020)[2] (the 'Guidelines') by the South African Competition Commission (the 'Commission'). Both of the Regulations and Guidelines, and the latter in particular, have sought to provide further clarity on the factors or benchmarks for assessing a buyer power abuse.

In what follows we discuss the three features of the buyer power provision, the difficulties associated with each feature from an economic perspective, what the Guidelines have suggested as the approach for dealing with each and what challenges are likely to remain.

Buyer power as a public interest consideration

Buyer power refers to the ability of downstream firms to affect the terms of trade with upstream suppliers.[3] From the perspective of identifying anticompetitive conduct based on a consumer welfare standard (the traditional approach), input prices that are too low because of the exertion of buyer power are rarely a concern. This is because the likelihood that such conduct will have a negative impact on consumer welfare or competition is extremely low. In most instances, the use of bargaining power tends to be efficiency enhancing as it can be used to counterbalance seller market power via a transfer of profits from suppliers (who have been keeping supra-competitive profits) to buyers.

Further, the economic literature indicates that some or all of the gains extracted from the supplier through buyer power are usually passed on to downstream customers and therefore are consumer welfare enhancing (not detrimental).[4]

1 Regulations on Buyer Power made by the Minister under Competition Act, 1998 (Government Gazette No 43018).

2 Competition Commission, 'Buyer Power Enforcement Guidelines' (2020).

3 OECD, 'Policy Roundtables: Monopsony and Buyer Power' (2008) p 21.

4 For example, an article published by the OECD states: 'If a lower price can be achieved without restricting supply, then in a competitive market place, any lower prices obtained by a powerful purchaser are likely to be passed on to consumers as part of a strategy to increase market share downstream.' *Ibid*, p 258.

Indeed, the concern with buyer power as an exploitative abuse of dominance under a consumer welfare standard only arises in the rare situations of monopsony power. This is where market power on the part of the dominant firm in both the buyer and downstream seller markets leads to a reduction in output, causing a fall in the overall welfare to end consumers and input producers.

However, in addition to protecting competition, the Competition Act also seeks to achieve certain public interest objectives, which may be broadly summarised as improved and more equitable access to the economy. It is this public interest objective that led to the inclusion of the buyer power provision in the Amendment Act. This brings an entirely different dimension to the consideration of buyer power. Indeed, the motivation for the inclusion of the buyer power provisions as section 8(1)(d)(vii) of the Act is described as follows:

> 'Subsection (1)(d)(vii) is introduced to protect suppliers to dominant firms, especially small and medium businesses or a firm owned or controlled by historically disadvantaged persons, from being required, through the abuse of dominance, to sell their goods or services at prices that impede their ability to participate effectively.'[5]

In other words, the provision is not only concerned with the detrimental impact that monopsony power can have on consumers but also with a much broader concern, namely, the potentially unfair and exploitative nature of bargaining power. The concern is that this power allows buyers to extract surplus from SME/HDP suppliers through unreasonable trading terms or prices that are too low, transferring undue risk to suppliers or putting their profits and margins under pressure.

The effect of this is a supplier-centric approach that seeks to elevate the welfare of particular economic actors (other than consumers), namely SMEs and HDP firms based on public interest. This approach, however, can result in an uncomfortable tension for the welfare purist – conduct that is neutral or positive for consumers could still be found to be an abuse because it has a negative impact on certain suppliers, or even a single supplier. In other words, the amendments suggest an intentional prioritisation of the welfare of SME/HDP firms over that of consumers in instances where these are in conflict.

The Guidelines do not try to resolve the tension between the competition and public interest consideration. To the contrary, they explicitly indicate that the Commission does not consider the provision to require an assessment of the effects on final consumers to establish a contravention:

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5 Competition Commission of South Africa, 'Background Note on the Competition Amendment Bill' (Government Gazette No 41294) p 16.

> 'An inquiry under section 8(4) is whether the prices and trading conditions imposed on suppliers in the designated class by a dominant firm are unfair or not. The focus of the inquiry is therefore on the treatment and welfare of suppliers in the designated class, and the application of a fairness principle to that treatment.'

The inquiry does not, in the Commission's view, require an assessment of the effects on final consumers. For instance, it is not relevant whether an unfairly low price achieved through the exercise of buyer power is passed through to consumers or not. The legislation does not require any weighing up of the welfare of suppliers in the designated class against final consumers.'[6]

The fact that the Guidelines do not try to resolve the aforementioned tension is not a mistake, nor should it be surprising for those who are familiar with the South African context where such trade-offs are not particularly novel. Indeed, the South African merger control regime requires an independent assessment of public interest factors such as the impact on employment, participation by SME and HDP firms and industrial development objectives.[7] This assessment is undertaken in addition to a competition assessment. Importantly, a merger can be blocked or allowed on public interest grounds alone – there is no requirement for a weighing-up of such considerations. Although this can bring challenges, over time practitioners and courts have become accustomed to and adept at dealing with the dual focus on traditional competition concerns as well as public interest considerations as part of a merger review.

Given the consistency with the merger provisions and the fact that South Africa has learnt to navigate these considerations in merger control (arguably with a fair degree of success), there is no real reason to expect that the Guidelines would try to square this circle in the context of buyer power. In any case, it is not clear that the tension is likely to be a common feature of such cases (and would almost certainly be less likely to occur in the current context than in the case of mergers). This is because the provision is limited to small firms that are unlikely to materially influence average prices and consequently the negative impact on downstream prices and final consumers is likely to be limited. Therefore, although potentially in tension with a strict consumer welfare (or even total welfare) approach, in our view the public interest focus is ultimately workable.

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6 Competition Commission of South Africa, 'Buyer Power Enforcement Guidelines' (2020) paras 2.2.1–2.2.2.

7 Public interest also features in the exemption regime but is rarely used and therefore has not had a material impact.

Bargaining power as an abuse of dominance

Given that the approach and intention of the legislation extends beyond monopsony power to exploitative bargaining power concerns, a second interesting and relatively novel aspect of the provisions is that they have been included in the abuse of dominance section of the Amendment Act. Thus, the provision only applies to buyers that are considered 'dominant' within the meaning of the Act. In contrast, other jurisdictions have generally regarded exploitative buyer power as a concern that is best dealt with outside the ambit of the abuse of dominance provisions, and often even outside of competition law itself. For example:

- France, Germany, Greece, Italy, Portugal and, recently, Belgium have separate provisions in their legislation for determining an abuse of economic dependence that is distinct from an abuse of market dominance. Economic dependence is a different concept to dominance with a wider scope of application. An abuse of economic dependence occurs when one economic actor is in a position of strength in relation to another, without necessarily holding a dominant position in a relevant market.[8]
- In Kenya an abuse of buyer power is prohibited under the Competition Act,[9] but as indicated in the associated Buyer Power Guidelines, the 'proof of dominance is not a mandatory criteria'. [10]
- The European Union and the United Kingdom have typically sought to deal with such concerns outside the scope of competition law. In particular, the EU has proposed addressing concerns around the exploitation of small food product suppliers via its 2018 proposal for a directive on unilateral trading practices (UTPs) in business-to-business relationships in the food supply chain.[11] Similarly, the UK introduced a Groceries Supply Code of Practice due to concerns around supplier exploitation through the transfer of excessive risks and unexpected costs.[12]

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8 BundesKartellamt, 'Buyer Power in Competition Law – Status and Perspectives, Background Paper Meeting of the Working Group on Competition Law' (2008) pp 6–7; Ignacio Herrera Anchustegui, 'Buyer power in agreements and abuse of market power cases: An overview of EU and national case law' (19 April 2018): www.concurrences.com/en/bulletin/special-issues/buyer-power-in-agreements-and-abuse-of-market-power-en/buyer-power-in-agreements-and-abuse-of-market-power-cases-an-overview-of-eu-and-en accessed 30 October 2020.

9 Competition Act (Kenya) 2010 (No 12).

10 Competition Authority of Kenya, 'Buyer Power Guidelines' (2017) para 22.

11 European Commission, 'Proposal for a Directive of the European Parliament and of the Council on unfair trading practices in business-to-business relationships in the food supply chain' COM(2018) 173 final.

12 UK Competition Commission, 'The Groceries (Supply Chain Practices) Market Investigation Order' (2009).

Part of the rationale behind these alternative approaches is that it is generally recognised by economists that concerns about exploitative buyer power can arise even when a buyer is not dominant in the relevant market. The existence of buyer power is determined by the relative bargaining position of the buyer and supplier and, as a result, a non-dominant buyer may exert bargaining power over a particular supplier even if it does not hold market power in the purchasing market as a whole. Consequently, the traditional tests of dominance are often seen as setting a much higher bar, which makes it difficult to capture much of the exploitative buyer power that is of concern.

Indeed, while Article 102(a) of the Treaty of the Functioning of the European Union allows for the prosecution of unfairly low purchase prices or unfair trading terms, such cases are rare. For example, the European Commission recently opted to develop the aforementioned directive on UTPs in the food supply chain due to an acknowledgment that these behaviours were generally outside the scope of EU (and national) competition law. This is because the latter 'requires the existence of a dominant position in a given market, as well as the identification of an abuse of that position that affects the market overall'.[13]

The South African Guidelines seem to be alive to these difficulties in that, although they refer to the market share thresholds for a presumption of dominance set by the Act,[14] they acknowledge that buyers with market shares below this threshold (ie, less than 35 per cent) may well have buyer power. The Guidelines go on to outline an approach to determining buyer power when a buyer has a market share of less than 35 per cent (the Act requires that market power[15] is established for firms with market share of less than 35 per cent). These include: (1) the supplier dependency on the buyer and outside options; (2) the alternative suppliers available to the buyer; and (3) the nature of supply negotiations.[16] Although this approach seeks to resolve the tension between buyer power and the traditional view of dominance, it creates potential difficulties.

First, such an approach diverges significantly from that traditionally adopted in South Africa when it comes to dominance (albeit supplier dominance). In particular, the typical approach to dominance has been largely structural in nature,

13 See n 11 above, p 3.

14 For firms with a share of between 35 per cent and 45 per cent there is a rebuttable presumption of dominance while for firms with a share of 45 per cent and above there is a non-rebuttable presumption of dominance. Firms with a market share of less than 35 per cent must be shown to possess market power.

15 Market power is: 'The power of a firm to control prices, or to exclude competition or to behave to an appreciable extent independently of its competitors, customers or suppliers'. See Competition Act (South Africa) 1998, s 7.

16 Competition Commission of South Africa, 'Buyer Power Enforcement Guidelines' (2020) para 4.4.

focusing on market shares and whether they reach the various thresholds prescribed in section 7 of the Act. Very few cases of abuse of dominance have dealt with firms falling below the market share thresholds for presumed dominance that must then be shown to possess market power.

Second, in addressing the requirement to show market power, the Guidelines appear to conflate the ideas of bargaining power, buyer power and dominance. In fact, the Guidelines seem to use these terms interchangeably and it is not clear that the factors identified by the Guidelines with respect to establishing buyer power are necessarily sufficient to establish dominance. This is not to say that there is no relationship between these various concepts. Indeed, if a firm does have market power (ie, buyer power for the market as a whole), it is most likely also to have bargaining power over individual suppliers. However, the literature is clear that bargaining power and buyer power are not equivalent to the notion of market power or dominance and that bargaining power can be exercised without a firm being dominant. In particular, to have market power it is generally considered that one must have substantial buyer power in the market as a whole.[17] That is, one must be able to dictate industry terms of supply or the conduct must result in a market-wide effect.[18] This could occur if, for example, there is a high level of economic dependency on an average basis across all suppliers.[19]

This is why other jurisdictions have either carved out a separate provision for economic dependence or have not sought to prosecute unfair purchasing practices as an infringement of competition rules.[20] Interestingly, in Kenya, like the case of South Africa, buyer power is dealt with under the abuse of dominance provisions in the Kenyan Competition Act.[21] However, unlike the South African Act, it appears that there is nothing in the wording of the Kenyan Act that actually requires dominance to be established in the case of establishing a buyer power abuse. As already indicated, this has been confirmed in the Guidelines issued by the Competition Authority of Kenya.[22]

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17 Pranvera Këllezi, 'Abuse of dominance below the Threshold of Dominance? Market Power, Market Dominance and Abuse of Economic Dependence in Mark-Oliver Mackenrodt, Beatriz Conde Gallrgo and Stefan Enchelmaier (eds), *Abuse of Dominant Position: New Interpretation, New Enforcement Mechanisms?* (Springer-Verlag Berlin Heidelber 2008); see n 8 above, Anchustegui; see n 8 above, BundesKartellamt; see n 3 above OECD.

18 Office of Fair Trade, 'The Competitive Effects of buyer groups' Economic Discussion Paper (2007), paras 1.20, 1.23, ft 5.

19 See n 8 above, BundesKartellamt, pp 6–7.

20 See, eg, the European Commission directive on unfair trading practices in business-to-business relationships in the food supply chain.

21 Competition Act (Kenya), s 24.

22 See n 10 above.

The implication is that South Africa is in a relatively unique position. The Guidelines certainly present a best-effort attempt at reconciling the concept of buyer power with dominance in order to capture the bargaining power concerns that the provisions were probably intended to address. However, there is still a question as to whether determining buyer power as outlined by the Guidelines will withstand legal scrutiny and sustain a finding of market power and dominance. Only time will tell whether this is the case.

Unfairly low prices as an abuse

Another unusual element of the buyer power provisions is that they cover unfair prices in addition to unfair trading terms. Although it is not unusual for authorities to seek to protect against unreasonable or unfair terms of trade that result in the transfer of unforeseen or undue costs and risks to suppliers, it is less common for them to target unfairly low prices as an exploitative abuse.

This is in part because of the benefits associated with the exercise of buyer power from a consumer welfare perspective, but also because, even in circumstances where authorities may suspect that the exercise of buyer power by a dominant firm results in valid abuse concerns, it is in fact very difficult to establish that purchase prices are indeed too low. This is the case for a number of reasons.

First, the costs of production will differ among firms, with some more efficient than others. In this context, a purchase price test would need to distinguish between situations where the supplier is simply inefficient and where the purchase price is genuinely too low. If other firms could supply profitably at that price (even if it is because they are large and have scale economies), it is unreasonable to expect a buyer to source from inefficient suppliers at higher prices simply because they are less efficient. This would have the undesirable consequences of either rewarding inefficiency in the supply chain, or resulting in buyers not purchasing from smaller firms.

Second, if the supplier is already active with a buyer then the courts are likely to be faced with the context where any price would be above at least variable costs because otherwise the supplier would not continue to supply. From an economic perspective, any price that is at least recovering variable costs is not normally considered too low in the context of a benchmark for predation. As such, the courts would need to engage in some form of assessment of the fairness of the division of margin between the supplier and the buyer. This too has no easy solution and would be subject to considerable disputes. This is especially the case if one takes into account the context of what is reasonable from the buyer's perspective and a consideration of the dynamic effects. For instance, a lower price may provide

the incentive for a buyer to take on a new supplier that poses a degree of risk not associated with incumbent suppliers. Similarly, a lower price may enhance the ability of the supplier to participate in the market through greater sales even if margins are initially low.

Third, there are a wide variety of additional reasons, not necessarily related to the exploitation of buyer power, as to why the price paid to suppliers may differ. These include differences in product quality and characteristics, including associated brand or risk (eg, reliability or experience of performance). These may constitute a sound basis for a buyer demanding a lower price relative to its other suppliers (based on lower economic value). Again, in most cases, the court is unlikely to have the ability to quantify such factors legitimately and without dispute.

The Regulations and Guidelines are alive to these difficulties and have sought to address them by limiting the application of unfair pricing largely to a comparative exercise. In particular, the Guidelines identify and focus on two benchmarks for unfair pricing to SMEs and HDP firms: (1) unjustifiably paying a lower price relative to other suppliers of like goods or services; and (2) an unjustified reduction in prices or imposition of costs on to the supplier.

Under the first benchmark category the Commission must first identify like goods or services based on a consideration of factors including product characteristics and demand side substitutability. In the case where there are no like goods, the Commission will seek to compare goods or services that are differentiated on factors that may be quantifiable through differences in costs.[23] When determining if a price difference relative to the like good will be deemed unfair, the Guidelines indicate that the Commission will take into account the consistency, duration and prevalence among other small suppliers of the price difference and, in particular, indicates an initial screening price difference of three per cent.[24]

Under the second category, the Commission will compare the effective price paid to the complainant or suppliers in the designated class before and after the price reduction or the imposition of costs. The Commission's assessment will account for the magnitude of the price reduction or costs, the circumstances for the reducing the effective price and whether they may be unfair.[25] The Guidelines suggest that unilateral, non-transparent and non-reciprocal reductions in the effective price are likely to be unfair and indicative of a buyer exercising its buyer power.[26]

The Guidelines indicate that such an inquiry does not require that a specific materiality threshold is passed in terms of the quantum of harm to the supplier in order to establish a contravention. However, in both instances, the respondent

23 Competition Commission, 'Buyer Power Enforcement Guidelines' (2020) para 6.8.2.
24 *Ibid*, paras 6.11.1–6.11.5.
25 *Ibid*, paras 6.16.1–6.16.3.
26 *Ibid*, paras 6.18.1–6.18.3.

may provide an objective justification for the lower price paid to the complainants. Factors that the Commission would consider include similar relative margins earned by the buyer, contractual volume commitments, additional costs incurred or differences in supply relationships.[27]

The comparator-focused approach of the Guidelines is helpful in that it seeks to circumvent some of the most problematic areas of dealing with an unfairly low price – namely the need to deal with cost and efficiency considerations when assessing whether a price is unfairly low. In addition, the Guidelines also clarify important elements of this approach, including when goods are likely to be comparable and potential objective justifications.[28] In doing so, the Guidelines provide important clarity on a number of the key issues that are likely to arise.

However, there are still a number of unanswered questions and challenges as to how the comparator test will be applied. For example, the initial screening threshold of a price difference of three per cent combined with a lack of materiality threshold in terms of the quantum of harm to the supplier sets a relatively low bar for a prima facie finding of abuse. This is exacerbated by the fact that the buyer power regulations also bear a reverse onus requirement.

The practical consequence of this is that a dominant buyer (which could be set at a lower standard than normal market dominance as previously discussed) would need to be able to justify the existence and magnitude of any price differences relating to small firms in order to comply with the buyer power provisions. This is particularly the case for 'like products', but also products that are not directly comparable yet could be subject to cost adjustments.

However, this is not always practical as many justifications are not easily quantifiable. For example, even in the case of like goods, prices can differ because of differences in risk or reliability associated with a supplier. Such a justification is not directly quantifiable and it is also unclear if the Commission would even accept this as a justification. Further, in the case of goods where differences are quantifiable and can be adjusted for (eg, if one good is fortified and the other is not), it is not clear that the buyer will have access to the required information on its suppliers' costs to appropriately estimate what the difference should be.

Given the aforementioned, it is also conceivable that the risks associated with taking on SME or HDP firms as suppliers may ultimately discourage at least some buyers from contracting with such firms in the first place. This may be particularly pronounced for new entrants where the risks (due to a lack of a track record of performance) are higher and buyers may not be able to compensate for such risks by requiring lower prices from these suppliers. This seems especially relevant in a

27 *Ibid*, paras 8.1–8.2.4.
28 *Ibid*, paras 6.7, 8.

retail or on-selling environment where goods are typically subject to some form of differentiation and where there are valid costs and risks associated with taking on new small suppliers but which are difficult to quantify.

Although it must be noted that section 8 of the Act includes an avoidance provision[29] that prohibits dominant buyers from circumventing the buyer power provisions by avoiding or refusing to purchase from a supplier that is an SME or HDP firm, such a provision is for extreme cases where there is clear evidence of avoidance. It is not clear that more marginal instances of refusals resulting from an overall decreased preference to deal with SME and HDP firms are intended to be caught by this provision, and in any case, would be extremely difficult to prove.

Where South Africa will ultimately land on this will depend on the types of cases that the Commission chooses to pursue, how strictly or aggressively it applies the criteria outlined in the Guidelines and the objective justifications that it is willing to accept.

Conclusion

South Africa is not the first jurisdiction to consider abuse of buyer power as a concern or to incorporate it into some form of legislation. However, the combination of the three elements discussed in this paper sets it apart from approaches adopted in other jurisdictions. This is in part because the Amendment Act and the buyer power provisions contained therein are aimed at targeting very specific public interest concerns that are driven by the fairly unique history and context of South Africa.

In our view, the Guidelines are a brave and honest attempt by the Competition Authority to meet the mandate laid out by the legislature and go a long way in clarifying how the provisions will be approached given their novel and untested nature. However, there are a number of questions relating to the application of this provision and consequently its ultimate effect on SME and HDP firms and the economy as a whole that remain. These issues will only be settled through the development of case precedent. This is going to be a fascinating space for competition lawyers and economists alike to watch over the next few years.

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29 Competition Act (South Africa) 1998, s 8(4)(b).

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Australia's draft News Media Bargaining Code

Katharine Kemp*

Introduction

News, the media through which it is spread and the means by which journalism is funded have all been transformed by the internet.[1] That transformation has led to tensions between leading digital platforms and traditional news businesses, particularly on the issue of funding. The Australian government has produced a 'world first' in competition policy: a proposal to legislate to require designated digital platforms – initially Google and Facebook – to compensate news media businesses for news content. Although a handful of other jurisdictions have used copyright regulation to require digital platforms to pay publishers for content,[2] the Australian proposal is for an amendment to competition legislation to require platforms to negotiate with news businesses on remuneration for news content made available on the platforms, including through mediation and, if no agreement can be reached, binding arbitration.[3]

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* I am grateful to David Howarth for very helpful comments on an earlier draft and to Roseanna Bricknell for research assistance; with the usual disclaimers.

1 A thorough review of the changes to news media and business responses internationally is given in F Cairncross, 'The Cairncross Review: A Sustainable Future for Journalism' (2019) chs 2, 3: www.gov.uk/government/publications/the-cairncross-review-a-sustainable-future-for-journalism accessed 12 January 2021 ('Cairncross Review').

2 See Part VI 'Overseas comparisons' below.

3 See Commonwealth Treasurer, 'Press Conference, CPO, Melbourne' (Transcript, 31 July 2020): https://ministers.treasury.gov.au/ministers/josh-frydenberg-2018/transcripts/press-conference-cpo-melbourne accessed 12 January 2021.

The News Media and Digital Platforms Mandatory Bargaining Code (the 'Code') is also intended to set standards on other aspects of the relationship between platforms and news media businesses, including information that the platforms must provide to publishers about the algorithmic ranking of news content and about the data that the platforms collect on users interacting with news content. After the Australian government's publication of a draft Code in July 2020,[4] Google and Facebook each started marketing campaigns, vigorously opposing the Code, calling the measures 'unreasonable', 'onerous' and 'one-sided',[5] and seeking consumer support in this opposition. The government has indicated its intention to introduce the final Code before the end of the year.

The proposal for the Code stems from recommendations by the Australian Competition and Consumer Commission (ACCC) in its *Digital Platforms Inquiry Final Report* ('DPI Report'),[6] after the 18-month Digital Platforms Inquiry (DPI). Conceived as an inquiry to assess the impact of large digital platforms on the revenue of traditional news businesses after changes to Australian cross-media ownership laws, the DPI ultimately assessed the state of competition in a number of sectors in which digital platforms – especially Google and Facebook – operate, and produced wide-ranging recommendations for reform.

According to the ACCC, the proposed Code is intended to reduce substantial inequalities in bargaining power between large digital platforms and news businesses and contribute to the sustainability of independent, high-quality journalism, especially in light of the benefit that platforms derive from displaying news content funded by publishers.[7] A number of commentators, however, claim the government is showing favouritism to large Australian publishers for political reasons, and threatening media diversity.[8]

This article proceeds as follows. Part II explains the origins of the DPI in the debate over the future of media diversity and journalism in Australia. Part III outlines significant findings made by the ACCC in the DPI Report about the market power

4 Exposure Draft: Treasury Laws Amendment (News Media and Digital Platforms Mandatory Bargaining Code) Bill 2020 ('Draft NMB Code'); Exposure Draft Explanatory Materials: Treasury Laws Amendment (News Media and Digital Platforms Mandatory Bargaining Code) Bill 2020 ('Explanatory Materials').

5 See Part IV 'Developments' below.

6 Australian Competition and Consumer Commission, 'Digital Platforms Inquiry: Final Report' (2019) ('ACCC DPI Report').

7 See ACCC, 'Draft media bargaining code', ACCC website www.accc.gov.au/focus-areas/digital-platforms/draft-news-media-bargaining-code .

8 See, eg, Kevin Rudd, 'On the News Media Bargaining Code' (31 August 2020): www.youtube.com/watch?v=nL6XBJ5CoXo accessed 12 January 2021; 'Australia's News Media Bargaining Code, Breaking Down the Code, Australia's Fake News' (blog post, 20 August 2020): https://stratechery.com/2020/australias-news-media-bargaining-code-breaking-down-the-code-australias-fake-news accessed 12 January 2021.

enjoyed by Google and Facebook, competitive dynamics between the platforms and news businesses, and the ACCC's reasoning in initially recommending voluntary codes. Part IV describes events after those recommendations, including the stalled negotiations over a voluntary code and Google and Facebook's campaigns against the draft Code. Part V outlines and analyses the provisions of the draft mandatory Code, in light of key criticisms. Part VI concludes with comparisons to measures in other jurisdictions and likely outcomes in Australia.

The origins of the DPI: media ownership and diversity

The DPI Report has become renowned for its wide-ranging recommendations, from significant privacy and consumer law reform to methods of funding journalism and a further inquiry by the ACCC into the advertising technology ('ad tech') sector.[9] It is easy to lose sight of the fact that the DPI was born of concerns about the future of media diversity in Australia.

'Cross-media ownership' rules have been a topic of almost continuous debate in Australian media policy since their introduction in the 1980s.[10] Intended to preserve diversity, the rules set limits on the different forms of traditional media (print, radio and television) that a single proprietor could own in a geographic market.[11] The growth of the internet made the distinction between traditional media and geographic markets seem increasingly quaint as digitalisation led to the internet becoming a form of universal media. In the past decade, traditional news businesses also began to experience dramatic losses in advertising revenues, due to the greatly increased popularity of digital advertising via online search and social media platforms, as well as the migration of classified advertisements to online platforms.[12] This led to calls for the relaxation of cross-media ownership laws in the interests of the survival of traditional Australian news businesses and quality journalism.[13]

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9 ACCC, 'Ad tech and ad agency services inquiry kicks off' (media release, 10 March 2020): www.accc.gov.au/media-release/ad-tech-and-ad-agency-services-inquiry-kicks-off accessed 12 January 2021.

10 See Jock Given, 'Cross-Media Ownership Laws: Refinement or Rejection' (2007) 30 *UNSW Law Journal* 258.

11 See Department of Communication, Australian government, 'Media Control and Ownership' (Policy Background Paper No 3, June 2014): www.communications.gov.au/publications/media-control-and-ownership-policy-background-paper-no3 accessed 12 January 2021 5-8.

12 ACCC DPI Report, 120–124.

13 Department of Communication, 'Media Control and Ownership'.

In the event, the passage of this legislation[14] depended on the vote of Nick Xenophon, an independent senator, and his allies in the Senate.[15] Xenophon made his support conditional on, among other things, the government commissioning an inquiry into the large digital platforms contributing to a loss of advertising revenue from traditional news businesses.[16] In December 2017, the federal Treasurer issued the Terms of Reference for the DPI, requiring the ACCC:[17]

> '… to hold an inquiry into the impact of digital search engines, social media platforms and other digital content aggregation platforms (platform services) on the state of competition in media and advertising services markets, in particular in relation to the supply of news and journalistic content, and the implications of this for media content creators, advertisers and consumers.'

After the publication of the Terms of Reference, a spokesperson for Xenophon's political party, the Nick Xenophon Team, said:[18]

> 'This inquiry will be important as it will expose the tactics search engines and social media platforms have employed to hoard advertising dollars, the conditions they have forced media organisations to accept, and the part they have played in the gradual erosion of the media's bottom line. They need to be called to account for their behaviour and lack of transparency, which is irrefutably having an impact on Australian media organisations.'

Traditional news media businesses have now arguably benefited doubly from the repeal of the cross-media laws: first through the repeal itself and then through many of the ACCC's recommendations, including proposal for the Code.

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14 Broadcasting Legislation Amendment (Broadcasting Reform) Act 2017 (Cth) repealed the '75% reach rule' (preventing a person being in a position to exercise control of commercial television broadcasting licences whose total licence area population exceeds 75 per cent of the population of Australia) and the '2 out of 3 rule' (preventing mergers involving more than two of three regulated media platforms (commercial television, commercial radio and associated newspapers) in any commercial radio licence area).

15 See Rhonda Jolly, 'Broadcasting Legislation Amendment (Broadcasting Reform) Bill 2017', Bills Digest No 8, 2017–18.

16 Amanda Meade and Katharine Murphy, 'Media bosses praise Xenophon and government for deal on ownership law' *The Guardian* (15 September 2017): www.theguardian.com/media/2017/sep/14/media-bosses-praise-xenophon-and-government-for-deal-on-ownership-law accessed 12 January 2021.

17 Treasurer, Commonwealth of Australia, 'Competition and Consumer Act 2010: Inquiry into Digital Platforms' (4 December 2017).

18 James Riley, 'ACCC targets tech platforms', *InnovationAus* (4 December 2017): www.innovationaus.com/accc-targets-tech-platforms accessed 12 January 2021, quoting Senator Stirling Griff.

DPI findings and recommendations

The ACCC conducted the DPI over 18 months from 2018 to 2019. Although the title of the inquiry referred to digital platforms in general, the ACCC focused most of its attention on Google and Facebook, the two platforms with the greatest shares in digital advertising and the most significance as sites for online news content.

In the DPI Report, the ACCC stated its view that Google and Facebook each had substantial market power in several markets, including:

- Google, in the markets for general search services and search advertising services; and
- Facebook, in the markets for social media services and display advertising services.

The ACCC also noted that Google and Facebook each had 'substantial bargaining power in its dealings with news media businesses in Australia'.[19]

The ACCC stated that there was also likely to be a market in which Google and Facebook supply a 'news referral service' to media businesses.[20] This appears to be the first time such a market has been defined or proposed. The ACCC explained that a large percentage of Australian consumers of news content accessed that content via digital platforms (and Google and Facebook in particular) rather than visiting the website of a news business directly. The ACCC explained that each of these platforms provided 'news referral services' which 'can take the form of media aggregation services, online search services or social media services'.[21]

For example, Google search users are shown news items in 'Top Stories' at the top of the Google search results page where Google considers a search term to have 'news intent'.[22] Google users can also view news items on 'Google News', a news aggregation website and app that presents 'a continuous flow of headlines from news articles, grouped by story'.[23] Facebook users are shown news items in their personalised 'Facebook News Feed'. These include news articles or links posted by news publishers on Facebook, which appear in the News Feeds of users who have liked or subscribed to receive posts from that publisher.[24] Consumers also increasingly use YouTube (owned by Google) and Instagram (owned by Facebook) to view news.[25] News items displayed via 'news referral services' generally display only a headline, image, short summary or 'snippet' from the item in question. If the platform user wishes to read the whole story or view the whole video, they can click the incorporated hyperlink

19 ACCC DPI Report, 8–9.
20 *Ibid*, 99–100.
21 *Ibid*, 207.
22 *Ibid*, 209.
23 *Ibid*, 207.
24 *Ibid*, 216.
25 *Ibid*, 219.

and be transferred to the publisher's website. According to the DPI Report, publishers receive a very high percentage of their traffic from either Google or Facebook.[26]

The ACCC found that Google and Facebook were in fact 'unavoidable trading partners' in the market for news referral services,[27] given that a publisher cannot feasibly refuse to have its content displayed on these platforms since the publisher will depend so heavily on the platform for traffic to its website and the subscription and advertising revenue that traffic creates. At the same time, Google and Facebook enjoy the benefits of providing their users with this news, without compensating the publishers for their content, especially when platform users skim news items on the platforms rather than continuing to the publisher website. This in turn reduces the resources available to pay for journalistic content.[28]

The ACCC formed the view that news businesses had no real power to negotiate with Google and Facebook individually to receive compensation for news content that is displayed on those platforms.[29] Publishers also claimed that attempts to negotiate could be met with retaliatory action by the platforms. In particular, the platforms are able to alter the algorithmic ranking of news content at will and dramatically decrease the referral traffic to a publisher without notice.

There is a clear public interest in access to quality, independent journalism in Australia, and particularly investigative journalism, which has higher costs and risks but also special significance in a thriving democracy. In the DPI Report, the ACCC made a number of proposals to improve the funding of quality journalism, including tax policies to encourage philanthropic support for journalism; stable government funding for public broadcasters; grants for local journalism; a mandatory take-down code for copyright-infringing content on platforms; and a process to implement a harmonised media regulatory framework. Most significantly, for present purposes, it recommended that 'designated digital platforms should provide codes of conduct governing relationships between digital platforms and media businesses' to the Australian Communications and Media Authority (ACMA).[30]

Developments: stalled negotiations, a draft mandatory code and platform reactions

After the DPI Report, in December 2019, the Treasurer directed the ACCC to facilitate negotiations between Google and Facebook and the news businesses

26 *Ibid*, 251. Some news businesses reported drops in website traffic of 40–50 per cent after a Facebook change in the algorithmic ranking of news content.
27 *Ibid*, 99–100.
28 *Ibid*, 17–19, 234.
29 *Ibid*, 253–254.
30 *Ibid*, recommendation 7, 16–17.

towards a single 'voluntary code to address bargaining power imbalances' between these parties, with the ACCC to provide an update on progress in May 2020 and a target date for the voluntary code to commence of November 2020.[31] However, in April 2020, the ACCC informed the Treasurer that negotiations between the parties had stalled. The Treasurer responded by directing the ACCC to draft a mandatory Code, a possibility foreshadowed in the Treasurer's original direction.[32]

In July 2020, the government published a draft Code for consultation.[33] Both Google and Facebook responded to the draft Code with claims that the Code itself would undermine the workings of the relevant markets. An 'Open Letter to Australians', from the Managing Director of Google Australia, warned Australian users that the draft Code 'puts the free services you use at risk' and claimed that Google may have to provide users' data to media businesses to comply with the Code.[34] (Google later clarified that it meant the Code puts Google's services at risk, and these services happen to be free, rather than suggesting it would start charging a monetary price for its services.[35]) In a blog post by the Managing Director of Facebook for Australia and New Zealand, Facebook announced that it would ban the sharing of news content on Facebook and Instagram by publishers and users in Australia if the draft Code becomes law.[36] The criticisms in these communications and others are explained in further detail in the following section.

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31 Australian government, 'Regulating in the digital age: Government Response and Implementation Roadmap for the Digital Platforms Inquiry' (December 2019) 8, 12: https://treasury.gov.au/publication/p2019-41708 accessed 12 January 2021 ('Government DPI Response').

32 Explanatory Materials, 4.

33 Draft NMB Code.

34 Mel Silva, Google Australia, 'Open letter to Australians' (17 August 2020): https://about.google/intl/ALL_au/google-in-australia/aug-17-letter accessed 12 January 2021 ('Google Open Letter'). A similar open letter was published and directed to YouTube users, and promoted on the YouTube page and at the front of YouTube videos watched by users: Gautam Anand, 'New Australian regulation will have negative consequences for the YouTube Community: what you need to know' (Google Australia blog post, 17 August 2020): https://blog.google/around-the-globe/google-asia/australia/new-australian-regulation-will-have-negative-consequences-youtube-community accessed 12 January 2021.

35 The original letter was updated by a further letter: Mel Silva, Google Australia, 'Update to our open letter to Australians' (undated 2020): https://about.google/intl/ALL_au/google-in-australia/an-open-letter/?utm_source=google&utm_medium=hpp&utm_campaign=middleslot-p2 accessed 12 January 2021 ('Google Updated Letter'). See further Mel Silva, 'Australian code's unreasonable payment rules' (Google Australia blog post, 11 October 2020): https://blog.google/around-the-globe/google-asia/australia/australia-code-payments accessed 12 January 2021.

36 Will Easton, Facebook, 'An Update About Changes to Facebook's Services in Australia' (blog post, 31 August 2020) https://about.fb.com/news/2020/08/changes-to-facebooks-services-in-australia accessed 12 January 2021.

The draft Code: criticisms and obligations

The draft Code, published in July 2020, would impose various obligations on designated digital platforms in their dealings with certain news businesses. Initially, Google and Facebook would be the only platforms designated under the Code.[37] The obligations owed by the platforms would apply to their relationships with news businesses that obtain registration with the ACMA under the Code ('registered news businesses').[38]

The draft Code imposes certain minimum standards on the platforms in respect of all registered news businesses.[39] These include obligations to provide the registered news businesses with information and notice about the platform's algorithmic ranking of news content, and information about the platform's practices in respect of users' data, which will be explained further.

The draft Code also provides that platforms must negotiate with registered news businesses to reach an agreement about certain aspects of their relationship when requested by a registered news business.[40] For most news businesses, these matters will include remuneration for news content that appears on the platform. Under the draft Code, registered news businesses can negotiate with each platform individually or as a group. The platform must submit to mediation as part of these negotiations and, if no agreement is reached after three months, submit to binding arbitration on the remuneration payable for news content.[41]

The draft Code proposes that this arbitration would consist of a process commonly known as 'final offer' or 'baseball' arbitration, of the kind popularised in salary arbitrations between baseball teams and players.[42] Each party has one opportunity to submit an offer to the arbitrator, and, with very limited exceptions, the arbitrator

37 Explanatory Materials, 4.

38 *Ibid*, 5-6. To be eligible for registration, news businesses must meet tests broadly requiring annual revenue in excess of AU$150,000; creation and online publication of predominantly 'core news content'; an Australian audience; and that news sources are subject to specified professional standards: Draft NMB Code, cl 52E–52K. 'Core news content' is content produced by a journalist that records, investigates or explains 'issues of public significance to Australians'; 'issues relevant to engaging Australians in public debate and in informing democratic decision making'; or 'content which relates to community and local events': Draft NMB Code, cl 52A.

39 Draft NMB Code, part IVBA, div 4.

40 *Ibid*, part IVBA, div 6.

41 Draft NMB Code, cl 52ZF; Explanatory Materials, 24.

42 Draft NMB Code, cl 52ZO; Explanatory Materials, 24. On 'baseball' arbitration, see Lochlin B Samples, 'Resolving Construction Disputes Through Baseball Arbitration', *American Bar Association* (12 March 2019): www.americanbar.org/groups/construction_industry/publications/under_construction/2019/spring/resolving-dispute-baseball accessed 12 January 2021; Productivity Commission, 'Telecommunications Competition Regulation: Inquiry Report' (Report No 16, 20 September 2001) 357.

must choose one of the party's offers as the final award. The rationale is that this process will compel parties to make their most reasonable offer up front, without prolonged hearings and negotiations.

One striking feature of the draft Code is that these provisions mandating mediation and arbitration on remuneration would apply only to commercial news businesses.[43] News businesses that receive government funding – the Australian Broadcasting Corporation (ABC) and Special Broadcasting Service (SBS) – are excluded from taking advantage of these provisions, although the Code's minimum standards would still apply in respect of the ABC and SBS. The rationale is that the impact of Google and Facebook on commercial news businesses is greater as a result of their loss of advertising revenue to these platforms.

The Code also imposes a non-discrimination obligation on the platforms in dealings with news media businesses.[44] The Explanatory Memorandum for the Bill explains that:[45]

> 'Discrimination in this context will be considered to occur if the news content of a registered news business is disadvantaged in comparison to other news content in terms of the crawling, indexing, ranking, display, presentation or other process undertaken by the digital platform on any service provided by the digital platform, on the basis of the registered news business' participation in the code.'

As explained later,[46] in other jurisdictions, Google in particular has established a pattern of excluding the news content of publishers that have sought to rely on laws that require Google to pay for online news content. The non-discrimination obligation is intended to avoid such a strategy in Australia, by preventing discrimination against a news business on the basis of its participation under the Code. A possible additional effect of this obligation would be to create a de facto right for Australian local media to access the news referral services of Google and Facebook, as soon as the platforms provide those services to any domestic or international media business.

It is not within the scope of this article to provide an encyclopaedic account of the machinery of the draft Code. Such an exercise would probably have limited value until there is a final Code. The remainder of this section assesses some of the key criticisms that have been raised against the draft Code, including claims that it:

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43 Draft NMB Code, cl 52Y(6), 52ZF(1).

44 *Ibid*, cl 52W.

45 Explanatory Materials, 20 [1.100].

46 See Part VI 'Overseas comparisons' below.

- fails to take account of the value platforms provide to publishers;
- proposes an inappropriate and unworkable solution in mandating 'baseball' arbitration;
- favours powerful publishers at the expense of small businesses by requiring notification of changes in algorithmic ranking; and
- jeopardises consumer privacy by requiring platforms to provide publishers with information about user data collected by the platforms.

Platform value to publishers

A key criticism levelled by the platforms is that the draft Code ignores the value that the platforms provide to publishers. Facebook claimed that the 'ACCC presumes that Facebook benefits most in its relationship with publishers, when in fact the reverse is true', and that:[47]

> 'News organisations in Australia and elsewhere choose to post news on Facebook […] and they encourage readers to share news across social platforms to increase readership of their stories. This in turn allows them to sell more subscriptions and advertising. Over the first five months of 2020 we sent 2.3 billion clicks from Facebook's News Feed back to Australian news websites at no charge – additional traffic worth an estimated $200 million AUD to Australian publishers.'

Google made similar arguments. It invested in a television advertisement in which a comedian acts out a trip on a bus to a restaurant and claims that the draft Code essentially requires the bus driver (Google) to pay the restaurant (publishers) for the privilege of delivering customers to the restaurant.[48] The analogy suggests that Google refuses to acknowledge any benefits it obtains by making publishers' news content available on its platform services. Facebook similarly claims that the benefit it receives from making publishers' news content available to its users is very small.

The draft Code requires the arbitrator, in determining the award, to take into account:[49]

- the direct benefit (whether monetary or otherwise) of the registered news business' 'covered news content' [50] to the digital platform service;

47 See n 36, Facebook blog post.

48 Mariam Cheik-Hussein, 'Google uses Aussie comedian Greta Lee Jackson to fight draft bargaining code' *AdNews* (30 September 2020): www.adnews.com.au/news/google-uses-aussie-comedian-greta-lee-jackson-to-fight-draft-bargaining-code accessed 12 January 2021.

49 Draft NMB Code, cl 52ZP.

50 According to the Explanatory Materials, 14, '"Covered news content" is intended to capture content including sports and entertainment related news such as interviews with coaches and players, reporting about the entertainment industry and coverage of reality television' but not broadcasts of sports games, drama or reality TV, talk-back radio, product reviews or industry reporting. This is a broader concept than the 'core news content' that the news business corporation must predominantly produce to become a registered news business, which requires content produced by a journalist who records, investigates or explains 'issues of public significance to Australians'; 'issues relevant to engaging Australians in public debate and in informing democratic decision making'; or 'content which relates to community and local events': Draft NMB Code, cl 52A.

- the indirect benefit (whether monetary or otherwise) of the registered news business' covered news content to the digital platform service;
- the cost to the registered news business of producing covered news content; and
- whether a particular remuneration amount would place an undue burden on the commercial interests of the digital platform service.

The arbitrator can also consider a submission from the ACCC. The 'indirect benefit' to be considered is the value of the service to the platform, including 'increased usage of the digital platform service and public perception benefits arising from the inclusion of Australian news'. The Explanatory Materials states that making 'news sources [available] on their digital platform services increases user trust and reliance on these services' and that indirect benefits 'also flow due to increased use of digital platforms because of the presence of covered news content generally'.[51]

It is apparent from the terms of these provisions that the draft Code does not require the arbitrator to take the value of a digital platform's news referral services into account, as opposed to the question of whether a proposed remuneration amount would 'place an undue burden on the commercial interests of the digital platform service'. In fairness, the arbitrator should have regard to the value received by both parties to this transaction. Another potential flaw in the Code is more fundamental: mandating remuneration by Google and Facebook for news businesses' content may make Australian news media businesses more reliant on these platforms, and less inclined to focus on rival platforms. This could effectively entrench the power enjoyed by the two dominant platforms.[52]

Effectiveness of 'baseball' arbitration for platform content

While the 'baseball' arbitration has an attractive simplicity of design, the resulting determination will effectively be a single figure reflecting all the complexity of the value exchanges between platforms and news media businesses, over which the parties are likely to have starkly different views. The parties' submissions on their respective offers are also limited to a relatively short 30 pages. While the arbitral award will only last for one year, there is nonetheless an element of finality about the arbitration, bearing in mind that a failure to implement an agreement giving effect to the determination within 30 days will expose the party to civil penalties of up to AU$10m or 10 per cent of turnover.[53]

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51 Explanatory Materials, 25–26.

52 Michael Bradley, 'Canberra (and Rupert) v big tech: can the government rein in Facebook and Google?' *Crikey* (31 August 2020): www.crikey.com.au/2020/08/31/scott-morrison-v-facebook-google accessed 12 January 2021.

53 Draft NMB Code, cl 52ZU–52ZV.

With that background, it seems inevitable that the 'losing' party in the arbitration will look to explore multiple bases for challenge. These may range from simple administrative judicial review challenges that the arbitrator did not take into account some relevant information, to a full constitutional challenge on the basis that the arbitrator is effectively performing a judicial function without being a duly-constituted court under Part III of the Australian Constitution.

There is precedent in other areas of infrastructure regulation that suggests the making of a determination by the arbitrator is unlikely to be the end of the dispute between the parties and instead will start another, more fundamental battle as to the legal basis for resolving the commercial dispute between the parties by this form of 'regulated negotiation'.[54] Given the pattern of Google's responses in particular to comparable regulation in other jurisdictions,[55] there is significant potential for extended litigation over the outcome of the arbitration, or the legitimacy of the Code at the outset.

Information regarding algorithmic ranking

The platforms have argued that the draft Code unfairly obliges them to reveal information concerning their algorithms to Australian publishers, which would: degrade the quality of the algorithmic ranking and therefore the platform service; potentially permit those publishers to 'game' the algorithmic ranking; and disadvantage smaller publishers who are not eligible for registration under the draft Code.

The draft Code provides that the platforms must generally[56] give a registered news business at least 28 days' notice if:

- changes are planned to be made to an algorithm of the digital platform service; and
- the changes are likely to have a significant effect on the ranking of the registered news business' covered news content made available by the digital platform service.[57]

The notice must describe the relevant change and the effect on the ranking of the registered news business' covered news content[58] made available by the digital platform service in terms that are readily comprehensible, as well as describing

54 See Productivity Commission, 'Telecommunications Competition Regulation: Inquiry Report' (Report No 16, 20 September 2001) 338–339.

55 See Part VI 'Overseas comparisons' below.

56 If the change relates to a matter of urgent public interest, notice can be given no later than 48 hours after the change is made: Draft NMB Code, cl 52N(2)(b)(ii).

57 *Ibid*, cl 52N.

58 On the meaning of 'covered news content', see n 47 above.

how the news business can minimise negative effects of the change on the ranking of that news content.[59]

Google's public campaign opposing the draft Code emphasised its view that these obligations would advantage large media businesses at the expense of both small businesses and the quality of Google Search, stating that:

> 'The current draft law would force us to give news publishers advance notice of significant changes to Search and other products and tell them how to minimise the effect on them. If you have a blog, YouTube channel or a small business website that appears in Search results, you'll be at a disadvantage compared to these news businesses. And if you use Search to find information, you'll be worse off because this rule will force us to slow down upgrades that improve Search for everyone.'

A number of commentators have also claimed that the government is using the Code to show favouritism to big publishers for political reasons, at the expense of the platforms and small businesses that produce news content.[60]

The non-discrimination obligation, discussed previously, is intended to prevent discrimination against news businesses based on their participation under the Code, as well as discrimination between registered news businesses. However, there are some concerns that are not solved by that obligation. First, it only applies in relation to registered new media businesses. Some smaller publishers will (by definition) be excluded from participation in the Code as a result of the monetary threshold for participation of AU$150,000 in annual revenue.[61] Second, identical outcomes may not result in substantive non-discrimination where the parties are themselves different. For example, a requirement by a platform that news media businesses receive notifications using a particular technology or interface may impose disproportionate fixed costs on small publishers that would make participation uneconomic or place them at a competitive disadvantage.

Information regarding personal data of platform users

In its open letter, Google complained that the draft Code would jeopardise the privacy of Australian Google users, stating that the draft Code 'could lead to your data being handed over to big news businesses'. It continued to explain to its users that:[62]

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59 Draft NMB Code, cl 52N(2)(c),(d).

60 See, eg, n 8 above, Kevin Rudd.

61 The news business must have annual revenue in excess of AU$150,000 to register under the draft Code: Draft NMB Code, cl 52E, 52G.

62 Google Open Letter.

> 'You trust us with your data and our job is to keep it safe. Under this law, Google has to tell news media businesses "how they can gain access" to data about your use of our products. There's no way of knowing if any data handed over would be protected, or how it might be used by news media businesses.'

In its response to Google's letter, the ACCC refuted several of its claims, including the suggestion that the platforms would be forced to share user data, stating that 'Google will not be required to share any additional user data with Australian news businesses unless it chooses to do so'.[63]

The ACCC's response does seem consistent with the terms of the draft Code, which states that, as part of the minimum standards that will apply to the platforms, the digital platform must ensure that certain information is provided to register news business corporations, including:[64]

- a list and explanation of the data the platform collects about the news business' users 'through their engagement with covered news content made available by the digital platform service';
- a list and explanation of the products and services supplied by the platform that collect such data about the news business' users;
- a list and explanation of the data that the platform has a practice of making available to registered news businesses; and
- 'information about how the registered news business corporation can gain access to the data mentioned in' the previous three bullet points.

These obligations do not expressly mandate any disclosure of user data. However, there is reason to clarify this position in the final Code. In the DPI Report, the ACCC originally recommended that, as part of the proposed Code, the platforms 'would be required to commit to sharing data on users' consumption of the media business' news content on the digital platform'.[65] The ACCC argued that, while consumers would not expect their 'browsing history, search queries or navigation history' to be passed on to media businesses, it was reasonable for media businesses to expect the platforms to provide data about users' consumption of the media business' news content on that platform and that such data 'could make media businesses more competitive in the supply of advertising services'.[66] Accordingly, it is clear that the ACCC did originally propose mandated disclosure of user data.

It may be true that the provision of such user data would allow media businesses to compete more effectively for advertising business, no doubt based in large part on more detailed profiling of consumers. At the same time, the news content an

63 ACCC, 'Response to Google open letter' (17 August 2020): www.accc.gov.au/media-release/response-to-google-open-letter accessed 12 January 2021.

64 Draft NMB Code, cl 52M(1)–(2).

65 ACCC DPI Report, 249.

66 *Ibid*, 248.

individual consumes and the quantity, frequency and timing of that consumption could allow these businesses to infer highly personal information about the individual, including their political views, ethnicity, level of education, sexuality, views on vaccination, health issues, age and family situation.

In the DPI Report, the ACCC highlighted the fact that news businesses can generally only track the behaviour of their users while they are on the news business' website. By contrast, Google and Facebook are able to track consumers across numerous third-party websites, in addition to their own services, due to the embedded Google and Facebook technologies in those third-party websites – such as 'sign-in' with Google or Facebook, Google analytics, the Facebook 'like' button and embedded YouTube videos.[67] News businesses argued that they should have access to more data collected by Google and Facebook about the news businesses' users, including data collected by Google and Facebook via their technologies embedded on the news businesses' own websites.[68]

In other contexts, Google and Facebook have been strongly criticised for these practices of tracking consumers across third-party websites without providing any or adequate opportunities for consumers to opt out of the tracking.[69] These practices do not respect consumer choices and should be stopped. In Australia, this is likely to require increased enforcement of existing privacy regulation as well as the reform of that regulation, in line with several other recommendations by the ACCC in the DPI Report.

After publication of the draft Code, Google argued that the final Code should clarify that the platforms are 'not required to share any additional data, over and above what publishers are already supplied'.[70] Readers might reasonably suspect that this argument is largely driven by Google's commercial interest in the competitive advantage it gains by having exclusive access to certain consumer data, including for its own advertising businesses. Google and Facebook have each been accused of,

67 *Ibid*, 247–248.

68 *Ibid*, 248.

69 Dina Srinivasan, 'The Antitrust Case Against Facebook: A Monopolist's Journey Towards Pervasive Surveillance in Spite of Consumers' Preference for Privacy' (2019) 16 *Berkeley Business Law Journal* 39, 72–81; Facebook Inc i.a. – The Use of Abusive Business Terms pursuant to Section 19(1) GWB (B6-22/16, Bundeskartellamt, Administrative Proceedings, 6 February 2016); Bundeskartellamt, Germany, 'Bundeskartellamt prohibits Facebook from combining user data from different sources: Background information on the Bundeskartellamt's Facebook proceeding' (7 February 2019); ACCC, 'Google Allegedly Misled Consumers on Collection and Use of Location Data' (media release, 29 October 2019); ACCC, 'ACCC Alleges Google Misled Consumers About Expanded Use of Personal Data' (media release, 27 July 2020). See further ACCC DPI Report, 389, 417–418.

70 Google Updated Letter.

and found to have engaged in, a number of unlawful activities that have seriously jeopardised the privacy of their users and other individuals.[71]

However, mandating that Google and Facebook share data about consumers' news consumption with news businesses risks exacerbating the degradation of consumers' privacy. Any proposal to improve competition in advertising services by increasing access to consumers' personal data should be subject to thorough consultation with consumer advocates and privacy advocates, to avoid creating a net social harm.

Overseas comparisons

To provide further context and identify trends relevant to the likely outcomes after legislation of the Code in Australia, this section outlines comparable measures proposed or adopted in other jurisdictions in an effort to require major digital platforms to pay for news content displayed on their platforms.

United Kingdom

In its original recommendation for a Code in the DPI Report, the ACCC expressly referred to the fact that its proposal 'shares many features with' the code proposed in the UK Cairncross Report.[72] In 2018 the UK Government commissioned a review, led by the journalist Dame Frances Cairncross, into the sustainability of the production and distribution of high-quality journalism in a news media market significantly affected by the 'digital revolution'.[73] The first recommendation of the 2019 Cairncross Report was that there should be new codes of conduct to rebalance the relationship between online platforms and publishers: that is, those online platforms upon which publishers increasingly depend for traffic should be required to set out codes of conduct to govern their commercial arrangements with news publishers, with oversight from a regulator.[74]

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71 See, eg, Federal Trade Commission, 'FTC's $5 Billion Facebook Settlement: Record-Breaking and History-Making' (24 July 2019): www.ftc.gov/news-events/blogs/business-blog/2019/07/ftcs-5-billion-facebook-settlement-record-breaking-history accessed 12 January 2021; Office of the Australian Information Commissioner, Australian Government, 'Commissioner Launches Federal Court Action Against Facebook' (9 March 2020): www.oaic.gov.au/updates/news-and-media/commissioner-launches-federal-court-action-against-facebook accessed 12 January 2021; ACCC, 'Google Allegedly Misled Consumers on Collection and Use of Location Data' (media release, 29 October 2019); ACCC, 'ACCC Alleges Google Misled Consumers About Expanded Use of Personal Data' (media release, 27 July 2020).

72 ACCC DPI Report, 254.

73 Cairncross Review, 5.

74 *Ibid*, 90.

The ACCC originally proposed that the ACCC and the ACMA would 'engage with the regulator responsible for overseeing the code of conduct proposed in the Cairncross Review' in the interests of international cooperation, shared learning from each other and, where appropriate, alignment of approaches to achieve the same objectives.[75] The UK Government has responded to the Cairncross Report, stating it agrees that there is an unequal relationship between publishers and search and social media platforms, that 'codes of conduct that formalise the relationships between news publishers and online platforms may help to rebalance that relationship'[76] and that it is working on this recommendation as part of a broader programme of work in respect of competition in digital markets. However, at this stage, the UK Government has not taken steps to implement this recommendation.[77] It seems unlikely there will be cooperation or shared learning on such codes between the two jurisdictions in the immediate future.

France

In 2019 France became the first country to implement the 2019 European Union Directive on Copyright in the Digital Single Market[78] into its national law.[79] The Directive permits publishers to request 'an appropriate share of revenues' as fees (referred to as a 'neighbouring right') from online platforms when the platforms display content online.[80] Google responded by stating it would show 'stripped-down' French news search results, limiting the use of snippets or thumbnail images from European publishers where the publishers did not provide their explicit consent.[81]

75 ACCC DPI Report, 255.

76 UK Department for Digital, Culture, Media and Sport, 'Government response to the Cairncross Review: a sustainable future for journalism' (policy paper, 27 January 2019) [10]–[11].

77 While the government's response on the media code recommendation was expected after the report on the Competition and Markets Authority's (CMA) market study into online platforms and digital advertising, that report was published in July 2020, without any subsequent announcement on the media code recommendation: UK Department for Digital, Culture, Media and Sport, 'Government response to the Cairncross Review' [12]–[13]; CMA, 'Online platforms and digital advertising: Market study final report' (1 July 2020, market study report).

78 Directive 2019/790 of 17 April 2019 on copyright and related rights in the Digital Single Market and amending Directives 96/9/EC and 2001/29/EC [2019] OJ L 130/92.

79 The French law was passed on 24 July 2019 and entered into force on 24 October 2019: Autorité de la Concurrence, 'Related rights: The Autorité imposes urgent interim measures on Google' (media release, 9 April 2020). Other Member States are required to translate the Directive into domestic legislation by June 2021: Directive 2019/790 of 17 April 2019 on copyright and related rights in the Digital Single Market and amending Directives 96/9/EC and 2001/29/EC [2019] OJ L 130/92, Art 29(1).

80 Directive 2019/790 of 17 April 2019 on copyright and related rights in the Digital Single Market and amending Directives 96/9/EC and 2001/29/EC [2019] OJ L 130/92, Art 15(5).

81 Aoife White, 'Google to strip down French news results under new rules' *Bloomberg* (25 September 2019), www.bloomberg.com/news/articles/2019-09-25/google-to-change-french-news-results-under-copyright-rules accessed 12 January 2021.

However, the Autorité de la Concurrence granted requests for urgent interim measures sought by publishers and the news agency Agence France Presse, ordering Google to 'negotiate in good faith' with French publishers for licensing fees for the reuse of their protected contents, within a three-month window.[82] In granting the publishers' requests, the Autorité found that Google's practices (that is, its threats to limit its display of news unless publishers consented to such display without remuneration) were likely to constitute an abuse of a dominant position.[83]

Google appealed the decision to the Paris Court of Appeal, arguing that it was adequately compensating news businesses by sending referral traffic to them. The Court dismissed the appeal, upholding the order of the Autorité requiring Google to negotiate with French publishers.[84] At the same time, Google indicated it had nearly reached a deal with French publishers to accept the neighbouring rights regime and pay publishers through its new News Showcase product.[85]

Spain

In 2014 Spain enacted a copyright law – nicknamed the 'Google fee'[86] – that required news aggregators to compensate publishers for displaying news snippets and links to news stories.[87] The law allows for sanctions of up to US$758,000 for violations.[88] Leading up to the introduction of the law, Google threatened to shut down its news aggregator service, Google News, in Spain.[89] It followed through on

82 Autorité de la Concurrence, 'Related rights: The Autorité imposes urgent interim measures on Google' (media release, 9 April 2020). See also Thibault Larger and Laura Kayali, 'French publishers win decisive battle against Google' *Politico* (4 September 2020), www.politico.com/news/2020/04/09/french-publishers-win-decisive-battle-against-google-177686 accessed 12 January 2021.

83 *Ibid*, Autorite de la Concurrence.

84 'French court: Google must open payment talks with publishers' *AP News* (8 October 2020), https://apnews.com/article/paris-europe-archive-france-676170fc19d38cb4d6a8885f9f839d7c accessed 12 January 2021; Natasha Lomas, 'Google must negotiate to pay for French news, appeals court confirms' *TechCrunch* (8 October 2020), https://techcrunch.com/2020/10/08/google-must-negotiate-to-pay-for-french-news-appeals-court-confirms accessed 12 January 2021.

85 Foo Yun Chee, 'Google poised to strike deal to pay French publishers for their news' *Reuters* (8 October 2020), www.reuters.com/article/us-alphabet-france-publishing/google-poised-to-strike-deal-to-pay-french-publishers-for-their-news-idUSKBN26S33C accessed 12 January 2021.

86 Mariana Marcaletti, 'Under Spain's 'Google Fee' law, news aggregators must pay publishers' *The Washington Post* (26 July 2014), www.washingtonpost.com/news/business/wp/2014/07/25/under-spains-google-fee-law-news-aggregators-must-pay-publishers accessed 12 January 2021.

87 Ley de Propiedad Intelectual 1996 (Spain), art 32.2.

88 Joe Mullin, 'Country by country, Europe falls in and out of love with a "Google tax"' *ArsTechnica* (1 November 2014), https://arstechnica.com/tech-policy/2014/10/country-by-country-europe-falls-in-and-out-of-love-with-a-google-tax accessed 12 January 2021.

89 Chris Johnston, 'Google 'Plays Hardball' in Spanish news row' *The Guardian* (16 December 2014), www.theguardian.com/technology/2014/dec/15/google-spanish-news-row accessed 12 January 2021; Eric Auchard, 'Google News to go dark in Spain over copyright fees' *The Sydney Morning Herald* (12 December 2014), www.smh.com.au/technology/google-news-to-go-dark-in-spain-over-copyright-fees-20141212-125hud.html accessed 12 January 2021.

the threat. Once the law was passed, Google closed Google News in that jurisdiction, and it remains unavailable in Spain.[90]

In 2015 a group of publishers commissioned a report which found that the Google fee law had an anti-competitive effect on online publishing, and that there was no real justification for the imposition of the fee.[91] The report suggested that:[92]

> 'an external intervention is not necessary and that solutions do exist for this alleged problem through bilateral negotiations between the parties. Indeed, this has occurred in countries including France, Belgium, and Germany, and at European level, where there have been attempts to implement a similar fee and where aggregators (particularly Google News) and publishers have reached "cooperation agreements".'

Germany

In 2013 Germany passed an ancillary copyright law, effectively requiring Google and other online search engines and news aggregators to pay for quotation snippets.[93] Headlines and very small text blocks were exempt from the remuneration obligation.[94] According to the new law, '[t]he publishers of newspapers and magazines shall have the exclusive right to make the newspaper or magazine or parts thereof available to the public for commercial purposes, unless it consists of individual words or very short text excerpts'.[95] This right was transferable and would expire one year after the publication of the newspaper or magazine.[96] The law further provided that it would be 'permissible to make the newspaper or magazine

90 Natasha Lomas, 'Google and Facebook must pay media for content reuse, says Australia' *TechCrunch* (21 April 2020), https://techcrunch.com/2020/04/20/google-and-facebook-must-pay-media-for-content-reuse-says-australia/?guccounter=1 accessed 12 January 2021.

91 NERA Economic Consulting, 'Impacto del Nuevo Artículo 32.2 de la Ley de Propiedad Intelectual: Informe para la Asociación Española de Editoriales de Publicaciones Periódicas (AEEPP)' (9 July 2015, report).

92 *Ibid*, xii.

93 With effect from 1 August 2013: Gesetz über Urheberrecht und verwandte Schutzrechte (Law on copyright and related rights) s 87f inserted by achtes Gesetz zur Änderung des Urheberrechtsgesetzes (Eighth Law amending the Law on Copyright) of 7 May 2013.

94 Gerrit Weismann, 'Axel Springer persists with Google demands' *Financial Times* (London, 6 March 2013).

95 Gesetz über Urheberrecht und verwandte Schutzrechte (Law on copyright and related rights) [87f]. For these purposes, a newspaper or magazine is defined as the editorial and technical preparation of journalistic contributions that are compiled and published periodically on any media under one title, which, after an assessment of the overall circumstances, is to be regarded as largely typical for the publishing house and the overwhelming majority of which does not serve self-advertising purposes. Journalistic contributions are, more specifically, articles and illustrations which serve to disseminate information, form opinions or entertain.

96 Gesetz über Urheberrecht und verwandte Schutzrechte (Law on copyright and related rights) [87g].

or parts thereof available to the public unless this is done by commercial operators of search engines or commercial operators of services that similarly publish content'.[97]

Google campaigned against the proposed amendments, aiming to mobilise German internet users in support of its position, with messages such as 'defend your web' and 'protect your web – find what you're looking for'.[98] Ultimately, the legislation passed was less onerous than initially proposed, since it excluded 'single words or very short text excerpts' from the remuneration obligation.[99]

By 2014, in compliance with the law and in response to legal action brought by VG Media, Google published only the headlines of articles unless publishers gave express consent for their content to be published by Google.[100] However, even the biggest German publisher, Axel Springer, subsequently agreed to Google's terms,[101] providing consent for its content to be published by Google, noting that it was forced to do so after traffic to its website fell sharply during the two weeks in which it refused consent for Google to publish without remuneration. Axel Springer regarded the dramatic drop in traffic to its publications as 'proof of Google's overwhelming power in the search market'.[102]

In 2017, the Landgericht Berlin sought intervention by the European Court of Justice, which in 2019 ruled that the German law was not enforceable and 'must be disregarded' on the basis that the regulation was a technical regulation of the

97 Gesetz über Urheberrecht und verwandte Schutzrechte (Law on copyright and related rights) [87g]. Gesetz über Urheberrecht und verwandte Schutzrechte (Law on copyright and related rights) [87h] provides that 'The author shall be entitled to an equitable share of the remuneration'.

98 Michiel Willems, 'Google campaigns against German tax proposals' *SNL Kagan Media & Communications Report* (Charlottewville, 30 November 2012); Gerrit Wiesmann, 'Google goes public over German copyright law' *Financial Times* (London, 27 November 2012).

99 Cornelius Rahn and Rainer Buergin, 'Google defeats publishers over web copyright in German vote' *Bloomberg* (1 March 2013), www.bloomberg.com/news/articles/2013-03-01/google-defeats-publishers-over-copyright-in-german-parliament accessed 12 January 2021.

100 Philipp Justus, 'News zu News bei Google' (Google Germany blog post, 1 October 2014), https://germany.googleblog.com/2014/10/news-zu-news-bei-google.html accessed 12 January 2021. VG Media, a consortium made up of about 200 publishers, took Google to regional court (Landgericht Berlin) for violation of the law.

101 According to Harro Ten Wolde and Eric Auchard, 'Germany's top publisher bows to Google in news licensing row' *Reuters* (Frankfurt, 6 November 2014), Google 'require[d] publishers who want their content to continue to show up in Google search results to give it explicit permission to do so and freedom from any liability for licensing fees under such laws'.

102 Harro Ten Wolde and Eric Auchard, 'Germany's top publisher bows to Google in news licensing row' *Reuters* (Frankfurt, 6 November 2014).

kind required to be communicated to the European Commission, which had not in fact been notified.[103]

Belgium

In 2006 three collecting societies in Belgium – Copiepresse, a news publishers trade group, SAJ, a journalism trade group, and Assucopie, a scientific, research and educational publishers trade group[104] – brought an action against Google, alleging copyright violations for its use of snippets and headlines in Google News and by virtue of its caching system. At first instance, the High Court of Brussels found that Google infringed the copyright of Belgian publishers (by default, as Google failed to appear at the hearing). It ordered Google to withdraw the infringing material from Google News and from its caching system and to establish a procedure that would require Google to take down any republished copyrighted material on 24 hours' notice from a collecting society or its members.[105]

Google opposed the default order, resulting in a case review by the High Court. In 2007 the High Court affirmed the original order, holding in part that the Google cache and Google News unlawfully reproduced original parts of copyrighted works.[106] On appeal to the Court of Appeal of Brussels in 2011, the Court affirmed the decision at first instance, relevantly requiring Google to withdraw infringing material from Google News and its cache (and to pay €25,000 per day for failure to do so).[107] In response, Google removed Copiepresse newspapers from all its search

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103 *VG Media Gesellschaft zur Verwertung der Urheber- und Leistungsschutzrechte von Medienunternehmen mbH v Google LLC* (Court of Justice of the European Union, C-299/17, ECLI:EU:C:2019:716, 12 September 2019); Court of Justice of the European Union, 'A German provision prohibiting internet search engines from using newspaper or magazine snippets without the publisher's authorisation must be disregarded in the absence of its prior notification to the Commission' (press release No 108/19, 12 September 2019). See also Foo Yun Chee and Klaus Lauer, 'Google wins legal battle with German publishers over fee demands' *Reuters* (US, 12 September 2019).

104 Philippe Laurent, 'Copiepresse SCRL & alii v. Google Inc. – In its decision of 5 May 2011, the Brussels Court of Appeal confirms the prohibitory injunction order banning Google News and Google's "in cache" function' (2011) 27(5) *Computer Law & Security Review* 542.

105 Philippe Laurent, 'Google News banned by Brussels High Court – Copiepresse SCRL v. Google Inc. – Prohibitory injunction of the President of the High Court of Brussels, 5 September 2006' (2007) 23(1) *Computer Law & Security Review* 82.

106 Philippe Laurent, 'Brussels High Court confirms Google News' ban – Copiepresse SCRL v. Google Inc. – Prohibitory injunction/stop order of the President of the High Court of Brussels, 13 February 2007 [opposition procedure against the first default stop order by the same President]' (2007) 23(3) *Computer Law & Security Review* 290.

107 Philippe Laurent, 'Copiepresse SCRL & alii v. Google Inc. – In its decision of 5 May 2011, the Brussels Court of Appeal confirms the prohibitory injunction order banning Google News and Google's "in cache" function' (2011) 27(5) *Computer Law & Security Review* 542.

results and Google News.[108] After that action, Copiepresse agreed to allow Google to use its content in its cache and to permit Google to re-index its newspaper websites for Google search (although the content was still not included on Google News).[109]

The following year, Google and the publishers reached an agreement that was to end 'all litigation' involving partnerships on a range of business initiatives aiming to promote the publishers' and Google's services, increase publisher revenue, increase reader engagement and increase content accessibility.[110] It appears that this involved Google buying 'millions of dollars of advertising' (reportedly, about US$6m) from the publishers, as well as paying the publishers' legal fees.[111] It did not involve any admission of copyright infringement or take the form of remuneration for news content.[112]

Conclusion

According to the Australian Government, the news content produced by Australian news media businesses has significant value for large digital platforms such as Google and Facebook, including the indirect value from users being more likely to frequent platforms that incorporate news content, and the increased trust and legitimacy associated with a platform that offers news content. The government believes that these platforms should provide some remuneration for the value they receive – under a mandatory code if necessary – rather than relying on their market power to refuse payment and deprive news businesses of vital funding for journalistic content. Google and Facebook each vigorously dispute these claims, arguing that they receive very little benefit from making such news available on their platforms and instead provide enormous benefits to news businesses in the form of referral traffic from their platforms, and resulting advertising and subscription revenue.

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108 Matthew Lasar, 'Google v Belgium 'link war' ends after years of conflict' *ArsTechnica* (20 July 2011), https://arstechnica.com/tech-policy/2011/07/google-versus-belgium-who-is-winning-nobody accessed 12 January 2021.

109 Peter Ollier, 'Google puts Copiepresse back in search results' (2011) *Managing Intellectual Property*; Steven Musil, 'Google settles copyright dispute with Belgium newspapers' *CNet* (13 December 2012), www.cnet.com/news/google-settles-copyright-dispute-with-belgium-newspapers accessed 12 January 2021.

110 Thierry Geerts, 'Partnering with Belgian news publishers' (Google Europe blog post, 12 December 2012), https://europe.googleblog.com/2012/12/partnering-with-belgian-news-publishers.html accessed 12 January 2021.

111 Xavier Ternisien, 'En conflit avec la presse belge, Google accepte de l'indemniser' *Le Monde* (Paris, 13 December 2012); Stephanie Bodoni, 'Google, Belgian Newspapers Settle Copyright Link Dispute' *Bloomberg* (14 December 2012), www.bloomberg.com/news/articles/2012-12-13/google-belgian-newspapers-settle-copyright-dispute-over-links accessed 12 January 2021.

112 See n 110 above.

Over the past 15 years, there is a clear trend of Google reducing or eliminating the availability of news content on its services in other jurisdictions when regulation has been introduced in an effort to mandate payment for online news content. In a number of cases, Google has removed the relevant news content from its services to avoid payment under the regulation, used legal avenues to challenge the regulation and negotiated with publishers on its own terms outside the regulation, generally avoiding establishing any precedent for direct payment for news content. In Australia, Facebook has now similarly threatened to ban the posting of news content by Australian publishers and users to avoid mandated payment for news content.

Under the Australian Code, the non-discrimination obligation and substantial penalties for breaching it make it unlikely that the platforms would attempt to target individual news businesses for exclusion based on the news business' attempts to rely on the Code to negotiate for remuneration. The stakes are higher. Google or Facebook would need to prevent the availability of all Australian news content to avoid paying remuneration under the Code. There is an opportunity for an interesting natural experiment concerning the actual value of news content to the relevant digital platforms services' if either platform proceeds with that strategy when the Code is enacted.

About the author

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Systems competition – China's challenge to the competition order

Do we need new rules to protect a level playing field for competition with firms from non-European Union countries?

Dr Thorsten Käseberg and Dr Sophie Gappa[1]

Introduction: a systemic challenge to the competition order

The European Union, and in particular Germany, have prospered from openness for trade and investment as part of the common commercial policy since the entry into force of the Treaty of Rome in 1958. Although there have been dry spells in international trade policy since the Second World War, there has been a long trajectory towards ever more trade and globalisation, which culminated in the accession of China to the World Trade Organization in 2001. Though many expected Chinese industry to move up along the value chain, commentators did not foresee the speed by which China would catch up and even overtake Western companies in certain high-tech and future sectors. More importantly, the working assumption that the Chinese economic and social model would converge towards Western models has not materialised. Its model of state capitalism (as of today) raises serious challenges to the EU's order based on economic and personal freedom, competition and individual privacy.

1 The authors write in their personal capacity.

The cornerstones of the European economic order include: (1) the four freedoms, which secure the internal flow of people, goods, services and capital; (2) the common commercial policy including adherence to WTO rules and international law; and (3) competition and state aid policy, including restrictions on public undertakings. Three elements of the Chinese model stand out for being particularly at odds with the EU's competition-based order: (1) extensive state ownership; (2) extensive state financing (in various forms); and (3) regulation that shields Chinese economic actors against foreign competition in the Chinese markets. While all these elements are not confined to China, the dimension of their strategic use is unique. In combination with an ever-growing economic clout of the Chinese economy, this has become a significant systemic challenge.

Distortive strategies and effects

One might argue that the present situation of relatively restricted access to the Chinese market for EU firms and a relatively unrestricted access for Chinese firms to the internal market may be preferable from a (short-term) economic welfare perspective (even for the EU) to a situation of a relatively restricted access to both markets. However, even leaving aside the human rights perspective, one cannot ignore the fact that the Chinese model: (1) is at risk of distorting the legitimacy of the game through 'financial doping'; (2) may lead to the loss of European players and inefficiency; and (3) the EU is at risk of losing its sovereignty in certain sectors of the economy. Therefore, Chinese state capitalism raises a systemic challenge.

In its 2019 EU-China strategic outlook, the European Commission (the 'Commission') identified a long list of distortive strategies applied by China, including:

> '… selective market opening, licensing and other investment restrictions, subsidies to both state-owned and private sector companies, closure of its procurement market, localisation requirements, including for data, the favouring of domestic operators in the protection and enforcement of intellectual property rights and other domestic laws, limiting access to government-funded programmes for foreign companies, and onerous requirements to access the Chinese market'.

One may add monopoly positions for Chinese companies in their home market and the resulting scale advantages, a preference for Chinese companies in the whole value chain as well as predatory pricing strategies.

As evident as these points may seem on a theoretical level, it would be worthwhile to obtain empirical evidence, or at least estimations, on the relative size of the distortions on competition and trade due to state-owned enterprises (SOEs) and subsidies as compared with other strategies mentioned. This may lead to the core

problem, which is that although Article 25 of the WTO Agreement on Subsidies and Countervailing Measures (SCM Agreement or ASCM) requires WTO members to notify subsidies to ensure transparency and allow other members to review each other's actions in this regard, the level of compliance by WTO members with this requirement has deteriorated significantly.[2] So the lack of evidence could be part of the systemic problem.

Nevertheless, qualitatively, the ways through which such measures may distort competition in the internal market are well known. Not only can they shield inefficiency, but they may also divert demand away from or discourage entry by more efficient suppliers, lead to inefficient resource allocation and market power problems, allow the acquisition of assets and shares at inflated prices, shift value creation to third states and lead to long-term disadvantages in R&D and innovation for future technologies.

Covid-19 and the level playing field

The coronavirus crisis has aggravated fears of a more uneven level playing field in several regards. First, companies with a digital business model have increased their market share at the expense of those that have not digitised their business. This substitution in demand, however, does not qualify as a level-playing field challenge from an economic point of view and should instead be seen as a driver for more efficient and future-proof business models.

Second, the different fiscal position of EU Member States has allowed some governments to step in through various instruments, ranging from taking control or shareholdings to giving credit and guarantees, to a very different extent. Although the prospective of having such policy leeway in times of crisis is a beneficial incentive to improve the fiscal position in normal times, the playing field between companies inside the internal market nevertheless should not be distorted – both in normal times and even more in times of crisis, when companies are at the margin, the game should be decided by efficiency, not by the relative strength of Member States granting aid. Therefore, EU state aid rules including the Commission's Temporary Framework play a central role in keeping up a level playing field in the Internal Market.

Third and most important in this context, the fear in particular of strategic takeovers of weakened EU companies by Chinese SOEs or firms that benefit significantly from government funding has increased the willingness of EU policymakers to consider stricter control of takeovers of EU companies by non-EU players.

2 Therefore, the EU proposal on the modernisation of the WTO did include a proposal to enhance transparency.

This fear has been based to some extent on the increase in acquisitions by Chinese companies after the financial crisis. While the United States has limited Chinese investment on the basis of national security concerns, in 2018 Chinese investment into the EU27 (excluding the United Kingdom) had the largest growth and reached 70 per cent of China's total foreign M&A in value.[3] Aggregate data shows that, so far, the fear of more foreign M&A activity in the wake of the Covid-19 pandemic in terms of overall investment has not materialised. However, it would be valuable to also have qualitative data on: (1) which (strategic) sectors and assets Chinese and other non-EU economic operators invest in; (2) whether they are willing to pay a mark-up over the market price; and (3) most importantly, whether they benefit from state aid.

Gaps in the EU's defence of its level playing field

To achieve market access and reciprocity for EU companies, the Commission's China Communication vows to reform the WTO – in particular on subsidies and forced technology transfers – conclude bilateral agreements on investment and adopt the International Procurement Instrument. The main action point, however, singles out foreign state ownership and state financing of foreign companies and promises to assess how the EU could appropriately deal with their distortive effects on the internal market.

The bloc's present economic toolbox does not cover the aforementioned distortive effects. First, EU competition rules apply without discrimination. In principle, they are not, and should not be, asymmetrical industrial or trade policy leveraging tools. In particular, EU merger control does not allow the Commission to intervene against the acquisition of a European company solely on the grounds that the buyer benefited from foreign subsidies. It should be mentioned here that there are ways to interpret and enforce existing rules in a more robust way against distortions due to SOEs and subsidies. A German-French-Polish paper has called for the state control of undertakings to be taken into account when calculating turnover, as well as the financial power of state-controlled and subsidised undertakings when deciding in substance on mergers. Academics have gone further and suggested treating all Chinese acquirers as part of a single broad syndicate in merger review and assuming an underlying coordination scheme in antitrust investigations.[4] Nevertheless, past and present reviews of mergers with Chinese acquirers show that it is extremely hard to obtain reliable information on state

3 Alicia Garcia Herrero, 'Europe in the midst of China-US strategic competition: What are the European Union's options?' Bruegel Working Paper (2019).

4 Nicolas Petit, 'Chinese State Capitalism and Western Antitrust Policy' American Security Project Paper (2016).

ownership and corporate control structures. As long as sufficient transparency is lacking, an assumption on single control at least for the question of notification might be an option. However, even such an interpretation would leave a significant gap in the toolbox.

Second, EU state aid instruments only cover aid granted by Member States. In contrast, subsidies granted by non-EU authorities fall outside EU state aid control, even where such foreign subsidies distort competition in the internal market.

Third, on a multilateral level, the existing instruments do not fully reflect the European standards for state aid. The SCM Agreement, for example, is limited in scope in that it only applies to goods, not services or investments. Therefore, double standards exist with regard to foreign and European subsidies and in many cases the EU cannot bring litigation against a WTO member even though a certain foreign subsidy would not meet European standards. Thus, EU trade defence instruments (safeguard and countervailing measures, such as anti-dumping and anti-subsidy policies) have a significant blind spot. These instruments do not cover all potential effects of unfair subsidies or support measures by non-EU countries because they are limited to those subsidies that are captured under the SCM Agreement. Additionally, they apply only in situations of subsidised or dumped imports of goods in the internal market. Also, anti-subsidy policy only captures public financial contributions, which are confined to a specific company, industry or group of companies or industries producing or exporting goods; it does not cover state ownership.

In addition, the existing EU public procurement framework does not specifically address distortions to the European procurement markets caused by foreign subsidies, and it does not allow, in principle, for the exclusion of a bidder solely on the ground that it might have benefited from distortive foreign subsidies.

Potential goals and instruments

Closing the aforementioned gaps is not an end in itself. A new instrument may serve several principal goals, gaining leverage or setting incentives in the systems' competition to achieve: (1) a change in China's strategy on SOEs and subsidies; (2) a general WTO solution; (3) in bilateral trade negotiations reciprocal access to the Chinese markets; or (4) obtaining a more level playing field inside the internal market.

Ideally, the new instrument would serve all purposes cumulatively. The most important one, however, is the fourth. While there are several (existing or potential) instruments for tackling specific aspects of the systemic challenge of state capitalism, notably the goal of levelling distortive effects in the internal market has not been

the centre of attention so far, and the other instruments are not designed to serve this objective. The goal of the International Procurement Instrument (IPI), for example, is to set incentives in trade negotiations in order to open procurement markets outside the EU for EU economic operators. In its present form it would not tackle distortions of procurement processes in the internal market that arise from foreign subsidies granted to firms participating in EU procurement markets.

Closely related to the question of what goal a new instrument can and should serve is whether the EU is willing to 'extend' its rules to scrutinise aid granted by non-EU governments to companies operating on the EU market. The EU has bound itself beyond WTO rules through its state aid rules and through the application of competition and state aid rules to public undertakings (Article 106(1) of the Treaty on the Functioning of the European Union). Defending and leveraging its economic order could mean that the EU has to put in place instruments to achieve goals and rules beyond what has been agreed on an international level as a minimum standard – potentially similar to a carbon border tax.

On a theoretical level, there are four possible options for a more even level playing field in the internal market: (1) reaching consensus with China about its economic operations in the market, either on multilaterally, plurilaterally or bilaterally; (2) lowering the material standards of the EU economic policy, notably in competition law; (3) extending the EU's toolbox in order to be able to tackle distortions where they arise; and (4) raising public investments for EU companies.

Looking back at the gaps and goals, from an economics textbook perspective, but also in the view of adherents to traditional trade policy and diplomats who fear retaliation, the first-best solution would be a reform and stricter implementation of the WTO rules, in particular of the SCM Agreement. To this end, the EU joined the US and Japan to form the so-called trilateral cooperation. Although they were able to agree at the beginning of this year that, for example, new types of unconditionally prohibited subsidies should be added to the SCM Agreement, there was no further progress reported since. Looking at the state of the negotiating function of the WTO, it is barely realistic that, despite continued EU efforts, all 164 members, including China, will any time soon agree on a modernised SCM Agreement to discipline subsidies in an effective way.

Second, changing existing instruments under EU law is not desirable. This applies both to trade instruments and competition policy. With regard to the control of external trade, as has been pointed out, the focus is on the distortion of trade flows, and the remedies are confined to border measures such as import duties. Targeting distortive state ownership and subsidies at the source or the border would be difficult to implement. With regard to investment screening, one might think about extending it to include anti-subsidy or, more broadly, 'strategic' EU interests.

The focus of the existing framework, however, is on technology and security issues, which are very different from distortions on pricing. Of course, it may even be a typical scenario where industrial strategy leads to the use of subsidies to acquire a technologically sensitive asset. Such a purchase may even lead to competition issues. From an analytical and institutional perspective, however, there are good reasons to keep separate those three different perspectives for the assessment of the acquisition.

Similarly, changing competition rules or their interpretation would only be feasible on the basis of non-discrimination. Taking into account state ownership within turnover calculation and subsidies within a market power assessment can and should be done – but as a matter of principle also with regard to EU firms. There is no asymmetric option in the sense of a laxer control of mergers of EU firms or a stricter control of non-EU firms. A general relaxation of EU competition policy to allow for the creation of 'European champions' would come at a high price in several forms: higher prices for European downstream firms and consumers, lower competitiveness and the loss also of the ability to intervene in non-EU cases.

The third option – extending the EU's regulatory toolbox – is the one the EU Commission has recently proposed; it will be the focus of the remaining section.

The fourth option would be the creation of an EU sovereign wealth fund. The Commission has indeed also recently sketched out plans for a 'European Future Fund'. Such an instrument would to some extent amount to copying China's playbook. Its legitimacy and efficiency would hinge to a large extent on the definition of its goals and functions (and their enforcement through its governance). As an instrument of last resort to counter an inflated takeover, it might be a strategic ad hoc complement to other tools. A better defensive instrument, however, would be the power to check publicly subsidised bids and restore normal conditions on the takeover market instead of using taxpayers' money. As a forward-looking instrument to invest in future growth sectors, a sovereign wealth fund may be used in those instances where control by the EU, or at least a residual degree of control through a minority investment, for a specified time period serves a specified strategic interest. It would be imperative to apply EU rules on state aid 'by analogy' to such a vehicle to keep it on a sound level-playing field footing. An EU fund may be preferable or at least a good complement to investment vehicles of the Member States in order to have a common EU strategy and ensure a level playing field within the EU.

As pointed out, except for the third one, all the aforementioned options do not go into heart of the challenge, which is the distortion that arises in the internal market through financial advantages from state resources for undertakings from non-EU Member States that operate inside the market. Therefore, from a conceptual point

of view, there is reasonable economic policy space for the proposals put forward by the Commission in its white paper on foreign subsidies. The significant advantage of this option is that it would allow, if designed properly, for addressing distortions of competition in the internal market without watering down the principles of the EU economic order and at the same time preserving the neutrality of its existing core instruments.

The proposals may come at a critical time in two regards: first, the saga in the US around the video-sharing app TikTok shows that a strong but rule-based approach to foreign economic operators' activities that clearly separates competition, security and subsidy aspects may be preferable in the long run to ad hoc discretionary intervention. The EU's debate will certainly be followed also from this perspective in other parts of the world, since the rise of China and ensuing tensions will probably even rise in the future.

Second, follow-up legislation to the Commission's proposal may also provide a regulatory backstop for the EU if the ongoing negotiations with the UK do not result in a commitment by the UK to keep up respect of the EU state aid rules when granting subsidies to UK companies that will be active in the internal market in the future.

The Commission's white paper

The 'White Paper on foreign subsidies in the Single Market' adopted by the Commission on 17 June 2020 attempts to address the distortive effects caused by foreign subsidies in the internal market, in particular by putting forward three modules. The Commission regards these modules as complementary to each other, rather than as substitutes. One main question for further debate will indeed be whether the legislative proposal should build on all three modules.

Module 1 – the broadest instrument – suggests a general market scrutiny instrument to capture all potential market situations in which foreign subsidies may have distortive effects in the internal market. It would be enforced by the Commission or a national authority, which could act *ex officio* in the case that a firm in the EU benefits from a foreign subsidy. The supervisory authority would assess the distortive effect of the subsidised activity or investment as well as the potential positive impact, which may outweigh the distortion ('EU interest test'). If the authority establishes a net negative impact, it may impose measures to remedy the likely negative effect, for example, redressive payments and structural or behavioural remedies. The white paper proposes a two-step procedure: first a preliminary review, then an in-depth investigation.

Several main questions arise: first, how should subsidies be defined? If the objective is to achieve a level playing field in the internal market, the concept should be close to the definition of 'state aid' as under EU law addressed to Member States. Another argument for a close alignment to the already existing concept of state aid is WTO compatibility.

Second, how does one assess and establish a distortive effect? The white paper suggests assuming that certain categories of foreign subsidies are likely to create distortions in the internal market because of their nature and form. These categories of foreign subsidies, for example, export financing or debt forgiveness to ailing enterprises, should be found to create distortions in the internal market. Further, the white paper suggests taking into account several indicators, such as the relative size of the subsidy and the situation on the market concerned. While the white paper also mentions the market conduct, it does not appear to endorse a Dutch proposal[5] that suggested adopting an abuse-of-dominance-like test. In that regard, and this makes sense, the white paper adopts more of a state aid test than a competition law test (such as a test as under abuse of dominance law).

Third, should positive effects of a subsidy be taken into account? If so, how? The white paper suggests 'where there is evidence of a possible positive impact that the supported economic activity or investment might have within the EU or on public policy interests recognised by the EU, the distortion should be weighed up against such possible positive impact'. According to the white paper, the possible positive impact may consist of the EU's public policy objectives. Such balancing test would be highly problematic for two main reasons: (1) its openness would make the instrument very complex to handle and open to political influence; and (2) even more important, with such wide balancing, it has no precedent in EU competition and state aid law. Although state aid law acknowledges public policy interests, it does so in a limited way. Under the balancing test as envisaged in the white paper a Chinese SOE, subsidised by the Chinese state, would be allowed to use its subsidy to outcompete firms in the internal market or acquire a European firm if the distortion of competition would be outweighed by, for example, job gains. Such a test would not only be hard to implement. It would predictably lead to bickering among Member States if, for example, Member State A benefits from the subsidy, while the disadvantaged competitor is located in Member State B. Although this is similar under the present state aid regime, the open-endedness of the white paper's approach would give this challenge a new dimension.

The fourth question is: how does one limit such far-reaching instrument in practice? While it may be beneficial both from a strategic leveraging perspective

5 Dutch Permanent Representation, *Strengthening the Level Playing Field on the Internal Market* (December 2019).

and from a substantive point of view to have an open test that would be able to capture all potential subsidies and their distortive effects, enforcement resources will and should be a limiting factor. How to design enforcement priorities will be crucial under such a test. One option for limitation could be to preclude actions for failure to act and to entirely rely on an *ex officio* enforcement system.

The resource question is intertwined with the fifth question: which institution should enforce the instrument? From a political economy perspective, there are many good arguments why ultimately it should be the European Commission which is best placed to enforce the instrument in a consistent manner. It can be less easily played off by non-EU jurisdictions and firms than individual Member States. On the other hand, the Commission may be well advised to draw on Member States' information and resources. The white paper envisages a system similar to the present European Competition Network regime for antitrust cases with two add-ons: (1) the option that several national authorities investigate jointly; and (2) that the Commission has the right to decide on the EU interest test. Another approach would be to leave the decision-taking in the hands of the Commission, while giving Member States' authorities rights to consult and intervene.

Module 2 focuses on foreign subsidies that facilitate the acquisition of EU firms. It intends to ensure that foreign subsidies do not give an unfair advantage on their recipients when they acquire stakes in EU firms. Under this module, the white paper proposes two different threshold concepts. Under one approach firms that benefit from financial support of a non-EU state would need to notify their acquisitions of EU undertakings, above the threshold of €100m of EU-wide turnover, to the Commission. If the Commission finds that the acquisition is facilitated by the foreign subsidy and distorts the internal market, it may either accept commitments by the notifying party that effectively remedy the distortion or, as a last resort, it could prohibit the acquisition. Under this module, the Commission would also apply the EU interest test.

The proposal for this module raises similar questions to module 1. However, there are also specific issues to be discussed further in the legislative procedure:

- First, the turnover threshold as proposed in the white paper appears to be too low and might be over-inclusive, also with a view to resources and red tape. Therefore, it may be necessary to transfer the higher threshold from the EU Merger Regulation of €250m of EU-wide turnover for the target.
- Second, with regard to procedure, the white paper, as for module 1, suggests to 'copy' the current distinction of phase 1 and phase 2 such as in merger control. While this appears reasonable, the Commission should ensure that the investigations under the new instrument would indeed run in parallel as much as possible to a potential merger review and an investment screening investigation.

- Third, under the white paper's test, the Commission would have to verify whether a (potentially) subsidised buyer acquires an EU target and whether this acquisition would lead to distortions in the internal market. While it appears sound to require causality between the planned acquisition and the distortive effect, it would be very difficult for the Commission to verify the link between the subsidy and the planned acquisition.

Module 3 addresses non-EU subsidies that enable bidders to gain an unfair advantage, for example, by submitting bids below market price or even below cost, which allow them to win public procurement contracts they would otherwise not have won. The white paper suggests a mechanism under which bidders would have to notify the contracting authority of financial contributions received from non-EU countries. The contracting and supervisory authorities would then investigate whether there is a foreign subsidy and whether it made the procurement procedure unfair. If these conditions are met, the bidder would be excluded from the procedure.

Even though module 3 has to be clearly distinguished from the proposal for an International Procurement Instrument due to its different goal and method, module 3 poses similar legal and practical difficulties with regard to the implementation. This applies in particular to possible significant delays in the award procedure (possibly suspension of the procedure pending a decision by the supervisory authorities), aspects of legal security as well as the administrative costs incurred by awarding authorities and undertakings. Practical solutions and high threshold values that adequately take the aforementioned issues into account are needed to ensure that such a module is fit for purpose. Alternatively, it is suggested that examining the extent to which distortions in the award procedure could be addressed via module 1.

The Commission will table a legislative proposal towards the end of the first quarter of 2021.

WTO compatibility

Irrespective of the WTO crisis, the Commission has committed itself to the multilateral trading system. Accordingly, the new instrument has to be in line with the EU's existing obligations under international public law. The white paper makes it clear that the Commission understands that its proposals are compatible with and complementary to WTO law and the EU's bilateral free trade agreements.

Although a definite answer on the question of the WTO compatibility will surely depend on the details of the legislative proposal, one cornerstone already defined in the white paper should be highlighted. According to annex 1 of the white paper

the term 'foreign subsidy' refers to 'a financial contribution by a government or any public body of a non-EU State, which confers a benefit to a recipient and which is limited, in law or in fact, to an individual undertaking or industry or to group of undertakings or industries'. As the Commission rightly points out, this notion relies on the subsidy definition set out in the relevant WTO rules, in particular in the SCM Agreement, while acknowledging that a subsidy can be granted directly or indirectly to an undertaking active in the EU.

This definition will play a critical role when looking at the two main concerns regarding the WTO conformity of the proposed modules: first, with regard to foreign production subsidies, the proposal may run afoul of Article 32.1 ASCM, which limits WTO members' ability to discipline subsidisation practices. More specifically, it prohibits WTO members from taking any specific action against a subsidy of another member that is not provided for under the SCM Agreement and the General Agreement on Tariffs and Trade. While the text of Article 1.1 ASCM gives no definite answer to the question whether it also covers a situation in which a subsidy is granted by a government to a production entity outside of its own territory, this will be decisive with a view to a possible infringement of Article 32.1 ASCM. The Commission appears to suggest that the entire SCM Agreement rulebook does not apply to these kinds of foreign subsidies, since no goods are crossing a border.

Second, with a view to foreign subsidies granted for the provision of services and for the participation in public procurement procedures, the proposal would especially have to be in line with the national treatment obligations under the General Agreement on Trade in Services (GATS) and the Agreement on Government Procurement (GPA). National treatment implies the absence of all discriminatory measures that may modify the conditions of competition to the detriment of foreign services or service suppliers vis-à-vis national services or service suppliers. As pointed out, the European Commission's proposal is limited to foreign subsidies that are subsidies granted by foreign governments. Therefore, the key question will be if the rules on 'foreign subsidies' will be similar to the EU state aid rules.

Conclusion

In sports, several rules, such as anti-doping and financial fair play, have long been deemed the necessary basis for legitimate and fair competition. To restore legitimacy and fairness in global business competition, the EU is right to rethink how to lever its state aid regime to achieve a more even playing field. To use a football analogy: It would be OK for Manchester City or Paris Saint-Germain

to buy a certain star player. It would be even OK from a level playing field perspective if they see higher added value in the acquisition for their team than other clubs and 'overpay'. If, however, certain clubs can outspend their competitors in the long run with a deep pocket financed by the state, this would ultimately delegitimise competition.

The Commission's white paper is therefore in many ways a fascinating conceptual project worth supporting. Commentators may be right that, on a communication level, 'hearts don't beat faster for the rules-based international order'.[6] Yet on a substantive level, the saga around TikTok shows that there is space for rule-based approaches to competition, state support and public policy considerations such as security. The white paper is an excellent starting point to come up with additional pieces of a European model.

6 Timothy Garton Ash, 'Hearts don't beat faster for "the rules-based international order"' *Financial Times* (12 September 2020).

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