

Intelligence MEMOS



From: D. Daniel Sokol
To: Canadians Concerned About Competition
Date: August 17, 2021
Re: **SOME PRINCIPLES FOR REGULATING BIG TECH**

Cases around the world have targeted technology platforms large and small. In some settings, regulatory initiatives have been introduced that focus not on enforcement, but on getting the politically expedient result, which can create unintended consequences by hurting economic growth and innovation. A number of jurisdictions are rushing to regulate without fully understanding the consequences of regulation.

Regulation has had mixed impacts. For example, GDPR, the European Union's influential privacy framework, has increased privacy protection at the expense of competition.

In real time, we can witness the negative effects of GDPR on innovation and competition, with important [work](#) by Jia, Jin, and Wagman and parallel work by Goldfarb and Johnson respectively (and I note that both Goldfarb and Johnson are Canadian).

Whereas some notion of efficiency may be (at least in practice) the only factor that determines outcomes in many competition systems, regulation may need to balance efficiency concerns with other factors. Sometimes these concerns may be valid, but other times they may result in less innovation and these tradeoffs need to be weighed very carefully.

The blizzard of regulatory action swirling around platforms is producing new rules and laws, expanded powers for existing regulatory authorities, and the establishment of new ones. These will not only affect Big Tech but also many other companies, in industries such as construction, healthcare, finance, energy, and industrial manufacturing, that have adopted or are considering adopting platform business models.

There are three main problems with limiting how platforms can offer services through structural separation of lines of business of a platform and its ecosystem, forced inter-operability, or forced sharing of data or algorithms with third parties.

First, the record of such types of vertical separation of lines of business has not been generally positive in banking, commerce, or airlines.

Second, some platforms use these first-party products and services as a critical strategic lever to differentiate their platforms and compete against larger or dominant platforms, and to re-direct innovation effort of complementors towards other, less-developed niches that benefit users. All of this tends to create more choice for consumers.

Third, while this restriction is designed to target the Big Tech companies, this policy could hinder business model innovation and digital transformation of incumbents in traditional sectors who are increasingly adopting platform-based business models and building their own ecosystems to remain competitive in industries as diverse as agriculture, banking, machinery, logistics, and healthcare.

What Should Be Done?

Without effective calibration of the regulation to reach only anticompetitive behaviour, regulation threatens to distort platform industries across the economy and hurt small businesses and consumers who rely upon these platforms.

Meanwhile, the proposed rules have doubtful efficacy for promoting competition and a different standard for "anticompetitive behavior" when it comes to targeted platforms regardless of the specific potentials benefits versus harms across platforms with different business models because effects are made at a general level rather than particularized to specific conduct. Aggressive regulation that does not focus on anti-competitive conduct goes too far and will distort incentives and destroy the value creation that platforms provide.

A different approach is needed to design an appropriate regulatory framework for the digital economy; one that builds general principles that should guide actions while leaving to antitrust (specialized) units to derive criteria to implement those principles to specific issues on a case-by-case. This can guarantee that law enforcement agencies like the Competition Bureau can learn and adapt to the dynamic digital environment and offer a principle-based approach. If Parliament sets out general principles, the Bureau can only issue guidelines and policy documents about its approach. The principles proposed here are but a starting point in this direction.

1. **Proportionality.** Have solutions that focus on the problem to be solved. In other words, do not destroy the benefits of the digital economy. Do not overreach because by doing so, the threat to innovation and value creation increase. (A good current example of overreach is Bill C-10.)

2. **Inclusion.** Platforms have created opportunities for disadvantaged groups around the world to become linked to the global economy. Part of the value of platforms has been the ability to promote business opportunities for traditionally underrepresented groups. Further, the two-sided nature of platforms with at least one side free really matters for those for whom the alternative to free (higher prices) is particularly difficult financially. Thus, increasing the costs of platforms may have unintended consequences on inclusion.

3. **Flexibility.** Do not create broad limits/prohibitions that are meant for one or two companies but are also applied to other companies, resulting in limits on all sorts of value creation. For example, lock-in matters except for when it does not. We have seen the limits of lock-in – it is not the case that once a Microsoft Windows user for word processing or Dropbox user for storage, you will never shift to a competing product – empirically across some industries. In other industries, lock-in may be more significant. As more parts of the economy become digitized, we need to think carefully about where problems may exist and may be in more need of regulation than others. There is an optimal mix of formal regulation, shared governance and self-governance that needs to be considered in the design of formal regulation, along with the adaptability for tweaks along the way.

This complexity requires care and nuance after significant study, something that Canadian lawmakers and the Competition Bureau should seriously consider before undertaking drastic change, to ensure we can reap benefits of change but not undermine the value creation that platforms provide.

D. Daniel Sokol is a professor at the University of Southern California's Gould School of Law and USC Marshall School of Business.

To send a comment or leave feedback, email us at blog@cdhowe.org.

The views expressed here are those of the author. The C.D. Howe Institute does not take corporate positions on policy matters.