Fideres Partners LLP
11 Old Jewry
London
EC2R 8DU
Tel. +44 20 3397 5161
Fax. +44 20 3397 5170

Monopolistic Practices Directorate
Competition Bureau
50 Victoria Street
Gatineau, Quebec
K1A 0C9
Submitted online at http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/frm-eng/MBED-AQZJP2

London, 14 May 2018

Dear Madam or Sir,

**Re: Response to the Competition Bureau, Draft Abuse of Dominance Enforcement Guidelines**

Fideres welcomes the opportunity to provide the Competition Bureau ("the Bureau") with our views on their draft Abuse of Dominance Enforcement Guidelines. Fideres is an economic consultancy committed to maintaining fair and transparent markets, and so appreciates the chance to contribute to the development of Canada's competition enforcement system.

In general, the draft guidelines provide a clear, non-exhaustive list of the range of exclusionary practices available to dominant firms. They also give good examples of empirical tests available to test for market abuse (for example, pricing below 'avoidable cost'). Fideres also shares the Bureau's concern to avoid over-enforcement – the need to prevent abusive practices should not disincentivize firms from *attempting* to achieve a dominant position, which can provide a strong R&D and product improvement incentive.[1]

However, we believe that the draft guidelines could be improved in several important respects. In particular, we recommend that the Bureau:

- Think more carefully about the newly-achieved market dominance of large tech companies, and what this means for enforcement of the Competition Act;
- Reconsider the existing statutory limits on fines for antitrust infringements.

We elaborate on both of these points below.

[1] See Motta, *Competition Policy: Theory and Practice* (Cambridge 2004); Buccirossi, *Handbook of Antitrust Economics* (Boston, 2008)

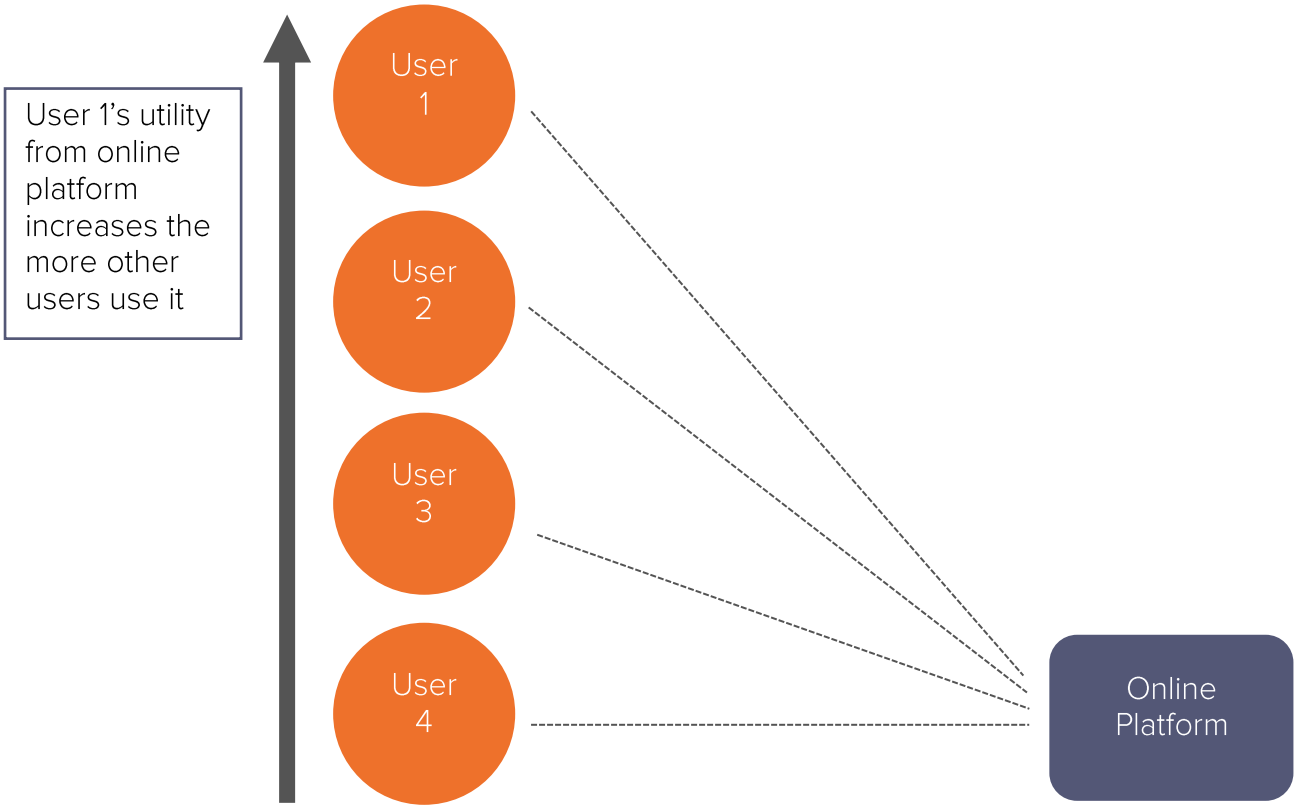
## 1 Networking Effects, Tech Companies and Abuse of Dominance

### (Responds to Section 2 of the Draft Guidelines: "Anti-competitive Acts")

The draft guidelines provide a non-exhaustive list of possible practices that the Bureau may classify as predatory, exclusionary or disciplinary conduct by a dominant firm. Examples given of exclusionary and disciplinary conduct include margin squeezing, exclusive dealing arrangements, high switching costs and tying/bundling. However, as many commentators have noted, traditional ideas of antitrust violations may need amending as the influence of large technology companies grow.[2] We note that the draft guidelines contain a somewhat limited discussion of 'network effects' and their implications for competition policy in a digital world.

A 'direct' network effect means that the success of a platform depends for one user on how many other users use the platform. For example, the utility of using Skype for one user depends on how many others they can connect to.

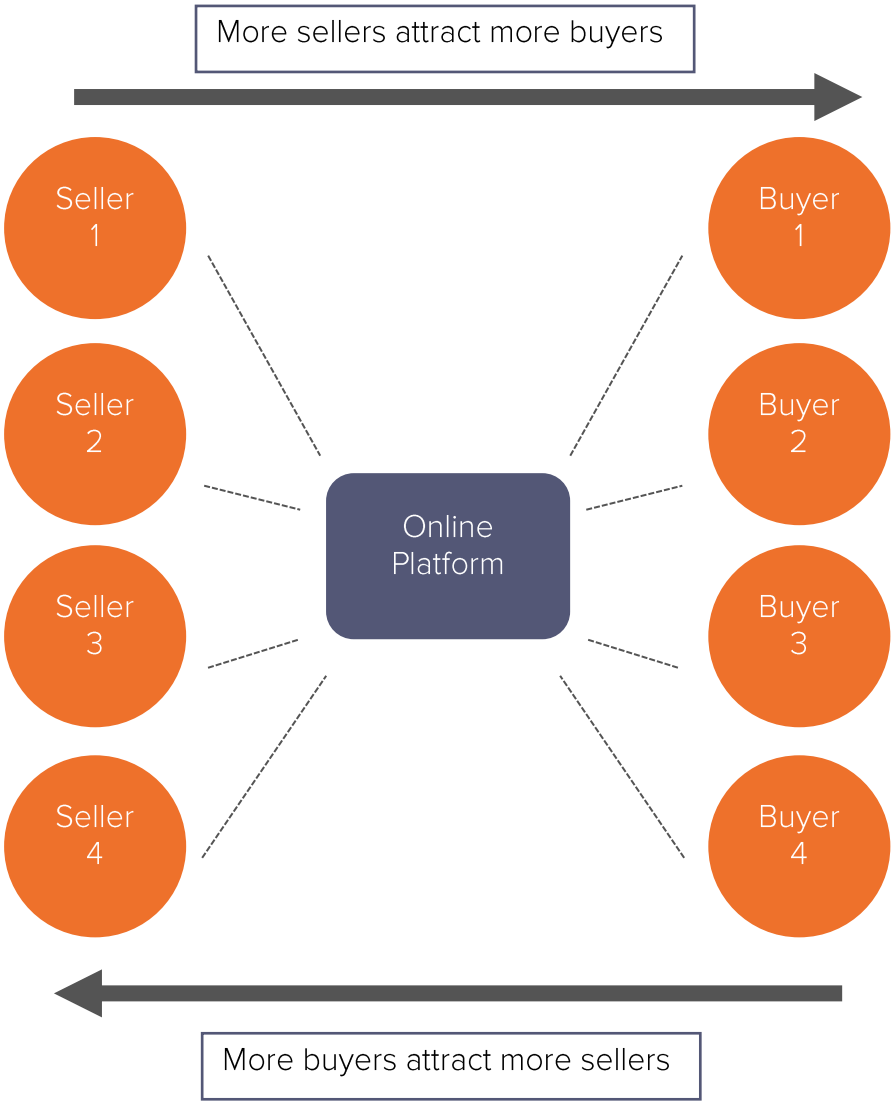
Figure 1: Direct Network Effects




'Indirect' network effects, in contrast, arise when more users on one side of a platform attract more users to the other side. For example, potential buyers using Amazon do not benefit *directly* from an increase in other buyers but benefit *indirectly* if the increase in buyers attracts more sellers.[3]

[2] See Motta, *Competition Policy: Theory and Practice* (2004); Ahlborn et al., 'Competition Policy in the New Economy: is European Competition Law up to the Challenge?' (2001)
[3] Haucap and Stuhmeier, 'Competition and antitrust in internet markets' (2015)

Figure 2: Indirect Network Effects




The existence of powerful market players exploiting network effects should not, in and of itself, concern regulators. In fact, large platforms connecting millions of users online have important efficiency justifications.[4] However, powerful technology companies exploiting their control over internet networking platforms creates new opportunities for market abuse that need to be addressed by competition authorities.

A well-known, recent example concerns Amazon's dispute with French publishing house Hachette in 2014. After disagreements with Hachette over e-book pricing, Amazon progressively made it more difficult for consumers to buy Hachette books on their platform.[5] Although Amazon did not ban Hachette books outright, they increased prices and delivery times for them, and took other steps (such as selective advertising) to direct consumers to other publishers.[6] This is an example of 'disciplinary' conduct. Yet it is does not neatly fit into any of

[4] Ibid.
[5] Kahn, 'Amazon's Antitrust Paradox' (2017)
[6] Krugman, 'Amazon's Monopsony is not OK' (2014)

the 'traditional' categories of exclusionary or disciplinary conduct discussed in the draft guidelines.

Another relevant example concerns search engine giant Google. In June 2017, the European Commission (EC) fined the company €2.4 billion for privileging its own online shopping platform in search results. Specifically, consumers searching for online shopping platforms would see Google's platform at the top of the search results. This amounted to a direct attempt to exploit the power of networking effects: the commercial success of Google's platform was strongly dependent on how many consumers visited the page, which in turn influenced how many sellers would sell their products there. The EC found that Google's platform had no discernible competitive advantage over its competitors, and that privileging it in search results amounted to abuse of dominance.[7] Like the Amazon case, this does not neatly fit into any categories of abuse of dominance discussed in the Bureau's draft guidelines.

The Google and Amazon examples illustrate only some of the ways that large technology companies can abuse their dominance of marketplaces on the internet.

In testing whether such practices amount to abuse of dominance, both qualitative and quantitative methods are necessary. In cases of disciplinary conduct by an online marketplace like Amazon, the Bureau can use resale price data to test whether the marketplace is deliberately charging higher resale prices for products supplied by a company it intends to discipline. Statistical tests, such as structural break analyses, can be used to assess whether these prices change significantly when the dominant firm is in a dispute with its suppliers. Other cases will require exploiting qualitative research on how consumers engage with the internet. For example, the EC's Google ruling relied on a study showing that results on the first page of an internet search receive 95% of all clicks from internet users, as well as a range of consumer surveys.

The box below summarizes our recommendations:

**Recommendation 1 for Draft Enforcement Guidelines**

- Add a comprehensive discussion of the importance of network effects in abuse of dominance claims;
- Add a summary of qualitative and quantitative methods that can be used to test for abusive conduct by tech companies.

## 2 Fines as Deterrents for Abusive Firms

### (Responds to Section 4 (B)(ii) of Draft Guidelines, "Administrative Monetary Penalties")

The purpose of an administrative monetary penalty (AMP) in Canadian competition law is to "promote compliance with the [Competition] Act, not to punish the respondent for

[7] European Commission Press Release, 'Antitrust: Commission fines Google €2.42 billion for abusing dominance as search engine' (2017)

anticompetitive conduct".[8] Leaving aside debates on the merits of punitive fines,[9] an AMP should, at the very least, deter dominant firms from abusing their market position. However, the Competition Act only allows for a maximum fine of $10 million, or $15 million for each subsequent order.

Fideres believes that such maximum fines do not offer adequate deterrence for large companies seeking to abuse their dominant position. Consider the table below, which outlines Canada's largest companies by market capitalization as of January 2018. For illustrative purposes, we include what percentage of their total market capitalization a $10 million fine would constitute.

Table 1: Largest Companies in Canada by Market Capitalization

| Company | Market Capitalisation ($ billions) | % of Total Market Cap. ($10 Million Fine) |
|---|---|---|
| Royal Bank of Canada | 122 | 0.008% |
| Toronto-Dominion Bank | 111 | 0.009% |
| Bank of Nova Scotia | 80 | 0.013% |
| Enbridge Inc. | 69 | 0.014% |
| Canadian National Railway Company | 63 | 0.016% |
| Suncor Energy Inc. | 62 | 0.016% |
| Bank of Montreal | 53 | 0.019% |
| Canadian Natural Resources Limited | 45 | 0.022% |
| Canadian Imperial Bank of Commerce | 44 | 0.023% |
| TransCanada Corporation | 43 | 0.023% |

*Source: Statista, Bloomberg*

If, instead, the $10 million fine were assessed relative to total sales affected by the abusive conduct (an approach followed in other jurisdictions – see below), it would likely constitute an even smaller percentage than those listed above. Clearly, a maximum fine of $10 million (or $15 million for each subsequent order) is not an adequate deterrent for companies whose market capitalization numbers in the tens or hundreds of billions of dollars.

The Bureau should consider adopting a criterion of proportionality in its enforcement guidelines, by setting the maximum fine as a percentage of sales affected by the infringement. In Europe, fines for guilty companies can be as large as 30% of the sales affected by the competition infringement (but may not exceed 10% of the overall annual turnover of the company).[10] Other regulators around the world follow a similar approach:[11]

[8] Canadian Competition Bureau, 'Draft Abuse of Dominance Enforcement Guidelines', Section 4 (B) (ii)
[9] Greenfield and Olsky, 'Treble Damages: To What Purpose And To What Effect?' (2007), http://www.wilmerhale.com/uploadedFiles/WilmerHale_Shared_Content/Files/Editorial/Publication/Treble%20Damages%20Article_%20BIICL%20conference.pdf
[10] European Commission Press Release, 'Fines for Breaking EU Competition Law' (2011)
[11] The table below merely provides examples of jurisdictions using this method, not an exhaustive list.

Table 2: Maximum Fines for Abuse of Dominance in other Jurisdictions

| Jurisdiction | Max. Fine for Abuse of Dominance Infringements |
|---|---|
| Brazil | 0.1-20% of affected sales |
| European Economic Area | 30% of affected sales; max. 10% of annual turnover |
| Japan | 6%-10% of affected sales |
| South Korea | 3% of affected sales |

*Source: OECD, Mondaq, Thomson Reuters*

This approach allows for larger companies to incur much higher penalties than the absolute limits prescribed in Canada. In the Google case referenced above, the EC applied this method to arrive at an overall fine of €2.42 billion. The EC and Korea's Fair Trade Commission also recently fined technology company Qualcomm €997m and ₩1.3 trillion (approx. €700m) for abusing its dominant position in the modem chip market.[12] This approach allows competition enforcement to be tailored to the size of the guilty company, which current Canadian law does not.

Alternatively, the Bureau may wish to consider setting fines equal to the full extent of the 'harm' generated by the abusive conduct. This requires modelling how the affected market would have evolved in the absence of abusive conduct by a dominant firm. For example, if a dominant firm engages in predatory pricing to force out existing competitors, data on competitors' past profits and revenues before the start of the infringement can be used to model what profits these competitors would have achieved in a fair market.[13] This is known as a 'comparator-based' approach. Several other statistical techniques and theoretical approaches (such as Bertrand and Cournot models) can be used to model how markets evolve in the absence of abusive conduct by a dominant firm.[14]

The box below summarizes our recommendations:

**Recommendation 2 for Draft Enforcement Guidelines**

- Scrapping absolute limits on fines for anticompetitive infringements;
- Setting fines either as a percentage of sales affected by the anticompetitive infringement, or to the full extent of the 'harm' generated by the abusive conduct.

Yours faithfully,

Alberto Thomas, Partner

Fideres Partners LLP

[12] European Commission Press Release, 'Commission fines Qualcomm €997m for abuse of dominant market position' (2018); Financial Times, 'Qualcomm fined $854m in South Korea antitrust case' (2016), https://www.ft.com/content/add12036-ccac-11e6-b8ce-b9c03770f8b1
[13] European Commission, 'Practical Guide: Quantifying Harm in Actions for Damages Based on Breaches of Article 101 or 102'
[14] See Davis and Garces, *Quantitative Techniques for Competition and Antitrust Analysis* (2010)

## About Fideres

Fideres is an economic consultancy focused on antitrust and competition work, with offices in North America and Europe. Fideres has extensive experience in identifying and analyzing anti-competitive behavior including economic analysis of price fixing, monopolization and abuse of dominance claims, as well as associated damages modelling.

Over the past 9 years, Fideres has been at the forefront of antitrust investigation in prominent cartel cases including major financial markets cases: LIBOR, Foreign Exchange, ISDAfix as well as cartels in the healthcare, shipping, food and technology sectors. To date, Fideres has acted as economic experts in private competition civil claims with aggregate damages in excess of $30bn.

Fideres is also assisting a number of regulators worldwide in their investigations and has given evidence before the U.K. Treasury Select Committee as part of their ongoing investigations into these areas and in particular with respect to the gold market.

For more information, please visit www.fideres.com