INTERNATIONAL ASSOCIATION OF ENTERTAINMENT LAWYERS

The AI Revolution: the International Legal Perspective

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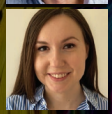

The Role of Competition Policy in Addressing Concerns with AI Markets: If the Shoe Fits…

By Lucas Ford & Sandra Potlog

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Authors: Lucas Ford & Sandra Potlog

» Introduction

It's not that surprising that some digital platforms that hold arguably large degrees of market power in some digital markets either have, or are in significantly advanced states to take, similar positions in relation to the development, production and / or distribution of AI. This is largely due to digital platforms and AI sharing the same essential inputs: compute, data and distribution networks.

But with AI developing at exponential rates, and in view of the vast number of emerging applications, understanding AI, let alone regulating it for potential harms and benefits, poses particular challenges. It would indeed be convenient if the newly minted digital platform regulation recently imposed in the EU and UK to address competition issues in that sector could simply be read across to AI to address those. But is it that simple?

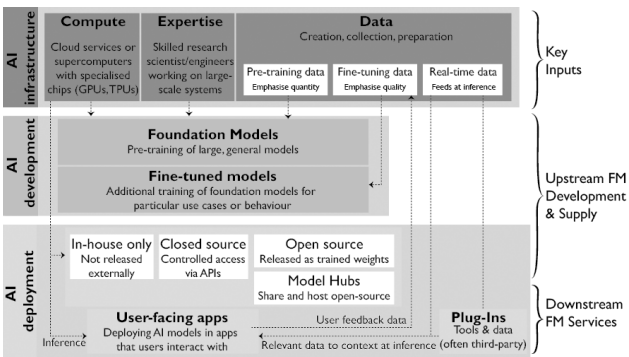
The need for effective competition is, while not an end in itself, one of a number of objectives that could materially contribute to ensuring AI develops in the interests of wider society and consumers in particular. But AI poses some particularly tricky issues. Some well-established competition economics/law concerns have been expressed that stem from the reality that AI's essential inputs are concentrated in the hands of a few market players who may have the ability and incentive to distort competition in favour of their own economic self-interest, at the expense of competition (innovation, price, quality) and consumers (which is the proper mandate of every shareholder, to be fair).

This tends to have a self-reinforcing effect in markets with network effects as they develop, and if they 'tip', firms with sufficient degrees of market power can strengthen and entrench their positions – making entry even more difficult and unlikely, while simultaneously facilitating the ability of 'incumbents' to leverage their positions into adjacent and 'downstream' markets where there is prospective competition.

Although among competition authorities and policy makers their theories of harm are still developing, in many places applying a 'smell test' i.e., if it's big and profitable it must be bad, they appear to intend to rely mostly on existing *ex post* competition law and new digital market regulations to treat competition concerns associated with the market power of digital platforms, partly on the basis it seems to be the same suppliers of key inputs. However, there are questions whether the new regulations can simply be read across to AI, not least because those digital platform regulations are new, and remain themselves untested in the markets they were designed to regulate.

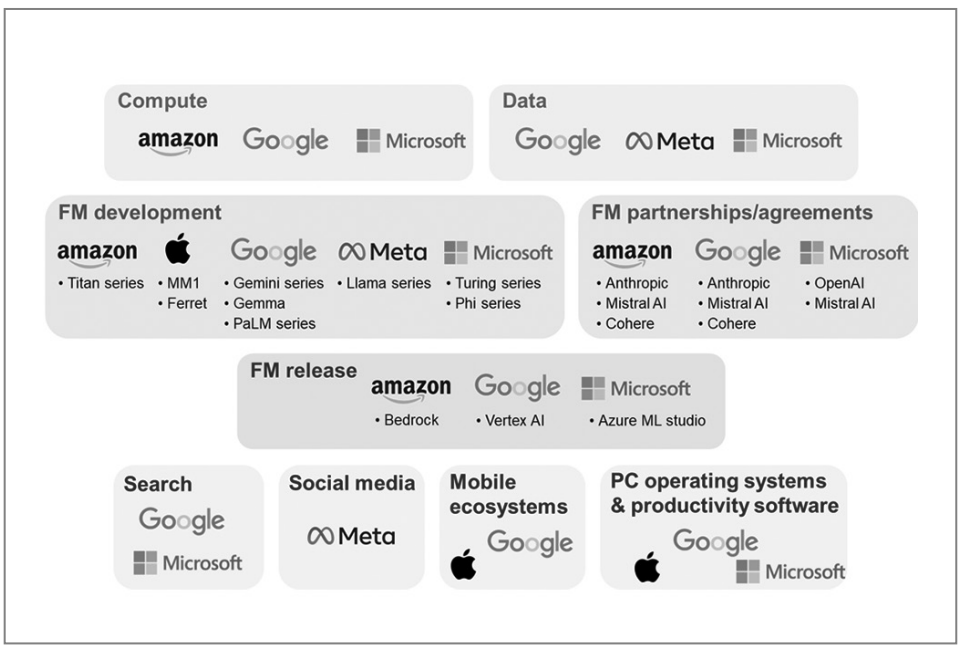
» Market Structure

The market structure for developing AI includes vertical and horizontal levels in the 'value chain' which illustrate where the essential inputs of concern sit.



Source: Parliamentary whitepaper: Large Language Models and Generative AI, February 2024

While the input 'levels' in the AI value chain are key to understanding market structure and where pinch points and 'power' might currently lie, it is still too early to tell (a) how durable this structure is and (b) (therefore) it could be premature (aka a mistake) to base an analysis of harms around a static view. It is nevertheless to be expected that some digital platforms that already have significant compute, expertise and data – such as Google, Microsoft, Amazon – were first movers in AI (closely followed by Apple and Meta) given their head start with common essential inputs for developing AI.



Source: CMA AI Strategic Update April 2024

Moving quickly, in some cases sideways, into the AI sector has a sound basis in scale economics (vis a vis entering from scratch) and, as a consequence, digital platforms are naturally well placed to use and deploy AI. Regulators, in their unavoidably catch-up way, have begun to develop more advanced theories of harm related to self-preferencing, bottlenecks/access, collusion (between AI) and 'partnerships' between providers[1] – what is less clear is the extent to which these concerns are based on a sort of paranoia stemming from their (bad) 'experience' with failing to prevent digital markets from tipping, and therefore being able to prevent perceived exploitation of market power.

» Regulation, For What Again?

While it is inherently impossible for competition-regulatory authorities to keep pace with the market, twelve months is a particularly long time in the world of AI. The UK Competition and Markets Authority (CMA) has been particularly proactive in developing its harm hypotheses and engaging with the market to understand the impact that competition in AI presents to consumers. Notwithstanding, the CMA's tone has developed quickly since its 'Initial Review' of foundation models (FMs) published on 4 May 2023, which was very much 'pro-innovation' and light-touch focussed. While it identified some competition concerns it was largely inconclusive on whether or what regulatory action was required.

Given the pace of AI over the past year this cannot be a criticism. The CMA's thinking has recently progressed quickly to its AI Foundation Models 'Update paper' on 11 April 2024 published alongside a speech from the CEO, Sarah Cardell, who summed up the journey:

> *"When we started this work, we were curious. Now, with a deeper understanding and having watched developments very closely, we have real concerns."*

Those 'concerns' (and others referred to above) were recently echoed in a rare *"Joint statement on competition in generative AI foundation models and AI products"* issued by the CMA, European Commission, US Department of Justice and US Federal Trade Commission.[2]

It is (now) uncontroversial that competition law has not had great success in addressing perceived concerns related to very large digital platforms. A plethora of antitrust cases around the globe, over decades, chewing up enormous amounts of regulatory resources (against the resources of some of the world's largest firms with every incentive to fight for their corner) have on most measures failed to achieve the outcomes wanted. Also on most measures, it's all a bit too late – markets have tipped, and penalties in the billions have failed to provide much deterrence.

Enter stage left ex ante regulations designed and introduced at haste (comparatively) in the EU in the form of the Digital Markets Act (DMA), and also (although less swiftly) in the UK in the form of the Digital Markets Competition and Consumer Act (DMCCA), to address the perceived problems posed by large digital platforms on a forward-looking basis. This largely translates to accepting and managing current market shares rather than trying to introduce a panacea that magically brings down entry barriers where so called 'entrenched' positions exist and resets competitive markets.

One benefit of decades of dealing with anti-trust cases against 'big tech' is that regulators have now had a ton of experience understanding and fine-tuning their focus on the types of harms and the conduct they want to prevent. The rules developed by both the DMA and DMCCA, with no doubt significant coordination between them, require the authorities to designate platforms as either 'Gatekeepers' in the EU or firms with 'Significant Market Status' in the UK, who then must comply with a broad list of 'dos and don'ts'. On 6 September 2023 the EC designated six digital platforms as 'Gatekeepers', subject to direct regulation under the DMA: Alphabet (Google), Amazon, Apple, ByteDance (TikTok), Meta (Facebook), Microsoft and later Booking.com for various 'core platform services' (CPS).[3] Similar designations are expected in the UK. Of course, most or all the designated CPS designated include an AI by now in one form or another in their services.

The DMA dos list of requirements that Gatekeepers/SMS firms must allow includes inter alia, interoperability with other platforms, access on fair, reasonable and non-discriminatory terms, and making pre-notification to the EC of any 'concentrations' (mergers) they want to undertake. The don'ts list includes requirements that Gatekeepers must not engage in 'self-preferencing' i.e., rank own products / services higher than downstream competitors without justification, use business customers' data to unfairly compete on a different service aka self-preference, establish unfair conditions for business users, or track end users outside the platform without the users' effective consent.

While the EU and UK are both trying to solve the same problems, with mostly the same actors, each have developed a slightly different approach to the design of their broadly similar rules. They are also out of sync, with the EU DMA coming into force on 1 November 2023 and the DMCCA passing into law on 24 May 2024, and expected to come into effect in the Autumn. Perhaps a mixed blessing for the CMA, as it has the opportunity to learn from the behaviour of the platforms and the EC's experience with the regulations.

» Too Good to be True?

All the while policy makers were in the process of coming to grips with digital platforms and developing regulations, AI has exploded onto the scene, with exponential development and market uptake (and value). And lo and behold, these digital market regulation 'dos and don'ts' all seem to be just the type of behaviours that authorities would also like large firms in the AI sector to comply with. But could it be a stroke of luck for policy makers that the recently minted digital platform rules (albeit arguably too late for *that* specific sector) can be read straight across to address the concerns that most of the same actors present in AI generation? Both the EC and the CMA have come out very confidently with 'yes they can!'.

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On 28 September 2023 Mr Alberto Bacchiega, Director for Digital Platforms at the Directorate- General for Competition, stated that the European Commission has *‘all the tools it needs’* to regulate AI.

In its AI strategic update paper, the CMA has stated:

> *“AI and its deployment by firms will be relevant to the CMA’s selection of SMS candidates, particularly where AI is deployed in connection with other, more established activities.”* [4]

That was lucky. Or was it *really*? It is obviously enticing to want to believe this, given the toil, pain and suffering involved in developing regulatory frameworks that are inherently imperfect. But when digital platform regulation was being designed FMs were clearly not even a glint in the eye of policy makers when they set out to address issues in that sector. It would therefore seem a bit too good to be true that a particular AI model developer happened to already be in scope of digital markets regulation for the purposes of those regulations, notwithstanding procedural requirements of robust evidence and rigorous analysis before designation pulling them within scope can take place.

Whether AI suppliers are within scope of any law or regulation, but in particular in relation to digital markets, must be based on whether the firm and AI service of concern (a) is capable of being ‘designated’ and (b) is providing a ‘service’ or ‘activity’ within the meaning of those regulations i.e., a *‘core platform services’* / CPS (DMA) or *‘digital activities’* (DMCCA).[5] And even if certain AI services do happen to tick the designation boxes, that is itself meaningless if any remedies or rules to address perceived harms are not relevant or suitable to address the concerns.

While some of the AI suppliers will almost certainly meet the quantitative thresholds for designation if AI was considered under the DMA, it is less clear that they (and other chip manufacturers and compute providers) will meet the ‘qualitative’ criteria required of providing an important ‘gateway between businesses and consumers’, in relation to

AI 'services' or 'activities' within scope of the DMA, particularly given 'AI' is in many cases more akin to a business input. The position is even more nuanced under the DMCCA which requires the regulator to undertake a detailed balancing exercise of whether the undertaking has 'substantial and entrenched' market power of 'strategic significance' in relation to the particular 'digital activity'. While the rules do envisage looking ahead, it is very unclear how a regulator could safely conclude anything about how entrenched or durable current market positions in AI are now or what things will look like in 3-5 years' time.

Article 2(2) DMA poses particular problems of rigidity with its baked in list of definitions of 'core platform services' that are within scope of the DMA from (a) – (j). While the list includes 'cloud computing services', aka distributed cloud infrastructure, in the list of CPS capable of being designated, this was in itself controversial due to the difficulty reconciling cloud computing with the objectives of the DMA, in particular addressing multi-sided markets and contestability.

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More difficulties seem likely to arise in the context of the use of cloud computing for AI given cloud computing is a 'service' used across an innumerable number of non-AI purposes, products and core infrastructure applications for businesses. It may therefore be a stretch to simply read Article 2(2) as capturing 'AI' without specific identification and categorisation (and compartmentalisation) of the particular use of cloud computing for the provision of AI before determining whether it was capable of designation as a CPS. While the Digital Services Act (DSA)[6] obviously serves a different purpose, Recital 13 is perhaps instructive on the EC's view of the role that 'ancillary' features of a service (such as coupling AI) should play in the scope of the regulation of digital services:

> *"For the purposes of this Regulation, cloud computing or web-hosting services should not be considered to be an online platform where dissemination of specific information to the public constitutes a minor and ancillary feature or a minor functionality of such services."*

Neither FMs nor other categories of AI where concerns of market concentration arise are included or inferred in the definitions of CPS in Article 2(2) DMA. However, while the list will be reviewed in 2026[7] it is far from straightforward to amend that list before then, and 2026 is a long way off in the AI time-space continuum. The EC must undertake a market investigation and develop a report to put before the European Council with a legislative proposal by the European Parliament to amend the DMA itself. This would be subject to review, first and second reading etc by the European Parliament. The process would also be subject to political wind and inevitably take significant time, something in short supply in this arena.[8]

However, not being on 'the list' has not prevented the EC determining that Meta's 'WhatsApp for Business Application Programming Interface' (API) is part of the 'WhatsApp' platform and forms part of the CPS for the purposes of designation. While there is little reasoning published to analyse, it is arguably far easier to understand given that WhatsApp's API is crucial to the platform's existence, whereas web browsers have developed and existed independently of AI since they began (despite now being integrated), which seems more likely to reconcile with the approach referred to by the EC in relation to cloud computing in Recital 13 DSA.

It is also noteworthy that none of the DMA designation decisions found or implied that the AIs integrated into their CPS (e.g., Google search and Gemini/Bard) were key to any of the decisions. In fact, AI wasn't even mentioned. The EC's designation investigation into Bing and Edge, which also come with bundled with Microsoft's AI 'Copilot', also concluded (not to designate) without focusing on the contribution Copilot makes, which is perhaps telling.

Did the EC really miss a trick by failing to publish a more detailed reasoned analysis (which it no doubt undertook) on the role of AI in the designation decisions and Copilot investigation? Or did it dodge the issue because adding the role of AI into the analysis would have been actively unhelpful to the conclusions, either because they (we) don't yet fully understand or appreciate the impact that AI is having on the core business of digital platforms? Or worse, was it because AI itself may have a disintermediation effect on core platform services which weakens the EC's conclusions on market power and thus designation?

As the DMCCA has greater flexibility built into it to address novel and/or as yet unidentified sources of market power, in particular via the discretion provided to the CMA when undertaking an SMS assessment, it may be better equipped to facilitate more in-depth analysis of the impact that AI has on digital activities in any market under consideration and markets adjacent. Indeed, it would not be surprising if, by the time

the DMCCA comes into full force, the CMA has new and novel uses of AI by digital platforms within its sights (just ask publishers).

Overall, it is not entirely clear that key parts of the AI value chain which have been identified as concerning can simply be pulled within this scope of digital platform regulation, or at least there has yet to be a debate about it. There is a lot to play for, and the opening salvos of the battles that are now on foot both with respect to designation decisions and compliance with the DMA may also serve as a warning shot as to how the debate may play out should regulators seek to apply digital platform regulation to AI without robust legal and economic justification (or even with it).

» Conclusion

AI is fast becoming indispensable to many businesses. This is no bad thing in itself, but it does increase the concern about its design, implementation and control. Competition policy (the application of *ex ante* and *ex post* regulation) is capable of providing a material contribution to some of the concerns levelled at the direction of AI, if developed on solid legal ground and implemented in a timely way.

This requires the sector, market structure and potential harms, to be properly understood to ensure regulatory frameworks (and their enforcement) *themselves* serve consumer interests. This implies a regulatory framework that can respond in a non-discriminatory way while balancing the need to encourage innovation, investment and technological development from AI suppliers. Whether through the DMA, the DMCCA or existing competition rules, regulators need to pay close attention to developments in supply of AI's essential inputs and use cases to protect against minority economic interests steering the ship.

It would be easy to conclude we are facing familiar theories of harm to competition and 'essential facilities' bottlenecks. But the framework of digital platform regulation is designed to address different problems, in markets that have already tipped. It would also be a stroke of fortune if newly minted digital platform regulation could be read directly across to regulating AI, but square pegs should not be in round holes. And as theories of harm are still emerging, it seems premature to focus heavily on the tools before the problems are understood. In view of the battle lines already drawn by those regulated under the DMA (as they themselves come to grips with the impacts), we probably should not expect less of a response if and when AI 'services' and 'activities' are subject to the same regulatory microscope.

[1] *https://www.gov.uk/government/news/cma-outlines-growing-concerns-in-markets-for-ai-foundation-models*

[2] *Joint statement on competition in generative AI foundation models and AI products - GOV.UK (www.gov.uk)*

[3] *The list is non-exhaustive.*

[4] *https://www.gov.uk/government/publications/cma-ai-strategic-update/cma-ai-strategic-update?fhch=0112bc200558753fbe5ff597ba72ed8d#the-cmas-understanding-of-the-risks-posed-by-ai*

[5] *Section 3.*

[6] *Regulation (EU) 2022/2065*

[7] *Article 53(3)*

[8] *EU policy makers may have recognised some of the shortcomings of the DMA in relation to cloud computing by introducing measures to address interoperability and portability in the EU Data Act 2023, due to come into force in late 2025. These measures have already been widely criticised and it is unclear how they will address specific concerns with the compute power required in AI ecosystems.*