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The UK's New Digital Markets Regime: Unfettered Discretion and Power for the CMA

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Background

On 24 May 2024, royal assent was granted to the UK Parliament's Digital Markets Competition and Consumers Act (**"DMCC"**) (available here), a year after the Bill was first introduced to Parliament. The DMCC brings the most significant reforms to UK competition and consumer law in two decades, enhancing the existing powers of the Competition and Markets Authority (**"CMA"**) that apply across the economy.

The DMCC introduces three key areas of change: (i) the introduction of a new *ex ante* digital markets regime; (ii) the strengthening of the CMA's consumer law enforcement powers; and (iii) the bolstering of the CMA's administrative and investigative powers more generally. On 9 September 2024, the UK Government set out its timeline to commencement, confirming the commencement timings for different parts of the Act, the first being commencement of the digital markets regime and the competition reforms, due in December 2024 / January 2025.

This post focuses on the DMCC's new digital markets regime, which targets perceived competition concerns connected to a handful of the most prominent tech firms in the UK (the **"SMS Regime"**). The regime will be run by the Digital Markets Unit (**"DMU"**), a new directorate that sits within the CMA, which has been preparing in "shadow" form since 2021 to take up its new role.

The incoming SMS Regime will sit alongside the CMA's economy-wide powers and hand it a powerful new toolkit specifically tailored for the "digital age", to complement them and fill perceived gaps. While the objectives of the regime are very similar to the European Union's Digital Markets Act (**"DMA"**), the UK regime is significantly more flexible, targeted and tailored. Unlike the DMA which creates presumptions for designation and contains a set of rules written by the European Parliament, the cornerstone of the SMS Regime is flexibility: no thresholds for designation and no rules apply until the CMA writes them. This is intended to allow bespoke rules for each designated firm and has been lauded as being more targeted, proportionate and – it is hoped – effective than a "one-size-fits-all" rulebook. Moreover, the CMA intends to take a new 'participative approach' to regulation under the SMS Regime, which will involve inclusive and transparent engagement with all stakeholders throughout the regime's enforcement.

We summarise below the new rules that could apply to the designated addressees and how the CMA is expected to implement the SMS Regime in practice.

Overview of the SMS Regime

The SMS Regime started its journey with the Furman Review (a report on competition in digital markets by independent experts, commissioned by the government and concluded in 2019), which recommended establishing a dedicated digital markets unit and the implementation of *ex ante* rules to better regulate platforms identified as having "strategic market status". This was closely followed by a Digital Markets Taskforce (**"Taskforce"**) led by the CMA in 2020, providing advice and recommendations to the UK government on the potential design and implementation of such a regime. In parallel, the CMA also conducted various investigations into the functioning of certain digital markets using its market study tools (including its Digital Advertising and Mobile Ecosystems Market Studies), the findings of which provided yet further impetus for the need for regime change to tackle the perceived competition concerns in digital markets.

Despite various political setbacks, the DMCC was eventually introduced to Parliament in Spring 2023 and gained royal assent a year later. While there was much debate on the regime during the Parliamentary process, its core elements have not changed significantly since the Bill was introduced and contain most of the key elements envisaged from the Taskforce and Furman Review.

SMS Designation

Designation is the gateway to the SMS Regime, from which all powers and obligations will flow. Once designated, a firm will typically remain captured for at least 5 years and will be subject to various obligations and monitoring requirements, as applied by the CMA in each particular case. Unlike the DMA, no obligations (other than merger reporting requirements, described below) automatically apply from SMS designation. Instead, once designated, the CMA will then have broad powers and discretion to design and impose various obligations on firms in relation to the relevant designated activity.

The CMA may designate a firm as having SMS where it demonstrates, following a 9-month investigation period (extendable by 3 months), that on the balance of probabilities, the following tests are met:

- **Turnover:** as an initial threshold test, any potential SMS firm must reach minimum turnover requirements (across its corporate group, including from non-digital activities) of: (i) £25 billion global turnover; or (ii) £1 billion UK turnover (s. 7 DMCC). While this test is significantly lower than e.g., the DMA's quantitative turnover threshold, the intention is to provide clear legal certainty to smaller firms against potential designation, with the CMA's expectation being that in reality only a handful of the largest firms will actually be designated.
- **Digital activity:** The CMA must identify a relevant digital activity operated by the firm to designate. This can broadly include any of the firm's services provided by means of the internet or other digital content (e.g. mobile apps, gaming content, music content), as well as any other activities carried out for those purposes (s. 3 DMCC). Unlike the EU's DMA, the CMA itself will determine and define the scope of each digital activity via separate investigations, with wide discretion to group activities of an undertaking together into a single designation (provided they have substantially the same / similar purposes or can be carried out in combination to fulfil a

specific purpose) (section 3(3) DMCC). This discretion provides potential efficiency for the CMA to streamline multiple investigations into one, but also poses risks that, without sufficient limitation, this could become a backdoor for the CMA to designate activities in which there is not substantial and entrenched market power.

- **Link to the UK:** The relevant digital activity must have a sufficient link to the UK. This is interpreted broadly and is likely to be a low bar for the CMA to prove, i.e. where the digital activity has a significant number of UK users, it carries on business in the UK, or is likely to have an effect on trade in the UK (see s. 4 DMCC).
- **Substantial and entrenched market power ("SEMP"):** the CMA must show that the firm has both substantial and entrenched market power (two separate tests), assessed by a forward-looking analysis projected into at least the next 5 years (taking account of any expected or foreseeable developments if the firm were not designated) (see s. 5 DMCC). Unlike the DMA, there are no specific quantitative thresholds that raise a presumption of the existence of SEMP. Moreover, despite the similarity of the "Significant Market Power" framework in the OFCOM context, the CMA has emphasised that the SEMP test will not (as OFCOM does) draw on the concept of "dominance" and will not apply highly relevant learnings from abuse of dominance enforcement on "market power" and "dominance" (see paragraph 2.45 of the CMA's Draft Digital Markets Competition Regime Guidance (see CMA194con here). The test, therefore, hands a great deal of discretion to the CMA to produce a finding of SEMP.
- **Position of strategic significance:** Designation also requires a firm to have a position of strategic significance in relation to the relevant digital activity. As with SEMP, there are no specific quantitative thresholds that raise a presumption of strategic significance. Instead, the CMA must simply demonstrate that the relevant digital activity has met one of four broad conditions i.e. (i) achieved significant scale or size; (ii) is used by a significant number of other firms in carrying on their business; (iii) has a position that would enable it to extend its market power to a range of other activities; or (iv) allows it to determine or substantially influence the conduct of other firms (see s. 6 DMCC). The CMA may draw on a broad range of quantitative and qualitative evidence to make such a finding (para 2.63 of CMA 194con), and it is likely that the strategic significance test will form a low bar for the CMA to prove.

Once the SMS Regime comes into force (anticipated in December 2024 / January 2025), the CMA has stated that it expects to conduct 3-4 SMS designation investigations in the first year, with parallel consultation on proposed Conduct Requirements (see para 10.4 of the Overview of the CMA's provisional approach to implement the new Digital Markets competition regime ("DMCC Roadmap") (see here). It is expected that the initial designation will reflect firms already facing scrutiny elsewhere (e.g. 'gatekeepers' under the DMA) and where the CMA already has an existing evidence base of concerns (such as in recent or ongoing markets / antitrust investigations) (para 4.6 of the DMCC Roadmap). In practice, this means the first designations will not come until late-2025 (i.e. nine months after commencement), and unlike the DMA, not all rules will start to apply at the same time. As described in further detail below, the CMA's powers to design and impose obligations on designated firms will follow a separate procedure to the designation process. However, to ensure efficient application of the regime, the CMA's design and implementation of some initial obligations may be run in parallel to the designation process and thus apply shortly after designation. The CMA will then have the ability to vary and iterate these obligations throughout the SMS firm's 5-year designation period.

Conduct Requirements (CRs)

Where a firm is designated as having SMS, the CMA will develop a bespoke code of conduct setting out the firm's CRs for the designated activity/activities.

The CMA's power to write conduct requirements is extremely broad – the only real requirement is that CRs must be "proportionate" (the proportionality test being arrived at following much Parliamentary debate) in the pursuit of principles of fair trading, open choice, trust and transparency (s 19(5 DMCC). These principles are defined very broadly in the DMCC, giving the DMU very wide discretion to decide what obligations should be imposed on each firm and craft them in such a way to fall within scope of the principles. While it is likely that CRs will include many of the same requirements as in the DMA, we expect that aspects of the SMS Regime will go beyond the DMA interventions (as well as being more targeted to each SMS firm), while some will be less restrictive (for further comment on this aspect, see here). As noted above, for efficiency, it is expected that initial CRs for prospective SMS firms will be developed (and consulted on) in parallel with the SMS designation investigations. This will allow the CMA to be able to immediately impose those CRs as soon as the firm is formally designated. The precise content of the CRs will therefore be finalised alongside designation (i.e. late-2025, at the earliest). Though the CMA can of course always decide to vary or iterate additional CRs on the SMS firm at a later date.

The CMA will also have powers to enforce the conduct requirements it applies, including by imposing fines of up to 10% of global turnover for breaches. The CMA may launch a six-month conduct investigation where it has reasonable grounds to suspect a CR breach (see ss. 26 and 30 DMCC). During this period, it may also impose interim enforcement orders and has the power to accept commitments from SMS firms in lieu of enforcement (s. 32 DMCC).

As part of the conduct investigation, an SMS firm may also submit evidence that the benefits to users of its conduct outweigh the harms of the breach and that the benefits "*could not be realised without the conduct*" (see ss 29 and 29(2) DMCC). This is known as the 'countervailing benefits exemption', and effectively establishes a defence to a breach. However, the bar to fulfil this exemption is particularly high and focused on user benefit. Unlike other traditional competition law tools, it is not simply a case of identifying an "objective justification" argument.

The CMA also has the power to subject SMS firms to the final offer mechanism (**"FOM"**) as a backstop for CR non-compliance. The CMA may apply FOM, where it has already imposed a CR for the SMS firm to trade on fair and reasonable terms, and the SMS firm fails to transact with a third party on such fair and reasonable terms in breach of a CR enforcement order. In such circumstances, FOM acts a process to ensure "fair" terms between SMS firms and those dealing with them, without the CMA needing to act as a price regulator. When triggered, the CMA will invite the SMS firm and the third party to each submit a payment term offer that they regard as fair and reasonable (s. 38(1) DMCC). The CMA will choose between the two offers. The FOM is intended to address the imbalance in bargaining power between SMS firms and other businesses, by incentivising parties to negotiate sincerely and fairly on payment terms (i.e., as the CMA can only choose between the two offers, parties are motivated to submit offers closer to a fair split of the joint value to increase the chances of their proposal being picked) (for further comment on FOM, see here). While the concept of FOM is derived from the context of negotiations between platforms and publishers (first considered in the CMA and Ofcom's joint advice to the UK Government on Platforms and Content Providers in 2021), under the DMCC, the CMA is not limited to only using FOM in such contexts.

Pro-competition interventions (PCIs)

The CMA will also have the ability to impose PCIs that address the 'root causes' of market power in the designated activity. These powers are very similar to those the CMA has under a Market Investigation Reference, but on a shorter (nine-month) timetable. It may begin a PCI investigation when it has reasonable grounds to consider that factor(s) relating to a digital activity may be having an adverse effect on competition (AEC) in the UK. Following an investigation, where the CMA finds an AEC, it will issue a PCI decision notice and within four months, where it would be proportionate to remedy the AEC, may impose pro-competition orders ranging from behavioural remedies to structural / operational separation of business units within the SMS firm. The order may also impose requirements to test and trial different remedies / remedy design options on a limited basis, before imposing any PCI on an enduring basis (s. 51 DMCC).

As with CRs, the CMA must consult on its proposed PCI decision and description of any proposed pro-competition order. The CMA is also able to accept commitments from SMS firms in place of a pro-competition order. When assessing whether a factor or combination of factors is having an AEC, the CMA will also consider in its assessment any competition-enhancing efficiencies that have resulted, or may be expected to result, from such factor(s) (see para 4.13 CMA 194con).

The CMA has also suggested that it may launch possible PCI investigations within a few months of commencement of the DMCC (see para 1.7 of the DMCC Roadmap).

Digital merger reporting requirements

The DMCC imposes certain mandatory merger reporting obligations on SMS firms, which contrasts against the typically voluntary nature of the UK's merger control regime. In particular, SMS firms will be obliged to report all material acquisitions (i.e., deal values of £25m and over) to the CMA which will result in the SMS firm's group having "qualifying status" (i.e., where shares / voting rights cross thresholds of 15%, 25% or 50%) in any undertaking that carries on activities in the UK, or supplies goods and services in the UK.

The CMA has published details of its proposed SMS Merger Reporting notice as part of its consultation on guidance for the SMS regime.

More generally, and outside the scope of this article, the DMCC also brings a host of other significant changes to UK merger control processes, which applies equally to all firms, irrespective of their 'digital' status (see here).

Appeals

Most decisions of the DMU will be subject to a review by the Competition Appeal Tribunal (CAT) on 'judicial review' grounds, and any person with sufficient interest can apply for review. This restricts the grounds on which a decision can be challenged: the CAT will only be able to intervene on grounds such as procedural fairness and errors of law, not purely on the basis that it would have reached a different conclusion.

Appeals of fines will be different: fines for breach can be appealed 'on the merits', while categories of financial penalties for procedural breaches, which will be reviewed in line with s.114 Enterprise Act which allows the CAT to quash a penalty, reduce the amount of penalty and change the date on which a penalty is payable.

Ultimately, this means that judicial oversight of many of the DMU's most consequential decisions (e.g., to designate a firm as having a SMS and impose conduct requirements) will remain limited, both in itself and by comparison to comparable regimes. Some parliamentary oversight on the CMA's powers is, however, provided through requirements that SMS Regime guidance (critical in a regime that provides such broad and vague powers) must be approved by the Secretary of State. The CMA will also report to Parliament on the DMCC as part of its Annual Report.

Conclusion

As the CMA prepares for the commencement of the DMCC in late 2024/early 2025, greater clarity is emerging on how it intends to administer the SMS Regime, including on how firms may engage in the process. The CMA has issued its DMCC Roadmap and a consultation on its proposed SMS Regime guidance (which will ultimately need to be approved by the Secretary of State – a late amendment to the legislation during the Parliamentary process intended to make the CMA more accountable to Parliament).

The DMCC hands the CMA incredibly broad powers to administer a regime that – if it achieves its stated goals – will be more flexible, targeted and proportionate than its EU counterpart in the DMA. Critically, the CMA has enormous discretion in deciding *who* to regulate and *what rules apply*. While there will doubtless be a significant part of the SMS regime that looks very similar to the DMA, the CMA has the power to go further than the DMA, where it deems it appropriate. At the same time, the CMA will be under pressure to ensure the UK does not look 'unfriendly' to tech businesses. This makes for an interesting potential tension which will doubtless loom large over the operation of the regime and how precisely the CMA navigates these potentially conflicting pressures will be fascinating to watch.

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