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House of Lords
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My Lords,

Thank you for your constructive engagement during the second Grand Committee session of the Digital Markets, Competition and Consumers Bill (the Bill) on Wednesday, 24 January.

During the session, I said I would write to you on: why we added a proportionality provision at the House of Commons report stage; the change in the 'indispensability' wording of the countervailing benefits exemption; the meaning of 'countervailing benefits'; clarifying how consumer benefits are considered in relation to conduct requirements and pro-competition interventions; Ofcom's role in private actions brought under Part 2 of the Communications Act 2003; and how the countervailing benefits exemption interacts with private actions brought under Part 1 of this Bill.

Why we added a proportionality provision at the House of Commons report stage:

The Government is committed to proportionate, pro-innovation regulation. This Bill will give the CMA significant new powers, and it is particularly important that they are exercised reasonably and proportionately.

Noble Lords have rightly said that the CMA has existing obligations to act proportionately, and these would already have applied in most of the interventions the CMA could make under the new digital markets regime. In most cases a firm would have been able to appeal a decision on the grounds of proportionality, in particular where interventions were disproportionate interferences with firms' property rights under the European Convention on Human Rights (ECHR).

However, there are cases where these rights do not apply and therefore decisions would not have been be open to challenge on grounds of proportionality. This includes cases where future contracts would be affected by an intervention, which currently would not engage Article 1 of the First Protocol (A1P1).

The Government engaged extensively with legal and tech stakeholders following Commons committee stage, who raised concerns that the Government's commitment to a proportionate regime was not sufficiently embodied in the legislation. The Government's amendments at Commons report stage therefore make it clear that the CMA must act proportionately in *all* cases. It also sets out explicitly what the CMA's interventions must be proportionate in relation to – for the purposes of one or more of the three objectives set out in clause 19(5) in the case of conduct requirements, and 'for the purposes of remedying, mitigating or preventing the adverse effect on competition' in the case of PCIs.

To be clear, these are all arguments that can be made under judicial review and so these appeals will be assessed under normal judicial review principles. We are not extending the appeals standard to "JR+" or an appeal on the merits with this change.

Finally, I would like to be clear that removing the proportionality requirement would not allow the CMA to act disproportionately – it would still be bound by public law requirements to act reasonably. However, this would be different to the requirement we added for proportionality where ECHR is not engaged. Instead, we think it right that the same, consistent approach should apply in all cases.

The change in the "indispensability" wording of the countervailing benefits exemption

I would now like to respond to the important points which arose in relation to the change in wording of the countervailing benefits exemption.

Baroness Harding asked about stakeholders who felt the previous "indispensability" wording was unclear. Stakeholders on all sides generally wanted greater clarity on what the threshold was and how the exemption would operate. By having the exemption threshold expressed in ordinary terms on the face of the Bill, the Government has sought to provide this clarity, while maintaining the same high threshold as the previous wording.

Related to this, I would also like to provide clarity on a point raised during my exchange with Lord Fox. The current wording of clause 29(2)(c) is that the *"benefits could not be realised without the conduct".* In the government's view, this wording has the same meaning and sets the same threshold as the previous wording, which was that the *"conduct is indispensable ... to the realisation of those benefits"*. I judge the two sentences to be indistinguishable in meaning as both sets of words mean that there must be no other reasonable, practicable way to achieve the same benefits with less anti-competitive conduct.

Finally, several Lords asked whether replacing the "indispensability" wording means legal precedent will no longer apply. As I outlined in the session, the fact the countervailing benefits exemption will apply within an entirely new regime means that existing case law would not be directly applicable anyway. Similar exemptions exist in competition legislation, namely the efficiencies exemption for anti-competitive agreements in section 9 of the Competition Act 1998, and the relevant consumer benefit test in market investigations under the Enterprise Act 2002. They are worded in different ways to each other, reflecting the particular statutory frameworks in which they sit.

For the Digital Markets regime, the well-understood application of these other existing measures can, and should, still help inform parties and the courts about how this one will operate.

I hope this helps to reassure the Noble Lords that the change in the "indispensability" wording is intended to be helpful to all stakeholders by increasing clarity, while – crucially – maintaining the same high threshold.

The meaning of 'countervailing benefits'

Lord Kamall raised an important question about what the government really means by 'countervailing benefits' in the countervailing benefits exemption. The hypothetical example below illustrates how the exemption can work in practice.

Conduct requirement on discriminatory policies (clause 20(3)(a))

An SMS firm could ban an application from its platform, thereby potentially breaching a conduct requirement not to apply discriminatory terms. Where the DMU launched an

investigation, the firm could claim that it banned the application to protect users' security and therefore that the countervailing benefits exemption should apply.

Crucially, the DMU would only close its investigation into the SMS firm's conduct if the firm provided sufficient evidence – such as an independent report from security experts – that all the criteria and the high threshold were met. This means the exemption could only be applied if there was sufficient evidence that the benefits (in this case, relating to the security of users) outweighed the harm on competition, and that those benefits could not be realised in a different way. I also want to remind Noble Lords of the other criteria that need to be met before the exemption can apply: the SMS firm's conduct must be proportionate to the realisation of the benefits, and the conduct must not eliminate or prevent effective competition.

I hope this explanation reassures Lord Kamall and other Noble Lords that the exemption has a high bar and that it will help ensure consumers get the best outcomes in both the short and longer term.

Clarity on how consumer benefits are considered in relation to conduct requirements and pro-competition interventions (PCIs)

Lord Kamall also asked for examples indicating how consumer benefits would be taken into account when imposing pro-competition interventions (PCIs). For the avoidance of any doubt, I will clarify the different ways consumer benefits are considered in relation to conduct requirements and pro-competition interventions.

Conduct Requirements

When setting conduct requirements, the DMU is required to take consumer benefits into account, in accordance with the provisions in clause 19(10), as well as its organisational duty to promote competition for the benefit of consumers. This is because it is important that conduct requirements do not prevent SMS firms from developing innovations which are beneficial for consumers. Conduct requirements are a type of ex-ante regulation, and can be used to prevent harm *before* it occurs. Therefore the countervailing benefits exemption, as outlined in detail above, is intended as a further safeguard in the legislation to ensure that benefits which might have been unknown when the conduct requirements were first imposed, can be recognised. The exemption is available for potential breaches of conduct requirements only.

Pro-competition interventions (PCIs)

While conduct requirements can prevent competition harms *before* they occur, PCIs will tackle the *sources* of a firm's market power which give rise to SMS, by addressing identified 'adverse effects on competition' (AECs). An AEC can relate to both the structural features of a digital activity that has tipped the market in favour of one or two powerful firms, and also the conduct of SMS firms that can result in competition harms. By promoting competition, PCIs will therefore make digital markets more contestable over time, leading to better outcomes for consumers.

Once the DMU has identified an AEC, it can consider any associated consumer benefits or consumer detriment connected to the competition problem. This can inform the design of any remedies that the DMU identifies to address the AEC. If an SMS firm identifies some benefit to consumers from the competition problem, then this does not prevent the DMU from making a PCI. This will allow the DMU to identify effective remedies, whilst at the same time preserving any associated consumer benefits or conversely minimising any associated consumer detriment. For example, the DMU may order an SMS firm to run a trial of different choice screen layouts, to determine which design is most effective at boosting competition whilst preserving any consumer benefits and avoiding unintended consequences. The DMU

will also be under an ongoing duty to monitor any PCIs it imposes, to ensure they remain appropriate for addressing the competition issues.

Ofcom's role in private actions brought under the Communications Act 2003

Baroness Stowell raised the important question of why we have chosen not to replicate the mechanism through which Ofcom's consent is required to bring certain private actions and whether there is inconsistency with our provision for a countervailing benefit exemption and private actions.

Under sections 104(4) and 105W(6) of the Communications Act 2003 claimants require consent from Ofcom to bring certain private actions. A small number of stakeholders have suggested that this approach should be adopted for the digital markets regime.

This mechanism raises a number of considerations in the digital markets context. Firstly, it would risk politicising the CMA, which would be required to make a contentious choice on whether to allow each private action. The decision to consent would itself also be appealable through judicial review, reducing certainty and clarity for stakeholders. These issues are less prevalent for breaches of requirements imposed by Ofcom as the primary route for redress is through the Communications Ombudsman, whereas there is no equivalent function in the digital regime.

Therefore I hope this will reassure my Noble Lords that replicating such a mechanism would not be suitable for private actions brought under Part 1 of this Bill.

Private actions and the countervailing benefit exemption

We have provided a countervailing benefits exemption in the digital markets regime as a safeguard, to ensure that the CMA has a mechanism to recognise consumer benefits which might have been unknown at the conduct requirement setting stage. The process, for assessing whether the criteria for the exemption have been met, will be rigorous to ensure that consumers get the best outcomes.

We have heard from a small number of stakeholders that they find it inconsistent that the countervailing benefit exemption should apply only to the CMA when investigating conduct breaches, and not to the courts in private actions.

Our position, and the Bill as drafted, recognises that the CMA should not punish nor prevent conduct which brings overwhelming wider benefits, but that such conduct may on occasion cause harm to a specific party. In these circumstances, a court remedy could be appropriate.

We also understand that whilst a court is not bound to consider the countervailing benefit exemption explicitly, a court would be likely, when considering appropriate remedies, to take into consideration where the CMA considers that the exemption applies to the firm's conduct.

Therefore, I hope this will reassure my Noble Lords that our approach strikes the right balance and that any changes would be undesirable on this matter.

I will place a copy of this letter in the libraries of both Houses.

Yours sincerely,

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Department for Science, Innovation & Technology