

Testimony of Tommaso Valletti, Ph.D.

**Professor of Economics
Imperial College Business School
Imperial College London**

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On
**“Online Platforms and Market Power Part 3:
The Role of Data and Privacy in Competition”**

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Chairman, Ranking Member, and Members of the Subcommittee, thank you for inviting me to testify today. My name is Tommaso Valletti and I am Professor of Economics at Imperial College Business School in London, UK. Between September 2016 and August 2019, I was Chief Competition Economist of the European Commission (DG COMP). In that role, I led the economic analysis of several cases involving digital platforms that are relevant for the issues that we are discussing today. In particular, I presided over the issuing of Google Shopping, the investigation and issuing of Google Android, the investigation and issuing of Google AdSense, and further investigations related to Google's local search, Apple's App Store, Amazon Marketplace and Facebook.

My views are only personal and do not represent in any way those of the European Commission. Still, I think that it is important to note that Europe has been at the forefront in the policy area concerning digital platforms, whereas US antitrust has been more reluctant to intervene. Europe has at times been looked at as a lagging economy with some jealousy vis-à-vis US tech giants. In reality, these are important issues that need to be tackled irrespective of the geographic origin of a particular company. In my experience, there is no anti-US sentiment in European competition enforcement, and all the evidence points to the contrary.¹

European competition policy towards platforms is based on sound economics, and Europe has led the way in realizing that there are potential problems related to digital platforms that can be also dealt with through antitrust enforcement. It is encouraging to see the attention this view is getting in the US now, and I applaud the current focus on these matters. There is in fact a widespread climate of reflection around the world, as evidenced by the many reports that are issued and hearings that are held on online platforms across jurisdictions. Interesting discussions are also happening, for instance, in France, Germany, the UK, as well as in Australia and Japan. These reports and hearings explore how competition authorities should meet the challenges arising from analyzing competition among platforms and show a high degree of convergence when it comes to identifying these challenges. The most important ones are (i) understanding the role of data, (ii) scrutinizing acquisitions of innovative start-ups by the incumbents, (iii) analyzing the source of platforms' market power, and (iv) supervising how platforms compete in markets with strong network externalities and returns to scale (especially in the absence of multi-homing, or protocol and data interoperability). It is inspiring to see this convergence of views and I very much hope that there will now be concerted action on these issues, given the global scale and size of the companies involved.

During my testimony today I will focus on what I see as the most important issues in the debate:

1. My first point is that data collection and privacy protection are at the very core of the business model of many online digital platforms. Little is known about data use and consumer preferences over privacy because of a conscious decision by the very same incumbent platforms not to disclose any data to independent researchers.

¹ See Anu Bradford, Robert J. Jackson and Jonathon Zytnick, "Is E.U. Merger Control Used for Protectionism? An Empirical Analysis", *Journal of Empirical Legal Studies* (2018). The authors analyse over 5,000 decisions by the European Commission between 1990 and 2014 and find no evidence that the Commission has used its authority to protectionist ends.

2. My second point is that privacy is a problem relevant for competition law.
3. My third point is that degradation of consumer privacy can lead to objective costs for platform users.
4. My fourth and last point is that there are several plausible theories of harm involving data and privacy protection that can be investigated.

My first point concerns the importance of data. The collection and use of personal data are key features of digital markets and has created significant benefits for consumers. Yet, they also pose considerable challenges, especially in concentrated markets and in the presence of market power. Some commentators have argued that data is the new oil. Others have gone to the opposite extreme by claiming data is as common as water. These sweeping generalizations are not useful. It is self-evident that data is key to digital platforms, and that some applications imply real-time knowledge of consumer behaviour as well as cross linkages across apps that only very few digital players have access to. Only a few digital gatekeepers are therefore in a position to control the tracking and linking of those behaviors across platforms, online services and websites: they can combine several datasets and create “superprofiles” of individual users. Ultimately this implies that real-time targeted advertising is done at the level of each individual consumer. This is the market for individual “attention” where the competitive analysis often has to be conducted.²

Unfortunately, the debate over the practical importance of data and the linkage to platforms’ market power is not helped by the lack of published empirical studies on these matters in academic journals in the field of economics. I conducted a simple exercise, counting the number of published articles in the so-called “top 5” journals in economics³ over the 5-year period 2014-2019 that used primary data from one of the top 5 digital companies (Google, Apple, Facebook, Amazon and Microsoft that collectively go under the acronym of GAFAM) to tackle a question related to competition or competition policy. These are companies that are collectively worth several trillion dollars and sit on an unprecedented trove of data that would allow us to shed light on these questions in a much more detailed fashion. Given that empirical work is the gold standard for economic studies, one would expect a large interest from economists worldwide in such studies. Even so, there are virtually *zero* published papers in the competition arena using the relevant data from these platforms.

This is not an academic curiosity, but it is the intentional outcome of data access choices made by the large digital players. The lack of access also implies that there is de facto no system of revolving doors between these companies and academia when it comes to young economists: if you are a young scholar and cannot publish, you are not going to come back to academia after an experience at one of the GAFAM.⁴ Possibly even worse, generations of bright

² See Andrea Prat and Tommaso Valletti, “Attention Oligopoly”, 2019. <http://dx.doi.org/10.2139/ssrn.3197930>. We propose a metric of consumer “attention” and argue that, when the market of digital platforms becomes concentrated, “attention” becomes a scarce resource for advertisers and only more expensive consumer products are ultimately shown to platform users, to the detriment of consumer welfare.

³ These are: American Economic Review, Econometrica, Journal of Political Economy, Quarterly Journal of Economics and Review of Economic Studies.

⁴ Microsoft Research is an exception, but again there are no published outcomes in competition economics over the period I considered.

academic economists have avoided investigating empirically the field altogether, as they anticipated that their efforts would not lead to publishable work. Because of this, academics have stopped asking relevant questions about GAFAM for too long, and the external understanding of digital issues has not much advanced empirically, compared to the internal knowledge of GAFAM that are therefore several steps ahead of anyone else, including the regulators. This lack of academic scrutiny also plagues the interpretation of the very few available studies coming from other data sources, so the debate necessarily remains at some vague abstract level, missing all the necessary empirical details of each case.⁵

A relevant example is the so-called “privacy paradox” – the idea that consumers care about preserving whatever privacy they have, but few actually take steps to share less data online. This observation is sometimes used to argue that one should not worry about privacy, as consumers “reveal” that they do not really care much about privacy. In reality, it is hard to draw such conclusions about people’s values from their actions (this is the so-called “revealed preference approach” in economists’ jargon). That is because consumers’ choices are shaped by very complex factors, which in the current case often include a very poor understanding of data practices. Consumers de facto face a pervasive and invisible collection of their personal information. Who has actually read lengthy and obscure privacy policy terms? Even if you have, what do they mean? The main issue is the lack of transparency about current and future data practices and the ability to understand the effects of such practices (think of common phrases like “we may collect your personal information for marketing purposes”, or “we may share your personal data with affiliates and trusted businesses”). Clearly, a revealed preference approach where the “user is king” cannot apply if the consumer cannot properly compare the possible future costs to present benefits, as the very same consumer is prevented from understanding these future costs. Consumers see the instant benefit of saying “yes” to opaque privacy terms, as there is an immediate reduction in transaction costs plus a reduced risk of losing some functionality of the platform, but cannot assess the implications of giving away their data that are bundled by design to the service they want.

Academics have been trying to get an idea about consumers’ preferences by conducting surveys and experiments. Alas, also in this case one cannot infer much from surveys that involve at most a few thousand individuals being asked questions or taking actions they do not fully comprehend. Consumers’ valuations of data privacy are shaped by factors like the wording of the questions they are asked, the information they are given, and the range of choices they are presented with. A top scholar in this field, Professor Alessandro Acquisti of Carnegie Mellon University, after having devoted almost two decades studying this phenomenon, concludes that consumers’ behavior and preferences are not a reliable indicator of how consumers value their own privacy, let alone how society as a whole should value it.⁶

⁵ One should not presume that the same happens in every other industry. On the contrary, with airlines, pharmaceuticals or telecommunications to name just a few, datasets are available to analyze their competitive landscape. Where individual data have been collected, these are anonymized following established protocols.

⁶ While of course every quote has to be read in a wider context, I would like to cite Prof. Acquisti *verbatim*: “Even subtle changes in the way privacy trade-offs are presented to individuals can cause radical changes in people’s valuations of their data or the importance of keeping their data protected. One of the conclusions of my research

Notwithstanding these empirical limitations, my second point concerns the extent to which competition authorities should consider privacy concerns *also* under competition law, besides privacy law or consumer law. First, these approaches are not mutually exclusive as one does not exclude the other. Second, I will argue that privacy is at the core of the economics of many digital platforms, and competition is shaped around it. The possible degradation of consumer data protection can result from market power, and it will undermine the competitive process as well as lead to detriment to consumer welfare. I also believe that several tools for intervention are already available, and one just needs to apply them.

Why is privacy a competition problem? For several reasons. Let me start from the obvious observation that competition takes place along several dimensions, with price being only one of them. Quality, choice, and innovation are also important aspects for competition and for consumer welfare. In fact, when dealing with digital platforms (Facebook and Google in particular), where business models have been consciously built around supposedly “free” services, in order to monetize in other tied markets (advertising in particular), it does not make much sense to focus the competitive assessment on prices, as these have been set at zero by choice. Quality, however, will often be the relevant locus of competition. Lack of competition, in many markets, will lead to higher prices and reduced quality. In the context of “zero” prices, the reduction in quality due to monopolization can become even more pronounced. A reduction in consumer data protection and consumer privacy is precisely a fitting example of such a reduction in quality.⁷

My third point is that privacy degradation can lead to an objective detriment to consumers. This can arise in different ways: e.g., through risk of data breach, identity theft, or customer profiling that is not done in the interest of consumers (e.g., scoring that can lead to discrimination, being shown more expensive search results, marketing based on vulnerability, risk analysis, etc.). These are all objective costs related to lower privacy and lack of competition. Part of the problem is that the giant digital incumbents have the ability to engage in “concealed” data practices,⁸ that is, they impose terms of service with weak privacy protection that are not well understood but still accepted by consumers because of a lack of alternatives – this is an indication of their market power. These practices undermine the role played by consumers, as they increase information asymmetries. They also undermine the competitive process in a way that can be particularly acute in digital markets. Digital markets already tend to exhibit features that make it difficult for new rivals to compete with dominant incumbents (e.g., network effects create barriers to entry). Concealed data practices make successful entry even less likely, both due to the competitive advantages enjoyed by the

is that it’s probably fruitless to try to pinpoint with a single number the value of privacy.” OneZero, September 17th, 2019; <https://t.co/6ktswjhqz>.

⁷ There exists a detailed case study about Facebook and its privacy policies. In the mid-2000s, when Facebook was an upstart social media platform, it tried to differentiate itself from the market leader, Myspace. In particular, Facebook publicly pledged to protect privacy. But as competition with Facebook began to disappear (also helped by Facebook’s acquisition of Instagram in 2012 and WhatsApp in 2014), Facebook revoked its users’ ability to vote on changes to its privacy policies. See Dina Srinivasan, “The Antitrust Case Against Facebook”, Berkeley Business Law Journal, vol. 19, 39-101 (2019).

⁸ Katharine Kemp, “Concealed Data Practices and Competition Law: Why Privacy Matters” (2019). https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3432769.

incumbent as a result of weak data protection, and due to the concealed nature of data practices that make comparisons of alternatives difficult to perform. Consumers are not able to contrast improved quality offered by rivals when they cannot make real comparisons. Similarly, consumers will not pay more to avoid a cost which cannot be evaluated.

My fourth and last point is about theories of competitive harm. Lower quality, which is the counterpart to high prices, can be seen in competition law terms as an exploitative conduct. In Europe, this is captured by the law against abuse of dominance under Article 102. In other jurisdictions it is not. Still, it would be wrong to ignore exploitative conduct because, as I just argued, lower privacy protection affects the core perimeter of competition among digital platforms: data, privacy and competition are inexorably linked. Diminished competition on privacy quality should therefore be taken into account in any assessment of the state of competition, and market power, of digital online platforms. Ultimately, one would like to see more competition in the market. With more competition (including competition over privacy terms), it would probably become clear that consumers are currently “underpaid”. If there is competition, it may ensue that the competitive price for personal data would not be zero, but that consumers should actually be compensated to permit the collection of their personal information.

Lower data protection can also lead to the standard legal category of exclusionary behaviour which undermines the competitive process. Imagine, as argued above, that the dominance of an incumbent digital platform allows it to impose restrictive terms of service and loose privacy terms. Consumers will then have to accept them, because of a lack of alternatives. The incumbent will thus acquire a data advantage compared to its competitors (which is magnified by the absence of interoperability and data portability). The incumbent then entrenches its dominant position, which allows it to extract rents (increased advertising revenues) and to impose even more restrictive privacy policies on consumers. As a result, leveraging in neighboring markets becomes easier: the rents enjoyed by the incumbent can be partly spent to “bribe”, for instance, phone manufacturers to accept pre-installation or exclusivity of the incumbent’s services, leading to foreclosed entry by competitors. Tying with other digital products will further strengthen the data advantage enjoyed by the dominant incumbent by cross-linking the data collected across services, creating a vicious circle.⁹

Limited data protection can therefore lead to both exploitative and exclusionary conduct by dominant platforms. These are all conducts that could, and in my opinion should, be investigated.

Thank you for your time. I really appreciate the opportunity to be here today, and I look forward to your questions.

⁹ Other exclusionary practices can easily be envisaged. Think of conducts where a dominant firm excludes privacy-enhancing apps from its platform. Or acquisitions of rivals that have been innovating on privacy, and so forth.