ITIF | INFORMATION TECHNOLOGY & INNOVATION FOUNDATION
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COMMENTS OF ITIF

Before the

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Brasilia, Federal District, Brazil

In the Matter of:	)	
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Draft Bill No. 2768/2022	)	Public Comment
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PUBLIC CONSULTATION ON DRAFT BILL NO. 2768/2022: ENABLING THE DIGITAL TRANSFORMATION THROUGH COMPETITION, NOT REGULATION

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INTRODUCTION

On October 11, 2022, João Maia (MP, Partido Liberal) presented Bill 2768/2022[1] (Bill) to the federal legislators of Brazil, which contemplates the regulation of its digital markets. The Bill proposes to amend two laws: the General Telecommunications Law[2] (9472/1997), which provides rules for the legal structure of telecoms services, defines the general principles governing the telecoms services, and created the Brazilian Telecoms Agency (Anatel); and the Brazilian Civil Framework of the Internet[3] (12,965, of April 23, 2014) which establishes the principles, guarantees, rights and duties for the use of the Internet in Brazil. The Bill bears a considerable resemblance to the Digital Markets Act (DMA)[4] of the European Union (EU), which gradually entered into force between May 2, 2023 and June 25, 2023. At present, the Brazilian "DMA" Bill is awaiting an opinion from the rapporteur at the Economic Development Commission (CDE) of the Brazilian Parliament.

The Schumpeter Project on Competition Policy of the Information Technology and Innovation Foundation (ITIF) appreciates the opportunity to comment on the Bill, and specifically to discuss its problems with respect to promoting innovation. ITIF is the world's top-ranked science and technology policy think tank. ITIF's comment proceeds in five parts. First, regulation in the digital sector should be necessary to remedy market failure, which does not appear to be the case here.[5] Second, even if regulation is justified to address

[1] Portal da Câmara dos Deputados (camara.leg.br).

[2] General Telecommunications Law, available at: L9472 (planalto.gov.br)

[3] The Brazilian Civil Framework of the Internet, 2016.

[4] The European Parliament and the Council of the European Union adopted the Digital Markets Act on 14 September 2022, a Regulation 2022/1925 on contestable and fair markets in the digital sector and amending Directives (EU) 2019/1937 and (EU) 2020/1828.

[5] The Digital Markets Act Is "Bad Economics and Bad Law," Says ITIF | ITIF

market failure, regulation should put forward clear goals that complement the broader legal and regulatory ecosystem, and here again the Bill is lacking. Third, even if the Bill could be facially justified, it is far too broad in its application. Fourth, the obligations in Article 10 of the Bill are substantially out of step with sound legal and economic principles for applying antitrust law to protect innovation. Finally, ITIF recommends Brazil step back from following the EU's experimental and harmful DMA regime[6] and at least wait[7] before embarking on a similar policy.[8] A brief conclusion follows.

THE DRAFT REGULATION IS UNNECESSARY

As a general matter, *ex ante* regulation is justified only in the presence of market failure. But the existence of market power does not by itself indicate that market failure exists. Since the groundbreaking work of Joseph Schumpeter in the 1940s, it has long been understood that competition is not merely, as neoclassical economics holds, an equilibrium where price equals marginal cost. Nor is it simply, as Adam Smith imagined, a rivalry between many sellers in a market. Rather, as Schumpeter explained, innovation or dynamic competition occurs through "gales of creative destruction"[9] whereby one firm competes *for* the market by creating a new product, only to be challenged by additional "leapfrog competition" that supplants the formerly dominant firm with a still newer product that not just dazzles consumers but allows for the firm to recoup the costs of its innovation.

In the context of these Schumpeterian dynamics, the Brazilian digital ecosystem does not appear to currently exhibit signs of market failure. On the contrary, Brazil's digital landscape is nascent and well positioned to become a vibrant and dynamic arena where firms are incentivized to compete through creative destruction. Indeed, the Brazilian economy had been marked by a period of substantial growth and social progress, and is poised for a 'digital transformation'. With a population of almost 220 million citizens, Brazil is the largest country in South America (and the fifth largest fintech market in the world), presenting an immense market potential.[10] Recent trends[11] indicate a commitment to digital innovation, as evidenced by the National Internet of Things Plan and the Brazilian Digital Transformation Strategy (E-Digital).[12] The vibrant and emerging digital market, with its potential to fuel productivity growth, has become a focal point in leveraging Brazil's economic resilience. As Brazil embraces policies that promote trust, innovation, and market openness, the digital sector thus constitutes as a significant aspect of the country's economic strategy. In sum, the

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[6] AURELIEN PORTUESE, The Digital Markets Act: A Triumph of Regulation Over Innovation | ITIF, 2022

[7] LILLA NORA KISS, The United States' Tech Regulatory Dilemma—Through a Foreigner's Eyes - Digital Platforms and American Life: A Project by the American Enterprise Institute (aei.org), 2023

[8] AURELIEN PORTUESE, The Digital Markets Act: European Precautionary Antitrust | ITIF, 2021

[9] JOSEPH A. SCHUMPETER, CAPITALISM, SOCIALISM, AND DEMOCRACY 81 (1942).

[10] MALENA DAILEY, Why the U.S. Rejected European Style Digital Markets Regulation: Considerations for Brazil's Tech Landscape, 2023, available at: https://www.progressivepolicy.org/wp-content/uploads/2023/10/PPI-Brazil-EU-Tech.pdf.

[11] See more at OECD: Brazil in the digital transformation: Opportunities and challenges | Going Digital in Brazil | OECD iLibrary (oecd-ilibrary.org).

[12] MCTIC (2018), Brazilian Digital Transformation Strategy: E-Digital, Ministério da Ciência, Tecnologia, Inovações e Comunicações, Brasilia, www.mctic.gov.br/mctic/export/sites/institucional/sessaoPublica/arquivos/digitalstrategy.pdf .

nascent and essential nature of Brazilian digital markets belies the existence of evident market failure but rather underscores the argument against immediate and extensive regulation.

Even in the case of market failure, regulation should only be undertaken if it would be superior to non-regulation. Especially in innovative industries, regulatory measures that go beyond competition law enforcement may impede the natural process of competition—hindering economic dynamism and stifling long-term growth.[13] Put another way, regulation can be far more harmful than helpful when addressing market failure, including by placing costs on market entrants that ultimately benefit established incumbents. That is, the entry of new, innovative firms and the competitive forces within the market, unimpeded by regulation, are often the best mechanisms to address any market imbalances.

Moreover, even if digital markets appear to exhibit monopolistic tendencies, such market power is often transient: dynamic competition, if left to function freely and on the merits, will support self-correction. In addition, any assessment of market power requires accurately defining markets. In the case of digital platforms, the relevant market is usually "eyeballs". A Sao Paulo resident that is using Twitter is not using YouTube, LinkedIn, Facebook or TikTok. In other words, even though digital plaforms serve particular niches, they compete fearcely for consumer attention. To the extent any become "lazy monopolists" they will quickly lose market share. Moreover, on the ad side of the market, there is intense competition[14], with Brazilian advertisers having a wide array of choices of getting their messages to consumers.[15]

Instead of preemptive regulatory measures, the emphasis should thus be placed on allowing innovation and competition to flourish by enabling a healthy competitive process, including through sound enforcement of Brazil's competition laws to address any anti-competitive conduct. At bottom, there is no evidence that the current Brazilian market has failed or discourages competition on the digital markets.

THE DRAFT REGULATION IS NOT PROPERLY TAILORED

Another major concern with the Bill is its incredibly broad and open-ended nature. *Ex-ante* regulation, which involves setting rules and standards before potential issues arise, requires well defined goals to be effective. Specifically, regulatory frameworks that are too broad and multifaceted risk hindering the adaptability and responsiveness that is particularly needed in digital markets, which are characterized by rapid technological evolution. In this sense, the ex-post nature of antitrust law, which involves addressing market issues after they have occurred, differs significantly from the ex-ante approach embraced by the proposed regulations, and should be the preferred form addressing potential market issues. Without question, the *ex-post* nature of antitrust allows for a more flexible response to emerging challenges, enabling authorities to intervene, when necessary, without preemptively constraining market dynamics.

Unfortunately, the Brazilian Bill provides a general framework is too all-encompassing to provide sufficient guidance about its application. Specifically, articles 4 and 5 of the Bill respectively delineate six broad and

[13] See Robert M. Solow, Technical Change and the Aggregate Production Function, 39 Rev. Econ. & Stat. 312 (1957); see also Charles I. Jones, Sources of U.S. Economic Growth in a World of Ideas, 92 Am. Econ. Rev. 220 (2002).

[14] Brazil - Finance (trade.gov)

[15] Brazil in the digital transformation: Opportunities and challenges | Going Digital in Brazil | OECD iLibrary (oecd-ilibrary.org)

incommensurable principles and five objectives that will surely create confusion. The objectives encompass economic development, fair competition, access to information, knowledge and culture, promotion of innovation, massification of new technologies and access models, encouragement of interoperability through open technological standards, and the incentivization of mechanisms for data portability—a hodge podge of conflicting goals. Some of these goals should be addressed by other legislative products and not by antitrust legislation. The same is true with the enumerated of principles such as freedom of initiative, free competition, consumer protection, reduction of regional and social inequalities, repression of abuse of economic power, and expansion of social participation in public interest matters. These far-reaching statements of principles and objectives lacks clarity, making it challenging to distinguish between regulatory priorities focused on maintaining fair competition and those aiming at broader societal and economic goals.

In addition to the need for a clearly defined set of goals, the Bill also introduces a risk of regulatory fragmentation, or the existence of disparate regulations that overlap and conflict with one another. The risks of regulatory fragmentation are evident from the European experience with the DMA.[16] In fact, while the DMA was introduced as an attempt to limit regulatory fragmentation by establishing EU-wide regulations, the legislation fell short of this goal, as it permitted additional national regulatory initiatives and did not remove existing national regulatory barriers. This lack of harmonization raised concerns about decentralized and disparate enforcement practices, potentially exacerbating regulatory fragmentation within the EU. For example, while the DMA allowed Member States to set new rules on gatekeepers, this flexibility contributed to potential inconsistencies and contradictions between the DMA and national rules. Such overlap is likely to hinder the harmonization of digital regulations within the EU, resulting in regulatory fragmentation and confusion rather than a unified approach.

The Bill seems poised to result in similar regulatory confusion. The Bill proposes that the regulation should be administered by the Telecommunications Agency (Anatel). However, the subject matter affects at least three agencies: Anatel, the Administrative Council for Economic Defense (CADE), and the Brazilian Data Protection Agency (ANPD). This regulatory triad plays distinct roles in overseeing different facets of the digital landscape, and the Bill's focus on digital platforms with essential access amplifies their interdependence. In so doing, the Bill, and particularly the allocation of powers to Anatel for monitoring and prosecuting anticompetitive conduct by digital platforms, introduces a serious risk of regulatory fragmentation. Specifically, concurrently empowering Anatel and CADE with full competition enforcement in digital markets raises concerns about the potential overlap and risk of over-enforcement in their respective actions.

THE DRAFT REGULATION APPLIES TOO BROADLY

Regulation should be narrowly focused to avoid imposing unnecessary costs on market participants, including the smaller players and entrants that may stimulate competition. Rather, as noted above, regulation should be targeted to address market failure and the corresponding dominant firms who enjoy a high degree of durable market power. On this score, the Bill's defines digital platforms having essential control as encompassing

[16] Aurelien Portuese: The Digital Markets Act: A Triumph of Regulation Over Innovation, 2022, available at: https://itif.org/publications/2022/08/24/digital-markets-act-a-triumph-of-regulation-over-innovation/.

companies with annual gross revenues exceeding BRL 70 million in services to Brazilians—which is less than $15 million.

This broad definition of digital platforms encompassing companies with annual gross revenues exceeding BRL 70 million in services to Brazilians introduces a paradoxical situation. The general definition of digital platforms and the *ipso iure* assumption that they market power that could be driving market failure seems very hard to support. Specifically, the Bill might ensnare not just the large players but also smaller entities that lack the market influence commensurate with the regulatory burden imposed. This counterproductive outcome could deter innovation, hinder market entry for smaller players who reach the threshold of the regulation, and potentially stifle the very competition the regulations aim to promote.

In this regard, the Bill reflects a striking departure from the EU's DMA lies in the definition of digital platforms deemed as "gatekeepers." That is, the European Commission's "gatekeeper" criteria are more nuanced, considering factors such as significant impact on the internal market, provision of core platform services crucial for business users, and an entrenched or foreseeable durable position. Currently, it only applies to the largest digital players. The European approach thus reflects a narrower understanding of what entities should be subject to regulation, and thus at least in one way avoids the pitfalls of undue overbreadth relative to the Bill. As a result, the draft Bill goes dangerously beyond the EU regulatory standards and risks imposing significant costs on Brazil's competitiveness relative to the EU and other jurisdictions.

THE DRAFT REGULATION WILL CHILL INNOVATION

The Brazilian DMA's overbroad definitions and lack of well-defined goals are not the only factors contributing to the Bill's problems from a competition and innovation perspective., First, Article 10 of the Bill introduces obligations for digital platforms with essential access control power to "non-refusal of provision of access to the digital platform to professional users." In general, sound legal principles provide for freedom for corporations to select their partners, as reflected in U.S. Supreme Court jurisprudence.[17] Although it is also true that under certain circumstances, there may be limits on this freedom for a firm with market power, a general prohibition on refusals to deal chills innovation. Specifically, maintaining the exclusivity of certain innovations can foster competition by encouraging companies to continuously strive for advancements, knowing that they can reap the rewards of their efforts without immediate compulsory sharing. This approach aligns with the idea that robust competition can be driven by a diversity of approaches and strategies among market players. Additionally, pro-competitive refusals to deal can stimulate a climate of healthy rivalry. For all these reasons, a nuanced approach is needed to help strike a balance between preventing anticompetitive behavior and recognizing the legitimate pro-competitive justifications that may underlie certain refusals to deal.

Although the Bill does not have a clear per se ban on self-preferencing, the unclear feature of its obligation relating to non-discrimination opens a wide window for interpretation that could dissuade businesses from enhancing and promoting their products, likely harming consumers. The goal is to help consumers and self-preferencing does that by definition. "Self-preferencing," though currently carrying a negative connotation, in

[17] *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919), The U.S. courts have acknowledged "the long recognized right [of even a monopolist] freely to exercise his own independent discretion as to parties with whom he will deal."

many cases reflects efficient behavior and organic vertical integration—prevalent business strategies across various industries. Given the importance of incremental innovation in driving growth,[18] the potential repercussions on economic efficiency and consumer benefits underscore the necessity for a more meticulously considered regulatory approach. Additionally, a universal ban on self-preferencing would discourage competitive market entry by limiting businesses' capacity to promote their own products. This approach could inadvertently hinder market dynamism and impede the positive effects of robust competition, therefore, it should be avoided. And finally, no one is forcing Brazilian consumers to consume the additional product or service of a digital company that chooses to preference their own. On two-sided markets platforms cater to both consumers and to producers. Consumers are inclined to leave if the platform fails to offer the diverse array of products and services they seek.

In sum, the obligations in Article 10 concerning refusals to deal and unclear rules on discrimination and self-preferencing appear likely to stifle legitimate practices and deter both established and emerging players from innovation.

RECOMMENDATIONS

For these reasons, ITIF has significant concerns about the Bill and offers the following recommendations:

- **Slow down:** Given the enormous implications of the DMA for Europe's digital economy, Brazil should put its own legislation on hold for at least until economists and other scholars can assess the impacts of the EU's DMA on EU consumers and the EU digital economy. Should the benefits outweigh the costs then Brazil should consider moving forward with its own legilation. But if the costs outweigh the benefits, it should not.
- **Reasses the justification for the Bill:** The size of the Brazilian market, coupled with its dynamic and innovative digital landscape, argues against immediate and extensive regulation. In the absence of clear market failures, the potential harm posed by regulation and its unintended consequences may outweigh the benefits, stifling the very innovation and entrepreneurship that are driving the country's economic resilience and digital transformation. As Brazil contemplates its digital future, a careful consideration of the inherent resilience of competitive dynamics is paramount to ensuring that regulatory measures align with the genuine economic needs and requirements of the burgeoning digital market.
- **Keep balance among regulatory agencies:** The Bill's decision to empower the Telecoms Agency, Anatel, to monitor and prosecute anticompetitive conduct raises concerns about regulatory fragmentation, overlapping regimes, and over-enforcement.
- **Focus application of the Bill as narrowly as possible:** The Bill adopts a broad approach of applying to all companies with annual gross revenues equal to or exceeding BRL 70 million in services provided to Brazilians. This seemingly indiscriminate definition not only targets major industry players but also casts a wide net, ensnaring smaller and medium-sized enterprises and startups. The

[18] The Aggregate Implications of Innovative Investment in the Garcia-Macia, Hsieh, and Klenow Model, AtkesonBurstein.pdf (umn.edu).

flawed approach risks placing an undue burden on smaller, aspiring businesses seeking to enter the market.

- **Reconsider the Article 10 Obligations**: Equally perplexing is the Bill's inclination towards general obligations limiting refusals to deal and self-preferencing. Such a blanket approach fails to account for the diverse nature of digital platforms, potentially stifling innovation and limiting the platforms' ability to optimize user experience and functionality.

CONCLUSION

The Brazilian legislative proposal, mirroring the European legislation on digital markets, signals a pivotal moment for the Brazilian nation's approach to regulating the emerging digital platform market. However, the EU's DMA has just recently became applicable in May 2023, and we do not yet know the practical consequences of the regulation. As Brazil is working on its own DMA, it should at minimum must be acutely aware of the potential problems and unproven benefits of sweeping economic regulation digital markets.

Thank you for your consideration.

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