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**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

**LATIN AMERICAN AND CARIBBEAN COMPETITION FORUM
Session I: Disruptive innovation in Latin America and the Caribbean:
Competition enforcement challenges and advocacy opportunities**

-- Call for Country Contributions --

12-13 April 2016, Mexico City, Mexico

The attached document is circulated in preparation for the discussion under Session I of the Latin American and Caribbean Competition Forum at its forthcoming meeting to be held on 12-13 April 2016 in Mexico. Delegates are requested to send written contributions for that session to the Secretariat by 11 March 2016 at the latest. Advance notice of contributions by Monday 15 February 2016 would be useful.

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LATIN AMERICAN AND CARIBBEAN COMPETITION FORUM



**14th Latin American and Caribbean Competition Forum
12-13 APRIL 2016, Mexico City, Mexico**

Session I

**Disruptive innovation in Latin America and the Caribbean:
Competition enforcement challenges and advocacy opportunities**

CALL FOR COUNTRY CONTRIBUTIONS

Introduction

1. This request for contributions is circulated in preparation for the discussions to be held at the 2016 Latin American Competition Forum on the topic of **“Disruptive Innovation in Latin America and the Caribbean: Competition Enforcement Challenges and Advocacy Opportunities”**. You are invited to make a written contribution this session.
2. In this call for contributions we aim to identify some topics that you may wish to address in your written and oral contributions. Please note that this list is neither prescriptive nor exhaustive.
3. To assist the OECD Secretariat in planning the session, please inform us by **15 February 2016** if you intend to submit a contribution. The contributions themselves should be sent by email (as a Word document in electronic format, 5 pages maximum in Spanish or English) to Angélique Servin [Angelique.Servin@oecd.org] and copied to: Lynn Robertson [Lynn.Robertson@oecd.org] by **11 March 2016 at the latest**. Country contributions will be circulated to participants through the LACCF website (www.oecd.org/competition/latinamerica and <http://laccf2016mexico.com/en/home-2/>).

Background

4. Disruptive innovations are new products, processes or business models that drastically alter markets in unexpected ways. They contrast with incremental or predictable improvements that leave the structure of markets intact. Disruptions often come from smaller firms (including new entrants) and, particularly in the case of internet or mobile technologies, scale up quickly at the expense of entrenched incumbents. While there is disagreement among theorists about the precise mechanism through which disruptive innovations influence markets and which recent innovations qualify as disruptive,¹ it is clear that technology-enabled innovations will continue to have fundamental impacts on market structure in the years ahead.

5. The Latin America and the Caribbean region is no exception to this trend, and has in recent years seen rapid market change spurred by web- and mobile-based innovations. These include services offered by large players from outside the region, such as Uber and Airbnb, as well as locally-developed and rapidly growing businesses such as Movilway and Easy Taxi. Several recent innovations in the financial services sector have targeted under-served segments of markets, including individuals without bank accounts, credit ratings or payment cards.

6. In this context, competition authorities face two significant challenges: applying competition laws to markets whose definition is made difficult by disruptive innovation, and advocating for competition in an atmosphere of significant controversy.

Enforcement Challenges

7. The definition of markets undergoing disruption by technology-enabled innovation presents competition authorities with several challenges. Rapid changes to, and blurring lines between, product and service offerings mean authorities risk defining a market that is too narrow, therefore reaching enforcement decisions that misunderstand markets and potentially hamper innovation. In other words, it is challenging for competition authorities to assess product substitution in fast-changing markets when applying traditional tools such as SSNIP² tests. This risk was famously illustrated by the determination of Clayton Christensen (who first coined the term ‘disruptive innovation’) that the iPhone would not be a successful disruptor in the mobile phone industry. He later acknowledged a mistake in market definition, stating that the iPhone was in fact disruptive to the laptop market.³

8. Two-sided markets also present an enduring challenge for competition authorities as the development of digital platforms continues apace. SSNIP tests and other traditional analyses must take into account the dynamic interaction of both sides of the market rather than considering each side separately. For instance, authorities should recognize that increases in listing prices on online product sales platforms

¹ Clayton Christensen, who first developed the term disruptive innovation, posits that disruptive innovations are those which either create a new market or enter a market at the low-end (the “overlooked segments” – (Christensen et al, 2015)), at a point where incumbents’ consumers would find the quality of the disruptive product to be inferior to what they are currently consuming. As such, incumbents would ignore the low end of the market, until disruptors improve their offering and begin capturing incumbent market share, at which point Christensen believes it is too late. In a recent paper, he argues that Uber cannot be considered to be disruptive because it cannot be said to be providing a lower quality service (Christensen et al, 2015). Some have disagreed with this model – specifically the focus on the low-end of the market and its application to recent innovations such as the iPhone (Lepore, 2014; Gans, 2015, Thompson, 2013).

² SSNIP is the abbreviation for: small but significant and non-transitory increase in price.

³ <http://www.bloomberg.com/bw/articles/2014-06-20/clayton-christensen-responds-to-new-yorker-takedown-of-disruptive-innovation#p3>.

could, by causing a reduction in listings, reduce the demand among users of the platform, meaning that both sides of the market would be impacted (see, for instance, Haucap and Stühmeier, 2015).

9. Other enforcement challenges for competition authorities in markets disrupted by innovation include the assessment of mergers justified by the presence of a disruptive entrant (the “but Amazon” defence), the use of most-favoured nation clauses by online platforms and the definition of markets for data, given data do not generally have supply and demand in a traditional sense (Graef, 2015). Finally, anticompetitive behaviour of incumbents to maintain market share in the wake of disruptive innovations will require continued enforcement using more traditional tools, such as CADE’s investigation in Brazil of the conduct of taxi drivers with respect to Uber.

Advocacy Opportunities

10. The change brought by disruptive innovations has not been universally welcomed. Incumbents have, particularly in the case of innovations affecting regulated industries, expressed opposition to disruptive business models and issued calls for regulating disruptive entrants. Sector regulators have examined extending current regimes to entrants offering disruptive innovations, or preventing them from entering the market. As such, there is a crucial role for competition authorities to ensure that the benefits of competition are considered in any effort to regulate or inhibit new market entry by innovative firms.

11. Traditional advocacy, supported by market studies, is ongoing in Latin America and the Caribbean, as demonstrated for instance by COFECE’s recent study which produced recommendations in favour of the legal recognition of Uber. The rapid pace of market development may, however, require competition authorities’ proactive involvement at the early stages of an innovation’s entry into markets. Proposals on this subject include those advocating for competition authorities to play a facilitating role in engagement between regulators and disruptive entrants (Fingleton, 2013), and enhanced market monitoring before and after undertaking market studies (Evans, 2014).

12. Such efforts are inherently challenging due to the difficulty of identifying whether innovations in their early stages are disruptive, rather than incremental improvements or services targeted at new segments unlikely to impact existing markets. To this end, Evans (2014) has called for the creation of “red flag disruption units” within competition authorities to enhance market intelligence. A clear understanding of the characteristics that make markets vulnerable to disruption could also facilitate these efforts.

Background Paper and Discussion Topics

13. The Secretariat’s Background Paper, which will be distributed shortly, can be used as a starting point for discussions in this session. The Annex identifies a number of relevant topics for discussion.

ANNEX. QUESTIONS FOR CONSIDERATION IN COUNTRY CONTRIBUTIONS

1. On disruptive innovations in Latin America and the Caribbean:
 - What recent innovations have been introduced in your jurisdiction that have disrupted, or have the potential to disrupt, existing markets?
 - How have incumbents reacted to these innovations? Have they engaged in anti-competitive conduct?
 - If the innovations took place in regulated industries, how did the regulator(s) respond?
 - Are there any unique characteristics of these innovations relative to disruptive innovations occurring in, or developed in, other regions of the world?
2. On market definition issues in innovation-driven markets:
 - Has your authority encountered challenges with respect to market definition in an innovation-driven market, including (i) rapidly evolving or disappearing boundaries between markets; or, (ii) highly customized products?
 - Has your authority seen the emergence of online platforms being used to justify mergers of “bricks and mortar” retailers (the “but Amazon” defence)? How did it respond?
3. On two-sided markets:
 - Has your authority adapted traditional market assessment tools to consider two-sided markets?
 - If so, has this approach led to different decisions than would have been made by considering each side of the market separately?
4. On competition authority engagement in industries facing potential disruption:
 - How can competition authorities identify disruptive innovations at an early stage in order to encourage engagement with regulators and monitor potential incumbent anti-competitive behaviour?
 - Other than through market studies and providing comment to regulators through formal processes, are there any opportunities for competition authorities to foster engagement between regulators and disruptors?
 - Given the unique characteristics of innovations identified in (1) (if any), how should competition advocacy efforts be tailored to Latin American and Caribbean markets?

SUGGESTED READING LIST

- Cortez, N. (2014), “Regulating Disruptive Innovation”, Berkeley Technology Law Journal, Vol. 29:175, <http://dx.doi.org/10.2139/ssrn.2436065>.
- Evans, D. and E. Mariscal, “Market Definition Analysis in Latin America with Applications to Internet-Based Industries”, *I/S: A Journal of Law and Policy*, Vol. 9:3, <http://moritzlaw.osu.edu/students/groups/is/files/2014/03/Evans-Mariscal.pdf>.
- Evans, P. (February 7, 2014), “Disruptive Competition Part 2: What Role for Regulators and Competition Policy?”, judoeconomics blog, <https://judoeconomics.wordpress.com/2014/02/07/disruptive-competition-part-2-what-role-for-regulators-and-competition-policy/>.
- Fingleton, J. (2013), *Disruptive Entry and Regulation in Financial Services*, Fingleton Associates, <http://www.fingletonassociates.com/speeches/disruptive-entry-and-regulation-in-financial-services/>.
- Graef, I. (2015), “Market Definition and Market Power in Data: The Case of Online Platforms”, *World Competition*, Issue 4, pp. 473–505, <http://www.kluwerlawonline.com/abstract.php?area=Journals&id=WOCO2015040>.
- Haucap, J. and T. Stühmeier (2015), “Competition and antitrust in internet markets”, *DICE Discussion Paper*, No. 199, <http://hdl.handle.net/10419/121420>.
- OECD Competition Committee Roundtable discussions (all available at <http://www.oecd.org/daf/competition/roundtables.htm>)
- Disruptive innovations and their effect on competition (2015)
 - Market definition (2012)
 - Market studies (2008)
- United Kingdom Competition Commission (2008), *Game Group PLC and Games Station Limited: A report on the completed acquisition by Game Group PLC of Games Station Limited*, London, http://webarchive.nationalarchives.gov.uk/20140402141250/http://www.competition-commission.org.uk/assets/competitioncommission/docs/pdf/non-inquiry/rep_pub/reports/2008/fulltext/536.pdf.