

VoxEU - Designing regulation for digital platforms: Why economists need to work on business models

There is a developed public discourse on the need for more enforcement, regulation and legislation of digital platforms. This article asks how economists can contribute to developing the debate on designing regulation for digital platforms, writes Cristina Caffarra, Federico Etro, Oliver Latham, Fiona Scott Morton for VoxEU



Where are we today on digital platform competition?

A lot of work has been done over the past two years on laying out systematic foundations for our understanding of some key characteristics of large digital platforms.

One area where issues are well understood is dynamic competition *for* the platform. From the original network effects models of the 1980s to the Microsoft era, we have theories (most notably, Carlton and Waldman 2002 and Choi and Stefanidis 2001) which rationalise why a platform might want to undermine certain complementary services because they constitute potential dynamic threats to the platform's core monopoly. These models rationalise well the historic Microsoft cases and subsequent enforcement against Google in Europe. Further literature (Choi and Jeon 2020, Etro and Caffarra 2017) also helped us understand how pricing constraints – e.g. the need to set a zero price on certain consumer-facing services – can generate inefficiencies which incentivise colonisation of adjacent markets on the part of platforms.

But there are gaps in our understanding on how platforms behave and what this means for welfare.

The main issue to be cracked for the forthcoming major regulatory effort in Europe is competition on the platform. How does the owner of a proprietary platform set the 'rules of the game' for third parties that operate and create joint value on their ecosystem? What about cases where the platform owner also supplies services in competition with these third parties? While control by the platform owner might generate efficiencies (e.g. if it internalises negative spillover effects on its quality, for example, in a way that other platform participants do not), it is also right to worry about harmful effects. This 'dual role' has come under major scrutiny in Europe, with investigations inter alia into the commissions Apple sets for in-app purchases of digital goods and the operation of Amazon's online marketplace.

A key quote from the article:

The research we have briefly mentioned here suggests that business models matter fundamentally when one is evaluating the dual role of platform owners as umpires and players in their ecosystem. At a general level, platforms that monetise on the consumer side (through the sale of a product, or consumer-side commissions on transactions) are those that best internalise the interest of consumers in their interactions with third-party players, relative to ad-funded platforms. [...]

We need a better understanding of the magnitude of the problems businesses are respectively trying to solve; how the different players respond to changes in prices or rules; how consumers differ and how many are of which type; how to measure overall welfare effects, not just partial analyses; and therefore how to determine which model best fits the data and which factors are most important.

For economists, what other models do we need? Do we have models that describe these situations well? What insights and empirical predictions can be drawn?

The full original article first appeared on VoxEU [here](#) on the 4 June, 2020.

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