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The *Android* effect

New Google decision, new record fine

by **Alec Burnside** and **Maria Loudjeva**

On 18 July 2018, following a 39-month investigation, the European Commission announced its decision in the *Android* case, imposing a record fine of €4.34bn and requiring Google to cease its infringing practices.[1] The Commission faulted Google for imposing illegal restrictions on Android device manufacturers and mobile network operators, designed to cement Google's dominance in general internet search. The abuses ran from 2011, and Google must now "cease and desist" within three months.

While the fine attracted significant media attention, and the decision sparked political reactions, €4.34bn represents just over two weeks of revenue for Google, and its stock price was not impacted. The greater impact should in theory flow from changes in the marketplace once Google ceases the foreclosing conduct that has fuelled its biggest growth engine: mobile phones. The hovering question, however, is whether it is too late for a flowering of the rival operating systems and competing search engines that Google has foreclosed: has the market tipped beyond retrieval?

Background

Android is a mobile operating system based on open source software and designed primarily for touchscreen mobile devices such as smartphones and tablets. The system was first launched in 2003 but its original developer was bought by Google in 2005. The Android operating system is distributed to device manufacturers free of charge.

The Commission launched an informal investigation in April 2013 following the receipt of a formal complaint by FairSearch, a group of companies then including Microsoft, Oracle and Foundem. Additional complaints were filed in 2014 by Aptoide, in 2015 by Disconnect Inc and Yandex, and in 2016 by the Open Internet Project. The formal proceedings, however, were opened in April 2015 citing concerns about Google's conduct as regards the Android operating system and applications. The *Android* investigation, although substantively distinct, forms part of a wider probe into Google's conduct in the EEA, including the favourable treatment by Google in its general search results of its own other specialised search services, and concerns with regard to copying of rivals' web content, advertising exclusivity and undue restrictions on advertisers.

At the time of writing the Commission's full decision has yet to be published, and so this comment is based on its press release.

Android's dominance

The Commission found Google to be dominant in the markets for:

1. ***General internet search services*** – mirroring its conclusions on dominance in the Google *Shopping* decision (not contested by Google in its grounds of appeal[2]) the Commission found that Google's market share exceeds 90% in most of the EEA member states;
2. ***Licensable smart mobile operating systems*** – through Android, Google was found to be dominant on the worldwide (excluding China) market for licensable smart mobile operating systems with a market share over 95%; and
3. ***App stores for the Android mobile operating system*** – Google's Play Store was found to account for more than 90% of the apps downloaded on Android devices.

Following the announcement of the decision, one of the most articulated critiques has been against the Commission's finding that other operating systems, notably Apple iOS, are not part of the same market as Android. The Commission took this view on the basis that iOS is not available for license by third-party original equipment manufacturers (OEMs), whereas the argument from the Google camp was that consumers choose between Android and Apple devices. But the customer for this purpose is logically not the end-purchaser, but rather the OEM. And, indeed, the OEMs do not have the option to install iOS or Blackberry; their alternative was, rather, Windows Mobile (which exited the market last year).

The Commission recognised the competition between Apple and Android devices at the level of the consumer, but

did not judge such competition to be sufficient to constrain Google at the upstream manufacturer level. In addition, the Commission found that switching costs for end-consumers are high between Apple and Android devices, inter alia, because data on Android devices is difficult to transfer onto an iPhone, and because of the much higher prices that Apple charges for its smartphones.

The abusive conduct

The Commission's finding of infringing conduct is based on a well-established legal theory – a classic tying/leveraging. By using its dominant position in Google Play (ie, in the market for app stores for the Android mobile operating system) to ensure that Google Search becomes the default search engine on more than 80% of all devices worldwide (excluding China), Google limited the scope for rival search engines to enter the market. The difference from *Shopping* will be noted: in that case the dominance in general search was the platform for abuse intended to extend Google's position in other markets. Here it was dominance in app stores which served to promote Google's interests in general search.

Google's infringement of Article 102 TFEU was facilitated through three specific types of restrictions which Google imposed on manufacturers and mobile network operators. According to the Commission, Google anticipated the shift from desktop to mobile search and adapted its practices with a view to avoiding the diversion of traffic flow away from its search engine. Currently about two-thirds of Google's total advertising revenue comes from mobile ads; and mobile internet makes up more than half of global internet traffic.

Notwithstanding the difference identified as to the dominance which was being abused (as compared to *Shopping*), and although the abusive conduct was different, there is a unifying objective: Google seeking to protect and extend its vast volume of data which it monetizes by way of selling targeted advertising. In *Android*, Google pursued its objective by forcing bundles of Google apps onto OEMs and effectively preventing them from promoting a competing operating system. In *Shopping* the Commission concluded that Google, through its dominant general search engine, artificially favoured its own specialised search service in order to ensure that data on "purchasing intent" is not diverted from its search engine. In the end both practices were aimed at keeping control of access to user data.

First abusive practice: Tying Google Play to an obligation to pre-install Google Chrome and the Google Search app

The Commission found that Google abused its dominant position by making the licensing of Google Play dependent on the pre-installation of its mobile apps and services. Tying is specifically mentioned in Article 102(d) TFEU as "*making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts*". In addition, tying may be abusive beyond these circumstances. For example, a tying practice could be found abusive even when there is a natural link between the two products[3] or when the tying is in accordance with commercial usage.[4]

The Commission found the following practices by Google to constitute illegal tying to the licensing of Google Play:

1. ***The tying of the Google Search app*** – as a result, Google has ensured that its Google Search app is pre-installed on practically all Android devices sold in the EEA.
2. ***The tying of the Google Chrome browser*** – as a result, Google has ensured that its mobile browser is pre-installed on practically all Android devices sold in the EEA. Browsers also represent an important entry point for search queries on mobile devices, and Google Search is the default search engine on Google Chrome.

As the first two abusive practices identified by the Commission refer to tying, it is worth keeping in mind the established criteria for treating a tie as abusive, when considering the Commission's findings.

There are four conditions for a tying to be found abusive: [5]

(a) the tying and tied goods are two separate products;
(b) the undertaking concerned is dominant in the tying product market;
(c) the undertaking concerned does not give customers a choice to obtain the tying product without the tied product; and
(d) the tying is liable to foreclose competition.

Assessing each of the criteria in turn, there seems to be no reasonable objection to the conclusion that Google Play, Google Chrome and Google Search are all different products. As noted above, Google Play accounts for more than 90% of all apps downloaded on Android devices; and the Commission's press release indicates that device manufacturers confirmed Google Play to have become a must-have app, ie one which users expect to find pre-installed on their devices. That being so, customers inevitably found Google Chrome and Search pre-installed as well. Google's behaviour had thus reduced the incentives of manufacturers to pre-install competing search and browser apps, as well as the incentives of users to download such apps. This reduced the ability of rivals to compete effectively with Google and acted to foreclose competition on the merits.

In its defence, Google argued that tying Google Search and Chrome was necessary to allow it to monetize its investment in Android. The Commission dismissed this argument, stating that Google is already collecting vast amounts of valuable data through the Google Play Store alone, making it unnecessary to impose restrictions on OEMs.

Although the full decision, with the evidence relied on and a detailed assessment, has not yet been published, the regulator has almost certainly followed the case of *Microsoft*[6] with respect to the tying branch of the abuse. Microsoft was abusing its dominant position by tying its Windows Media Player to its Windows Operating System. The irony is that Google was one of the complainants in another competition case where Microsoft was accused of tying its web browser, Internet Explorer, to Windows. Eventually Microsoft settled the case with the Commission by committing to allow computer manufacturers and users to turn Internet Explorer off and to offer Windows users unbiased choice among different web browsers by means of a browser choice screen.[7] As previously mentioned, in its *Android* decision the Commission has followed clear precedent in its choice of legal theory.

Second abusive practice: Tying Google's proprietary apps to an obligation not to pre-install any alternative version of Android

The second abusive practice adopted by Google is covered by the same legal principles as the first, ie making the conclusion of contracts subject to an unwarranted supplementary obligation: as a condition of licensing Google Play, OEMs had to commit not to be involved with devices running rival versions of Android.

When Google develops a new version of Android it publishes the source code online. According to the Commission press release, this allows third parties to download and modify the code and create so-called Android forks. However, in order to be able to pre-install Google's proprietary apps, including the Play Store and Google Search, on their devices manufacturers had to commit not to develop or sell even a single device running on any alternative version of Android that was not approved by Google. According to the Commission, its investigation showed that Google's conduct notably prevented large manufacturers from developing and offering devices operating with Amazon's Android fork system, "Fire OS".

Third abusive practice: Granting revenue share payments conditional on Google Search being the only pre-installed search engine on Android devices

Between 2011 and 2014, Google granted significant financial incentives to some of the largest OEMs as well as mobile network operators on condition that they exclusively pre-installed Google Search on their Android devices. The effect on competition naturally was to foreclose distribution of competing search apps.

According to the press release, the Commission's analysis showed that a rival search engine would not have been in a position to compensate an OEM or a mobile network operator for the loss of the revenue share payments from Google and still make profit.

Again there is nothing novel in the theory of harm here and a good precedent on which the Commission is likely to have relied is the case of *Intel*[8]. In 2009 Intel was found in breach of Article 102 for paying a computer retailer in exchange for it not selling computers incorporating its competitor AMD's chips. In addition, Intel was paying computer manufacturers in exchange for delaying the launch of computers with competing AMD chips. After lengthy court battles the Court of Justice returned the *Intel* decision to the lower court but for an unconnected reason (because of the General Court's failure to review the Commission's application of the "as efficient competitor" test) without suggestion that the theory of harm or the legal basis were at fault.

The significance of pre-installation

Since pre-installation appears as the common theme among Google's abusive practices, it is important to address its significance. Some critiques of the Commission decision argue that just because a Google app is pre-installed or set as a default does not mean that consumers must choose to use that app and thus generate revenue and traffic for Google. In its familiar catechism, Google asserts that competition is "one-click away" and that downloading another app takes seconds, very different nowadays compared to the era of Microsoft's antitrust struggles. The Commission, on the contrary, has stated in its press release that pre-installation creates a "status quo bias". We await the full decision for details of the empirical analysis of how default status influences user behaviour, but there was something of a preview in the press release which explained that on Android devices (with Google Search and Chrome pre-installed) more than 95% of all search queries were made via Google Search, ie less than 5% of the users downloaded competing apps. Perhaps a truer indication of the importance that Google attaches to pre-installation is to be found in its choosing to pay $3bn to Apple in 2017 in return for Google Chrome being the default search engine on the iPhone[9] – this being only the latest of such payments, dating back to 2014.

The pre-installation of Google's apps, according to the Commission, reduced the incentives of OEMs to pre-install competing search and browser apps, as well as the incentives of users to download such apps. Critics of the Commission decision argue that the obligations to pre-install the Google apps are irrelevant as OEMs would in any case have chosen to set the Google apps as defaults on their devices. However, the fundamental question is surely not whether OEMs would have in any case chosen Google's apps but that such choice should not have been influenced by (a) the bundling of Google's proprietary apps being a pre-condition for getting the must-have Google Play, and/or (b) financial incentives in exchange for exclusivity.

The remedy

Naturally the most eye-catching element of the *Android* decision is the record-high fine. The bigger question, however,

is what Google will do to address the concerns raised in the Commission decision and to bring the anticompetitive conduct to an end. Despite Google's intention to appeal the decision, it now must comply with the Commission's cease-and-desist order within a 90-day deadline or face penalty payments of up to 5% of the average daily worldwide turnover of the combined Alphabet group. Compliance, at a superficial level, is much simpler than in *Shopping*, where Google needed to come forward with a solution. In *Android* the Commission tells Google to end the tying of apps, end the prohibition of Android forks and remove any financial incentives tied to Google apps exclusivity. So Google should simply strike the offending clauses from new contracts, and no doubt inform its universe of contractual partners that they are not bound by any existing clauses.

Experience tells us, however, that Google will look for a minimalist form of compliance – as it did in *Shopping*, which has produced not the slightest ripple effect into Google's preferencing in other areas of specialised search. At least Google is enjoined not to replace the offending clauses with other measures of equivalent effect.

The bigger question, however, is whether Google has been able, during the long delay in bringing the case to decision, to entrench itself so effectively that it can relax these clauses without feeling any effect. So, for example, Amazon – a sometime would-be entrant into smartphones, with a plan to use open source Android – has already declared that it will not now renew the effort.

Early commentary speculated that unbundling Google Play Store, Google Search App and Google Chrome will disrupt Google's main revenue flow, ie the advertising revenue coming from Google Search. This could mean that Google might start charging for the use of Android software (with critics of the decision arguing that this would be to the detriment of the consumer). But Google has been quick to announce that it will ensure continued availability of Android. Android is the conduit for the flow of user data back to Google which fuels its income stream, so Google is hardly likely to want to make it less attractive. Of course the notion that Android is "free" is a relative thing: free in a monetary sense, but users pay with their personal data. Data attracts advertisers, advertisers pay for access to the user. So the more data Google collects through its search engine, the more income it will generate.

Albeit an extreme solution, a potential remedy could be breaking Google up. Such a possibility has been voiced by DG Competition's own chief economist, Tommaso Valletti, who mused out loud, before the decision was taken, that a break-up might ultimately be the way forward. The power to impose structural measures is available, if there is no less intrusive way of achieving what needs to be done.[10]

Or, short of enforcing a change of ownership, there is precedent for separations within a continuing single ownership (think gas and electricity) – so-called "legal unbundling". But the approach is challenging, because the incentives for self-favouring remain unaffected. Witness the ineffectiveness of the *Shopping* remedy, where Google is consistently the highest bidder in the auction it has instituted – then of course simply transferring the auction price from one pocket to another.

Conclusion

Important as it is, the *Android* decision is no more than a staging post in the Commission's long struggles with Google. An appeal is anticipated, while the *Shopping* appeal is barely advanced. The next stage in the struggles will likely be the Commission's assessment of Google's *Shopping* remedies, to be expected in the next months, with the possibility of significant further fines.

While Google has already been a defining feature of Commissioner Vestager's term in office, with a year to go in her mandate the full story is not yet told. Indeed there are many pending complaints not yet addressed. The views of the General Court are on the other hand unlikely to materialise within that period. Ultimately they will provide valuable confirmation of how the law should be applied in a new market economy where price is not the driving factor.

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Endnotes

1. Commission Press Release, "Antitrust: Commission fines Google €4.34 billion for illegal practices regarding Android mobile devices to strengthen dominance of Google's search engine", 18 July 2018.
2. Official Journal notice of appeal in Case T-612/17 *Google and Alphabet v Commission* [2017] OJ C 369/37, 30.10.2017.
3. Case C-333/94 P Tetra Pak II (n 3), para 37.
4. Case T-83/91 Tetra Pak II (n 39), para 137.
5. Case COMP/C-3/37.792 Microsoft.
6. Case COMP/C-3/37.792 Microsoft.
7. Case COMP/C-3/39.530 – Microsoft (tying).
8. Case COMP 37.990 Intel.
9. https://www.cnbc.com/2017/08/14/google-paying-apple-3-billion-to-remain-default-search--bernstein.html
10. Article 7(1), Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in art 81 and 82 of the Treaty.