



# New CMA Guidance on the Digital Markets Regime published for consultation

The Digital Markets, Competition and Consumers Act 2024 received Royal Assent on 24 May 2024. This article considers who will be impacted by the new digital markets regime, the requirements it will introduce, and how it may be enforced, and summarises the CMA's new draft guidance under consultation on how it intends to implement the regime in practice.

## DMCCA enacted

The Digital Markets, Competition and Consumers Act 2024 (**DMCCA**) completed its legislative journey on 24 May 2024 and received Royal Assent.

The passing of the DMCCA into law aims to address the evolving landscape of digital markets and the status of large digital companies, representing a significant milestone in the regulation of competition and digital markets. In seeking to achieve its aims, the DMCCA has created a comprehensive legislative framework for the regulation of digital markets and has introduced wide ranging powers for the Competition and Markets Authority (**CMA**) to enforce consumer protection law.

In this article we consider who will be impacted by the new digital markets regime, the requirements it will introduce, and how it may be enforced, and summarise the CMA's new draft guidance under consultation<sup>1</sup> on how it intends to implement the regime in practice.

## Which firms may face SMS designation?

The DMCCA will have the most impact on large digital firms designated with "Strategic Market Status" (**SMS**). There are a series of thresholds that will be considered by the CMA before a firm is designated with SMS. The following conditions must be met:

### Authors

**Tom McQuail**  
Partner

**David Cran**  
Partner

**Melanie Musgrave**  
of Counsel

**Leonia Chesterfield**  
of Counsel

**Ben Powell**  
Associate

<sup>1</sup> Consultation on new digital markets competition guidance: <https://connect.cma.gov.uk/cma-new-digital-markets-regime>

- *Digital activity*: the firm carries out a digital activity, such as the provision of services on the internet or digital content (including services provided free of charge).
- *Link to the UK*: the digital activity must be linked to the UK. For instance, it has a significant number of UK users, carries on business in the UK, or carries on digital activity that may impact trade in the UK.
- *Turnover condition*: the firm must have a minimum global turnover of £25b or a total UK turnover exceeding £1b.
- *Market power*: the firm must have substantial and entrenched market power (to be assessed by reference to what the firm could do over the next five years if it were not designated as an SMS).
- *Strategic significance*: the firm must also have a position of strategic significance in that its digital activity either:
  - is significant in size or scale
  - is used as a service by a significant number of other firms
  - places it in a position to extend its market power to other activities, or
  - allows it to influence the conduct of other firms.

The CMA draft guidance provides a steer on how each of the above thresholds will be assessed in practice. We set out the key points the CMA will take into account when assessing these thresholds below.

### Digital activity

- One firm may be subject to multiple SMS designations in respect of distinct digital activities.
- Digital activities may be grouped where they have substantially the same or similar purposes
- The assessment and identification of digital activity will be case-specific.

### Link to the United Kingdom

- There is no quantitative threshold for how many users constitutes “significant” users.
- Indirect provision of services and the provision of services through agents or subsidiaries will be captured for the purposes of this criterion.
- Conduct relating to digital activity occurring outside of the UK which could foreseeably impact UK trade may also satisfy this criterion.

### Turnover

- Turnover may include revenue generated by non-digital activities.
- Turnover of the whole corporate group will be considered.
- The CMA’s starting point for assessing turnover will be the group’s latest accounts, and where these are not available (or where data is not clear) the CMA may use its investigatory powers to obtain relevant data.

### Substantial and entrenched market power

- The CMA will consider available alternatives and possibilities for entry and expansion in assessing market power though it will not be required to define a market.
- A firm’s market power would need to be sustained over a substantive period.
- Substantial and entrenched market power is a distinct legal concept from that of “dominance” used in competition law and so will not be assessed by reference to existing case law.

- Where the CMA has found evidence that a firm has substantial market power at the time of the SMS investigation, this will generally support a finding that market power is entrenched, where there is no clear and convincing evidence that relevant developments will be likely to dissipate the firm's market power in the next five years.

### Strategic significance

- There is no quantitative threshold for when size or scale of the potential SMS firm can be considered as significant nor one specific metric which the CMA will use for all assessments.
- There is no quantitative threshold for when the number of other firms using the SMS firm's digital services to carry on their business can be considered as significant.
- The SMS firm's ability to extend its market power will be assessed by reference to its past activity, whether its service impacts other firms' ability to compete, and whether the SMS firm's digital activities make it easier for it to expand into other areas.
- Examples of a firm's ability to influence other firms could include offering interrelated products or offering a platform that includes content moderation services.

### The CMA's approach to SMS designation

- The CMA will provide (and publish) an investigation notice once it begins investigating possible SMS designation.
- The investigation will have a nine-month deadline commencing from the date the notice is provided to the SMS firm (though this deadline may be extended).
- The prospective SMS firm will be invited to respond during the investigation and, at the outset, the CMA will issue an invitation to comment for third parties to make submissions.
- The CMA will publish its proposed decision and invite further consultation.
- The CMA will provide an "SMS decision notice" including the reasoning for its decision (though may close an investigation before making a decision to designate).
- The designation will take effect for five years beginning from the day after the notice is provided.
- Before the end of the five years the designation will be reviewed (and in some cases the CMA may bring forward the re-assessment process).

Given the flexibility of the above thresholds, any firm providing services in the UK digital markets sector and generating revenues exceeding the relevant amounts could potentially satisfy SMS designation requirements, although it is understood that the intention is only the most substantial digital firms will be in scope. For those firms facing SMS designation, market power and strategic significance may become key points of contention in the designation process given the subjectivity of the criteria tied to those thresholds.

## Consequences of designation

SMS designation is the gateway into the digital markets regime. Once a firm is designated with SMS, it may be subject to bespoke conduct requirements and pro-competition interventions. It will also face a mandatory merger reporting requirement. We summarise the key ways in which these new requirements are expected to impact SMS firms below.

### Conduct Requirements (CRs)

The CMA's stated aim with CRs is to "address not only existing issues in relation to a relevant digital activity, but also protect against the risk that the firm seeks to take advantage of its substantial and entrenched market power in respect of that digital activity and position of

*strategic significance in ways that could exploit consumers and businesses or undermine fair competition*". To achieve this aim, the CMA's Digital Markets Unit (**DMU**) will have authority to enforce customised CRs where the DMU considers that the requirement is proportionate and would promote fair dealing (e.g. reasonable terms), open choices (e.g. ease of switching providers), or trust and transparency (e.g. providing sufficient information for informed decisions).

The types of CRs permitted by the DMCCA are expansive and can be amended by the Secretary of State as necessary, empowering the CMA to impose CRs in most (if not all) digital market areas. Whilst the DMCCA provides that SMS will be designated in relation to specific digital activities, the CMA may also impose CRs relating to conduct outside of the digital activity in relation to which the SMS has received designation. Consequently, a firm with substantive influence in one sector of the digital market could be subject to CRs in relation to other sectors of the digital market that it does not currently have a presence in. The CMA draft guidance notes that in carrying out its assessment of when CRs of this nature may be appropriate, the CMA will consider whether the firm's expansion into the new digital activity will increase its substantial and entrenched market power or strengthen its strategic significance.

The CMA draft guidance notes that when considering whether to impose a CR the CMA will consider the CR's objective, the type of CRs that would be most effective, and the proportionality of the CR. It also notes that the CMA will elect to impose the least onerous conduct requirement where multiple CRs could achieve the intended aim.

Once a CR has been imposed the CMA will monitor the SMS firm's compliance. CRs will generally apply until the end of the five-year designation period though if changes in the market render the CR inappropriate the CMA may conduct a public consultation and revoke the CR.

If there are reasonable grounds to suspect the CR has been breached during the designation period, the DMU will investigate the breach and notify the firm of any findings within six months and may issue enforcement orders if an adverse finding is made. Alternatively, the CMA may accept commitments from SMS firms to address the relevant competition issue, indicating that there may be room for SMS firms and the CMA to co-operatively identify the most efficient resolution to competition issues.

Overall, the DMCCA provides the CMA with significant flexibility over how CRs may be applied, and the draft guidance indicates that the CMA is prepared to impose expansive CRs to regulate digital markets.

### **Pro-Competitive Interventions (PCIs)**

The new regime also empowers the DMU to investigate factors adversely affecting competition and issue a PCI if an adverse effect on competition (**AEC**) is then found.

Once the CMA opens an AEC investigation and notifies the SMS firm, it will have nine months to reach a final decision on whether an AEC has been found, following which it will have four months to make a pro-competition order.

The draft guidance notes that in assessing an AEC the CMA will not be required to define a relevant market. The CMA will instead consider a broad range of matters in assessing whether a factor relating to digital activity prevents, restricts or distorts the market. This will include indicators such as the SMS firm's profits, competitive positions of rivals, barriers to entry into the market, and the ability of users to switch between alternatives.

If the CMA deems an intervention to be necessary it will assess the appropriate intervention by reference to the purpose of the PCI, what the most effective PCI may be, and the

proportionality of the PCI. PCI remedies can be structural or behavioural, and could include (non-exhaustively):

- General restrictions on conduct (e.g. prohibiting combination of user data).
- General obligations (e.g. making a service interoperable with a competitor's).
- Requirements to divest an aspect of the business.
- Supply and publication of information such as user data (including to competitors).

The DMCCA provides that the CMA must confirm a review date when issuing PCOs, but does not specify limitations on when the review date must be, leaving the length of PCI windows open to the CMA's discretion. The draft guidance is silent on this point, although it does discuss that PCIs may be imposed on a trial basis if it is feasible to do so and may provide valuable evidence of effectiveness.

As with CRs, the CMA draft guidance reiterates that PCIs will only be issued where proportionate and the CMA will seek to implement the least onerous PCI available. SMS firms may provide commitments as to future conduct in respect of an AEC, which may in certain circumstances satisfy the CMA's concerns (thereby providing the CMA with flexibility to conclude an investigation if an appropriate proposal is received). The CMA will consider scope, effectiveness, timeframe, and whether the SMS has offered to appoint a monitoring trustee before accepting a commitment.

The draft guidance notes that the CMA does not anticipate accepting commitments at a late stage of investigation and reiterates the requirement to publicly consult before accepting any commitment. As such, firms considering commitments after receiving a PCI notice should do so sooner rather than later.

### Merger reporting duties

SMS firms and (where it is part of a group, any member of that group) have a duty to report certain acquisitions of shares and/or voting rights in targets that have a UK nexus. This compulsory duty to report is novel as previously the UK merger regime has been voluntary, rather than mandatory.

The CMA has issued draft guidance on what amounts to a "reportable event"<sup>2</sup>, how a report should be submitted<sup>3</sup> and how the reporting requirements under the DMCCA will be enforced. It is worth noting that the duty to report is not limited to acquisitions related to a digital activity in respect of which an SMS firm is designated. It applies to all reportable events by SMS firms regardless of area of activity.

### Investigatory powers

The DMCCA grants the CMA comprehensive investigatory powers to administer and enforce the digital markets regime, including that the CMA may:

- Require parties to provide information such as documents and data relevant to an investigation.
- Access premises to supervise document collection processes.
- Require individuals to attend interviews.

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<sup>2</sup> A transaction may be subject to reporting requirements if it meets the relevant thresholds. It must result in 'qualifying status' (based on percentage of shares or voting rights the SMS firm will hold following the transaction); have a nexus to the UK; and meet the consideration value threshold.

<sup>3</sup> A proposed notice of information that should be included in a report has been issued as part of the CMA's consultation materials.

- Enter premises without warrant for the purposes of a breach investigation.

Two key points that SMS firms should take note of are that: the requirement to provide data could include requests for prior versions of algorithms; and the CMA may require firms to name a senior manager who is responsible for compliance with information requests.

## Enforcement

There are a range of competition requirements that the CMA may seek to enforce under the DMCCA including CRs, Interim Enforcement Orders (**IEOs**), Enforcement Orders (**EOs**), Final Offer Orders, Pro-Competition Orders (**PCOs**), Commitments, and Merger Reporting Requirements. The CMA will generally follow the procedure below:

- If the CMA considers a breach of a competition requirement may have occurred, it may conduct an initial assessment and invite comments on compliance from the SMS firm before launching a formal investigation (though it is not required to take this initial step).
- If the CMA has reasonable grounds to believe that a competition requirement has been breached, it may open an investigation.
- Once an investigation is opened, the CMA will specify a period for the SMS firm to make representations and invite representations from interested parties.
- The CMA will then make provisional findings and invite further representations. The CMA will also consider whether a financial penalty should be imposed for breach of the competition requirement and provide a provisional penalty notice (this decision may be influenced by whether the SMS firm has provided a commitment during the investigation).
- If the CMA concludes the investigation and identifies a breach, it may issue an EO imposing obligations to remedy the breach, require compliance with a PCO, or apply for a court order enforcing a commitment.
- Where appropriate the CMA may also instigate criminal prosecution against senior managers and/or seek a competition disqualification order against a director.

## Penalties for non-compliance

In addition to potential criminal prosecutions and enforcement orders, the CMA may seek to impose penalties on the SMS firm where non-compliance is “without reasonable excuse”. It is not yet certain what will constitute reasonable excuse; however the draft guidance notes that good commercial reasons for non-compliance is unlikely to constitute a reasonable excuse; and that the CMA is unlikely to accept an excuse where reasonable steps to comply have not been taken.

The draft guidance indicates that penalties are likely to be imposed where the CMA considers:

- there has been a serious, negligent, or intentional failure to comply
- the firm obtained a benefit from the failure
- there have been repeated failures, or
- there has been a delay in reporting the failure.

When considering how best to incentivise compliance, the CMA may elect to impose a daily penalty, fixed penalty, or both. Even if the failure has been remedied, the CMA may still impose a penalty to ensure deterrence from future breaches. The DMCCA provides that the CMA may impose penalties of up to 10% of the SMS firm’s group turnover, or 5% of the total daily turnover. The level of quantum will be assessed via the following steps:

- Assessment of turnover generated in the UK and the seriousness of the failure (factors impacting seriousness may be the nature of the failure, duration, benefits gained, or harm caused <sup>4</sup>).
- Adjustment for deterrence (penalties may be increased to ensure they substantively exceed any profits gained to ensure it is not beneficial to breach competition requirements).
- Adjustment for aggravating factors (such as attempts to frustrate enforcement, involvement of senior management, concealment, retaliatory measures taken, or repeated failures).
- Proportionality assessment (to ensure the penalty does not exceed the statutory maximum).

Once a decision is made on quantum, the CMA will issue a final penalty notice setting out the details of the penalty and a date for payment. SMS firms will be able to appeal penalties or the quantum imposed via the CAT, which will no doubt lead to hotly contested legal disputes in due course.

### Next steps

The powers granted to the CMA under the DMCCA are extremely broad and represent a significant milestone in the regulation of digital markets and competition in the UK.

The CMA's draft guidance provides useful insights into how the CMA may exercise its powers and is due to be finalised after a consultation process ending on 12 July 2024. The new powers are expected to come into effect in October 2024. Given the breadth and flexibility of the powers introduced, it is clear that the DMU will play a crucial role in shaping the future of competition in UK digital markets.

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<sup>4</sup> It is also worth noting that the CMA may use its own figures as a reference point instead of turnover.