

COMPETITION & REGULATORY NEWSLETTER

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CMA issues report and guiding principles following initial review of AI foundation models

Introduction

On 18 September 2023, the UK Competition and Markets Authority (CMA) published a [report](#) setting out its findings following its initial review of AI foundation models. The report reflects the CMA's early thinking on the impact of AI foundation models on UK consumers, businesses and the economy, and contains several principles proposed by the CMA to guide the development and deployment of this technology in the future.

Background

Foundation models (FMs) have emerged in the last five years as a type of AI technology trained on vast quantities of data, that can be used for a wide range of tasks and applications. This includes, for example, chatbots such as OpenAI's ChatGPT and code writing assistants. Foundation models can also be used to automate parts of processes or workflows within organisations, including through AI assistant features such as Microsoft's Office 365 Copilot.

In May this year, the CMA announced the launch of an initial review into the impact of FMs from a competition and consumer protection perspective. The CMA stated at the time that it was carrying out this review with a view to, among other things, "*ensuring it has sufficient information to take informed decisions in relation to its work*". More particularly, the CMA hoped to obtain an early understanding of:

- how markets created or impacted by the development of FMs could evolve;
- the potential opportunities and risks for competition and consumer protection; and
- the principles which could best guide ongoing developments in FMs to ensure innovation and benefits to people, businesses and the economy.

The launch of the review was covered in more detail in a [previous](#) edition of our Competition & Regulatory newsletter.

Report findings

The report sets out the CMA's initial findings in respect of three levels of the value chain: (i) the development of FMs; (ii) how FMs are used in other markets and user applications, and (iii) the experience consumers have when using these new AI tools, in particular whether they can make informed choices and are treated fairly.

Competition in the development of FMs

The CMA states in its report that "*it has seen evidence indicating that there is currently vibrant competition*" at this level of the supply chain, with a range of larger and smaller

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firms investing in and developing FMs, and a mix of open and closed-source FMs being available and competing. The report notes that around 160 FMs have been developed and released since the first public FM was released in 2018. It also highlights that the impact of FMs could allow a wider range of firms to compete successfully and challenge existing market leaders.

As part of its review, the CMA has considered potential barriers to entry, including the extent to which there are economies of scale and other characteristics of FM development and deployment that tend towards market concentration, consolidation and integration. The CMA has found that FM developers depend on access to certain key inputs including significant computing power, large quantities of training data, skilled research scientists and engineers and access to substantial capital. According to the CMA, access to these key inputs could influence the development and competitiveness of FMs in the future.

The CMA acknowledges that, given the wide range of FM deployment options, a spectrum of possible firm and market structures may arise in the future. The CMA states in its report that it will not hesitate to use its competition enforcement and market investigation powers where appropriate, if competition issues emerge in the market for the development of FMs.

The impact of FMs on competition in other markets and potential outcomes

The CMA has found that, as a result of the vibrant competition taking place among FM developers upstream, FMs are being deployed downstream in a growing range of applications across the economy, including search, productivity software, social media and healthcare. The evidence gathered by the CMA points towards the “*potential for FMs to transform a wide range of services and be the catalyst for significant innovation and competitive disruption in markets*”.

However, the CMA notes that it is currently uncertain exactly how important FMs will be in the future and which downstream markets will be most affected by the deployment of FMs. According to the CMA, a key factor in ensuring FMs drive competition in downstream markets will be the continued availability of a wide range of innovative deployment options that downstream firms can easily switch between. The CMA has identified the following factors as potential areas for future concern:

- significant data feedback effects that may tip the downstream market towards concentration;
- consumers’ inability to meaningfully choose between FM services or switch away from downstream ecosystems; and
- vertical integration and partnerships that “*harm competition or restrict businesses’ choices*”.

Consumer protection

The CMA considers that the adoption of FM services is likely to be more positive if consumers are sufficiently protected from the harms that may result from the use of FM tools, and if both consumers and businesses fully understand their risks and limitations. The CMA notes that raising awareness of when an FM-based service is being used to generate an output is critical to avoiding false or misleading information and allowing consumers to make informed decisions. Consumer harms identified as arising from FMs included fake reviews, phishing, hidden advertising and deep fakes.

The CMA considers that a key driver to improving the reliability and accuracy of FMs for consumers is robust competitive pressure at the various levels of the supply chain. The report also conveys the CMA’s view that there should be accountability over FM outputs and clear consumer redress where things go wrong. According to the CMA, proper allocation of responsibility is a key incentive for FM developers and companies to improve the consumer experience.

Proposed principles and next steps

Based on these findings, the CMA has proposed the following guiding principles for the future development and deployment of AI:

- **Accountability** of FM developers and deployers for outputs provided to consumers.

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- **Ongoing access** to key inputs necessary to compete in the FM market. This includes access to large data sets, computing power, expertise, and capital.
- **Sustained diversity** of business models, including both open-source and closed-source FMs.
- **Sufficient choice** for businesses so that they can access FMs in a variety of ways, including through partnerships or third party plug-ins.
- **Flexibility** to enable consumers to switch and/or use multiple FMs easily, including the ability to "port" their data between services.
- **Fair dealing** and restrictions on businesses engaging in what the CMA perceives to be anti-competitive conduct relating to the FM products - including self-preferencing and tying/bundling.
- **Transparency** regarding the risks and limitations of FM-generated content to enable consumers to make informed choices.

The CMA has stated that the initial report is only the beginning of a significant programme of engagement that it is undertaking in this area. The CMA is planning to seek views both on the overall report and on the proposed principles themselves. An update on the CMA's thinking and how the proposed principles have been received is expected in early 2024, following engagement by the CMA with a variety of stakeholders in the UK, US and elsewhere, and reflecting further developments in the market.

While the CMA's engagement and review of FMs continues, businesses should expect that any mergers or acquisitions involving AI technology and FMs will be scrutinised carefully. Firms with existing or potential FM technology should likewise be cautious to comply with competition law as future collaborations or agreements will likely pique the interest of the CMA and other regulators.

OTHER DEVELOPMENTS

ANTITRUST

Competition Appeal Tribunal upholds CMA decision in hydrocortisone pricing case

On 18 September 2023, the Competition Appeal Tribunal (CAT) published its [judgment](#) in an appeal by various parties against the CMA's [infringement decision](#) in the hydrocortisone pricing case.

In July 2021, the CMA found that Auden McKenzie and Actavis UK (now known as Accord-UK), who had acquired Auden McKenzie in 2015, had abused their dominant position, under Chapter II of the Competition Act 1998 (the Act), through the excessive pricing of hydrocortisone tablets between 2008 and 2018. During their investigation, the CMA found that prices of hydrocortisone tablets had risen by over 10,000 per cent when compared to the original branded version of the drug. The price increased from 70p for one pack of 10mg tablets in April 2008 to £72 per packet by March 2016. The CMA also found that Auden McKenzie, and subsequently Actavis UK, had colluded with certain potential competitors to refrain from entering the market to supply hydrocortisone tablets, in breach of Chapter I of the Act. The CMA imposed total fines of £266.5 million on the various parties for the collusion and abuse of dominance infringements. The current parent companies of Actavis UK, Intas/Accord, and the former parent company, Allergan, were held liable for some of the fines imposed.

The CAT's judgment only dealt with the abuse of dominance findings, leaving the collusion aspects to be covered in a separate judgment. The CAT unanimously upheld the abuse of dominance infringement decision, concluding that the prices charged were "*well in excess of what was fair*" and resulted in "*significant economic harm to the wider community*". However, the CAT found that the former parent company, Allergan, should not have to pay a penalty for the period when it owned Actavis UK subject to 'hold separate' commitments as these meant that Allergan did not exercise control over its subsidiary in the relevant time period. The CAT therefore reduced the penalty imposed on Allergan by £26 million. The CAT affirmed the remaining penalties imposed by the CMA on the appellants, leaving a total amount of £130 million - the highest CMA penalty upheld by the CAT to date.

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European Commission carries out unannounced inspections in the medical devices sector

The European Commission raided the office of an unnamed company active in the cardiovascular medical devices sector, as a preliminary step in its investigation into suspected anti-competitive behaviour. The Commission released a [statement](#) to this effect on the 19 September 2023, stating that the unannounced inspection was a result of concerns that the company may have infringed Article 102 of the Treaty on the Functioning of the European Union, which prohibits abuses of dominant market positions. The Commission was accompanied by the relevant national competition authority of the Member State of the company's home jurisdiction.

The Commission has increased its use of dawn raids since the coronavirus pandemic, conducting raids in at least ten probes since 2022 across various industries, including fashion, synthetic turf, energy drinks, fragrances, and online food delivery. The rise of home working, use of personal devices for work and cloud computing have all added to the complications for companies subject to dawn raids.

SUBSIDY CONTROL

European Commission announces an anti-subsidy investigation on Chinese electric vehicles

Following months of speculation, the President of the European Commission, Ursula von der Leyen, announced in the [State of the Union address](#) that electric vehicles built in China will be subject to an EU anti-subsidy investigation. In announcing the investigation, the President noted that *“Europe is open to competition. Not a race to the bottom.”*

The probe is the result of concerns that subsidised Chinese cars may cause distortions to the EU market with artificially low prices. China is currently the world's biggest electric vehicle producer.

An anti-subsidy investigation requires *“sufficient prima facie evidence”* that a country is subsidising companies exporting a particular product to the EU and that this is harmful to the EU industry. Should the Commission conclude that the subsidised imports are causing injury to the EU automotive industry, it may decide to impose countervailing duties. The Commission has up to 13 months from the initiation of its investigation to impose any measures.

The China Chamber of Commerce to the EU (CCCEU), an industrial association representing Chinese firms in the EU, has [noted](#) its opposition to the investigation, claiming that the competitive advantage of Chinese-built cars is not a result of subsidies. The CCCEU has urged the Commission to review the probe *“objectively”*.

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