

When Newcomers are Gatekeepers

Ofcom's future approach to mobile markets public consultation

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Theoretical summary

The analysis offered in the discussion paper underpinning Ofcom's future approach to mobile markets is robust and convincing. It should also pay attention on establishing the level of interdependence of mobile markets with other digital markets. Any analysis of mobile markets in isolation from the broader context risks offering a fragmented, unrepresentative or misleading picture. Mobile markets should be analysed in conjunction with the processes taking place in adjacent sectors of the digital economy. This means the toolkit of narrow product market definition, as used in enforcing *ex-post* competition law, should not be transposed mechanistically to the policy discussion on the future regulatory approaches to mobile markets.

What may appear to be a new market entry to the area of mobile services (and thus being beneficial for competition), may in reality be a market expansion, where the entrenched power of some online gatekeepers is being swiftly leveraged to mobile markets. The implications of such a transposition of market power from some digital markets to the others would be detrimental both for those digital markets, which are already characterised by systemic entrenched features, as the leveraging would enable further strengthening of the current

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gatekeepers, as well as projecting their market power into the newly entered mobile markets.

If the evolution of the mechanisms of private relay and eSIM continues its current trajectory, UK MNOs will likely face strong competition with entrenched gatekeepers, who have cemented their dominance in their 'native' product markets. Should these undertakings enter the UK mobile retail market, they would have the remarkable ability to synergise, optimise and consolidate by offering various bundled solutions to consumers, by synthesising their resources, competences and technology; and by (i) first disintermediating the current MNOs and their customers/consumers and then (ii) re-intermediating them with each other under the new model with the cemented mobile operating systems (MOS) duopoly becoming an indispensable, and unavoidable controller of the redesigned supply chain (via the mechanism of eSIMs and various advanced models of online choice architecture).

In defining the regulatory approach to shaping digital markets, regulators should place greater emphasis on the need to consider the evolution of digital markets from a more strategic, long-term point of view, rather than just through the optics of consumer/customer interests/welfare/wellbeing considerations, even if the latter scenario would receive very little opposition from business and end users. Both may well see these consolidation processes as developing in line with their own short-term economic interests, expectations, and behavioural patterns.

A more proactive role of regulators does not imply less competition. This is particularly the case in situations when the areas of regulatory attention are characterised by systemic market failures, which require a more proactive attitude, shaping and steering. Digital markets are among such markets requiring stronger (but balanced) intervention in order to function properly. They are characterised by systemic market failures,² and without strategic regulatory coordination are susceptible to unhealthy mutations. Such coordination should reflect the interests of UK digital society. These interests are much broader and more diverse, going far beyond traditional neoclassical economics.

In addition to being asymmetric in its methodological scope, the new regulatory philosophy for shaping digital markets is characterised by its 'smart' elements. This idea is reflected in the need to proactively shape and design competitive

² E.g., strong network effects, zero-price nature of most of the markets, winner-takes-all and market tipping, economies of scale and scope, data synergy and competition for the markets.

process in digital markets, rather than just sporadically protect competition from instances of explicit infringements *ex-post*. This smart proactive modality requires regulators to be more strategic in calibrating the configuration of the markets.

Introduction

This paper is written in response to Ofcom's future approach to mobile markets public consultation. It aims to articulate and substantiate the need of evaluating the evolution of mobile markets in conjunction with and through the prism of the broader economic processes occurring in the digital economy.

The paper provides theoretical underpinning to the argument that the mobile operating system duopoly has sufficient power to constraint competition in the retail mobile (connectivity) market. The potential leveraging power of the duopoly is most clear in the following markets/disintermediation technologies:

- mobile operating systems (full control, self-preferencing and possibility of disintermediation)
- app stores (full control, self-preferencing and possibility of disintermediation)
- eSIM (full control, self-preferencing and possibility of disintermediation)
- private relay (full control, self-preferencing and possibility of disintermediation)
- digital advertising (near to full control, self-preferencing and possibility of disintermediation)

The main *normative* thesis of this submission is that the UK's retail mobile markets should be protected, steered and shaped not in isolation, but as an integral part of the holistic and synchronous regulatory agenda in the area of the digital economy.³ A narrow insulated analysis of the processes taking place in the UK's retail mobile markets may lead to the conclusion that an active entry to these markets by the undertaking having an entrenched position in other areas

³ Angela Zhang, 'Agility Over Stability: China's Great Reversal in Regulating the Platform Economy', available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3892642, p. 15: 'Law is never complete as it cannot possibly anticipate all contingencies. [...] This is particularly the case for disruptive technologies such as online platforms, which have grown so rapidly that existing rules and regulations often fail to cover their innovative products or services. [...] As such, regulators often don't become aware of problems until they become serious. Even when the regulators become aware of problems, it still takes time for the legislature and law enforcers to formulate a unified and coherent response'.

of the digital economy is beneficial as it would diversify and intensify competition in the UK's retail mobile markets. As the processes taking place in various digital markets are interdependent, the increased role of the undertakings with entrenched status in other markets would create a real risk of disintermediation followed by further strengthening of the role and impact of the entrenched market players in the UK digital society.

The main *methodological* proposition is that the analysis of (i) mobile markets in isolation from (ii) the market of mobile operating systems; (iii) the markets of digital content distribution; (iv) the markets of online advertising; (v) the markets of handset manufacturing and (vi) the markets of data governance may only explain an unrepresentative (though at first glance well-structured and logically convincing) part of the broader intertwined processes taking place in the UK's digital economy.

Market definition

While each of the above markets is characterised by peculiar and very specific features, the interconnection between them is self-evident. The power in one market is in one way or another transposable to the others.

Of course, the strong interdependence of the processes taking place in these six markets does not necessitate their uncritical conceptual fusion into one meta-market. It would be equally grotesque however to study the evolution of these markets in complete isolation. This explains the need of developing a meaningful analytical framework, exploring in more detail the impact each of these markets has on the others.

The current gatekeepers in the market of MOSs hold a durable, stable and unchallengeable duopoly power. Their entrenched status in the market of MOSs allows virtually an absolute control over the ways of how all other mobile markets' players interact with each other and with their end users.

This unique market status of the MOSs providers makes them essential trading partners in the industry of mobile communications. A potential implementation/scaling up of further disintermediating solutions offered in particular in *private relay* and *eSIM* technologies would distort the delicate balance in digital markets, shifting the yet tolerable status of *essentiality* to the bottleneck-unavoidability one. No meaningful interaction can be made, and no

significant value can be generated without an active intermediation of the MOSs providers.

A further strengthened position in the mobile communications supply chain would enable the MOSs providers a significant leveraging power to transpose their present dominance in most of other digital markets to the UK retail mobile market.

In as much as the market of mobile operating systems is deeply interlinked with the markets of digital content distribution; online advertising; handset manufacturing; and data governance (and to a different degree with all 'core platform services' as envisaged by Art 2(2) of the EU Digital Markets Act proposal),⁴ any analysis of the future development of the former would be fragmented, partial and unrepresentative without factoring in the processes taking place in the latter markets.

Such strong interdependence between these markets does not imply the need to analyse all of them as a single market. On the contrary, robust economic analysis requires rather narrow delineation of the markets and the processes which have an impact on their development. The fact of market interdependence alone does not challenge the traditional approaches to market definition. It challenges and relativises however the validity and practicality of the outcomes derived from such narrow, context-specific definition of product markets, as well as the overall practicality of such narrow market analysis.

The rationale of *ex-post* competition law requires narrow product and geographical market definitions not least because the investigated undertakings are subject to strict legal liability. The analysis concerns the proof of an infringement of the law. In this context the narrow market definition is a robust and necessary legal test. Without such a test the scope of legal liability would be too amorphous and susceptible to arbitrariness.

The regimes of *ex-ante* regulation or consultation on policy priorities/interpretation are not conceptually constrained by the narrow market definition requirements. Their purpose is not punitive but restorative and

⁴ The DMA Proposal, Art 2(2): "Core platform service' means any of the following: (a) online intermediation services [such as e-commerce market places or online software applications services]; (b) online search engines; (c) online social networking services; (d) video-sharing platform services; (e) number-independent interpersonal communication services [messengers]; (f) operating systems; (g) cloud computing services; (h) advertising services, including any advertising networks, advertising exchanges and any other advertising intermediation services, provided by a provider of any of the core platform services listed in points (a) to (g)". The latest version of the DMA also includes the category of web browsers, virtual assistants and connected TV.

proactive. As no infringer has to be identified and subject to legal liability, the room for methodological flexibility and scientific apparatus for defining the scope of analysis become both much wider and more flexible.

The logic of narrow market definition is not directly transposable from the ex-post to ex-ante modality.

Synchronous response by different digital regulators

The gatekeepers' duopoly has generated an unprecedented economic power in the markets of MOSs; digital content distribution; online advertising; handset manufacturing; and data governance. This power is characterised by direct synergetic effects. Scaling up in one market makes maintaining and strengthening power in the others much easier, more harmonious and intuitive to consumers. The expanding effect is natural, essentially unavoidable and (which makes it even more challenging from the perspective of competition policy) readily justified as protecting security and privacy.

This explains the wide range of synchronous proactive actions by regulators, antitrust enforcers and legislators across various developed economic jurisdictions, aiming to introduce a range of legal, economic and policy mechanisms in an attempt to mitigate the prolific imbalances.⁵

The feature which unites all of these initiatives is *regulatory asymmetry*, which envisages a more proactive enforcement of the existing⁶ and drafting of new targeted rules, aiming to impose additional (and thus asymmetric) obligations on the gatekeepers. These additional obligations are expected to complement existing *ex-post* competition law.

⁵ Australian Competition and Consumer Commission 'Digital Advertising Services Inquiry', Final Report, 28 September 2021; UK Competition and Market Authority, 'Online platforms and digital advertising Market study' Final report, 1 July 2020; European Parliament, 'Online advertising: the impact of targeted advertising on advertisers, market access and consumer choice', Directorate-General for Internal Policies Commissioned Report, 21 June 2021; Autorité de la concurrence Décision 21-D-11 du 07 juin 2021 relative à des pratiques mises en œuvre dans le secteur de la publicité sur Internet, 07 June 2021; Gesetz zur Änderung des Gesetzes gegen Wettbewerbsbeschränkungen für ein fokussiertes, proaktives und digitales Wettbewerbsrecht 4.0 und anderer wettbewerbsrechtlicher Bestimmungen („GWB-Digitalisierungsgesetz“), 18.01.2021; The Parliament of the Commonwealth of Australia, House of Representatives, 'News Media and Digital Platforms Mandatory Bargaining Code Act', Act no: 21, 02 March 2021.

⁶ Jens-Uwe Franck, Martin Peitz, 'How to Challenge Big Tech', in Heiko Richter, Marlene Straub, Erik Tuchtfield (eds.), 'To Break Up or Regulate Big Tech? Avenues to Constrain Private Power in the DSA/DMA Package', Max Planck Institute for Innovation and Competition Research Paper No. 25, October 2021, p. 84.

Most of these initiatives are introduced outside of traditional competition law as the purpose for their introduction is much more policy shaping than legally prohibitive. The foundations of the new regulatory philosophy vis-à-vis gatekeepers are based in proactive modality.⁷ This implies an engaged designing of the digital economy and digital society more broadly. It goes far beyond the protective, *watchdog* function. In other words, the emerging digital competition policy goes beyond both the established instruments of *ex-post* competition law as well as the established mechanism of *ex-ante* sector-specific regulation.

There is increasing consent among legislators and regulators that the new asymmetric approach to digital markets is the only meaningful way to address systemic market failures, to protect and promote competition in the digital economy and to steer the development of the industry in such a way that it corresponds to the interests and priorities of our society.

From the narrow formulaic perspective of *ex-post* competition policy, the MOSs duopoly could be seen as new entrants to retail mobile markets. This would imply very lenient, if not welcoming, regulatory treatment in the area of mobile markets. Such an approach would be detrimental to competition in digital markets in the long run. All digital markets in general, and the above mentioned six markets, are interdependent and evolving in combination. In most of these markets the duopoly (willingly or not) constrains competitive dynamics, preventing most instances of healthy economic rivalry. Gaining a decisive level of absolute disintermediating capacity in retail mobile markets would further strengthen the overall gatekeeping status of the MOS duopoly.

Proactive and holistic approach to digital markets

The main proposition of this submission is therefore that the potential of the MOSs duopoly to enter the retail mobile markets should not be seen through the prism of a narrow methodological toolkit of neoclassical microeconomics. While nominally, and in the short-term perspective, such an entry may show signs of triggering and intensifying competition in the retail mobile markets, its medium- and long-term implications on competition in the digital economy are likely to

⁷ Anupam Chander, Haochen Sun, 'Sovereignty 2.0', University of Hong Kong Faculty of Law Research Paper, No. 041, September 2021, p. 8.: 'When Thomas Hobbes imagined an "Artificiall Man" in the form of a state, [...] he was not picturing Facebook. But the reality is that modern leviathans like Facebook and Google, and even Reddit and Twitter, exercise enormous power over our lives. Increasingly, governments across the world have sought to bring these companies under their control. While China pioneered data sovereignty, it is now the demand of governments from Australia to Zimbabwe'.

lead to further qualitative and quantitative consolidations and significant increase of the disproportionate bottleneck power of the duopoly in the markets of mobile operating systems; digital content distribution; online advertising; handset manufacturing; data governance and others.

The unprecedented market power in these and adjacent markets would allow the duopoly a speedy and effective disintermediation of the present supply chain in the area of retail mobile market using the tools, which are currently legitimate and not prohibited by *ex-post* competition rules. Such disintermediation could be done either directly via eSIM⁸ or indirectly via MOSs preinstalled by most of handset manufacturers.⁹

The focus of sectoral digital regulators is gradually shifting from the narrow, case-specific, axiomatic and syllogistic application of traditional competition rules (i.e., one relying mainly on theoretical microeconomic models rather than on the real-life policy-making vision) to establishing broader, more strategic, proactive and holistic principles. The responsive approach alone is insufficient in dealing with all emerging problems and opportunities. The latter trend requires more intense communication and greater understanding of the agenda, priorities and toolkit of each of the digital regulators. The establishment of the UK Digital Regulation Cooperation Forum embodies and epitomises this trend.

Another dimension of a more informed and strategic sectoral enforcement concerns the increased role of the Government in shaping the UK digital economy. The recent DCMS & BEIS consultations on the reform of competition law in general¹⁰ and its digital aspects in particular¹¹ demonstrate the systemic nature of these processes.

In line with the logic and the philosophy of a more systemic approach to regulating the digital economy, it is important to address the development of mobile markets not in isolation but as part of the broader processes taking place in the markets of digital content distribution; online advertising; handset manufacturing; and data governance. Ofcom's discussion paper on its future

⁸ See the rationale in e.g., BT Group Response to Statement of Scope of the CMA Mobile Ecosystems Market Study, 26 July 2021.

⁹ See e.g., the rationale in EU Commission Android Decision – Case AT.40099, Google Android, [2018], C(2018) 4761 final.

¹⁰ UK Department of Business, Energy and Industrial Strategy Public Consultation 'Reforming Competition and Consumer Policy: Driving growth and delivering competitive markets that work for consumers', July 2021.

¹¹ UK Department for Digital, Culture, Media & Sport and Department for Business, Energy & Industrial Strategy, 'A New Pro-Competition Regime for Digital Markets', Public consultation, 20 July 2021.

approach to mobile markets is mindful of this broader strategic trend as well, stating *inter alia* that ‘the competitive dynamics are changing and there is uncertainty over what the longer-term impact will be’,¹² and inviting an open discussion among the stakeholders on what Ofcom’s future approach to mobile markets should be.

In response to this invitation, this paper submits that Ofcom should shape UK mobile markets bearing in mind not only direct, immediate and measurable performance of these markets, but also taking into account the broader strategic challenges and opportunities of the UK digital economy as envisaged, for example, in UK Department for Business, Energy & Industrial Strategy, ‘Regulation for the Fourth Industrial Revolution’, Policy Paper¹³ and Final Report of The UK Taskforce on Innovation, Growth and Regulatory Reform.¹⁴

This implies an objective and commended trend of a greater discretion on the part of ‘the UK’s regulatory bodies, removing many of the detailed rules in the existing statutory frameworks to make them less prescriptive (replacing them with outcomes to be achieved), and allowing the regulatory regime to be shaped more by case law’,¹⁵ acknowledging a greater role for interpretation, relative indeterminacy, horizon scanning and regulatory experimentation (sandbox).

The role of price/consumer welfare in assessing market performance

Another important dimension of the emerging paradigm is the diversification of goals and priorities. While under the previous modality the main criterion for evaluating the performance of the markets was consumers/end users and their welfare/wellbeing, the constellation of digital interests in society is becoming more diverse.

Low prices are no longer the gold standard for assessing the effective functioning of the markets. The widespread presence of zero-sum markets, various instances

¹² Ofcom’s future approach to mobile markets A discussion paper, 09 February 2022, 1.25.

¹³ UK Department for Business, Energy & Industrial Strategy, ‘Regulation for the Fourth Industrial Revolution’, Policy Paper, 11 June 2019, p. 5.: ‘The Fourth Industrial Revolution presents challenges for regulatory systems across the globe, as they struggle to keep pace with rapid, complex technological innovation. [...] We need to act now to maintain our world-beating regulatory system in this period of transformational change’.

¹⁴ Final Report of The UK Taskforce on Innovation, Growth and Regulatory Reform, May 2021, 1.8: [There is a need in delegating] ‘greater flexibility to regulators to put the principles of agile regulation into practice, allowing more to be done through decisions, guidance and rules rather than legislation’.

¹⁵ UK Department for Business, Energy & Industrial Strategy, ‘Regulation for the Fourth Industrial Revolution’, Policy Paper, 11 June 2019, 3.1.2.

of leveraging market power from one area to the other, rapid internationalisation and interdependence of global markets, as well as an increased consensus about the main strategic technique of competitors being competition for the markets rather than competition in the markets, make it clear that the prices paid by consumers are only a fragment of the meaningful strategic assessment of market performance.

Any meaningful digital competition policy is primarily focused on the structure of the markets, the format of competitive dynamics taking place in these markets, and the effective implementation of the economic interests of a specific society more generally. It goes without saying that consumers would ultimately be the final beneficiaries of these fair and contestable markets, but their welfare cannot be used as a direct manifestation of the effectiveness of a specific policy.

Also, from a purely behavioural perspective, consumers cannot be the main direct beneficiaries of the rules, as a critical mass appears to be happy with the *status quo*. A well-described ‘privacy paradox’¹⁶ explicates consumers declaring their interest in privacy while ignoring this aspect in their digital routine. The paradox may be extended to other aspects of consumer psychology. Not only are many consumers complacent about online privacy, they are equally ignorant of and/or disregard other behavioural patterns shaped by the gatekeepers.

Consumers appear content to live in the digital universe with the parameters predefined for us by algorithms. The literature on hard and soft online addictions, path dependencies, dark patterns, echo chambers and filter bubbling is disappointingly pervasive and alarming. The latest studies¹⁷ illustrate convincingly that the ability to control and shape online choice architecture leads to designing consumer behaviour in a way, anticipated and projected by the architect. Adding the choice screen option for selecting retail mobile service provider would represent another instance of such consumer steering.

All of the above explains why the focus of the new rules has shifted from consumers to the markets. Protecting and promoting the competitive process in the markets appears to be the main goal and function of digital competition law. This conclusion, however, does not make it clear which specific dimension of the

¹⁶ Miriam Caroline Buiten, ‘Exploitative Abuses In Digital Markets: Between Competition Law and Data Protection Law’, “[P]rivacy paradox’ [is a situation, in] which consumers state that they value privacy despite not acting in accordance with this’. *Journal of Antitrust Enforcement*, Vol. 9, No. 2, 2021, p. 286.

¹⁷ See e.g., the CMA Research and analysis Evidence review of Online Choice Architecture and consumer and competition harm, 05 April 2022.

competitive process in the digital markets should be given a priority. The remaining rubrics address these options in turn.

The real criteria for evaluating the effective functioning/development of the markets are not formulaic but contextual; not categorical but open to interpretation in light of the UK's strategic priorities in shaping its digital markets. Applying any other methodological approach would open the doors for further leveraging of market power and competences of the duopoly to the area of retail mobile connectivity. Any static microeconomic toolkit exploring the situation in the market consulted by the Ofcom would offer a comfortable and convincing answer that the industry of M(V)NO would be better off once faced more realistic and intense competition from the new MOSs entrants.

Another important implication from this methodological observation is that consolidation in retail mobile markets may lead to an increase of competition in the broader digital spheres. Allowing MNOs to scale up would enable their strategic long-term innovation and investment. There is a need to soften the categorical stereotypes about price competition and consumer welfare as the only/central parameter of regulatory analysis. Such an approach would be workable only if the MNO were not facing strong geographical and product interdependencies.

Conclusion

If the evolution of the mechanisms of private relay and eSIM continue in the current trajectory, UK MNOs will be likely to face strong competition with entrenched gatekeepers who have cemented their dominance in their 'native' product markets. Should these undertakings enter the UK mobile retail market, they would have a remarkable ability to synergise, optimise and consolidate offering to consumers through various bundled solutions, by synthesising their resources, competences and technology; and by (i) first disintermediating the current MNOs and their customers/consumers and then (ii) re-intermediating them with each other under the new model with the cemented MOS duopoly becoming an indispensable, and unavoidable controller of the redesigned supply chain (via the mechanism of eSIMs and new online choice architecture).

Historically, over the last two decades the incumbent mobile operators faced much more stringent regulatory constraints than counterparts in MOS, online advertising, data governance, content distribution and other digital markets. There was an

obvious disbalance with strict rules with regard to MNOs and very permissive attitudes to the gatekeepers.

Most advanced jurisdictions have acknowledged the second part of the disbalance. The latest wave of the active enforcement of *ex-post* competition rules, as well as various legislative initiatives aimed at remedying the excessive market power of gatekeepers proves that the previous regulatory modality was based on a false understanding of the dynamics of the digital market process. This acknowledgement however offers only a fragmented explanation of the situation and only a partial remedy. The missing part concerns the increased role of MNOs in digital connectivity. Competition in these markets can be triggered not only by imposing on gatekeepers the stricter *ex-ante* obligations towards their business and end users. This recalibration is indeed important, but it is unlikely to trigger sufficient new competitive dynamics unless it is accompanied by a willingness by other players such as MNOs seeking to compete within digital markets.

By softening the anachronistically disproportional regulatory burden on the MNOs (reflected e.g., in the categorical prohibition of any instance of commercial traffic management) and by shifting it to the gatekeepers, the competitive dynamics could be restored using the natural market means. The only meaningful competitors to the current gatekeepers are MNOs. Allowing them more economic freedom and the regulatory assurance from the excessive interventionism could lead to the recalibration of the digital markets with the emerged MNOs competing effectively in more and more segments with the gatekeepers. Clearly, this revision of the regulatory philosophy requires more nuanced and more engaged consultation and discussion.

The conclusion of this paper is that competition in mobile markets cannot be analysed mechanistically. Any regulatory framework that considers new entries to these markets by the MOS duopoly as being pro-competitive may well appear on the surface to be methodologically correct. Yet such approaches would be static, short-sighted and counterproductive. The MOS duopoly has all the technological competence and economic interest to establish itself as an additional intermediary between the M(V)NO and end users, disintermediating the former from the latter, recalibrating market protocols and synchronising the newly established power in the mobile markets with the existing (and growing) market power in other digital markets, such as (i) the market of mobile operating systems; (ii) the markets of

digital content distribution; (iii) the markets of online advertising; (iv) the markets of handset manufacturing and (v) the markets of data governance.

If these processes continue evolving in this trajectory, very quickly and with ease the retail mobile markets (or at least the value of these markets) could become subsumed into the markets of the mobile ecosystems.

Even if the emergence of the new intermediaries (eSIM controllers) would diversify competition between the M(V)NOs, such a diversification would yet lead to further strengthening of the Mobile Operation System (MOS) duopoly. In as much as the digital markets are interdependent and cannot be analysed in isolation, the emerged market power in the retail mobile market would have further spillover effects on all other digital markets where the MOS duopoly has already cemented its position. Such leveraging of the market power is very common, fairly intuitive and manifestly plausible.

The analysis of the future development of retail mobile markets cannot be performed in isolation from the current regulatory initiatives to constrain the omnipotent power of the digital gatekeepers. Without such coordination, there is a risk of a significant divergence of various UK digital regulatory policies, leading to a counterproductive situation when one digital policy negates the expected effect of the other by shielding the addressees of the latter from the regulatory rigidity of the former.