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Implications of E-commerce for Competition Policy - Note by Korea

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More documents related to this discussion can be found at www.oecd.org/daf/competition/e-commerce-implications-for-competition-policy.htm

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Korea

1. Intro

1. Korea's e-commerce[1] market has been growing rapidly with its sales amounting to approximately 78 trillion won as of 2017.[2] This accounts for roughly 20% of the total retail sales in Korea. The expansion of e-commerce is causing a tremendous change to retail market and affecting consumers' purchase patterns. Consumers can readily purchase products anytime they want at reasonable prices without having to go to the markets or department stores. Also, consumers produce product information and evaluation, and share with other consumers, thus, having the power to influence the market and companies.

2. On the other hand, there is a flip side to the rapid growth of e-commerce market. Sometimes small enterprises or consumers suffer harm due to anticompetitive conduct or unfair trade practices. In particular, in case of *open market*[3], which takes up a large share of e-commerce market, there may be problematic situations for both the stores and consumers. For instance, the stores that sell goods or services through the open market may have unfair trade relations with the open market operators, and consumers can face difficulties in resolving issues because the open market operator does not bear the responsibility as a transaction party.

3. Accordingly, the KFTC is trying to promote competition and correct unfair trade practices in the e-commerce sector through enforcement of competition law. The KFTC is also making efforts to protect consumers and small and medium-sized suppliers in the e-commerce sector by enforcing Consumer Protection in E-commerce Act[4] and Fair Transactions in Large Franchise and Retail Business Act.[5]

4. In this paper, we are going to introduce the KFTC's major enforcement cases in e-commerce sector including 'eBay's acquisition of Gmarket' in which market definition was a problem due to two-sided characteristics of the open market, and 'Naver's case of consent order where abuse of market dominance by Internet Portal service[6] was problematic.

2. Enforcement cases in Korea's e-commerce sector

2.1. eBay's acquisition of Gmarket

2.1.1. Case overview

5. The eBay signed an MOU agreeing to buy more than 50% of Gmarket's shares, which is an open market operator. Before making a formal notification, it made a preliminary filing with the KFTC in May 24, 2008. The eBay is the biggest shareholder of Auction, another open market operator. With the acquisition, a horizontal integration occurred, which caused both the Korea's largest and second-largest open market operators, Gmarket and Auction, to belong to eBay.

6. Unlike general online shopping malls, which conduct merchandise planning, marketing, sales and customer service directly on their own, open market operators just

provide space and methods for transaction, and generate revenue from sales commissions that sellers pay.

7. Open market is a two-sided platform in nature for three reasons. First, there are two distinct customer groups; sellers and consumers. Second, indirect network effects exist between the two groups. Third, through the intermediation of open market, the transaction cost between the two groups can be reduced. Therefore, how to define the scope of the relevant market had been the crucial issue to discuss when conducting a merger review.

2.1.2. Relevant market delineation

Delineating separately for consumer market and seller market

8. The relevant market refers to the group of goods or services that can be switched to other goods or services when there is a significant and non-transitory increase in price. When delineating the market, various factors should be taken into consideration. For example, the factors include similarities in the price of products, similarities in the function and usage of products, buyers' perception of products' substitutability and related purchase pattern, and sellers' perception of products' substitutability and related pattern of business decision.[7]

9. In other words, whether one side in the two-sided market can be separately defined depends on the recognition on the substitutability of the services provided to each side, etc. In the merger review for this case as well, consumers' side and sellers' side had been defined as separate markets based on the contents of service provided by the open market operator to consumers and sellers and the substitutability.

10. In the consumers' side, open markets and general online shopping malls[8] provide similar services, and it is relatively easy for consumers to switch transaction from one to the other. Thus, it is safe to say that demand substitutability exist between open markets and general online shopping malls. Accordingly, the relevant market for consumers' side has been defined as the whole online shopping market including open markets.

11. On the other hand, however, in the sellers' side, sellers of the general online shopping malls have to pay high commission in return for various services such as providing customer service or refunds. In contrast, sellers of the open market only have to pay low commission in return for just the minimum service. Thus, sellers recognize the open market differently from general online shopping malls. Accordingly, the relevant market for sellers' side has been defined as open market service market distinguishing from general online shopping malls.

2.1.3. Anti-competitive effects and remedies

12. Post-merger, the market share of eBay in the online shopping market of consumers' side is 36.4% as of 2007, not satisfying the requirements of presuming market dominance[9]. Therefore, the merger is not presumptive of anticompetitive effects in accordance with the Monopoly Regulation and Fair Trade Act (hereinafter the "MRFTA"). Furthermore, with relatively low switching cost for consumers, it is easy to shift to other buying channels. Therefore, the KFTC concluded that there was no anti-competitive effects caused by the proposed merger.

13. On the other hand, in case of open market service market for the sellers' side, the market share of the post-merger firm reached a whopping 87.5% constituting

requirements of presuming anticompetitive effects. Hence, the KFTC concluded that eBay was likely to raise the sales commission based on a high level of customer loyalty toward Auction and Gmarket. Moreover, the KFTC saw it difficult for businesses to newly enter the open market service market.

14. However, the KFTC only imposed behavioral remedies[10] against eBay to prohibit the commission hike for the following three years, after concluding that the anticompetitive concerns such as entry barriers may be addressed in a mid-to-long term considering that e-commerce-based industry is in the midst of a rapid change.

15. In fact, *11th Street*, which is the new open market operator, has grown to have 10.7% market share in the first quarter of 2009 after entering the market early 2008. Also, daily deal sites such as Coupang and Wemakeprice that used to be online shopping mall operators in the past have recently entered into open market business. Taking those into account, it may well be argued that behavioral remedies and the duration imposed by the KFTC against the proposed merger were appropriate.

2.2. Naver's consent order against abuse of market dominance

2.2.1. Case overview

16. In May 2013, the KFTC launched an investigation against Naver for allegedly misleading consumers with the unclear distinction between its organic search results and keyword advertisements.

17. During the KFTC's investigations, Naver applied for a consent order proposing remedies to resolve anticompetitive concerns. After concluding that it was appropriate in addressing anticompetitive concerns, the KFTC then approved the remedy proposal and closed the case.

2.2.2. Relevant market and market dominance

18. Naver is an Internet portal service provider offering IS-4C[11], namely the service of search, contents, communication, community and commerce. The problematic conduct in this case was regarding the search service market[12] which allows consumers to easily find information on the internet.

19. Naver has been maintaining its position as the nation's largest enterprise in the online search service market since 2010. At the time of the investigation in 2014, Naver accounted for as much as 75% market share in the search service market.

2.2.3. Anti-competitive behaviours and effects

20. First, Naver's online search service provided its own paid search advertisements[13] on top of the search results, not the general results through internal search algorithms. When posting such keyword advertisements, Naver did not clearly indicate that those results are paid by advertisers to be exposed on the top, and misled the consumers that they were general search results.

21. In regard to this business practice, the KFTC conducted a survey on 1000 users through a research firm. The survey revealed that 85.9% of respondents said they could not distinguish organic search results from advertisements. They responded that the reasons for the search results to be posted on the top were because they were high in search frequency, or they were certified by Naver as high in quality.

22. The KFTC concluded that Naver, the market dominant player in the online search service market, interfered with consumers from making informed decisions by not clearly distinguishing between organic search results and advertisements, thereby causing concerns that Naver might unduly make the competitors' customers switch to trading with Naver.[14]

23. Second, Naver signed agreements with online shopping malls, movie ticket sites, online bookstores, etc., and grouped them respectively into so-called Naver shopping, Naver films and Naver books. When the users searched for related keywords, it provided organic search results along with Naver's paid-services. Naver generated revenues by receiving advertisement fees from concerned enterprises on a regular basis or receiving fees when the users visit the sites through Naver and buy goods or services. However, Naver did not clearly inform the users of this fact.

24. The KFTC concluded that Naver hindered consumers from making informed decisions by providing organic search results along with paid services and not clearly notifying the users of the fact that Naver receives fees from those enterprises, and also leveraging its market dominance in the online search service market to its paid services and incurring anticompetitive effects.

2.2.4. Consent order

25. In November 2011, Naver submitted the remedy proposal with regard to the advertisement search results as the followings: (1) clearly indicate it is an advertisement; and (2) notify the users of the fact that Naver receives advertisement fees. Moreover, Naver submitted the remedy proposal with regard to the Naver's paid services that include the followings; (1) indicate the name of the company (Naver) in the service; and (2) clearly notify that those paid services are Naver's own services with which it receives fee in return for favorable exposure from respective enterprise.

26. Subsequently, in March 2014, the KFTC approved the proposed remedies, taking into account the following factors: (1) remedy proposal by Naver can sufficiently resolve anticompetitive concerns; (2) the online search service market is an innovative market that requires consideration to its dynamic market conditions and technology developments; and (3) online search is so closely related to users' daily lives that swift restoration of competition order is imperative.

[1] The term *online shopping* is more frequently used in Korea.

[2] *2017 Annual online shopping trends* by Statistics Korea (Feb 2, 2018)

[3] Refers to online market place where anyone can freely buy or sell products. As of 2017, the transaction size through major open market businesses such as Gmarket, Auction, 11th Street, etc. amounts to roughly 30 trillion won.

[4] In Korea, Consumer Protection in E-commerce Act has been enacted and put in place to prevent consumer harm due to non-face-to-face transaction. This Act imposes obligations on online shopping malls such as notification for starting the business to the KFTC or other local municipalities, information provision for consumers (business registration number, business address for place of business, contact information, etc.), no interference for withdrawal of contract, etc. For open markets, they are subject to notification obligation, but considering they are just intermediary agents, different forms of obligations are imposed. (e.g. open market site has to bear information that it is not the transaction party)

[5] In Korea, Large Franchise and Retail Business Act has been enacted and put in place to regulate unfair trade practices of large retail businesses with great buying power against small and medium

suppliers. Online shopping malls (open market operators that are categorized into intermediary agents, not retailers, are not included) are also subject to this Act if the turnover of the previous business year exceeds 100 billion won. According to this Act, unreasonable return of goods, reduction of price or passing the promotional cost on to stores is prohibited.

[6] Internet Portal refers to a gate which provides search service allowing users to move to other internet sites. Recently, however, its role as an ultimate site that provides various services other than search engine is becoming more important. (More detail explanation to be stated below.)

[7] Guidelines for the Combination of Enterprises Review (Public Notification, KFTC 2015-3)

[8] Refer to the online shopping malls in which owners register products onto their shipping mall on their own, and sell to consumers under their responsibility.

[9] Article 7 (4) 1 of the MRFTA, In cases of a combination of enterprises falling under any of the following subparagraphs, it shall be presumed that competition is practically suppressed in a particular business area:

(a)In cases where the aggregate of the market share of the company concerned satisfies the presumptive requirements for a market dominating enterprise (market share of one company exceeds 50% or less than three companies' market share exceeds 75%.;

(b)In cases where the aggregate of the market share of the company concerned is the largest in the business area concerned;

(c)In cases where the aggregate of the market share of the company concerned exceeds the market share of a company with the second largest market share by not less than 25% of the aggregate of the market share;

[10] 1) prohibit raising sales commission, 2)restrict raising registration fee and service (advertising) fee (excluding auction type) to fall within the consumer price inflation, 3)establish measures to protect small and medium sellers, 4)establish and implement measures for complying with MRFTA, and notify the contents

[11] A set of diverse services such as search service, contents providing service such as news, map, sports and finance, communication service such as email and messenger, community service such as blog, online cafes, etc., and commercial service such as online shopping.

[12] It generally has a complex nature; two-sided markets with multihoming effects and network effects, innovative market, and dynamic competitive market.

[13] When a user types in a specific keyword, the advertisements of the advertisers who paid for those keywords are exposed.

[14] Article 23 (1) 3 of the MRFTA and article 36 (1) 4 of Enforcement Decree