

COMPETITION & REGULATORY NEWSLETTER

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CMA publishes AI Foundation Models update paper

Introduction

On 11 April 2024, the UK Competition and Markets Authority (CMA) published an [update](#) to its initial report on AI Foundation Models.

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. FMs can also be used to automate parts of processes or workflows within organisations.

The CMA's [initial report](#) was published in September 2023 (as reported in a [previous edition](#) of this newsletter). It reflected the CMA's early thinking on the impact of FMs on UK consumers, businesses and the economy, and contained principles proposed by the CMA to guide the development and deployment of this technology in the future. Last week's update paper reflects developments in the sector since the initial report, and outlines updated principles to reflect these changes as well as feedback from key stakeholders.

The CMA's key findings

The update paper notes a number of trends in the FM sector since the initial report, including the increasing use of generative AI by consumers and businesses, the growth and ever-expanding capabilities of FMs and the increased integration of FMs into other products. It also notes the importance of key inputs, namely compute (meaning the resources required for software/program computation, such as processing power, memory, storage etc.), data and talent, with partnerships and strategic investments proving a key way for FM developers to access these inputs, and firms engaging in talent wars to attract expertise.

A key observation from the CMA is the increasingly interconnected nature of the FM value chain, with the largest and most established tech firms becoming active across multiple levels. Such interconnectedness results from increased vertical integration and an increasing number of partnerships, investments and strategic agreements between firms operating at different levels, as well as strategic hires of key talent.

Risks to fair, open and effective competition

As a result, the CMA is concerned that the FM sector is developing in ways that "risk negative market outcomes", and has identified three risks to fair, open and effective competition:

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- *Firms that control critical inputs for developing FMs may restrict access to them to shield themselves from competition.* The CMA is concerned that where firms control key inputs for developing FMs (compute, data, expertise) they could restrict access to them in order to prevent the development of challengers to their own FMs or protect their position in related markets.
- *Powerful incumbents could exploit their positions in consumer or business facing markets to distort choice in FM services and restrict competition in FM deployment.* The CMA is concerned that consumer choice over which FM service they use could be influenced if incumbent market players, who control access points to a market, are able to integrate FMs into their existing products - in particular, these firms may be able to give an advantage to their own FM services or those of their partners. The CMA notes that consumers should be able to choose how they use FMs and switch between different options without being locked into one provider or ecosystem.
- *Partnerships involving key players could reinforce or extend existing positions of market power through the value chain.* The CMA recognises that we are witnessing “a proliferation of partnerships and strategic investments in the FM value chain”, as well as “strategic hires of talent”. Importantly, the CMA recognises that such partnerships may be an “essential ingredient” of the development and investment ecosystem in this space. Nevertheless, it notes that such partnerships do not always fall within merger control rules, and it is therefore vigilant towards the possibility that incumbent firms may use such partnerships and investments to “quash competitive threats”. The CMA says that it is monitoring current and emerging partnerships closely, and “stepping up” its use of merger control to examine whether such arrangements fall within the current rules and, if so, whether they give rise to competition concerns.

Updated principles

In light of these perceived risks, the CMA’s update paper sets out updated principles. The updated principles largely mirror those in its initial report, encompassing: (i) access; (ii) diversity; (iii) choice; (iv) fair dealing; (v) transparency; and (vi) accountability. However, greater emphasis is given in the updated principles to the need to prevent powerful partnerships and integrated firms reducing the ability of others to compete and being used to insulate the firms in question from competition. The updated principles also spell out more clearly that it is the responsibility of all firms to help foster the development of a competitive market. The CMA also makes clear at various points in the update paper that it will take account of developments in FM-related markets when considering which digital activities to prioritise for investigation under new powers anticipated in the Digital Markets, Competition and Consumers Bill (DMCC).

AI and consumer protection

The CMA notes that it is also building its understanding of how consumer protection issues might map on to AI-based products and services. To this end, the CMA is undertaking joint research with the Digital Regulation Cooperation Forum to explore consumers’ understanding and use of FM services.

It notes that its “transparency” and “accountability” principles aim to ensure that consumers and businesses have sufficient information on the risks and benefits of AI products. It will also consider issuing proactive guidance to firms on how to comply with consumer law in AI-related markets if it sees uncertainty or particular issues that need clarification. In addition, it notes that the DMCC anticipates new powers for the CMA directly to enforce consumer protection law - powers which it says it is “ready to use” to tackle firms that “do not play by the rules”.

Looking forward

The CMA recognises that fair, open and effective competition and consumer protection are key parts of the broader regulatory landscape in relation to AI in the UK. The UK government recently published its response to the consultation on its AI White Paper, in which it called on regulators including the CMA to outline their

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strategic approach to AI by the end of this month - we will therefore see the CMA's response on this very soon. The CMA also plans to provide another update on its work on FMs this autumn.

OTHER DEVELOPMENTS

MERGER CONTROL

Court of Appeal upholds prohibition of Cérélia/Jus-Rol merger

On 11 April 2024, Cérélia lost its second legal challenge against the CMA's decision to prohibit its completed acquisition of Jus-Rol.

As reported in a [previous edition](#) of this newsletter, in January 2022, Cérélia acquired the Jus-Rol business of General Mills. The CMA launched an in-depth investigation into the completed acquisition and concluded in January 2023 that the merger had led to a substantial lessening of competition in the UK market for the supply of dough-to-bake products to grocery retailers. The CMA determined that the only acceptable remedy was an asset divestment involving the sale of the entire Jus-Rol business to an independent buyer, in effect unwinding the merger.

Following Cérélia's appeal of the CMA decision on judicial review grounds, the Competition Appeal Tribunal (CAT) upheld the prohibition of the merger. The CAT confirmed that the scope of the CMA's remedy was sufficiently reasoned and proportionate and that the process followed by the CMA was rational and fair.

Cérélia launched a further appeal in the UK Court of Appeal. Cérélia's first and second grounds of appeal challenged the conclusion that the merged entity would not be held in competitive check by two alternative suppliers of ready-to-bake products to UK grocery retailers. Additionally, Cérélia raised procedural unfairness challenges relating to the process followed by the CMA in its initial investigation, particularly the extension of the timeline for review for "special reasons" under section 39(3) of the Enterprise Act 2002 (for details, please refer to our previous newsletter).

The Court of Appeal [fully dismissed](#) the appeal brought by Cérélia, finding that the CAT's conclusions were correct, that the CMA conducted a rational and fair investigation and the processes followed by the CMA were lawful. The judgment is the latest illustration of the largely deferential standard applied by the CAT and the Court of Appeal in their respective reviews of CMA merger prohibition decisions. Cérélia is now expected to commence the sale process.

ANTITRUST

Sports Direct refused injunction in kit-selling suit against Newcastle United

On 12 April 2024, the CAT [rejected](#) Sports Direct's application for a pre-trial injunction to compel Newcastle United FC to continue to supply it with replica kit for the upcoming football season.

The case relates to the termination of Newcastle United FC's existing supply arrangements with Sports Direct, a large sports retailer which is owned by former Newcastle United owner Mike Ashley. Sports Direct had applied to the CAT for an injunction on the basis that the football club's refusal to continue to supply it with replica kit for the 2024/2025 season constituted:

- An abuse of the football club's dominant position in the market for the wholesale supply of the club's replica kit in the UK, contrary to the Chapter II prohibition of the Competition Act 1998; and
- A breach of the Chapter I prohibition on anti-competitive agreements, on the basis that the football club had entered into exclusive supply arrangements with Adidas and JD Sports, another sports retailer, that "*have the effect of foreclosing Sports Direct from the market*" for Newcastle United FC replica kit.

In considering the request for an injunction, the CAT found that Sports Direct had failed to establish a "serious issue to be tried" or an arguable case that ceasing an existing supply arrangement constituted an abuse of

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dominance. The CAT went further in suggesting that the proposition that Newcastle United FC and Adidas were generally obliged to maintain supply to Sports Direct over time “*represents a significant fetter on competition, not an enhancement of it*”. The CAT similarly concluded that no arguable case had been made to establish that the arrangements with Adidas and JD Sports were improperly collusive under the Chapter I prohibition.

The CAT stated that its refusal to grant interim relief makes “*a speedy trial more, and not less, urgent*” and has invited the parties to provide rapid proposals to allow the action to proceed to trial. The CAT has since refused permission to appeal its 12 April judgment.

GENERAL COMPETITION

China addresses price discrimination in new regulation for consumer protection

On 19 March 2024, China’s State Administration for Market Regulation (SAMR) released the [Regulation on the Implementation of Consumer Rights Protection Law](#), which is set to take effect on 1 July 2024. While the overarching theme is to supplement the existing consumer protection law and enhance consumer welfare in general, the new regulation also contains specific provisions that aim to address issues in online consumption, which in recent years has grown significantly to capture almost 30 per cent of total retail sales in China, resulting in an increase in related complaints.

Notably, while short of banning big data-enabled personalised pricing, the new regulation prohibits businesses from charging discriminatory prices without consumers’ knowledge. This complements the SAMR guidance under the Anti-Monopoly Guidelines on Platform Economy, which indicate that it may be an abuse of a platform’s dominant market position if the platform applies differential treatment to transaction counterparties without justifiable reasons. The counterparties’ paying capacity, consumption preference and use habits are specifically identified as relevant factors under the Anti-Monopoly Guidelines. The new regulation further seeks to improve price transparency by ensuring that consumers are aware of differential pricing even if it is for a “*legitimate*” purpose, as permitted under the Anti-Monopoly Guidelines (e.g. promotional activities targeted at new users).

The new regulation also prohibits businesses from collecting consumers’ personal information “*excessively*” - while it is silent on what is considered excessive, this may arguably include information that businesses collect for the primary purpose of implementing personalised pricing. It remains to be seen how these new provisions will be interpreted by the Chinese authorities and courts in practice to address the concerns related to personalised pricing in a meaningful manner.

Under China’s consumer protection regime, certain infringements (e.g. relating to product quality, false advertisement) may be penalised with a fine of up to ten times the amount of the illegal gain, and up to RMB 500,000 (around £56,000) in the absence of any illegal gain.

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