Regulation for Digital Platforms: Lessons from the Banking Industry

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Despite there being no shortage of problems for lawmakers to grapple with, scrutiny over the biggest U.S. technology companies (sometimes referred to as "digital platforms") has increased notably over the last few months.[1] The concerns of lawmakers are wide-ranging, mostly reacting to the view that these companies are gatekeepers to information, public opinion and markets, and that their unique access to user information and data may give rise to data privacy, competition and conflicts-of-interest issues. As a result, there is a growing push, particularly but not exclusively among Democrats, to come up with solutions for how digital platforms might be regulated. One approach put forward by some Democrats is to implement holding company regulation based in part on the way banks are regulated under the Bank Holding Company Act (the "BHC Act").

Below, we offer observations on what it would mean to use the BHC Act as a model for regulation of digital platforms. Key issues and elements of a framework that is based on the BHC Act would include:

- express restrictions on activities or lines of business;
- standards to determine when a company is affiliated with a digital platform (and thus subject to the regulatory framework);
- processes and restrictions with respect to mergers and acquisitions and other expansionary transactions within the industry; and
- standards to apply the framework to U.S. companies operating abroad and to non-U.S. companies operating within the United States.

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[1] For instance, on July 29, 2020, the CEOs of Amazon, Facebook, Apple and Google testified at length during a hearing held by the Antitrust Subcommittee of the Judiciary Committee of the House of Representatives. A separate Senate Commerce Committee hearing is also scheduled for October 28, 2020, at which the CEOs of Facebook and Google will again testify along with the CEO of Twitter.

BACKGROUND ON POLITICAL FOCUS

The idea of using a separation regime[2] for digital platforms has been proposed by various commenters.[3] Indeed, in March of last year, during her presidential campaign run, Senator Elizabeth Warren supported this approach.[4] More recently, on October 6, 2020, the Democratic majority staff of the House Judiciary Committee's Antitrust Subcommittee released findings and recommendations regarding the state of competition in the digital economy and recommended the use of a separation regime involving line of business restrictions.[5] Thus, the outcome of the forthcoming election may dictate the extent to which this concept continues to gain traction.

SEPARATION IN THE BANKING INDUSTRY

In the United States, bank holding companies have long been regulated through a comprehensive separation regime, starting with the enactment of the BHC Act in 1956. The fundamental idea supporting separation in the banking industry is that traditional banking activities, *i.e.*, deposit-taking and lending, should be kept separate from commercial activities, *e.g.*, owning a manufacturing or other nonfinancial business. The concept is premised on the idea that banks have certain inherent advantages over other private businesses when it comes to raising capital. Customers place their money with a bank because they know that the bank is supervised by a governmental authority and is backstopped to a certain extent by the federal government (*e.g.*, deposit insurance, access to Federal Reserve liquidity). Absent regulation and supervision and a separation regime, the theory is that banks may be incentivized to use customer deposits to support riskier commercial activities that could generate greater returns (and risks) than traditional lending. In short, without a separation regime, these incentives could cause a

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2 In addition to the BHC Act, other separation regimes include the model used to regulate the railroad industry.

3 *See, e.g.*, Linda Khan, The Separation of Platforms and Commerce, 119 Colum. L. Rev. 973 (2019) (arguing that the potential hazards posed by dominant tech platforms could be addressed through separation regimes, and discussing the BHC Act as an example of a separation regime, among others).

4 *See* Elizabeth Warren, Here's How We Can Break Up Big Tech, Medium (Mar. 8, 2019), https://medium.com/@teamwarren/heres-how-we-can-break-up-big-tech-9ad9e0da324c (explaining the need for a regulatory regime that would require a structural separation between a technology platform and other businesses).

5 Investigation of Competition in Digital Markets, Majority Staff Report and Recommendations, Subcommittee on Antitrust, Commercial and Administrative Law of the Committee on the Judiciary, 380 (Oct. 6, 2020), https://judiciary.house.gov/uploadedfiles/competition_in_digital_markets.pdf (citing the Bank Holding Company Act and noting that to "address this underlying conflict of interest, Subcommittee staff recommends that Congress consider legislation that draws on two mainstay tools of the antimonopoly toolkit: structural separations and line of business restrictions. Structural separations prohibit a dominant intermediary from operating in markets that place the intermediary in competition with the firms dependent on its infrastructure. Line of business restrictions, meanwhile, generally limit the markets in which a dominant firm can engage.").

bank to fail to focus on its primary responsibilities to its customers or result in the bank's commercial affiliates exercising an unfair competitive advantage over their commercial competitors.

THE ROLE OF AN EXPERT AGENCY

Establishing and implementing a separation regime, however, is not so easy. Implementation of the BHC Act was, and still is, dependent on a highly sophisticated expert agency, the Federal Reserve Board (the "FRB"), that is familiar with the ins and outs of an increasingly complex banking industry. The FRB's regulation is supported by a deeply talented staff of economists, lawyers, policy professionals and bank supervisors. And, even for this expert agency, the BHC Act has proven difficult to straightforwardly administer, often resulting in the FRB revising its own rules or facing the need to provide interpretive guidance to clarify ambiguities. The lesson of this history may be that implementing a separation regime for a complex industry involves constant calibration and recalibration. Such a regulatory process is never static.

We expect that any separation regime that would be applied to digital platforms would similarly depend on an expert agency to administer the regulatory framework. The structure and form of that agency could take a number of shapes. Although it is not common, there are recent examples of standing up new federal agencies to handle complex and difficult policy issues.[6] As has happened in the past, staff from existing agencies with relevant expertise could be transferred to the new agency.

TRANSPORTABLE ELEMENTS OF THE BHC ACT REGIME

The BHC Act provides examples of key issues and elements that will need to be considered if a separation regime were to be applied to digital platforms. Although a wide range of details and issues would need to be sorted and resolved, key issues and elements from the BHC Act framework that would need to be addressed include: (1) express restrictions on activities or lines of business, (2) a control framework to determine when one company is sufficiently "separate" from another, (3) processes and restrictions with respect to expansionary transactions within the industry, and (4) how the framework applies to U.S. companies operating abroad and to non-U.S. companies operating within the United States.

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[6] The Consumer Financial Protection Bureau, for instance, was established by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Dodd-Frank Act also created the Financial Stability Oversight Council, charged with monitoring risks to U.S. financial stability, among other things.

Activities Restrictions. The BHC Act permits bank holding companies to engage in a limited set of activities, generally only those that are closely related to banking. A bank holding company may also receive a special type of treatment that permits it to engage in activities that are "financial in nature," or complementary or incidental thereto. *De minimis* investments in companies are also generally permitted. Other activities not included in any of the aforementioned categories generally are not permitted.

These activities restrictions work to limit bank holding companies from entering certain business lines. However, similar to the FRB's control framework, these restrictions on activities have given rise to difficult interpretive questions that the FRB has had to resolve over time. When exactly is a bank holding company engaged in an activity? What activities are financial in nature? Under what circumstances should new activities be considered to be permissible for a bank holding company? As innovation takes place, is it possible to analyze new types of business activities under a framework that was adopted twenty years ago?

A principal goal of any separation regime is to limit the lines of business in which the regulated company may engage. For that goal, the BHC Act and its implementing regulations offer a useful rubric. If there is a lesson to be learned, however, it is that no matter how the scope of permissible activities may be defined for a digital platform, there almost certainly will be ambiguities and difficult interpretive questions that will have to be resolved over time.

Control Framework. One fundamental aspect of the BHC Act is its framework for determining when one company is deemed to be affiliated with another. Said differently, this framework is used to determine when a company is sufficiently "separate" from the bank holding company to be outside the regulatory perimeter. The control framework governs all investments and is complex, taking into account a number of factors, such as voting and nonvoting equity stakes, governance and management rights, and business relationships. A regulator, agency charged with enforcement, or case law could develop a similarly complex, and potentially opaque, control framework for determining when there is sufficient separateness between a digital platform and another company.

Expansionary Transactions. There are special rules and review processes that apply when a bank holding company seeks to acquire another bank, bank holding company or financial business. These rules are designed to promote competitiveness, attention to the specific needs of the communities served, the safety and soundness of the relevant banks and bank holding companies, and, for larger transactions, U.S. financial stability, among other things.

Thus, another question is whether any new regulatory framework for digital platforms would need to have a similar process. In addition, what factors would govern regulatory

review of expansionary proposals and what goals they would be designed to promote is of course an important question that we would expect to be debated.

Extraterritorial Application. The BHC Act has complex rules governing how it applies to U.S. firms operating internationally and non-U.S. firms operating in the United States. Presumably, a similar territorial scope would need to be drawn in a framework for digital platforms.

CONCLUSION

Whether and to what extent a new regulatory framework will be enacted for digital platforms of course remains unclear. However, if policymakers ultimately were to implement a separation regime, we believe the BHC Act offers useful and transferrable concepts that give us some sense of the issues that will need to be resolved and will be relevant on an ongoing basis for a new regulatory framework.

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