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Does Disruptive Innovation “Disrupt” Competition Law Enforcement? The Review and Reflection

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Abstract

Disruptive innovation is vital to enterprises' productivity, consumer welfare and national economic growth; however, competition enforcers face formidable challenges. After reviewing the competition enforcement issues concerned with the definitions of markets, unilateral anti-competitive practices and merger controls in relation to disruptive innovation, the relevance of these issues to the competition authorities leads to conclusions along three dimensions. Firstly, even though the disputes like that resulting from the Uber case has demonstrated how great an impact new business models have brought to bear on the integration of competition law and other legal regimes that also affect other public policy purposes, existing competition rules and analytical tools are still of great help in targeting the impugned activities in the disrupted ecosystem, but with certain adjustments being made to the current enforcement methodology. Secondly, in order to preserve the incentives for disruption and avoid unnecessary restraints on innovation, it is necessary to promote competition to both regulators and legislators with a view to keeping markets open, facilitating disruptors, and ultimately benefiting consumers. Thirdly, since disruptive innovation is not easy to recognize, especially within a dynamic digital economy, a sectoral inquiry would be a feasible measure to enhance the enforcer's awareness of modern digital-based markets. This will also further help them remain alert to potential innovation, and finally help them survive the disruption and disruptors.

Keywords: Disruptive Innovation, Innovators, Value Network, Uber, Digital-based Economy, New Business Model.

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1. Introduction

With the era of knowledge-based economy and the emerging information society¹, it is recognized that ideas for innovation can stem from many sources, and can assume any forms. Technology innovation, particularly relating to information technology-associated sphere, has been an essential drive for global economic growth in the past decade. The introduction of smartphones is a classic example of innovative development in mobile communications, not only displacing the prevailing mobile handsets at that time, also bringing tremendous change to our life today. Apple's iPhone and other smart phones using Google's Android system has shaken the incumbent firms' positions and ultimately destroyed their market shares. The successful sales of smart phones ensure the profitability of existing sector within the commodity's value chain including semiconductors, iPhone manufacturers or wifi services providers, etc. But when Apple's revenue declined for the first time in 13 years in the second quarter of 2016, the NASDAQ points were brought down immediately when the news was released. Alongside the profound effects on the industry, smart phones' impacts on today's business lifestyle go further when, by taking advantage of the established networks connecting mobile phones through the Internet and application software (APPs), the creative business models emerge, expand and prevail with incredible forces and speed among commercial communities and consumers globally. Uber and Airbnb are mostly mentioned disruptors of innovative business models in sharing economy². The so-called disruptive innovations have brought the disruptive effects not only on the products or services they have contributed, but also on how the global competition law enforcers respond to this new scenario. It is particularly true when competition law enforcers deal with cases concerning information technology-based knowledge such as computer hardware, computing software, internet, e-commerce, etc. The entailed challenges for competition authorities mostly are, among others, market

¹ For the better understanding of the knowledge-based economy and information society, as well as the interplay between and analyses of information, technology, learning and the modern economic growth, see OECD, *THE KNOWLEDGE-BASED ECONOMY*, OCDE/GD(96)102 (1996).

² For detail explanations of the parameters of the shared economy, see Michael N. Widener, "Shared Spatial Regulating in Shared-Economy Districts," *46(1) Seton Hall Law Review*, 111-187 (2016).

definition, the choice of regulatory tools, survey of harm to competition, and even the determination of whether those conducts investigated are really within the realm of competition law.

In addition to the introduction, this paper will first explore the definition of disruptive innovation which is followed by the brief review of the relationship between competition policy and innovation, then come up with the discussion of market definition under consideration of disruptive innovation, and continue to examine the law enforcement issues concerning anti-competitive conducts and merger review within the context of disruptive innovation, at last provide the author’s personal observations as the conclusion.

2. Defining Disruptive Innovation - The Characteristics of Disruptive Innovation

2.1 Delivering radical changes to the market

When the term “disruptive innovation” was first introduced in the business management academics, the original theory focused on disruptive technologies³. The usage of similar ideas has expanded over time, and today this term can be referred to different kinds of disruptive development including business-model innovations and radical product innovations⁴. Even though there are scholars arguing that the essence of each type of innovation is fundamentally diverse and should not be mixed together⁵, the all-in-one concept of disruptive innovations seems to be prevailing within the context of competition law and its enforcement. For example, at the discussion forum of OECD,

³ Clayton M. Christensen, *The Innovator’s Dilemma: When New Technologies Cause Great Firms to Fail*, Harvard Business School Press (1997).

⁴ Constantinos Markides, “Disruptive Innovation: In Need of Better Theory,” *23(1) The Journal of Product Innovation Management*, 19 (2006).

⁵ *Ibid.* The main grounds for this view, from the perspective of business management, are that the incumbents will face drastically different challenges and the implications for managers are totally different when confronting dissimilar innovations. For example, when we talk about innovations in business model, the suppliers do not provide or invent new products or services, but re-define what the existing products or services are all about or how they are provided. The innovators have to find the key success factors in their ways of doing business activities and attracting customers. But when it comes to product innovations (e.g. cars, television, personal computer, smart phone), the disruptive effects imposed are both on manufacturers and customers; therefore, the innovations are normally driven by a supply push originating from new technology developers.

the idea of disruptive innovations was allowed to include not only products and manufacturing process, but new business models as well⁶. This view may be reasonable because, no matter which kind of innovation is concerned, they share one of the characteristics of disruptive innovations, i.e., delivering radical changes to the market, disrupting or destroying existing markets, and the ultimate concern of competition law and the enforcers are how the actions or activities questioned affect the functioning of relevant markets. The disruption introduced by innovators can either replace the incumbent enterprises (e.g. the displacement of established mobile handset leader Nokia by Apple's iPhone and smart phones using Android system)⁷, or expand the market size, often thanks to digital technologies, by providing competitive goods or services in a new way and attracting consumers to upscale the demand side dimension without inventing new products or services (e.g. Uber, Airbnb, Kabbage). They can also just create new markets by bringing brand new ideas and luring customers to adapt themselves and consume those innovated products or services (i.e. Facebook). In sum, the alteration of markets brought by innovations is dramatic or fundamental but irregular, rather than incremental improvements on products' or services' performance under expectation.

⁶ OECD, HEARING ON DISRUPTIVE INNOVATIONS, DAF/COMP(2015)3, 3-5 (2015).

⁷ *Ibid*, 2.

2.2 Beyond the coverage of traditional value network⁸

The space or circumstance for disruptive innovation to take place is normally outside the value network of established firms. Disruptive innovations introduce a different package of attributes from the one that customers historically value. However, those attributes may not all surpass those the traditional product or services has, but adds values enough of the old features that consumers still need, and draw attention to them. For instance, streaming videos over the Internet provided the possibility of accessing content anywhere, although at the initial stage, streaming performed worse in terms of the traditional value of quality⁹. However, the disruptive innovators are sometimes not the new businesses, but the incumbents themselves. Nestlé disrupted the coffee market, which was already supplied by Nestlé itself and many other brands, with Nespresso, an innovative way of serving coffee drink with capsuled coffee, and changed a lot of people’s habit for preparing their first cup of coffee in the morning.

⁸ In the last several decades, value chain is the traditional concept and tool to understand and portray the chained linkage activities that exist in the physical world within, particularly, manufacturing industry. This concept had helped frame out the way how we recognize the value and value creation in industries. However, within the era of digital economy, as products and services have become digitalization and dematerialization, the concept of value chain seems to be inappropriate. The center of the value chain is the end product or service and the chain is designed around the activities required to produce it. The outputs of upstream suppliers are the necessary inputs for the down-stream firms’ production of goods or services. However, with the value network concept and the reality of network economy, all the players within a network will co-operate or co-create the values. Therefore, the strategic analyses should not limit to the linear relationship between upper level suppliers and the producers at the lower level, but focus on the valuing creating system itself, within which different economic actors, including suppliers, partners, allies, customers, regulators, etc., work together to co-produce values. The crucial defining feature of networks is the complementarity between two or more network components and the node and links between those component networks are essential in order to successfully deliver service over a network. For example, an integrated mobile telecommunications company can be seen as the combination of three functions, e.g., customer relationship business, service and content innovation and commercialization, and infrastructure management. In contrast with the traditional value chain concept, these functions are performed simultaneously rather than sequentially, and mutual adjustments between those segments or components in response to the circumstances outside the network are required. Generally speaking, with the networked economy, analysts emphasize not only the direct relationships between operators and customers, but also relationships between all the members within the network. For more detail explanation, see Joe Peppard & Anna Rylander, “From Value Chain to Value Network: Insights for Mobile Operators,” *24(2) European Management Journal*, 131-133 (2006).

⁹ European Commission, “Competition policy brief - EU merger control and innovation,” 2, April 2016, http://ec.europa.eu/competition/publications/cpb/2016/2016_001_en.pdf, last visited on date: 2016/12/30.

2.3 The Internet

Another prominent feature of today's disruptive innovations, even though not all cases applied¹⁰, is the association with internet-based services. By taking advantage of the Internet, nowadays many disruptive innovations rely on the digitalization of the economy and are, increasingly, platform-based¹¹. As a highly ready-scaled up platform, the Internet owns the quantity of potentially worldwide-based users; therefore the speed of expansion and global penetration are extraordinary, bringing down the cost of reaching and adding additional customers; therefore, making it possible for innovative businesses to grow unprecedentedly fast¹². The combination of the Internet and smartphones seems to be the necessities for the realization of disruption in conventional industries today.

2.4 A market entry strategy

From the perspective of business management, disruptive innovation represents a strategy of market entry, and have made entering into a market much easier, faster and less costly and difficult than before¹³; therefore imposing incredible competition pressure on the market's incumbent firms. There were not too fewer cases that one single-handed firm endangered the market shares of the established enterprises and gained a strong market power. The incumbents have the incentives to respond by taking actions such as retarding the entrance of innovators with unlawful unilateral strategies¹⁴, intervening the process of disruption by way of acquiring the potential disruptor, or proclaiming or lobbying for consistent application of public regulatory regulations on innovators, e.g. Uber vehicles

¹⁰ For example, IKEA's success was not built on its operation on the Internet but on its appeal to customers who are willing to assemble furniture themselves in order to gain the benefit of lower prices. OECD, *supra* note 6, 5.

¹¹ OECD, *HEARING ON DISRUPTIVE INNOVATIONS*, Note by BIAC, DAF/COMP/WD(2015)48, 2 (2015).

¹² OECD, *supra* note 6, 4-5.

¹³ OECD, *DISRUPTIVE INNOVATION AND COMPETITION POLICY ENFORCEMENT*, Note by Alexandre de Stree and Pierre Larouche, DAF/COMP/GF(2015)7, 5 (2015).

¹⁴ These strategies such as predatory pricing, exclusive dealing, etc. may be less successful against disruptive innovators than against those entrants who adopt traditional ways of operation. For example, the conventional movie rental real shops may not have survived the entry of Netflix, which uses technology of streaming on the Internet and provides greater convenience of selecting movies, even if the old style vending shops had invoked the pricing battle on the markets.

versus traditional taxis. All these situations raise certain competition concerns and give rise social debates, which deserve competition authorities to consider on which role and to what extent the competition policy should play. The discussions in next section may not cover all the issues mentioned above, but focus, from the author’s view, on somehow the more competition law significance ones, including the issue of market definition, unilateral anti-competitive conducts, and merger control, and see how the antitrust law enforcement would be like in the ongoing digitalization economy.

3. Competition policy and disruptive innovation

Given the description above concerning the concept of disruptive innovation and those often-cited successful cases like Uber, Airbnb or Facebook, we can see a significant shared feature among them: gathering information through the Internet and the innovative ways of using those information. One thing which can best characterize the competitive digital industry is the intensive and continuous investment in research and development. In the meantime, innovation for new digital platforms and applications is the only force for surviving a firm in such a technologically dynamic market¹⁵. Based on the presumption that more innovation is good for society, the intervention of competition enforcement is supposed to aim at tackle the obstacles to competition, including any possible hindrance for innovation. However, the relationship between competition policy and innovation has been a long-history controversy within the economic academy since Joseph Schumpeter’s writing was first published in 1943¹⁶. Taking the skepticism and negative stand, Schumpeter argued that large firms and monopolists have more incentives for innovation in the view of future possible returns. The opposite theory which takes a positive position toward the relationship between competition and innovation by another economist

¹⁵ Howard A. Shelanski, “Information, Innovation and Competition Policy for the Internet,” *161 University of Pennsylvania Law Review*, 1684-1685 (2013).

¹⁶ Joseph A. Schumpeter, *Capitalism, Socialism & Democracy*, Introduction by Richard Swedberg, <http://cnqzu.com/library/Economics/marxian%20economics/Schumpeter.%20Joseph-Capitalism.%20Socialism%20and%20Democracy.pdf>, last visited on date: 2017/2/20.

Kenneth Arrow emphasized competition as the driver of innovation¹⁷.

Since then, this issue has continuously received attention in economic literature, the conclusion is still unsettled¹⁸. However, after a blanket review of recent literature, the common understanding is that the competition law agencies should *protect the process of innovation* by keeping the market open for potential innovators¹⁹. In other words, which theory we rely on does not truly matter because maintenance and preservation of process of competition is of essence for the achievement of anti-trust law's objective²⁰. Protecting competition, rather than competitors, and ensuring consumers' welfare are the main purposes of competition policy²¹. As explained by one of those scholars, the Schumpeter theory does not imply that antitrust has no role in protecting innovation²² when we notice that the competition agencies in the world have taken measures to ensure the efforts for disruptive innovation is not impeded by dominant firms²³. Furthermore, by refocusing on innovation effects in targeted types of industries and practices, the competition enforcement can really promote innovation²⁴.

4. Market Definition and Disruptive Innovation

Defining the market concerned or clarifying the market structure is crucial in order to

¹⁷ Kenneth J. Arrow, "Economic Welfare and the Allocation of Recourses for Invention," *The Rate and Direction of Inventive Activity: Economic and Social Factors*, Princeton University Press, 609-626 (1962). Chapter URL: <http://www.nber.org/chapters/c2144>, last visited on date: 2017/2/19.

¹⁸ Pilar Beneito, Paz Coscollá-Girona, María Engracia Rochina-Barrachina & Amparo Sanchis, "Competitive Pressure and Innovation at the Firm Level," *63(3) The Journal of Industrial Economics*, 423 (2015).

¹⁹ OECD, *supra* note 13, 5.

²⁰ This views had long been proclaimed by the EU's Court of Justice or the General Court in the settled-case rulings, *see* Joined Cases C-501/06 P, C-513/06 P, C-515/06 P and C-519/06 P *Glaxo-SmithKline Services Unlimited v. Commission* [2009] ECR I-09291, para. 63; Case T-201/04 *Microsoft v. Commission* [2007] ECR II-3601, para. 664. As the result of antitrust enactment in Taiwan, Taiwan's Fair Trade Act declares in its Article 1 the purposes of this law including maintaining trading order, protecting consumers' interests, ensuring free and fair competition, and promoting economic stability and prosperity.

²¹ The general debate and transformation of the goals of EU competition law, *see* Ioannis Lianos, *Some Reflection on the Question of the Goals of EU Competition Law*, Center for Law, Economics and Society (CLEs), Working Paper Series 3/2013 (2013).

²² OECD, *supra* note 13, 6.

²³ Howard A. Shelanski, *supra* note 15, 1692-1701.

²⁴ Jonathan Baker, "Beyond Schumpeter vs. Arrow: How Antitrust Fosters Innovation," *74 Antitrust Law Journal* (2007).

decide whether the measures taken by the firms on the market are anticompetitive or not. Market definition is particularly of relevance within the context of disruptive innovations since one of the disruption’s distinctive characteristics is its capability to “disrupt” the existing market and destroy the incumbent firms. However, this seemingly accustomed task for competition authorities in their usual investigation procedures has become more challenging due to the facts that, first, competition laws originally emphasizes the static inefficiency on the market resulting from cartel or unilateral anti-competitive behaviors, paying less attention to the effects of innovations, and, second, with disruptive innovation, competition takes place at the level of market definition²⁵. Consequently the already defined market does not remain constant through the analysis but fluctuating, the calculation of overall market power and the assessment of the competitive effect are hardly conclusive. The rise of Uber demonstrates what the situation is envisaged when the new pattern of ride services emerge *vis à vis* the current competition law system.

4.1 The Uber case in Taiwan

4.1.1 Background

Uber maintains a platform for fulfilling the function of matching drivers and riders via a specific smartphone app. Uber operated this service model first in San Francisco in 2010 and now are in more than 50 countries in the world. In Taiwan, the categories that Uber had registered for operating its network here include business consultancy, data processing, third-party payment, etc. but not vehicle-for-hire service. Uber does not recruit its own driver employees but invites the intending car owners to apply and register as Uber drivers after satisfying a certain conditions set by Uber. The pricing of the Uber ride is surging, depending on how hard it is for the successful matching of supply and demand, and sometimes consumers pay 10 times the usual rate. Uber has never deemed itself as a traditional taxi company, and, of course, it had never received a license required for operating a transportation company in Taiwan.

²⁵ OECD, *supra* note 13, 6.

The Uber's novel business model has been deemed as one of the representative disruptive innovations and marked the era of so-called sharing economy. Its matching platform, by utilizing the widespread Internet and smartphone technologies and creating a separate marketplace, enables numerous driving service suppliers (normally are individuals or small entities) and consumers efficiently complete the transactions and brings benefits to the consumers. However, analogous to the situation in other countries, Taiwan's legal system imposes on traditional taxi onerous rules to comply for the sake of consumers' safety or labor conditions, such as the need of a driving license, a commercial plate and compulsory insurance for the customers, and the driver's background check, etc., which means a more frequent and detail inspection by the government while Uber has obviously skipped most of them or has just fulfilled some of them at a less severe scrutiny level²⁶ due to, as Uber itself has constantly asserted, its platform characteristics and the pattern of business operations²⁷.

4.1.2 The Accusation of Uber's unfair competition

After Uber's rapid expansion in the world including Taiwan and continuing loss of customers and transaction opportunities under the competitive pressure from Uber, many individual occupational drivers, in association with the automobile transportation organizations, protested and claimed that Uber had unfair competitive advantages, because the latter was not subject to the same regulatory restrictions and obligations such as limited number of licenses, price control, etc. and therefore urged the government to undertake enforcement actions intensively. The governmental agency in charge of motor vehicles administrative management in Taiwan is the Directorate General of Highways (DGH), Ministry of Transportation and Communications. The DGH enforces transportation laws

²⁶ Benjamin Edelman, "Whither Uber?: Competitive Dynamics in Transportation Networks," *11(2) Competition Policy International*, 13-22 (2015).

²⁷ The similar battles across the EU countries on whether Uber should be treated as a transportation service or merely as a digital platform has heated and culminated when the European Court of Justice took up this landmark case, referred by a Spanish judge, and Uber appeared before the Court on November 26, 2016. The ruling is not expected before March 2017 at the earliest. Mark Scott, "Transportation or Digital Platform? Classifying Uber in Europe," *The New York Times*, B1 (2016/11/28).

and regulations which aim at saving public interests and serve legitimate policy objectives. After having considered all the circumstances of this controversy and having consulted other related authorities, the DGH fined Uber up to NT\$150,000 for each offense and mandated to suspend its operation according to paragraph 2, Article 77 of the Highway Act²⁸ ²⁹. The DGH also fined the Uber drivers in several cases on the same grounds. After a series of administrative appeal procedures, many of those pecuniary decisions were appealed before Taiwan’s High Administrative Court, seeking the annulment of those punishments and prohibition. Following the examination of the facts concerned and the provisions applied in those specific cases, the High Administrative Court revoked the DGH decisions, declaring that, with regard to the business suspension order, the DGH had wrongly subjected the merits of those cases under the application of the Highway Act, neglecting the fact that the business of Uber in Taiwan is focused on management consultancy and data processing services, etc., but not automobile transportation³⁰ ³¹.

4.1.3 Re-define the market

Obviously, the views held in those rulings were neither within the spectrum nor from the perspective of competition law, consequently without using any tools of market definition and measurement of market power. The court’s decision in favor of Uber apparently has, to a certain extent, reflected the unsuited application of traditional antitrust

²⁸ Paragraph 2, Article 77 of the Highway Act: “Those who manage an automobile ... transportation enterprise without applying for sanction under this Act shall be fined ...The highway authorities should also coercively suspend the business, distrain the license plates of illegally operating vehicles..., or revoke the proprietor’s owned vehicle license plates.”

²⁹ Due to the alleged violation taking place at a variety of locations, as of today there were more than 280 cases, in which Uber was repeatedly fined by the DGH from NT\$ 10,000 to 150,000 for each breach of law.

³⁰ Concerning the other issue of the appeal, i.e. the decision of fine, the High administrative Court had also rebuked DGH’s decision on the legal bases of violating the principle of “*clear and definite*”, which is set out in the Article 5 of the Administrative Procedure Act. *See* the Judgment of Taipei High Administrative Court 2015, Sù Tzu No. 868.

³¹ In several other occasions, DGH had also parallel fined the Uber drivers, by invoking the same article and clauses, i.e. paragraph 2, Article 77 of the Highway Act, based on the established facts that they had managed automobile transportation enterprises without applying for sanction in advance. Not surprisingly those decisions had been brought to the High Administrative Court for appeal. With regard to the issue of Uber driver’s status in the law suits concerned, in favor of the DGH’s finding, the Court has repeatedly confirmed in its decisions that the Uber drivers are occupational and running the transportation business to gain fiscal interests for themselves. *See* the Judgments of Taipei High Administrative Court 2015, Sù Tzu No. 1022 and No. 1396.

analytical methodology in such a disruptive business model. More illustrations for understanding the concept of “competition taken place at the level of market definition” are as following.

Starting from a separate market---

It is noticeable that Uber started up on a market which is basically different from or outside of that of traditional taxi ride. Uber’s service-providing pattern (based on the idea of shared economy and smartphone plus apps are must), the employees’ expertise or technologies required, and the properties needed for operation, etc. are so distinctive from the traditional taxi ride and, therefore, Uber can be seen as standing on another relevant market.

Value-added services---

In addition to the customers’ satisfaction for delivery, which is the overlapped value that the traditional services and the innovative ones can provide, Uber presents added values such as convenience and certainty of knowing a taxi will arrive, better vehicles, multiple choices of cars, most of the time, cheaper fare, etc. Arguably, from the perspective of consumers, Uber’s app-based ride service and traditional taxi may be interchangeable in term of the ultimate intended use, the separate value network on which the disruptor dwells and takes center stage has been created, even though both two value networks or relevant markets overlap on a certain proportion of low-end customers.

Shifting and re-defining the relevant market ---

Due to successfully attracting consumers a lot enough and shifting them from the existing taxi market to the separate new one, the ecosystem of the business or the industry has been altering, the post-disruption market may be redefined. After the eruption of market disruption by Uber, the market position of incumbent firms and the competitive efficiency needs to be re-examined³².

Adaptive analyses needed ---

The disruptive business model like Uber draws the attention of competition agencies to

³² Alternatively, we may keep the backdrop of original definition of market constantly through the whole process of analyses; nevertheless, the incumbent firm’s position is overall less significant. OECD, *supra* note 13, 6.

consider if there is a need for adaptive analyses. From the explanation above, we can see the boundary of competition is fluctuating; in other words, the market(s) in the case at hand is dynamic and evolving. In order to properly value the real competition efficiency of the relevant market, it is suggestively plausible, turning from the traditional methodology of defining the static relevant market, to emphasize the survey of enterprises' market conducts and also call for the innovative theory of harm within a broader scenario. In other words, the enforcers need to focus their analyses on whether the incumbents have taken anti-competitive conducts aiming at preventing potential disruptors from marketing-shifting or widening the overlap of lower-end value network, rather than on if the existing enterprises' practices actually have the effects of raising the costs for new entry and therefore foreclosure the market as ordinarily defined³³.

4.2 The latest development of the Uber controversy in Taiwan

Taiwan's competition authority, the Fair Trade Commission (FTFC) has taken a careful stance toward the Uber controversy and has not formally launched an anti-trust investigation, making its position on this dispute still unveiled. The latest decision FTFC had made on Uber was to fine Uber NT\$ 1 million for the violation of Article 21, Taiwan's Fair Trade Act, on the grounds of false advertisements and misleading people to believe that sharing one's own spare car and providing ride services without vocational license are not against the law, and wrongfully proclaiming that being Uber driver could make them gain more income³⁴. Obviously, the FTFC took advantage of the tools it held for tackling unfair competition, rather than for anti-competitive practices.

The controversies continue to evolve. Taxi drivers had kept vigorously pushing the government to directly encounter the fact of “unfair” competition by Uber and reform of transportation management system. The latest development in Taiwan is that, after reviewing taxi regulations and considering the fairness of competition between taxi drivers with Uber, the central government transportation authority reiterated its control policy and

³³ *Ibid*, 6-7.

³⁴ Decision of the Fair Trade Commission, Kung Ch'u Tzu No. 105065.

insisted on that Uber is not allowed by law to hire unlicensed drivers to offer services. In the meantime, the transportation authority has proposed to Taiwan's parliament an amendment to the Highway Act, which would increase penalties for illegally providing taxi riding services to up to NT\$ 25 million, of course, invoking Uber's response saying that "innovation is threatened by proposed bill, and it sends a signal that Taiwan is fearful of or disregarding innovation of technology"³⁵. The revisions have now been approved by Taiwan's law-making body, the Legislative Yuan³⁶, and it is expected to come into force soon in a wake of the necessary executive procedures.

4.3 The author's comment on Taiwan's Uber case

It is true that Uber is now a non-negligible existence which has aroused the debate over to what extent the government should deploy regulatory measures on Uber and Uber's drivers in order to, on the one hand, maintain the "fair competition" between traditional taxis and Uber riding services, and, on the other hand, safeguard the incentives for potential innovators to undertake risky, expensive process of creating innovative products or services and preserve opportunities for those new competitors to enter the market, which ultimately secure consumers' substantial benefits. Competition enforcers should carefully balance those competing considerations and avoid unnecessary or excessive regulations. From the author's perspective, facing the dynamic market(s) and the need for adaptive analyses in Uber case, the entry of Uber has actually enhanced, rather than reduced, the competition in the vehicle-for-hire market. Raising entry barriers or increasing cost for operation, e.g., the regulatory measures associated with high penalties such as the proposed Highway Act amendment mentioned above, will just deter the realization of any disruptive innovation, which is one of the key economic drivers that we need most. As the competition authority in Taiwan, TFTC should take the initiative for competition advocacy, urging other regulators refraining from adopting unduly restrictions which have the foreclosure effect and consequently protect incumbents but not

³⁵ Lauly Li, "Innovation is threatened by proposed bill: Uber," *Taipei Times*, 4 (2016/12/7).

³⁶ "Fines for illegal transport services raised," *The China Post*, 15 (2016/12/17).

competition itself³⁷ during the process of transition caused by disruptive innovation. The newly enacted requirement demanding the app-based ride company like Uber must obtain a commercial transportation license and register as a transportation company before their operations would be unnecessary and inappropriate, ignoring Uber’s distinctive feature of innovative sharing economy on platform.

The author also supports taking advantage of regulatory measures to protect consumers’ safety or to serve other legitimate goals pursued by the laws and regulations concerning transportation, but they should be tailored to suit the features and the mechanism that the Uber-like platform sharing economy presents. The practical reality is that many jurisdictions, such as California and other different levels of government in the US, have taken actions to regulate transportation network companies and their drivers and carefully crafted those regulations, which Uber described as “smart regulations” to accommodate the new industry³⁸. That means it would be possibly workable and acceptable by both the regulatory authority and Uber to enact, through negotiations, in order to regulate the ride-hailing services and properly incorporate the innovative economic activities on platform into our stifled economy. This is just the way that several our neighboring Asian countries like the Philippines, Singapore, Australia have currently undertaken.³⁹

5. Anti-competitive Conduct and Disruptive Innovation

Most of the anti-competitive cases relating to innovation associate with incremental ones, so that we are not surprised to find there are not many disruptive innovation cases dealt with by competition agencies so far. Based on the rationale of re-defining and shifting the market described in section III, the incumbents intend to mothball disruptive

³⁷ The US Federal Trade Commission holds the similar stance toward how lawmakers and regulators should response to the disruptive innovation like Uber’s business model and help shape the inevitable transition caused by disruptive innovation. OECD, *HEARING ON DISRUPTIVE INNOVATION-Note by United States*, Directorate for Financial and Enterprise Affairs Competition Committee, DAF/COMP/WD(2015)54 (2015).

³⁸ US Federal Trade Commission, *The “Sharing” Economy, Issues Facing Platforms, Participants & Regulators*, An FTC Staff Report, 72 (2016).

³⁹ Matthew Fulco, “Will Taiwan Share in the Sharing Economy?” *46(12) Taiwan Business TOPIC*, Cover Story, 20 (2016).

innovations, prevent them from emerging and stop them reshaping the market. By way of approaching the customers of existing companies, innovators gain the niches, compete vigorously or ultimately force out the incumbents. Hence the established companies may have the incentives to impede disruptive innovation by taking unilateral strategies such as predatory pricing, several forms of vertical restraints including exclusive dealing, or the difficulties of patent licensing. Those practices are aimed at intercepting the interface or making it more difficult for the disruptors to access to customers, and finally deterring away potential disruptors. Normally the more dominant power a firm presents on the market, the more likely incentive it has to prevent the disruptor from emerging into the market; therefore, the market position of an established firm is especially relevant for making the case of the anti-competitive conduct relating to disruptive innovations.

The most remarkable example elaborating the protection of disruptive innovation by anti-trust action is the *Microsoft* case. In its decision in 2004 confirming the violation of Article 82 (now Article 102 of the Treaty on the Functioning of the European Union), the European Commission established that Microsoft held a quasi-monopolistic position on the personal computer (PC) operating system market, and had abused its dominant position by tying Windows Media Player to its Windows PC operating system, reducing competition in the relevant markets, thereby preventing innovations and choices and bringing the substantial detriment to consumers. The Commission's decision confirmed that Microsoft prevented innovative server products from being brought to the market, and that competition in the streaming media player market was distorted⁴⁰. Based on the similar legal and economic grounds in the previous Microsoft case in 2004, in 2009 again, the Commission further challenged Microsoft, stating that, by tying Windows with Internet Explorer, which is the product on a very different market, the Internet browser market, Microsoft made Internet Explorer available on 90% of the world's PCs, shielding Internet Explorer from competition with other browsers, and preventing Netscape from executing a disruptive innovation strategy, which is ultimately detrimental to the pace of product innovation^{41 42}.

⁴⁰ Commission Decision of 24 March 2004, Case 37792, *Microsoft*.

⁴¹ Commission Decision of 16 December 2009, Case 39430, *Microsoft (tying)*.

The most recent case which could be seen as an imitated version of the Microsoft case is Google’s strategy to make mobile device manufacturers pre-install Google’s mobile operating system and applications. The European Commission, by sending Statement of Objection, informed Google and its parent company, Alphabet, its preliminary view that Google has abused its dominant position by imposing restrictions on Android device manufacturers and mobile network operators. According the Commission’s investigation, smartphones and tablets account for more than half of global internet traffic, and are expected to account for even more in the future. About 80% of smart mobile devices in Europe and in the world run on Android, the mobile operating system developed by Google. The Commission considered that Google enjoyed a dominant position, respectively, in the markets for the general Internet search services, the licensable smart mobile operating system and app stores for the Android mobile operating system, generally holding market shares of more than 90% in each of these markets in the EU. Google obliged manufacturers who use Android for their devices to pre-install Google’s proprietary apps, including Google Search, Google Chrome, and Google’s app store for Android, Play Store. Google also prevented device manufacturers from selling smart mobile devices running on competing operating systems based on the Android open-source code, and provided financial incentives for them to do so. The Commission concerned those conducts would introduce the elimination of possible competition from competing mobile browsers and operating systems, then a further consolidation of the dominant position of Google Search in the general Internet search services, finally stifling innovation on apps and services in the wider mobile space, and causing harm to consumers⁴³.

Google’s practices have managed to leverage its market power in the operating system market to those of browsers and other smartphone-used apps. This case, again, shows that the dominant established company, once being able to foresee the possible tract

⁴² In 2002, TFTA had initiated the investigation, actively or by complaints, on Microsoft cases in which the facts and issues covered were more or less similar with those in EU. However, the official and formal decisions had not been made and the procedures were eventually closed by way of contracting an administrative agreement between the TFTA and Microsoft, after accepting the commitments offered by Microsoft.

⁴³ Commission Decision of 20 April 2016, Case 40099, *Google Android*.

of disruptive development, may execute the strategy to render the possible innovation more difficult.

6. Disruptive Innovation and Acquisition

In addition to unlawful unilateral practices, established firms may deploy the strategy of buying out potentially innovative rivals to avoid any possible realization of innovation. Normally the target gains its foothold on the market which is not the same one as the incumbent exists, if we use the traditional methodology to delineate the market; in other words, they are on separate relevant markets or on different value networks. So the incumbent firms may deem the threats imposed by the target standing on another market are potential; nevertheless, the real goal of the target is not to enter into the existing market but to create one or re-defined the market where it takes central stage, by way of accessing the customers on the original market and shifting them to another value network. Once the established enterprises have detected the intention of and the threats from disruptors in another market, they may take actions to prevent the potential disruptor from re-defining the relevant market, rather than from foreclosing it. One of the incumbent firms' choices in response to the disruptive innovator is to acquire it before the disruptor comes to the market or becomes visible. This situation imposes challenges of competition analyses on authorities in the context of a merger review.

Firstly, when the acquisition and merger takes place, the potential disruptors may be still small and, consequently, the quantitative thresholds for notifying the authority for approval such as the amount of turnover or market share are not yet satisfied and hence the notification is not needed. It is reasonably possible that the acquisitions and mergers with high potential/low turnover targets which could be harmful to innovations have been realized without prior scrutiny. Facebook's acquisition of Whatsapp in 2014 is a case in point. The Facebook/Whatsapp transaction attracted media's attention in part due to the US\$19 billion paid for a company with the annually global turnover of only around 10 million euros, which is far below the threshold required for the EU Commission's jurisdiction. In addition to the prominence of those two parties involved in this acquisition,

and in light of the growing importance of digital services in Europe and the huge amount of users across the EU, this merger raised competition concerns exceeding many transactions which do fall under the preview of competition agencies⁴⁴. The inevitable solution for this might be amending the rules of games and provide new thresholds specifically designed for the application of acquisition and merger cases involving potential disruptors. One suggested complementary threshold is, in addition to the turnover, based on the value of the transaction. Because the value of the disruptor may be high, and the cost for the procurement may reflect the importance and financial reward of the innovation in the future, thus buying a low turnover firm with a high price might be an indication of harm to innovation and deserves careful examination^{45 46}.

Another related concern is that, even the transaction has been subject to the survey for approval, the agencies may be short of the ability to recognize the possible innovation and have only limited vision to factor the innovation into analyses. The two prominent competition law regimes at both sides of the Atlantic, the EU and the US, have not segmented disruptive innovation from innovation in their respective merger control rules. They have not either particularly defined what a disruptor⁴⁷ is in the context of merger and acquisition, nor given a clear guide on how to assess the effects of innovation in a merger review. Therefore, it is seemingly like that the test generally applied for assessing mergers can be used in the cases involving acquiring a disruptive innovator. In other words, the core issue is all about how to assess the effects of merger and acquisition on innovation, regardless what type of the innovation it is. For example, based on a test of significant

⁴⁴ Eleonora Ocello, Cristina Sjödin & Anatoly Subočs, “What’s Up with Merger Control in the Digital Sector? Lessons from the Facebook/WhatsApp EU merger case,” Competition merger brief 1/2015, European Commission, 2 (2015).

⁴⁵ OECD, *supra* note 11, 9.

⁴⁶ Drawing from this experience, the German competition authority suggested in 2015 applying a size of transaction threshold to encompass acquisitions involving start-ups with low revenue at the time they are bought. Bruno Lasserre, “New business models and competition enforcement: must we ride the tide of change?” *11(1) Competition Policy International*, 27 (2015).

⁴⁷ For instance, the EU2004 Horizontal Merger Guidelines states at para. 41: ...a ‘maverick’ firm that has a history of preventing or disrupting coordination, for example by failing to follow price increases by its competitors, or has characteristics that gives it an incentive to favour different strategic choices than its coordinating competitors would prefer. Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, *Official Journal*, C 31, 5-18(2004). Those definitions of a maverick in the Guidelines are supposed to be broader than a disruptive innovator.

impediment of effective competition/substantial lessening of competition (SIEC/SLC), the EU's Merger Regulation⁴⁸ provides the substantive standard for merger assessment which is covering all aspects of a loss of effective competition including harms to consumers resulting from hampering innovation. If anti-competitive effects of a merger have been established, the Merger Regulation also acknowledges that efficiencies gained from innovation can offset the harm. Those efficiencies put forward by the emerging parties should be beneficial for consumers, merger-specific, i.e. they can only be attained through the merger, and can be verifiable⁴⁹. The effects-based approach and careful analyses, on a case-by-case basis against the dynamic relevant market, can help the agencies discover the incentive or ability of merging parties to increase prices afterward even lack of dominance⁵⁰. However, the rationale⁵¹ has always raised the doubt that accurately ascertaining the plans or purposes of the acquiring firm at *ex ante* stage of a merger is not always possible. The evidences gathered to reflect the acquiring firm's intention should be crucial and definite⁵².

7. Relevance to competition authorities

7.1 The usability of competition law

It goes without saying that the disruptive business models or the so-called platform economy have brought certain challenges for competition law enforcers on the analyses, *inter alia*, of market definition, assessment of market power and even theory of harm as discussed above. Someone would suggest if there is the need for a new set of competition regulations targeting the disruptive operators like Uber. From the author's view, based on

⁴⁸ Council Regulation (EC)N0 139/2004 of 20 January 2004 on the control of concentrations between undertakings, *Official Journal*, L 24, 1-22 (2004).

⁴⁹ OECD, *THE IMPACT OF DISRUPTIVE INNOVATIONS ON COMPETITION LAW ENFORCEMENT*, Contribution from European Commission, DAF/COMP/GF/WD(2015)39, 3 (2015).

⁵⁰ Bruno Lasserre, *supra* note 46, 27.

⁵¹ The European Commission has implemented this pattern of analyses in on innovation-related cases spread in a variety of industry in recently years, *see* European Commission, "EU merger control and innovation," *Competition policy brief*, 4-7 (2016), http://ec.europa.eu/competition/publications/cpb/2016/2016_001_en.pdf, last visited on date: 2016/12/30.

⁵² OECD, *supra* note 13, 11.

previous observations, even the Uber-like market players may be unique enough to arouse enforcement conflicts in different countries, the loose definition of disruptive innovation or a broad category of firms appearing on certain platforms does not necessarily make them stay out of the radius of traditional competition law. One main theme shared among law enforcers in the world is that safeguarding the welfare and benefit for consumers inducing from disruptive innovation is important. Hence, competition law, with its universal common principles and legal concepts, and the nature of case-by-case approach, provide a satisfactory basis for competitive analyses only if the enforcers are always mindful of protecting the incentives of innovation in each stage of analytical framework, including the step of market definition and competitive effects evaluation. By way of taking into account various possible sources of competition, i.e., the competitive dynamics, usually coming from outside the conventional antitrust markets and bringing disruption over the existing markets and eco-systems, as well as developing the insights, based on enforcement experiences, into the possible ways of impeding disruptive innovation, the competition authorities may find the existing competition law tools, if properly applied, still effectively useful⁵³.

7.2 Advocacy to the public and regulators

It is commonly agreed that innovations, including disruptive innovations, are of importance for a country’s competitiveness, and how to survive the incentives for innovation has become crucial when the global economies had kept going slump in recent years. Advocacy for a more reasonably regulatory system and raising awareness of the benefits of competition are always the alternative that competition authorities can have. If we consider the principle of anti-trust law, i.e. protecting process of competition rather than protecting competitors, it tends to come to the view that seeking to enforce existing unnecessarily anti-competitive regulations on innovators would impede further evolution of disruption and ultimately harm the interests of consumers. What the incumbents have

⁵³ OECD, *supra* note 11, 6.

actually done, such as requesting the government by the traditional taxi drivers to treat Uber like a transportation company and force it to comply with the transportation regulations in order to protect their positions, is to prevent the competitor (Uber) from competing with them and, consequently, restricts competition. From the perspective of competition policy, this approach which is currently deployed by our DGH and the Ministry of Transportation and Communications, would be improper for the materialization of over-all public interest. Alternatively, the agencies should take opportunities for advocacy to public and to regulators in order to facilitate disruptors.

As to the advocacy to regulators, the experience of the US Federal Trade Commission (FTC) is of value for reference. Under the state action doctrine in US, state authorities have immunity from federal anti-trust laws if the actions taken are pursuant to a clear state policy but have anti-competitive effects. In this situation, the FTC would not have any mandate to take enforcement action, but by taking advantage of any forms of recommendations to the state legislators, suggesting them to ease the restrictive regulations like what the FTC did in Tesla motor dealer case^{54 55}. As the only competition authority in Taiwan, TFTC, when facing the Uber unresolved controversy, is at the appropriate position to take initiative and assume the task, either within the executive administration or before legislators during the drafting or review processes, to diffuse the importance and benefit of competition laws and try to exert certain influence on the enactment or the manner in which the regulators would enforce the regulations. It is especially worthy because the stakes for consumers in the context of disruptive innovation-related economy tend to be bigger.

⁵⁴ Tesla Motors came into the US automobile market with a potentially disruptive model by opening its own showrooms and selling cars directly to consumers through the Internet; i.e. Tesla sells cars without dealers. The incumbents and dealers required some of the US states to enforce old regulations to ban Tesla's direct sales. The rules for selling automobiles in US and the discussion of Tesla's distribution controversy, see Daniel A. Crane, "Tesla and the Car Dealers' Lobby," *Law & Economics Working Papers*, Paper 101 (2014).

⁵⁵ "FTC Staff: Missouri and New Jersey Should Repeal Their Prohibition on Direct-to-Consumer Auto Sales by Manufacturers", Press Release, 2014/5/16, <https://www.ftc.gov/news-events/press-releases/2014/05/ftc-staff-missouri-new-jersey-should-repeal-their-prohibitions>, last visited on date : 2016/12/30.

7.3 Considering the feasibility of Sector inquiry

It is undeniable that a clear analytical framework is desirable when competition authorities have cases involving innovations at hand. But it is also the reality that competition authorities may be short of the ability to sense possible existence of innovation due to few precedents and lack of experiences, and, in turn, limit their visions to take innovation into account properly. From the author’s view, competition authorities need to understand in-depth the whole picture of the environment in which the incumbents and the potential disruptors may come into and co-exist. We can see that modern technological developments are mostly associated with computers, the Internet, electronic communications, mobile apps, and accumulation of big data, etc. and those related segments are integrated into a layered hierarchical ecosystem and have formed into a continuously expanding value network, where the most possibility of disruptive innovations would take place. This feature has characterized the digital economy or platform business models today. For the purpose of improving enforcers’ knowledge in modern technologies and backdrops of the cases under investigation, and better understanding the interplay between information technology and competition law, a sector inquiry or a market investigation would be suggestively feasible. The results of the inquiry would help competition officials acutely grab the sense of disruptive innovation, and develop workable tools to make precise diagnose in a specific case at hand on those issues such as market definition, measurement of market power and theories of harm in line with the ongoing digitalization trend. Two European prominent competition law agencies, the authorities from Germany and France had reportedly cooperated in investigating the relation between big data and competition law and concurrently studied the results of the inquiry⁵⁶. France itself also launched a full sector inquiry into data-related markets and strategies in May 2016. The author personally suggests that TFTC may consider to plan out a suitable inquiry into the related sectors or industries in Taiwan, as part of the

⁵⁶ Autorité de la concurrence & Bundeskartellamt, “Competition Law and Data,” 10th May, 2016, <http://www.autoritedelaconcurrence.fr/doc/reportcompetitionlawanddatafinal.pdf>, last visited on date: 2016/12/30.

preparation for future enforcement on the cases involving disruptive innovation.

8. Conclusion

While it is commonly understood that disruptive innovation is vital to enterprises' productivity, consumer welfare and national economic growth, the challenges faced by competition enforcers are real. Even though the dispute like Uber case has demonstrated how much the impact that the new business models have brought on the integration of competition law and other legal regimes bearing some other public policies' purposes, we believe that the existing competition rules and the analysis tools are still of great help to target the impugned activities on the disrupted ecosystem, but with a certain of adjustments on the current enforcement methodology concerning market definition, theory of harm, threshold for merger control, and competition effect assessment, etc. In order to preserve the incentives for disruption and avoid unnecessarily anti-competitive restraints on possible innovation, the competition advocacy by competition agencies to regulators and legislators is needed with a view to keeping market open, facilitating disruptors, and ultimately benefiting the consumers. Disruptive innovation is, by its nature, not easy to be recognized, especially within the complicated environment of digital economy, a sectoral inquiry would be a feasible measures to enhance enforcers' awareness of modern digital-based markets, further help them keep alert on potential innovation, and finally survive disruption and disruptors.

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論破壞性創新與競爭法之執行—回顧與前瞻

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摘要

破壞性創新於事業之生產力、消費者利益以及國家經濟成長至關重要，然而也對競爭主管機關的執法帶來挑戰，無論是市場界定、個別事業採取的反競爭行為，或在結合管制等議題上，都可能因為破壞性創新的存在，就執行方法或競爭效果評估上予以調整的必要。以 Uber 案的爭議為例，可充分說明所謂新商業模式對競爭法以及其他負有各類公益目的的法律間整合，形成何等的衝擊，惟本文認為，只要在方法上作出必要的調整，現行競爭法規及其分析工具在面對破壞性創新對產業生態系造成的影響時，仍具其有效性。此外，為保存創新的動機與誘因，避免不必要的限制而抑制創新，競爭主管機關應主動對立法者與社會大眾進行競爭倡議，說明市場開放以及協助創新者的必要，以便最終使消費者獲利。由於破壞性創新的本質就是不易被察覺其可能的存在，在複雜的數位經濟環境下尤為如此，本文認為，發動對數位經濟相關產業的調查，可提升主管機關認識當代以數位為基礎的產業現況，協助他們對潛在的創新保持警覺，有助於保全破壞性創新的發展。

關鍵詞：破壞性創新、創新者、價值網絡、Uber、數位經濟、新商業模式

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