

FAANGs –biter bitten

April 2018



The 'FAANGs' are once more in the news. Facebook, Apple, Amazon, Netflix, and Google's parent company Alphabet are in the spotlight once again, as anxious investors watch their stock prices suffer collateral damage from revelations around Facebook's data management practices and the alleged shadier purposes of third parties linked to Cambridge Analytica.

US tech sell-off bites

Investors' fears of much greater regulation and scrutiny of industry-wide practices are probably well-founded, and the markets seem to agree. The NYSE's 'Fang+' index tracks the following ten tech companies' stocks: Facebook, Apple, Amazon, Netflix, Google, Alibaba, Baidu, Nvidia, Tesla, Twitter. The NYSE Fang+ index hit a year's high on 12 March this year at 2770.53 points, falling precipitously to 2382.89 just over a fortnight later on Wednesday 28 March. More than \$42 billion was wiped off Facebook's stock price in the immediate wake of the CA scandal, though it has since recovered some ground. Good questions are now being asked of tech giants about how they handle customers' data, but if their answers continue to be found wanting then others will seek to answer those questions for them. Enter stage left, the regulators, closely followed by politicians.

Two weeks after the Observer broke the story on the Cambridge Analytica scandal, where data from more than 70 million Facebook users' profiles was alleged to have been 'harvested' and used without proper permission by third parties in the 2016 US election, the US Federal Trade Commission announced 26 March 2018 their investigation of Facebook due to 'substantial concerns

about [their] privacy practices'. There may be fines to pay of the order of billions of dollars if the company is found to be in breach of a 2011 settlement with the FTC.

'The wicked flee when no man pursueth' – Proverbs 28:1

In the UK, the enforcement of data regulation falls to the Information Commissioner's Office, who issued the following statement on 24 March:

"The warrant to inspect the premises of Cambridge Analytica was executed at 20.00 on 23 March 2018. Our investigators left the premises at about 03.00. We will now need to assess and consider the evidence before deciding the next steps and coming to any conclusions. This is one part of a larger investigation by the ICO into the use of personal data and analytics by political campaigns, parties, social media companies and other commercial actors."

It appears that the ICO had to wait four days for the warrant to be executed, as the Information Commissioner Elizabeth Denham appeared to confirm on Channel 4 news on Tuesday night (20 March) that a warrant had been applied for but at that time had not yet been granted.

Matt Hancock, Secretary of State for the Dept of Digital, Culture, Media & Sport, in a recent Commons debate on the passage of the Data Protection Act that brings the EU's GDPR into UK law said:

"It is increasingly clear that we need a new settlement with these big tech companies. There is no doubt that the Data Protection Bill currently before this Parliament takes us significantly forward....there is clearly huge benefit for both the rest of the EU and the UK in having a strong, rich and deep relationship in terms of how data are transferred, but as the evidence of the past few days has shown, that must be done on the basis of strong data protection."

A war on two fronts

Following these recent developments, the debate around tech companies and their impact upon society (for good or ill) has crystallised around two things: how tech companies handle our data (and who uses it for what purpose), and where they pay tax, too. Is a war on two fronts brewing?

In response to a written question about putting a value on the gain to the taxpayer from introducing revenue-based taxes on multinational companies from veteran MP Frank Field, Chair of the Work & Pensions Commission, Mel Stride, Financial Secretary to the Treasury answered:

"The UK applies value-added tax to businesses' supplies of goods and services to UK consumers. Corporation tax is imposed on a business's profits relating to value generated through UK activities. The government continues to support the principle that a multinational group's profits should be taxed in the countries in which it generates value. It does not, for example, believe that the profits of a business that undertakes all of its activities in the UK should be taxed in overseas markets in which the business's goods and services might be sold.

The UK Government has set out its receptiveness to exploring interim measures with like-minded countries, like a tax on revenues, to tax certain digital businesses which generate value from UK users. That would be designed to compensate for unrecognised user-created value pending wider reform of the international corporate tax system. The yield from such a tax would depend on its scope, rate and detailed design."

Nobody wants to drive the golden goose from its nest, much less slay it, particularly when many thousands of jobs depend upon it. However, when that goose's offerings are more hen's egg-sized, it is inevitable that politicians and regulators will take a much closer look.

Regulation with teeth

The European Commission however, has already bared its teeth, with the Commissioner for Competition Margrethe Vestager going after Google for \$2.8 billion in fines for breaching anti-trust rules (starting with the Foundem case), and Apple for \$15.3 million in back taxes which the the Irish Government is expected to collect.

In her TED talk from September 2017 - 'The New Age of Corporate Monopolies' – Vestager explains why markets need clear rules, and how even the most innovative companies can become a problem when they become too dominant. "Real and fair competition has a vital role to play in building the trust we need to get the best of our societies," Vestager says. "And that starts with enforcing our rules."

Vestager's five year term as the EU's Competition Commissioner is due to come to an end in 2019. She confirmed in January that she was seeking a second term with the Commission, and has made no secret of her wish to retain the competition portfolio. Whilst many commissioners have remained for a second term, they rarely retain the same portfolio for consecutive terms of office.

Cook v Zuck

Tim Cook, CEO of Apple, was last month asked by MSNBC what he would do if he were in Mark Zuckerberg's shoes. His reply – 'I wouldn't be in this situation' – provoked Zuckerberg to remark that Cook's comments were 'extremely glib and not at all aligned with the truth'. Cook, as per Jobs before him, insists that Apple is not and has never been interesting in monetising their users' data. Almost all of Apple's revenues (some \$229 billion in 2017, compared to \$24 billion just ten years prior) are made by selling undeniably beautiful and practical hardware, rather than data for advertisers to use.

Whilst these two companies find themselves lumped in the same index (much to Cook's apparent chagrin), they do operate on rather different business models. Apple make tangible, physical products - with Facebook the user's data is the product (and they don't get paid for it). What started out as an online college yearbook has morphed into a giant global corporation with 2 billion active users. Zuckerberg's defence: 'If you want to build a service which is not just serving rich people, then you need to have something that people can afford...at Facebook, we are squarely in the camp of companies that work hard to charge you less and provide a free service that everyone can use' would hold far more water if only the company had been clearer from the start on what they and their commercial customers do with their users' data.

Facebook's business model was certainly the main focus of the US Congress' marathon five-hour session with Zuckerberg on 10 April, with one commentator's likening of this to Zuckerberg '...explaining colours to cats' (certainly there were a few people in that room for whom cookies are something that their grandchildren eat with a glass of milk). However, the chair of the Senate commerce committee expressed the view that 'for this model to persist, both sides of the bargain need to know what's involved'.

Apples & oranges

Is this the ages-old clash between manufacturing and new-fangled service industries simply re-cast for the digital age, pitching an industry veteran against an entrepreneurial young 'upstart'?

Cynics amongst us might say that Cook is simply trying to put some clear blue water between Apple and Facebook, in order to dampen down 'contagion' between the two stocks' share prices – quite rightly, from the point of view of the Apple stockholder, be they an employee or an external investor. Is he merely trying to immunise Apple against catching Facebook's flu or does he have a broader point – when we compare Facebook with any of their tech index cohorts, are we actually comparing apples with oranges?

Data for good

One of the saddest things about the current furore is that it casts a lengthy shadow over the more noble purposes to which Facebook's power can be directed. Used properly, Facebook data CAN do huge amounts of good in society – it can even save lives. Take for example, their 'Data for Good' division. Since 2014, this Facebook division has worked with aid groups such as UNICEF, the Red Cross and the World Food Programme in disaster zones to provide near real-time maps of users' geographic coordinates, allowing for a more coordinated, timely and targeted deployment of life-saving aid. 'Disaster Maps' has been deployed during more than 100 worldwide crises over the past year, including hurricanes Harvey, Irma and Maria, the California wildfires and a volcanic eruption in Bali, to name but a few.

Cometh the hour, cometh....GDPR

The EU's General Data Protection Regulation comes into force on 25 May 2018 across the European Union, but due to its scope the effects of this legislation will be felt supranationally. Six long years in the making, GDPR will have a big impact on how we in the share plans world use employee data for the most benign of practices around share schemes management, and many of our plan issuer members are immersed in preparation for these changes. The language of privacy notices, mapping of data management practices, understanding the changes in legal liabilities and responsibilities between data processors and data, and of course the rights of the data subject too, must all be considered. Subject Access Requests now have to be responded to within a month and the old £10 fee can no longer be charged – a cottage industry in the making, but who will end up bearing the cost of compliance? The slightly better news seems to be the emergence of consensus around the use of relevant personal data in connection with share plans on the lawful basis of 'legitimate interests' and in some circumstances to fulfil contractual obligations. For a 101 on consent and other GDPR myths, the ICO's blog is a good place to start:

<https://iconewsblog.org.uk/2017/08/16/consent-is-not-the-silver-bullet-for-gdpr-compliance/>

Evolution or revolution?

So what next for tech giants, especially Facebook? Some might suggest: play fair – not fast and loose - with your customers' data, give back to society on a meaningful scale, and pay fairer taxes...or else face even greater regulation which will do serious damage to your revenue models, as well as your stock price. Others will feel that voluntary improvements to data management practices, and efforts in tackling trolling, hate-speech and fake news (the very worst elements of our global online society) have all been too slow and rather half-hearted in the face of commercial expedience.

Should social media users be able to pay to keep their data private, opting out of adverts, tracking etc? Will a more ethically-driven alternative to Facebook emerge and gain traction fast enough with early adopters in order to mount a serious, scale-able challenge to Facebook's global supremacy?

Can Facebook actually make changes to its business model sufficiently and quickly enough to ward off the threat of regulation? At the Congressional hearing, one senator cut to the chase: '...if you and other social media companies do not get your act in order, none of us is going to have any privacy any more. If Facebook and other online companies will not or cannot fix the privacy invasions, then we are going to have to'. Many would argue that the horse has already bolted (and is somewhere over the metaphorical hill) regarding privacy, but regardless, the second part of that senator's statement is the company's key challenge for the foreseeable future.

Asked if he would embrace regulation, Zuckerberg said 'If it's the right regulation, then yes'. It remains to be seen who gets to define what form the 'right' regulation will take, at least in the US.

A handwritten signature in black ink, appearing to read 'G Stopp', with a long horizontal flourish underneath.

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