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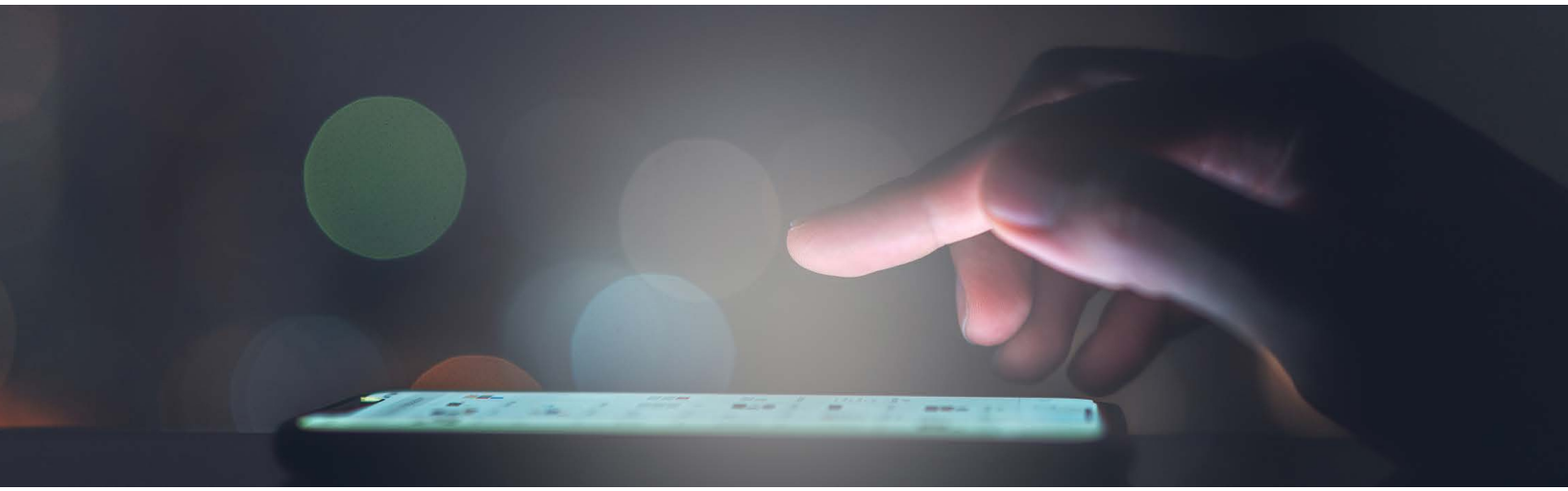

The Platform Economy

by Anuj Saush, Mark Fenwick, and Erik P. M. Vermeulen

A significant development in the global economy over the last two decades has been the emergence of businesses that organize and define themselves as "platforms." A platform is any organization that uses digital and other emerging technologies to create value by facilitating connections between two or more groups of users. Some platforms facilitate connections between the buyer and seller of goods (Amazon) or between those wanting a service and those willing to provide it (Uber). Others simply facilitate connections (information exchange) between friends (Facebook). While platforms have grown to become some of the largest companies in the world, they have struggled to maintain their initial promise and have raised concerns about privacy and anticompetitive business practices. Brands that were once disruptive have lost much of their shine. The result is that many people are now deeply ambivalent about platforms. Nonetheless, the potential of digital technology presents an opportunity for companies to consider platforms as part of a hybrid business model. This report provides an overview of the platform economy, introduces the concept of a "sustainable platform," and provides insights on managing platforms in the long term.

Insights for What's Ahead

The platform model is disrupting traditional economic theories based on organizations, firms, and markets. The Internet, algorithms, online ratings, and artificial intelligence provide instant access to all kinds of information with minimal effort, offering new opportunities for firms to bind users to their platform, set up partnerships, and engage in constant innovation across multiple sectors of the economy. The success of platforms across diverse industries shows the enormous disruptive power of this new way of operating a business.

Platforms can be a source of competitive advantage, and companies may want to consider them as part of a hybrid business model. In 2019, seven of the 10 most valuable companies globally were based on a platform business model.[1] As platforms continue to grow and become a major force across industries, many incumbent organizations (e.g., Siemens, Vorwerk, etc.) have responded by reexamining a part of their business models to integrate platform strategies and investing in capabilities for platforms. Engaging with platforms can be a prerequisite in the time to come. Companies can start by reiterating parts of their business model to transition from products/services to platforms.

There is more to a successful platform than simply leveraging networked digital technologies. A successful platform must acquire and retain users, underscoring the importance of creating an open, inclusive, and responsible community. Platforms also need to create a strong culture and a flat organizational structure to enable growth. Lastly, platforms operate in a hypercompetitive market characterized by exponential technological growth—highlighting the need to innovate continually and pursue multipartner collaboration.

Regulatory activity related to platforms is expected to increase. The legal framework to govern platforms is evolving. While many jurisdictions currently have no legal frameworks to monitor or regulate platforms, more regulations are expected in this area. Most notably, the forthcoming EU Digital Services Act seeks to create a framework for the supervision of platforms to ensure effective enforcement. In the United States, Google faces a set of lawsuits brought by federal and state antitrust regulators. Companies should keep abreast of emerging regulatory trends and self-regulate to proactively meet stakeholder expectations before the law requires it.

The "best" approach to manage a platform depends on the individualized circumstances of a particular business model and its goals. Every firm, considering any form of platform, must analyze its own needs and aim to find the unique recipe to maximize opportunities for sustained growth while upholding its responsibilities to the society and environment.

1 See: Jennifer Schenker, "The Platform Economy," The Innovator, January 19, 2019.

The Rise of the Platform Economy

Platforms use digital and other emerging technologies to create value by facilitating connections between two or more groups of users. The type of connection varies depending on the platform. Some platforms facilitate connections between the buyer and seller of goods (Amazon) or between those wanting a service and those willing to provide it (Uber). Others simply facilitate connections (information exchange) between friends (Facebook). However, what all these platforms have in common is that they make connections between value creators and value extractors. The platform generates a profit from making these connections, either by taking a commission or advertising. Table 1 highlights the diversity of the platform model.

Table 1

Platforms and their users

Platform Type	Examples	User Group 1 *(creators)*	User Group 2 *(extractors)*
Exchange Platform	*Amazon, Alibaba*	Producers of Goods	Consumers of Goods
Service Platform	*Airbnb, Uber*	Service Providers	Service Users
Content Platform	*YouTube, Medium, Netflix*	Content Creators	Content Consumers
Software Platform	*Apple iOS, Google Android*	App Developers	Smartphone Users
Social Platform	*Facebook, Instagram*	Friends	Friends
Investment Platform	*Priceland, OpenTable*	Investor	Businesses
Smart Contract Platform	*Ethereum*	Contract Party 1	Contract Party 2

The remarkable success of platforms has been made possible by the emergence of a number of interconnected digital technologies—most obviously, PCs and smartphones, the internet, algorithms, and cloud computing. The mass dissemination of these technologies encourages more users and other service providers to join a platform, adding more so-called content which, in turn, attracts additional content creators and consumers.

> Platforms benefit enormously from network effects; the more people that use a platform, the more it benefits everyone.[2]

2 See: Nirmala Reddy, "How to Harness the Power of Network Effects," Forbes Coaches Council post, January 2, 2018.

Moreover, the global proliferation of digital technologies and communication networks means that platforms can be established anywhere. The emergence of hugely successful platforms in China (Alibaba) or Indonesia (Gojek) illustrates the universal appeal and adaptability of this business model. The diversity and adaptability of platforms mean that they can be attractive in any sector of the economy—not just tech companies—all over the world, not just in more developed economies.

The success of platforms has forced many incumbent organizations to reexamine a part of their business models and pursue platform projects. Many traditional retailers, for example, are shifting their products' distribution channels from physical stores to online platforms. The automotive industry is transitioning to connected cars and autonomous vehicles. Many industrial organizations now wish to reinvent themselves as platform service providers rather than remaining producers of goods. The intersection of the digital and physical provides companies an opportunity to innovate and build platforms.

German-based industrial company Siemens AG is pursuing several platform projects where it combines the physical and the digital worlds to create insights and business value for mutual benefits. For example, Railigent—its software-as-a-service platform—uses railroad sensors to monitor and connect activity data to run assets at full 100 percent availability and detect failures before they occur.[3] B2C companies are also venturing into the platforms.

Vorwerk—an international diversified corporation and maker of Thermomix—released a modernized Thermomix in 2014, which came with a chip allowing users to find recipes on the device itself. The digital connection and Internet of Things (IoT) allowed Vorwerk to offer additional services to its customers as well as reinforce the community, and initiate partnership with delivery companies to deliver ingredients. And, more recently, as new fintech startups are moving into the financial services sector, many incumbent banks are considering how to introduce platform services.[4]

> "Platforms are nonlinear, they're networked, and the highest value lies outside the firm. We have to train people on platform ecosystems. We all have to relearn business models and revamp our culture."
>
> Dr. Roland Busch Deputy Chief Executive Officer and CTO, Siemens

Platforms are disruptive and can offer strong potential of growth. Companies should consider deploying platforms as one of the possible business growth strategies. However, many executives are ambivalent about platforms. Given the potential of platforms, it makes sense to deepen the understanding of this new business form and explore how platforms can be managed responsibly.

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3 "Platforms Adapt to Survive," MIT Initiative on the Digital Economy Platform Strategy Summit 2020, October 2020.

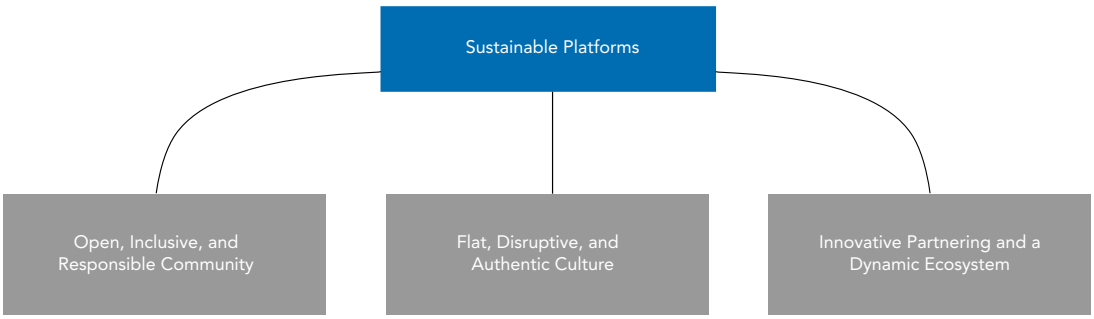
4 See: "A Vision for Platform-Based Banking," EY, 2018.

Characteristics of a Sustainable Platform

There is more to a successful platform than simply leveraging networked digital technologies to facilitate connections and adopting a leaner and more agile type of organization. We have identified three characteristics that make up a sustainable platform. While not many platforms may achieve this ideal, the goal of becoming and then remaining a sustainable platform will maximize the chance of continued relevance and positive brand image. Considering these characteristics will also help overcome the challenges and risks that may arise: unfair practices of online platforms vis-à-vis their clients or customers—no redress in case of problems; dissemination of illegal content online, such as incitement to terrorism, illegal hate speech, material, infringements of IP rights; abuse of dominant position; and misuse of online platforms by malicious actors to spread disinformation, affecting democratic participation.[5]

Figure 1

Characteristics of a Sustainable Platform



Source: The Conference Board

Open, Inclusive, and Responsible Community

To operate effectively, a platform must acquire and then retain users, and to do that it needs to be open to user feedback. A distinctive feature of a platform business strategy is its relative dependence on retaining and leveraging stakeholders' input and feedback to improve the user experience and, therefore, promote engagement with the platform.

A successful platform consequently needs to build and maintain an active and healthy community, ensuring a sustainable relationship between the platform and its participants. A successful platform needs to make the shift from a closed system to a more open community or ecosystem, and the effect of this pressure is the blurring of the distinction

5 "How Do Online Platforms Shape Our Lives and Businesses?" European Commission, February 25, 2021.

between the inside and outside of the organization. There is a strong incentive for platforms to institutionalize open dialogue and communication with its users and other stakeholders.

The smarter platforms understand that communication is not a one-way process of information disclosure (from platform operators to platform users) but, instead, requires a more engaged, responsive, and open process that encourages a mutually productive dialogue. In such circumstances, the tight control of information characteristic of (closed) companies becomes a high-risk strategy.

Flat, Disruptive, and Authentic Culture

Culture is an important element or component of a platform. In a digital age, the culture of a business cannot be concealed. Sooner or later, it becomes visible and determines how consumers perceive products or services. As such, culture is no longer distinguishable from the product but is part of it. And if the culture is "wrong" in some way, users and consumers are much more likely to reject a firm's products and migrate to rivals.

The stronger the culture, the less corporate processes and procedures are needed. Processes and procedures can,over time, kill creativity and distort the organizational culture. Constant dedication to identifiable core values is essential in building and maintaining an authentic culture. To create such a culture of genuine entrepreneurship, trust, freedom, and responsibility, a business must identify and then live by a set of core values in all its decisions and operations. The culture needs to become an authentic, lived manifestation of these core values.

Hierarchies and procedures need to be replaced by flatter structures, and a "best idea wins" culture. Employees in search of a meaningful career experience are not willing to passively accept the view of managers and will move somewhere else if the organization does not afford opportunities to contribute to their personal growth. In this way, a flat hierarchy works to retain the relevance of the organization for employees and other company insiders, as well as for the consumers who benefit from the higher-quality products or services that such a flat culture produces. Of course, creating flatter organization structure is a challenge for all organizations today, but it is a particularly pressing issue for organizations operating as platforms.

Innovative Partnering and a Dynamic Ecosystem

All platforms operate in hypercompetitive global markets against a background of exponential technological development, fast-moving business developments, and continuously evolving consumer demands. This operating environment creates a constant pressure on platforms to evolve their business model. Simple tweaks to existing platform services are not going to be enough to survive in the medium to long term. Indeed, if one looks at any of the major platforms, one can see a constant expansion in platform services.

However, the delivery of innovation over the long term is never smooth and requires a higher degree of cooperation between multiple actors both inside and outside the firm. Platform evolution requires gathering disparate elements (of hardware and software)

and integrating them into a coherent product that delivers a value proposition that has relevancy for platform users. This task of gathering, identifying, coordinating, and combining diverse elements require high levels of cooperation both within the platform and also with external partners.

A platform's capacity to build and maintain inclusive relationships in which partners work collaboratively together will become crucial. From this point of view, the existence of hierarchies or "silos" with entrenched interests becomes enormously counterproductive, as platforms that fail to embrace the possibilities of a more inclusive style of partnering will struggle to innovate.

Partnering for innovation in this way also involves rethinking the external boundaries of the platform to include actors that are not generally thought of as being part of the organization, but who nevertheless have a crucial bearing on decisions and actions. In particular, the list of inside actors should be expanded beyond the traditional list of executives, managers, and employees. Key stakeholders now include the early adopters and other key opinion leaders within the platform community, but also research centers, universities, and start-up companies. Traditionally, such actors have been conceptualized as being on the outside, or peripheral to a large company, but the need for inclusive partnering means that such metaphors are no longer appropriate given the increasingly central role that such actors play.

Managing Platforms and Navigating New Legal Risk

While the regulatory construct may not develop as fast as the platforms, platforms still need to abide by the rules applying to companies and act responsibly, despite the less defined setup. A well-governed platform must be responsive and prioritize agility over control while providing a framework to ensure compliance. Given the fast-changing environment in which platforms operate and the dynamic nature of platforms, companies need to explore a management structure that is more dynamic, responsive, and experimental.[6] The "best" approach to manage a platform depends on the individualized circumstances of a particular business model and its goals. Every firm, considering any form of platform, must analyze its own needs and aim to find the unique recipe to maximize opportunities for sustained growth, while upholding its responsibilities to the society and environment.

EU Digital Services Act

The legal framework to govern digital services in the EU has remained unchanged since the adoption of the e-Commerce Directive in 2000—but no longer. The "Digital Services Act" package seeks to create a modern system of cooperation for the supervision of platforms to ensure that platforms behave fairly with consumers and their competitors, and guarantee effective enforcement.

Policy Package	Policy Actions
Enhanced consumer protection and common e-commerce rules	1. Fair and transparent contract terms and general conditions for business partners and consumers 2. Reinforced minimum information requirements for commercial communications 3. Increased transparency of commercial communications 4. Extension of scope of the e-Commerce Directive to service providers from non-EU countries 5. Limitations on intrusiveness of advertising
Creation of a framework for content management and curation that guarantees the protection of rights and freedoms	1. Clear and standardized notice-and-action procedures to deal with illegal and harmful content 2. Enhanced transparency on content curation and reporting obligations for platforms 3. Out-of-court dispute settlement on content management, particularly on notice-and-actions procedures
Specific regulation to ensure fair competition in online platform ecosystems	1. New horizontal rules in the Platform to Business Regulation for all digital platforms 2. Creation of a specialized body to reinforce oversight of the behavior of systemic platforms 3. Creation of specific ex ante rules that would apply only to systemic platforms to ban or restrict certain unfair business practices
Cross-cutting policies to ensure enforcement and guarantee clarity	1. Clarification of key definitions 2. Clarification of liability exemptions for online intermediaries 3. Establishment of transparency and explainability standards and procedures for algorithms 4. Measures to ensure enforcement

6 Mark Fenwick and Erik P. M. Vermeulen, "Regulation Tomorrow: What Happens When Technology Is Faster Than the Law," *American University Business Law Review, 2017.*

Foundations for effective platform management

- **Adopt an organization-wide perspective**. Some companies delegate platform business management to a technology committee. While this arrangement may work, it is necessary that the technology committee and leadership team do not view platform management in isolation. Creating a sustainable platform is not limited to a particular function; it touches different parts of the organization (governance, human capital, marketing, product development, legal, and strategy). An organization-wide platform management approach can help companies realize the full potential of platforms since it allows complete visibility. The objective is not to have control but to have a centralized decision-making committee to evaluate ideas against the strategic priorities. Companies need to invest in educating boards and senior executive teams on platforms as this will enable them to oversee risks and opportunities.
- **Seek to understand unintended consequences**. Companies must strive for a comprehensive understanding of the potential implications including unintended consequences (e.g., downstream harm due to biased-data practices, dilution of workers' rights over time). For example, a study of around 1,000 executives across industries in Europe and the United States found that only about half the companies have policies and procedures in place to identify and address ethical considerations—either in the initial design of artificial intelligence (AI) applications or in their behavior after the system was launched.[7] Platforms may or may not involve AI application, but companies do need to ensure that they apply an ethical lens to platform management.
- **Strengthen self-regulation.** Platforms, in Europe, will likely be subject to due diligence obligations and face increased transparency obligations, increasing their compliance costs and complexity of their oversight. Like many other environmental, social, and governance issues, it is likely that other jurisdictions may follow with regulatory interventions for platforms. Companies in other jurisdictions should seek to strengthen and adopt self-regulation to help them prepare for forthcoming standards and regulations and meet stakeholder expectations.

We are heading into a future where more and more companies are likely to embrace platforms as part of their business model. While the platform may offer growth opportunities, companies need to tread this journey carefully.

This publication is based on "A Sustainable Platform Economy & the Future of Corporate Governance", written by Mark Fenwick and Erik P.M. Vermeulen.

7 J.P. Gownder, Poornima Ramaswamy, James Jeude, and Jerry A. Smith, "Making AI Responsible—And Effective," Cognizant (video), 2018.

About the Authors

Anuj Saush leads the sustainability research practice for The Conference Board Sustainability Center in Europe. He started his career as an environmental consultant, focusing on strategy, innovation, and compliance, and then transitioned into corporate sustainability roles, where he has the experience of leading and delivering sustainability strategy, supply chain, circular economy, and social enterprise programs. Anuj's previous roles include positions at the international professional services firm, PwC, and with the low-carbon energy group, EDF.

Mark Fenwick is a Professor of International Business Law at the Faculty of Law, Kyushu University, Fukuoka, Japan. His primary research interests are in the fields of business regulation in a digital age, and disruptive innovation and the law. Recent publications include *New Technology, Big Data & the Law* (Springer, 2017, co-edited with Marcelo Corralles and Nikolaus Forgo); *The Shifting Meaning of Legal Certainty in Comparative & Transnational Law* (Hart, 2017, co-edited with Stefan Wrbka and Matthias Siems); *Robotics, AI and the Future of Law* (Springer, 2018, co-edited with Nikolaus Forgo); *International Business Law: Emerging Fields of Regulation* (Hart, 2018, co-authored with Stefan Wrbka); *Smart Contracts, Blockchain & the Law* (Springer, 2019, co-edited with Marcelo Corrales and Helena Haapio); and *Smart Contracts: Technological, Legal & Business Perspectives* (Hart, 2021, co-edited with Marcelo Corales and Stefan Wrbka). He has a PhD in law from the University of Cambridge and has been a visiting professor at Duke University, Hong Kong University, Shanghai University of Finance and Economics, the National University of Singapore, Tilburg University, and Vietnam National University.

Erik P.M. Vermeulen's work can be broken down into three categories. First, Erik is a Professor of Business and Financial Law and the Director of the International Business Law program at Tilburg University in the Netherlands. He teaches business organizations and governance, law and technology, and business innovation and finance at Tilburg Law School, TIAS School for Business and Society, and at other universities around the world. Erik has appeared at numerous conferences as a featured or keynote speaker. Second, Erik works at the intersection of the academic and corporate worlds. He is a Senior Legal Counsel at Signify (formerly known as Philips Lighting). He works on corporate matters, mergers & acquisitions, and reorganizations. Third, Erik can be described as a content creator. He has a blog at erikpmvermeulen.medium.com, where he shares insights into how emerging technologies are creating new opportunities across all areas of the economy and society. In our fast-changing world, Erik revisits long-held assumptions and theories, and seeks to develop new models more appropriate to the next normal. He is a top writer in innovation, education, and gaming on online publication platform Medium.

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THE CONFERENCE BOARD, INC. | www.conferenceboard.org
AMERICAS | +1 212 759 0900 | customer.service@conferenceboard.org
ASIA | +65 8298 3403 | service.ap@conferenceboard.org
EUROPE, MIDDLE EAST, AFRICA | +32 2 675 54 05 | brussels@conferenceboard.org
COMMITTEE FOR ECONOMIC DEVELOPMENT
OF THE CONFERENCE BOARD | +1 202 469 7286 | www.ced.org
THE CONFERENCE BOARD OF CANADA | +1 613 526 3280 | www.conferenceboard.ca

PUBLISHING TEAM
EDITOR Babette Plessers
GRAPHICS Maria Cristina Rueda
DESIGN Marja van de Bunt