

MFN Clauses and Antitrust Enforcement and Policy
U.S. Department of Justice and Federal Trade Commission
10 September 2012

Price relationship agreements in the UK and EU: a retail-MFN enforcement gap?

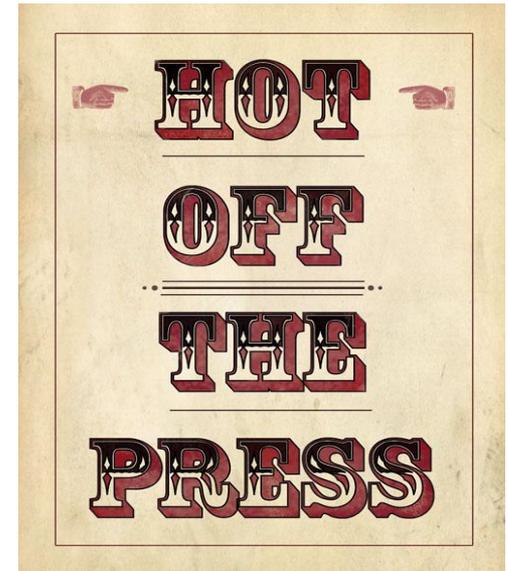
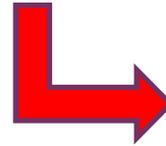
Nelson Jung
Director
Office of Fair Trading

The views expressed are personal and should not be taken as representing those of the Office of Fair Trading.

Today's lunchtime menu

- Starter

- *'Can "fair" prices be unfair?'* A report on Price Relationship Agreements by LEAR published today(!)



- Entrée

- UK/EU cases
 - Hotel online booking
 - E-books
 - Other UK and EU cases

- Desert

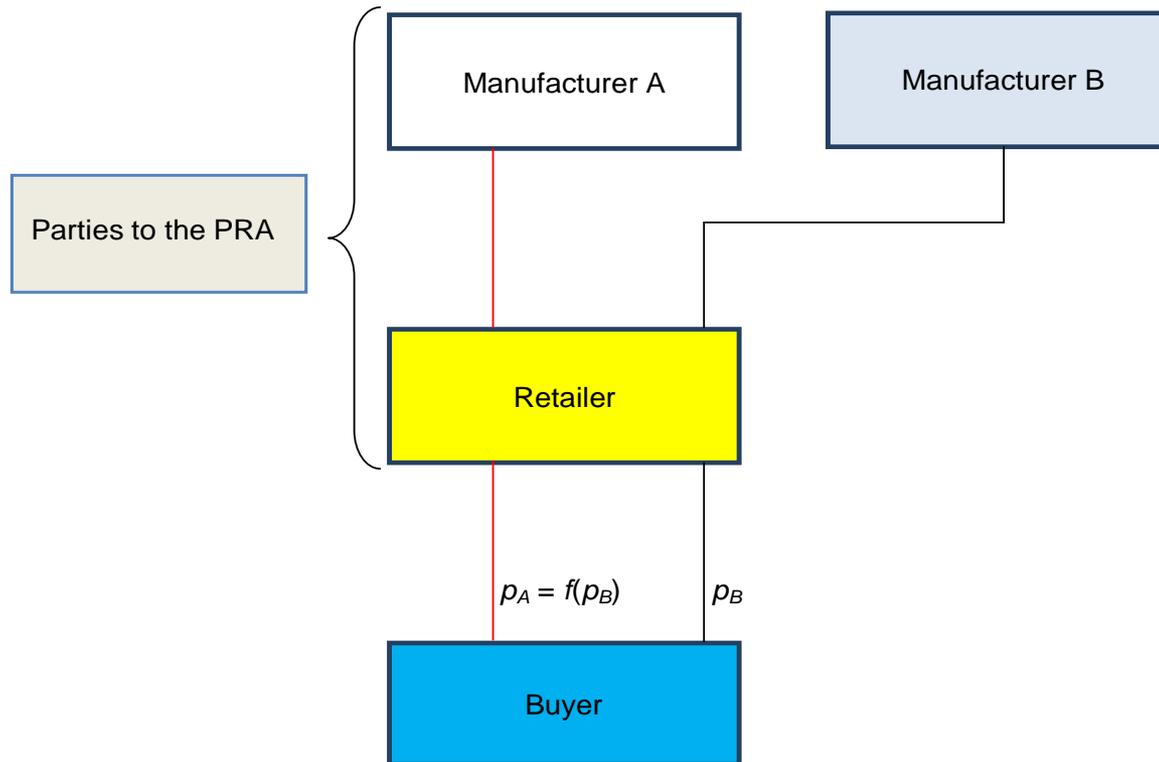
- Pricing relativities agreements, RPM and retail-MFNs - similar harm, different legal treatment? Is there a 'retail-MFN enforcement gap'?

Price Relationship Agreements

- **LEAR report covers different categories of Price Relationship Agreements (PRAs)**
- **Across-sellers PRAs**
 - Promise made by a seller to its customers that if a customer finds a competitor offering a lower price for the same product, it will match that lower price. This promise may be either in an advertisement, or embedded in a long-term contract.
- **Across-customers PRAs**
 - Contractual obligation on a seller to offer to a customer the best price it offers to any other customer during a specific period of time (wholesale-MFNs)
- **Third-party PRAs**
 - ➔ **Pricing relativities agreements**
 - Retailer undertakes to set the price at which it resells manufacturer A's products with reference to the price at which it sells the products of manufacturer B
 - ➔ **Across-platform parity agreements (retail-MFNs)**
 - Requires the seller to sell a good or service on a platform at a price that is not higher than the price the seller charges on other platforms

Pricing relativities agreements

- Retailer undertakes to set the price at which it resells manufacturer A's products with reference to the price at which it sells the products of manufacturer B
- Restriction of retailer's ability to independently set its *relative* retail prices



Effects of Pricing Relativities Agreements

● Potential effects of Pricing Relativities Agreements

- May affect competition inter-brand competition between manufacturers and intra-brand competition between retailers of the same manufacturer

'Despite the fact that pricing relativities agreements are different from RPM agreements, we believe that some of the findings that the economic literature has reached on the latter apply also to the former'
(paragraph 6.15 of the LEAR report)

● Theories of harm

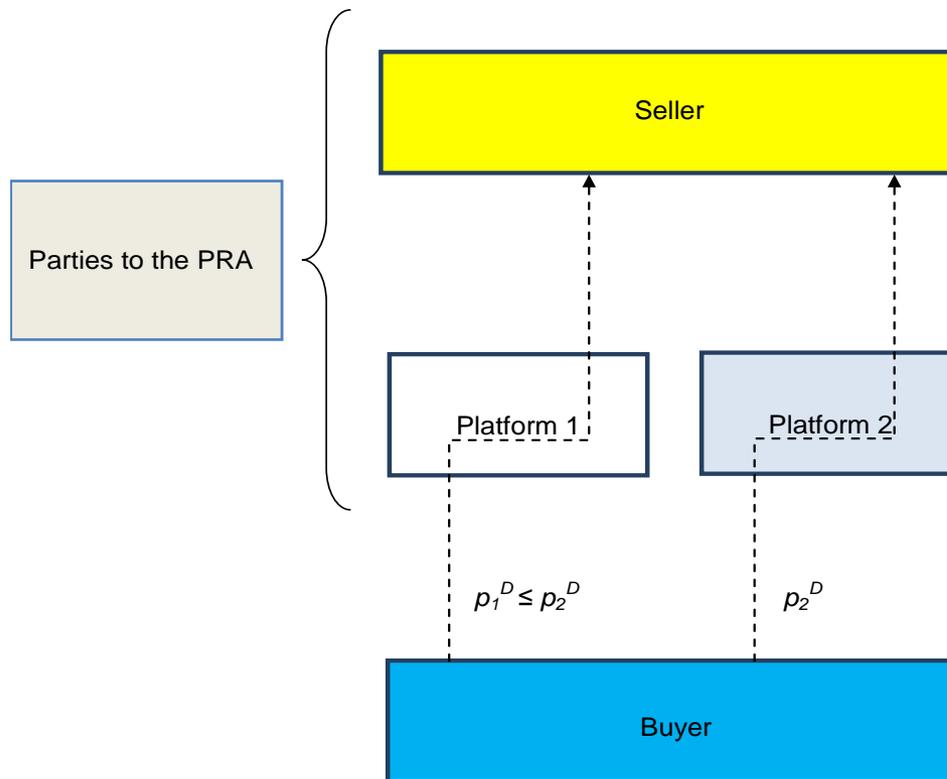
- may facilitate collusion upstream if they improve price transparency (as with RPM).
- May soften competition upstream – competing manufacturers may refrain from adopting aggressive pricing policies.
- May give rise to market foreclosure – may be credibly used to implement a limit pricing strategy that discourages entry if the pricing relativity applies to new entrants
- May soften intra-brand competition – circumstances in which a price reduction would be profitable for a specific manufacturer's product but unprofitable if a PRA requires lowering a competing product's price as well; also impacts on retailer's ability to use one manufacturer's product as a loss leader

● Potential efficiencies

- Could potentially mitigate double marginalisation BUT not clear that it would be effective at all – if at all, it would generally be less effective and more restrictive of competition than RPM
- May address free-riding issues in certain circumstances

Across-Platforms Parity Agreements (retail-MFNs)

- Requires the seller to sell a good or service on a platform at a price that is not higher than the price the seller charges on other platforms



Effects of Across-Platforms Parity Agreements

● Potential effects of Across-Platforms Parity Agreements

- Price of goods or services on platform is defined in relation to the price charged on other, competing platforms
- Platforms serving as intermediaries, prevalent in the online world
- Not exclusive to online world: 'real world' example could be shopping mall requiring retailers not to price goods below the price charged at the shopping mall at any other retail presences

● Theories of harm

- May foreclose effective entry of other platforms – sellers are prevented from charging lower prices on a new platform that would be prepared to charge the seller a lower transaction fee; reduces ability of new platforms to attract buyers and sellers; entry may be prevented if new entrant is more efficient than incumbent(s)
- May soften competition between platforms, thereby increasing the fees paid by the sellers and, as a consequence, the prices charged to customers - customers buying from the platform with the lower transaction fee to some extent subsidise customers buying from the platform with higher transaction fees, which lowers the incentive of platforms to reduce transaction fees
- May facilitate collusion between platforms – if platforms set collusive fees to sellers, the advantage of deviating by reducing the sellers' fee is strongly diminished as the fee reduction will be passed on also to customers using other platforms; also improves monitoring ability
- May facilitate collusion between sellers– limit the ability of sellers to price-discriminate across platforms and thus may facilitate collusion insofar as they improve the sellers' ability to monitor each other's pricing and reduce the cost of enforcing a horizontal agreement

● Potential efficiencies

- May serve to protect a platform's investments

Legal assessment in the UK/EU and relevant cases



Legal assessment of Pricing Relativities Agreements in the UK/EU

- Vertical restraints are assessed under the Vertical Agreements Block Exemption Regulation (VABER).
- Certain 'black-listed' restrictions do not benefit from exemption under the VABER, including vertical agreements which

*'directly or indirectly, in isolation or in combination with other factors under the control of the parties, have as their object the restriction of the **buyer's** ability to determine its sale price...'*

- The Vertical Guidelines explain that agreements having as their direct or indirect object the establishment of a fixed or minimum resale price or a fixed or minimum price level to be observed by the buyer *'can be achieved by indirect means.'*
- Such indirect means include

'linking the prescribed resale price to the resale price of competitors'.

- Pricing Relativities Agreements restrict the ability of the buyer (i.e. the retailer) to determine its retail prices for competing linked brands.
- As such, Pricing Relativities Agreements do not benefit from exemption under the VABER.
- Restriction by 'object'
- Individual exemption? Parties to demonstrate that criteria are met

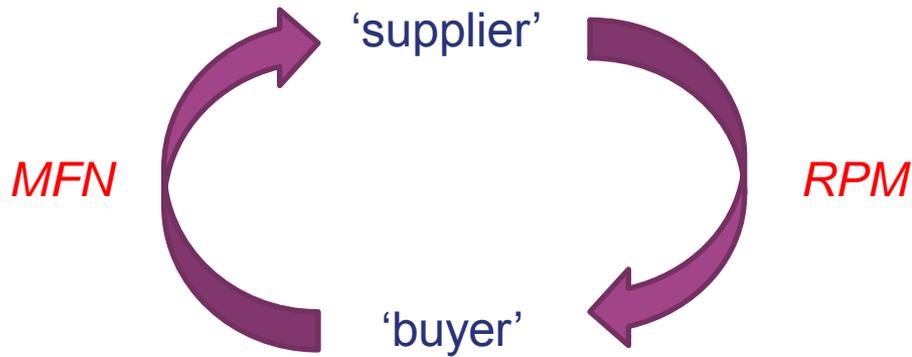
Legal assessment of retail-MFNs (1)

- **Can retail-MFNs benefit from block exemption under VABER? Treated differently from Pricing Relativities Agreements and RPM?**
- **Relevant questions:**
 - Do retail-MFNs *'directly or indirectly, in isolation or in combination with other factors under the control of the parties, have as their object the restriction of the buyer's ability to determine its sale price...'* ?
 - Who is the *'buyer'*?
- **Definition of *'buyer'* under the VABER:**

'buyer' includes an undertaking which, under an agreement falling within Article 101(1) of the Treaty, sells goods or services on behalf of another undertaking
- **Restriction by 'object' or 'effect' – implications for burden of proof**
- **If not 'hardcore', 30% market share test under the VABER**
- **Presumption of legality conferred by VABER**
 - Possibility of withdrawal if cumulative effect of parallel networks of vertical agreements restricts access to the relevant market or access therein (only European Commission if relevant geographic market wider than single EU Member State)
 - Disapplication of VABER – European Commission can adopt regulation

(When) do MFNs result in RPM?

'MFNRPM'?



Hotel online booking – RPM?

- **OFT issued a Statement of Objections (SO) alleging that Booking.com, Expedia and IHG infringed competition law in relation to the online supply of room only hotel accommodation by online travel agents.**
 - Allegations that Booking.com and Expedia each entered into separate arrangements with IHG which restricted the online travel agent's ability to discount the price of room only hotel accommodation.
 - OFT's **provisional** view: these restrictions are by their nature, anti-competitive in that they could limit price competition between online travel agents and increase barriers to entry and expansion for online travel agents that may seek to gain market share by offering discounts to consumers.
 - Parties to make representations; SO not infringement finding

“The online travel market may appear to offer plenty of choice and competition, but the reality is that there are lots of different shop windows selling the same rooms at the same prices.”

(Source: Mark Datta, Blink Booking, Financial Times 31 July 2012)

- **General rule: discounting restrictions amount to RPM, unless the intermediary (e.g. the agent) whose ability to determine the sale price is restricted can be regarded as *‘an auxiliary organ forming an integral part of the principal’s undertaking’* .**
- **Referred to as ‘genuine’ agency - but what makes an agent ‘genuine’ or ‘non-genuine’?**

How to spot a 'non-genuine agent' ...



Link between retail-MFNs and genuine agency

- Concept of 'single economic unit' whereby agent is comparable to 'commercial employee'
- A range of factors to assess 'genuine agency'
 - Is the **commercial and/or financial risk** borne by the agent in relation to the supply of the relevant goods or services '*material*' or '*non-negligible*'?
 - Does the agent have **influence over the principal's commercial strategy**?

If an agent imposes a retail-MFN on its principal, is it behaving like a commercial employee?
(...or more like the tail wagging the dog?)
 - Assessment of other factors illustrating (lack of) **unity of conduct** between principal and agent

Link between retail-MFNs and genuine agency

Existence of retail- MFN imposed by agent on principal indicative of non-genuine agency?



©Linda Silvestri

“Expedia threatens if Travelocity gets a lower rate,” said the Trump International Beach Resort, in Florida. “If we do not maintain parity with all, we are threatened with poor placement and in the worst case removal from sales sites.” (Source: Sunday Times, 2 September 2012)

Retail-MFNs without RPM?

- If agent 'non-genuine', discounting restrictions → RPM

*In the case of agency agreements, the principal normally establishes the sale price, as the agent does not become the owner of the goods. However, where such an agreement cannot be qualified as an agency agreement for the purposes of applying Article 101(1) an obligation preventing or restricting the agent from sharing his commission, fixed or variable, with the customer would be a hardcore restriction under Article 4(a) of the VABER. In order to avoid including this hardcore restriction in the agreement, **the agent should thus be left free to lower the effective price paid by the customer without reducing the income for the principal.** (paragraph 49 of the Vertical Guidelines, emphasis added)*

- If RPM is removed, will retail-MFNs gradually disappear (to the extent that retail-MFNs are predicated on the principal having the power to set retail prices)?



- What about circumstances in which it would not be appropriate for the 'buyer' to independently determine sale prices or 'share its commission'?

E-books and other EU cases

- **E-books: OFT has closed its investigation into whether arrangements that certain publishers have put in place with some retailers for the sale of e-books may breach competition rules. European Commission's investigation ongoing.**
- **US E-books consent decree - a blueprint for EU to abandon retail MFNs and discounting restrictions?**

For two years, Settling Defendants shall not restrict, limit, or impede an E-book Retailer's ability to set, alter, or reduce the Retail Price of any E-book or to offer price discounts or any other form of promotions to encourage consumers to Purchase one or more E-books, such two-year period to run separately for each E-book Retailer, at the option of the Settling Defendant [...]

Settling Defendants shall not enter into any agreement with an E-book Retailer relating to the Sale of E-books that contains a Price MFN.

Source: E-books consent decree (Case 1:12-cv-02826-UA)

- **Limited case-law on MFNs in EU: Hollywood studios; Digitisation of European cinemas; E.ON Ruhrgas –Gazprom gas supply**

Enforcement action against retail-MFNs on a standalone basis....?



...but for how long..?

Thank you!

Questions?

