

Unclassified

DAF/COMP/WD(2015)58

Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development

08-Oct-2015

English - Or. English

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

HEARING ON ACROSS PLATFORM PARITY AGREEMENTS

-- Note by Italy --

27-28 October 2015

This document reproduces a written contribution from Italy submitted for Item 7 of the 124th OECD Competition Committee on 27-28 October 2015.

More documents related to this discussion can be found at www.oecd.org/daf/competition/competition-crossplatform-parity.htm

Please contact Ms. Cristiana Vitale if you have any questions regarding this document [E-mail: cristiana.vitale@oecd.org].

JT03383482

Complete document available on OLIS in its original format

This document and any map included herein are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area.



DAF/COMP/WD(2015)58
Unclassified

English - Or. English

-- Italy --

1. Introduction

1. In Italy, turnover generated by e-commerce in 2014 amounted to an estimated €13.3bn, a level which is relatively small compared to other European countries¹. Even if online purchasing is growing fast (+17.5% in 2014), it is still not widespread: according to 2014 Eurostat data, individuals who made at least one online purchase in a 12 month period increased from 15 per cent in 2011 to 22 per cent in 2014, but is still well below the EU-28 average (50%). On the enterprise side, in 2014 only a small proportion of firms (8 per cent) received orders via computer mediated networks, compared to the EU-28 countries average of 18 per cent.

2. The share of online sales going through dot.com companies increased to 54% in 2014 (from 47% in 2010), while the rest is generated by the more traditional retailers/suppliers. In particular, with respect to the tourism industry, the online travel agencies (also OTAs) represent nearly 70% of the online hotel booking segment in terms of sales.

3. Therefore, while traditional markets are still predominant and the influence of e-commerce still limited, online platforms are becoming an important channel of the online purchases. The development of online markets brings several benefits to consumers as well as businesses, lowering consumers' search costs, expanding the boundaries for trade and facilitating the emergence of new business models.

4. Nevertheless the recourse to certain contract clauses in the relationship between retailers and suppliers in the online markets can raise competition concerns. In particular, vertical clauses between suppliers and retailers specifying a relative relationship between prices of competing products or charged by competing retailers - referred to as Across Platform Parity Clauses (or APPAs) when the retailers involved in these agreements are online selling platforms – can be particularly problematic as they might soften price competition and/or prevent the entry of other online platforms.

5. The Italian Competition Authority (ICA or Authority) has recently dealt with APPAs in a case regarding the market for online hotel reservation services and two Online Travel Agencies (OTAs), Booking.com and Expedia². This investigation was carried out in parallel with the competition agencies of France and Sweden which conducted similar investigations: as a result of intense cooperation, among the three agencies and with the European Commission, in April 21, 2015 the three competition authorities closed the proceedings against Booking.com by accepting the same remedy package³. Booking.com's commitments apply to all bookings made by consumers worldwide in respect of hotels and other accommodations located in France, Italy and Sweden and they became effective from 1 July 2015, for a period of five years⁴.

6. The assessment of this kind of cases poses several challenges to a competition authority. While it is important not to stifle innovation, investment and the development of new markets and business models, it is also important to ensure that these developments do not restrict competition to the detriment of consumers. In this respect the Italian Competition Authority considers that in the Booking.com case it

¹ For instance: UK (€127bn), Germany (€71bn) and France (€57bn). Source: European B2C E-commerce Report 2015.

² Case No. I779 - *Mercato dei servizi turistici-prenotazioni alberghiere on line*.

³ A joint press release (in English) is available at: <http://www.agcm.it/en/newsroom/press-releases/2207-commitments-offered-by-booking-com-closed-the-investigation-in-italy-france-and-sweden.html>

⁴ The case is still pending with respect to Expedia.

managed to strike a balance between preventing potential restrictions to competition while preserving operators' ability to offer and develop innovative services that are valuable to consumers.

7. In this case the tool of commitments proved particularly apt at addressing the competition concerns in a timely manner, providing certainty to the firms involved and ensuring that consumers can benefit from the competition improvements introduced by the commitments.

8. This contribution, after briefly describing the legal and analytical framework underpinning the case, reports in details the competitive concerns that led to the investigation, the content of the commitments and their assessment by the Authority.

2. The application of competition law to APPAs

2.1 *Legal framework*

9. In Italy APPA clauses, as other vertical restraints, fall within the scope of article 2 of Law 287/90 (the Competition Law) on agreements (or Article 101 of the Treaty on the Functioning of the European Union (TFEU) if they may affect trade between Member States of the European Union) and that prevent, restrict or distort competition in the internal market of the EU. In assessing a case under Article 101 of the TFEU, efficiency claims can be invoked and assessed under Article 101(3) of the TFEU⁵.

10. Vertical restraints might also fall within the scope of article 3 of the Competition Law (or Art. 102 of the TFEU if they affect trade among Member States) on the abuse of dominant position if they are unilaterally imposed by a party holding a dominant position and are aimed at excluding competitors.

2.2 *Economic Assessment*

11. Online platforms, such as those operated by OTAs, typically operate in two-sided markets, coordinating the interdependent demands of two distinct groups of customers, who need to interact with each other.

12. Given this context, the ICA may consider several theories of harm in assessing the competitive effects of APPAs. For instance, they may soften competition among platforms⁶ or facilitate collusion between platforms in setting fees to the sellers⁷. In addition, APPAs may foreclose entry of new platforms

⁵ Against an allegation whereby an APPA type of agreement restricts competition pursuant to Art. 101 TFEU, a firm may invoke an individual exemption under Art. 101(3) or an exemption under the European 'Vertical Block Exemption Regulation' (the VBER), which entered into force on 1 June 2010 and which provides a safe harbour for most vertical agreements. The VBER creates a presumption of legality for vertical agreements whereby the market share of the supplier and the buyer do not exceed the threshold of 30%. However, exceeding the market share threshold of 30 % does not create a presumption of illegality. This threshold serves only to distinguish those agreements which benefit from a presumption of legality from those which require individual examination.

⁶ Since platforms also compete on the fees they ask to sellers, there is no incentive for one platform to offer a lower usage fee to its sellers since any price reduction offered by the sellers who received a lower fee will have to be applied across all platforms. As a consequence, platforms have lower incentives to reduce the fee charged to the seller.

⁷ An APPA improves the platforms' ability to monitor each other's usage fees and detect deviations since sellers are likely to reveal to all other platforms the lower fee they might receive by one deviating platform.

offering a lower transaction fee to the sellers, so as to allow them to charge lower prices and attract buyers to their new platforms⁸.

13. In any event, the ICA's approach to the analysis of the competitive effects of APPAs entails an evaluation of case-specific evidence, which is particularly relevant in the assessment of these cases.

14. An evaluation of the nature of the agreement is important to check whether the presence of other clauses serving as monitoring tools might reinforce some potential anticompetitive effects (e.g., facilitating collusion between platforms). Another relevant aspect in assessing the agreement is the extension of its application, for example in terms of platforms and sellers.

15. Other elements to consider are the market positions of the platforms under investigation and the competing platforms in terms of sales from buyers, fees charged to sellers and number of sellers operating on the platforms (relative to the online platform segment and more generally to the online trading segment which include other online channels). From this perspective, it is important to analyse the distribution of sellers across platforms and the degree of overlap of the same sellers in the various platforms.

16. Finally, the analysis of barriers to entry and expansion (e.g., investment costs to build a platform and reaching a critical mass due to the presence of network effects) is fundamental to the competitive assessment together with the analysis of the evolution of the industry.

17. The main efficiency justification that would be applicable to APPAs hinges on the free-riding problem and on the objective of the platform owner to protect the investment it undertook to develop the platform, especially if the success of the trading platform depends on a number of ancillary services that might reduce the asymmetry of information that afflicts on-line sales. For instance, if the platform has invested over time in building a reputation for its services (e.g. how it selects the sellers present on it, how it grades their reliability, the quality of its reviews and so on), it may not want retailers to benefit in attracting buyers, but then have buyers make their purchases on the lower quality/lower cost platform.

18. This effect may be particularly important for trading platforms as they present the typical features of two-sided markets, i.e., indirect network externalities. Indeed, platforms need to attract sellers and buyers at the same time; hence, losing some buyers may have a tremendous impact on the viability of the platform as it may make the platform less appealing for sellers, which in turn diminishes the value of the platform for buyers, and so on. The price paid by a buyer to a seller through the platform influences the willingness of buyers to make purchases through that platform and, therefore, the attractiveness of that platform. Hence, the platform will try to find some means to influence the seller's pricing decisions and, therefore, may ask the seller to agree to an APPA.

3. Booking.com case: the market for online hotel reservation services

3.1 The theory of harm and relevant markets

19. In May 2014 the ICA, following complaints by the Italian Hotels Association (Federalberghi) opened a proceeding against Booking.com – the market leader in Italy - and Expedia in order to investigate possible restrictions of competition related to the use of price (and others conditions) parity clauses in contracts stipulated between the main online travel agencies (OTAs) and their hotel partners.

⁸ If the incumbent platform has signed an APPA with its sellers, covering also new platform operators, these sellers cannot charge lower prices on the new platform. However, the sole restriction of price competition among platforms brought about by the APPA may not be sufficient in itself to support a theory of harm based on foreclosure if the platform in question holds a limited share of the market.

20. In particular the ICA was concerned by the price parity clauses applied by the two OTAs to their hotel partners, whereby the latter would not be able to offer equal or better room rates on any other sales channels, offline and online, including other OTA platforms and hotel's own websites. These parity clauses applied not only to prices but also to other terms and conditions, including room availability.

21. The main competition concern for the Authority was that these parity clauses restricting the vertical relationships between the two OTAs and their hotel partners would have effects on the horizontal dimension, i.e., competition among OTAs and more generally among all sales channels. In particular, these parity clauses could have the potential to substantially restrict:

- competition between OTAs on commission fees they request to their hotel partners: in presence of parity clauses, an OTA has no incentives to offer lower fees as these lower costs for the hotels cannot be translated in lower room rates offered on its platform due to the parity obligation; and,
- competition on price (and other conditions) offered to final users by hotels within the OTA channel and across the other sales channels, online and offline, direct and indirect (e.g., hotels' own websites, traditional travel agencies).

22. In addition, the softening of competition among OTAs could foreclose the market, preventing entry of new OTAs.

23. The ICA considered that the relevant market for the assessment of the parity clauses is the market for online hotel booking services, distinct from the market for offline hotel booking services. As for the geographic dimension, the market was considered national given that Booking.com and Expedia operate with country specific websites and differentiate their commission fees based on the national borders. In 2013 online hotel booking through OTAs represented nearly 70% of the online channel (in terms of turnover of hotels), and [25-30]% of total hotel reservations; room booking at the hotels website represents only [5-15]% of total hotel reservations.

3.2 *Booking.com's commitments*

24. During the investigation, Booking.com submitted commitments consisting in a significant reduction of the scope of the price parity clauses. The revised clauses will only apply to prices and other conditions publicly offered by the hotels through their own direct online sales channels, leaving them free to set prices and conditions on other OTAs and on their direct offline channels, as well as in the context of their loyalty programs.

25. In particular, Booking.com has committed to:

1. refraining from requiring accommodations to enforce parity clauses on price and other conditions offered on any other OTA (Price Parity / Conditions Parity);
2. refraining from requiring accommodations to offer on Booking.com the same or a greater number of rooms, of any type, as those offered on any other OTA, or as is reserved for the accommodation itself (Availability Parity);
3. allowing accommodations to offer equal or better conditions on Offline Channels than those offered on Booking.com, provided that these conditions are not published online or marketed online (i.e., they are aimed at the general public);

4. refraining from restricting unpublished conditions that accommodations are able to offer, provided that these are not marketed online at the general public: in other words, Booking.com may prevent its hotel partners from offering better conditions if they are made available online to the general public (so called “narrow” MFN clause)⁹.

26. Commitments 1) and 2) above are expected to significantly increase competition between Booking.com and other OTAs in the online hotel reservation market compared to the ex-ante situation. Hotel partners with Booking.com are now allowed to offer not only better room rates and conditions on the other platforms but also different number and types of room. Therefore hotels have more flexibility in allocating rooms across different OTA’s platforms and may use this competitive variable when negotiating their commission fees with the OTAs.

27. According to the ICA, these commitments will also improve competition between OTAs on the level of commission fees they request to hotels. In presence of parity clauses, OTAs did not have incentives to offer lower commission fees to attract hotels to their platforms since these lower fees for the hotels could not be translated in lower room rates offered on the platforms. These two commitments were considered sufficient to stimulate the competition among OTAs which, while representing nearly 70% of the online booking segment (in terms of hotel sales), accounted for only [25-30]% of the total hotel reservations in 2013.

28. Commitment 3) above reflects the concern expressed during the market test that the parity clauses had the effect of unduly protecting the OTAs from the competition of offline sales channels. Under this commitment, Booking.com’s hotel partners are now able to offer equal or better room rates and conditions (than those offered to Booking.com) to all Offline channels¹⁰ provided that terms are not marketed online¹¹ or published online¹², i.e., provided that they are not aimed at the general public via online channels. In other words, bookings made in person at an accommodation’s reception, by telephoning an accommodation, or at a bricks and mortar travel agency are no longer constrained.

29. Since in Italy the offline channel represents [60-70]% of all hotel reservations, this further concession from Booking.com is expected to provide hotels with the ability to compete against Booking.com and other OTA more vigorously in the offline channels.

30. Commitment 4) above relates to the important issue of the ability of the hotels to compete against Booking through their own online channel. The preliminary commitment package of Booking.com envisaged the elimination of the parity clauses only with respect to other OTAs, i.e., excluding hotels’ websites. However, during the market test it was argued that this commitment (called narrow MFN clause) would have

⁹ In addition, Booking.com will not offer lower commission rates or other incentives to accommodations that are conditional on accommodations observing Price Parity, Conditions Parity and/or Availability Parity, which Booking.com has committed to abandon, such as: de-listing or threaten to de-list any accommodation; increasing commissions (or impose any other charges); and, different treatment on Booking.com’s ranking algorithm.

¹⁰ “Offline Channel” means a channel that does not involve the use of the internet, such as bookings made in person at an accommodation’s reception, by telephoning an accommodation, or at a bricks and mortar travel agency.

¹¹ “Marketed Online” means marketed to the general public online by any means, including on mobile applications. This definition does not include online marketing that is not aimed at the general public: it excludes in particular email, SMS and instant messaging communications

¹² “Published Online” means made available to the general public online by any means, including on mobile applications. In the case of rates, publication includes the display of the actual rates or sufficient detail for the consumer to calculate rates.

no pro-competitive effects as it would ultimately replicate the status quo (i.e., parity clauses applying to all channels): respondents to the market test complained that the hotel partners with Booking.com would have no incentive to offer better terms on OTA platforms than those offered to their own websites as they are interested in promoting their direct channels and avoid any cannibalization of the sales.

31. The promotion of direct channels by hotels partly conflicts with the interest, on the other hand, of Booking.com and OTAs in limiting the free-riding problem and protecting their investments in the online platforms. Striking a balance between these two legitimate interests hinges on the definition of extent of the application of the parity clauses. In its final version, the parity clause has been amended so that it applies only on deals offered through their own websites to the public at large: Booking's hotel partners are still able to offer promotions through their own online channel provided that these promotions are targeted/selective and not marketed online to the general public. In the preliminary version of the commitments this possibility was limited to hotels prior customers and other "closed user groups".

32. In the ICA's view, this additional concession made by Booking.com addresses the concern regarding the problem of cannibalization of sales. Market conditions in Italy appeared not to support such concern: the hotel website channel represents only [5-15]% of total (online and offline) hotel reservations and [25-35]% of the sales made via the online channel.

33. Furthermore, the hotel industry is very fragmented. In particular, independent hotels represent 85% of all hotels, they are generally small in size and the majority of their direct sales occur through offline channels (where the APPAs clauses no longer apply). In addition, small hotels not always have the capacity to operate and maintain online booking facilities: thus, OTAs services represent an important opportunity for them to expand their sales. On the other hand, large hotel chains, which represent only 6% of all hotels in Italy, have the majority of their online sales through their websites and cannibalization of sales may be of a concern for them. For this reason, the commitment 4) above was amended to allow hotels to offer more favourable terms to not only their loyalty programme customers (as initially proposed) but also to all customers provided that these discounts are not marketed and advertised online to the general public.

34. More generally, the ICA considered that the cannibalization of sales argument has to be confronted with the circumstance that the promotion through direct online channel comes at cost: hotels still have to bear investment costs on their website and booking system to increase their visibility on internet: therefore, the use of OTA platforms which charge commission fees for their intermediation and promotional services may not necessarily be more expensive than the online direct channel.

35. The Authority carried out an analysis of the incentives based on an economic model simulating competition between OTAs. The model was originally presented by Booking.com during the investigation to the three competition agencies. After adapting the economic model to their national market structure, the three agencies run a simulation exercise to test the impact of Booking.com's commitments to limit the scope of application of parity clauses. The exercise showed that, when moving to a scenario with a "narrow" parity clause as envisaged in the commitment package, there existed numerous pairs of commission fees and room rates which could be "credibly" pursued by OTAs and hotels, i.e., potentially profitable.

36. This analysis confirmed the Authority's view that the commitments offered by Booking.com were able to considerably increase the opportunities and incentives for OTAs and hotels to differentiate commission fees and room rates respectively across all sales channels, compared to the situation prior the investigation.

4. Conclusions

37. As a result of the expansion of the internet economy there has been significant entry of web-based businesses many of which are two-sided platforms. The use of Internet is significantly changing the way in which goods and services are distributed, particularly with respect to some sectors such as tourist services. Future developments of Internet might bring some novelties resulting in new efficiency justifications for vertical restraints in their “online” version compared to the offline one (for instance, if manufacturers’, distributors’ and consumers’ interests are aligned in new different ways). In this respect the main challenge for competition authorities is to gain an understanding of the specificities of markets and business models which will often require a case by case analysis.

38. Notwithstanding this, the Italian Competition Authority considers that the economic framework and the traditional antitrust tools are, in general, still valid and there is no need, at the moment, for different or special rules or approaches for online vertical conducts since the possible anti- and pro-competitive effects are similar and the existing rules are flexible enough.

39. Another aspect to consider is that businesses developed through online platforms are inherently global and the interests at stake go far beyond national boundaries. Coordination and communications among investigating agencies are important even when the national specificities might entail final decisions taken at the national level.

40. In the Booking.com case the European Competition Network (ECN) and the rules on cooperation envisaged in Regulation 1/2003 provided a very useful framework and allowed the competition authorities of France, Italy and Sweden to have very useful discussions on the issues at stake ultimately paving the way for an alignment of their decisions. On the procedural side, the Authority considered it important to also align its investigation timetable to ensure the continued coordination with the other agencies: the deadline for the submission of the final commitments (three months from the start of the antitrust investigation) envisaged in the Italian legislative framework was extended to allow the continuation of the discussions among the coordinating agencies and to facilitate Booking.com efforts in dealing with several authorities at the same time and in elaborating a common commitment package.

41. In the Authority’s view the efforts involved in this approach allowed the adoption of commitments that were appropriate in striking a balance between preventing potential restrictions to competition while preserving operators’ ability to offer and develop innovative services that are valuable to consumers.

42. Although it is too early to make any assessment of the effect of the decision some reports already show that hotels are exploiting the possibility opened by the elimination of some of the clauses through personalized offers to their customers that enrich the choices and benefits for consumers¹³.

¹³ See International New York Times, September 1 2015, “Hotels work to skip the middleman”.