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DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

**Summary Record: ANNEX TO THE SUMMARY RECORD OF THE 124th MEETING OF
THE COMPETITION COMMITTEE HELD ON 27-28 OCTOBER 2015**

Executive Summary of the Hearing on Across-Platforms Parity Agreements

28 October 2015

Paris, France

*This Executive Summary by the OECD Secretariat contains the key findings from the discussion held under Item 7 of the 124th meeting of the Competition Committee on 27-28 October 2015.
More documents related to this discussion can be found at www.oecd.org/daf/competition/competition-cross-platform-parity.htm.*

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Executive Summary of the Hearing on Across-Platforms Parity Agreements

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By the Secretariat¹

From the discussion at the hearing, the delegates' and experts' written submissions, several key points have emerged:

1. There is increasing concern at online platforms using across platform parity agreements (APPAs) that prevent producers from setting lower retail prices on rival platforms that offer more competitive commission rates. This removes the incentive for platforms to compete on the commission they charge to producers and hence inflates the commissions and the final prices paid by consumers. These agreements may also prevent entry from new low cost platforms, reduce innovation, and even facilitate collusion.

The hearing showed that, although the number of cases is currently small, there is increasing concern at online platforms using agreements that prevent producers from setting lower retail prices on rival platforms that offer more competitive commission rates. In addition, the competitive implications of agreements that limit the freedom of producers on online platforms were generally less well understood than those caused by other types of traditional vertical constraints. It was noted that these agreements could include constraints on terms and conditions as well as prices.

Four direct theories of harm were articulated during the discussion. Firstly and most importantly the use of these agreements means that platforms cannot price differentiate in order to increase their volume of sales or bookings. Rival platforms therefore have no incentive to undercut the commission that producers are charged by a platform with an APPA. Equally platforms with an APPA can increase their commission without fear that it will create a price disparity and lead to them losing volume. This means that in addition to eliminating intra-brand price competition the APPA can significantly inflate prices across the producers on the platform even if there is healthy inter-brand competition.

Secondly it was suggested that APPAs prevented new entry by low-cost platforms, while encouraging entry by high-cost platforms that compete on quality rather than price. The absence of price differentiation prevents consumers from identifying their preferred balance of price and quality. Thirdly, it was argued that in the presence of APPAs platforms were less likely to compete to offer producers a better quality service because these agreements prevented the producer from rewarding producers by steering consumers towards platforms that offered better services (e.g. anti-fraud protection). Finally, there was a concern that APPAs might facilitate collusion: either on retail prices amongst producers by improving their ability to monitor adherence to collusive agreements; or amongst platforms on their commission by creating an automatic punishment mechanism for platforms that might deviate from the collusive commission.

¹ This Executive Summary does not necessarily represent the consensus view of the Competition Committee. It does, however, encapsulate key points from the discussion at the session, the delegates' written submissions, the panellists' presentations and the Secretariat's issues paper.

2. There was also concern that a decision by platforms and producers to adopt an agency relationship might increase prices, and that the agreement of APPAs would help the firms to adopt such a relationship. APPAs might therefore also be indirectly responsible for price increases that occur when platforms and producers adopt an agency relationship.

There are broadly two potential forms for a supply chain relationship between a platform and a producer. Platforms can purchase from producers in wholesale markets and sell those products to consumers within retail markets. Alternatively, producers may sell directly to consumers after purchasing retail support services from a platform (either by paying the platform a commission, as for example hotels pay online travel agents, or through another payment mechanism). Note that different firms set the price that consumers pay depending on which of these relationships they adopt.

A consistent finding in the literature is that retail prices would be set at higher levels if firms that operate at less competitive parts of the supply chain set them. For example, if platforms face less competitive pressure than producers do, then platforms would set higher retail prices than those that the producers would set. Therefore if the ability to agree an APPA makes it profitable for a platform to allow producers to set retail prices, rather than themselves setting prices under competitive pressure from rival platforms, then permitting the APPA might result in higher prices for consumers.

3. Across Platforms Parity Agreements may also have efficiency enhancing effects that are beneficial for consumers. They can remove the risk that consumers use a platform to compare products and enjoy additional services (such as customer reviews), and then purchase their favoured product directly from the producer or on a cheaper platform. As a result, they can ensure that platforms are not discouraged from investing in the quality of their platform. The benefit that consumers derive from these investments and the extent to which these investments might also be protected through less anti-competitive measures is likely to depend on case specific factors.

APPAs may create benefits for consumers by improving the quality of the platform. It was argued that additional investments in the quality of the platform are possible because APPAs protect platforms from free-riding behaviour. Furthermore it was argued that no other alternatives existed, such as different remuneration models that would offer the same protection while efficiently aligning the interests of the producer and platform.

The evidence in a number of the cases discussed suggested that the risk of free-riding was significant. However, it was less clear whether free-riding would result in platform's exiting the market, particularly given the value that platforms could obtain from collecting rich consumer datasets. Therefore it is still unclear whether the important consumer benefits that the existence of online platforms themselves brings, in terms of increased inter-brand competition and visibility of small producers, depends upon the use of APPAs. Nevertheless, depending on the specifics of each case, there would appear to be a risk that some investments would no longer be made in the absence of APPAs. However, in the cases discussed the nature of these potentially forgone investments had generally not been specified. It was suggested that these might often be investments in advertising campaigns and platform branding rather than the platform functionality that would improve the quality of the platform for consumers.

It was stated that it was important to understand whether these quality-enhancing investments could be protected through less anti-competitive means. A range of potential alternative payment models were identified that would be effective in protecting the investments; however it was argued that this protection could only be gained at the expense of efficiency. For example the free-riding issue could be resolved by asking producers to pay the platform a fixed listings fee or a fee for each viewing of their product obtained through the platform. However it was argued that this model could place too much risk on the producer and would not incentivise platforms to encourage consumers to make a purchase. In response, it was argued that a two-part tariff could align incentives, share risk, and offer platforms some protection against free-riding on investments. Nevertheless, it was agreed that the role of competition authorities is not to recommend the business models firms should adopt and that any assessment of potential alternatives should be done only to form a view of the relevant counterfactual against which to assess the efficiencies that had been claimed.

4. The magnitude of the anticompetitive effects of these agreements will depend on the market power of the platform requesting the agreement. The effects may also depend on the scope of the agreement; however, the impact of the scope of an APPA on the degree of price competition amongst platforms appears likely to depend on the specifics of the case.

The size of the price increase will depend on the market power of the platform that imposes the APPA (assuming that firms act independently and do not co-ordinate). This is because producers are not able to credibly threaten to delist their product from a platform that requires an APPA when that platform has market power. For example, a platform might have market power if they control access to a significant group of single-homing consumers, or if they have a large market share of multi-homing consumers. In contrast, it was suggested that the threat of producers delisting from a small new entrant platform might be credible. In those circumstances, there might remain some degree of competitive pressure upon its commission rate even if the producers agree to the APPA (which they may not).

The magnitude of the effect can also depend on the scope of the agreement. Broadly-defined APPAs require that producers set prices on a platform that are the same as the prices that consumers might find on other platforms or in other sales channels. This can therefore lead to the elimination of intra-brand retail price competition. In contrast many agencies and commentators claim that narrowly-defined APPAs, which impose parity only between the platform and the producer's own website, might maintain a degree of price competition amongst platforms, while avoiding what can often be the major source of free-riding (i.e. direct sales on the producer's website).

In theory, narrowly defined APPAs might be of less concern than broadly defined APPAs since they allow producers to seek to reduce platform commissions by threatening to sell more cheaply through rival platforms. However, the threat to sell more cheaply through rival platforms may not be credible for certain types of producers. For example, it will not be credible if a producer is not willing to set prices on rival platforms that undercut the prices on their own website. Producers might be unwilling to do so because of the same risk of free-riding that has been identified above. However, even if producers are willing to undercut themselves, they may nevertheless be discouraged from investing in their own website that they would in the absence of the narrow APPA.

It was also noted that a producer might credibly threaten to undercut the price on its own website if the producer has a strong brand and its direct purchasers are less price sensitive than purchasers via the platform (as was the case in price comparison websites for car insurance). However, this may not be the case in markets composed of large numbers of small producers without strong brands where direct purchasers might be those that are most price sensitive. As a result, it remains unclear whether more narrowly defined APPAs resolve the concerns since they may continue to apply upward pressure on the commission that the platform charges many of its producers and hence on the price paid by consumers.

5. The hearing considered a variety of legal approaches used by competition agencies to assess APPAs. In some cases the agreements had been considered as horizontal conspiracies to fix prices. In other cases they were considered as vertical price restraints. One expert suggested that these restraints should be treated as restrictions by object, with exemptions granted where the firms demonstrate that the agreement generates countervailing efficiencies, while others argued that a case-by-case approach was required for the assessment of competitive effect, and that targeted remedies might benefit consumers.

The discussion showed that APPAs have been dealt with differently in different jurisdictions. There have been some cases in which APPAs have been considered as agreements between competitors to fix prices (Flight Centre). More commonly, however, competition authorities have assessed them as vertical price restraints. One expert said that broadly defined APPAs were equivalent to RPM agreements. As such he argued that broadly-defined APPAs should be dealt with no less harshly than RPM agreements, and said that there was a strong case that they should be treated as restrictions by object, with exemptions granted only where efficiencies were successfully demonstrated by the firms. Another participant however argued that the overall impact of broadly defined APPAs was ambiguous and therefore that they should be subjected to a case-by-case analysis. It was argued that such an effects based analysis would allow authorities to put in place remedies that narrowed the scope of the APPA and hence permitted to remove its anti-competitive effects.

6. The hearing also discussed the different approaches that have been taken to remedy the impact of APPAs. These included prohibitions and commitments to narrow the definition of the APPA. Each of these remedies carries certain risks.

Different approaches had been adopted in different cases and across different jurisdictions, however most authorities that had reached findings or accepted commitments were planning to review ex-post the impact of these actions. This suggests that in future more will be known about which remedies are effective and which are not.

Some authorities had prohibited APPAs in certain markets, or proposed to do so. In one case the state had overruled the authority and prohibited APPAs through direct legislation that sought to protect consumers. One authority noted that, in addition to requiring the removal of APPAs, it had found it necessary to prohibit equivalent behaviours that might reproduce the parity setting effects of the APPA without the need for this to be set out in a formal agreement. In particular the authority had been concerned that, despite the order to remove the APPA, a platform with market power might nevertheless be able to punish any producer that offered lower prices on rival platforms by delisting them. The platform might therefore successfully create and maintain price parity without needing to write it down in an agreement. This would allow it to comply with a simple prohibition while continuing to restrict competition.

Other authorities had accepted commitments and closed investigations in APPA cases, these commitments included narrowing the scope of the APPA to exclude other platforms and offline selling channels (in some cases for a specified period of time). However, it was unclear whether this might create additional search costs for consumers by requiring them to directly contact producers in order to compare their best prices. By doing so the remedy might risk reducing inter-brand competition and lead to higher prices for consumers.