



Most Favored Nation Clauses: Is It the End of the Road?

Webinar co-hosted by Steptoe & Oxera Consulting

25 October 2017



Today's webinar agenda

- **What are MFNs?**
- **Why are the European authorities concerned?**
- **Enforcement to date**
- **What does this mean for your MFNs?**
- **Closing remarks**
- **Q&As**

Today's Panel

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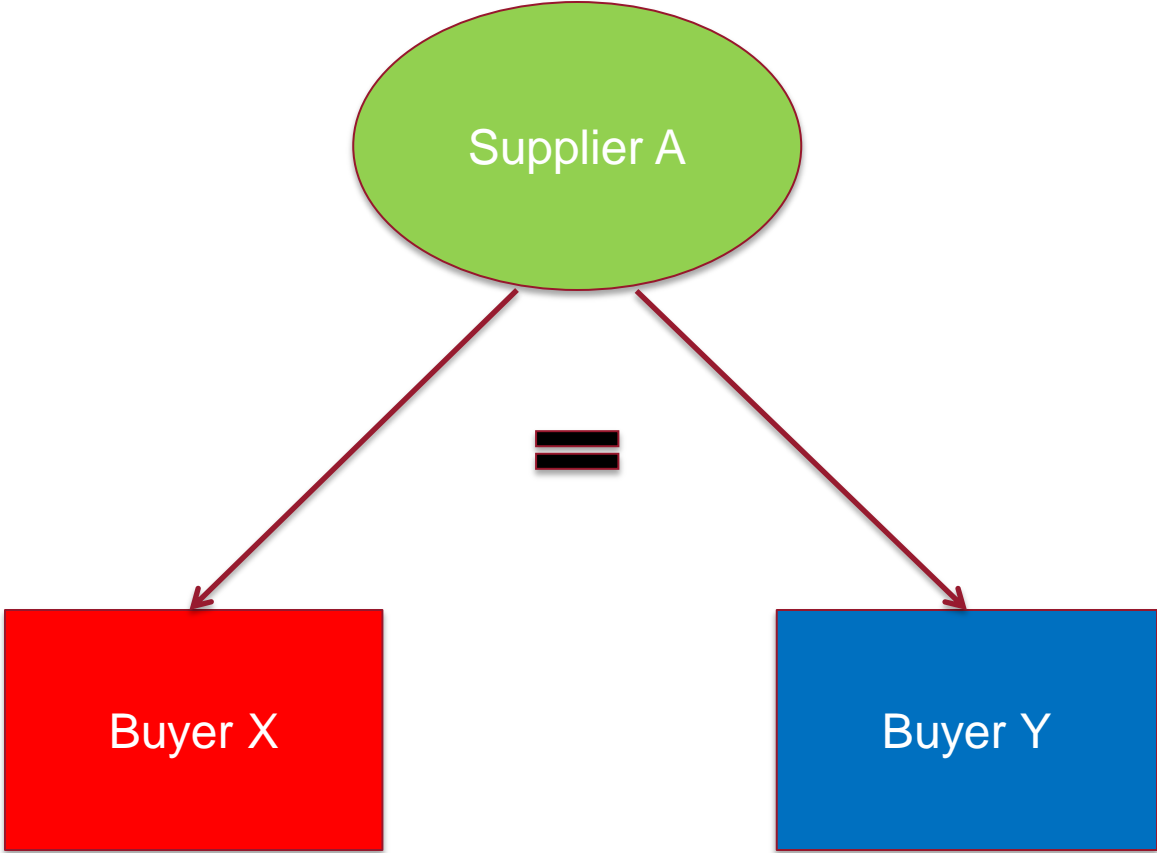
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A BRIEF INTRODUCTION TO MOST FAVORED NATION CLAUSES

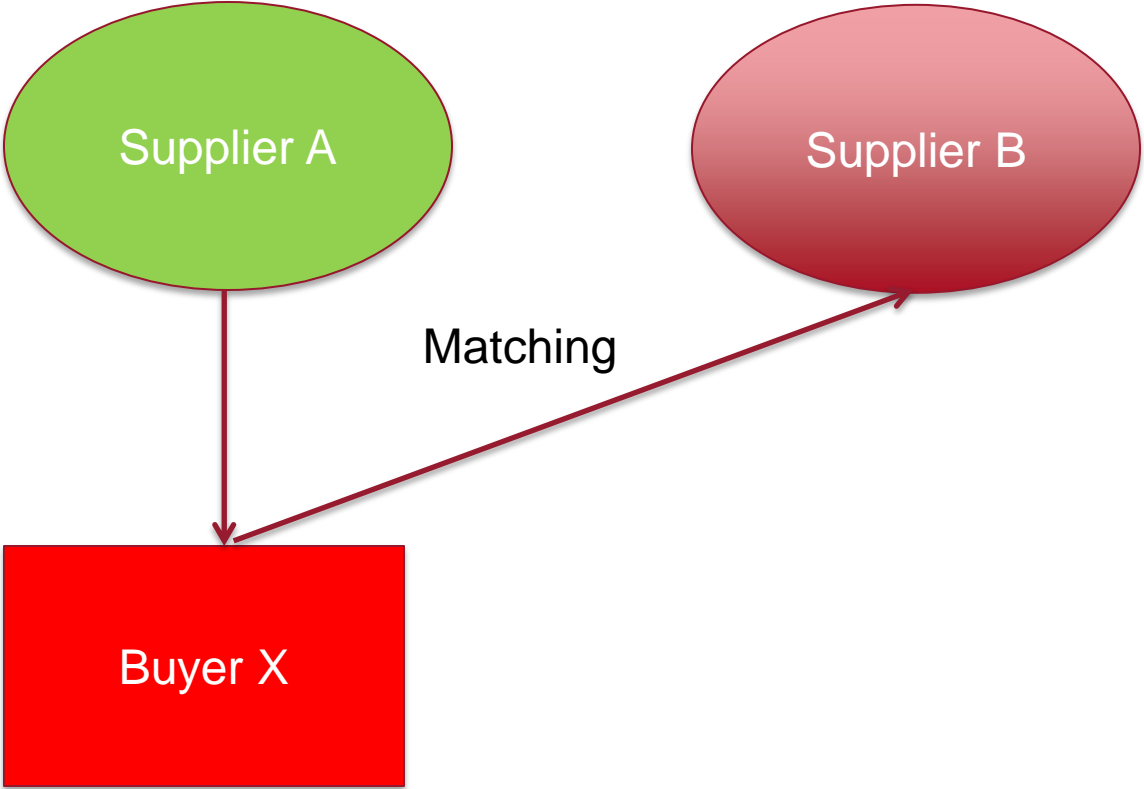
What is MFN?

- **Borrowed from international trade**
- **Covers a wide range of business configurations**
- **Key feature is “parity”**
 - The terms and conditions of sale/supply are set by reference to or even match the terms and conditions applicable to other sale/supply relationships
- **Usually focus has been on price parity but recent interest in non-price aspects of the contractual relationship as well**

Typical MFNs - Across customer agreements

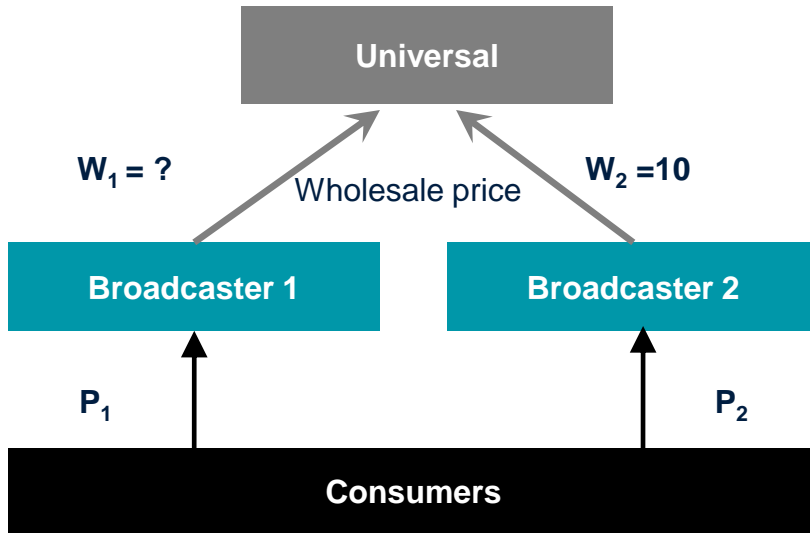


Typical MFNs - Across supplier agreement

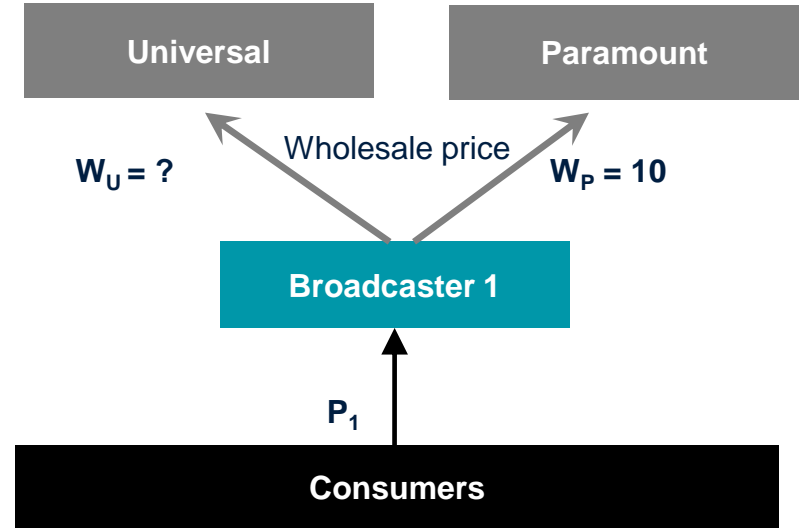


Typology

Wholesale MFNs



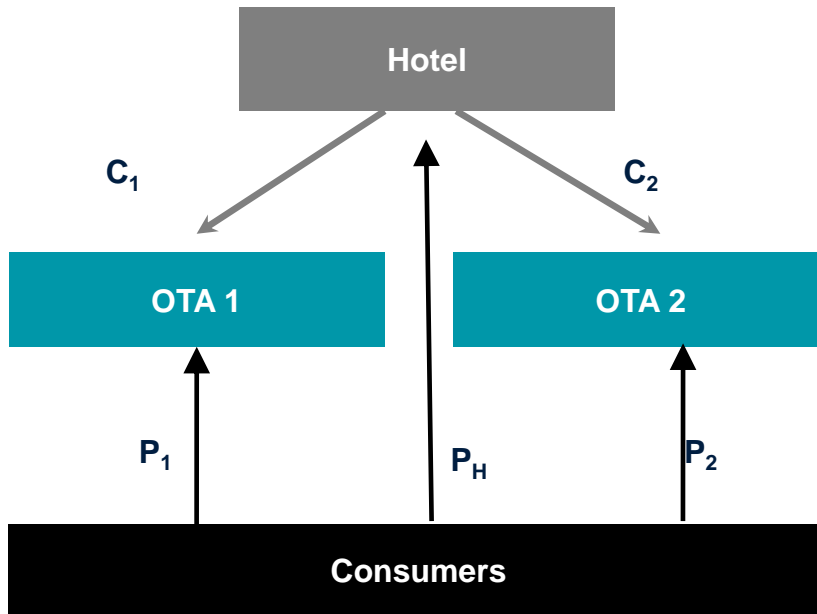
- Wholesale MFN for buyer broadcaster 1
→ $W_1 < \text{or} = 10$
- Broadcasters free to charge retail price



- Wholesale MFN for Universal
→ $W_U > \text{or} = 10$
- Film studios investigation (2002): alignment of price of studios

Typology

Retail price MFNs



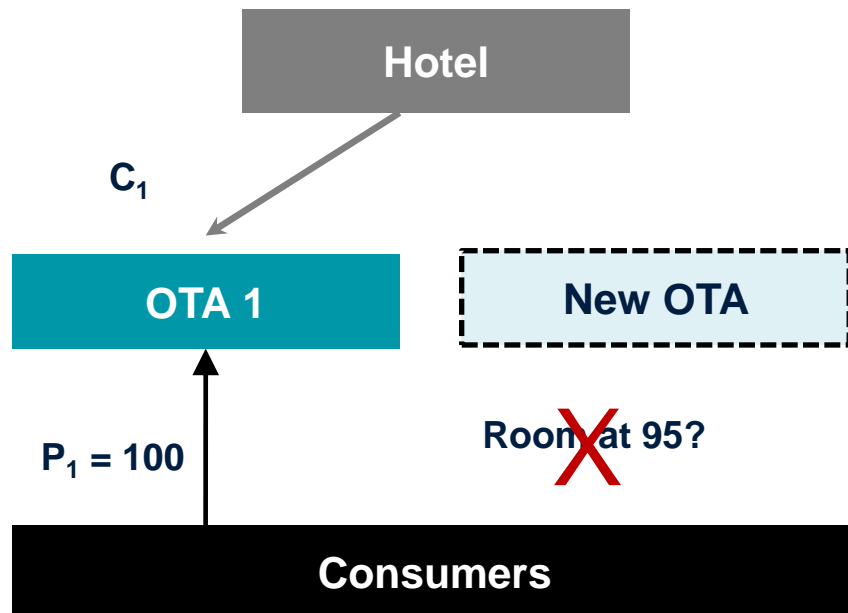
- Two types:
- 'Wide' MFN: retailer gets the lowest price relative to other retailers and supplier's own channel
- 'Narrow' MFN: retailer gets a lower price than only supplier's own channel
- Common in agency models (*hotel bookings, e-books, insurance*)

Why is it used, by whom?

- **Avoid discrimination device**
 - Create parity or level playing field
- **Protect investment and seek commitment**
- **Most often binds the supplier to the benefit of buyer or reseller**
- **Industries**
 - Common in industrial supply chains to avoid conferring cost advantage to specific buyers
 - Common in (online) retail to avoid price disparities across retailers/plaftorms

WHY IS IT A SOURCE OF CONCERN FOR AUTHORITIES?

Theories of harm



1) Potential foreclosure of new entry

- New retailer/platform cannot offer lower prices to gain market share even if it offers lower commission
 - incumbent retailer/platform has no incentive to reduce commissions
 - higher cost for suppliers, and potentially higher prices to consumers
- Similar concern for non-price parity clauses (new business models e.g.)
- Less of a concern if no across-retailer/wide MN but only narrow MFN
- More of a concern with agency agreements as retailer does not discount (*Hotels, insurance*)

Theories of harm (cont'd)

2) Can soften competition between retailers and/or between retailer and supplier

- By similar logic, due to the 'guarantee', retailer/platform in agency relationship may have a reduced incentive to compete with others through commissions
- *Hotels, insurance*
- Narrow MFNs can restrict the supplier's ability to compete through its own sales channel and reduce pricing freedom

3) Can facilitate collusion/alignment among suppliers

- Can act as a commitment device to facilitate price alignment (*Apple E-books*)
- Wide-spread MFNs with retailers reduce incentive for a supplier to defect
- Also reduces retailers' incentives to discount and could lead to RPM-type effects

ENFORCEMENT TO DATE

ENFORCEMENT FOCUS TO DATE

NON - PRICE	E-books II (Amazon)	?
	Booking.com Motor insurance (UK) E-books I (Apple)	Hollywood Studios (2002)
PRICE	RETAIL	UPSTREAM

The Booking.com saga

■ **Clause under investigation**

- Booking.com imposed to hotels MFNs whereby
 - Hotels' offers must be at least as favourable as those offered on:
 - Competing platforms ('Wide MFNs')
 - Other online and offline distribution channels, such as hotel's own website ('Narrow MFNs')
 - The MFNs applied to price (e.g. room price) and non-price conditions (e.g. booking conditions)
- Pervasiveness of the clause across the industry (e.g. Expedia)

■ **National competition authorities (NCAs) dealt with the case in the framework of the ECN**

The Booking.com saga (cont'd)

■ Legal analysis

- Booking.com as a dominant undertaking (+50% market share, indirect network effects, few competitors)
- Diverging approach among NCAs
 - **France, Italy, Sweden, etc.:** wide MFNs are anticompetitive
 - Less competition between competing platforms
 - Foreclosure of new entrants
 - Effect reinforced by pervasiveness of the clause on the market
 - **Germany:** also takes issue with narrow MFNs
 - Infringe the hotels' freedom to set their own prices
 - Makes market entry more difficult for new platforms

■ Outcome of the review

- Most Member States banned wide MFNs only
- Germany banned all MFNs (wide and narrow)

E-books I (Apple) and II (Amazon)

Same sector, same regulator, but different approach

	<i>E-books I</i>	<i>E-books II</i>
Enforcer	European Commission	
MFN scheme	<ul style="list-style-type: none"> • <u>Price</u> MFN, whereby publishers had to match any lower price for every e-book offered by other online retailers • MFN part of a coordinated plan to switch from wholesale to agency in order to increase retail prices 	<ul style="list-style-type: none"> • <u>Price and non-price (e.g. terms and conditions)</u> MFNs • Non-price MFNs relate to: business model, catalogue parity, feature parity
Legal analysis	<ul style="list-style-type: none"> • Article 101 TFEU : MFN as a tool to achieve switch from wholesale to agency • As such, restriction by object 	<ul style="list-style-type: none"> • Article 102 TFEU • Amazon's market shares above 70% • Anticompetitive effects
Outcome	Commitment decisions	

Private motor insurance market

■ Clause under investigation

- A number of price comparison websites imposed on insurers a retail MFN clause that required parity with
 - Competing comparison websites ('wide MFNs')
 - The insurer's direct channel of sale ('narrow MFNs')

■ The **UK CMA** investigated the market

■ Legal analysis

- Pervasiveness: 80% of the insurance policies sold through comparison websites included a MFN
- Anti-competitive effects?
 - Wide MFNs have anticompetitive effects
 - Narrow MFN are not anticompetitive

■ Outcome

- Ban on wide MFN only

WHAT DOES THIS MEAN FOR YOUR MFNs?

Is current enforcement a template for assessing MFNs?

- **Enforcement to date focused on scenarios where**
 - All about retail MFNs
 - At least one side of the market is characterized by monopsony power or tight oligopoly
 - Less concentrated market on the supply-side
 - Parity mechanism applied in a systematic and pervasive way
 - Risk of collusive outcome (softening of competition) and/or raise barriers to entry
- **Those scenarios were rather “extreme”**
- **Unlikely that they can be applied to all situations where MFNs are considered and applied**
- **Then, what should be the relevant analytical framework?**

What do Article 101 TFEU and Vertical Guidelines teach us?

- **Risk of horizontal collusive outcome**
 - e.g. MFN made at the request of large buyer seeking alignment to best prices that buyer has negotiated with other suppliers
 - Risk of ‘hub-and-spoke’ cartel where buyer operates as ‘hub’
 - Price alignment among suppliers
 - Lower incentive to reduce prices

- **Vertical issue: MFN as a facilitation device to RPM**
 - Para. 48 of the Vertical guidelines:
 - RPM “*can be made more effective when combined with measures which may reduce the buyer’s incentive to lower the resale price, such as the supplier printing a recommended resale price on the product or the supplier obliging the buyer to apply a most-favoured-customer clause*”
 - Reduce incentive of distributor to lower the resale price to customers

Exemptible under VBER or Article 101(3) TFEU?

- **Outside those situations, MFN should not be treated as “hardcore” restriction under the VBER**
 - Eligible to exemption if market shares of supplier/distributor each below 30%
 - Possible withdrawal in case of cumulative effect
 - Above market share thresholds, look at possible anticompetitive effects
 - Market foreclosure?
 - Collusive outcome?
 - If negative effects identified, consider efficiencies and balancing to determine if exemptible under Article 101(3) TFEU

Change the narrative

Effect-based framework called for



- **What is the MFN mechanism about?**
 - Type of MFN: retail or wholesale; agency model or not; wide vs. narrow?
 - Extent of use of MFNs in industry: widespread MFNs more likely to raise concerns
 - Used by large incumbents or entrant?
- **Market characteristics**
 - What is the level of market concentration at buyer level?
 - Extent to which products / services are highly differentiated?
 - Retail level characterized by high barriers?
 - Existing degree of market transparency?
- **Where is the harm?**
- **What are the benefits/efficiencies of the MFN scheme?**

Are there potential benefits from MFNs?

Limits
free-riding

limit 'free-riding' by suppliers (Hotel) and other retailers
e.g. a high quality OTA can be assured of returns

Prevents
hold-up
of investments

retail MFNs by incentivising investments in better marketing or price comparison features

Reduces
transaction
costs

e.g. MFNs can reduce lengthy and frequent renegotiations between

Have past intervention been effective?

Empirical ex post assessment

- **European Commission study into hotel booking cases**
 - survey of 1,600 hotels/chains and econometric analysis of meta-search price data (2015-16)
 - no evidence of change in commission after MFN ban
 - no evidence of price or availability differentials between OTAs
- **CMA study into private motor insurance wide-MFN ban**
 - econometric analysis of data on commissions (2010-2016)
 - finds that ban on wide MFNs resulted in 3-4% fall in commissions
 - overall effect on consumer prices?

[European Commission and various authorities \(2017\), 'Report on the monitoring exercise carried out in the online hotel booking sector by the EU competition authorities in 2016', April; and Competition and Markets Authority \(2017\) 'Digital comparison tools market study' final report, 26 September.](#)

Final word: Beware of national singularities

- **Enforcement may vary from one country to another**
 - Illustrated in Booking.com
 - Germany viewed both wide and narrow MFNs as illegal, contrary to other jurisdictions
- **Specific legislation may address concerns with MFNs beyond antitrust**
- **For instance, in France...**
 - Post Booking.com, France (but also Italy and Germany) adopted specific legislation to regulate the relationship between booking platforms and hotels and actually also prohibited narrow MFNs
 - More widely, the Code of Commerce provides: "*Are null clauses or contracts providing that a producer, trader or person registered with the French Trade Register has to possibility to automatically benefit from more favourable conditions granted to competitors by the other party to the contract*" (Article L.442-6 II (d)).

CONCLUDING REMARKS

QUESTIONS?

