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The case against 'Narrow' price parity clauses

Vikas Kathuria, Dr. [a,b,*], *Mark-Oliver Mackenrodt, Prof. Dr. Dr.* [c]

[a] *Observer Research Foundation, New Delhi, India*
[b] *Max Planck Institute for Innovation and Competition, Munich, Germany*
[c] *Attorney at Law (New York), Technical University Munich (TUM), School of Management and Affiliated Research Fellow at the Max Planck Institute for Innovation and Competition, Munich, Germany*

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ABSTRACT

Authors: Price parity clauses have received significant amount of attention from both academics and antitrust agencies. The predominant view is that 'narrow' parity clauses are not as pernicious as 'wide' parity clauses and they are necessary to restrict free-riding; for instance, free-riding of hotels on Online Travel Agents' (OTAs) efforts. This paper challenges this understanding. The paper builds upon a recent investigation report from the Bundeskartellamt in Booking.com case that empirically shows the insignificance of free-riding in the market for online hotel intermediation. With explicit reference to these empirical findings the German Supreme Court (BGH) has rejected a justification of narrow parity clauses and declared them as illegal. In the absence of a free-riding argument, the theory of harm that 'narrow' parity clauses stifle intra-brand competition between different distribution channels and foreclose the market for the brokerage of hotel rooms through OTAs does not meet any justification. Additionally, the paper argues that even in the presence of free-riding, the transfer of wealth from hotels to OTAs is unjustified as 'narrow' parity clauses incentivise OTAs more than the risk they undertake.

1. Introduction

There are several different business models in the e-commerce sector. At the core of every business model is the motivation of profitability. Business models are supposed to work within the boundaries drawn by the legal framework. Competition law regularly forbids business models that stifle competition and harm consumers. For instance, some vertical agreements, in light of the prevailing market conditions, may be detrimental to consumer welfare.

Price parity clauses in the online hotel booking sector have received good deal of attention in the EU from antitrust agencies and academics.[1] Outside the EU, other jurisdictions as well such as the US, India and Brazil have flagged concerns with respect to the use of these clauses in online markets.[2] So far, the predominant view seems to be that 'wide' clauses are violative of competition law; whereas, 'narrow' parity clauses supposedly capture the free-riding problem and are thus in-

[1] Price parity clauses are also referred to as retail best price clauses, MFN clauses or simply best price clauses.

[2] Competition Commission of India, Case No. 1 of 2020, Rubtub Solutions Pvt. Ltd. And MakeMyTrip India Pvt. Ltd. (MMT); see also, Market Study on E-commerce in India< https://www.cci.gov.in/sites/default/files/whats_newdocument/Market-study-on-e-Commerce-in-India.pdf> (accessed 12 December 2020); Brazil (CADE) <http://en.cade.gov.br/press-releases/booking-decolar-and-expedia-reach-cease-and-desist-agreement-with-the-brazilian-administrative-council-for-economic-defense> (accessed 12 December 2020); the US <https://techcrunch.com/2019/03/11/amazon-reportedly-nixes-its-price-parity-requirement-for-third-party-sellers-in-the-u-s/> (accessed 12 December 2020).

* Corresponding author.
E-mail addresses: Vikas.kathuria@ip.mpg.de (V. Kathuria), Mark.oliver@ip.mpg.de (M.-O. Mackenrodt).

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dispensable for the Online Travel Agents (OTAs). This is not a settled issue, however.

This paper argues that the predominant view that 'narrow' price parity clauses are pro-competitive inasmuch as they capture free-riding by hotels on platforms is not correct. The core of the article, that hotels do not free-ride on OTAs, is based on the recent investigation report[3] of the Bundeskartellamt that empirically supports its conceptual arguments in the Booking.com case (2015), where it had held narrow parity clauses as anti-competitive. Importantly, in the context of OTAs, hitherto there was no or little empirical evidence published on the actual relevance and magnitudes of free-riding behavior.[4] Thus, the investigation report will have important implications for competition policy vis-à-vis online hotel booking services. Meanwhile the German Supreme Court (Bundesgerichtshof, BGH) has declared narrow parity clauses as illegal and has based its conclusions on the empirical findings of the Bundeskartellamt's investigation report.[5] Additionally, the paper argues that 'narrow' parity clauses incentivise OTAs more than the quantum of risk that they undertake and hence the transfer of wealth from hotels to platforms is unjustified. Although, the paper scrutinises the validity of 'narrow' parity clauses in the OTA sector, where most cases have originated, the sceptism about free-riding argument may be extended to other sectors too, calling for an empirical assessment, instead of assuming the existence of free-riding.

The paper has four parts. Part 2 succinctly introduces the readers to 'narrow' and 'wide' price parity clauses. This part also provides a brief history of different antitrust agencies' position on these clauses. Part 3, the core of the chapter, sets out arguments against 'narrow' parity clauses. Part 4 concludes.

2. Price parity clauses— introduction and a brief history

Online Travel Agents (OTAs) are price comparison platforms that also provide the option of booking a hotel room through the same platform. These OTAs earn through a percentage commission per booking and through advertisements, hotel assurance and customer programmes.[6] Often, OTAs operate on 'agency model'. In the 'agency' business model, the platform does not purchase the goods from the supplier, which is the case in the 'wholesale' model. Thus, in the agency model, OTAs act as intermediaries, where the price of a hotel room is decided by the hotel.

These e-commerce platforms that provide the facility of comparison and booking are ubiquitous in the online economy. Aside from hotel booking, they are also present in the entertainment, insurance, energy supply, digital goods, and payment systems.[7] Such platforms have become indispensable for product/service providers for reaching their customers and for providing a bunch of services such as warehousing facilities, transactional support services, promotion and advertising, centralized payment processing, shipment and delivery of goods, refund and replacement etc. Importantly, these platforms that very often provide the facility of price and condition comparison, cut down the search cost of consumers.

The predominant business model of OTAs is to charge a certain percentage of the hotel room price as a commission on every booking made through their portals.[8] While portals may charge on average 10–15% on the overnight price,[9] maintaining an online booking feature on the hotel's own website costs on average 5–7% of the sales earned.[10] Naturally, therefore, it is cheaper for the hotels to offer a room on their direct channel, i.e. on their own website. Further, should competing portals choose to charge a lesser commission, they can outcompete a portal. Consequently, it is in the commercial interest of a portal to ensure customers choose it over a hotel's own booking channel or over other similar portals where the same room is available. To this end, portals resort to 'wide' and 'narrow' price parity clauses to make their offered prices more lucrative and their platform more attractive.

By way of a 'narrow' parity clause, a portal obtains rate parity with respect to the rooms that a hotel lists on its own direct distribution channel. This means that for a room, which is also listed on the OTA portal, the price which is advertised on the hotel's own website will always be equal or higher than the price on the portal. Through a 'wide' parity clause, a portal, in addition, obtains rate parity vis-à-vis other competing portals.

[3] The Bundeskartellamt, The effects of narrow price parity clauses on online sales – Investigation results from the Bundeskartellamt's Booking proceeding, August 2020 <https://www.bundeskartellamt.de/SharedDocs/Publikation/EN/Schriftenreihe_Digitales_VII.pdf;jsessionid=53BA333295E25F424F264A06525E5845.2_cid390?__blob=publicationFile&v=3> (accessed 12 December 2020).

[4] Sean Ennis, Marc Ivaldi and Vicente Lagos, "Price Parity Clauses for Hotel Room Booking: Empirical Evidence From Regulatory Change" (2020) CEPR Discussion Paper 14771<https://cepr.org/active/publications/discussion_papers/dp.php?dpno=14771> (accessed 06.06.2021) .

[5] BGH, 18 May 2021, KVR 54/20, press release no 099/2021 of 18 May 2021, https://www.bundesgerichtshof.de/SharedDocs/Pressemitteilungen/DE/2021/2021099.html?nn=10690868< accessed 06.06.2021).

[6] Market Study on E-Commerce in India (n 2), page 11. Customer programmes are subscription-based programmes that entail certain additional benefits for customers such as free cancellation, 24×7 support etc.

[7] Andrea Mantovani, Claudio Piga and Carlo Reggiani, "On the Economics Effects of Price Parity Clauses-What Do We Know Three Years Later?" (2018) 9(10) Journal of European Competition Law & Practice 650-654.

[8] For instance, in the agreement with hotels, Booking.com charged a standard commission of 10-15 % on the overnight price for each realized booking. In some cases this commission could be as high as 30-50%. Bundeskartellamt, B 9-121/13, Booking. Com decision (English)< https://www.bundeskartellamt.de/SharedDocs/Entscheidung/EN/Entscheidungen/Kartellverbot/B9-121-13.pdf?__blob=publicationFile&v=2> (accessed 13 December 2020), paragraph 18.

[9] Ibid, paragraph 18.

[10] Ibid, paragraph 21.

Wide price parity clause	Narrow price parity clause
• No lesser price on seller's own website • No lesser price on all other platforms • May also include price parity with supplier's offline price	• No lesser price on seller's own website • May also include price parity with supplier's offline price

It has to be noted that, of course, there are not only two categories of parity clauses. Depending on the drafting of the contractual clauses there is a wide range of different parity clauses which may need to be assessed individually. For example, in the Czech booking.com case, hotel owners were prohibited from offering better prices and conditions not only on their own website and in other online distribution channels but also in their own offline distribution channels.[11] Such a rather strict parity clause contains an even stronger limitation of the economic freedom of hotel owners. By contrast, in the German booking.com case the parity clauses (which were prohibited by the authority) refered only to online distribution channels.

In order to make price parity clauses more effective they are often combined with quality parity clauses and additional contractual obligations like an obligation to guarantee the availability of a certain minimum number of rooms of the same quality at a certain price.

It was initially thought that wide parity clauses serve an important purpose in that they "…resolve the hold-up problem, often manifested in vertical relationships, by removing the risk of the supplier, or other sellers, free-riding on the PCWs' [Price Comparison Websites'] investment in promoting the supplier's products and services."[12] It was subsequently recognized that wide parity clauses may result in harm as well. In particular, there are two main types of anticompetitive harm of 'wide' price parity clauses that were acknowledged by several competition authorities.[13]

1 Softening of competition among OTAs
2 Foreclosure of entry for new OTAs

Competition between OTAs is softened[14] in the presence of parity clauses because they can charge a high fee from hotels without having to be concerned that the hotel room could be offered at a lower end price in a competing distribution channel. Hotel room customers have little or no cheaper alternative to turn to for booking the same room. Accordingly, a higher commission fee and a higher room price on the OTA result in a lower impairment to the reach of the OTA vis-a-vis hotel room customers and the pressure to lower the commission fee is weaker. Vice versa, a competing OTA has a lower incentive to lower its fees for hotels because this will not lead to a lower end price as compared to other OTAs or other distribution channels. A lower price on an OTA would therefore not extend its reach. Therefore, the parity clause has a negative economic effect which is comparable to a direct coordination between OTAs and to the establishment of a minimum price floor. This restraint of competition for lower fees is more likely to occur if the OTAs have a high market share or market power.

In addition, parity clauses can foreclose market entry for new OTAs.[15] For a successful market entry an OTA platform needs to generate high network effects. A new OTA will be more attractive for customers if they can find a high number of hotels on the platform. Vice versa, the OTA will be more attractive for hotels to offer their rooms if they can reach a high number of potential guests. Therefore, successful market entry requires attracting a high number of users on both market sides. However, a new OTA who would want to offer lower fees to hotels would in fact be hindered by parity clauses to advertise lower prices to hotel customers. The reason is that the hotels who have signed best price clauses with the established and often dominant hotel platform would be required to offer the same lower end price on the established platform. As a consequence, the revenues of the hotel from bookings through the established platform tend to be reduced as the portal fee there would remain the same but the price asked for the room has to be lower.[16] For the hotel, the parity clause makes lowering the price more expensive because it has to be lowered also in other channels. This would, however, reduce

[11] UOHS (Czech competition authority), Press release of 11 November 2019< https://www.uohs.cz/en/competition/news-competition/2691-the-chairman-of-the-office-confirmed-fine-imposed-on-bookingcom-for-prohibited-vertical-agreements-preventing-competition.html> (accessed 13 December 2020).

[12] Ariel Ezrachi, "The Competitive Effects of Parity Clauses on Online Commerce" (2015) 11 (2-3) European Competition Journal, 488-519; see also Jonathan B. Baker & Fiona Scott Morton, "Antitrust Enforcement Against Platform MFNs" (2018) 127 (7) Yale Law Journal 2176-2202, footnote 23.

[13] Ibid, Baker & Morton. The authors base their reasoning on the economic studies on the adverse effect of MFN clauses on competition; See also, Simonetta Vezzoso, "Online platforms, rate parity and the free-riding defense" in P. Nihoul, P.V. Cleynenbreugel (Eds.), *The roles of innovation in competition law analysis* (2018), pp. 371-374, page 350; see also, Chiara Caccinelli, Joëlle Toledano, "Assessing Anticompetitive Practices in Two-Sided Markets: The Booking.com Cases" (2018) 14(2), Journal of Competition Law & Economics, pp.193-234.. The authors discuss the theory of harm devised by the French, Italian, Swedish and German competition agencies and also compare the analysis undertaken by these agencies; see also, Margherita Colangelo, "Parity clauses and competition law in digital marketplaces: the case of online hotel booking" (2017) 8(1) Journal of European Competition Law & Practice,3-14.

[14] See for example Bundeskartellamt- HRS, 20 December 2013< https://www.bundeskartellamt.de/SharedDocs/Entscheidung/EN/Entscheidungen/Kartellverbot/B9-66-10.pdf%3F__blob%3DpublicationFile%26v%3D3> (accessed 13 December 2020), para. 157.

[15] Ibid, para. 161.

[16] For example: A hotel room is offered on the established platform for € 100. After deduction of a 15% fee the hotel makes €85 as revenues. A start-up platform only charges 10% distribution fee in order to attract the hotel. If the hotel now offers the room for € 95,55 on this platform it pays 10% distribution fee and the hotel makes € 86 revenues on the start-up platform. But now the parity clause kicks in and the hotel has to lower its end price also on the established platform to € 95,55. With a 15% fee the hotel now only makes € 81,22 revenue per room booking on this established platform. Accordingly, in many instances the hotel will lose more revenue on the established platform than it gains on the start-up platform.

the incentive of the hotel to switch to the new platform. Also, the new platform is less likely to attract potential hotel guests if they can always find the same lowered price on the established booking platform.

In addition, parity clauses can lead to further kinds of harm to competition. It is also possible that a wide parity clause can support coordination among vendors (e.g. hotels) by discouraging cheating against an implicit or explicit coordination.[17] Also, hotels are deprived of their freedom to price differentiate between different distribution channels. If a hotel wants to lower its room prices on its own website it also has to lower the price in other distribution channels which are affected by the parity clause. This makes price cuts more costly and creates a moment of inertia when it comes to making special offers. Hotel room customers[18] can be harmed if they cannot profit from competition and price differentiation between different distribution channels and they indirectly happen to finance the higher distribution cost through higher room prices. For example, even a customer who has never used an OTA and who books a room in a different channel may have to pay a higher price. Additionally, research points out that wide parity clauses result in higher fee charged to hotels.[19]

Accordingly, most competition authorities took a stand against wide parity clauses.[20] After prohibition decisions or commitment decisions in several European Union Member states, Booking.com (July 2015) and Expedia (August 2015) eventually stopped using wide parity clauses across European Union Member States in their contracts with hotel portals for the brokerage of rooms.[21]

With respect to narrow parity clauses, there still seems to be no consensus. The German competition authority (the Bundeskartellamt) was, as it seems, the first one to hold even narrow parity clauses anti-competitive in a case against the leading OTA Booking.com. The main anticompetitive harm, as the Bundeskartellamt argued, from narrow clauses is that these clauses stifle competition among OTAs.

Although, in principle, a hotel is allowed to advertise a lower price compared to Booking.com on competing portals, it has no real incentives to do so as it is not permitted to match this price on its own website.[22] This implies that in the real sense a room's price on a hotel's website would always be at least as much as the price for that room on Booking.com, and thus always higher than the price advertised on competing platforms where a lower price was offered. In reality, therefore, a hotel would be reluctant to offer a lower price to Booking.com's competitors. This, in effect, results in lessening of competition among portals.

The anti-competitive effect is further amplified due to the minimum availability clause and the best price guarantee clause that Booking.com had also included in its agreements with hotels.[23] The possibility of competing portals charging lower commission and thus offer better prices than Booking.com cannot materialize in reality due to reputational effects and due to the possibility of a quick response by other hotels.[24] Therefore, narrow parity clauses potentially lead to similar negative effects on competition like wide parity clauses.

According to the Bundeskartellamt, narrow best price clauses also foreclosed the portal market by making entry more difficult for new hotel booking portals. Since a newcomer portal does not have the possibility to offer prices lower than the established portals, for the reasons explained above, gaining market share in such a market is significantly difficult. The Bundeskartellamt supported this reasoning by showing lack of entry by any serious newcomer in past years.[25]

Finally, the Bundeskartellamt reasoned that due to the restriction imposed on hotels, there was no incentive for hotels to compete with each other for equivalent rooms; thus, narrow best price clauses also restrict inter-brand competition among hotels.[26]

The Bundeskartellamt noted that no countervailing efficiencies were resulting from the narrow parity clause.[27] In particular, Booking.com could not prove that narrow best price clauses could prevent a decline in sales, prevent free-riding by hotels on portals as a genuine free-riding did not exist in the first place, ensure incentive to invest in the quality of the portal, and capture free-riding on the advertising investments.[28]

In June 2019, the OLG Düsseldorf overturned the decision by the Bundeskartellamt against Booking.com and held that narrow parity clauses were valid under Art 101 TFEU. The OLG Düsseldorf agreed that there was harm to competition but

[17] Baker & Morton (n 12), page 2182.

[18] See for example Bundeskartellamt- HRS (n 14) , para. 161, 165.

[19] Ennis et al 2020 (n 4).

[20] The Bundeskartellamt, Amazon removes price parity obligation for retailers on its Marketplace platform, B6-46/12, 9 December 2013<http://www.bundeskartellamt.de/SharedDocs/Entscheidung/EN/Fallberichte/Kartellverbot/2013/B6-46-12.pdf%3F__blob%3DpublicationFile%26v%3D2> (accessed 13 December 2020); The UK OFT also had opened investigation into wide MFN clauses adopted by Amazon, which was closed following Amazon's decision to end this practice< https://www.gov.uk/cma-cases/amazon-online-retailer-investigation-into-anti-competitive-practices> (accessed 13 December 2020); The Bundeskartellamt, Online hotel portal HRS's 'best price' clause violates competition law – Proceedings also initiated against other hotel portals, < https://www.bundeskartellamt.de/SharedDocs/Meldung/EN/Pressemitteilungen/2013/20_12_2013_HRS.html> (accessed 13 December 2020) (affirmed by the Disseldorf Higher Regional Court); France, Italy, and Sweden, conducted a joint investigation against Booking.com, where Booking.com committed to change 'wide' parity clauses into 'narrow' parity clauses, see Report On The Monitoring Exercise Carried Out In The Online Hotel Booking Sector by EU Competition Authorities in 2016< https://ec.europa.eu/competition/ecn/hotel_monitoring_report_en.pdf> (accessed 13 December 2020).

[21] See Ibid, Report On The Monitoring Exercise Carried Out In The Online Hotel Booking Sector by EU Competition Authorities in 2016, page 4 where a more detailed overview with regard to different Member States of the European Union can be found.

[22] Bundeskartellamt- Booking.com (n 8) paragraphs 195. For an elaborate explanation see also, Matthias Hunold, "Best Price Clauses: What Policy as Regards Online Platforms?" (2017) 8(2) Journal of European Competition law & Practice 119-124, pp 120-121.

[23] Ibid, Bundeskartellamt-Booking.com, paragraphs 190-201.

[24] Ibid, paragraphs 203-205.

[25] Ibid, paragraph 220-223.

[26] Ibid, paragraph 229-233.

[27] Ibid, paragraph 261-267.

[28] Ibid, paragraph 266 –279

argued that narrow parity clauses constituted an 'ancillary restraint' complementing the main contract between Booking.com and the hotels regarding the brokerage of hotel booking by end customers.[29] Instead of taking a full-fledged enquiry under Articles 101 (1) and 101(3) of TFEU, the OLG relied on the unwritten exception to Art 101 TFEU in the form of the 'ancillary restraint' theory.[30] According to the OLG, narrow clauses were necessary to maintain the business model of hotel portals as hotels would otherwise have the ability and incentive to advertise lower prices on their own website. It is, therefore, clear that for the OLG, hotels free-riding on portals was a possibility.

In the course of proceedings, the OLG had requested the Bundeskartellamt to empirically assess if the narrow parity clause could constitute an 'ancillary restraint' that was necessary to prevent a "disloyal exploitation" of the services provided by Booking.com by its hotel partners.[31] Thus, for the Bundeskartellamt, the center of the enquiry was to see if hotels can free-ride on a portal. The Bundeskartellamt carried out this enquiry empirically and published the results in August 2020. The empirical assessment covers a time span in which the leading portals first used wide parity clauses, then they resorted to narrow parity clauses and finally when they abandoned parity clauses.[32] The analysis in the following part draws from this report. As discussed below the BGH has – relying on the report's findings – rejected the OLG's approach and declared narrow parity clauses as illegal.

2.1. *Narrow MFN clauses and free-riding*

The proffered justifications for narrow MFN clauses, in general, are twofold. First, the "narrow" clauses restrict free-riding by the upstream supplier[33]; second, these clauses prohibit hold up by the suppliers. Both these justifications, however, can be contested.

So far as the hold-up argument is concerned, in the case of online portals, there is no product/seller specific investment that can result in a hold-up. Thus, the most prominent argument favouring narrow parity clauses is the possibility of hotels 'free-riding' on the online platforms.

Free-riding is a genuine problem where a third-party can benefit from the resources created by another without compensating for it.[34] Free-riding in the context of search platforms has been termed as "showrooming" .[35] The economic literature does not necessarily find narrow clauses to be anti-competitive.[36] This is because the literature assumes that "showrooming", i.e., a hotel free-riding on a portal is a possible scenario.[37] The Swedish competition authority was also convinced that hotels could free-ride on platforms.[38] Subsequently, the Swedish Patent and Market Court of Appeals as well declared narrow price parity clauses to be consistent with Art 101 TFEU in May 2019.[39]

Vertical restraints are justified under competition law when they minimize the risk exposure of the party that bears the same.[40] Free-riding is a valid concern when a party can benefit from the investment made by others without paying for it. To this end, restricting free-riding by a contractual stipulation can be justified. In the absence of this provision, consumers can benefit from comparing products at a showroom, and complete their purchase at a retailer's other outlets where the product is offered at cheaper prices as operational costs (e.g. rent) are not as high.

In those cases where a platform invests, it becomes prone to free-riding by other platforms who do not make the same investment. For instance, a particular e-commerce platform, that sells products, allows its users the facility to return the product within a specific time if they are not satisfied with it. It is easy to see that other platforms who do not provide this facility can offer their product at cheaper rates and hence can free-ride on the former platform. In this case, across platform parity clause may capture the free-riding behavior.

Vertical free-riding is also a possibility when a manufacturer tries to undercut a multi-product retailer who invests in promoting a particular kind of product (not a particular brand). In this case, while the downstream retailer takes the risk, the upstream manufacturer takes the rewards.

[29] OLG Düsseldorf, 4 June 2019, VI-Kart 2/16 (V).

[30] This dogmatic approach came as a change of course. In the same matter the OLG Düsseldorf had taken an interim decision in 2016. In this decision the OLG Düsseldorf had no serious doubts as to the correctness of the decision of the Bundeskartellamt. It did not apply the ancillary restraints doctrine but applied Art. 101 (1) TFEU findng harm to competition and then rejected a justification by Art. 101 (3) TFEU, see OLG Düsseldorf, 4 May 2016, VI-Kart 1/16 (V).

[31] Bundeskartellamt, August 2020 (n 3) page 1-2.

[32] Wide and narrow parity clauses were abandoned in the second half of 2015.

[33] Notably, capturing the free-rider problem through the narrow best price clause was argued (and rejected) as an efficiency gain in Booking.com case. Bundeskartellamt-Booking.com (n 8), paragraph 268. The empirical assessment of a possible free riding would be similar in the framework of the ancillary restraints doctrine and in the framework of a justification under Art. 101 (3) TFEU.

[34] The OECD < https://stats.oecd.org/glossary/detail.asp?ID=3222> (accessed 13 December 2020).

[35] See, Chengsi Wang and Julian Wright, "Search platforms: showrooming and price parity clauses" (Spring 2020) 51(1) RAND Journal of Economics, 32–58; see also, Matthias Hunold, Reinhold Kesler, Ulrich Laitenberger and Frank Schlütter, "Evaluation of best price clauses in online hotel bookings" (2018) 61 International Journal of Industrial Organization 542-571.

[36] Ibid, Wang & Wright (2020) page 53. "Thus, our findings support banning wide-PPCs, but whether narrow-PPCs should be banned as well depends on whether platforms would remain viable [i.e., the positive fee it can sustain is sufficiently high to cover the platform's cost] without them."

[37] Ibid.

[38] Matthias Hunold (n 22), page 122.

[39] Booking.com B.V. and Bookingdotcom Sverige AB v. Visita, Decision of Court of Appeal, 9 May 2019—Case No. PMT 7779-18 < https://link.springer.com/article/10.1007/s40319-019-00884-z#citeas> (accessed 13 December 2020); see also, Mark-Oliver Mackenrodt, "Price and Condition Parity Clauses in Contracts Between Hotel Booking Platforms and Hotels" (2019)50 IIC, 1131-1143. However, the Swedish court found that there is no harm to competiton in the sense of Art. 101(1) TFEU and, therefore, did not discuss freeriding.

[40] See in general, Vincent Verouden, Vertical Agreements: Motivation and Impact, in Issues in Competition Law and Policy (ABA Section of Antitrust Law 2008).

In the online economy, the possibility of 'free-riding' and the consequent efforts to capture the same increase due to at least two reasons. First, the ease facilitated by technology where consumers can, with little effort, compare prices and services. Second, the detection of free-riding by parties is also easy.[41]

Despite this, a free-riding possibility does not provide a *carte blanche* to the parties. It has been known that in order for a low-price retailer to free-ride on a high-price retailer who offers better pre-sale services "the good needs to be relatively new or technically complex as the customer otherwise may very well know what he wants from past purchases."[42] In the online economy, where not much is established about the nature of competition, a possibility of free-riding cannot always justify restrictive clauses without any supportive evidence.

After almost five years since the Bundeskartellamt passed the order in Booking.com case, it has at request of the OLG Düsseldorf come up with an empirical report to assess free-riding and other allegations. Thus, this report empirically tests the conceptual theories of the Bundeskartellamt in its 2015 order against Booking.com.

The Bundeskartellamt in its report found no significant evidence of free-riding. Around 99% of consumers who first found their accommodation on Booking.com subsequently also booked it there.[43] Importantly, it identified two distinct sets of hotel room consumers. Almost two-thirds of the bookings via hotel's own direct channel is made by those consumers who already knew the accommodation before the booking.[44] The remaining one-third who booked via hotel's own direct channel without knowing the hotel already, were mostly directed by Google or "another website".[45] Booking via online hotels platforms constitutes the majority of online sales as around three-quarters booking happen through the hotel platforms.[46] The empirical findings also showed that even long after the abandonment of the parity clauses consumers booked the hotel room where they first found it with 99% booking it on booking.com after finding the accommodation there which points to the absence of a significant free riding.[47]

The Bundeskartellamt shows in its report that the elimination of the narrow MFN clause did not harm Booking.com's market success and that Booking.com did not suffer any appreciable disadvantage due to the abandonment of the MFN claus. Booking remains the leading online hotel platform in Germany, and even further consolidated its market position and achieved enormous growth rates.[48]

Booking had argued before the Bundeskartellamt that elimination of the narrow price parity clause would result in losses in sale and hence it would not have sufficient incentives to invest in the quality of the portal.[49] The Bundeskartellamt had refuted the argument by observing that reduced bookings due to the elimination of the narrow parity clause would trigger investment in the attractiveness of the portal.[50] This turned out to be true as inferred from the increased market share of Booking.com. Both Booking.com and Expedia witnessed an increase in their market share from 2013 to 2017 in Germany.[51] Notably, both these operators had ceased resorting to any price parity clauses from 2015. The BGH, in its recent judgment, referred to these findings and argued that the parity clauses are not objectively necessary for the operation of the platform services as would be required to apply the ancillary restraints doctrine.[52] In rejecting the application of Art. 101 (3) TFEU the BGH argued that the Bundeskartellamt's findings did not contain any indication that free riding would jeopardice efficient operation of the platform while the restrictive effects of the parity clauses on the hotel's own online distribution were significant.[53] After the elimination of the parity clauses the price differentiation between the hotels own websites and the platform noticeably increased.[54]

It also appears that the elimination of narrow parity clauses did not drastically reduce the level of commission charged by the platforms. According to the market investigation, the average amount of commission brokered via the three major platforms for hotel rooms in 2017 was approximately 12–17% of the room price.[55]

The free-riding argument appears to be the primary defense to retain the narrow MFN clause. The above section, however, shows that in reality, the free-riding defense did not hold up against empirical scrutiny undertaken by the Bundeskartellamt. It is important to note that a free-riding possibility arises only with respect to the percentage cut on each booking. If portals adopt a different business model, the possibility of free-riding can be avoided.

Remarkably, Montvani et al. find that the removal of both types of parity clauses post Macron Law in France led to a decrease in the hotel prices listed on Booking.com, resulting in savings for consumers.[56] This work, therefore, supports the theory of harm vis-à-vis both types of parity clauses. Previ-

[41] Simonetta Vezzoso (n 13), page 347. The author notes "…it is much more practical to enforce a contractual condition of this sort in online markets, where economic agents are already routinely tracking the prices of competing offers algorithmically."
[42] Luc Peeperkorn, "The Economics of Verticals", Competition Policy Newsletter 1998- number 2- June, page 6.
[43] Bundeskartellamt, August 2020 Report (n 3) paragraph 142.
[44] Ibid, page 8
[45] Ibid, page 8.
[46] Ibid, page 4.
[47] Ibid, page 6.
[48] Ibid, page 3.
[49] Bundeskartellamt- Booking.com (n 8), paragraph 273.
[50] Ibid.
[51] Bundeskartellamt, August 2020 Report (n 3), paragraphs 8-9.
[52] BGH, 18 May 2021, (n 5).
[53] Ibid
[54] Bundeskartellamt, August 2020 Report (n 3), page 5.
[55] Ibid, paragraph 74.
[56] Andrea Mantovani , Claudio A. Piga and Carlo Reggiani, "Online platform price parity clauses: Evidence from the EU Booking.com case" (2021) European Economic Review 131. This finding is more nuanced though. The authors note that " the initial positive response faded away in the medium-run, in which relevant price reductions (although not always statistically significant) were registered only for highly-rated and chain hotels. This suggests that the policy intervention might have strengthened the position of those organized structural units that were able to efficiently use their direct channel and, probably, renegotiate the commission fees with OTAs. Instead, independent and family run hotels were probably not able to modify their contractual terms. Policy makers may therefore need to resort to additional provisions, such as imposing limits to commission fees…" page 16.

ously, Hurnold et al. showed that the abolition of narrow parity clauses in Germany led to decrease in prices on the direct channel (especially for chain hotels).[57] The authors attributed this result to the presence of free-riding, which the Bundeskartellamt report negated. The combined reading suggests that while even in the absence of such clauses platforms could grow, the removal led to positive effects on consumer welfare too.

In a recent development, the German Supreme Court (BGH), on appeal, in May 2021, upheld the Bundeskartellamt's decision and declared narrow parity clauses as illegal.[58] In this decision the BGH based its conclusions on the empirical findings of the Bundeskartellamt's investigation report. The BGH pointed out that narrow parity clauses restrict competiton because they prohibit hotels from offering lower prices to customers in the hotels' own online distribution channels (i.e. on the hotel websites) as compared to the prices on the platform. Accordingly, hotels could not pass on a lower price to customers which did not reflect the platform's percentage fee[59] even if the customer did not use the platform.

It is important to note that the BGH based on systematic considerations expressly rejected the applicability of the ancillary restraints doctrine and, in addition, noted that based on the empirical findings, in any case, the doctrine's requirement were not met with regard to the parity clauses. The ancillary restraints doctrine provides for an unwritten exemption to the finding of a restraint of competition in the sense of Art. 101 (1) TFEU. This requires that a restriction – in this case the best price clause – is directly related and objectively necessary to the operation of the non-restrictive main agreement – in this case the brokerage of rooms by the platform – and proportionate.[60] Unlike a justification according to Art. 101 (3), the application of the ancillary restraints doctrine does not involve a balancing of anti-competitive and pro-competitive effects.[61] The BGH held that purported efficiencies of the parity clause like securing an adequate remuneration for the platform service through avoiding a free rider problem would need to be carefully balanced against its anti-competitive effects and such a balancing exercise could exclusively be conducted within the framework of Art. 101 (3) TFEU.[62]

The BGH further found that the parity clauses are not exempt by the vertical block exemption regulation because the hotel platform's market share exceeded 30%. Also, the BGH held that the requirements for a justification of the parity clauses according to Art. 101 (3) TFEU were not fulfilled. This would require that best price clauses contribute to an improvement of the production or distribution of goods or to promoting technical or economic progress. In addition, the restricitions by the parity clause would need to be indispensable for achieving these efficiencies and to be proportionate. The BGH stated that a platform offers to consumers a comfortable and attractive service for finding and buying products and services and to hotels a wider market reach. However, the BGH found that the parity clause is not indispensable for the provision of these platform services.[63] The BGH notes that the existence of a free rider scenario may not be excluded. However, the BGH referred to the empirical examinations of the Bundeskartellamt and found that there are no indications that free riding would jeopardize the efficiency of the platform's service.[64] At the same time the best price clause would considerably restrict the hotel's own online distribution of hotel rooms which is independent from the platform.

3. What if narrow clauses cause no harm to competition and capture a genuine free-riding?

The Swedish Court of Appeals in June 2019 rejected the theory of harm that had convinced the Bundeskartellamt in 2015 to sanction narrow parity clause in the Booking.com case. The Swedish court rejected the robustness of the economic evidence that showed that narrow parity clauses reduce competition in the online hotel booking platform market and that prices for hotel rooms would be lower without narrow parity clauses.[65] Some might, therefore, argue that the economic evidence supporting the theory of harm is not conclusive. Additionally, whereas the Bundeskartellamt found no proof of free-riding, what should be the outcome if there does exist free-riding as some have noted? Should in such cases where there is no harm to competition in the first place or there does exist a valid free-riding defense, narrow parity clauses be justified? There are good reasons to prohibit narrow clauses even in such cases.

As seen above, both wide and narrow price parity clauses ensure that customers complete their purchase on the portal. This results in hotels paying the commission to portals. If most booking transactions take place through portals it will result in wealth transfer from hotels to portals in the form of commissions. In view of the indispensability of portals for hotels to reach a high number of customers hotels cannot stop availing their services. Considering, however, that in the market for the brokerage of rooms through platforms, hotels bear the risk of non-or under-utilization of hotel operations, parity

[57] Hunold et al (n 35).
[58] BGH, 18 May 2021 (n 5).
[59] Ibid.
[60] See for example ECJ, 11 Sept. 2014, C-283/12 – *MasterCard*, para. 89; General Court, 18 Sept. 2001, T-112/99 – Metropole Television (M6), para. 106.
[61] See for example General Court, 18 Sept. 2001, T-112/99 – Metropole Television (M6), para. 107, 108.
[62] BGH, 18 May 2021 (n 5). In addition, given the high relevance of online platforms in very different sectors of the economy the legal assessment of parity clauses which can take different shapes should rather be based on the established and more nuanced principles of Art. 101 (3) TFEU, Mark-Oliver Mackenrodt (n 39), page 1142.
[63] BGH, 18 May 2021 (n5).
[64] Ibid.
[65] 9 May 2019, PMT 7779-18, (n 39) pp 18-27; for a critical assessment of the court's reasoning see also, Mark-Oliver Mackenrodt (n 39), pages 1137-1139. The Swedish Court had argued that there was no restraint of competition by the parity clause because the empirical evidence at hand would show that after the abandonment of the parity clauses hotels anyway did not offer lower prices in their own distribution channel. However, this argument could be interpreted as an indirect admission that the parity clause is not necessary for the operation of the platform. In any case, it should have been sufficient for a restraint of competition that hotels were deprived of the possibility to offer lower prices on their websites.

clauses distort the equitable distribution of incentives. Thus, the risk that hotels incur does not result in the accrual of proportional rewards.[66] In the long run, this may adversely affect the quality of hotel services.

In the proceedings before the Bundeskartellamt, hotels also expressed concerns about parity clauses causing loss of pricing sovereignty.[67] So far as the loss of sovereignty is concerned, it cannot be a reason to be sceptical of any vertical agreement, as all restraints impose some restriction on the sovereignty of the parties to the agreement. Such restrictions can either relate to price (e.g., maximum retail price) or non-price conduct (e.g., exclusive dealing, exclusive distribution etc.) However, the loss of pricing sovereignty in the hotel brokerage market through OTAs is connected with the risk of non-utilization or under-utilization of the hotel business, as such risk is borne solely by the hotels, not by the hotel portals.[68] Additionally, a prohibition on narrow parity clauses also lends an opportunity to the hotels to control prices and terms on their own channel that can be quickly altered in response to the demand.[69] This, in turn, is beneficial for both hotels and consumers.

In the markets, whenever a 'free-riding' argument is raised, resort can be made to the risk and incentive equation. It is difficult to quantify the investments made by parties to the transaction and then determine their proportionate return. When, however, the risk and incentive seem disproportionate, and an alternative more benign business model is possible, parties can be directed to the alternative.

The present business model of OTA is charging the cost-per-acquisition (CPA) percentage fee. If CPA were the only business model, Booking could have made a better case before the Bundeskartellamt. Even though the Bundeskartellamt was not required to assess the indispensability requirement, as Booking.com could not show any efficiencies resulting from the narrow clause in the first place, it still went ahead and pointed to alternative business models that could still be possibly profitable for Booking.com, while ensuring customers benefitted from the service package provided by hotel portals without adverse effects on competition.[70] The Bundeskartellamt had suggested some other business models, such as fees for end customers, cost-per-click payment, or listing fees for the hotels. Even if hotels could free-ride on portals, narrow clauses would still be anti-competitive as other less restrictive business models could be possible.[71]

Some have shown scepticism about the viability of the registration fee model; however, other models such as per-click fees or referral fees could still be viable.[72] The Bundeskartellamt's latest report supports this argument by showing that even without narrow parity clauses Booking.com could increase its market share.

The Bundekartellamt did not consider it to be sufficiently shown that in the absence of parity clauses there would be a lack of incentive for the OTA to invest in its attractiveness.[73] Indeed, even absent parity clauses OTAs have –out of their very own business interest – an incentive to invest in the convenience of the portal. If the OTA is more attractive it is more likely to attract hotel room customers to its website.

It is interesting to note that this value capture, although not equitable, cannot be sufficiently addressed or corrected by antitrust law. But as one can observe, harm to welfare still occurs due to the misallocation of incentives. Against this backdrop, a regulation that restricts OTAs to mandate 'narrow' MFN seems justified. Notably, several jurisdictions have introduced special rules – usually in other codes than the antitrust code – to interdict wide as well as narrow parity clauses.[74] For example, Austria has included a prohibition of best price clauses in the hotel sector into the black list of illegal clauses of its unfair competition law.[75] On the European level, Art. 10 (1) of the platform to business regulation (P2B) 2019/1150[76] addresses parity clauses. It requires that an intermediation platform which uses best price clauses in its terms and conditions indicates the main economic, commercial or legal considerations for these restrictions. The reasons need to be easily available to the public. The P2B regulation applies since 12 July 2020 in the Member States. However, a mere transparency approach may not be sufficient to address the potential harm from best price clauses. In any case Art. 10 (2) P2B regulation explicitly states that it does not exclude other legal limitations on the use of parity clauses which may derive from other legal acts of the European Union or from laws of the Member States. In

[66] Bundeskartellamt- Booking.com (n 8), pages 70-71. "In this survey, a significant majority of hotels stated that they highly value their power to set prices, which they view as the entrepreneurial counterpart of the risk of non- or under-utilization of their hotel operations that is borne by them alone and not, for example, by a hotel booking portal such as Booking."

[67] Ibid, paragraph 47, also paragraph 234.

[68] Ibid.

[69] Ibid, paragraph 195-196.

[70] It would be to the OTA to show that a particular feature of the business model is indispensable. The economic freedom to design a particular business model finds its limits in the legal order and, in particular, in competition law, see for example German Federal Supreme Court, 23 June 2020, KVR 69/19 – Facebook (interim decision), para. 122.

[71] Guidelines on vertical restraints, SEC(2010) 411, paragraph 125; see also, J. Faull and A. Nikpay (eds.), The EU Law of Competition (3rd edn, Oxford University Press, 2014) paragraph 3.494. "A restriction is indispensable if its absence would eliminate or significantly reduce the efficiencies achieved by the agreement or make it significantly less likely that they will materialize. The assessment of alternative solutions must take into account the actual or potential improvement in competition by the elimination of a particular restriction or the application of a less restrictive alternative."

[72] Chengsi Wang and Julian Wright, (n 35) page 53.

[73] Bundeskartellamt- Booking.com (n 8), paragraph 273.

[74] See for example: France: Art. 133 Abs. 2 der französischen Loi N° 2015-990 („loi Macron"), Italy: Art. 50 Legge annuale per il mercato e la concorrenza v. 29.8.2017; Belgium: Art. 6 Loi relative à la liberté tarifaire des exploitants d'hébergements touristiques dans les contrats conclus avec les opérateurs de plateformes de réservation en ligne v. 30.7.2018.

[75] See § 1 (4) no 2 öUWG, no 32 in the blacklist of öUWG.

[76] Regulation (eu) 2019/1150 of the European Parliament and of the Councilof 20 June 2019 on promoting fairness and transparency for business users of online intermediation services <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R1150&from=EN> (accssed 06.06.2021).

the drafting of the EU Digital Market Act (DMA), rules on parity clauses are discussed which go beyond a mere transparency approach. Article 5 (b) of the proposed DMA prohibits wide parity clauses.[77] Switzerland is also deliberating to prohibit both clauses.[78]

3.1. *So what do OTAs do?*

Indeed, hotel portals play a major role as an alternative distribution channel by offering a bouquet of "search, compare, and book". In essence, these platforms are an alternative channel to reach out to the customers. The task of an OTA is to facilitate the ease of search and reduce its cost. This ease of booking after comparison is a demand-enhancing feature of platforms. Such demand-enhancement feature can still be retained when OTAs practice a business model without parity clauses. Accordingly, the general benefits of platforms as a distribution channel cannot be invoked as a justification for parity clauses.[79] To serve as a justification the benefit would need to be directly linked to the parity clause.

When platforms get interested in the prices sellers charge to buyers, it takes away a part of sellers' autonomy to act in the marketplace. Aside from the Bundeskartellamt, the market study on e-commerce in India as well resonates this concern by observing that "[b]usinesses, especially in the service categories, also pointed out the rather disquieting trend of their decision-making power vis-à-vis key business variables *de facto* being shifted to the intermediary platforms."[80] Maybe other business models are not as financially lucrative as the commission model, yet they can be compliant with competition law.

The Bundeskartellamt discussed alternative business models while denying that including the narrow best price clause was indispensable so far as the third criterion of Art 101 (3) is concerned.[81] Some realistic alternatives could include listing fees, membership models and advertising space-related fees. Additionally, it also accepted the continuation of the commission model without narrow best price clauses.[82] All the efficiencies that PCWs offer with the 'narrow' clause can still be retained if they charge a fixed fee instead of taking a cut per transaction. This is evident from the latest report by the Bundeskartellamt. The only viable reason to practice 'narrow' clauses would be to avoid 'free-riding'. A high-value and high-cost platform can still survive if its practices fixed fee revenue model. As this platform provides better quality, it may charge a higher fee to sellers.

4. Conclusion

Price parity clauses in online markets have drawn considerable attention from both antitrust agencies and academics. After some years of litigation and debate, a consensus has emerged on the adverse effects of wide parity clauses on competition. The welfare effects of narrow parity clauses, however, are still not clear and consequently different antitrust agencies have treated them differently. This legal uncertainty around narrow parity clauses was the motivation behind this paper to assess the effects of these clauses on competition.

The paper succinctly introduced narrow and wide parity clauses. It also briefly looked at the treatment of narrow parity clauses by different antitrust agencies. The main reason to practice narrow parity clauses, as evident from the reasoning of antitrust agencies and courts and as proffered as a justification, is to restrict free-riding of hotels on the aggregator OTA platforms. The paper showed, relying upon the empirical evidence presented in the latest investigation report of the Bundeskartellamt, that a theoretical possibility of free-riding does not materialize in reality in the market for the brokerage of hotel rooms through OTAs. The BGH in its decision form May 2021 which declared narrow parity clauses as illegal relied on these empirical findings. The investigation report showed that there are two distinct user groups—one—that constitutes the majority—who search hotel rooms on OTAs and also complete their booking there; second, who already know about the hotel and prefer to book via the direct channel. It also showed that even without the narrow parity clauses, Booking.com and Expedia witnessed a growth in their market share. Thus, the prohibition of narrow parity clauses did not harm their businesses.

The paper also discussed an alternative hypothetical scenario where narrow parity clauses do not lead to any harm to competition among OTAs or among hotels, and also restrict free-riding by hotels on OTAs. Even in such cases, prohibiting narrow parity clauses is welfare-enhancing as while hotels bear the risk of non-or under-utilization of rooms, parity clauses result in wealth transfer from hotels to portals who bear no such risk. Thus will harm the hotels in the long run.

What is more, OTAs can switch to other more benign business models as the Bundeskartellamt had discussed in its 2015 order. All in all, the paper showed that OTAs, even though indispensable in terms of the services offered, are just one out of several possible alternative channels to reach out to customers and all the benefits of their services can be retained even with the removal of narrow parity clauses.

Declaration of Competing Interest

The authors declare no conflict of interest whatsoever.

Data availability

No data was used for the research described in the article.

[77] Proposal for a Regulation of the European Parliament and of the Council on contestable and fair markets in the digital sector (Digital Markets Act) COM(2020) 842 final< https://ec.europa.eu/info/sites/default/files/proposal-regulation-single-market-digital-services-digital-services-act_en.pdf> (accessed 06.06.2021)

[78] Switzerland opens consultation on prohibiting online booking platforms from including price parity clauses in contracts with hotels, 25.11.2020 <https://www.cms-lawnow.com/ealerts/2020/11/switzerland-opens-consultation-on-prohibiting-online-booking-platforms-from-including-price-parity> accessed 0606.2021).

[79] Bundeskartellamt- Booking.com (n 8), paragraph 261-264.

[80] Market Study on E-Commerce in India (n 2), page 23.

[81] Bundeskartellamt- Booking.com (n 8), paragraph 288-295.

[82] Ibid, paragraph 296.