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Vertical Block Exemption Regulation (VBER)
HOTREC feedback on European Commission Inception Impact Assessment

1. Introduction

HOTREC welcomes the European Commission's intention to revise the EU Vertical Block Exemption Regulation (VBER) before its expiration on 31 May 2022 and the possibility to provide feedback on the Inception Impact Assessment published on 23 October 2020.

The VBER exempts from article 101(1) those vertical agreements for which it can be assumed with sufficient certainty that they satisfy the conditions of Article 101(3) of the Treaty. In particular, these agreements must fulfil the criteria of article 2, the market share threshold indicated in article 3 (no more than 30% of market share held for the buyer and the seller) and shall not contain hard core restrictions mentioned in article 4 (e.g. price fixing, some territorial restrictions, etc.)

Our response focuses on MFN/parity clauses imposed by Online Travel Agent platforms (OTAs), which are considered as vertical agreements and may fall in the scope of this regulation if conditions are met. **The revision of the VBER and related guidelines represents an important opportunity to address MFN/parity clauses imposed by OTAs on hoteliers.** This market is currently characterised by the dominance of 3 market players which operate with almost identical terms and conditions on the market of digital distribution and intermediation of hotel services. The VBER was conceived at the time where this market was emerging and these market-players had not acquired yet such collective dominant position. The VBER is currently not fit to apprehend this market.

With regard to the VBER Inception Impact Assessment, **HOTREC would urge the European Commission to address parity obligations (point d) in the upcoming revision of the VBER**:

- Exclude Option 1 (no policy change)
- Consider Option 2 as long as it explicitly removes the benefit of the VBER for MFN clauses in the market of digital distribution and intermediation of hotel and other accommodation services. However, we would underline that such an option would need to adequately address the potential legal uncertainties and loopholes as to prevent OTAs from using the VBER as the basis for a continued use of MFN clauses.
- Favour Option 3: removing the benefit of the block exemption for all types of parity obligations by including them in the list of excluded restrictions (Article 5 VBER), thus requiring an individual effects-based assessment in all cases.

MFN clauses should be included in the list of hard-core restrictions (art. 4 VBER), in line with the prohibitions established in several Member States (e.g. France, Italy, Austria, Belgium) . MFN clauses are widespread in online distribution markets. Existing competition case law on hotel booking portals show that MFN clauses entail – by object and by effect – massive restrictions of competition within the meaning of art. 101 (1) TFEU. The VBER / VGL do not provide a sufficiently robust basis to prevent them, creating legal uncertainties. MFN clauses have become the key instrument for dominant suppliers, purchasers and internet platforms to shield themselves against competition. There is absolutely no benefits neither for competition nor for consumers which could justify the use of MFN clauses. Existing case law shows that the allegations that MFN clauses would be pro-competitive (i.e. free-riding argument) are unfounded.

2. THE VBER and MFN/parity clauses

The current VBER gives vertical agreements between companies with less than 30% market share a presumption of compliance with EU competition rules. This means that agreements with OTAs with less than 30% market share on the relevant national market (e.g. HRS, Expedia in some countries) benefit from this presumption of compliance. Moreover, companies with more than 30% market share do not benefit from this presumption of compliance, but

this does not mean that their vertical agreements are per se anti-competitive, it only means that a case by case analysis needs to be made in such cases.

The difficulty to make a correct delimitation of the relevant market share (which evolve rapidly) and the fact that MFN/parity clauses are not really mentioned in the VBER and guidelines justify in themselves the need to revise both the VBER and the guidelines.

The main proposals by HOTREC for the revision of the VBER are the following:

- Need to revise the market share threshold for agreements with online platforms (as it is not for for digital markets) and replace it with a dominance test;
- For agreement with online platforms, MFN should be considered as a hard-core restriction, meaning that the clauses are per se considered anti-competitive (whatever the market share).

MFN clauses imposed by OTAs on hoteliers have drawn specific attention in the Evaluation support study on the EU competition rules applicable to vertical agreements in the VBER undertaken in 2020. The study explicitly concludes that MFN clauses applied by OTAs in the hotel industry generates anti-competitive effects (page 145):

"Retail MFN clauses have recently become prevalent in the online world and have been used by online platforms to bind suppliers into price parity guarantees. In this context, concerns have been raised by interviewed stakeholders on the application of MFN clauses by online travel agencies in the hotel industry. The theoretical literature and the competition authorities that have investigated 'wide' and 'narrow' MFN clauses do not appear to have reached a consensus on whether narrow MFN clauses raise less competition concerns than wide MFN clauses. However, as regards this evaluation study, qualitative insights gained from the stakeholder interviews and the results of the econometric analysis suggest that narrow MFNs have generated the same anti-competitive effects as wide MFNs in the hotel sector.

These findings appear to be in line with the observation in the recent report on Competition policy for the digital era[1] that "if competition between platforms is sufficiently vigorous, it could be sufficient to forbid wide MFNs while still allowing narrow MFNs. If competition between platforms is weak, then pressure on the dominant platforms can only come from other sales channels and it would be appropriate for competition authorities to also prohibit narrow MFNs."

However, the same report emphasises that the effects of MFN clauses depend on the particular characteristics of the market in which they are used, and therefore a case-by-case analysis is necessary. The evidence collected in the study does not support general conclusions about the effects of narrow as compared with wide MFNs in sectors other than the hotel sector. Indeed, outside this sector, the study has not found any widespread evidence that narrow or wide MFN clauses produce anti-competitive effects."

The findings of the econometric analysis in this study suggest that:

- "narrow MFN clauses limit competition in the hotel booking sector, and result in higher prices for consumers. Given that no statistically significant effect on demand was identified, a ban on narrow MFN clauses (in the observed countries) appears to have increased consumer welfare" (page 113)
- "There is also evidence of cumulative effects of MFN clauses being associated with higher hotel own prices. This can be interpreted as reflecting a generally weaker competition in the market for online hotel booking associated with a wider use of MFN clauses by platforms." (page 121)

We would also draw attention to the findings of the German BundesKartellamt report on 'The effects of narrow price parity clauses on online sales–Investigation results from the Bundeskartellamt's Booking proceeding'[2]. The main findings of the report, which investigated the period from 2015 until the summer of 2018 during which price parity clauses were not applied by OTAs on hoteliers, make the case for including such MFN clauses as hardcore restrictions:

- The elimination of narrow price parity clauses did not harm the leading OTA on the German market (Booking.com) which remained 'almost indispensable in economic terms' for hoteliers;
- More than half of the accommodations cooperating with Booking.com made use of the options for price differentiation which was (temporarily) available between Booking.com and the hotels' own direct online sales.

[1] European Commission (2019). Competition policy for the digital era. Available at: https://ec.europa.eu/competition/publications/reports/kd0419345enn.pdf

2 The effects of narrow price parity clauses on online sales–Investigation results from the Bundeskartellamt's Booking proceeding. Series of Bundeskartellamt papers on "Competition and Consumer Protection in theDigital Economy", August2020 https://www.bundeskartellamt.de/SharedDocs/Publikation/EN/Schriftenreihe_Digitales_VII.pdf;jsessionid=AA7B408CA649249EDF9D982F176D16D6.1_cid387?__blob=publicationFile&v=3

- Consumers rarely compare prices and they book where they first found the accommodation, which rules out any significant free-riding activity;
- Most consumers who use the hotels' direct online sales channels have already been familiar with their hotel prior to booking.

3. HOTREC detailed position on VBER

The VBER was conceived at the time where the online travel agent market was emerging. Market-players had not acquired yet such a collective dominant position. The VBER is currently not fit to apprehend this market, as it is based on a traditional supply chain concept which does not match digital market realities and new dominance of online platforms.

OTA Market dominance
Today, 93% of the market is controlled by 3 Online Travel Agents, and they impose very similar conditions for hotels. The VBER uses a market share test to assess the market powers of undertakings. The 30% market share threshold on the distributor side has proven to be ill-suited in the online environment.

This test gives uncertainty on the demarcation of the market, especially on online markets and is not the most relevant to assess market dominance in online platform markets. We propose to replace the market share test by a dominance test which would a) interconnect arts. 101 and 102 TFEU, b) allow undertakings to use the case law of art. 102 TFEU (on abuse of dominant position and collective dominance) for their self-assessments and c) oblige undertakings to make a comprehensive analysis of the market conditions and their relative market power before imposing vertical restraints.

Narrow MFN Clauses – price parity
A 2nd issue results from the wording of art. 4 (1) VBER on the prohibition of resale price maintenance. The economic effects of MFN clauses are largely identical to those of RPM, but are not caught by the wording of art. 4 (1) VBER, because the wording does not cover cases in which a powerful "buyer" imposes RPM obligations on the supplier (e.g. MFN clauses). The anti-competitive effects are, however, identical in both cases. Art. 4 VBER should therefore abandon the concept of buyer / supplier but follow a holistic approach through a ban as a hardcore restriction under art. 4 (a) VBER of any restriction of a trading partner's liberty to freely set its sales prices. Restriction of sales prices are not compatible with EU competition law and should in any event only be justifiable under art. 101 (3) TFEU.

MFN clauses should be included in the list of hard-core restrictions (art. 4 VBER), in line with the prohibitions established in several Member States. MFN clauses are widespread in online distribution markets. Existing competition case law on hotel booking portals show that MFN clauses entail – by object and by effect – massive restrictions of competition within the meaning of art. 101 (1) TFEU. The VBER / VGL do not provide a sufficiently robust basis to prevent them, creating legal uncertainties. MFN clauses have become the key instrument for dominant suppliers, purchasers and internet platforms to shield themselves against competition. There is absolutely no benefits neither for competition nor for consumers which could justify the use of MFN clauses. Existing case law shows that the allegations that MFN clauses would be procompetitive (i.e. free-riding argument) are unfounded.

Towards a new VBER
The VBER is not restrictive enough to ensure that only competitively neutral agreements are caught by the block exemption. It is based on a traditional supply chain concept which does not match digital market realities. Using a market share test instead of a dominance test includes jointly dominant undertakings in the ambit of the block exemption as long as their market share remains short of the 30%. From a competition policy and economic perspective, however, it does not seem appropriate for online markets. Art. 4 VBER should be rephrased to ensure that the exemption does not apply to undertakings which solely or together with others hold a dominant position within the meaning of art. 102 TFEU.

For the reasons stated above, hotels and other accommodation providers are still today exposed to MFN clauses across the EU – in particular in those EU Member States where neither the national competition authority, nor the legislator has intervened, such as in Spain or the Netherlands for instance. If the VBER and VGL were prolonged without changes, the legal uncertainties and shortcomings as described above would persist and – most importantly – the online booking portals would likely continue to use these legal uncertainties and loopholes as the basis for a

continued use of MFN clauses. The massive restriction of competition caused by these clauses to the detriment of accommodation providers and end-customers would continue.

VBER and brand-bidding

Article 2(3) of the VBER provides that the block exemption applies to contractual provisions that regulate the use of the supplier's Intellectual Property by its distributors (provided that all conditions for the exemption are satisfied). However, the Guess case (Case AT.40428, decision of 17 December 2018) has created legal uncertainty on the possibility for companies who do not operate within a selective distribution system to pursue a strategy of imposing restrictions on keyword bidding in online search advertising auctions.

It would be excessively far-reaching to interpret the Guess case as meaning that any restriction on keyword bidding in online search advertising would amount to a by object infringement and/or a hardcore restriction under Article 4(b) or 4(c) of the VBER. Therefore, a clarification is needed that the VBER applies to provisions which relate to both the use and/or the limitation to use the supplier's Intellectual Property, both offline and online – especially in cases where there is no selective distribution systems in place. This is fundamental in the hospitality sector, as online distribution is controlled by a duopoly of two dominant platforms which enjoy significant market power. Given the massive SEO spending by these dominant platforms, some restrictions on keyword bidding is the only way for hotel, and in particular SMEs, to ensure an even limited direct visibility on search engines websites like Google.

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