



Unilateral Conduct Working Group

Vertical Restraints

Report to Steering Group on Outcomes of Consultation Process

April 2017

Introduction

1. The Unilateral Conduct Working Group (**UCWG**) work plan for 2016-19 establishes a project to explore the development of a program of work examining the effects on competition of vertical restraints, with a view to promoting increased understanding within the ICN community, and, where possible, convergence.
2. On 26 October 2016, an Issues Paper – *Vertical Restraints: Options for Future Work* – was circulated to the membership of the UCWG for consultation. The consultation period ended in January 2017.
3. The purpose of the Issues Paper was to provide a basis for consultation with UCWG members and non-governmental advisers (**NGAs**) on options and priorities for future work by the UCWG in the area of vertical restraints with a view to commencing development of work product(s) during the 2017 ICN year.
4. This document, which follows the structure of the Issues Paper,¹ is a report to the ICN Steering Group following the consultation process. It summarises the responses to the consultation and sets out the issues that have been identified as being of greatest interest/priority for further work by the UCWG.
5. The outcomes of the consultation process, as reflected in this report, have been discussed during an interactive webinar attended by UCWG members on 4 April 2017.

Online vs offline

6. Respondents were asked to consider whether online markets present particular challenges for competition law enforcement, and whether future work should focus on online vertical restraints (questions (i) and (ii)).
7. A number of respondents were of the view that online markets present additional challenges for competition law enforcement as compared to more traditional markets; and respondents generally expressed a preference that the UCWG work program on vertical restraints focus on online markets. However, several respondents considered that the work program should also give consideration to offline markets.
8. Observations made in that regard include:
 - a. Different business models may be at play in online markets, which are often dynamic, fast-paced markets. For example, in some cases online players operate as an intermediary between two groups; in other cases as a matchmaker or agent.
 - b. Analysis of online markets requires a thorough understanding of online business models, incentives and strategies, which may differ from those in offline markets, in order to correctly assess whether conduct gives rise to negative effects, and whether efficiency claims (including free-riding justifications), which may be different to bricks-and-mortar markets, are well-founded. For example, complex algorithms and technical issues such as access to different platforms (multi-homing) need to be understood and analysed.

¹ The questions addressed in the Issues Paper are set out in the Annex to this report.

- c. It can be challenging to define relevant markets. For example, the SSNIP test must be adapted or replaced for markets where goods and services are offered free of charge.
- d. Online markets can be multi-sided. In such markets it may be necessary to balance potential damages caused on one side of the market with potential benefits on the other side. It is also important to recognise the impact that indirect network effects can have on platforms (e.g. reputation-based platforms such as eBay and Alibaba, where a platform's reputation can act as a barrier to entry and prevent switching).
- e. Online markets may be cross-border in nature and issues may arise in identifying the applicable law(s) and the competent authority(ies) in a given case. Issues also arise in relation to differences in legal regimes in different jurisdictions and the need for cooperation between authorities.

Theoretical analysis

- 9. As presented in the Issues Paper, one approach for the UCWG work program is to focus on a theoretical consideration of vertical restraints. Respondents were asked to consider whether the work program should have a theoretical focus, including guidance in relation to the following issues (questions (iii) to (vi)):
 - a. The key theories of harm arising in relation to vertical restraints.
 - b. The key market failures arising in relation to vertical restraints.
 - c. The evaluation of key efficiencies claimed in relation to vertical restraints.
 - d. Particular forms of vertical restraint, such as those that appear to be in particular use online.
- 10. Many respondents expressed interest in a theoretical analysis covering these issues. It was also noted that theories of harm, market failures and efficiencies should be considered together, including attention to the relationships between various vertical restraints. Particular areas of focus referred to include softening of competition, facilitation of collusion, raising rivals costs, foreclosure of rivals, reduction of intra- and inter-brand competition, free-riding, information asymmetries, the role of "big data" in possibly creating or strengthening market power of platforms, justification for RPM, role of buyer power, assessment of most favoured nation/customer clauses, two-sided and multi-sided markets.
- 11. Interest was also expressed for future work to focus on specific forms of vertical restraint, in particular those used in online markets. Most favoured nation/customer (MFN) clauses were referred to specifically by several respondents. A number of respondents also expressed the view that work on these issues should not be merely theoretical, but should include specific case examples, studies and analysis.
- 12. Observations made include:
 - a. Theory of harm plays a key role – the magnitude of anti-competitive effects may shed light on the possibility of allowing block exemptions or safe harbours.

- b. Focus on the theory of harm is beneficial in avoiding inappropriate *per se* characterisation of certain kinds of vertical restraints as likely harmful without an examination of their actual effects.
 - c. Consideration of how to counter key market failures by means other than vertical restraints for the benefit of consumers would be useful.
 - d. Market failures should be at the very root of any public policy intervention. Thus, in order to determine whether competition intervention is necessary and appropriately tailored, it is important to understand the competition harm it intends to address. Harm to competition, rather than competitors, should be the basis for any competition enforcement intervention.
 - e. Care has to be taken to note that, like theories of harm, theories of market failure continue to evolve, particularly in new distribution environments. It is important to keep an open mind as to the possibility of market failures which may not previously have been encountered.
 - f. The importance of dynamic efficiencies in online markets should be considered.
 - g. Theories as to efficiencies are not a static set of arguments.
 - h. Examples of measurement of efficiency claims would be useful, e.g. what data is needed.
 - i. Guidance would benefit from a basis in practical cases and challenges faced by antitrust authorities.
 - j. Given that interest in MFN clauses is increasing, it would be useful to analyse practical aspects of MFN cases, such as (i) methods of market definition, (ii) appropriate factors to measure market shares/market power (e.g. where goods/services are provided free of charge), (iii) proving anti-competitive effects, (iv) treatment of efficiency claims, (v) designing of remedies (penalties), (vi) jurisdictional issues.
13. Respondents were also asked whether the work should consider how market power is/should be assessed in online distribution markets and whether this is different to how market power is assessed in offline markets (question (vii)).
14. There was broad agreement that this would be useful, in particular when dealing with multi-sided platforms. The acquisition and use of big data/personal data was also referred to as conferring competitive advantage, and whether and how competition agencies should take this into account in their assessments.
15. Finally, respondents were asked whether a review or compilation of the academic literature on vertical restraints should be prepared as part of the analysis (question (viii)). While respondents recognised that such an undertaking would be beneficial, it was generally felt that other work should take priority.

Case studies and empirical analysis

16. Another approach presented in the Issues Paper is for the UCWG work program to focus on specific cases where vertical restraints have been considered by competition

agencies. Such work could be carried out in conjunction with or separately from a theoretical analysis.

17. Respondents were asked to consider whether there were benefits in developing a UCWG library resource of vertical restraint cases, and whether such case studies should be supplemented by webinars or other discussion forums.
18. A number of respondents noted their interest in the creation of a library/database of selected vertical restraints cases, noting that such a resource could be used by agencies to learn from similar cases in other jurisdictions. It was suggested that a focus on individual case studies will achieve a better understanding of the different approaches to vertical restraints in different jurisdictions. It was suggested that the ICN could develop a standard case form for members to complete, in English. It was noted that this would facilitate the reporting of cases to the library/database and allow the antitrust community to have access to the experiences and case law of authorities in non-English speaking countries.
19. Respondents were also asked whether there were benefits to undertaking empirical analysis / *ex post* review of the impact of different vertical restraints and of decisions prohibiting/authorising certain vertical restraints, and whether they were aware of any such analysis / reviews in their jurisdictions.
20. While there was general agreement that empirical analysis / *ex post* review was useful, it was felt that it might still be too early to carry out such analysis/review in the online context, and that this might be a focus for future work. As regards existing work in this area, reference was made in particular to the European Commission's (DG Competition) ongoing *ex-post* evaluation, together with a number of other EU competition authorities, of the hotel online booking cases.² However, in general it appears that not many empirical analysis / *ex post* reviews have been carried out in member jurisdictions.

Practical issues

21. Respondents were asked to consider whether there were benefits in addressing more practical aspects of assessing and addressing vertical restraints, such as identification and prioritisation of cases; if so, what this work should address; and what their preferred work product would be.
22. It was generally felt that, while beneficial, less priority should be allocated to practical aspects of assessing vertical restraints. It was felt that some of these issues would be covered by work undertaken in relation to the theoretical aspects of vertical restraints (questions (iii) to (v)) and, more generally, that purely practical aspects might be scope for future work.
23. Examples provided of issues such practical work could cover include: investigative strategies and techniques, type of information to request, prioritisation, assessment techniques, remedies, ways to identify efficiencies and market failures, cross-border issues, benefits of cooperation between authorities, potential setbacks from the different interpretations of vertical restraints in different jurisdictions, effective advocacy, determination of penalties.

² Reference was also made to empirical work in Germany (HRS, B9-66/10, 20.12.2013 and Booking.com, B9-121/13, 22.12.2015), Turkey and the UK.

Other

24. Finally, respondents were given the chance to provide any additional thoughts or comments.
25. One important point made was the importance of having regard to work on vertical restraints being carried out by other bodies, in order to avoid duplication and to exploit synergies. For example, it was noted that the OECD Competition Committee has approved a scoping note on a possible long-term project on “Competition, Digital Economy and Innovation”.

Preliminary conclusions

26. A number of preliminary conclusions can be drawn from responses, including:
 - while there is interest in a focus on online vertical restraints, respondents noted that work program should not overlook matters arising in offline markets
 - there is support for theoretical analysis of issues arising in respect of vertical restraints, including theories of harm, market failures and efficiencies
 - there is also support for analysis that focuses on particular forms of restraint, for example most favoured nation clauses
 - the development of a selected case study resource, based upon a template approach, would be beneficial.
27. Drawing on these conclusions and in consultation with the UCWG membership, it is intended that the UCWG develop a new work product analysing selected hypothetical scenarios for relevant theories of harm, market failures and efficiencies. The work product may also consider practical matters, such as the information that may assist agencies in assessing the effect on competition of the restraint and should draw on relevant case examples. Further details, including milestones for the development of the work product, will be included in the UCWG long form work plan.

Annex

Questions addressed in the Issues Paper

- (i) *Do online markets present particular challenges for competition law enforcement? If so, what are they?*
- (ii) *Should the UCWG vertical restraints work program focus on online markets? What reasons support this?*
- (iii) *Should the ICN provide guidance to members on the key theories of harm arising in relation to vertical restraints? Are there particular areas of focus for such work (for example, horizontal effects; foreclosure of rivals)?*
- (iv) *Should the ICN provide guidance to members on the key market failures arising in relation to vertical restraints? Are there particular market failures that deserve greater focus under the UCWG's work program? If so, which ones and why?*
- (v) *Are guidance materials needed to assist in the evaluation of key efficiencies claimed in relation to vertical restraints? Why? If yes, what efficiency claims should guidance address?*
- (vi) *Should the UCWG's work program focus on the theoretical analysis of particular forms of vertical restraint, such as those that appear to be in particular use online (for example, emerging conduct in online distribution models, such as retail MFN clauses or online sales limitations/bans)? Why?*
- (vii) *Should the work consider how market power is/should be assessed in online distribution markets and whether this is different to how market power is assessed in offline markets?*
- (viii) *Should a review or compilation of the academic literature on vertical restraints be prepared as part of the analysis?*
- (ix) *Are there benefits in developing a UCWG library resource of vertical restraint cases? Should such case studies be supplemented by webinars or other discussion forums?*
- (x) *Are there benefits to undertaking empirical analysis / ex post review?*
- (xi) *Are you aware of empirical analysis / ex-post reviews that have been undertaken or commenced in your jurisdiction into the impact of (i) different vertical restraints; or (ii) decisions prohibiting/authorising particular vertical restraints and that could contribute to a UCWG work product? Please provide brief details.*
- (xii) *What kind of work product could be envisaged (for example, a case book of examples)? What would be your preferred work product?*
- (xiii) *Are there benefits in addressing more practical aspects of assessing and addressing vertical restraints? What are these benefits?*

- (xiv) What should this work address? (For example, investigative strategies and techniques; identification and determination of penalties; the role for advocacy; prioritisation; jurisdictional issues)?*
- (xv) What kind of work product could be envisaged (for example, are there practical tools that could be developed for case handlers to assist them when assessing whether particular vertical restraints merit investigation; a case book of examples)? What would be your preferred work product?*
- (xvi) Please provide any additional thoughts or comments (including any additional areas for consideration) on the future UCWG work in relation to vertical restraints or on the approaches outlined in this issues paper.*