

The law and economics of most-favoured nation clauses

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1. Introduction

Most favoured nation clauses (“MFNs”), *i.e.*, agreements whereby a seller agrees that a buyer will benefit from terms that are at least as favourable as those offered by the seller to any other buyer,¹ have come under scrutiny in recent years in the European Union (“EU”), the United States (“US”) and beyond. Whilst the main focus of this scrutiny has been initially on the so-called wholesale MFNs, there has been a growing interest in cases involving ‘retail price’ MFNs. In these cases the MFN agreement references the end retail price rather than the wholesale price that traditional MFNs refer to.

Although since the *E-Books* case (a “retail MFN” case), which was settled in 2013,² the European Commission (“the Commission”) had not assessed the competitive impact of MFNs, it has recently opened a formal antitrust investigation into certain business practices carried out by Amazon in the online distribution of books. In particular, the Commission is investigating whether certain clauses included in Amazon’s contracts with publishers, which through different means ensure that Amazon, is offered terms at least as good as those offered to its competitors, are compatible with EU competition law.³

Similar MFNs, such as those included into contractual provisions for online hotel reservation services, have also been scrutinised by certain national competition authorities (“NCAs”) of the EU. In addition, both the German and the UK authorities have taken issue with Amazon’s “price parity” policy and the United Kingdom’s Competition Markets Authority (“CMA”) has recently opened an investigation into MFNs relating to motor insurance price comparison websites.

Despite this relatively recent interest, there does not appear to be clear guidance at either EU or national level as to how to assess MFNs from a competition law perspective, specifically with regard to MFNs that reference the retail price rather than the wholesale price. This article aims at providing a broad frame of reference for analysing this type of clauses, based on the case-law and practice of the European Courts and the European Commission.

2. The origins and features of MFNs

2.1. MFNs and international law

The origins of MFNs can be traced back to international trade law. In this context, MFNs may be defined as agreements whereby one State party to an investment treaty commits to provide investors with treatment no less favourable than the treatment it provides to investors under other investment treaties.

For centuries, MFNs have been included in treaties between sovereign states. For instance, it is noteworthy that the US included an MFN in its first international treaty, *i.e.*, the Treaty of Amity

¹ Another form of MFN is that in which a buyer agrees that a seller benefit from terms that are at least as favourable as those offered by the buyer to any other seller

² Case 39847 *E-Books*.

³ *Commission opens formal investigation into Amazon’s e-book distribution arrangements*, June 11, 2015 (available at: http://europa.eu/rapid/press-release_IP-15-5166_en.htm).



Figure 1 - Main types of most favoured nation clauses ("MFNs")

and Commerce with France, of February 6, 1778.⁴ In addition, in the 1800's and 1900's, MFNs were often included in a number of friendship, commerce and navigation treaties.⁵

Nowadays, many international agreements still contain MFNs. For instance, Article 1(1) of the General Agreement on Tariffs and Trade reads as follows:⁶

"Any advantage, favor, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties".

Article 2 of the General Agreement on Trade in Services⁷ and Article 4 of the Agreement on Trade-Related Aspects of Intellectual Property Rights⁸ contain similar provisions.⁹

4 Mike McClure, Most favored nation clauses: no favored view on how they should be interpreted, November 15, 2012.

5 Mike McClure, Most favored nation clauses: no favored view on how they should be interpreted, November 15, 2012.

6 General Agreement on Tariffs and Trade, April 15, 1994 (available at: https://www.wto.org/english/docs_e/legal_e/gatt47_e.pdf).

7 General Agreement on Trade in Services, April 15, 1994, Article 2 ("With respect to any measure covered by this Agreement, each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favorable than that it accords to like services and service suppliers of any other country") (available at: https://www.wto.org/english/docs_e/legal_e/26-gats.pdf).

8 Agreement on Trade-Related Aspects of Intellectual Property Rights, April 15, 1994, Article 4 ("With regard to the protection of intellectual property, any advantage, favor, privilege or immunity granted by a Member to the nationals of any other country shall be accorded immediately and unconditionally to the nationals of all other Members") (available at: https://www.wto.org/english/tratop_e/trips_e/t_agm2_e.htm).

9 There is a significant amount of economic literature analyzing the

This public international law concept has recently been the focus of attention of competition authorities in the EU, the US and beyond.

2.2. MFNs: concept and typology

From a competition law perspective, MFNs may be very broadly defined as an agreement whereby a seller agrees that a buyer will benefit from terms that are at least as favourable as those offered by the seller to any other buyer. As discussed above, these terms may include wholesale selling terms, or retail selling terms. The three main types of MFNs are shown in figure 1.

An example of the wholesale MFN is the film studios case in which the pay-TV distributors agreed to pay the film studio at least as high a price as any other deal it made with rival film studios. As mentioned, the third type of MFN is illustrated in the *E-Books* case, discussed in more detail below. In this case the MFN related to the retail price – with the publisher committing to the distribution platform to charge a retail price for its e-books on this plat-

effects of MFN clauses in the context of international trade. This literature is not uniform. On the one hand, some authors suggest that there is a strong economic rationale for MFN provisions, based on the assumption that discrimination is in itself undesirable from an economic point of view. In this regard, it has been argued that "non-discrimination can have a salutary effect of minimizing distortions of liberal trade [...] MFN often causes a generalization of liberalizing trade policies, so that overall more trade liberalization occurs (the multiplier effect of the MFN clause)" (see, John H. Jackson, *The World Trading System – Law and Policy of International Economic Relations*, 2nd ed. MIT Press, Cambridge, MA, Chapter 6, p. 158-160). On the other hand, another group of authors has suggested that, in specific circumstances, the maximization of global welfare may require limiting imports and setting positive tariffs, in which case discrimination may be socially desirable (see, Henrik Horn, Petros C. Mavroidis, *Economic and legal aspects of the Most-Favoured-Nation clause*, *European Journal of Political Economy*, Vol.17 (2001), p. 244).

form that are at least as low as the prices it charges on rival platforms.

MFNs may be bilaterally negotiated or unilaterally adopted, explicitly agreed upon or induced through different economic mechanisms. Also, MFNs may be categorized as contemporaneous, *e.g.*, applying to current prices, or retroactive, *e.g.*, involving a promise to rebate to the beneficiary the difference between a lower current price given to another buyer and a higher prior price paid by such beneficiary. They may protect the buyer, the seller or both.

3. Overview of the decisional practice of the Commission and the NCAs

3.1. The film studios investigation

In May 2002, the Commission investigated a number of MFN clauses contained in the contracts of the major Hollywood film studios with pay-TV service providers.

These clauses featured in most of the “output deals” between the major Hollywood film studios—NBC Universal, Paramount Pictures Corp. Inc. (subsidiary of Viacom), Buena Vista International Inc. (subsidiary of The Walt Disney Company), Warner Bros Entertainment Inc., MGM Studios Inc., and Dreamworks LLC—and the European pay-TV broadcasters that acquired broadcasting rights from these studios.

“Output deals”, whereby studios typically agree to sell their entire film production to broadcasters for a given period of time, are commonplace in the film industry. The MFN clauses in these contracts gave the studios the right to obtain the most favourable terms agreed between a pay-TV broadcaster and any other film studio. The Commission claimed that these clauses led to an anticompetitive alignment of the prices paid to the Hollywood studios.

However, in October 2004, the Commission decided to close its investigation after six of these studios decided to withdraw the clauses from their “output deals”.¹⁰

¹⁰ Case No COMP/38427 PO Pay Television Film Output Agreements. See EC Press Release, Commission closes investigation into contracts of six Hollywood studios with European pay-TVs, October 26, 2004 (available at: http://europa.eu/rapid/press-release_IP-04-1314_en.htm).

3.2. The e-books investigation

The Commission also analysed the use of MFN clauses in the *E-Books* investigation, which took place between 2011 and 2013.¹¹

In January 2010, each of Penguin, Simon & Schuster, HarperCollins, Hachette and Holtzbrinck/Macmillan (together, the “Five Publishers”) switched, in the United States, from a wholesale model, under which each retailer independently determined the retail price of the e-books it sold, to an agency model, under which each publisher entered into an agreement with Apple for the sale of e-books, pursuant to which the publishers set the price at which Apple could sell their e-books in the then-coming iBookstore. Each of these agency agreements contained similar key terms, including a retail price MFN clause, under which publishers had to lower the price of the e-book in the iBookstore to match the lowest price at which the specific e-book was sold. Some of the publishers subsequently entered into agency agreements with Amazon and other retailers in the United States, and with Apple for e-books sold in the United Kingdom, France, and Germany.

In December 2011, the Commission opened formal proceedings against the Five Publishers and Apple. The Commission was concerned that the Five Publishers’ change to the agency model would result in higher prices. The Commission took the preliminary view that the MFN acted as a “commitment device” to align the Five Publishers incentives to force Amazon to change its business model. According to the Commission the MFN made it very expensive for the Five Publishers to continue to allow Amazon to discount the price of books below that of Apple.¹² The MFN thus committed the Five Publishers to move it Amazon to an agency agreement in which the Five Publishers chose the retail price.

Each of the Five Publishers was in a position to force Amazon to accept changing to the agency model or otherwise face the risk of being denied access to the e-books of each of the Five Publishers, assuming that all Five Publishers had the same incentive during the same time period, and that Amazon could not have sustained simultaneous-

¹¹ Case 39847 *E-Books*.

¹² Statement on commitments from Apple and four publishing groups for sale of e-books. EC Press Release, 13 December 2012

ly being denied access even to only a part of the e-books catalogue of each of the Five Publishers. The Commission took the preliminary view that the Five Publishers' contemporaneous switching of Amazon to the agency model may have resulted from a concerted practice with the object of raising retail prices of e-books in the EEA or preventing the emergence of lower prices for e-books in the EEA.

However, the Commission's investigation was closed following binding commitments submitted in December 2012 (and April 2013 by Penguin). These commitments provided that the publishers would terminate their existing agency agreements with e-book distributors, and that the new agency agreements would allow agents to discount within their commissions. The commitments also placed a five year ban on price MFNs.

There has been a growing interest in cases involving 'retail price' MFNs

3.3. The online booking investigations

Since 2010, several NCAs have launched inquiries into MFNs in the online booking sector. These MFNs have been scrutinized in Austria, Denmark, France, Germany, Hungary, Ireland, Italy, Sweden, Switzerland and the United Kingdom.¹³ In what follows, we briefly refer to the investigations launched by NCAs in the United Kingdom, Germany, Italy and France.

3.3.1. United Kingdom

The former United Kingdom NCA, *i.e.*, the Office of Fair Trading ("OFT"), launched a formal investigation in September 2010 into vertical agreements concluded between hotels and online travel agencies ("OTAs") which it suspected to be in breach of Chapter I of the Competition Act and of Article 101 of the TFEU.

On July 31, 2012, the OFT announced that it had issued a statement of objections to Booking.com B.V., Expedia Inc. and InterContinental Hotels Group plc. The OFT alleged that Booking.com and Expedia each entered into separate agreements with InterContinental Hotels which restricted the OTAs' ability to discount the price of room-only hotel accommodation. The OFT considered that these agreements were anti-competitive as they could limit price competition between OTAs and also increase barriers to entry and expansion for OTAs that may seek to gain market share by offering discounts to consumers.

Although MFNs were not the main focus of the OFT's investigation, the OFT did analyse the impact of MFNs on the ability of OTAs to offer discounts. In particular, the OFT analysed so-called retail rate MFNs, whereby a hotel agreed to provide an OTA with access to a room reservation at a booking rate no higher than the lowest booking rate displayed by any other online distributor, thereby guaranteeing that an OTA could not be undercut by other OTAs.

The OFT accepted the commitments offered by the parties. In particular, the parties agreed that: (i) the OTAs would be free to offer reductions off headline room rates but only to consumers who are already "members" (or part of a "closed group")¹⁴ of the relevant OTA and who had made at least on prior booking with it; (ii) the hotels would also be free to offer reductions off their headline room rates; (iii) the OTAs could publicize information regarding the availability of their discounts, but again only to their members; and (iv) the hotels could not impose accounting requirements on the OTAs in relation to commission or margin level caps that may restrict the OTAs from being able to offer discounts. The OFT recognized that these proposed commitments would not remove all restrictions on the ability of the OTAs to discount headline room rates. However, it considered that there was force in the parties' arguments that there were efficiencies in enabling hotels to have control over the headline rate for their hotel rooms and thus to restrict discounting.

¹³ Edurne Navarro Varona and Aarón Hernández Canales, *Online Hotel Booking*, CPI Antitrust Chronicle, May 2015 (1), p. 4.

¹⁴ The commitments refer to such membership as being part of a "Closed Group", defined as "group where membership is not automatic and where: (i) consumers actively opt in to become a member; (ii) any online or mobile interface used by Closed Group Members is password protected; and (iii) Closed Group Members have completed a Customer Profile."

Although the OFT did not make an assessment of whether MFN provisions may give rise to a breach of the Chapter I prohibition and/or Article 101 TFEU, in order to ensure the effectiveness of the commitments, the parties committed to amend, remove or not include any provisions in current and future commercial arrangements that could undermine discounting freedoms, which could include amending MFN provisions, if necessary.¹⁵ The OFT's decision accepting the commitments was quashed on appeal by the Competition Appeals Tribunal ("CAT"), on September 26, 2014, as a result of a challenge from Skyscanner (a meta-search price comparison website). The CAT held that the OFT had failed to take into account properly, or at all, the representations that Skyscanner made on the impact the commitments would have on price transparency. This objection centred on the restriction on disclosure of specific price information outside the "closed groups" established as part of the commitment arrangements.

The CAT also found that the OFT had failed to exercise its power to accept commitments rationally and to promote pro-competitive principles. Indeed while acknowledging it had not been asked to evaluate the effect of the commitments, the CAT held that whilst it is "*theoretically possible*" it "*rather doubt[ed]*" that the commitments would benefit consumers and recognized and highlighted the role that price comparison websites such as Skyscanner play in promoting price transparency.¹⁶ The original commitments raised serious concerns that at the very least merited more thorough analysis from the OFT – they barred OTAs from advertising and offering discounts to anybody except pre-existing customers, but being able to offer such discounts and promotions is vital for OTAs to develop customer bases in the first place. That the commitments gave rise to this "chicken-and-egg" scenario made them unlikely to aid competition – indeed, they may well have decreased the existing level of price transparency, and thereby hindered competition in the space.

The CAT found that by concluding that the restriction was a restriction by object in its initial statement of objections, the OFT had not undertaken any detailed market analysis and so was not in a

position to understand fully the effect of the proposed commitments when it accepted them. The investigation was subsequently reopened by the CMA, which has not yet reached a final conclusion.

Booking.com has announced that from July 1, 2015, it will abandon its price, availability and booking parity provisions with respect to other online travel agencies in its terms with all accommodation partners across Europe, including in the UK. However it will maintain its price and booking availability provisions with respect to the hotels' own websites. This announcement has close similarities to the remedy suggested by the UK Competition Commission in Motor Insurance. The CMA states that it is considering this significant development closely.

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3.3.2. Germany

On February 15, 2012, in interim proceedings, the Düsseldorf Court of Appeal prohibited the Hotel Reservation Service ("HRS"), an online hotel booking platform, from enforcing an MFN contained in its contracts with hotel partners.

Under the contested clause, hotels undertook not to offer other internet providers more favorable conditions than those offered to HRS with respect to price, availability and cancellation terms. The Court reasoned that the MFN infringed Section 1 of the Gesetz gegen Wettbewerbsbeschränkungen ("GWB"), as it restricted the hotels' freedom to set prices independently. The MFN was thus prejudicial to the largely price-driven competition among hotel booking portals.

These Court proceedings are independent of the Bundeskartellamt or Federal Cartel Office ("FCO") action against HRS' MFN, initiated on February 10,

¹⁵ OFT, Hotel online booking: Decision to accept commitments to remove certain discounting restrictions for Online Travel Agents, January 31, 2014, section 6.39 and 6.40.

¹⁶ [2014] CAT 16, par

2012. The FCO issued a first statement of objections against HRS, arguing that HRS' MFN restricted competition between online hotel booking providers and prevented market entry. In addition to the MFN, in March 2012, each hotel also agreed to refrain from offering more favorable conditions even when customers attempted to book directly at the hotel's reception.

On July 25, 2013, the FCO issued a second statement of objections against HRS, which confirmed its initial finding as to the anticompetitive effect of the MFN and expressed further concern regarding the additional provision of March 2012 according to which hotels agreed not to offer more favorable conditions for direct bookings. In addition, the FCO noted that MFN clauses similar to that used by HRS were applied by other online platform operators in different sectors, and consequently, that the HRS proceedings would be of importance for a variety of other online platforms.

On December 20, 2013, the FCO prohibited HRS' MFN, and ordered HRS to remove these clauses from all contracts and general terms and conditions with contracting hotels by March 1, 2014.¹⁷ The FCO considered that HRS' MFNs restricted competition between online hotel booking platforms, prevented new market entry, and constituted an unfair hindrance to the small and medium-sized hotels which were dependent on HRS.

The FCO left open the question of whether MFN clauses are a non-exemptible hardcore restriction under the EU Block Exemption Regulation, as HRS had held a market share in excess of the 30% threshold for the past four years.¹⁸ The FCO reasoned that the MFN clauses removed hotel portals' incentives to offer lower commissions to the hotels, or to face competition by adopting new sales strategies. It further reasoned that in addition to limiting new market entry, the MFN clauses also significantly restricted the opportunities open to hotels, in particular, hotels could not use different portals and/or other sales channels in order to make offers at different prices and conditions.

¹⁷ Press release of the Bundeskartellamt of July 25, 2013, (HRS) (available at: http://www.bundeskartellamt.de/SharedDocs/Meldung/EN/Pressemitteilungen/2013/25_07_2013_HRS.html).

¹⁸ Interestingly the FCO found the market share to be in excess of 30% on the basis that the hotel's own websites sales were not in competition with OTA sales. However when assessing the MFNs the FCO found that these clauses as applied to the hotel's own website sales were also anti-competitive.

Finally, the FCO reasoned that the MFN clauses imposed by the two other major hotel portals in Germany, Booking.com and Expedia, strengthened the restriction of competition brought about by HRS' MFN clause. The FCO also initiated proceedings against Booking.com and Expedia over their MFN clauses.

The FCO's decision of December 20, 2013 was subsequently upheld on appeal to the Düsseldorf Court of Appeals, which rejected HRS's appeal.¹⁹ Commenting on the Düsseldorf Court of Appeals' judgment, the President of the FCO Andreas Mundt stated the following:

"[T]he Düsseldorf Higher Regional Court has decided on a fundamental issue concerning restrictions of competition in online sales. 'Best price' clauses are only beneficial to the consumer at first glance because ultimately they restrict competition between the hotel booking platforms. Booking portals which demand lower commission from the hotels cannot offer lower hotel prices. The clauses also make the entry of new platforms to the market more difficult. Consumers therefore benefit directly from the court's decision. Competition between the portals for lower hotel room prices or favorable cancellation conditions will increase. It will be easier for new hotel booking portals with innovative services to enter the market. We will now quickly pursue our current proceedings against the 'best price' clauses of Booking and Expedia, HRS's competitors."

3.3.3. Italy

On May 7, 2014, the Italian Competition Authority ("ICA") opened an investigation involving OTAs Expedia Inc., Expedia Italy S.r.l., Booking.com B.V., and Booking.com (Italia), concerning MFNs included in their contracts with partner hotels. According to the ICA, the MFNs were liable to restrict competition because they: (i) restricted price competition between the OTAs and the hotels; and (ii) hindered new market entry of OTAs.

Booking.com offered a package of commitments in order to address the ICA's concerns. These commitments differentiated between direct and indirect sales channels.

¹⁹ OLG Düsseldorf, VI - Kart. 1/14 (V). Press release of the Bundeskartellamt of January 9, 2015 (available at: http://www.bundeskartellamt.de/SharedDocs/Meldung/EN/Pressemitteilungen/2015/09_01_2015_hrs.html).

With regard to direct sales channels, Booking.com could still require its partner hotels to offer on Booking.com's website the same prices and/or other special conditions publicly offered by the hotels through their own direct sales channels, whether online or offline. Booking.com would, however, allow the hotels to apply discounts on the rates offered on their platforms to specific categories of clients.

With regard to indirect sales channels, the partner hotels would no longer be bound to offer on Booking.com's website prices equal to or lower than those offered to other providers, whether online or offline. In addition, Booking.com would refrain from offering lower commission rates and/or other types of incentives to hotels upon the condition that they set their prices at the same level to or lower than those offered on other platforms.

On December 15, 2014, the ICA began its market test to assess these commitments. On April 21, 2015, the ICA rendered the commitments offered by Booking.com BV and Booking.com legally binding, and closed the investigation with respect to these companies. At that time, the proceedings with regard to Expedia were still pending.

3.3.4. France

In 2013, the French Competition Authority (“FCA”) launched an investigation into online hotel booking platforms on foot of a complaint put forward by hotel unions. The unions accused online hotel booking platforms – in particular Booking.com – of imposing MFNs.

The FCA provisionally determined that the implementation of these parity clauses may give rise to anti-competitive effects, finding that it would likely reduce competition between booking.com and competing platforms. The FCA noted that whatever the level of the commission rate charged by booking.com, hotels were obliged to grant it room rates, the number of rooms available for booking, and terms and conditions of sale, that were as favorable as those to be found on competing platforms. Furthermore, the FCA provisionally determined that MFNs may lead to the foreclosure of smaller platforms or those that had just entered the online booking market. Even when lower commission rates were offered which were more attractive to hotels, these platforms could not

differentiate in prices and offer cheaper room rates to customers.

Booking.com offered a package of commitments, which mirrored those offered in Italy, in order to address the FCA's concerns. As stated by the FCA:

“Essentially booking.com is undertaking to remove the pricing parity clause from its contracts which oblige hotels to offer booking.com conditions that are, at least as favorable as those offered on competing platforms. Booking.com has further offered to extend this commitment to all the EEA countries. Thanks to this commitment, hotels will enable competition between booking platforms and thus allow the cost of commission, and ultimately room rates, to fall. These commitments should therefore benefit both hotels and consumers... While increasing competition between reservations platforms, the proposed commitments guarantee the viability of their economic model while maintaining parity with respect to the hotel booking channels. A balanced solution is thus proposed, providing an impetus to competition in the market in order to bring down prices while preserving the existing efficiency gains.”²⁰

The FCA market tested these commitments and, after evaluating the results, accepted the commitments in its decision of April 21, 2015.²¹ This decision has been appealed before the Court of Appeal in Paris. The appeal is still pending.

3.4. The Amazon investigation

Amazon's MFNs/price parity policy has undergone scrutiny by NCAs in Germany and the United Kingdom, and recently, by the Commission.

On February 20, 2013, the FCO initiated proceedings against Amazon Germany concerning an MFN applied to retailers offering their products via Amazon's online trading platform, Amazon Marketplace. Under the contested clause, retailers undertook to offer their products at the most favourable price via Amazon Marketplace compared to their offer either on other online platforms or in their own online shops. The FCO took the view

²⁰ See http://www.autoritedelaconurrence.fr/user/standard.php?id_rub=592&id_article=2463.

²¹ Décision n° 15-D-06 du 21 avril 2015 sur les pratiques mises en oeuvre par les sociétés Booking.com B.V., Booking.com France SAS et Booking.com Customer Service France SAS dans le secteur de la réservation hôtelière en ligne (available at: <http://www.autoritedelaconurrence.fr/user/avisdec.php?numero=15D06>).

that this practice may violate Section 1 of the CWB by restricting competition between online trading platforms. In particular, the FCO argued that the combination of high Amazon Marketplace fees and the MFN may result in entry barriers for new platforms and a high price level to the detriment of consumers.

On August 27, 2013, Amazon notified the FCO that it would no longer apply its MFN to Amazon Marketplace, and made the necessary changes to its general terms and conditions for some retailers. The FCO assessed whether Amazon's actions were sufficient to alleviate the FCO's concerns, and made clear that it expected Amazon to refrain from imposing MFNs for good. Having demanded modifications to Amazon's initial notification of changes, in particular, that Amazon remove its MFN from all contracts across Europe, the FCO subsequently closed its proceedings against Amazon on November 26, 2013.

Amazon's MFNs/price parity policy has undergone scrutiny by NCAs in Germany and the United Kingdom, and recently, by the Commission

During the investigation, the FCO cooperated closely with the OFT, which carried out a parallel investigation into the MFNs applied to Amazon Marketplace. The FCO and the OFT terminated their respective investigations on November 26 and 29, 2013. As a result of the FCO and OFT proceedings, Amazon abandoned MFNs throughout the EU.

Amazon's price parity policy has also recently come under the scrutiny of the European Commission. Indeed, as mentioned above, the Commission has recently opened a formal antitrust investigation into certain business practices carried out by Amazon in the distribution of electronic books.²²

²² Commission opens formal investigation into Amazon's e-book distri-

In particular, the Commission is investigating whether certain clauses included in Amazon's contracts with publishers, which through different means ensure that Amazon is offered terms at least as good as those offered to its competitors, are compatible with EU competition law.²³ The Commission's investigation is focused on clauses which allegedly shield Amazon from competition from other e-book distributors, *e.g.*, clauses granting Amazon the right to be informed of more favourable or alternative terms offered to its competitors. The Commission is concerned that such clauses may make it more difficult for other e-book distributors to compete with Amazon by developing new and innovative products and services, thereby limiting competition between e-book distributors and reducing consumer choice.²⁴

3.5. The private motor insurance investigation

On September 24, 2014, the CMA published a report on its investigation into a number of areas of the private motor insurance ("PMI") market.²⁵ The report considers, *inter alia*, the question whether MFNs contained in agreements between PMI providers and car insurance price comparison websites ("PCWs") may give rise to anti-competitive effects.

The CMA distinguished between two types of MFN clauses which benefit PCWs: (i) so-called narrow MFNs, pursuant to which the price on the PMI provider's own website will never be lower than the price on the PCW; and (ii) so-called wide MFNs, pursuant to which the price through any other sales channel (including other PCWs) will never be lower than the price on a given PCW.

The CMA observed that so-called narrow MFNs were unlikely to give rise to anti-competitive effects, given that they only limited the competitive constraint exerted by the own-website channel on PCWs, and such a constraint would in any event be insignificant. Further, the CMA analysed the possible pro-competitive effects of these clauses and concluded that narrow MFNs were a legitimate

²² *Commission opens formal investigation into Amazon's e-book distribution arrangements*, June 11, 2015 (available at: http://europa.eu/rapid/press-release_IP-15-5166_en.htm).

²³ *Commission opens formal investigation into Amazon's e-book distribution arrangements*, June 11, 2015 (available at: http://europa.eu/rapid/press-release_IP-15-5166_en.htm).

²⁴ *Commission opens formal investigation into Amazon's e-book distribution arrangements*, June 11, 2015 (available at: http://europa.eu/rapid/press-release_IP-15-5166_en.htm).

²⁵ See <https://www.gov.uk/cma-cases/private-motor-insurance-market-investigation>.

tool used by PCWs to build consumer trust in their service offering. Therefore, even if narrow MFNs could raise some anti-competitive effects, they may be necessary for PCWs to survive. In addition, the CMA concluded that such clauses ensure that PCWs maintain their credibility and continue to provide this time-saving service. In so doing, they maintain the reduction in search costs brought about by PCWs, which enhances inter-brand competition and increases customer price sensitivity.

MFNs may constitute an effective means of protecting the interest of a buyer

In contrast, the CMA considered that wide MFNs were likely to have an anti-competitive effect both in the PCW market and in the PMI market. In particular, the CMA found that wide MFNs soften price competition between PCWs in relation to PMI. Where a wide MFN is in place, a PCW does not face the possibility that a retail customer will find the same PMI policy more cheaply on a competing PCW. In addition, there is little incentive for a PCW facing a competitor with a wide MFN clause to seek better PMI prices for their retail consumers from the insurers. Any such better price will also be passed on to the competitor. Therefore, there is little reward for commission fee reductions and less incentive to oppose raising fees. Finally, the CMA stated that the softening of price competition between PCWs is likely to lead to less entry, less innovation and higher commission fees, resulting in higher premiums. Finally, the CMA found that wide MFNs provide no pro-competitive effects over and above the effects of narrow MFNs.

Accordingly, the CMA concluded that so-called wide MFNs prevent price competition between PCWs, and therefore ultimately restrict entry to the PCW market, reduce innovation by PCWs and increase prices for PMI to the prejudice of consumers.

4. The competitive effects of MFN provisions

4.1. Potential pro-competitive effects of MFNs

While MFNs have been subject to antitrust scrutiny due to their potential anti-competitive effects, there can be efficiency reasons associated with the use of these contractual provisions. The three main possible efficiency-enhancing effects of MFNs, depending on the factual context, are: (i) the reduction of free-riding problems; (ii) the mitigation of “hold up” problems; (iii) the reduction of transaction and (re)negotiation costs; and (iv) the reduction of delays in transacting.

4.1.1. MFNs may reduce “free-riding” problems

As with other vertical constraints, MFNs, both at the retail and the wholesale levels, may reduce free-riding on either parties’ investments. This efficiency rationale has been particularly cited in the context of retail or online platform MFNs. This is because online platforms are generally two sided markets. The platform must attract both the buyer and the seller to the platform. However because the different sides of the platform may have different willingness to pay for the platform’s service, the optimal tariff may not involve charging both sides the same amount for access to the platform.²⁶ For example, in online booking platforms the customer does not pay for searching the platform to find a hotel, whereas the hotel pays when the customer books that hotel. The ability to separate this search hotel search functionality and the booking functionality creates an arbitrage opportunity for the hotel. The hotel would like to use the platform to allow the customer to find its hotel, but then complete the booking on its own website in order to avoid paying the platform. Thus the hotel may be tempted to ‘free-ride’ on the search and promotion services that the platform provides for the hotel.²⁷

The same issues will also arise between ‘full-function’ platforms and ‘low-cost’ platforms. A seller may sign up to a full-function platform in order to promote its product and allow customers find out

²⁶ For a discussion of the optimal tariff structure in two-sided markets see Rochet, J. C. et J. Tirole. 2003, Platform Competition in Two-sided Markets. *Journal of the European Economic Association* 1 (4): 990–1029.

²⁷ Matthew Bennett, Online Platforms: Retailers, Genuine Agents or None of the Above? *CPI Antitrust Chronicle*, June 2012. See also Paolo Buccirosi, Background Note, OECD Policy Roundtable on Vertical Restraints for On-line Sales, 2013

about its products, but then encourage users to go to a 'low-cost' platform to actually buy the product. The seller pays less commission on the low-cost platform, and the buyer can have a lower price. However the full-function platform will not be able to recover the investments it has made in its search functionality and may either leave the market or be forced to migrate to a lower-cost platform business model.

Retail MFNs solve this problem by ensuring that sellers cannot price their products or services on other platforms or channels at a lower price than on the 'full-function' platform. This ensures that the seller cannot free-ride on the platform services by pricing more cheaply elsewhere.

4.1.2. MFNs may mitigate "hold up" problems

Certain transactions require that buyers and/or sellers carry out costly relationship-specific investments, *i.e.*, investments which are only of value in the context of the anticipated relationship between a given buyer and seller.²⁸

This is the case, for instance, of a buyer who has to make significant investments in order to set up an *ad hoc* distribution system for the products/services acquired from a given seller, and/or to train his employees to handle the particular product/service sold by that seller. Relationship-specific investments may significantly benefit consumers by, for instance, allowing new, better or cheaper products to enter the market, and/or enabling consumers to have access to information.²⁹

Similar to the free-riding issue discussed above, there is a risk that, once the buyer has carried out such investments, the seller will start selling the product/service in question to a competitor of the buyer at a lower price.³⁰ This would place the buyer at a competitive disadvantage, and as a consequence, the buyer may not be able to recoup his/her investment.

Conscious of the existence of such a risk, a buyer may not be willing to carry out a relationship-spe-

cific investment unless and until s/he has a guarantee that s/he will be able to recoup his sunk costs.³¹ MFNs may constitute an effective means of protecting the interests of a buyer and of providing it with the necessary incentives to commit to such investments.³² Indeed, if the seller grants the buyer an MFN, the buyer will rest assured that, after carrying out the investments, the seller will not be able to sell the same product/service to his competitors at a lower price thereby preventing him/her from recouping his/her investment.

Similarly, it is possible that a seller may carry out a relationship-specific investment, in which case an MFN can be used to ensure that the seller will receive the buyer's most favourable terms.³³

4.1.3. MFNs may reduce transaction and (re)negotiation costs

An MFN may enable a buyer to obtain the most favourable terms from a seller without having to carry out extensive research in order to find the best available price and without having to engage in lengthy negotiations.³⁴

An MFN may significantly reduce renegotiation costs, as a buyer will not have to attempt to renegotiate his price downward in the face of a price reduction to one of his competitors, but instead, will benefit from price reductions granted to competitors automatically.³⁵ Moreover, the inclusion of an MFN may make it more attractive for the parties to enter into a long-term contract, thereby eliminating the need for periodic renegotiations.³⁶ Indeed, if an MFN clause is put in place, when negotiating the terms of a long-term contract, a buyer will not be concerned that the seller may offer more favourable terms to one of his/her competitors, thus

28 Jason J. Wu and John P. Bigelow, *Competition and the Most Favoured Nation Clause*, CPI Antitrust Chronicle, July 2013 (2), p. 5.

29 Ingrid Vandenborre and Michael J. Frese, *Most Favoured Nation Clauses Revisited*, European Competition Law Review, Issue 12, 2014, p. 589.

30 Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favored-Nation Provisions*, Antitrust, Vol. 27, No. 2, Spring 2013, p. 21.

31 Ingrid Vandenborre and Michael J. Frese, *Most Favoured Nation Clauses Revisited*, European Competition Law Review, Issue 12, 2014, p. 589.

32 Noëlle Lenoir, Marco Plankensteiner and Elise Créquer, *Increased Scrutiny of Most Favoured Nation Clauses in Vertical Agreements, Getting the Deal Through – Vertical Agreements 2014*, Law Business Research Ltd, p. 5.

33 Jason J. Wu and John P. Bigelow, *Competition and the Most Favoured Nation Clause*, CPI Antitrust Chronicle, July 2013 (2), p. 6.

34 Jennifer D. Lee, *Post U.S. v. Apple: How Should Most-Favoured Nation Clauses be Treated Now?*, Cardozo Arts & Entertainment, Volume 33, Issue 1, p. 252.

35 Jennifer D. Lee, *Post U.S. v. Apple: How Should Most-Favoured Nation Clauses be Treated Now?*, Cardozo Arts & Entertainment, Volume 33, Issue 1, p. 252.

36 Ingrid Vandenborre and Michael J. Frese, *Most Favoured Nation Clauses Revisited*, European Competition Law Review, Issue 12, 2014, p. 589.

placing him at a competitive disadvantage. In addition, an MFN may constitute an effective means of guaranteeing pricing flexibility, *i.e.*, of enabling the parties to enter into a long-term contract without having to establish a fixed price and thus facilitating adaptation to changes in market conditions over time.³⁷

Finally, it has been highlighted that there are two factors that mitigate such efficiency gains. Indeed, although MFNs may reduce negotiation costs they may in turn lead to an increase in monitoring costs, insofar as the buyer will tend to monitor whether the seller is adhering to the MFN or not.³⁸ In addition, and as discussed in section 4.2, an MFN may reduce the incentive for both sellers and buyers to seek discounts, in particular when a significant number of buyers benefit from MFNs. While a seller will be more hesitant to grant discounts, as any discount may be extended to other buyers benefiting from the MFN, a buyer will have less of an incentive to require discounts as this will not grant him/her a cost advantage over his/her competitors who also benefit from MFNs.³⁹

4.1.4. MFNs may reduce contractual negotiations delays

An MFN may reduce contractual negotiations delays by discouraging buyers and/or sellers from delaying and waiting for a better deal.⁴⁰

On the one hand, an MFN may enable a seller to reduce delays which may be sought by a buyer if such buyer expects prices to fall over time. This may be the case, in particular, for time-specific products/services or perishable production capacity.⁴¹ For instance, a buyer may delay the acquisition of a concert ticket if s/he expects prices for such tickets to fall close to the concert date. In these circumstances, an MFN may be used to guarantee to early ticket buyers that, in case prices fall over time, they

will receive the difference between what they paid and the price paid by the last buyer(s).⁴²

On the other hand, an MFN may also enable a buyer to reduce delays which may be sought by a seller who expects prices to rise over time. This may happen if a buyer's project requires agreement with multiple sellers.⁴³ For instance, a land developer who is attempting to acquire multiple plots of land from different owners may be confronted with significant delays, as the different sellers may have an incentive to attempt to be the last seller(s) in order to maximize their chances of extracting a better deal from the buyer. In these circumstances, an MFN may be used to guarantee to early sellers that, if or in instances when the buyer pays higher prices for plots of land over time, they will receive the difference between what they received and what the last seller(s) received.⁴⁴

4.2. Potential anti-competitive effects of MFNs

While there is a material body of literature discussing the potential benefits of MFNs, the main focus in the legal and economic literature has been on the threats to competition associated with the introduction of MFNs in certain market settings.⁴⁵ Various commentators have identified MFNs as a means of facilitating collusion/dampening competition or entrenching market power. We outline below the main forms of competitive harm associated with MFNs. We also set out what the evidentiary burden appears to be when determining whether or not MFNs are likely to infringe EU competition law (Articles 101 and 102 TFEU).

37 Jason J. Wu and John P. Bigelow, *Competition and the Most Favoured Nation Clause*, CPI Antitrust Chronicle, July 2013 (2), p. 6.

38 Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favoured-Nation Provisions*, Antitrust, Vol. 27, No. 2, Spring 2013, p. 22.

39 Jennifer D. Lee, *Post U.S. v. Apple: How Should Most-Favoured Nation Clauses be Treated Now?*, Cardozo Arts & Entertainment, Volume 33, Issue 1, p. 252.

40 Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favoured-Nation Provisions*, Antitrust, Vol. 27, No. 2, Spring 2013, p. 21.

41 Jason J. Wu and John P. Bigelow, *Competition and the Most Favoured Nation Clause*, CPI Antitrust Chronicle, July 2013 (2), p. 6.

42 Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favoured-Nation Provisions*, Antitrust, Vol. 27, No. 2, Spring 2013, p. 21.

43 Jennifer D. Lee, *Post U.S. v. Apple: How Should Most-Favoured Nation Clauses be Treated Now?*, Cardozo Arts & Entertainment, Volume 33, Issue 1, p. 251.

44 Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favoured-Nation Provisions*, Antitrust, Vol. 27, No. 2, Spring 2013, p. 21.

45 Steven C. Salop and Fiona Scott Morton, *Developing an Administrable MFN Enforcement Policy*, Antitrust Vol. 27, No.2, Spring 2013; Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favoured-Nation Provisions*, Antitrust Vol. 27, No. 2, Spring 2013; Fiona Scott-Morton, "Contracts that Reference Rivals", Department of Justice, April 5, 2012; Justin Coombs, *Most Favoured Customer Clause and competition law: An overview of EU and national case law*, e-Competition n°64758; Ingrid Vandendorre and Michael J. Frese, "Most Favoured Nation Clauses Revisited", European Competition Law Review, 2014; Nöelle Lenoir, Marco Plankensteiner and Elise Créquer, *Increased Scrutiny of Most Favoured Nation Clauses in Vertical Agreements*, 2014; Laura Atlee & Yves Botteman, *Resale Price Maintenance and Most-Favored Nation Clauses: The Future Does Not Look Bright*, Competition Policy International, Inc. 2013.

4.2.1. MFNs may facilitate collusion/dampen competition

MFNs may facilitate explicit collusion

The members of a cartel are likely to gain from any contractual mechanism that can credibly ensure one another that they will not cut prices. Granting wide-spread MFNs can serve that purpose. Indeed, if the members of the cartel include MFNs in their contracts with buyers, a cheat would be forced to offer the lower price to all of its customers, if the reduced price were known to the cheat's customers.⁴⁶ Such selective price cuts may become very expensive and therefore less likely to occur.⁴⁷ Further, MFNs can also help cartelists by making deviation from the cartel easier to detect.⁴⁸

MFNs may facilitate tacit collusion/dampen competition

MFNs can dampen competition or make it easier for firms to tacitly co-ordinate with one another. If a firm knows that one, some, or all of its rivals have entered into MFN agreements, they are less likely to reduce their prices as this will be automatically matched by its rivals. These dampening concerns have been particularly clear in platform or retail MFNs as in these cases the constraint takes place on the retail price. If a platform imposes an MFN on sellers that stipulates that sellers cannot price more cheaply on other platforms, this may not only reduce rival platform's incentives to reduce their commissions, but may also increase the incentive of the MFN instigating platform to increase its commission. In the presence of a platform MFN, increasing the platform's commission to sellers forces the sellers either to absorb the higher commission (thereby not increasing their price), or increase their prices not only on the platform but also rival platforms to remain compliant with the platform MFN clause. Accordingly, MFNs may serve to "dampen competition" in the absence of an explicit agreement between competitors.⁴⁹

Although MFN clauses can reduce a platform's incentives to offer low commissions, the magnitude of this effect depends crucially on the importance of the platform. Whilst sellers may be constrained in their ability to price by the MFN, they still have the ability to withdraw from the platform in order to avoid the MFN. Thus, the ability of the platform to impose an MFN which goes against the seller's interests (i.e. increases its commission), depends upon the importance of the platform. The more competition/substitution there is between platforms, the easier it will be for the seller to simply withdraw from any platform that does not provide sufficient value to the seller.

MFNs can dampen competition or make it easier for firms to tacitly co-ordinate with one another

Second, it should also be noted that the presence of MFN clauses actually increase sellers' incentive to resist commission (by de-listing) increases if the sellers are relatively close substitutes. This is because by leaving the platform imposing an MFN, the seller now has an advantage versus its rival sellers, as it now able to reduce its price relative to rival sellers and capture greater sales. This additional incentive to the seller from withdrawing/de-listing is only available when the platform in question imposes an MFN.

Retail/platform MFNs may also raise concerns in the context of facilitating the sustainability of tacit coordination. A firm may agree to an MFN to send out a signal to other players to raise their prices. If an MFN is effective enough to discourage price cutting, it could obviate the need for a risky explicit agreement.⁵⁰ However it should be noted that the use of MFN clauses as a coordination 'signal' is not costless. As discussed above, sellers will have a

⁴⁶ Panel Summaries from DOJ and FTC Workshop on MFN Clauses and Antitrust Enforcement and Policy.

⁴⁷ Ingrid Vandenborre and Michael J. Frese, *Most Favored Nation Clauses Revisited*, European Competition Law Review, 2014.

⁴⁸ Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favored-Nation Provisions*, Antitrust Vol. 27, No. 2, Spring 2013.

⁴⁹ Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favored-Nation Provisions*, Antitrust Vol. 27, No. 2, Spring 2013.

⁵⁰ Jason J. Wu & John P. Bigelow, *Competition and the Most Favored Nation Clause*, CPI Antitrust Chronicle, July 2013 (2).

greater incentive to withdraw/de-list from the platform/firm imposing the MFN, thereby reducing the platform/firm's sales. This ability to withdraw/de-list (and hence the cost of the signal) will be greater the more fragmented the market in which the platform operates. Therefore it is not always clear that using the MFN as a signaling device is an optimal strategy.

In summary, taking account of the potential for sellers to withdraw/de-list, narrows the concern that MFNs may dampen competition to relatively highly concentrated markets, i.e. to markets where sellers or retailers have little choice but to accept the MFN clause. In markets where sellers have many alternatives the platform is unlikely to be able to use MFNs to sustain higher prices/commissions to sellers.

Related to this concern is how MFNs may affect a supplier's ability to discriminate between different distributors. Setting different prices for different sales channels may be a legitimate way of reacting to different distribution costs or levels of competitive pressure. A seller's promise to extend price discounts to other buyers with an MFN however reduces the seller's incentive to offer price discounts. Indeed, as indicated in a US Department of Justice report, a firm that is required "to reduce prices to some only at the cost of reducing prices to all may well end up by reducing them to none".⁵¹

A restriction on the freedom of action of a seller to price differentiate may indeed discourage the seller in question from lowering prices to buyers, and lead to price increases. The empirical work on MFNs appears to show that MFNs may lead to higher prices, particularly when the buyer subject to the MFN has a higher market share.⁵² Arbatskaya, Hviid and Shaffer conducted a case study on price match and low price guarantees for tires, and found that the more widespread MFNs were in this industry, the higher prices were – "the positive impact of the extent to which LPGs [low-price

guarantees] are widespread in a given market is highly significant... The effect of all firms adopting an LPG in a market is found to be an increase in prices of about 10 percent." They went on to conclude that "If price coordination is enhanced by a widespread adoption of LPGs, then **the share of firms that have a price-matching or price-beating guarantee in the market may play an important role in the price formation.**"

Accordingly, MFNs may result in the application of uniform prices to all customers, unless the seller retains the possibility to increase prices for certain customers by not agreeing to MFNs with them. This effect may be strengthened where the use of MFNs is generalized.⁵³

MFNs may result in the application of uniform prices to all customers

In the European setting, these types of MFNs could be assimilated to a "concerted practice" under Article 101 TFEU, if it can be shown that their introduction substitute practical cooperation between them for the risks of competition.⁵⁴ As noted above, this is, at least in part, what the Commission alleged in the *E-books* case. Indeed, the Commission appeared to take the preliminary view that MFNs acted as a commitment device to move all distributors, including Amazon, to an agency model, a move which in the view of the Commission would result in higher prices.⁵⁵ In other words, the

51 Noëlle Lenoir, Marco Plankensteiner and Elise Créquer, *Increased Scrutiny of Most Favored Nation Clauses in Vertical Agreements*, Law Business Research Ltd 2014.

52 Maria Arbatskaya, Morten Hviid & Greg Shaffer, *On the Incidence and Variety of Low-Price Guarantees: A Case Study*, 47 *Journal of Law & Economics* 307 (2004); Maria Arbatskaya, Morten Hviid & Greg Shaffer, *Promises to Match or Beat the Competition: Evidence from Retail Tire Prices*, 8 *Advances in Applied Microeconomics* 123 (1999); Fiona Scott-Morton, *The Strategic Response by Pharmaceutical Firms to the Medicaid Most-Favored-Customer Rules*, 28 *RAND Journal of Economics* 269 (1997).

53 For a more detailed discussion of the welfare effects of MFN clauses from the perspective of price discrimination, see LEAR Report, *Can "Fair" Prices Be Unfair? A Review of Price Relationship Agreements* (September 2012).

54 Case 48/69 ICI v Commission EU:C:1972:70, paragraph 64.

55 Summary decision – "The retail price MFN clause provided that each of the publishers would have to match on Apple's iBookstore store any lower prices available for the same e-book titles from other online retailers. Combined with the other key pricing terms, the MFN clause would have resulted in lower revenues for publishers if other retailers continued to offer e-books at the prices then prevalent on the market. The Commission took the preliminary view that the financial implications for publishers of the retail price MFN clause were such that this clause acted as a joint commit-

Commission appeared to consider that the MFNs between the publishers and Apple constituted the facilitating device of the alleged concerted practice.

Evidentiary burden to demonstrate the collusive impact of MFNs

European competition authorities, including the Commission itself, have only recently started to examine the anticompetitive potential of MFNs. MFNs do not feature as a discrete category in the Commission's horizontal guidelines, and only appear in the vertical guidelines as a means to reinforce the effectiveness of resale price maintenance (RPM) policies by reducing the buyer's incentive to lower the resale price.⁵⁶ The Commission has therefore provided little guidance as to under what conditions and what type of evidence would justify the application of Article 101 TFEU to MFNs.

In particular, there is little guidance as to whether and under which circumstances MFNs could be held to amount to an infringement of competition by object. In *E-Books*, the Commission took the preliminary view that the MFNs agreed between major publishers and Apple constituted a restriction of competition by object. The Commission relied on the *T-Mobile* case, noting that when assessing whether a practice is anticompetitive, "*regard must be paid in particular to the objectives which it is intended to attain and to its economic and legal context*".⁵⁷ The Commission concluded that the introduction of MFNs formed part of a concerted practice that had the objective of restricting competition. The Commission provided only a brief explanation for its finding of an "object" restriction in this case. However, its findings were only preliminary given that the Commission's investigations were closed following commitments submitted by the publishers and Apple. In any event, the Commission did not appear to identify the MFNs themselves as having the object of restricting competition, only the

overall concerted practice of which they allegedly formed part. Accordingly, it cannot be said that it viewed MFNs as falling in themselves within the object box.

In this regard, account should be taken of the more exacting rules set out in *Groupement des Carte Bancaires* for object restrictions. Indeed, the ECJ's ruling in that case calls for the Commission to engage in a robust analysis of what constitutes an object infringement. As held by the ECJ – "[I]n order to determine whether an agreement between undertakings or a decision by an association of undertakings reveals a sufficient degree of harm to competition that it may be considered a restriction of competition 'by object' within the meaning of Article [101 TFEU], regard must be had to the content of its provisions, its objectives and the economic and legal context of which it forms a part. When determining that context, it is also necessary to take into consideration the nature of the goods or services affected, as well as the real conditions of the functioning and structure of the market or markets in question".⁵⁸

This assessment would require, a detailed analysis of all the relevant factors including MFNs potential efficiency enhancing effects and the level of competitive harm. Indeed, as set out above, MFNs may be pro-competitive in a number of circumstances, and these circumstances would have to be properly weighed in any assessment of the conditions for the applicability of the restriction by object characterization.

That does not mean that the Commission should shy away from examining the potential anti-competitive effects of MFNs. The Commission could, for instance, analyze the price trends of firms who instigate the MFN before and after the adoption of MFNs to check whether prices increased appreciably and systematically after the introduction of MFNs as this may provide an indication as to whether MFNs softened competition or facilitated a collusive equilibrium.⁵⁹

MFNs may also be shown to restrict competition by either object or effect together with other contractual provisions and/or market behavior. In *E-Books*,

ment device'. Each of the five publishers was in a position to force Amazon to accept changing to the agency model or otherwise face the risk of being denied access to the e-books of each of the five publishers, assuming that all five publishers had the same incentive during the same time period, and that Amazon could not have sustained simultaneously being denied access even to only a part of the e-books catalogue of each of the five publishers'.

56 Guidelines on Vertical Restraints, para. 48

57 Joined Cases 96/82 to 102/82, 104/82, 105/82, 108/82 and 110/82 IAZ International Belgium and Others v Commission EU:C:1983:310, paragraph 25; Case C-8/08 T-Mobile Netherlands and Others EU:C:2009:343, paragraph 27.

58 Case C-67/13 P *CB v Commission* [2014] not yet published, para. 53.

59 Analysing the price of rival firms/platforms may not be informative as by definition the MFN will ensure that lower cost rivals prices increase (thereby solving the free-riding issue). Hence an increase in rival prices could equally be evidence that there is a potential free-riding issue.

the Commission found that MFNs breached competition by object in combination with other factual and contractual elements.

Accordingly MFNs may or may not be considered as being anti-competitive by their object, but may in any event restrict competition by effect.⁶⁰

MFNs may also lead to foreclosure effects and thus breach Article 101. We examine the conditions for the application of Article 101 TFEU to the possible foreclosure effects of MFNs in the next section together with the possible application of Article 102 TFEU to MFNs.

Broad bases MFNs can entrench the market power of dominant entities to the point of making such power unassailable

4.2.2. MFNs and abuse of dominance/monopolization

A second major area of concern with respect to MFNs is their use by dominant firms or by firms enjoying a significant amount of market power.⁶¹ Indeed, when adopted by firms having a significant amount of market power, trading partners may not have the ability to refuse MFNs. This may allow MFNs to entrench the firm's market power

60 Noëlle Lenoir, Marco Plankensteiner and Elise Créquer, *Increased Scrutiny of Most Favored Nation Clauses in Vertical Agreements*, Law Business Research Ltd 2014.

61 Steven C. Salop and Fiona Scott Morton, *Developing an Administrable MFN Enforcement Policy*, Antitrust Vol. 27, No.2, Spring 2013; Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favored-Nation Provisions*, Antitrust Vol. 27, No. 2, Spring 2013; Fiona Scott-Morton, *Contracts that Reference Rivals*, Department of Justice, April 5, 2012; Justin Coombs, *Most Favored Customer Clause and competition law: An overview of EU and national case law*, e-Competition n°64758; Ingrid Vandenborre and Michael J. Frese, *Most Favored Nation Clauses Revisited*, European Competition Law Review, 2014; Noëlle Lenoir, Marco Plankensteiner and Elise Créquer, *Increased Scrutiny of Most Favored Nation Clauses in Vertical Agreements*, 2014; Laura Atlee & Yves Botteman, *Resale Price Maintenance and Most-Favored Nation Clauses: The Future Does Not Look Bright*, Competition Policy International, Inc. 2013.

by either softening competition or preventing the emergence or expansion of rivals.⁶² In principle, all of the efficiencies of MFNs discussed previously could still arise in this case, however the potential for harm is greater and therefore may be more likely to offset the efficiency gains associated with these clauses.

MFNs may create barriers to entry

The most immediate possible anticompetitive effect of MFNs when imposed by a firm having a significant amount of market power is the potential to foreclosure of competitors. Indeed, if the only way for new entrants and/or non-dominant undertakings to compete with such a firm is to offer a lower price than the incumbent, price MFNs may foreclose such competition. However to the extent that there are other means to compete and the MFN does not cover those means, – for example innovation, business model, product range, etc., then entrants may still be free to compete on that basis.⁶³

Of course the more restrictive the MFN is in covering all competitive parameters (i.e. including innovation and product range) the more difficult it will be for any new entrant to differentiate itself from the incumbent in order to enter and win market share. Under certain circumstances, it is only through these differentiation strategies that new entrants and/or smaller competitors may effectively compete with a firm having a significant amount of market power. If in these market settings the incumbent imposes MFNs on its suppliers or distributors, this may effectively neutralize any entry/expansion and hence durably entrench the incumbent's position.⁶⁴ As noted by, Baker and Chevalier:

“An MFN can harm competition through exclusion by making it impossible for a dominant incumbent firm's rivals, including entrants, to bargain with input suppliers or distributors for a low price. When the suppliers or distributors have an MFN with a large incumbent, they would lose too much if they made that kind of deal with a small rival or entrant. In this

62 Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favored-Nation Provisions*, Antitrust Vol. 27, No. 2, Spring 2013.

63 Fiona Scott-Morton, *Contracts that Reference Rivals*, Department of Justice, April 5, 2012.

64 See Andre Boik and Kenneth S. Corts, “The Effects of Platform MFNs on Competition and Entry”, working paper, University of Toronto, 18 June 2014.

*way, the MFN discourages the rivals from lowering their own costs, and so prevents them from competing aggressively.*⁶⁵

To achieve this result MFNs need not be based only on price, they need also relate to other variables of completion including product differentiation, innovation, business model,⁶⁶ etc. as this may allow the incumbent neutralize any competitive threat be it based on price and/or quality.

Accordingly, broad based MFNs can entrench the market power of dominant entities to the point of making such power unassailable. This in turn could lead to higher prices (as has been borne out by the empirical work on MFNs) and less innovation.⁶⁷

Indeed, as noted by Scott-Morton, Former Deputy Assistant Attorney General of the Antitrust Division of the U.S. Department of Justice:

“Typically, the literature models the incumbent(s) as having some advantage the entrant (initially) lacks. For example, the incumbent has a known brand, a reputation for quality, or switching costs. In such a circumstance, the entrant needs to provide consumers a reason to purchase its product, or a tool to overcome the incumbent’s advantage. Typical models use price as that tool; the entrant provides a discount relative to the incumbent and induces consumers to try its

*product. However, when the MFN is in place, the incumbent is contractually entitled to the low price of the entrant. Thus the entrant can never create an advantage vis-à-vis the incumbent, and entry is blocked. The DOJ consent decree in Delta Dental (1995) is a nice example of the intuition behind this type of model.*⁶⁸

Accordingly, MFNs may further entrench the incumbent’s market position and lead to the marginalization of competitors to the detriment of consumers. It is this potential effect that appears to be at the core of the Commission’s latest investigation into Amazon’s business practices. The Commission stated that it will focus its investigation on certain parity clauses included in Amazon’s contracts with publishers.

*“These clauses require publishers to inform Amazon about more favourable or alternative terms offered to Amazon’s competitors and/or offer Amazon similar terms and conditions than to its competitors, or through other means ensure that Amazon is offered terms at least as good as those for its competitors. The Commission has concerns that such clauses may make it more difficult for other e-book distributors to compete with Amazon by developing new and innovative products and services. The Commission will investigate whether such clauses may limit competition between different e-book distributors and may reduce choice for consumers. If confirmed, such behaviour could violate EU antitrust rules that prohibit abuses of a dominant market position and restrictive business practices. The opening of proceedings does not pre-judge in any way the outcome of the investigation.”*⁶⁹

65 See Jonathan B. Baker and Judith A. Chevalier, *The Competitive Consequences of Most-Favored-Nation Provisions*, Antitrust Vol. 27, No. 2, Spring 2013 (emphasis added).

66 This clause could make it unworkable for a supplier to experiment with new business models. A company may indeed prefer to trial a new product or business model with a smaller partner, to ensure that the damage is small if something goes wrong. If a supplier is forced to offer experimental terms to their main distributor, it would likely be too risky to experiment at all.

67 The empirical work on MFNs appears to demonstrate that MFNs may lead to higher prices, particularly when the buyer protected by the MFN has a higher market share. See Maria Arbatskaya, Morten Hviid & Greg Shaffer, *On the Incidence and Variety of Low-Price Guarantees: A Case Study*, 47 *Journal of Law & Economics* 307 (2004); Maria Arbatskaya, Morten Hviid & Greg Shaffer, *Promises to Match or Beat the Competition: Evidence from Retail Tire Prices*, 8 *Advances Applied Microeconomics* 123 (1999); Fiona Scott-Morton, *The Strategic Response by Pharmaceutical Firms to the Medicaid Most-Favored-Customer Rules*, 28 *RAND Journal of Economics* 269 (1997). Arbatskaya, Hviid and Shaffer conducted a case study on price match and low price guarantees for tires, and found that the more widespread MFNs were in this industry, the higher prices were – “the positive impact of the extent to which LPGs [low-price guarantees] are widespread in a given market is highly significant. . . The effect of all firms adopting an LPG in a market is found to be an increase in prices of about 10 percent.” They went on to conclude that “If price coordination is enhanced by a widespread adoption of LPGs, then the share of firms that have a price-matching or price-beating guarantee in the market may play an important role in the price formation.”

68 Fiona Scott-Morton, *Contracts that Reference Rivals*, Department of Justice, April 5, 2012 (emphasis added).

69 See EC Press Release, Commission opens formal investigation into Amazon’s e-book distribution arrangements, June 11, 2015, available at http://europa.eu/rapid/press-release_IP-15-5166_en.htm.

5. Conclusions

Whether MFNs are damaging or beneficial to consumers depends, *inter alia*, on the specific competitive dynamics of the market in question, as well as on the market position of their beneficiaries. While they may be justified by efficiency considerations, they may also, in certain market settings, likely give rise to competition concerns, this is the case, in particular of:⁷⁰

- **MFNs adopted by dominant entities/entities with significant market power.** As discussed, the threat to competition arising from MFNs is indeed a function of the market power of the entity it benefits. Where a dominant entity or a company with significant market power enjoys the benefit of an MFN, it may give rise to strong foreclosure or softening of competition effects. This is not to say that MFNs are always problematic, and indeed they may be harmless. However, MFNs imposed by dominant firms or firms with significant market power should be subject to particularly close scrutiny.⁷¹
- **Markets characterized by the presence of barriers to entry.** As a corollary of the above, the foreclosure and softening of competition potential of MFNs is most pronounced in markets characterized by high barriers to entry. In these markets, their trading partners will have relatively few outside options in the form of new entrants, and therefore new entrants and smaller competitors are particularly valuable. To the extent that substantial entry is foreclosed through broad based MFNs that eliminate the ability to develop differentiating strategies to compete in the market, consumers will be harmed.
- **Concentrated Markets.** MFN clauses may be more likely to be harmful in highly concentrated markets where trading partners have relatively few alternatives. It is in such markets that the ability for trading partners to resist MFNs that lead to higher costs will be lowest. Furthermore where there are relatively few players, a seller using MFN clauses enabling it to increase its prices will likely face a lesser risk of losing its customers to competing sellers.⁷²

- **Multiple MFNs With High Market Coverage.** In general the broader the coverage of MFNs, the more likely they are to have negative price effects.⁷³ However it should also be noted that in fragmented markets with a broad coverage of MFNs, firms would also have significant incentives to remove the MFN and trade freely with alternative trading partners.
- **Market Transparency.** MFNs may facilitate collusion by increasing transparency and/or chilling the incentive to lower prices.⁷⁴

Where these conditions do not obtain, competition authorities may be less concerned about MFNs. In any event, there is little doubt that competition authorities will increasingly examine the use of MFNs, and that companies, in particular those with significant market power, should assess more carefully their likely impact on competition.

The authors would like to thank Ian Hastings, Ben Holles and Ana Doblaz for their contribution.

70 Steven C. Salop and Fiona Scott Morton, *Developing an Administrative MFN Enforcement Policy*, Antitrust Vol. 27, No.2, Spring 2013.

71 Noëlle Lenoir, Marco Plankensteiner and Elise Créquer, *Increased Scrutiny of Most Favored Nation Clauses in Vertical Agreements*, Law Business Research Ltd 2014.

72 Noëlle Lenoir, Marco Plankensteiner and Elise Créquer, *Increased*

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73 Steven C. Salop and Fiona Scott Morton, *Developing an Administrative MFN Enforcement Policy*, Antitrust Vol. 27, No.2, Spring 2013.

74 Ingrid Vandenborre, Michael J. Frese, *Most Favored Nation Clauses Revisited*, European Competition Law Review, Issue 12 2014.