EUROPEAN COMMISSION

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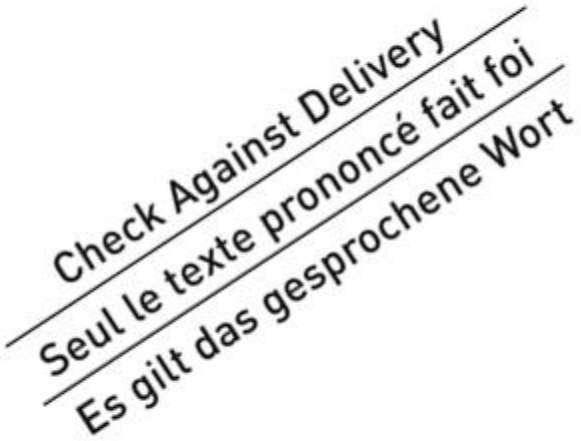
Vertical restraints, digital marketplaces, and enforcement tools



ICN Annual Conference 2018
New Delhi, 22 March 2018

Vertical restraints, digital marketplaces, and enforcement tools

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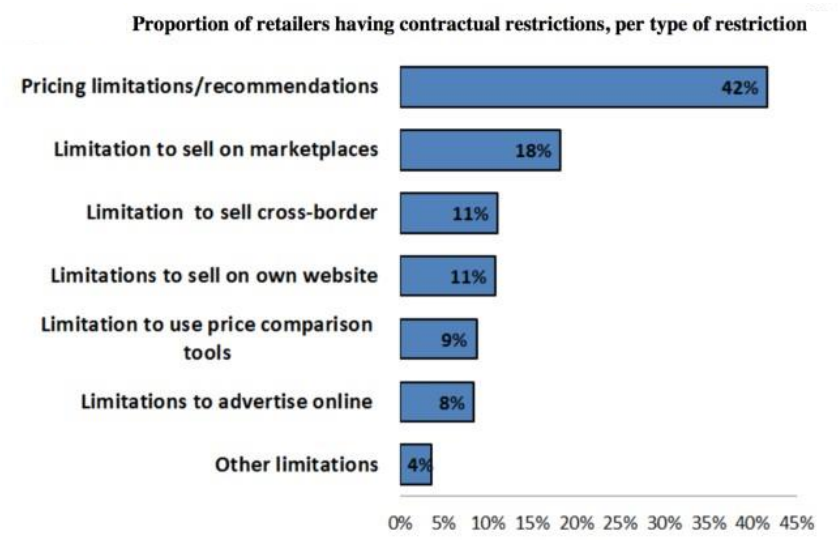
Why do we do look into vertical restraints in Europe and why has there been a recent enforcement focus on them?

Consumers are embracing e-commerce with increasing enthusiasm. At the same time, e-commerce has changed the dynamics and incentives of companies in the distribution chain. The European Commission's wide scale sector inquiry into e-commerce markets carried out between 2015 and 2017 – which had about 1,800 respondents and allowed us to analyse about 8,000 distribution agreements – shows that vertical restrictions affecting online sales are widespread. While e-commerce has enormous potential to boost cross-border trade, technical measures allow companies to implement or monitor vertical restrictions with little effort, for example through geo-blocking practices.

E-commerce sector inquiry: Findings on vertical restraints



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When it comes to pricing, e-commerce on the one hand significantly increases price competition; on the other it provides possibilities for manufacturers to easily monitor the price-setting behaviour of retailers and intervene to dampen price pressure. Many online retailers use pricing software to automatically adjust retail prices to those of competitors. 53% of the e-commerce sector inquiry respondents track competitors' online prices and 67% of these do so automatically using software designed for the purpose. 78% of retailers who use price-tracking software adjust their own prices to those of their competitors. Most of the restrictions we see are well-established vertical restraints in digital garb, such as resale price maintenance or territorial sales restrictions. Other restrictions – such as sales or advertising restrictions concerning online platforms or so-called MFN-clauses (Most-Favoured-Nation or Most-Favoured-Customer clauses) – may raise new issues.

While vertical restraints are typically less harmful than horizontal restraints between competitors, they may also negatively affect competition, especially when they are widespread as we found in the e-commerce sector inquiry. Vertical restraints may lead to foreclosure of other suppliers or buyers and facilitate collusion at the supplier or buyer level. RPM practices directly lead to a reduction of intrabrand price competition and MFN-clauses used by online platforms may for example lead to the foreclosure of more efficient smaller platforms.

In addition, we in Europe are particularly concerned about vertical restrictions used to partition markets along national borders. Such market fragmentation is in contradiction to our objective of building an integrated Single Market in Europe. Promoting market integration is a specific goal of EU competition rules enshrined in the Treaty of Rome. In the last 60 years the EU Courts have constantly found that vertical restrictions hindering market

integration restrict competition. In the context of the e-commerce sector inquiry, the Commission has initiated a number of specific investigations regarding vertical restraints – which are ongoing – namely on territorial restrictions and on resale-price-management practices.

Online platforms increasingly act as intermediaries for e-commerce transactions

E-commerce is a game changer for many businesses. Business models such as online platforms which intermediate e-commerce transactions are on the rise. Platforms are particularly important for SMEs as they offer easy access to new markets, customers and business opportunities. Their increased importance can be seen in the results of the Commission's e-commerce sector inquiry. The results show that smaller and medium sized retailers of goods (with a turnover of less than €2 million) are more likely to sell on online marketplaces such as Amazon and e-Bay; less likely to sell through their own online shops only; and typically achieved a higher proportion of their turnover via online marketplaces compared to other online sales channels. The leading online platforms are large companies which benefit from strong indirect network effects that may further strengthen their market power.

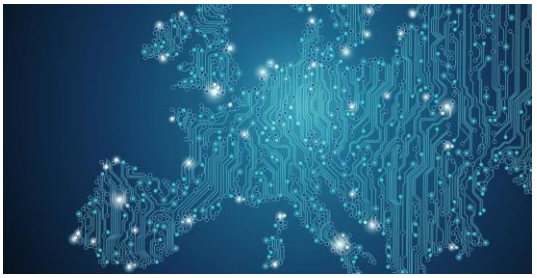
In this environment, we have to ask ourselves how can we deal with these intermediaries under competition rules. How do we qualify platforms' business models as we analyse the relationships they establish with other businesses? Are these classical vertical agreements between suppliers and buyers? Who is the supplier and who is the buyer? Should e-

commerce platforms be considered as distributors in a vertical distribution chain? Or should they be considered as mere providers of intermediation or platform services? What are the relevant criteria we can use to distinguish between the two? The answers to these questions will have important consequences for the legal analysis of such restrictions as MFN clauses, for market definition, and ultimately for the analysis of market power. Each platform and business model will have to be analysed on a case-by-case basis. Important factors in this analysis will be the concrete function of individual platforms and their actual involvement in the transaction with consumers.

Another question that needs to be answered is to which extent manufacturers can prevent their distributors from selling on online platforms? They may consider that online sales harm their brand image. They may be concerned about the growing market power of platforms and may want to counterbalance it by not having their products sold on a specific platform. The European Court of Justice recently sided with manufacturers' concerns in the "Coty" judgment allowing them to retain the freedom to decide by themselves to which extent they can consent to the sale of their products on online platforms and to control the distribution of their products.

Of course, these questions are not only for competition law. The European Commission is currently assessing whether the imbalance of bargaining power between online platforms and business users as well as the increased dependency on such platforms by SMEs requires regulatory intervention outside the area of competition law to address certain unfair practices of online platforms, such as for example non-negotiable terms and conditions, delisting of products, lack of transparency, and lack of effective redress.

Broader Commission's initiatives



- Competition policy and enforcement part of a broader policy toolkit
- European Commission looking into platforms for possible intervention beyond competition law
- Internal reflections ongoing based on a broad range of evidence

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Platforms' market power

Online platforms may gain significant market power and competition law enforcers must be able to tackle restrictions that harm competition between online platforms. We have achieved exactly that in our Amazon e-books case, which shows that our enforcement in digital markets is delivering results and is delivering them quickly.

The Amazon e-book case

- Markets for platform must stay open and contestable
- Keen competition between online platforms is vital

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In June 2015, we opened an investigation against Amazon because we had concerns about Amazon's practices regarding certain MFN clauses in its e-books distribution agreements. At the time, Amazon was using different MFN clauses in its e-book distribution contracts. These clauses required publishers to inform Amazon when offering more favourable terms elsewhere and to make them also available to Amazon. The clauses involved not only pricing but also many aspects that a competitor could use to differentiate itself from Amazon, such as other business or distribution models, earlier launch dates for the e-books or promotional offers.

Our preliminary assessment showed that these clauses were likely to make it impossible for Amazon’s rivals to stand out and come up with innovative distribution models in order to challenge Amazon. The contested clauses were preliminarily considered as hindering e-book suppliers and competing e-book retailers' ability and incentives to support and invest in alternative and differentiated business models and e-book offerings. Further, they appeared to be reducing the competitiveness of e-book retailers by limiting their ability and incentive to develop and differentiate their e-book offerings, thereby reducing barriers to entry and expansion in the relevant markets. Finally, the contested clauses likely hindered entry and

expansion of competing e-book retailers, and therefore competition at the e-books retail distribution level.

In short, Amazon's practices regarding the contested clauses may have led to less choice, less innovation and higher prices for consumers. Moreover, the Commission preliminarily considered that the combination of the different clauses was likely to reinforce the potential anti-competitive effects of the individual clauses. In order to terminate the antitrust proceedings, in early 2017, Amazon offered not to enforce the respective clauses for a period of 5 years Europe-wide and not to include them in any new contracts. These commitments were declared legally binding by the Commission in May 2017 after less than two years since the opening of the investigation. A trustee is in charge of monitoring the application of the commitments.

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Evolving business models might require evolving approaches in the assessment under competition law. The particularities of online platforms require an adaptation and refinement of the application of existing tools, to allow competition authorities to tackle harmful practices and capture the particularities of the markets concerned properly. It is important to keep platform markets open and contestable and allow competition between multiple online platforms.

The Google Shopping case

- Google foreclosed competition and became market leader in all 13 EEA markets concerned
- Less choice and innovation for consumers
- Reduced incentives to innovate and improve for competitors

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This is what the Commission did in its Google Shopping decision of June 2017 in which it concluded that Google had abused its dominant position through the more favourable treatment of its comparison shopping service vis-à-vis its rivals in its general search results.

This more favourable treatment manifested itself in two ways. First, Google demoted rival comparison shopping services in its general search results. At the same time, Google systematically gave prominent placement in a rich format to its own comparison shopping service in response to relevant product-related queries. To be clear, we did not have an issue either with the design of the algorithm as such nor to the presentation of comparison shopping results in a prominent manner, but to the fact that Google did not subject its comparison shopping service to the same algorithm and the same demotion mechanism as rivals, and at the same time that it was systematically only Google's comparison shopping results that were prominently displayed.

The abuse is a classical leveraging abuse where a dominant company gives its own product in an adjacent market an illegal advantage. It is based on a detailed analysis of effects. In particular – following the analysis of 5.2 Terabytes of data, i.e. 1.7 billion search queries – the decision found that Google is a very important source of traffic for competing comparison shopping services and based on a range of empirical sources, that there is a clear link between visibility and format in Google's general search results and how much a site gets clicked on. Results that are higher and in a more visible format attract significantly more clicks than those that are lower or beyond the first page. On average, rivals were on the fourth page, which is as good as being virtually invisible. Google itself was clearly aware of this link.

On this basis, the decision concluded that Google's comparison shopping service gained significant traffic at the expense of its rivals. It did so not on the merits, but because, irrespective of its relevance to a particular query, it was systematically positioned at the top of Google's general search results whilst rivals were demoted. Google foreclosed competition in all 13 EEA markets concerned, becoming the market leader in these markets, in many of them by a large amount. Google's conduct reduced genuine choice and innovation. Consumers would rarely even see, let alone click on, rival comparison shopping services, and these were deterred from innovating because they knew that however good they are, this would be the case.

Conclusion

The European Commission is following these market developments very closely on the basis of extensive fact- and evidence-finding and strives to tackle practices that are detrimental to consumer welfare. Digitalisation, development of online trade and the enhanced role of platforms lead to disruptive change in this environment. The task of competition enforcers is to make sure that this disruption translates into tangible benefits for consumers. For this to happen, we need to keep markets open and contestable, including through the deployment of our enforcement tools.

Thank you.