



(Re)visiting vertical agreements with digital platforms

EAGCP Plenary Meeting
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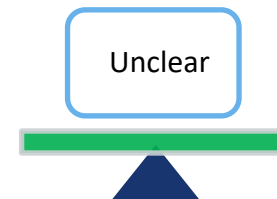
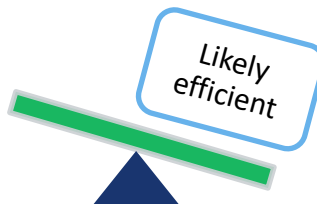
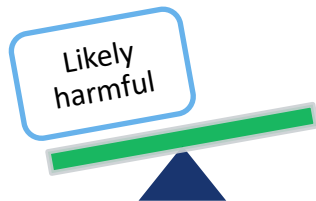
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organisation with which I am associated!

Background

- ❖ The 2010 EU Vertical Agreements Block Exemption Regulation expires on 31 May 2022. The current VABER is accompanied by Guidelines on Vertical Restraints.
- ❖ The growth of digital platforms, and increasing concerns around them, raises an obvious question:
 - How well are these addressed in the current VABER and guidelines?
- ❖ Answer: Not well at all. Platforms are not typical sellers or buyers.
 - Even in guidelines, the word ‘platform’ only occurs three times (on p 21), in relation to agreements between a supplier and distributor about use of a third party platform.
 - Nothing about vertical agreements with digital platforms.
- ❖ Does this matter? I think so.

VABER – A quick reminder of the basics



Hardcore restrictions	Block exemption (or no infringement)	Case by case analysis required
<ul style="list-style-type: none"> • Fixed/minimum RPM • Absolute territorial protection • A number of restrictions on distributors ability to sell freely online 	<p>Exempt: Most other restrictions, so long as <u>buyer</u> and <u>supplier</u> both have less than 30% market share.</p> <p>No infringement for purely qualitative selective distribution , max RPM or agency arrangements</p>	<p>Everything else....but generally more likely to be exempt if looks more like something that would be exempt</p>

NB Exemption can theoretically be removed where networks of agreements, but seems almost impossible.

Key questions raised

1. What is different about the economics of digital platforms?
2. Why does this matter?
3. What new types of vertical agreements are we seeing?
4. What are the economic issues arising from these?
5. What are some implications for the VABER (and verticals guidelines)?

NB Upfront health warning: This presentation is designed to generate discussion. It offers more questions than answers! And it is based on zero modelling.

1. What is different about the economics of digital platforms?

- ❖ Potentially very ‘tippy’ markets (many are duopolies/monopolies) due to:
 - Strong – and global – economies of scale and scope; no major capacity constraints.
 - Strong network effects, both direct and indirect.
 - The importance of data, including further economies of scale and scope.
 - Behavioural biases, especially amongst consumers.

- ❖ Does tipping matter?
 - In general, competition **in** the market preferable to competition **for** the market.
 - ‘Tipped markets’ especially problematic if limited potential for then ‘re-tipping’, since embedded monopolies have poor incentives to offer good VfM or invest in innovation.
 - Tipping also problematic if the ‘best platform’ doesn’t win the market.

1. What is different about the economics of digital platforms?

- ❖ In addition, if one platform market tips, this can increase the likelihood that other related markets will also tip (to the same firm):
 - either because of economic dependence of the second market on the first (eg self-preferencing issues)
 - or due to strong economies of scope across markets (eg through re-use of data)
- ❖ Even without tipping, platforms may be ‘must have’ bottlenecks over access by business users to ‘single homing’ consumers/eyeballs. This in turn gives platforms substantial power to control online success of business users via their control of criteria for platform access/ranking/scoring/prominence.

2. Why does this matter?

- ❖ Even for well-understood VRs, we arguably need a more stringent approach if they may exacerbate the risk of market tipping or extension into new markets.
 - And may want to do this before markets start tipping (ie when shares are fairly low)
 - But may also want to be relatively lenient towards factors that limit tipping.
- ❖ Tricky issue: Some vertical restraints can act in both directions. For example:
 - Multi-homing can be valuable in preventing market tipping. As such, exclusivity provisions, which create single homing on one side of a platform, might be expected to increase the likelihood of market tipping.
 - At the same time, platform differentiation can help to prevent tipping. As such, exclusivity provisions which enable platforms to offer differentiated products may help to reduce the likelihood of market tipping.

2. Why does this matter?

- ❖ How might the 30% market share threshold in VABER apply to competing platforms:
 - Does a ‘bottleneck’ position on one side of a platform automatically imply > 30% in a narrow one-sided market?
 - Or should we apply a ‘two-sided’ approach to market definition, looking at overall competition between platforms ?
 - If the former, VRs will rarely be block exempt. But the latter may understate the competitive importance of the ‘bottleneck’.

- ❖ Which fits best with theories of harm?
 - If worried about overall platform profits, two-sided approach makes sense.
 - But we may also be worried that a bottleneck position could give a platform the ability and incentive to impose highly anti-competitive VRs on business users.

2. Why does this matter?

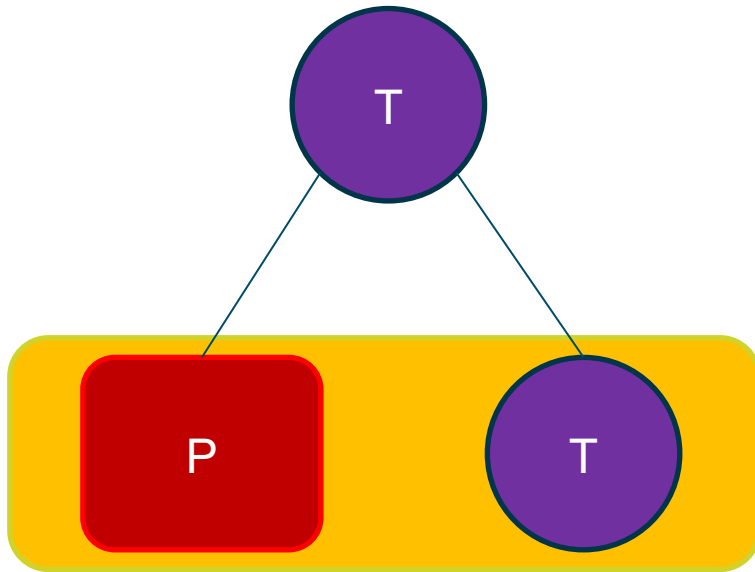
- ❖ Factors other than market share as a buyer or seller may also be relevant:
 - VRs may be more harmful than the platform company's share in a relevant market might suggest, **if that company has a very strong position in a related market**
 - Eg. Google Home may have stronger incentive and ability to impose anticompetitive VRs than its 24% share of home digital assistants might suggest
 - VRs may be more harmful than the platform company's share in a relevant market might suggest, **if that company is also active as a horizontal rival of those 3rd parties**
 - Eg Amazon Marketplace may have a stronger incentive to impose anticompetitive VRs on its traders than its share as a platform in some online markets might suggest, due to its role as a rival to those traders. [effectively self-preferencing]

2. Why does this matter?

- ❖ **Key point:** We seem to observe a number of new types of vertical agreements **between** platforms and their business users.
 - i. Vertical agreements which restrict horizontal competition between a platform and a trader in selling the trader's own product.
 - ii. Vertical agreements which restrict or distort horizontal competition in the market using the platform.
 - iii. Vertical agreements which limit competition across platforms.
- ❖ These are now discussed in more detail. [NB Not focusing here on agreements between sellers and buyers that **relate to** their use of platforms – eg platform bans]

3. What new types of vertical agreements are we seeing between platforms and their business users? (i)

- i. Vertical agreements which restrict horizontal competition between a platform and a trader in selling the trader's own product.



- ❖ Could be imposed by the platform on the trader, eg:
 - Narrow MFNs
- ❖ Or by the trader on the platform, eg:
 - Non-resolicitation clauses
- ❖ Or by either on either, or agreed, eg:
 - Keyword-bidding restrictions: Agreements not to competing in bidding on keywords (or other forms of advertising)

4. What are the economic issues arising? (i)

- ❖ Effectively horizontal agreements between a platform and trader's own sales arm.
- ❖ But, apart from advertising restrictions in Dec 2018 Guess case, and narrow MFNs in some jurisdictions, all treated leniently so far.
 - And NB Guess case about supplier/retailer agreement, not a supplier/platform.
- ❖ NB Can partly be seen as a battle over brand.
 - Platforms want to embed their brand as 'first point of call' for the customer journey and in doing so to commoditise suppliers.
 - Suppliers want to retain control over their own brand/trademark, which is a key part of their competitive proposition, and to remain a 'first point of call' for (at least) returning customers.

Some economic pros and cons

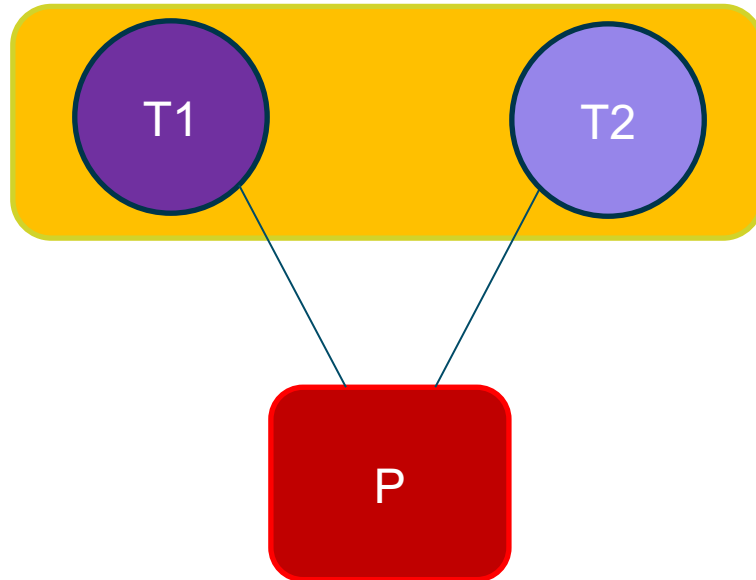
	Pro-competitive arguments	Anti-competitive arguments
Keyword-bidding restrictions	<ul style="list-style-type: none"> ❖ Limit exploitation by advertising platforms of ‘narrow market power’. [NB Higher prices for advertising likely to be passed on as higher prices to consumers.] ❖ May limit consumer confusion. ❖ May help protect trader’s brand value (If restriction is on platform). ❖ Encourage platform use by traders (if restriction is on platform). 	<ul style="list-style-type: none"> ❖ Limits direct competition between brand and platform <ul style="list-style-type: none"> ➤ although does depend on the counterfactual. ❖ Harm to trader’s brand (if restriction is on trader not to advertise) <ul style="list-style-type: none"> ➤ This could in turn harm other platforms, if they partly rely on exploiting traders’ brands.

Some economic pros and cons

	Pro-competitive arguments	Anti-competitive arguments
Non-resolicitation clauses	<ul style="list-style-type: none"> ❖ Limit excessive consumer switching, and allows recoupment of customer acquisition costs. ❖ Encourage platform use by traders. ❖ May help to preserve multiple routes to market. 	<ul style="list-style-type: none"> ❖ Limits active competition for consumers, in a situation where strong consumer inertia. ❖ May aid exploitation of non-switchers (If price discrimination possible).
Narrow MFNs	<ul style="list-style-type: none"> ❖ Limits free riding by traders on platform investment. ❖ Encourages consumer search across traders by making platform primary point of call, where 'best offers' must be made. 	<ul style="list-style-type: none"> ❖ Reduces pressure on platform commission rates if direct supply would otherwise be a constraint. ❖ 'Battle over brand' harm to trader ❖ Network of narrow MFNs can act as wide MFN (See later).

3. What new types of vertical agreements are we seeing between platforms and their business users? (ii)

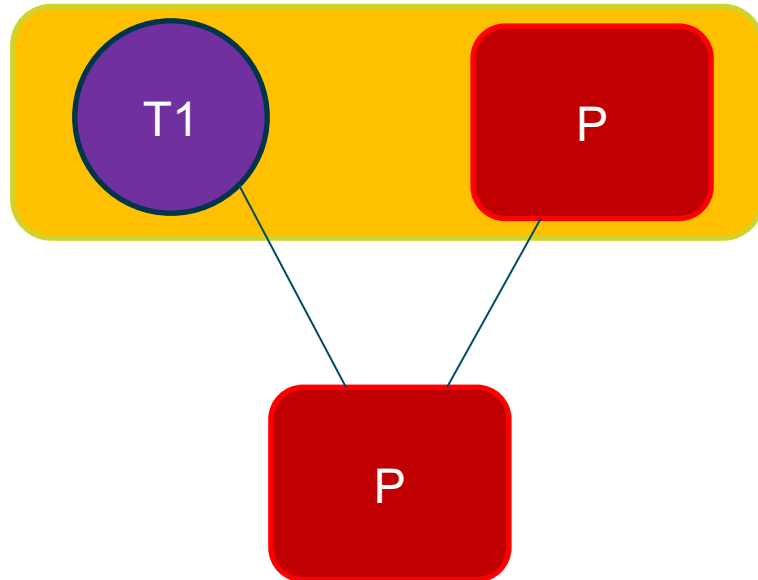
- ii. Vertical agreements which restrict or distort horizontal competition in the market using the platform



- ❖ These include:
 - Unfair and non-transparent terms around eg access, prominence, scoring, rankings.
 - Refusal to give relevant info to trader about its sales.

3. What new types of vertical agreements are we seeing between platforms and their business users? (ii)

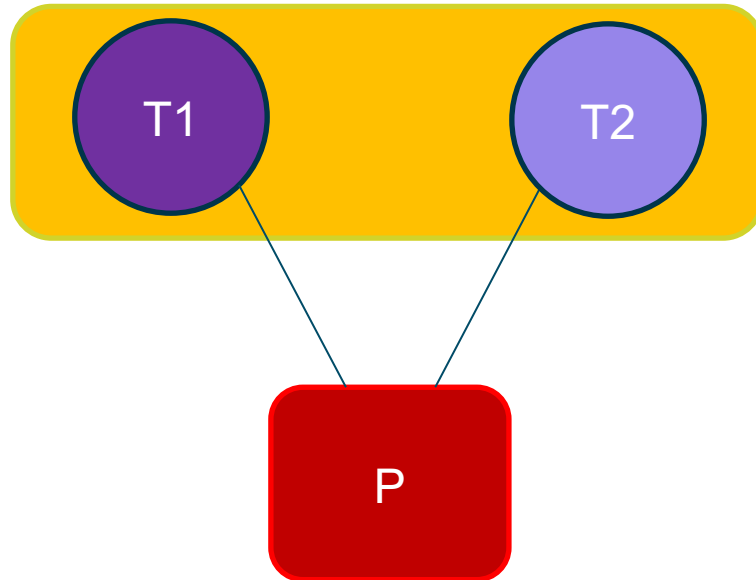
- ii. Vertical agreements which restrict or distort horizontal competition in the market using the platform



- ❖ These include:
 - Unfair and non-transparent terms around eg access, prominence, scoring, rankings.
 - Refusal to give relevant info to trader about its sales.
- ❖ Especially concerning **where platform is also active as a rival in the related market**. Can also lead to:
 - Requirements on traders to give business information to platform.

3. What new types of vertical agreements are we seeing between platforms and their business users? (ii)

- ii. Vertical agreements which restrict or distort horizontal competition in the market using the platform



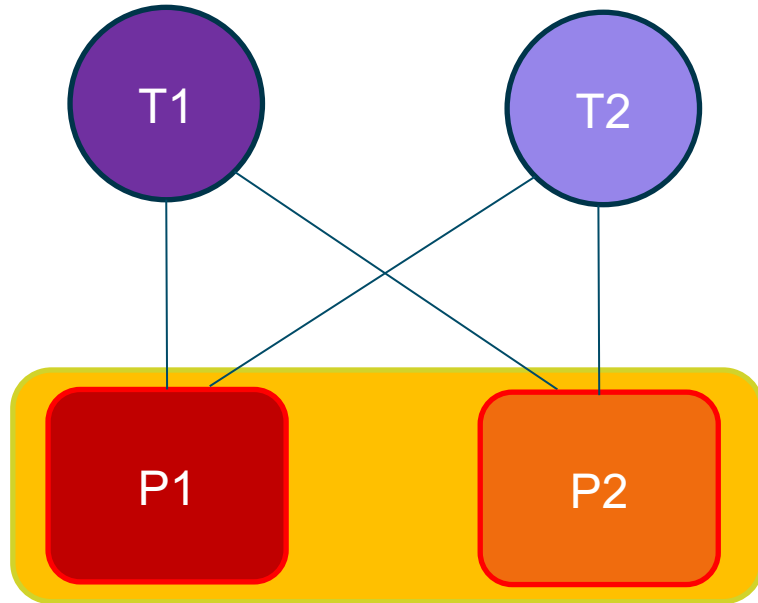
- ❖ NB Also, risk of price delegation to a automated dynamic pricing platform! (Eg Boomerang)
- Could this lead to 'hub and spoke' type collusion?

4. What are the economic issues arising? (ii)

- ❖ Four key types of concern:
 - *Exploitative*: Provide an enhanced route to exploit a bottleneck position over traders.
 - *Distortionary*: Distorts competition between platform users.
 - *Exclusionary*: Most likely to occur when the platform is also active in the user market (self-preferencing).
 - *Collusion across traders*: Via delegation of pricing.
- ❖ NB The new EU Platform to Business regulation will help limit the first three concerns, though requiring clearer disclosure around access and ranking criteria.
 - But this may not be enough.... Should VABER/guidelines also have a role?

3. What new types of vertical agreements are we seeing between platforms and their business users? (iii)

iii. Vertical agreements which limit competition across platforms.



- ❖ These include:
 - [Exclusive dealing]
 - Wide MFNs (on price and on content)
 - Restrictions around data access and use (Eg Google advertising allegations)

4. What are the economic issues arising? (iii)

- ❖ MFNs can dampen competition on commissions and deter entry (see Rossi's slides).
- ❖ A further common issue is these agreements tend to limit multi-homing, either on the trader side or the consumer side.
 - Pros: Can enhance competition, taking market structure as given, if it competition for single-homing side increases.
 - Cons: Can increase risk of market tipping!

[Addendum]

- ❖ NB1: These graphics place platforms downstream, to reflect proximity to end consumers, but this may be misleading.
 - Platforms can equally be seen as upstream suppliers (eg of distribution/ advertising/price formation services)
 - [NB Does price setting by traders on platforms equate to RPM?]

- ❖ NB2: We also observe ranking criteria which equate to vertical agreements:
 - Sometimes explicitly (eg Booking.com and MFNs)
 - Sometimes implicitly (eg criteria relating to conversion rates)

[See: Hunold et al (2018)]

5. What are the implications for the VABER and guidelines?

- ❖ Important to (re)visit the approach to vertical agreements with platforms.
- ❖ BUT far from straightforward to determine right approach.
- ❖ Key question is whether appropriate to apply VABER if both market shares < 30%. This in turn depends on:
 - whether a bottleneck position suggests narrow markets, even if competition with other platforms in wider platform market. If so, VABER as it stands does nothing
 - whether a platform's position in both markets is relevant to likely effects
 - whether a platform's position in related markets is relevant to likely effects
- Another question is whether a more interventionist approach is required in order to prevent risk of rapid market tipping even from a low initial share. It is also important to understand better the likely effects of networks of agreements
- ❖ **More thinking required.** (Yes, a cop out!). Looking forward to Staff Working Document!



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Questions/discussion

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