

## **Anything wrong with asking for the best price?**

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## Introduction

1. Most Favoured Nation (“MFN”) clauses have garnered considerable attention from competition regulators lately. In its basic form, MFN clause is a vertical agreement where one party to the contract agrees to provide terms to the other that are at least as favourable as those granted to any other party(s). These clauses are used in industries as diverse as the health insurance industry, media industry and gas industry.

2. MFN clauses may differ across several dimensions. The clauses may be implemented at a wholesale level or a retail level and the adoption of the clause may be part of a long term contract or as a unilaterally announced policy. MFN clauses may make reference to prices offered to other buyers in the same period (i.e. contemporaneous policy) or in the future period (i.e. retroactive policy). For example, a buyer that benefits from a retroactive MFN may be assured that, should a discount be subsequently given to future buyers, the discount would also be given to him for the earlier purchase. MFN clauses may be structured as a ‘MFN-plus’ which assures the buyer that it will receive better terms and conditions vis-à-vis its competitors, or ‘equal-to-MFN’ which guarantees the same terms and conditions as its competitors.<sup>1</sup>

3. With the development of e-commerce in various industries and increasing market power of some established internet platforms, other varieties of MFN clauses have emerged. In particular, one such form of MFN clause, commonly known as a retail price MFN clause, has been the centre of several recent antitrust cases. A retail price MFN clause is an agreement between a seller and an intermediary (i.e. a platform), which stipulates that the seller does not price its goods at a lower retail price on other intermediaries. Competition regulators have stepped in to investigate and challenge these MFN arrangements, for example in the E-Books case by the European Commission, the online hotel portal case by the German Federal Cartel Office and it was also a key aspect of the recently concluded market investigation into the Private Motor Insurance industry in the UK by the Competition & Markets Authority (“CMA”).<sup>2</sup>

4. In Singapore, the internet has grown to become a ubiquitous medium which businesses and consumers use to conduct economic transactions. The Straits Times reported that online shoppers will spend SGD4.4 billion in 2015 up from an estimated SGD1.9 billion in 2012.<sup>3</sup> With more consumers and businesses turning to e-commerce, the

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<sup>1</sup> DOJ/FTC Workshop on Most-Favored Nations Clauses and Antitrust Enforcement and Policy, *Competitive Harm from MFNs: Economic Theories* (Jonathan B. Baker) and *Efficiencies from MFNs: Economic Theories* (Judith A. Chevalier), 10 Sep 2012. URL: <http://www.justice.gov/atr/public/workshops/mfn/>

<sup>2</sup> The Wall Street Journal, “*Favored Nations’ fight for online digital rights*”, 14 Jun 2012. URL: <http://online.wsj.com/news/articles/SB10001424052702303410404577466940749077080>. See also Bundeskartellamt, “*Online hotel portal HRS’s ‘best price’ clause violates competition law – proceedings also initiated against other hotel portals*”, 20 Dec 2013. URL: [http://www.bundeskartellamt.de/SharedDocs/Meldung/EN/Pressemitteilungen/2013/20\\_12\\_2013\\_HRS.html](http://www.bundeskartellamt.de/SharedDocs/Meldung/EN/Pressemitteilungen/2013/20_12_2013_HRS.html). See also European Commission, *Case COMP/AT.39847 E-Books*, 12 Dec 2012. URL: [http://ec.europa.eu/competition/antitrust/cases/dec\\_docs/39847/39847\\_26804\\_4.pdf](http://ec.europa.eu/competition/antitrust/cases/dec_docs/39847/39847_26804_4.pdf). See also Office of Fair Trading, *CA98/01/2010 Case CE/2596-03*, 15 April 2010. URL: <http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.oft.gov.uk/OFTwork/competition-act-and-cartels/ca98/decisions/tobacco>

<sup>3</sup> The Straits Times, “*Singaporeans are Big Online Shoppers*”, 18 Aug 2013.

use of MFN clauses in the online market may potentially be relevant to Singapore as well.

5. This paper discusses some cases involving MFN clauses, in particular, to draw out the forms of these clauses, the theories of harm (“TOHs”) and the possible pro-competitive benefits arising from the use of these MFN clauses. We will then examine the assessment of such MFN clauses under the Singapore framework.

#### Across-buyers MFN clauses: Offer me your best price

6. Across-buyers MFN clauses is essentially a vertical agreement between a seller and a buyer where the seller agrees to provide terms to a buyer that are at least as favourable as those granted to any other buyer(s). Across-buyers MFN clauses may occur at the wholesale or retail level; and in instances where an across-buyers MFN clause constrains the wholesale price between a supplier and a retailer, it may be also termed as a “wholesale MFN clause”. This form of MFN clauses was the subject of the case brought against Blue Cross Blue Shield (“Blue Cross”).

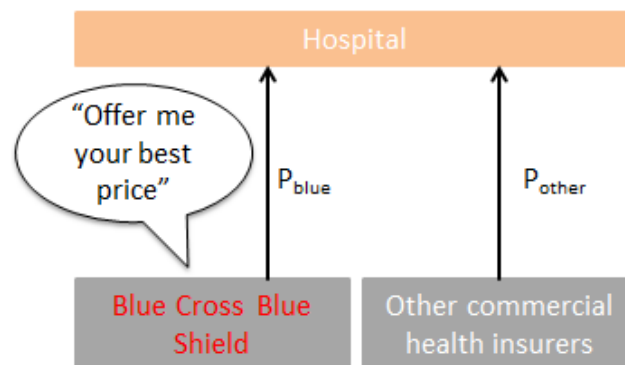
#### *Blue Cross*

7. In 2010, the United States Department of Justice (“DOJ”) brought a case against Blue Cross with regard to the ‘equal-to-MFN’ and ‘MFN-plus’ clauses that were included in the contracts between Blue Cross and more than 70 general acute care hospitals in Michigan. Blue Cross was regarded as a commercial health insurance provider with market power in the relevant local geographic markets within Michigan at that point in time. It had identified that the discounts obtained from the hospitals were its largest source of competitive advantage; hence it sought and included two forms of MFN clauses into the contracts with some of the general acute care hospitals in Michigan, namely ‘equal-to-MFN’ clauses; and ‘MFN-plus’ clauses. In most instances, Blue Cross agreed to pay a higher price to the hospitals in exchange for an MFN clause. This assured Blue Cross that, while its cost was raised, its competitors would face the same higher cost or even higher costs.<sup>4</sup> The reference prices in these MFN clauses were taken from prices offered by the same hospital (i.e. supplier of service) to other commercial insurers (i.e. buyer of service). These MFN agreements are illustrated in Figure 1 below.

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<sup>4</sup> The United States Department of Justice, *United States and State of Michigan v. Blue Cross Blue Shield of Michigan*, 2010. URL: <http://www.justice.gov/atr/cases/bcbasmfn.html>.

**Figure 1: MFN clauses implemented between Blue Cross and the hospitals**



**Notes:**

- $P_{blue}$  and  $P_{other}$  are prices charged by the hospital to Blue Cross and the other commercial insurers respectively.
- The equal-to-MFN clauses require hospitals to charge other commercial insurers at least as much as they charge Blue Cross, i.e.  $P_{other} \geq P_{blue}$ .
- The MFN-plus clauses require hospitals to charge some or all other commercial insurers more than they charge Blue Cross, i.e.  $P_{other} > P_{blue}$ .

**Anti-competitive potential of across-buyers MFN clauses**

8. The use of across-buyers MFN clauses may, under certain circumstances, give rise to anti-competitive effects such as raising entry barriers in the buyers’ market which leads to reduced entry and higher prices to consumers; and facilitating and sustaining collusion between the sellers.

**Raising entry barriers**

9. In the Blue Cross case, the DOJ noted that a key component of commercial health insurance is the access to a network of hospitals. Further, as hospital costs are a substantial portion of medical care cost, insurers’ hospital costs are an important element of insurer’s ability to offer competitive prices. The MFN clauses in Blue Cross’ contracts with at least one significant hospital in each local geographic market had the effect of raising entry barriers and reducing competition among commercial health insurers as competitors were unable to obtain competitive rates. Instances of failed entry by other commercial health insurance providers were detailed in the civil action filed by the DOJ. For example, a competitor, Priority Health, decided not to enter the market after obtaining an offer with significantly higher rates from Marquette General Hospital (which had a MFN-plus agreement with Blue Cross).<sup>5</sup>

10. The DOJ also raised its concern that the MFN clauses had the effect of limiting the hospitals from offering more discounts to Blue Cross’ competitors. In doing so, it restricted its competitors’ abilities to obtain competitive or lower prices from the hospitals, which affected their ability to compete with Blue Cross effectively. MFN-plus clauses further

<sup>5</sup> *ibid.*

amplified this effect by ensuring that Blue Cross would be given a lower rate than its competitors. As a result of these MFN clauses, some hospitals revised the discounts given to other commercial health insurance providers and this consequently reduced the other insurers' ability to compete effectively, further lessening competition in the commercial health insurance market.<sup>6</sup>

### European Cinemas

11. Foreclosure concerns were also raised by the European Commission ("EC") in its investigations involving across-buyers MFN clauses in the contracts relating to the financing and installation of digital projection equipment in European Cinemas. Both film distributors and cinemas contribute towards the investment costs which are initially paid by a third party equipment integrator, where the film studios paid contribution fees for the digital projection in cinemas.<sup>7</sup> The contracts between the major Hollywood film studios and the equipment integrators included MFN clauses which gave the respective film studio the most favourable terms, i.e. lower payments to the integrators for the recoupment of the equipment. The EC noted that the MFN clauses in the contracts could hinder the equipment integrators from entering into contracts with distributors of independent/art house films with different business model from that of the Hollywood film studios. This may then restrict independent distributors' access to these cinemas, hence leading to foreclosure effects in the market.<sup>8</sup>

### Delta Dental

12. Across-buyers MFN clauses may have the effect of reducing the seller's incentive to negotiate with the new entrant and offer lower prices as it would have to provide the same discount to the incumbent firm protected by the MFN clause. As such, a new entrant to the buyers' market may not be able to negotiate with sellers and enter the market using a low cost/low price strategy. Such effects were observed in the DOJ case against Delta Dental of Rhode Island ("Delta Dental") where Delta Dental, Rhode Island's largest dental insurer, entered into agreements containing across-buyers MFN clauses with 90 percent of dentists in Rhode Island. These clauses stipulated that Delta Dental has the right to lower the fees it pays a dentist to the level of the lowest fees that the dentist charges any other plan. As the largest player in the dental insurance market, Delta Dental provided a large part of most Rhode Island's dentists' income. As such, if these dentists were to reduce their fees to other dental insurers/managed care plans, the resulting decrease in income from Delta Dental would be larger than the additional income from the other dental insurers/managed care plans. Hence, the participating dentists had strong disincentives to contract with dental

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<sup>6</sup> The United States Department of Justice, *United States and State of Michigan v. Blue Cross Blue Shield of Michigan*. Civil Action No. 2: 10-cv-15155-DPH-MKM Complaint, 18 Oct 2010. Specifically paragraphs 49 to 79. URL: <http://www.justice.gov/atr/cases/f263200/263235.htm>.

<sup>7</sup> Under the "virtual print fee" model, a third party equipment integrator obtains financing, pays upfront for the digital equipment and installs it in the cinemas. The film distributors pay the integrator a fee every time a digital film is shown in the cinema, which goes towards the recoupment of the equipment cost. On the other hand, cinema exhibitors make an upfront payment to the integrator. The virtual print fee covers majority of the costs. URL: [http://europa.eu/rapid/press-release\\_IP-11-257\\_en.htm](http://europa.eu/rapid/press-release_IP-11-257_en.htm).

<sup>8</sup> European Commission, *Commission closes probe into Hollywood studio after they change terms of contracts for digitisation of European Cinemas*, 4 Mar 2011. URL: [http://europa.eu/rapid/press-release\\_IP-11-257\\_en.htm](http://europa.eu/rapid/press-release_IP-11-257_en.htm).

managed care plans at fees that were below that for Delta Dental and these plans were unable to enter and compete in the market for dental insurance (details of failed entry are provided in the Competition Impact Statement). The across-buyer MFN clauses implemented by Delta Dental protected Delta Dental from competition from such lower-cost plans.<sup>9</sup>

13. In arriving at its conclusion in the Delta Dental case, it was noted that the widespread usage of MFN clauses may amplify such foreclosure effects as it enables a seller to increase its price with lowered risk that the buyer may turn to other sellers. The DOJ pointed out that the across-buyers MFN clause contained within the contracts between Delta Dental and 90 percent of Rhode Island dentists had “eliminated most discounting by dentists below Delta’s fees... and set a floor on dental fees, thus raising the costs of dental services and dental insurance to Rhode Island consumers”.<sup>10</sup>

14. In considering the facts surrounding these three cases, there appears to be two key factors that may amplify foreclosure effects arising from the use of across-buyers MFN clauses. First, foreclosure effects may be amplified if a large proportion of the sellers are constrained by the MFN clauses as new entrant has few options to turn to. This was the case in both Delta Dental and the Digitisation of European Cinemas case. While in the Blue Cross case, it was noted that important hospitals (i.e. at least one significant hospital in each local market) were constrained by the MFN clauses in their contracts with Blue Cross. This raises the question as to whether there is a need to consider the significance of seller and whether the inputs from the sellers are essential for the buyers to provide its product/services. Second, foreclosure effects may also be amplified if many buyers engage MFN clauses in their contracts with the sellers. With more MFN clauses among the buyers, it may be harder for a new entrant to overcome the price restraints and to adopt a differentiated and/or low cost strategy to enter the market. This was evidenced in the Digitisation of European Cinemas case. Lastly, regulators have highlighted various instances of failed entry as a key evidence of the foreclosure effects in both the Blue Cross case and the Delta Dental case.

#### *Facilitating and sustaining collusion*

15. Existing literature on across-buyers MFN clauses has argued that such clauses may facilitate and sustain collusion in the sellers’ market. In such instances, across-buyers MFN clauses may be offered and initiated by the sellers. Baker (1995) argued that starting from a collusive equilibrium, the across-buyers MFN clauses reduce the seller’s incentive to deviate from a coordinated horizontal arrangement as it is unable to limit its discounts to only one buyer and has to offer the same/more discount to buyers protected by the across-buyers MFN clauses. Further, a buyer would have less incentive to bargain for more discounts, knowing that the same discounts will be extended to its competitors who are protected by the across-buyers MFN clauses and it will not have any competitive advantage over them. These effects diminish a buyer’s response to an increase in price and hence stabilises the collusive equilibrium among the sellers.<sup>11</sup>

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<sup>9</sup> The United States Department of Justice, *United States of America v. Delta Dental of Rhode Island*. Civil Action No. 96-113P, 19 Feb 1997. URL: <http://www.justice.gov/atr/cases/f1000/1074.htm>.

<sup>10</sup> *Ibid.*

<sup>11</sup> Jonathan B. Baker, “Vertical Restraints with Horizontal Consequences: Competitive Effects of Most-Favored-Customer Clauses”, *Antitrust Law Journal*, Vol. 64, No. 3, Spring 1996, pp. 517 - 534.



## Ethyl

16. These facilitating coordinated effects were one of the objections of the Federal Trade Commission (“FTC”)’s Ethyl litigation, and the DOJ’s consent order prohibiting anti-competitive practices in the electrical equipment industry. In the Ethyl case, FTC alleged that two of the four producers of antiknock gasoline additives, which together controlled 71 percent of the market, had used MFN clauses to reduce uncertainty about competitors’ prices and incentives to discount, thereby facilitating the maintenance of substantial, uniform price levels and the reduction or elimination of price competition.<sup>12</sup> However, the courts concluded that there was no evidence to suggest that Ethyl or Du Pont had adopted the MFN clauses for the purpose of influencing the price discounting policies of other producers or to facilitate their adoption or adherence to uniform prices. In considering the case, the courts also noted that the competitors of Ethyl and Du Pont made limited/no use of such MFN clauses in their contracts with customers. Further, regardless of the practices, competitors learned of each other’s prices anyway within hours and that most of the significant competition within the industry occurred on non-price terms.<sup>13</sup>

### Efficiencies that may arise from the use of across-buyers MFN clauses

17. The use of across-buyers MFN clauses may give rise to potential efficiencies such as reducing search costs for buyers and negotiation costs for both buyers and sellers; avoiding hold-up of investments; providing flexibility in long term contracts; avoiding price discrimination between customers; and signalling the quality of the seller’s products.

#### *Reduce negotiation costs*

18. A clear benefit of utilising across-buyers MFN clause is that it reduces the frequency and costs of negotiations for both the buyer and the seller as the price of the contract is automatically reviewed vis-à-vis the prices offered by the seller to other buyers.<sup>14</sup>

#### *Avoid potential investment hold-up*

19. Across-buyers MFN clauses may also be used to avoid potential hold-up in investment. For projects that may require relationship-specific investments, buyers may be unwilling to commit itself to such an investment for fear of subsequent opportunistic and exploitative behaviour of the seller. In such a case, across-buyers MFN clauses would commit the seller ex-ante not to expropriate the buyer’s investments and to provide similar/better price to the buyer vis-à-vis other buyers. Hence, in certain scenarios, across-buyers MFN clauses may solve the hold-up problem and facilitates new investment and innovation in the market.<sup>15</sup> In the case of the digitisation of European Cinemas, the EC acknowledged that the contracts between the major Hollywood film Studios and the third party integrators provided incentives to roll out digital projection equipment in European

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<sup>12</sup> E.I. du Pont de Nemours & Co. v. FTC (Ethyl) 729 F.2d (2d Cir. 1984).

<sup>13</sup> *Ibid.*

<sup>14</sup> Martha Samuelson, Nikita Piankov and Brian Ellman, “Assessing the effects of Most-Favored Nation Clauses” ABA Section of Antitrust Law, Spring Meeting 2012. URL: [http://www.analysisgroup.com/uploadedfiles/publishing/articles/samuelson\\_mfn\\_springaba\\_2012.pdf](http://www.analysisgroup.com/uploadedfiles/publishing/articles/samuelson_mfn_springaba_2012.pdf)

<sup>15</sup> Victor P. Goldberg and John R. Erickson, “Quantity and price adjustment in long-term contracts: A case study of petroleum coke”, Journal of Law and Economics, Vol. 30, No. 2 (Oct, 1987), pp. 369 – 398.

cinemas.<sup>16</sup>

### *Reduce price rigidity in long-term contracts*

20. The inclusion of across-buyers MFN clauses in long-term contracts may reduce the price rigidity in such contracts. It enables prices to be linked to current demand and supply conditions in the market and provides the contractual parties with more precise indicators for their production and consumption decisions.<sup>17</sup>

### *Guarantee against price discrimination*

21. The use of across-buyer MFN clauses may act as a guarantee against price discrimination between different buyers who compete with each other. This was pointed out in the Ethyl case where Ethyl and Du Pont argued that it had adopted the across-buyer MFN clauses as a guarantee against price discrimination between its own customers. This assured the smaller refiners that they would not be placed at a competitive disadvantage on account of price discounts given to larger buyers such as Standard Oil, Texaco and Gulf.<sup>18</sup>

### *Signal of quality*

22. As an extension of using price as a signal of quality, the sellers may also use across-buyers MFN clauses to guarantee that the goods are of high quality. By offering a retroactive across-buyers MFN clause, a high-quality seller will be able to commit that the good will maintain its quality in the future. On the other hand, a low-quality seller will not undertake such a MFN clause as it wants to retain the ability to reduce its prices in the future and it cannot afford the cost from the “penalty” associated with the retroactive MFN clauses (i.e. compensating the difference between what they paid and the lowered prices to buyers in the earlier period).<sup>19</sup>

### *Retail price MFN clauses: Price on mine no higher than on yours/others*

23. Increasingly, we are seeing the use of retail price MFN clauses in contracts for products sold through internet online platforms. Unlike the across-buyers MFN clause, retail price MFN clauses constrain, not the prices between the platform and the seller, but the seller’s retail prices to consumers, who are third parties in the agreement between the platform and the seller. For example, a retail price MFN clause may require the sellers to price the products no higher than the price set on other platforms. As they are primarily implemented between retail platforms and its sellers, this form of retail price MFN clause

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<sup>16</sup> European Commission, *Commission closes probe into Hollywood studio after they change terms of contracts for digitisation of European Cinemas*, 4 Mar 2011. URL: [http://europa.eu/rapid/press-release\\_IP-11-257\\_en.htm](http://europa.eu/rapid/press-release_IP-11-257_en.htm).

<sup>17</sup> Leslie M. Marx and Greg Shaffer, “*Opportunism and Menus of Two-part Tariffs*”, *International Journal of Industrial Organisation*, Vol. 22, Issue 10, Dec 2004, pp. 1399 – 1414.

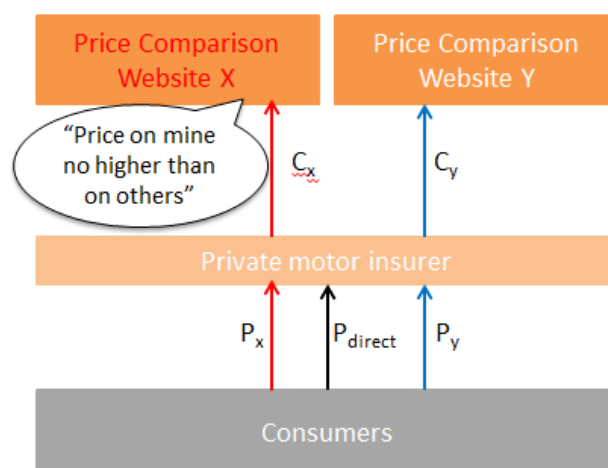
<sup>18</sup> *E.I. du Pont de Nemours & Co. v. FTC (Ethyl)* 729 F.2d (2d Cir. 1984).

<sup>19</sup> DOJ/FTC Workshop on Most-Favored Nations Clauses and Antitrust Enforcement and Policy, “*Efficiencies from MFNs: Economic Theories*”, Judith A. Chevalier, 10 Sep 2012. URL: <http://www.justice.gov/atr/public/workshops/mfn/>. See also LEAR Report, “*Can ‘Fair’ Prices be Unfair? A Review of Price Relationship Agreements*”, Sep 2012. URL: [http://www.learlab.com/pdf/oft1438\\_1347291420.pdf](http://www.learlab.com/pdf/oft1438_1347291420.pdf).

may be termed as an “across-platforms parity agreement” or “across-platforms MFN agreement”.<sup>20</sup> In the recently concluded market investigation into the Private Motor Insurance (“motor insurance”) market in UK, the CMA examined the effects of such retail price MFN clauses in the market.<sup>21</sup>

24. Price comparison websites (“PCWs”) are an important distribution channel used by the private motor insurers. The private motor insurers set the prices of the motor insurance and PCWs earn a commission for motor insurance sold through their platform. Two broad categories of MFN clauses were included within the contract between the PCWs and the private motor insurers, namely wide MFN clauses and narrow MFN clauses. These are illustrated in Figure 2 below.

**Figure 2: PCW’s Retail MFN clauses**



**Notes:**

1.  $P_x$ ,  $P_{direct}$  and  $P_y$  are prices of motor insurance set by the private motor insurer on the PCW X, its own website and other PCWs respectively.
2.  $C_x$  and  $C_y$  are commission fees paid by motor insurer to PCW X and PCW Y.
3. The narrow MFN clauses require the price of the motor insurance on the PCW to be no higher than the prices on the private motor insurer’s own website, i.e.  $P_{direct} \geq P_x$ .
4. The wide MFN clauses require the price of the motor insurances on the PCW to be no higher than the prices on the private motor insurer’s own website and on other PCWs, i.e.  $P_{direct} \geq P_x$  and  $P_y \geq P_x$ . In some instances, the wide MFN clauses also included offline sales channels too.

<sup>20</sup> LEAR Report, “Can ‘Fair’ Prices be Unfair? A Review of Price Relationship Agreements”, Sep 2012. The report broadly categorised agreements between a platform and a seller which constrain the prices paid by parties who are not a party to the agreement as “across-platforms parity agreements”. URL: [http://www.learlab.com/pdf/oft1438\\_1347291420.pdf](http://www.learlab.com/pdf/oft1438_1347291420.pdf).

<sup>21</sup> Competition and Markets Authority, *Private Motor Insurance market investigation Final Report*, 24 Sep 2014. The market was defined to refer specifically to private motor insurance and thus excluded insurance of commercial and public service vehicles, and motorcycles. URL: <https://www.gov.uk/cma-cases/private-motor-insurance-market-investigation>

## Anti-competitive potential of retail price MFN clauses

25. Retail price MFN clauses may, under certain circumstances, cause exclusionary and collusive harm to competition. Under an exclusionary theory of harm, retail price MFN clauses may increase entry barriers, resulting in reduced entry and innovation; and higher commission fees and policy premiums. Under a collusive theory of harm, retail price MFN may facilitate collusion between platforms and/or sellers, resulting in a coordinated dampening of competition.

### *Exclusionary theories of harm*

#### *Private Motor Insurance market investigation*

26. In assessing the anti-competitive effects that may arise due to the MFN clauses implemented between the PCWs and private motor insurers, the CMA found that the wide MFN clauses prevented potential entrants in the PCW market from adopting a differentiated, low-premium entry strategy. They are unable to offer consumers a lower premium as long as those policies are covered by the wide MFN clauses. Covea SGAM pointed out that the difficulty of launching with a differentiated offering in the market was a key factor which deterred it from entering the PCW market.<sup>22</sup>

27. With regard to the commission fees and policy premiums, the CMA considered whether the MFN clauses, when applied together with the agency model, affected competition by increasing commission fees and policy premiums. There was information to suggest that the some PCWs wish to offer reduced commission fees in order for insurers to price their premiums lower on their platforms. But they were unable to do so in the presence of wide MFN clauses.<sup>23</sup> This implies that the commission fees and the insurance premiums would have been lower in the absence of these wide MFN clauses. Hence, the wide MFN clauses had the effect of softening competition in the PCW market as it reduces the competitive constraints faced by the PCWs, enabling it to set higher prices to insurers than it would have in the absence of the wide MFN clauses.

28. The likelihood and extent of the anti-competitive effects that may potentially arise are affected by the scope of the retail price MFN clauses and the market structure. The CMA found that the use of narrow MFN clauses, which restricted the prices of motor insurance on the private motor insurer's direct website, did not remove a significant competitive constraint on the commission fees of the PCWs. This was due to the lower acquisition cost of new customers through PCWs vis-à-vis the insurers' direct websites; and strong elements of inter-brand competition on each PCW. These factors incentivise each insurer to price their motor insurance more competitively on PCWs as compared to their own websites. As such, compared to these factors, the pricing on the motor insurers' own websites were not found to be a strong constraint on the PCWs and hence, the use of narrow MFN clauses should not give rise to anti-competitive effects in the market.<sup>24</sup>

29. In their competitive assessment of the narrow MFN clauses, the CMA also

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<sup>22</sup> *Ibid.*

<sup>23</sup> *Ibid.*

<sup>24</sup> *Ibid.*

considered the network effect that may arise from the implementation of a series of narrow MFN clauses. They found that there are only a small number of motor insurers with significant direct sales whereby a series of narrow MFN clauses would affect the constraint on commission fees to PCWs. It further noted that even in the absence of the narrow MFN clauses, insurers seeking to protect its direct sales channel would not contract with an insurer with a low-premium strategy. Hence, CMA concluded that the narrow MFN clauses were unlikely to have a network effect which impacts on competition between PCWs.<sup>25</sup>

### Hotel online booking

30. These competitive concerns were also raised by a small online travel agency, Skoosh in its complaint relating to the hotel online booking sector. It claimed that the retail price MFN clauses used by Booking.com, Expedia and the Intercontinental Hotel Group (“IHG”) affected its ability to reduce its own commission such that hotels are able to offer discounted hotel rooms via its platform. Skoosh further claimed that the retail price MFN clauses reduced its ability to establish a presence in the online hotel booking market and to compete effectively with these chains.<sup>26</sup> Under these retail price MFN clauses, a hotel agrees to provide the online travel agent (“OTA”) with access to a room reservation (for the OTA to offer to consumers) at a booking rate which is no higher than the lowest booking rate displayed by any other online distributor. This guarantees the OTA the lowest booking rate in relation to other OTAs.<sup>27</sup>

31. In its statement of objections, the United Kingdom Office of Fair Trading (“OFT”, now known as CMA) found that Booking.com and Expedia each entered into separate arrangements with IHG which restricted the online travel agent's ability to discount the price of room only hotel accommodation. It differentiated the restrictions on discounting, which include discounts funded by the OTA from their own margin or commission, from the retail price MFN clauses, which were considered as rate parity clauses across the OTAs. The OFT considered that the restrictions on discounting limited price competition between OTAs and increases barriers to entry and expansion for OTAs that may seek to increase its market share by offering discounts to consumers. On 31 January 2014, the OFT accepted commitments from Booking.com and Expedia and from IHG where OTAs and hotels will be free to offer discounts off headline room rates. Though OFT noted that it has not assessed MFN clauses as part of its investigation, the commitment specified that the OTA shall not enter or enforce any MFN or equivalent clauses in respect of reductions off headline room rates offered by the hotels to their members in order to ensure that the commitments are effective.<sup>28</sup> Skyscanner appealed against the commitments and these were struck down by the Competition Appeals Tribunal in September 2014 on the basis that the OFT failed to consider Skyscanner’s objections and the possible impact on price transparency of an

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<sup>25</sup> *Ibid.*

<sup>26</sup> Dorian Harris (Director of Skoosh), “Open letter to William Baer, Arnold & Porter LLP”, 8 Aug 2012. URL: <http://dorian.skoosh.com/open-letter-to-william-baer-arnold-porter-llp/>

<sup>27</sup> Office of Fair Trading, *Hotel online booking: Decision to accept commitments to remove certain discounting restrictions for Online Travel Agents*, Jan 2014. URL: [http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.oft.gov.uk/shared\\_of/ca-and-cartels/oft1514dec.pdf](http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.oft.gov.uk/shared_of/ca-and-cartels/oft1514dec.pdf)

<sup>28</sup> *Ibid.*

obvious and clear restriction on disclosure of price information.<sup>29</sup>

### *Collusive theories of harm*

32. Retail price MFN clauses may also have the potential to facilitate collusion between sellers. The report by LEAR for the OFT published in 2012 (“LEAR report”) pointed out that such clauses may reduce the variety of prices offered by sellers and improves the sellers’ ability to monitor each other’s prices. This consequently reduces the cost of enforcing a horizontal agreement.<sup>30</sup>

#### *E-Books*

33. In its decision of the E-Books case, the EC considered that the retail price MFN clauses between the major publishers<sup>31</sup> and Apple, together with the agency model, acted as a “joint commitment device”. This created strong incentives for each of the publisher to convert other retailers, such as Amazon, to the agency model with the same key terms. Consequently, this facilitated the joint switch for the sale of e-books from a wholesale model to an agency model with the same key pricing terms on a global basis. The EC was of the view that this amounted to a concerted practice between the five publishers and Apple. In the final commitments accepted by the EC, the publishers and Apple have agreed to restraints which included a ban on retail price MFN clauses.<sup>32</sup>

#### *Flight Centre*

34. In the judgement handed down on 6 December 2013, the Australian courts found that the retail price MFN clauses in the six contracts between Flight Centre Limited (“Flight Centre”) and international airlines, namely Singapore Airlines, Malaysia Airlines and Emirates, gave rise to anti-competitive effect as the intention of these clauses was to eliminate differences in air fares of the same airline so as to maintain Flight Centre’s margins in each of those six occasions. In arriving at its decision, the courts considered that Flight Centre, a travel agent, competes with international airlines for the retail or distribution margin on the sale of international air fares as their services are considered substitutable by the consumers.<sup>33</sup> This was subsequently appealed by Flight Centre and on 31 July 2015, the Full Federal Court of Australia allowed Flight Centre’s appeal. The Full Court found that there was no separate market for booking and distribution services to consumers, and consequently Flight Centre and the airlines did not compete with each other in such a market. Instead the Full Court was of the view that the supply of booking

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<sup>29</sup> Competition Appeal Tribunal, *Skyscanner Limited supported by Skoosh International Ltd v Competition and Markets Authority supported by Booking.com B.V., Expedia Inc. and Intercontinental Hotels Group PLC*, Judgement. Case No: 1226/2/12/14, 26 Sep 2014. URL: <http://www.catribunal.org.uk/237-8431/1226-2-12-14-Skyscanner-Limited.html>

<sup>30</sup> LEAR Report, “Can ‘Fair’ Prices be Unfair? A Review of Price Relationship Agreements”, Sep 2012. URL: [http://www.learlab.com/pdf/oft1438\\_1347291420.pdf](http://www.learlab.com/pdf/oft1438_1347291420.pdf).

<sup>31</sup> The major publishers are Hachette, Harper Collins, Holtzbrinck/Macmillan, Simon Schuster and Penguin.

<sup>32</sup> European Commission, *Summary Decision dated 12 Dec 2012 and 25 Jul 2013 – Case COMP/39/847 – E-Books*. URL: [http://ec.europa.eu/competition/elojade/isef/case\\_details.cfm?proc\\_code=1\\_39847](http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=1_39847)

<sup>33</sup> Federal Court of Australia, *Australian Competition and Consumer Commission v Flight Centre Limited (No 2)* [2013] FCA 1313, 6 Dec 2013. URL: <http://www.judgments.fedcourt.gov.au/judgments/Judgments/fca/single/2013/2013fca1313>



and distribution services was an ancillary part of the supply of international passenger air travel, in which Flight Centre acted as an agent for the airlines.<sup>34</sup>

### Benefits that may arise from the use of retail price MFN clauses

35. Pro-competitive benefits to consumers arising from the use of retail price MFN clauses may materialise in the form of brand protection and enhanced value of the intermediary/platform, and protecting the investments made by platform owners.

#### *Brand protection*

36. Brand reputation is an important factor for intermediary/platforms as they seek to attract demands from two groups of customers to transact via the platform. Taking the example of a payment card network, a payment brand may be damaged if merchants charge different fees to customers based on their choice of payment brands at the point of sale. The unpredictable terms may reduce customers' confidence in the payment brand. In this case, retail price MFN clauses help to ensure the consistent treatment across the customer's choice of payment cards and this helps to maintain the integrity of the platform.<sup>35</sup>

#### *Protection of investments against free riding*

37. Retail price MFN clauses may help a high cost/high quality platform to protect its investments by preventing free-riding by other platforms. For example, a high quality platform may provide a range of pre-sale services (for free) to attract customers. However in the absence of retail price MFN clauses, customers may utilise these free pre-sale services to research on their products and transact on a low quality/low cost platform. Hence, retail price MFN prevents free-riding by low quality/low cost platforms by preventing these platforms from selling at lower prices.<sup>36</sup> This may then encourage platforms to innovate and invest in these additional services. Consequently, this may also encourage more inter-brand competition between sellers through these platforms.

#### *Private Motor Insurance market investigation*

38. In the market investigation into the motor insurance industry, the CMA found that the narrow MFN clauses were required to ensure the credibility of the PCWs and to reduce insurers from free-riding on the advertising provided by the PCWs. This provided the assurance to consumers that PCWs are comparing accurate prices among the various motor insurances. In doing so, PCWs assisted in reducing search costs for consumers, which enhanced competition between insurers and increased customer price sensitivity. In view of the benefits arising from narrow MFN clauses, it was assessed that the wide MFN clauses did not give rise to any pro-competitive benefits, over and above the narrow MFN clauses.

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<sup>34</sup> Federal Court of Australia, *Flight Centre Limited v Australian Competition and Consumer Commission* (2015) FCAFC 104. URL: <http://www.judgments.fedcourt.gov.au/judgments/Judgments/fca/full/2015/2015fcafc0104>

<sup>35</sup> Martha Samuelson, Nikita Piankov and Brian Ellman, "Assessing the effects of Most-Favored Nation Clauses" ABA Section of Antitrust Law, Spring Meeting 2012. URL: [http://www.analysisgroup.com/uploadedfiles/publishing/articles/samuelson\\_mfn\\_springaba\\_2012.pdf](http://www.analysisgroup.com/uploadedfiles/publishing/articles/samuelson_mfn_springaba_2012.pdf)

<sup>36</sup> LEAR Report, "Can 'Fair' Prices be Unfair? A Review of Price Relationship Agreements", Sep 2012. URL: [http://www.learlab.com/pdf/oft1438\\_1347291420.pdf](http://www.learlab.com/pdf/oft1438_1347291420.pdf).

As such, by weighing the anti-competitive effects against the pro-competitive benefits, the CMA assessed that an adverse effect on competition arises from wide MFN clauses, but not from narrow MFN clauses. CMA then imposed a prohibition on wide MFN clauses and 'equivalent behaviours' between PCWs and private motor insurers.<sup>37</sup>

### HRS

39. Similar wide retail price MFN clauses were also observed in the online hotel portal market in Germany. In this case, it was assessed that the MFN clauses used by HRS, an online hotel portal, gave rise to exclusionary effects and restricted competition between hotel portals. However, in contrast with the consumer behaviour found in UK, the German Federal Cartel Office found the risk of possible free-riding by the hotels (customer comparing information through the hotel portal, but making the booking through the hotel's website) to be insignificant.<sup>38</sup> This difference in consumer behaviour may explain why CMA considered a narrow form of MFN clauses to be necessary for PCWs in the motor insurance market in UK, while the German Federal Cartel Office did not consider such MFN clauses to be essential for the online hotel portal market in Germany.

### Assessment of MFN clauses under the Singapore framework

40. Section 34 of the Competition Act (Cap. 50B) ("the Act") prohibits agreements, decisions and practices which prevent, restrict or distort competition. Insofar as MFN clauses are agreements entered into between two or more undertaking<sup>39</sup> each of which operate at different level of the production or distribution chain, they are likely to fall within the definition of 'vertical agreements' which are excluded from section 34 prohibition by way of the Third Schedule to the Act. That being said, in the scenario where the MFN clauses are part of a network of agreements to facilitate horizontal collusion, the MFN clauses may be considered as having object the prevention, restriction or distortion of competition and may still be caught under the section 34 prohibition.

41. In a context of dominance, a MFN clause may be caught under section 47 of the Act if it gives rise to foreclosure effects in the markets and raises barriers to entry. Hence, to the extent that these MFN clauses are used to maintain or reinforce dominant market position through such exclusionary effects, they may constitute an abuse of a dominant position under the Act.

42. In assessing whether the section 47 prohibition applies, one has to determine firstly whether an undertaking is dominant in a relevant market, either in Singapore or elsewhere. For this purpose, market share figures of an undertaking is an important factor in assessing dominance, though on its own, it does not determine whether an undertaking is

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<sup>37</sup> Competition and Markets Authority, *Private Motor Insurance market investigation Final Report*, 24 Sep 2014. URL: <https://www.gov.uk/cma-cases/private-motor-insurance-market-investigation>

<sup>38</sup> Mondaq, "Germany: German Federal Cartel Office prohibits hotel portal HRS from using parity clauses", 17 Apr 2014. URL: <http://www.mondaq.com/x/307812/Antitrust+Competition/German+Federal+Cartel+Office+Prohibits+Hotel+Portal+HRS+From+Using+Parity+Clauses>

<sup>39</sup>"Undertaking" means any person, being an individual, a body corporate, an unincorporated body of persons or any other entity, capable of carrying on commercial or economic activities relating to goods or services.



dominant.<sup>40</sup> However evaluating the market share figures of the contracting parties to the MFN clauses may not be a good indicator of the full extent of the effects arising from the use of MFN clauses. Due to the price reference nature of the MFN clauses, an MFN clause may constrain the prices offered to competitors or the prices to consumers. In certain circumstances, the market share of an undertaking may not cross the dominance threshold even when the MFN clauses result in appreciable effects on the behaviour of other firms. This was also highlighted by the CMA in its market investigation into motor insurance market, where it noted that a wide MFN has a large market influence and that “one wide MFN with a single PCW would continue to constrain policy pricing on all PCWs.”<sup>41</sup>

43. Hence, except in cases where MFN clauses are a guise for horizontal agreements, the assessment of these MFN clauses, both the basic form and the retail price MFN clauses, are typically taken under an effects-based approach. Hence, any anti-competitive effects will be weighed against pro-competitive benefits that may arise from the use of these MFN clauses. The occurrence and extent of these effects will depend on factors such as, amongst others, market structure, the form of the MFN clause used and the industry usage of such MFN clauses. This requires a case-by-case analysis of the facts and circumstances. The presence or absence of any single characteristic or even a set of characteristics does not mean that an MFN clause is high-risk, but rather that a closer analysis is required before reaching a final conclusion.

## Summary

44. The above cases show that MFN clauses have the potential to give rise to pro-competitive benefits as well as anti-competitive effects on the market. The extent of the potential harm and/or benefit on the market depend on factors including the market structure, the form of the MFN clause used, and the characteristics of the sellers and buyers in the market.

45. Under the Singapore legislative framework, in view of the vertical exclusion, MFN clauses may be caught under the section 34 prohibition if it is a guise for horizontal agreements which gives rise to anti-competitive effects or have as their object the prevention, restriction and distortion of competition in the market. In a context of dominance, MFN clauses may be caught under the section 47 prohibition to the extent it is used to maintain or reinforce dominant market position through exclusionary effects. However in such cases, it is noted that market share figures may not necessarily be a good indicator of the full extent of the effects, as the MFN clause would affect the behaviours of other firms. The assessment of such MFN clauses requires a case-by-case analysis, looking at the facts and the circumstances surrounding the use of MFN clauses.

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<sup>40</sup> CCS, *CCS Guidelines on the Section 47 Prohibition*, paragraph 3.5

<sup>41</sup> Competition and Markets Authority, *Private Motor Insurance market investigation Final Report*, 24 Sep 2014. Paragraph 8.29 of the report. URL: <https://www.gov.uk/cma-cases/private-motor-insurance-market-investigation>