

On the economic effects of price parity clauses - what do we know three years later?¹

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Key Points

- The period 2015-17 was characterised in the EU by important antitrust decisions regarding the use of price parity clauses by online travel agencies (OTAs).
- National competition authorities (NCAs) across the EU reached different resolutions, thus providing an opportunity for comparative analysis.
- We gather recent empirical studies on the removal of parity clauses and provide evidence on the dynamics of hotel prices posted on Booking.com in France, Italy, and Spain.
- We argue that antitrust enforcement against price parities increased competition in the OTA sector, rendered the contractual relations with hotels more transparent, and incentivised OTAs to improve their services.

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1. Introduction

Price parity clauses, also known as most favoured nations (MFN) provisions, are contractual terms used by online platforms to prevent client sellers from offering their products or services at cheaper prices on alternative sales channels. They are widespread in industries such as entertainment, insurance, energy supply, digital goods, and payment systems. Competition authorities around the world are increasingly concerned about the anticompetitive effects of these clauses, especially in markets dominated by few players. In the past years, EU national competition authorities (NCAs) have reached important decisions on parity clauses adopted by leading online travel agencies (OTAs) such as Booking.com and Expedia. Tourist accommodation in 2014 was booked online for 55% of the trips made by EU residents.² The majority of these online sales took place through OTAs, with Booking.com controlling almost 60% of the market.³ The use of price parity clauses by dominant OTAs such as Booking.com was then considered as a relevant issue to be addressed.

The OTA sector is usually characterised by an "agency" model. Hotels decide the final price on the OTA, which charges a commission rate when the room is booked through its platform. This business model may seem innocuous in terms of competition concerns, as the hotel simply pays a fee for the service provided by the OTA. However, the adoption of parity clauses within an agency model may result in anticompetitive effects, especially when these clauses are particularly restrictive. Price parity clauses imposed on hotels are usually of two types. A "wide" parity clause forces the client hotel to charge the lowest price on the contracted OTA, whereas a "narrow" parity clause allows the hotel to set a lower price when selling through other OTAs. In both cases, the hotel is bound not to charge a lower price through its direct sales channel. The "theory of harm" relies upon the fact that these clauses, especially in their "wide" version, stifle competition between OTAs.⁴ This increases the commission rate paid by client hotels, which would in turn raise final prices. The "narrow" version has been viewed as a compromise between increasing competition in this sector and rewarding OTAs for their service. In absence of any form of price parity, consumers would simply consult OTAs to compare prices, and then book through direct channels if these offered better deals.⁵ There are, however, many criticisms towards the use of narrow price parities, as they also raise concerns in terms of restricting competition in the OTA sector.⁶

On the basis of this "theory of harm", a number of NCAs across the EU decided to intervene. Following an investigation opened in June 2014, the French, Italian and Swedish NCAs accepted in

² http://ec.europa.eu/eurostat/statistics-explained/index.php/Statistics_on_ICT_use_in_tourism, accessed 23 December 2017.

³ HOTREC 2015-16 Annual Report, available at: <http://www.hotrec.eu/cust/documentrequest.aspx?DocID=4995>, accessed 28 December 2017.

⁴ Jonathan B. Baker & Fiona Scott Morton, 'Antitrust Enforcement Against Platform MFNs', *Yale Law Journal*, 2018, *forthcoming*. They explain how price parity clauses adopted by online platforms can harm competition by keeping prices high and discouraging the entry of new platform rivals.

⁵ Chengsi Wang & Julian Wright, 'Search Platforms: Showrooming and Price Parity Clauses', mimeo, 2017. Available at: <https://www.dropbox.com/s/3ur67nomzm7o72y/intermediation%20and%20search.pdf?dl=0>, accessed 20 January 2018. They introduce the concept of "showrooming", *i.e.* the potential free-riding activity of users that value the intermediation service provided by the platform, but then switch to the direct channel to obtain a discount.

⁶ Matthias Hunold, 'Best Price Clauses: What Policy as Regards Online Platforms?' *Journal of European Competition Law & Practice*, 2017, Vol. 8(2), 119-125. He reckons that narrow price parities may restrict competition between OTAs more or less in the same way as wide ones.

April 2015 the commitment by Booking.com to switch from wide to narrow price parity clauses.⁷ Booking.com decided to extend its commitment throughout the EU, starting July 1st, 2015. Expedia also committed to switch to narrow price parities by the end of 2015. France and Germany went even further. In August 2015, the French Parliament promulgated the Macron Law, according to which all price parity clauses were prohibited.⁸ The Bundeskartellamt reached a similar decision in December 2015.⁹ Finally, price parity clauses were also completely banned in Austria from January 2017 and in Italy from August 2017.¹⁰ However, comparable initiatives have not yet been carried out in other parts of the world, including the US.¹¹ It follows that the EU experience represents an interesting scenario to gauge the effects of removing price parity clauses in the OTA sector.

2. Economic Effects of the Antitrust Decisions

A growing number of theoretical and empirical papers have attempted to evaluate the economic effects of price parity clauses. Most of the theoretical contributions formalised the aforementioned “theory of harm” by showing that price parity clauses drive commission rates up, thereby increasing final prices.¹² Very recent papers have focused on OTAs, following the EU experience.¹³ They acknowledge the anticompetitive effects of price parities, but also provide some justifications for their adoption. Bjorn O. Johansen & Thibaud Vergé identify scenarios in which price parity clauses

⁷ Konkursverket, decision of April 15, 2015 – 596/2013 – Booking.com; Autorité de la concurrence, decision of April 21, 2015 – 15-D-06 – Booking.com; Autorità Garante della Concorrenza e del Mercato, decision of April 21, 2015 – I779 – Booking.com.

⁸ See Loi n° 2015-990 du 6 août 2015 pour la croissance, l’activité et l’égalité des chances économiques, article L. 311-5-1 du code de tourisme.

⁹ Bundeskartellamt, decision of December 23, 2015, B 9–121/13. Hunold 2017, *supra note* 6, explains the rationale behind Bundeskartellamt’s decision in comparison to that adopted by French, Italian and Swedish NCAs. Chiara Caccinelli & Joëlle Toledano, ‘Assessing Anticompetitive Practices in Two-Sided Markets: The Booking.com Cases’, 28th European Regional ITS Conference, 2017. Available at <https://www.econstor.eu/handle/10419/169452>, accessed 5 March 2018. They provide a detailed comparative analysis of the four competition proceedings against Booking.com.

¹⁰ HOTREC, ‘HOTREC applauds Austria and France - Ban on Parity Clauses’, press report September 7, 2016, available at: <http://www.hotrec.eu/newsroom/press-releases-1714/hotrec-applauds-austria-and-france---ban-of-parity-clauses.aspx>, accessed 5 March 2018. HOTREC, ‘Also Italy Prohibits Rate Parity Clauses of Online Booking Platforms by Law’, press report August 3, 2017, available at: <http://www.hotrec.eu/newsroom/press-releases-1714/also-italy-prohibits-rate-parity-clauses-of-online-booking-platforms-by-law.aspx>, accessed 4 January 2018.

¹¹ Baker & Scott Morton, 2017, *supra note* 4. They argue that antitrust enforcement against price parity clauses adopted by platforms such as OTAs should also be a priority in the US.

¹² Andre Boik & Kenneth S. Corts, ‘The Effects of Platform Most-Favored-Nation Clauses on Competition and Entry’, *Journal of Law and Economics*, 2016, Vol. 59, 105-134. They find that parity clauses lead to higher platform fees and retail prices; moreover, they tend to discourage entrants pursuing lower-cost business models. Justin P. Johnson, ‘The Agency Model and MFN Clauses’, *Review of Economic Studies*, 2017, Vol. 84(3), 1151-1185. He also concludes that parity clauses increase retail prices through a surge in commission rates. Benjamin Edelman & Julian Wright, ‘Price Coherence and Excessive Intermediation’, *Quarterly Journal of Economics*, 2015, Vol. 130(3), 1283-1328. They show that parity clauses lead to excessive investment in frills, harming consumers by diverting them from direct channels.

¹³ Wang & Wright 2016, *supra note* 5. The authors acknowledge the intermediation service offered by OTAs, and are inclined to allow narrow price parities clauses. Bjørn Olav Johnsen & Thibaud Vergé, ‘Platform Parity Clauses with Direct Sales’, 2017, University of Bergen Department of Economics, Working Paper No. 1/17 2017. Available at http://www.uib.no/sites/w3.uib.no/files/attachments/working_paper_01-17_revidert.pdf, accessed 20 January 2018. They argue that OTAs may refrain from charging excessive commission rates if hotels are given the option to delist.

benefit not only OTAs, but also consumers and hotels.¹⁴ This occurs when the degree of competition between hotels is particularly fierce.

Empirical contributions may prove even more relevant, as there is scope for a comparative analysis of different national regimes. As we highlighted in the previous section, the intervention against price parity clauses in the EU has not only intensified in the past three years, but has also been carried out differently across member states. In particular, the initial shift from wide to narrow parities was followed by a total ban of parity clauses but only in some EU states. Table 1 summarises the main decisions discussed in Section 1 and their implications in terms of price parity regimes.

Table 1. Main decisions on price parity clauses and resulting regimes in the EU.

| Date | Event | Regime |
|---------------|--|------------------------------|
| April 2015 | Booking.com's commitment accepted | Wide price parities |
| July 2015 | The commitment comes into force | Narrow price parities |
| August 2015 | Law Macron promulgated | No price parities in France |
| February 2016 | Bundeskartellamt's decision comes into force | No price parities in Germany |
| January 2017 | Austrian bill comes into force | No price parities in Austria |
| August 2017 | Italian competition bill comes into force | No price parities in Italy |

It would therefore be possible to investigate not only whether these interventions at large have led to substantial results, but also which one was more effective. However, empirical studies may face difficulty in obtaining reliable data. In 2015, the EU commissioned a report to evaluate the effect of the removal of price parity clauses.¹⁵ The analysis was based upon data collected from OTAs combined with a survey filled out by hotel owners, focusing on the period before and after the switch from wide to narrow parity clauses. The report showed no clear evidence that commission rates had lowered between July 2015 and June 2016, nor that hotels charged different prices across their sales channels. However, the results were not conclusive and called for further enquiry. In particular, the percentage of hotels responding to the survey was not very high.

Importantly, recent research has tried to overcome the dearth of data in order to shed some light on this complex issue. Matthias Hunold, Reinhold Kesler, Ulrich Laitenberger & Frank Schlütter gathered data of more than 30,000 hotels in Kayak.com from January 2016 until January 2017.¹⁶ They focused on the full ban of price parity clauses, showing that it induced hotels to increase their use of Booking.com not only in Germany, but also in France and Austria. Interestingly, they also found that the ban encouraged hotels to charge the lowest price on the direct channel. This was particularly evident in Germany. Sean Ennis, Marc Ivaldi & Vicente Lagos used a dataset of proprietary hotel-level data for 2014 and 2016, for different hotels both in the EU and around the world.¹⁷ Their evidence suggests that the switch from wide to narrow price parities caused a price

¹⁴ Johansen & Vergé 2017, *supra note* 13.

¹⁵ European Commission and the Belgian, Czech, French, German, Hungarian, Irish, Italian, Dutch, Swedish and UK NCAs, 'Report on the monitoring exercise carried out in the online hotel booking sector by the EU competition authorities in 2016', April 2017, available at: http://ec.europa.eu/competition/ecn/hotel_monitoring_report_en.pdf, accessed 28 December 2017.

¹⁶ Matthias Hunold, Reinhold Kesler, Ulrich Laitenberger, Frank Schlütter, 'Evaluation of Best Price Clauses in Hotel Booking', 2017, ZEW Centre for European Economic Research Discussion Paper No. 16-066, available at: <http://ftp.zew.de/pub/zew-docs/dp/dp16066.pdf>, accessed 6 March 2018.

¹⁷ Sean Ennis, Marc Ivaldi & Vicente Lagos, 'Price-Parity-Clauses on Hotel Room Booking: Empirical Evidence from Industry Data', in progress.

decrease on direct channels with respect to OTAs in the EU, especially for more expensive hotels. Arthur Cazaubiel, Morgane Cure, Bjørn Olav Johansen & Thibaud Vergé obtained a unique dataset from two major hotel chains in Scandinavia containing prices, volumes and sales channels between 2012 and 2016.¹⁸ This ongoing study aims to estimate the degree of substitution between Booking.com and Expedia, and hotels' own websites, by considering a boycott against Expedia headed by hotels between 2012 and 2014. This could provide an indirect measure of the potential anticompetitive effect of price parity clauses. Preliminary evidence shows that most consumers remained loyal to Expedia during the boycott.

Our own investigation both differs and complements the empirical analysis carried out in the previous papers.¹⁹ We collected data of listed prices on Booking.com in the period 2014-16 for tourism regions in the Mediterranean that belong to three EU countries: France, Italy, and Spain.²⁰ Hence, our dataset allowed us to compare prices on Booking.com before and after the most relevant EU antitrust decisions. In addition, as the three countries differed in their commitment against price parity clauses, we can consider both the shift from wide to narrow and then from narrow to no price parities at all. As previously introduced, France and Italy actively enquired on the case, whereas Spain adopted a 'wait-and-see' approach. Moreover, France abolished all types of parity clauses in August 2015. We matched rooms with similar characteristics and compared prices at a one-year distance by considering the exact booking day. For a tourist searching for a room 10 days before the third Saturday of September, for instance, we compared room prices retrieved on the following dates: September 10, 2014; September 9, 2015; September 7, 2016.²¹

Table 2. The price of a double room in our sample in the period 2014-16 (in euros).

| | France | Italy | Spain |
|--------------|--------|---------|---------|
| 2014 | 120 | 104 | 119 |
| 2015 | 113 | 100 | 118 |
| 2016 | 118 | 112 | 141 |
| Observations | 74,375 | 202,336 | 113,938 |

The results of our empirical analysis, briefly summarised in Table 2, revealed a significant price drop between 2014 and 2015, followed by a price increase between 2015 and 2016.²² At country level, France and Italy experienced a more pronounced price decrease in the period 2014-15, and a less intense price surge in 2015-16. Although many interpretations are plausible, we hold that the price reduction observed in 2015 with respect to the previous year was mainly due to the antitrust

¹⁸ Arthur Cazaubiel, Morgane Cure, Bjørn Olav Johansen & Thibaud Vergé, 'Substitution between Online Distribution Channels: An Empirical Evaluation on the Scandinavian Hotel Industry', in progress.

¹⁹ Andrea Mantovani, Claudio Piga & Carlo Reggiani, 'The Dynamics of Online Hotel Prices and the EU Booking.com Case', 2017, NET Institute Working Paper No. 17-04. Available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3049339, accessed 20 February 2018.

²⁰ The data refer to Sardinia and Sicily (Italy), Balearic Islands (Spain) and Corsica (France), which represent comparable alternatives for tourists. They were retrieved using a "web crawler" which automatically connected to Booking.com and launched queries in all the hotels available in the above regions. The "crawler" then saved information about the prices together with the characteristics of the rooms. It also retrieved data on the characteristics of the hotels (e.g. number of rooms, star rating, reviews).

²¹ Keep in mind that 2016 was a leap year.

²² Table 2 presents descriptive evidence on the average price of a double room in our matched sample. In our paper, we provide a more precise regression analysis on the dynamics of hotel prices, controlling for changes in individual room characteristics (e.g. sea view, breakfast included), hotel characteristics, and proxies of tourist flows and town level hotel occupancy rates. Moreover, we perform a diff-in-diff analysis to assess the impact of the main antitrust events.

investigations, which induced Booking.com to eliminate wide parity clauses. This should bolster competition in the OTA sector, thus reducing commission rates and, in turn, the final hotel prices. Country patterns are also in line with the intensity of the antitrust activity, given that France and Italy experienced more significant price reductions than Spain. Although parity clauses were (partially or totally) banned in 2016, prices bounced back with respect to 2015. This, however, does not mean that the decisions against Booking.com were ineffective. Rather, we argue that these measures contributed to limit potential price surges that could have resulted from the demand boom. The North African turmoil, which reached its peak in Tunisia and Egypt between 2015 and 2016, dramatically impacted tourism flows, especially in 2016.²³ Indeed, the regions that we consider highly benefited from the redirection of tourists from North African beach resorts to the Mediterranean islands of Italy, France, and especially Spain. However, also for this second period, the country pattern may reflect the intensity of the antitrust actions, as the price increase was less prominent in proactive countries such as France and Italy. In particular, France is the only country where prices did not return to 2014 levels, notwithstanding the demand boost (see again Table 2). To sum up, our results seem to highlight a beneficial effect of the EU antitrust intervention for hotel guests. On the one hand, the removal of price parities contributed to the observed reduction of prices listed on Booking.com between 2014 and 2015, proportional to the intensity of a country's antitrust engagement. On the other hand, this removal may have limited the price increase that took place between 2015 and 2016, mainly driven by enhanced demand.

3. The Response of Booking.com

In April 2015, Booking.com introduced the BookingSuite system, which helps independent hotels to build innovative and user-friendly websites. It may of course be a coincidence that this system was launched the same month in which Booking.com committed to eliminating wide price parities in France, Italy, and Sweden. However, it is undisputed that, between 2015 and 2016, leading OTAs, Booking.com *in primis*, enhanced the quality of the service they provide to both client hotels and final customers. On the one hand, Booking.com improved the layout of its website and added complementary features for travellers. For example, starting from summer 2015, Booking.com increased its presence on social media.²⁴ Between February and July 2016, it personalised some of its offers and ameliorated the way guests communicated with hotels.²⁵ In July 2016, it introduced the Booking Experiences Tool, through which users can browse a full list of things to do in the selected destination and book tickets in advance. On the other hand, it expanded its support to client hotels. In March 2016, the RateManager platform was introduced to suggest optimal room prices depending on a number of factors, such as expected demand, weather forecast, special events, and so on. An important online feature was also added: a hotel room was not only indicated as discounted, but Booking.com upped its game and started to include both the full price, crossed out in red, and the discounted price showing the percentage reduction that hotel guests would be saving.

²³ The Sousse attack in Tunisia on 26 June 2015, with a death toll of 38 tourists, 30 of whom were British, had a strong emotional impact. UK issued a travel ban and the number of British tourists travelling to Tunisia fell by 90% in 2016.

²⁴ In August 2015, for example, Booking.com invited tourists to share pictures of their summer travels and converted some of these pictures into animated GIFs.

²⁵ In February 2016, Booking.com introduced the PassionSearch service which helps tourists find their best suited destination. In May 2016, it launched the Booking Messages Interface, a chat tool that connects hotels and tourists.

All in all, the quality of the booking service offered by the platform appears to have been increased in the past three years along several dimensions, or though it seemed.

These innovative strategies cannot be directly linked to the NCAs' decisions explained above. However, Booking.com may have simply accelerated the introduction of such complimentary services for both travellers and client hotels, following the ban on parity clauses. This may help explain the price dynamics documented in our study for the period 2015-16, where prices bounced back.²⁶ If this interpretation is correct, eventual price increases following the decisions against price parities should not raise too much concern, as they may be driven by service improvements offered by OTAs. Nevertheless, one of these newly introduced features, namely the percentage price reduction displayed to Booking.com's users, deserves more attention. The supposedly 'original' price could be distorted upwards, based on a particularly high price available only for a brief period, for example during the weekend. Hence, one may wonder whether hotels adopting this discounting strategy actually ended up lowering the prices posted on Booking.com. Our data enabled us to delve deeper into this issue.²⁷ In particular, we found that specifically 3 and 4-star hotels using the discount feature were more likely to have raised their prices. A similar conclusion also holds for 2-star hotels in Spain and Italy. It is therefore possible that most hotels adopted this discount feature as part of a well-designed revenue management strategy that helps maintain high prices. The only exception is represented by 5-star hotels that, as common practice, use discounts to fill up available rooms.

4. Future Outlook

Price parity clauses have come under the spotlight as they are widely used by dominant OTAs, such as Booking.com and Expedia. As explained, between 2015 and 2016 important decisions were made at the EU level in order to progressively eliminate these contractual agreements. The aim was to increase competition in the OTA sector and guarantee hotels a higher flexibility in setting their prices. The recent empirical literature reported in Section 2 provides complementary results that are in line with the ultimate goal of the EU antitrust intervention. In fact, the switch from wide to narrow price parities has been associated to price reductions on direct channels²⁸, whereas the full ban on price parities increased the use of OTAs by hotels²⁹. Moreover, the progressive elimination of price parities contributed to lower prices on Booking.com, especially in 2015³⁰. However, given the current data available, these results cannot be considered as conclusive with regard to partial or full removal of price parity clauses. In particular, empirical findings on changes in the OTA commission rates before and after the antitrust decisions are scarce.

Further enquiry is also required in relation to the potential negative effect on consumers of these (often not transparent) innovative features and contractual agreements. On October 27, 2017, the Competition and Market Authority (CMA) opened an investigation in order to verify "the clarity, accuracy and presentation of information on sites, which could mislead people and stop them

²⁶ Mantovani, Piga & Reggiani, 2017, *supra* note 19.

²⁷ Mantovani, Piga & Reggiani, 2017, *supra* note 19.

²⁸ Ennis, Ivaldi & Lagos, 2017, *supra* note 17.

²⁹ Hunold, Kesler, Laitenberger & Schlutter, 2016, *supra* note 16.

³⁰ Mantovani, Piga & Reggiani, 2017, *supra* note 19.

finding the best deal”.³¹ This investigation aims at examining several practices, including not only the aforementioned discount claims, but also hotel ranking on dominant OTAs, pressure selling strategies, and hidden charges. Regarding the way hotels appear in OTA rankings, this does not come as a surprise as one of the factors affecting this ranking is the commission fees paid to the platform. Booking.com, for example, is increasingly adopting a ‘commission override’ system, whereby a hotel’s visibility on the platform is proportional to the commission fee.³² It follows that competition in the OTA sector can be stifled even in absence of price parity clauses. In fact, hotels may feel forced to pay high fees to dominant OTAs in order to appear first in searches, independently of other factors that should primarily influence consumer choice. As for pressure selling, *i.e.* techniques used to rush consumers into on-the-spot booking, and hidden charges such as unexpected fees which pop up at the very last stage of the payment process, these practices represent new areas for investigation.

³¹ <https://www.gov.uk/government/news/cma-launches-consumer-law-investigation-into-hotel-booking-sites>, accessed 11 January 2018.

³² Booking.com introduced the "Preferred" program, which consists in awarding an exclusive status to high-performing lodgings that appear towards the top of search results. One of the conditions is "to be part of the top 30% performing properties in your area. This is calculated automatically and unilaterally by Booking.com and based on and influenced by various factors, including but not limited to the commission percentage (to be) paid by the Accommodations..."; <https://partnerhelp.booking.com/hc/en-us/articles/213301825-What-is-the-Preferred-programme->, accessed 6 March 2018.