

UK Office of Fair Trading Consults on Commitments in Relation to Online Hotel Pricing

Jennifer Marsh

K & L Gates, United Kingdom

The UK Office of Fair Trading (“OFT”) announced in September 2010 that it was launching a formal investigation into suspected breaches of UK and EU competition law¹ in the hotel online booking sector. It subsequently issued a statement of objections setting out the case against the relevant parties. However, the OFT indicated on 9 August 2013 that, rather than proceeding to an infringement decision, it proposed to accept commitments from the parties to modify their behaviour.

OFT Concerns

The OFT was concerned that a major hotel group was restricting the ability of online travel agents (“OTAs”) to discount the price of room-only hotel accommodation, i.e. resale price maintenance. It considered that such practices were widespread in the industry. In the OFT’s view, the effect of such restrictions could be to:

- limit competition between OTAs and between OTAs and hotels’ own online platforms; and
- create barriers to entry by preventing new OTAs, potentially with more efficient business models than incumbents, from achieving growth through discounted sales.

Industry Context

The OFT chose to focus its investigation on one hotel group and two OTAs but with the clear intention of setting a precedent for the industry as a whole. As the OFT stated, “The OFT limited the scope of its investigation to a small number of major companies, with a view to achieving a swift and effective outcome. However, the investigation is likely to have wider implications as the alleged practices are potentially widespread in the industry.”²

One argument which it is believed that the parties sought to advance but which the OFT has not accepted is that OTAs are genuine agents of hotel chains, such that it would be appropriate for the hotels to set the OTAs’ prices. For this argument to have applied, the OFT would need to have been satisfied that the OTAs did not bear the usual commercial risks of being in business for their own account.

The OFT noted in its commitments proposal³ that it was looking at two OTA business models: firstly, the merchant model whereby the OTA supplies hotel accommo-

dation at a mark-up against the net rate paid by the OTA to the hotel and the customers pay the OTA directly when the reservation is made. Secondly, the commission-based model whereby the customer pays the hotel the booking rate at the end of their stay and the hotel then pays the OTA a pre-agreed commission. In the first case, a discounting restriction would prevent an OTA from sacrificing its margin or part of it and in the second would prevent it sacrificing its commission or part of it.

The OFT considered that “best rate guarantees” are widespread in the industry. This is where a hotel agrees to provide an OTA with a retail rate for hotel accommodation which is no less favourable than the lowest retail rate displayed by other online distribution outlets. It is effectively a guarantee to an OTA that it cannot be undercut by its competitors. The OFT has not directly considered best rate guarantees in its investigation but rather has focussed purely on resale price maintenance.

This should not necessarily be taken as a green light under UK/EU law for such “rate parity” arrangements. The OFT has indicated that it might yet investigate such clauses in other industries and, amongst other authorities, the German Federal Cartel Office is currently investigating whether such clauses in the hotel sector are anti-competitive.

Commitments Process

Under OFT guidance, the OFT must be satisfied that the commitments offered fully address its competition concerns. The primary criteria which the OFT is likely to consider in determining whether it is appropriate to accept binding commitments are whether:

- the competition concerns are readily identifiable;
- the competition concerns are fully addressed by the commitments offered; and
- the proposed commitments are capable of being implemented effectively and, if necessary, within a short period of time.⁴

Commitments Proposed

The OFT has indicated that it intends to accept the proposed commitments on the basis that they will introduce some price competition and reduce barriers to entry. Unusually however it proposes to leave some discounting restrictions in place on the basis that allowing hotels to

determine OTAs' resale rates may create efficiencies and ultimately be of some benefit to consumers. As well as consulting on the commitments themselves, the OFT requested third party views on the validity of such efficiencies arguments.

Under the terms of the proposed commitments, OTAs would be free to offer reductions off headline room rates but only to "closed groups". Membership of such groups would not be automatic, rather consumers would have to actively opt in and they would need to use passwords and have created a customer profile. Eligibility for discounted rates would also be dependent on the end-user having previously made a non-refundable, "full-price" booking with the relevant OTA. Furthermore, OTAs would not be able to publicise information regarding the specific level of discounts to non-members.

The efficiencies arguments, which the OFT considers may justify leaving in place "residual restrictions," are outlined below.

The headline rate for hotel rooms acts as an important indicator of quality for consumers and unrestricted discounting by OTAs may undermine this and damage the hotel's brand or reputation. Hotels may, as a result, be reluctant to use OTAs which would further result in a lower availability of rooms to consumers, lower inter-brand competition and raise prices and search costs.

Yield (revenue) management pricing is essential in the industry as this enables hotels to adjust room rates frequently in the window between the time at which a room becomes available to book and the occupancy date, responding to updated information on the level of demand for their rooms. As OTAs do not take any inventory risk in relation to unsold rooms (they do not have unsold stock in their store rooms which they bear the risk of not being able to sell), their incentives are not aligned with those of hotels in this respect.

Unrestricted discounting by OTAs would cannibalise sales in the hotels' direct online sales channels. As hotels do not pay commission in their direct channel, this would significantly impact the hotels' profitability and create a risk that certain hotels would refuse to deal with OTAs, deal with fewer OTAs or offer less inventory to OTAs. Consumers would then be left with fewer hotels on

OTAs, increased search costs and reduced inter-brand competition.

IF OTAs are permitted to engage in unrestricted discounting, there is a risk that "no-frills" websites could "free-ride" on investments made by other OTAs, e.g. in terms of website functionality of customer support. This may undermine the incentive for OTAs to invest in valuable services for customers.

What happens next?

Depending on the comments received during its consultation, the OFT may now proceed to accept the commitments in their current form. Alternatively, it may accept modified commitments, e.g. to address specific concerns raised during the consultation. Finally, the OFT may continue with its investigation if it decides it is not satisfied with the commitments offered to it, potentially proceeding to a finding of infringement.

In the US, a class action is ongoing in the District Court of North California,⁵ alleging that certain OTAs and hoteliers had conspired to restrict room-rate discounts and limit competition from smaller online retailers. It will be interesting to see whether the US process results in a more negative approach to online resale restrictions than the OFT process, given that it has in recent, post-*Leegin*⁶ years been assumed that a resale price maintenance argument had a greater prospect of success under EU law than in the US.

¹ Chapter I of the Competition Act 1998 and Article 101 of the Treaty on the functioning of the European Union, the prohibitions on anti-competitive agreements within the UK and between EU member states, respectively.

² www.ofi.gov.uk/news-and-updates/press/2013/59-13

³ www.ofi.gov.uk/shared_ofi/ca-and-cartels/ofi1500.pdf, paragraphs 3.17 ff.

⁴ OFT1263rev, paragraphs 10.15 - 10.16

⁵ *Turik et al*, U.S. District Court, Northern District of California, No. 12-4365. Also in the U.S. a class action is ongoing in respect of rate parity obligations - *In re: Online Travel Company Hotel Book Antitrust Litigation*, Case No. MDL-2405, U.S. District Court for the Northern District of Texas

⁶ *Leegin Creative Leather Products Inc. v. PSKS Inc.* 551 U.S. 877 (2007)