

CONSULTATION NOTICE ON THE REVISED COMMITMENTS

ANNEXE 4

SUMMARY OF RESPONSES TO THE CONSULTATION

This Annexe summarises the key issues raised in the responses received to the Consultation,¹ together with the OFT's response. The main points fell under five key headings and have been grouped accordingly for the purposes of this overview:

1. Commitments do not address rate parity and other MFN provisions directly
2. Impact on the structure of the market
3. Third party views on efficiency arguments put forward by the Parties
4. Geographic scope of the Commitments
5. Duration of the Commitments

The Consultation ran for five weeks and closed on 13 September 2013. The OFT received over thirty-five responses from a range of respondents including independent hotels, hotel chains, OTAs, industry associations and other interested third parties.

Issue 1: Commitments do not address rate parity and other MFN provisions directly

1. The majority of respondents raised concerns with rate parity and/or other MFN provisions, which were not the focus of the OFT's investigation and which, therefore, the Commitments do not address directly.
2. Hotels in particular submitted that rate parity provisions prevent them reflecting the different costs, service standards or business models of various distribution channels in different rates between channels. In addition to rate parity provisions, concerns were also raised about other (non-price) MFN/parity provisions, such as provisions requiring hotels to offer OTAs last room availability and their most favourable booking and cancellation conditions.

¹ Defined terms used herein have the same meaning as those used in the Consultation Notice on the Revised Commitments.

3. Some respondents urged the OFT to investigate issues associated with rate parity and/or other MFN provisions in close cooperation with other NCAs in the EEA and/or the European Commission in order to ensure the consistent application of European competition law in the hotel online booking sector.
4. Several respondents raised concerns about the application of rate parity provisions to hotels' own booking websites and offline channels. The respondents thought that this in turn could prevent hotels from offering equivalent discounts to those that the Commitments enable OTAs to offer to members of their closed groups (indirectly, by requiring the hotel to offer OTAs the same (discounted) rate made available via its own booking website). These respondents were therefore concerned that the Commitments could give OTAs an unfair competitive advantage in the online offering of hotel accommodation bookings to end-users.
5. Only one respondent submitted that rate parity is important for consumers to know that no matter where they book they will not get a cheaper rate for the same room.

OFT response

6. The focus of the OFT's investigation has been the current restrictions on OTAs' discounting off the Room-Only Rate set by a hotel. The OFT has not investigated MFN provisions in this case and has made no assessment of whether MFN provisions may give rise to a breach of the Chapter I prohibition and/or Article 101 TFEU.^{2,3}
7. However, to ensure that the Commitments are effective, the Parties have committed to amend, remove or not include any provisions in current and future commercial arrangements between them that could undermine the new discounting freedoms provided for by the Commitments. This could include amending any MFN provisions, if necessary. The Parties must also use reasonable endeavours to ensure that there are no provisions in their current agreements with other OTAs and hotels which would undermine the new discounting freedoms, and must not include such

²Therefore, the Parties have not had the opportunity to respond formally to comments raised by respondents on these issues.

³ See paragraphs 3.26 to 3.30 of the Consultation Notice on the Revised Commitments for further detail of the OFT's position on rate parity/ retail rate MFN provisions in this case.

provisions in any new arrangements. Again, this could include amending any MFN provisions, if necessary. In particular, MFN provisions must not be enforced in respect of either (i) the offering of discounts complying with the Principles to closed group members who have made a prior booking, or (ii) the publication of details of such discounts to members of the closed group.⁴

8. In addition, the OFT received a number of queries about the extent to which the Commitments have an impact on the ability of hotels to offer discounts to closed groups. To address these queries, the Parties have offered drafting amendments to the Commitments to clarify the ability of hotels to offer discounts to closed groups.⁵ In particular, in the Revised Commitments the Parties have clarified that OTAs shall not enter into or enforce any MFN or equivalent provisions in respect of reductions off headline room rates offered by hotels to their closed group members. This is subject to the condition that the hotel does not publicise information regarding the specific level of discounts for a particular hotel room to consumers who are not members of that closed group. This mirrors the restrictions on OTAs' advertising of hotel room discounts set out in the Commitments.

Issue 2: Impact on the structure of the market

9. Many respondents indicated that the Commitments could have an adverse impact on the structure of the market by strengthening OTAs' market positions vis-à-vis hotels; strengthening Booking.com and Expedia's market positions; and/or impacting on consumers' ability to shop around.

Commitments may strengthen OTAs' market positions vis-à-vis hotels

10. Some respondents highlighted a risk that the Commitments could lead to a shift of consumer purchasing behaviour away from hotels' own booking websites to OTAs. It was submitted that this could raise hotels' distribution costs and hotels might therefore limit their dealings with OTAs that engage in discounting or offer less inventory to those OTAs.

⁴ However, the Commitments do not affect the application of MFN provisions against discounts which are published outside of the closed group to which the discount has been offered.

⁵ See paragraphs 3.14 to 3.18 of the Consultation Notice on the Revised Commitments for further detail.

On the other hand, the OFT was also told that OTAs are already able to offer certain discounts to consumers via closed group discounting schemes and it was submitted that the proposed Commitments would not change the current position.

11. Some concern was also raised by respondents about the wider applicability of the Commitments beyond the Parties. In particular, the OFT was told that independent hotels may not be in the same bargaining position with OTAs as international hotel chains such as IHG. The OFT was told that many hotels (particularly independent hotels) feel that they have to work with OTAs in order to reach a wider customer base. Therefore, the OFT was told, OTAs (particularly the larger OTAs such as Booking.com and Expedia) are in a strong bargaining position vis-à-vis those hotels.
12. There was also a concern that the prior booking requirement might favour OTAs above hotels' own booking websites because consumers are less likely to make as many bookings on a hotel's own website as on an OTA which offers a selection of different hotels in different locations.
13. Some respondents suggested that the Commitments should ensure that OTAs would not be permitted to retaliate against hotels, for example by demoting them in OTA listings, if hotels engaged in discounting consistent with the Principles or permitted other OTAs to discount.
14. The OFT was also told that it might be difficult for hotels to monitor OTA compliance with the Principles under the commission-based model (as opposed to the merchant model),⁶ and that the Commitments should incorporate a right for hotels to regularly request information to monitor OTA compliance.
15. In addition to questions around how the Commitments would affect hotels' relationships with OTAs, the OFT was asked whether the Commitments would apply to the wholesale channel, where hotels do not have direct contractual relationships with OTAs.

⁶ As explained in Annexe 2 to the Consultation Notice on the Revised Commitments, under the merchant model, the OTA charges the customer a retail price and remits a rate net of its agreed margin to the hotel. Under the commission-based model, the hotel charges the customer and then pays the OTA a commission.

Commitments may strengthen Booking.com and Expedia's market positions

16. Several respondents queried whether the design of the Commitments, for example, the requirements for consumers to have joined a closed group and made a prior booking before becoming eligible for a discount, would risk entrenching the existing market positions of Booking.com and Expedia. For example, consumers might remain loyal to specific OTAs rather than join multiple OTA or hotel closed groups to compare prices, and the prior booking requirement might dissuade consumers from using other OTAs or the hotel's own website to make subsequent purchases once they had made their first booking with one OTA.
17. Respondents also suggested that OTAs such as Booking.com and Expedia could have a competitive advantage over new entrant OTAs under the proposed Commitments because they already have access to an extensive customer base and may have pre-existing membership schemes. Likewise, the OFT was told that smaller OTAs and independent hotels might be less able than larger OTAs and hotels to invest in the relevant technology to operate closed groups that would monitor prior bookings.
18. In addition, the OFT was told that the larger OTAs have a greater ability than smaller OTAs and hotels to advertise, for example by being ranked higher in search engine results. It was submitted that smaller OTAs typically negotiate lower commission rates from hotels than the larger OTAs. Therefore, the OFT was told that, because the Commitments envisage OTAs being able to discount only up to the level of their commission for the relevant hotel property, smaller OTAs would have less commission with which to offer discounts. This factor, combined with smaller OTAs' lesser market presence, may suggest that the Commitments would not lower barriers to entry. One respondent recommended that the OFT consider imposing the same commission levels for all hotels and OTAs as part of the Commitments, to ensure an equal basis for offering discounts.

Commitments may impact on consumers' ability to shop around

19. Some respondents considered that the definition of closed group is too narrow, for example, the definition excludes consumers who have signed up to a newsletter/ mailing list. However, the OFT was also told that the closed group criteria are easily satisfied and that discounts would therefore be so widely available that it would become impossible for hotels to maintain the integrity of their headline room rates.
20. Some respondents raised concerns about consumer confusion regarding the availability and level of discounts. For example, it was submitted that because price differences would only be visible to closed group members, rather than publicly, it would not be easy for consumers to compare the effective prices being offered by OTAs and hotels via their closed groups. It was also queried whether consumers would be able to figure out which website will offer the best long-term deal.
21. It was raised that the marketing message around closed group discounting could be confusing for consumers. There was also some concern about the need to provide personal data when joining a closed group, potentially to multiple booking sites.

OFT response

Competition between OTAs and hotels' direct online booking channels

22. The Commitments did not specify what type of hotel discounting would be consistent with the Principles. As mentioned at paragraph 8 above, the OFT received a number of queries about the extent to which the Commitments would have an impact on hotels' ability to offer discounts. To address these queries, the Parties have offered drafting amendments to the Commitments to clarify the ability of hotels to offer discounts to closed groups.⁷
23. The Revised Commitments would provide hotels with a greater ability to discount than OTAs because the Revised Commitments do not envisage any form of financial 'cap' or limitation on the extent of the discounts that hotels could offer to closed group members without MFN or

⁷ See paragraphs 3.14 to 3.18 of the Consultation Notice on the Revised Commitments for further detail.

equivalent provisions being enforced against them. Therefore, the OFT does not currently consider that the prior booking requirement and OTAs' ability to offer a wider selection of hotel accommodation than hotels would unduly affect hotels' ability to compete with OTAs' closed group discounting schemes.

24. As regards retaliatory action by OTAs, the OFT notes that it would be inconsistent with the spirit of the Commitments for OTAs to take such action against hotels that offered discounts in accordance with the Principles, or permitted other OTAs to do so. The Commitments provide that third parties may write to the OFT/CMA regarding alleged non-compliance by Expedia and Booking.com with the Commitments.
25. As regards hotels' ability to monitor OTA compliance with the Principles, it is not clear to the OFT why it would be more difficult for hotels to monitor OTA compliance with the Principles under the commission-based model than under the merchant model. It is not the OFT's intention to favour any particular business model. The OFT notes that the Commitments already provide that hotels contracting with OTAs would be entitled to require such information as may reasonably be required to enable them to assess and verify compliance with the core Principles, such as the commission cap. However, hotels could not impose any method of accounting on any OTA which may restrict, limit or impede OTAs from operating on the basis of arrangements which are consistent with the Principles.
26. On the question of whether the Commitments would apply to the wholesale channel, the focus of the OFT's investigation has been the current restrictions on OTAs' discounting off the Room-Only Rate set by a hotel. The OFT has made no assessment of whether similar restrictions may exist in the wholesale channel.

Competition between OTAs

27. As explained in section 3 of the Consultation Notice on the Revised Commitments, one of the OFT's competition concerns is that the current restrictions on discounting may create barriers to entry to the extent that they prevent new OTAs from entering the market and/or achieving sufficient scale (with discounted rates for Room-Only hotel accommodation). As a result, a more efficient new entrant may be

unable to use its lower costs to offer larger discounts in order to attract customers away from incumbent OTAs. Currently, potential entrants may therefore need to create strong non-price related incentives for consumers to search for their sites and switch away from the established OTAs. The current restrictions on offering discounts to consumers may also mean that, even if small-scale entry does occur, it creates little incentive or ability for the incumbent OTAs to lower their commissions or reduce effective prices.

28. Therefore, the OFT has considered carefully the concerns raised by a number of respondents regarding whether the Commitments (contrary to what they are designed to achieve) may make market entry for OTAs more difficult and may inadvertently cement the market positions of the large, incumbent OTAs.
29. In particular, the OFT has considered the possibility that by restricting the eligibility of discounts to those customers that have made a prior booking with a specific OTA, the Commitments might have the effect of raising switching costs (as customers would have to forgo the discount that might be available from his/her current OTA, in order to become eligible for discounts for all future purchases under a rival OTA's membership scheme⁸) and as a result, might impact on competition between OTAs.
30. The OFT recognises that this might present an obstacle to switching to the extent that consumers do not place sufficient weight on uncertain future benefits (that is, future discounts at the rival OTA), as hotel room purchases may be relatively infrequent and the level of potential discounts uncertain. This could render competition between rival OTAs' membership schemes less effective than in other sectors where competing, non-exclusive loyalty schemes and 'multi-homing' are commonplace (for example, supermarket club cards, coffee shop loyalty cards).
31. The OFT recognises that as there is currently likely to be limited, if any, intra-brand competition between OTAs on Room-Only Rates, there is

⁸ It should be noted, however, that this 'cost' of forgoing a discount at the OTA at which the consumer is already a member would only arise if that OTA actually offered a discount at the particular hotel on the particular date the consumer wished to book.

little direct evidence on the likely proportion of customers that would search for discounts and switch between OTAs to take advantage of such discounts.⁹ However, the OFT notes that the majority of consumers surveyed in the consumer focus groups were open to joining multiple closed groups. Moreover, although they might try to remain loyal to one group initially, they did not want to find themselves tied to one OTA and wanted to be able to continue to shop around to take advantage of the best offers.

32. The OFT's current view is that the switching cost arising from the prior booking requirement would not undermine the ability for greater price competition to emerge in this market, for the following reasons:

- Most consumers surveyed in the consumer focus groups were not overly concerned with the idea of having to make one full price booking in order to receive discounts. They felt that if they had found a good enough deal on a hotel room, then it would not be an issue to pay full price for it – and that getting a discount at a later date would be an additional bonus.
- While it might be easy for consumers to switch between OTAs currently, there are limited benefits from doing so in respect of Room-Only hotel accommodation due to the current restrictions on discounting. By contrast, if customers expected to make a number of future purchases, the switching cost under the Commitments would be small in comparison with future benefits (that is, long-term eligibility for discounts).
- The switching cost would not necessarily result in an exclusivity effect as consumers could 'multi-home'. They could make an initial purchase with multiple OTAs in order to be eligible for immediate discounts with all of them (and they would not incur any switching cost at all if the OTA they are already a member of does not offer a discount at the hotel/night). As explained above, the majority of consumers surveyed in the consumer focus groups were open to joining multiple closed groups.

⁹ However, one of the Parties has provided evidence indicating that a significant proportion of consumers are price sensitive and that price is the most important criterion that consumers use when sorting search results for hotel rooms.

- The threat of switching by marginal customers who are price-sensitive and search for lower prices would provide incentives for incumbent OTAs to continue to offer attractive loyalty schemes, even to those customers that did not want to switch or 'multi-home' between OTAs.
 - Any loyalty effect might strengthen the incentives for Booking.com and Expedia to offer substantial discounts in competition with one another as well as in response to the threat of entry.
 - Some switching costs might make the threat of entry a greater constraint on the incumbent OTAs (as it would be more difficult for the incumbent OTAs to win back customers from a new entrant's closed group).
33. Therefore, the OFT expects that, if the Revised Commitments were ultimately accepted by the OFT and OTAs obtain the discounting freedom envisaged, they would need to offer competitive discounts to 'multi-homing' customers to discourage them from purchasing through a rival OTA whose closed group the customer had already joined. All closed group members would benefit from this price competition, whether or not they had joined a rival OTA's closed group.
34. The OFT currently considers that the fact that the Commitments would provide new entrant OTAs with additional scope to compete for customers by allowing them to offer discounting schemes (and the potential to offer generous discounts on future purchases) should in itself provide consumers with an even greater incentive to search across OTAs for the best available deals and to become members of more than one closed group to find out details of specific discounts on offer to eligible members, thereby increasing the competitive constraint on the incumbent OTAs.¹⁰
35. In addition, the Commitments envisage a cap on OTA discounting up to the level of the OTA's commission revenue or margins. The OFT

¹⁰ Joining a closed group is intended to be a relatively low threshold, which may require only the entry of certain personal details online. This means that consumers would not be disincentivised from joining several groups due to onerous joining mechanisms. Depending on the OTA offering the scheme, no purchase may be required to join the closed group itself (as opposed to being eligible for discounts).

currently considers that such a cap might serve to protect new entrant OTAs from an aggressive response (for example, retaliatory deep-discounting) by incumbent OTAs that might otherwise deter entry.

36. The OFT recognises that the incumbent OTAs might benefit from economies of scale as they would have access to an extensive, existing customer base and might have pre-existing membership schemes. However, the Commitments are intended to provide a level playing field between large, incumbent OTAs; smaller OTAs wishing to expand; and potential entrants, as follows:
- The prior booking requirement would be satisfied only through purchases made **after entry into force of the Commitments**. Therefore, previous purchases at OTAs (including the incumbent OTAs) would not be relevant in assessing whether a customer is eligible for discounts. In addition, new entrant OTAs would not be prevented from incentivising consumers to make the first purchase (making them eligible for future discounts) in innovative ways.
 - OTAs would be able to fund discounts up to the aggregate commission earned for a hotel property for up to one year. This would allow OTAs with lower commission levels to have greater flexibility in the discounts they offer, for example by saving up their commission to enable them to engage in deeper discounting.
37. In light of the above, the OFT currently considers that the Commitments would increase incentives for new entry and lower barriers to entry created by the current restrictions on discounting. The OFT currently also considers that, on balance, the benefits to competition from allowing closed group discounting under the Commitments would be likely to outweigh the potential risk from creating any switching costs, relative to the current market position.
38. Although the OFT was told that smaller OTAs and independent hotels may be less able than larger OTAs and hotels to invest in the technology to allow them to operate closed group schemes, the OFT did not receive evidence demonstrating that the costs of doing so would be prohibitive, that is, that smaller OTAs and hotels would be unable to offer such discounting schemes or membership programmes.

39. In respect of consumer and data protection legislation concerns, the Commitments would operate without prejudice to applicable consumer and data protection legislation and the OFT expects organisations to comply with their legal obligations at all times.

Issue 3: Third party views on efficiency arguments put forward by the Parties

40. Overall, the feedback from the Consultation suggested that the Commitments are sufficient to address the issue of restrictions on OTAs' ability to offer discounts, which was the focus of the OFT's investigation, that is, that the Commitments would not need to allow OTAs to engage in full, unrestricted discounting. Several respondents supported the efficiency arguments put forward by the Parties to justify the retention of some restrictions on OTA discounting. In particular, the OFT was told that:

- From a hotel's perspective, headline room rates can act as an **important indicator of quality** for consumers. If such rates are routinely undermined by OTAs offering significant discounts off the headline rate then this may damage the value of a hotel's brand in the eyes of consumers and its position relative to competitors and may adversely impact inter-brand competition.¹¹
- All hotel respondents who made comments on the efficiency arguments put forward by the Parties highlighted the importance of **yield (revenue) management strategies** to the efficient operation of their businesses. This can involve the regular adjustment of room rates to respond to observed changes in consumer demand. This allows hotels to manage their inventory more efficiently and avoid being left with unoccupied rooms. By contrast, the OFT was told that because OTAs do not take on any inventory risk, they may not have the same incentives as the hotel to adjust prices to maximise occupancy levels.

¹¹ The OFT understands, for example, that whilst hotels themselves may engage in deep-discounting of rates from time to time in order to sell unoccupied rooms, this is normally done through an opaque channel operated by an OTA whereby the name of the hotel is only revealed once the consumer has made a booking.

- A number of hotels also supported the Parties' contention that fully unrestricted discounting by OTAs would lead to a **cannibalisation of hotels' direct online sales channels** and would therefore have the effect of raising hotels' distribution costs and dissuade them from dealing with OTAs (or as many OTAs as they currently do).
41. During the Consultation, the OFT also received additional representations and argument from the Parties on the need for hotels to independently set and control headline room rates, in particular to facilitate the efficient operation of yield management techniques and also to avoid free-riding. However, in the absence of an appropriate counter-factual, the OFT did not receive any evidence to substantiate the Parties' contention that the specific shape of the residual restrictions proposed in the Commitments, for example, the closed group and prior booking requirements, are essential to deliver the efficiencies claimed by the Parties. For example, the OFT did not receive any evidence from hotels to substantiate the claim that yield management would be wholly unworkable without some form of discounting restrictions such as the specific restrictions proposed in the Commitments.
42. Moreover, a number of respondents challenged the strength of the efficiency arguments. For example, in relation to the free-riding argument, it was questioned whether, in practice, the remaining discounting restrictions are necessary to ensure that OTAs continue to invest in website functionality and customer services.

OFT response

43. The responses to the Consultation and further representations from the Parties suggest that, in the specific factual context, the arguments put forward for the existence of efficiencies are likely to have some merit in this sector.
44. However, the OFT did not receive evidence that either strongly confirmed or refuted the efficiency arguments put forward by the Parties to justify the residual restrictions remaining under the Commitments. Therefore, the OFT currently has insufficient evidence on which to make a definitive assessment of these efficiency arguments. In particular, the OFT has insufficient evidence on which to make a definitive assessment of

whether removing all restrictions on OTA discounting would have all of the potentially negative consequences claimed by the Parties.

45. Based on its assessment of the evidence available, the OFT has sought to strike the right balance in terms of the extent of the intervention needed in this sector to address its competition concerns, as set out in paragraphs 3.31ff of the Consultation Notice on the Revised Commitments.

Issue 4: Geographic scope of the Commitments

46. Some respondents questioned why the Commitments applied only in respect of UK residents and identified a possible discrimination issue with such an approach. Another respondent questioned why the Commitments applied only to EU hotels, rather than hotels worldwide.

OFT response

47. The OFT notes these submissions. For the reasons set out at paragraphs 3.19 to 3.21 of the Consultation Notice on the Revised Commitments, the Revised Commitments amend the geographic scope of the Commitments so that they would apply to bookings made by EEA residents for rooms in hotels located in the UK, rather than to bookings made by UK residents for rooms in hotels located in the EU.

Issue 5: Duration of the Commitments

48. It was raised by some respondents that the proposed three-year term of the Commitments might be insufficient because it would not generate sufficient legal certainty and the Parties would not be obliged to comply thereafter.

OFT response

49. The OFT notes these submissions. However, the OFT is aware that online travel agency services, including hotel online booking, is a growing, dynamic sector and some respondents to the Consultation urged the OFT to consider the risk that the Commitments could cause distortions. Therefore, the OFT now considers that the three-year period originally proposed risks excessive regulatory intervention in a dynamic,

innovative sector, and would not allow the OFT to react as quickly to any changes. In light of these considerations and for the reasons set out at paragraphs 3.22 to 3.24 of the Consultation Notice on the Revised Commitments, the Revised Commitments amend the duration of the Commitments to specify that they shall remain in force for a period of two years, rather than three years.