

## Why competition law applies to the “innovative” Internet? Lessons from Europe

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### Speed read

Why should regulators pursue Google when it has brought huge innovation and benefits? Or Expedia and Booking.com when they have done so much to bring down prices, made the market transparent and opened up options for hotels large and small? Isn't action to shut down their innovation counter-productive? Alexander Italianer, Director-General of the EU Competition branch provided some answers in a speech last month.<sup>1</sup>



### Why does competition law have a role on the internet?

Dr Italianer quotes famous Austrian economist, Joseph Schumpeter's, “creative destruction” concept which has played out in many industries, such as power loom weaving in the 18th century and the car industry in the early 1900s. He says it now plays out in the internet world. Revolutionary new industries replace the old, and the new industries and their market positions quickly become more stable. After a while innovation takes place incrementally rather than exponentially.

There is rapid change in the internet world, but even so, says Dr Italianer, some providers have quickly matured and established strong market positions. That leads to incremental rather than exponential innovation.

The impact of the internet on economies is so great that it calls for greater focus: for example, he quotes data that it took the Industrial Revolution fifty years to achieve the same rise in living standards that the internet achieved over fifteen years.

So, he says, competition concerns and competition law continue to apply on the internet.<sup>2</sup> States Dr Italianer:

*“...even in an area that is unique to the internet [such as the Google case overviewed below], the antitrust concerns we investigated can be found in any student handbook on competition law.*

*To sum it up: characteristics of the Internet such as ease of use, worldwide reach and speed of innovation provide new dimensions to classic competition concerns.”*

We'll pick two of the real life examples that Dr Italianer uses: the hotel booking cases and the current action against Google. We've left out two of the big ones he deals with: net neutrality and also Pay TV and the Internet.

### Expedia and Booking.com

To book a hotel back in the day, you had to go through a travel agent, or direct to the hotel.

Enter a new type of middleman: the online travel agent. By searching on the internet, consumers can find dozens of hotels at each destination, each with pictures of the hotel and reviews by other customers. The hotel market has become more transparent and instant worldwide visibility has made it easier for small hotels to compete with large chains.

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So that’s all good news? Well, yes.....and no. Enter a new twist on the long standing restriction on resale price maintenance (RPM).<sup>3</sup> In classic RPM cases, the supplier uses its market power to force resellers to sell its products at a certain price. But here, the online travel agent –the reseller rather than the supplier - may have the power and the ability to engage in RPM.<sup>4</sup> For example, increasingly smaller hotels cannot dispense with the online travel agents’ services, with their market power, global brands and advertising budgets to match.

The RPM happens by way of most favoured nation clauses: the hotel must always or mostly provide the online travel agent with the best price, and the hotel cannot supply rooms more cheaply directly to consumers or through other agents. While only 20% of bookings are made through online travel agencies and 10% through hotel websites, this RPM (in the form of a price parity clause) generally extends to the other 70% of customers.

In the UK, regulatory action led to Booking.com and Expedia giving undertakings curtailing this action.<sup>5</sup> The RPM might:

- Eliminate intra-brand competition for the same room;
- Reduce the incentive for online travel agents to compete on commission; and
- May create barriers for new online travel agents to enter the market.

**Google**

The US regulator backed off taking action against Google, but the EU continued. The signs are that the EU and Google are about to do a deal to stop proceedings being issued. Google will undertake to curtail its conduct.

The EU is concerned that Google is using the dominance of its general search engine that many of us use to promote its specialised services, such as price comparison, hotel and restaurant reviews. The results for those specialised services appear more prominently than those offered by competing services.

As Dr Italianer notes: “*The challenge is to address this issue without limiting Google’s ability to innovate.*”

Google is proposing commitments, which might be acceptable to the EU, to display three visible links to rival services, so that users can make an informed decision.

Another EU concern is Google’s use of content from third party web sites without their permission. For example, Google’s restaurant search also showed reviews of restaurants on other websites so that the user didn’t need to visit that site. The competing site lost the eyeballs for ads, which went to Google instead. Competitors could opt out but at the cost of not being included in the Google general search, a high cost indeed.

Google has now offered to address this by permitting opt out that will not affect the page ranking on a general search.

Dr Italianer identifies two other abuse of dominant position issues with Google:

- Google required publishers to obtain all or most of the search, displayed on their websites, from Google;
- Google did not allow software developers to develop tools that made it easy to transfer ad campaigns from Google’s Adwords service to competing services.

Google has now committed to end both types of behaviour.

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Conclusion

The Director-General concludes:

*“If one thing is clear, it is that despite the speed of developments on the Internet, competition enforcers and policy makers in Europe are dealing actively with anticompetitive behaviour.*

*The speed of online developments and differing circumstances mean that competition enforcers and legislators in Europe and around the world may adopt slightly different approaches to different cases.”*

1. See [http://ec.europa.eu/competition/speeches/text/sp2014\\_01\\_en.pdf](http://ec.europa.eu/competition/speeches/text/sp2014_01_en.pdf). Address to the 47th Innsbruck Symposium 7 March 2014- “Real sector economy and the internet – digital interconnection as an issue for competition policy”.

2. Matt Sumpter in his book, NZ Competition Law and Policy (CCH 2010) at Para 910 has an interesting analysis on the effect of the internet on RPM, cartel activity and free riding.

3. In NZ whether under per se RPM provisions and/or the more general bilateral conduct provisions (s 27 and 30 Commerce Act)

4. Dr Italianer describes this as RPM and as a variation called parity pricing. Technically it may not be, but he describes how under EU law it can be RPM, and, in other jurisdictions, even if not per se RPM, it might breach general bilateral conduct provisions such as s 27 and 30 Commerce Act (NZ).

5. In Germany overlapping action was taken against a major German online travel agent, HRS.com

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