Cooley

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On 8 August 2022, the UK's Competition Appeal Tribunal (CAT) unanimously set aside a £17.9 million fine imposed on the Compare The Market website (CTM) by the Competition and Markets Authority (CMA). The CAT held that the CMA had failed to show that CTM's historical use of wide retail parity obligations, also known as most favoured nation (MFN) clauses, had anticompetitive effects.

The CAT's judgment is another example in the ongoing debate about how competition law should treat MFN clauses, adding to a fragmented legal landscape in which the European Commission, individual EU member states and the UK have taken various different approaches in recent years.

We've summarised below the key points of the CAT judgment and explained what it means for businesses that use MFN clauses in their agreements with suppliers or customers.

Refresher on MFN clauses

MFN clauses come in many forms. At their core, MFN clauses prohibit contract party 1 from offering better terms to a third party than to contract party 2. MFN clauses can relate to all aspects of a contractual relationship, including price, availability of products, services and quality.

The legal treatment of MFN clauses may differ based on several factors, as outlined below.

- **Whether the MFN is 'wide' or 'narrow':** Wide MFNs apply to a supplier's **indirect** sales channels (e.g., sales through other intermediaries), while narrow MFNs apply to a supplier's **direct** sales channel (e.g., through the supplier's own website).
- **Whether the MFN clause operates at the business-to-business or retail level:** As explained below, wide retail MFN clauses are prohibited in the UK.
- **The industry impacted by the MFN clause:** For example, some EU member states have prohibited MFN clauses in the hotel online booking sector.
- **The identity of the contract parties:** For example, the upcoming EU Digital Markets Act will prohibit wide and narrow MFN clauses for certain services by designated gatekeepers.

Since 1 June 2022, UK legislation has included wide retail MFN clauses in its list of 'hardcore restrictions' of competition, meaning that any agreement containing such a clause is presumed illegal. In the EU, wide retail parity clauses are instead 'excluded' from legislative safe harbours in contracts with online intermediation services, meaning that their competitive impact needs to be assessed on a case-by-case basis.

The CMA's challenge to MFN clauses used by CTM

The CMA's November 2020 decision challenged agreements between CTM and 32 home insurance providers that contained wide retail MFN clauses preventing home insurance providers from quoting lower prices to consumers on other price comparison websites (PCWs).

The CMA found that the MFN clauses in question were in breach of competition law by 'effect' because they:

- Reduced the insurers' incentive to offer lower prices (e.g., promotional deals) to CTM's rivals.
- Discouraged CTM's rivals from offering lower commission fees and thereby gain a competitive advantage over CTM.
- Restricted CTM's rivals' ability to expand because they were unable to secure a price advantage over CTM.
- Limited competition between home insurers more generally. (The CMA found that because the 32 insurers competed less strongly on price, other providers were subject to less competitive pressure, and competition on retail prices between all insurers competing on PCWs was reduced.)

The CMA also noted that the contracts with CTM prevented insurers from quoting lower prices on their own websites (i.e., via a narrow MFN clause), but found that such narrow MFN clauses were a 'feature of the market'. The CMA considered that narrow MFN clauses prevented insurers from free riding on investments made by PCWs into their own websites and services, because they stopped insurers from undercutting the prices shown on PCWs (where large numbers of customers would see offers) on their own websites.

The CAT reverses the CMA's findings

The CAT disagreed with the CMA's analysis and quashed the decision on the basis that the CMA had failed to show that the MFN clauses had anticompetitive effects. In particular, the CAT criticised the evidence basis on which the CMA sought to base its decision, noting that it was 'anecdotal' and untestable by either CTM or the CAT itself.

In the CAT's view, the CMA had the burden of proving the adverse effect on competition on the balance of probabilities. The fact that the CMA merely showed that the wide MFN clauses were contractually complied with was not enough for this purpose.

In particular, the CAT found that the CMA had not sufficiently taken into account that MFN clauses could have pro-competitive or at least neutral effects on the incentive of home insurance providers to lower commissions, promotional discounts, or the home insurance products themselves. The CAT noted that wide MFN clauses only restricted the price at which home insurers could offer their products through PCWs – they did not restrict competition on the level of premiums – and faulted the CMA for not considering this in its analysis.

Furthermore, the CAT found that wide MFN clauses in the home insurance market would in many cases not prevent differential pricing between PCWs. The CAT noted that for the wide MFN clauses to have an effect, a consumer's risk profile would have to be identical across different PCWs, requiring the same questions to be asked and the same answers to be provided. The CAT found that this was not necessarily the case in practice.

The CAT also clarified that wide MFN clauses are not 'by-object' restrictions (i.e., presumptively anticompetitive regardless of effect). The CAT found that wide MFN clauses could result in a number of different outcomes, not all of which were anticompetitive. By way of example, the CAT referred again to competition between home insurance providers on prices offered to consumers, noting that this might even be 'sharpened' as a result of home insurers having to offer the same low price across different sales channels. Furthermore, the CAT emphasised that CTM and home insurers had agreed to the MFN clauses voluntarily and may have had commercial reasons for doing so.

What's next?

The CAT's judgment adds to the ongoing debate about the impact of parity clauses on competition and how these should be treated legally.

Shortly after the CAT judgment, the European Commission published the results of its market study on hotel distribution practices in the EU. One finding of the market study was that laws in Austria and Belgium banning the use of wide and narrow online travel agent parity clauses in the hotel sector did not appear to have led to material changes in hotel distribution practices, including no material increase in commission rates or noticeable effect on hotel price differentiation strategies, relative to the other member states covered by the study.

The CAT's findings are more in line with these market study findings than with the legislation in the UK banning wide retail parity restrictions. Nevertheless, the CMA has not given any indication that it is reconsidering the status of wide retail MFN clauses as 'hardcore restrictions' of competition law (although it also does not appear to have appealed the judgment).

Businesses will have to ensure that MFN restrictions – especially those with cross-border effects – are legally robust in what is an increasingly fragmented European landscape and assess any restrictions carefully.

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