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Research on Anti-monopoly Regulation of the MFN Clause on Internet Platforms

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Abstract: With the continuous development of electronic information technology, internet companies are playing an increasingly important role in the business field. This evolution has not only catalyzed shifts in business models and transaction habits but has also introduced novel practices, such as the integration of Most-Favored-Nation clauses (MFN clauses) that were formerly exclusive to traditional business domains. Currently, MFN clauses are widely used in commercial activities between internet platform companies, which require high attention from antitrust enforcement agencies. Through a comprehensive analysis of existing literature and research, this study aims to shed light on the similarities and differences between these two types of MFN clauses, offering valuable insights into the evolving landscape of business practices within the digital age. In addition, the article also uses case analysis to examine two typical cases in foreign jurisdictions, demonstrating the regulatory approaches of the extraterritorial judiciary towards MFN clauses within internet platforms. Based on the analysis, the conclusion of this paper is that the for "collusive" MFN clause, the "illegal per se doctrine" should be applied for "exclusive" MFN clause, the principle of reasonableness should be applied, taking account of both the effects on restricting and promoting competition.

Keywords: antitrust law, MFN clause, internet platforms, US apple e-book case, EU amazon case

1. Introduction

With the advent of the digital age, internet platform enterprises have begun to develop. Various platforms such as search engines, mobile payments, and social networks have emerged in the market rapidly and continuously, changing various aspects of people's daily lives. At the same time, this has led to increasingly fierce market competition and various new forms of competition, including the "The Most Favoured Nation (MFN) Clause". As a new type of transaction method, the MFN clause has a dual effect on competition and has received high attention from anti-monopoly agencies in various countries in recent years, such as the "Apple e-book monopoly case" in the United States and the "Amazon abuse of market dominance case" in the European Union [1] Although there is no similar judicial practice in China, it does not mean that such situations do not exist. With the further development of the internet industry, the anti-monopoly risks that the MFN clause may bring will also threaten China's competitive market. Therefore, it is necessary to clarify the anti-monopoly

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issues of this clause and formulate a clear regulatory path. This article aims to establish a regulatory framework and provide a roadmap for China in addressing the MFN clause in the context of anti-monopoly regulations, drawing insights from prominent cases such as the US Apple e-book case and the EU Amazon abuse of market dominance case. By analyzing these cases, valuable lessons can be learned, helping China develop effective strategies and policies to regulate the MFN clause and promote fair competition in the market.

2. Overview of the MFN Clause

2.1. The MFN Clause in Traditional Industries

The MFN clause originated in the international trade field, mainly used to restrict trade between countries, involving tariffs, navigation, imports and exports, and other aspects. The MFN clause requires countries to extend the trade conditions they provide to one country to all trade partners within the clause, to ensure that trade partners within the clause receive the same trade conditions [2] In the context of traditional industries, the preferential treatment clause is referred to as the “Most Favored Customer Clause”, which can apply to both buyers and sellers. Typically, the seller commits to a specific buyer that they will not offer more favorable conditions to other buyers. Should more favorable conditions be extended to other buyers, those covered by this clause will automatically receive the same preferential treatment. While the content of MFN clauses may involve various preferential conditions, the ultimate impact often manifests in the pricing. When MFN clauses encompass all buyers of the seller, all buyers will be subject to the same price. However, if the agreement benefits only certain buyers, the seller may still charge higher prices to buyers outside the agreement [3].

2.2. The MFN Clause in Internet Platforms

With the development of the digital economy, the internet has become an essential factor in people’s lives. In the daily business operations of internet platform enterprises, MFN clauses have emerged and, unlike which in traditional industries, require special attention from antitrust agencies. As platform enterprises mostly act as intermediaries between buyers and sellers, the application of MFN clauses in internet platforms differs from that in traditional industries. Firstly, MFN clauses in internet platforms mainly exist between sellers and platforms and do not restrict the price at which the platform acquires goods from the seller but rather the price at which the seller sells goods on the platform. Secondly, while MFN clauses in traditional industries restrict the transaction price between buyers and sellers, resulting in the beneficiary being one of the parties involved in the transaction, MFN clauses in internet platforms restrict the price at which sellers sell goods to consumers on the platform, with the beneficiary being a third party outside of the agreement, namely consumers on the Internet [4]. More importantly, there are two types of MFN clauses in internet platforms: broad and narrow ones. Broad MFN clauses not only restrict sellers from offering preferential prices through self-built channels but also prohibit them from selling goods at lower prices on other platforms. On the other hand, narrow MFN clauses solely restrict sellers from providing preferential prices through self-built channels, while allowing them to offer more favorable conditions on other platforms [5].

3. Case Studies Involving MFN Clauses in the Internet Platform Industry

3.1. The Apple E-books Case

In 2007, Amazon launched its electronic book product, Kindle. Publishers began collaborating with Amazon to sell e-books at wholesale prices to sell on the Kindle e-book platform. However, in order

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to dominate the e-book market, Amazon set a uniform price of $9.99 for e-books, which was even lower than the wholesale price from publishers. Due to this low price, Amazon quickly captured over 90% of the e-book market, causing panic among publishers. If Amazon gained market dominance, it would use this position to lower wholesale prices and reduce publisher profits. This policy also posed a threat to other competitors in the e-book market, such as Apple Inc. In response to Amazon's market dominance and its policy of lowering wholesale prices to reduce publisher profits, Apple Inc. adopted an agency model with Most-Favored-Nation (MFN) clauses to counter Amazon's expansion [6]. Under the agency model, publishers directly sold e-books on the iBook platform and independently set the price of e-books, while the MFN clauses required publishers to offer Apple the most favorable price. If a lower price was offered elsewhere, publishers had to adjust the iBook price accordingly. Apple's strategy was successful, as publishers signed contracts with Apple and pressured Amazon to adopt the agency model, allowing publishers to set their own prices. Under pressure from publishers, Amazon eventually compromised and also adopted the agency model. However, Amazon reported Apple to the US Federal Trade Commission, accusing it of violating the Sherman Act. In the legal battle that followed, Apple lost the case and was ordered to pay a penalty of $450 million.

This case raises two issues worth noting: the definition of MFN clauses and if the "illegal per se doctrine" can be applied in the analysis of MFN clauses. In this case, the court believes that Apple's behavior involved horizontal monopoly, while Apple argued that its relationship with publishers was clearly upstream and downstream, and should be considered a vertical monopoly. However, the appellate court rejects Apple's argument. The implementation of MFN clauses by Apple resulted in all publishers reaching an agreement with the company, leading to price collusion among publishers. Apple's purpose behind setting the MFN clauses was to collaborate with publishers to raise the price of e-books. At the same time, the court believes that the "illegal per se doctrine" should be applied, directly determining Apple's agreement as a horizontal monopoly agreement. Apple argued that if the court adopted this doctrine, MFN clauses commonly used in business practices would be considered illegal, which would seriously violate business norms. However, through analysis of the court's viewpoint, it can be concluded that the court did not directly determine that the MFN clause itself was a horizontal agreement and subject to the "illegal per se doctrine". Instead, the court analyzed Apple's behavior, concluding that its behavior involved "hub-and-spoke agreements" and further determined that the agreement was a horizontal monopoly agreement [7]. Therefore, MFN clauses on internet platforms are not usually directly considered horizontal agreements subject to the "illegal per se doctrine", but are determined based on the specific behavior of the subject.

3.2. The Amazon E-books Case

In 2015, the EU launched an anti-monopoly investigation into Amazon's e-book sales business, believing that a series of MFN agreements it signed with publishers constituted an abuse of its dominant market position. These MFN clauses included various terms such as "equal business models," "equal agency prices," and "equal wholesale prices." After the EU launched the investigation, Amazon committed to stop using MFN clauses, and then the EU terminated the investigation [8]. In the Apple e-book case, the MFN clauses adopted by Apple are seen as collusion between Apple and publishers.

In this case, the MFN clauses are viewed as an abuse of Amazon's dominant market position. When Amazon had a certain degree of market dominance, the MFN clauses it adopted were likely to constitute an abuse of its dominant market position. The effect of these agreements in restricting competition is mainly reflected in the following aspects: the effects on restricting price competition, reducing product differentiation and hindering innovation. Due to the existence of MFN clauses, publishers who sign agreements with Amazon will lose the motivation to seek cooperation with other platforms in the market. For other competitors in the market, the conspiratorial price or conditions

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they reach with publishers will be directly offered to Amazon without any conditions. This means that these platform companies cannot offer more favorable conditions to publishers, which in turn reduces the negotiating power of publishers with other companies in the market, affecting price competition. Secondly, a series of MFN clauses signed between Amazon and publishers require publishers to provide the same preferential prices, business models, and so on to Amazon as they do to other platforms or channels, which will cause products in the market to tend towards homogenization. Moreover, for potential competitors and new entrants in the market, they cannot attract publishers through differentiation, which hinders market entry and expansion. Thirdly, this series of MFN clauses will greatly reduce the subjective willingness of market entities to innovate. Amazon's use of MFN clauses allows the company to passively benefit from the innovations and business model advancements of other competitors in the market. When other entities introduce new products or innovative business models, Amazon can immediately enjoy the same benefits due to the existing MFN agreements. This situation creates a disincentive for other companies to invest in new innovations since their efforts will automatically be extended to Amazon without any additional benefits or exclusivity.

4. Suggestions on the Regulatory Path in the Chinese Legal System

Currently, in China, prominent Internet companies like Alibaba, Tencent, and Baidu have emerged as major drivers of the country's economic growth. Similarly, MFN clauses have become prevalent in the daily transactions between internet platform companies in China, playing a significant role in competition within the Chinese internet sector. However, However, China's judicial practice in this area remains limited, and the country's antitrust enforcement agencies lack a well-defined approach to regulating such MFN clauses. To address this regulatory gap, this article explores insights from the regulatory strategies employed by executive agencies and courts in the United States and Europe. By analyzing relevant cases, the aim is to derive inspiration and propose potential improvements to regulatory ideas and methods for Chinese antitrust enforcement agencies.

4.1. Effect-oriented Analysis to Determine Whether MFN Clauses Are "Collusive" or "Exclusionary"

In China, MFN clauses mainly involve horizontal monopoly agreements, vertical monopoly agreements, or abuse of market dominance. When MFN clauses exist in transactions between platform companies, Chinese antitrust authorities should conduct specific analysis based on the specific behavior of the platform companies. Therefore, Chinese enforcement agencies need to categorize MFN clauses when conducting investigations. If the MFN clause objectively leads to collusion between market players at the same level, it can be considered a "collusive" MFN clause. If the effect of the MFN clause is reflected in prices and it restricts other equal competitors from participating in competition fairly or the dominant player occupies a relatively large market share, it can be considered an "exclusionary" MFN clause.

4.2. Application of the "Illegal Perse Doctrine" and the Principle of Reasonableness

After distinguishing between "collusive" and "exclusionary" MFN clauses by combining the behavior of market players and the content of the MFN clauses, the next step for Chinese antitrust enforcement agencies is to determine the rules for different types of MFN agreements. In analyzing the anticompetitive effects of a certain behavior, Chinese antitrust analysis generally applies the "illegal per se doctrine" or "the principle of reasonableness" [9]. When the MFN clause belongs to the "collusive" type, it essentially belongs to a horizontal monopoly agreement, and the "illegal per se doctrine" should be applied without the need for a reasonableness defense. When the MFN clause

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belongs to the "exclusionary" type, a reasonableness analysis should be conducted based on the company's market share, specific behavior, or the effect of the behavior, and it cannot be assumed that the MFN agreement is illegal.

4.3. Efficiency Defense

It is worth mentioning that since MFN agreements can become a tradition in commercial practice, they must have their advantages [10]. For China's Internet economy, the MFN agreements that appear between platform companies also have the effect of promoting competition. From a positive perspective, MFN clauses can bring low-price benefits, avoid information asymmetry between buyers and sellers, and can keep prices at a relatively low level, benefiting consumers. At the same time, MFN clauses can also effectively reduce negotiation costs between platform companies, reduce the cost of collecting information for business entities, which may ultimately be reflected in lower prices of goods and services for consumers. Moreover, MFN clauses can also prevent "free-riding" behavior to a certain extent. If early investors in the market maintain the best trading conditions through MFN clauses, it can effectively prevent later competitors from "free-riding". Therefore, when Chinese antitrust enforcement agencies conduct a reasonableness analysis, the promotion and restriction of competition by MFN clauses should be fully considered, and a comprehensive judgment should be made.

5. Conclusion

This study defines the Most-Favored-Nation (MFN) clause in traditional industries and on internet platforms, and clarifies that the main feature of MFN on internet platforms is that it restricts sellers from selling goods on the platform at lower prices. Secondly, the beneficiaries of MFN clauses on internet platforms are not the parties to the agreement, but third parties outside the agreement, namely internet consumers. In addition, MFN clauses on internet platforms can be divided into broad and narrow MFN clauses. The former requires that sellers cannot sell goods at lower prices on other platforms, while the latter allows for more favorable conditions on other platforms.

This paper analyzes two typical cases involving MFN clauses in internet platform industries, the Apple e-book case and the Amazon e-book case, reflecting different analytical methods and regulatory paths for MFN clauses in judicial practice. Currently, MFN clauses on internet platforms mainly involve horizontal monopoly agreements, vertical monopoly agreements, and abuse of market dominance, requiring antitrust enforcement agencies to analyze specific situations.

Finally, this paper provides regulatory path suggestions for China's antitrust enforcement agencies regarding the regulation of MFN clauses. First, the enforcement agencies should conduct an effect-oriented analysis, distinguishing MFN clauses as "collusive" or "exclusive". Secondly, based on the different types of MFN clauses, different principles should be applied. If it is a "collusive" MFN clause, the "illegal per se doctrine" should be applied; if it is an "exclusive" MFN clause, the principle of reasonableness should be applied for regulation. Finally, when applying the principle of reasonableness, the promoting effect of MFN clauses on competition should be fully considered and analyzed comprehensively.

The shortcoming of this article is the lack of practical experience in our judicial system regarding the MFN clause. As a result, we rely on foreign court views and opinions, leading to some arguments and conclusions lacking localization. Theoretical basis of the article may be affected as a consequence. In the near future, with more relevant cases in China's judicial field, Chinese antitrust enforcement agencies will be able to better analyze and regulate the issues of competition restrictions related to MFN clauses. Through a series of practical experiences, they can develop and plan the most suitable regulatory approach for China. With mature legal rules, China can promote healthy competition

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among enterprises while fully protecting all participants in the market in the course of digital economic development.

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