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The Competition Ordinance – Enforcement, Compliance and Relevance to IT Companies and Professionals

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ISACA

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Outline

- Introduction of the Competition Commission and Competition Ordinance
- The Competition Rules – First Conduct Rule and Second Conduct Rule
- Making a complaint to the Competition Commission
- Investigation by the Competition Commission
- Enforcement and Sanction
- Complying with the Competition Ordinance
- HK's First Competition Law case to the Competition Tribunal
- Q&A

Introduction

- The Competition Ordinance (the “**CO**”)
 - Passed on **2 June 2012**
 - Commenced and in full operation since **14 December 2015**
 - Objective of CO: to provide a legal framework to curb anti-competitive conduct in various sectors, with a view to maintaining fair and sustainable competition in the market

Introduction

The Competition Commission (競爭事務委員會)

- Established in May 2013
- Prepare regulatory guidelines and promote public understanding of the CO
- Duty to issue guidelines regarding
 - Interpretation and enforcement of conduct rules
 - Manner in receiving applications for decisions or block exemption orders
 - Exercise of power to make a decision or grant block exemptions

Introduction

The Competition Commission (競爭事務委員會)

- Issued 6 Guidelines on 27 July 2015, which covers-
 - How the Commission expects to interpret CO
 - Procedures for handling complaints, conducting investigations and considering applications relating to exclusions and exemptions
- Guidelines are not subsidiary legislations and are non-binding
- Contravention of guidelines does not entail any civil or criminal liability

Introduction



The Competition Commission (競爭事務委員會)

- Wide-ranging investigation powers
 - To order production of documents and other information
 - To hear relevant persons
 - To enter and search premises with warrant
- Enforcement powers
 - To accept commitments from undertakings in return for CC's agreement not to bring proceedings before CT or to drop existing proceedings
- No sanction power

Concept of Competition

- The Ordinance enables businesses to resist anti-competitive terms and constraints on their freedom to operate
- The Ordinance prevents businesses from
 - abusing market power; and
 - creating entry barriers to the detriment of other businesses



Competition Ordinance (CO) - Scope of Application

The Ordinance applies to “**undertakings (業務實體)**”

- S2(1) of CO defines undertakings as “*any entity, regardless of legal status that engages in economic activity*”
- Examples of undertakings include-
 - individual companies
 - groups of companies
 - partnerships
 - individuals operating as sole traders or subcontractors
 - cooperatives
 - societies
 - business chambers
 - trade associations
 - non-profit organizations



Competition Ordinance (CO) - Scope of Application

- The key question is whether the relevant entity is **engaged in an economic activity**
- The term economic activity, while not defined in the Ordinance, generally refers to activities consisting of offering products in a market regardless of whether the activity is intended to earn a profit
- Not include an individual acting as a final consumer

Scope of Application – Undertakings wholly excluded

1. Statutory bodies (s3 of CO)

- “Statutory body” – “persons, corporate or unincorporated, established under an Ordinance, or constituted or appointed by an Ordinance, but do not include companies, trustees, societies, co-operatives and trade unions”
- EXCEPT those listed in a separate regulation to be adopted by the Chief Executive in Council
- Until such regulation comes into force, ALL statutory bodies are excluded from CO

2. Specified persons or persons engaged in specified activities (s4 of CO)

- The CE in Council may, by regulation, dis-apply the substantive provisions of CO in relation to all or part of the activities by any other person

The Competition Rules

- The Ordinance contains three competition rules:
 1. **First Conduct Rule (Section 6 of CO):** prohibits anti-competitive conduct involving more than one party;
 2. **Second Conduct Rule (Section 21 of CO):** prohibits anti-competitive conduct by a party with substantial market power; and
 3. **Merger Rule (Section 177, Schedule 7 of CO):** prohibits anti-competitive mergers and acquisitions in the telecommunications sector
- The First Conduct Rule is of most relevance to SMEs

First Conduct Rule

S6 of CO provides:

“An undertaking must not -

- (a) make or give effect to an agreement;*
- (b) engage in a concerted practice; or*
- (c) as a member of an association of undertakings, make or give effect to a decision of the association,*

if the object or effect of the agreement, concerted practice or decision is to prevent, restrict or distort competition in Hong Kong.”

First Conduct Rule

Single economic unit (單一經濟個體)

- The FCR does not apply to conducts which involve two or more entities if these entities belong to the same undertaking
- Generally, if entity A **exercises decisive influence** over the commercial policy of entity B, whether through legal or de facto control, then A and B will be considered as an SEU
- E.g. an agreement between a parent company A and its subsidiary B will not be subject to FCR if A exercises decisive influence over B



First Conduct Rule

Single economic unit (單一經濟個體)

- Whether a joint venture entity forms a single undertaking with any of its parents will be determined on a case by case basis
- Generally, if two or more parent entities have power to block actions which determine the strategic commercial behaviour of the joint venture (i.e. if there is joint control – including de facto control), the joint venture will not form part of the SEU as any of its parents

First Conduct Rule

Independent distributors vs. distribution agents (獨立分銷商及分銷代理)

- Whether FCR applies to supplier and third party distributor relationships depends on whether they are part of the same SEU
 - Supplier and independent third party distributor → FCR applies
 - Supplier and distribution agent → FCR does not apply



First Conduct Rule

Independent distributors vs. distribution agents (獨立分銷商及分銷代理)

- Factors for determining whether a third party is a true distribution agent
 - Supplier's level of control over the third party
 - Level of financial or commercial risk borne by the third party in relation to the activities for which it has been appointed as a distribution agent; e.g.
 - Does title to the contract products pass to the distributor?
 - Which party is responsible for product warranty?
 - Which party bears the costs or risks associated with non-performance by customers (e.g. late or non-payment)?
 - Which party is responsible for advertising and marketing costs?

First Conduct Rule

Independent distributors vs. distribution agents (獨立分銷商及分銷代理)

- Where a third party is a true distribution agent
 - FCR does not apply to the restrictions imposed in the distribution agreement on the distributor
 - The selling function of the distributor with respect to the contract products forms part of the supplier's undertaking



First Conduct Rule

Employees and trade unions (僱員及工會)

- An employee is not an undertaking
- Discussions or arrangements in relation to salary or other working conditions between employees and their employer take place within the framework of a SEU and are therefore outside of scope of the FCR
- Where a trade union acts as on behalf of its members in collective bargaining with an employer on terms and conditions of work, the trade union is not engaged in economic activity and is not an undertaking



First Conduct Rule

Agreement

- “Any arrangement or understanding, whether express or implied, written or oral”
- Test – whether there is a **meeting of minds** between the parties concerned
 - Not necessary to show that an undertaking participated in or agreed to each and every aspect of an anti-competitive agreement for the undertaking to be held responsible for the agreement as a whole
 - Sufficient if the undertaking knew, or should have known, that the collusion in which it participated was part of an overall plan intended to harm competition

First Conduct Rule

Agreement

- Applies to both horizontal and vertical agreements
 - Horizontal agreements – arrangements among competitors
 - Vertical agreements – agreements between undertakings active at a different level in the production or distribution chain

First Conduct Rule

Concerted practice (經協調做法)

- Not defined in CO
- A form of cooperation, falling short of an agreement, where undertakings knowingly substitute practical cooperation for risks of competition
- E.g. exchange of competitively sensitive information (such as pricing strategy) where
 - Information is given with the expectation or intention that the recipient will act on the information when determining its conduct in the market;
 - Recipient does act or intends to act on the information

First Conduct Rule

Decision of an association of undertakings

- FCR also applies where an undertaking, as a member of an association of undertakings, makes or gives effect to a decision of the association which has the object or effect of harming competition
- Decision of the association includes
 - Constitution
 - Rules
 - Resolutions
 - Rulings
 - Decisions
 - Guidelines
 - Recommendations

First Conduct Rule

Decision of an association of undertakings

- Typical decisions of associations which are likely to have the object of harming competition; e.g.
 - Recommended fee scales
 - “Reference” prices of trade and professional associations

First Conduct Rule

Object or Effect of Harming Competition (損害競爭的目的或效果)

- Most arrangements assessed on whether they have (or are likely to have) the **effect** of harming competition
- Some arrangements so consistently harmful said to have the **object** of harming competition – no need to assess actual or likely effects

First Conduct Rule

Object or Effect of Harming Competition (損害競爭的目的或效果)

(a) Object

- An objective assessment of the aims of an agreement viewed in its context and its implementation; **NOT merely the subjective intention of the parties**
- Typical examples of agreements with the object of harming competition include agreements between competitors to fix prices, to share markets, to restrict output, to rig bids
- Possible **inference of object** from the facts underlying the agreement and the specific circumstances in which it will operate or does operate
- Breach of FCR if one of its objects is to prevent, restrict or distort competition in Hong Kong

First Conduct Rule

Object or Effect of Harming Competition (損害競爭的目的或效果)

(b) Effect

- Not only actual effects but also likely effects of the agreement
- An agreement with anti-competitive effect must have an adverse impact on one or more of the parameters of competition; e.g.
 - Price
 - Output
 - Product quality
 - Product variety
 - Innovation
- Whether there has been an **appreciable adverse effect** on competition in the relevant market → must be **more than minimal**
- Breach of FCR if one of its effects is to prevent, restrict or distort competition in Hong Kong

First Conduct Rule

Object or Effect of Harming Competition (損害競爭的目的或效果)

- S7(1) of CO provides that if an agreement has **more than one object**, it will be capable of contravening the First Conduct Rule if any **one of its objects** is to harm competition
- S7(2) of CO provides that an anti-competitive object may be ascertained by inference
- S7(3) of CO provides that if an agreement has **more than one effect**, it is considered to have an anti-competitive effect if **one of its effects** is anti-competitive

First Conduct Rule

Territorial Application (S4 of CO)

- First Conduct Rule applies to an agreement, concerted practice or decision that has the object or effect of preventing, restricting or distorting competition in Hong Kong even if—
 - The agreement or decision is made or given effect to outside Hong Kong;
 - the concerted practice is engaged in outside Hong Kong;
 - any party to the agreement or concerted practice is outside Hong Kong; or
 - Any undertaking or association of undertakings giving effect to a decision is outside Hong Kong.

First Conduct Rule

Agreements that may contravene FCR

- **Horizontal agreements**
 - agreements made between two or more actual or potential competitors, each operating at the same level of the production or distribution chain
 - more likely to harm competition as they involve cooperation between competitors

First Conduct Rule

Agreements that may contravene FCR

- **Vertical agreements**
 - agreements made between undertakings that operate, for the purposes of the agreement, at a different level of the production or distribution chain
 - E.g.
 - undertaking A produces raw material
 - undertaking B uses the raw material acquired from A as an input in making B's own product
 - usually unlikely to harm competition, but not always: resale price maintenance (discussed later)

First Conduct Rule

Preventing, restricting or distorting competition

- S2 of CO defines “**serious anti-competitive conducts**”, namely any conduct that consists of any of the following or any combination of the following:-
 1. Price Fixing
 2. Market Sharing
 3. Output Restriction
 4. Bid-rigging

First Conduct Rule

(1) Price Fixing

- It means “*fixing, maintaining, increasing or controlling the price for the supply of goods or services*”
- **Price** in this context includes
 - any element of price; and
 - any discount, rebate, allowance, price concession or other advantage in relation to the supply of products

First Conduct Rule

(1) Price Fixing

- **Horizontal price fixing: direct agreement** on a specified price, the amount or percentage by which prices are to be increased or a price range
- **Indirect price fixing** includes-
 - Agreeing not to quote a price without consulting competitors, or not to charge less than any other price in the market; and
 - exchange of information on future price intentions

First Conduct Rule

(1) Price Fixing

- Price fixing might arise through the activities of a **trade association** or **professional body**
- Example: non-binding price recommendations or fee scales issued by a trade association to its members

First Conduct Rule

(2) Market Sharing

- It means “allocating sales, territories, customers or markets for the production or supply of goods or services”
- E.g. agreement not to –
 - Compete in the production of each other’s goods;
 - Sell in each other’s geographic “territories”;
 - Solicit or sell to each other’s customers (non-poaching agreement);
 - Expand into a market in which another participant is an actual or potential rival

First Conduct Rule

(3) Output Restriction

- It means “*fixing, maintaining, controlling, preventing, limiting or eliminating the production or supply of goods or services*”
- It can take the form of production or sales quota arrangements involving undertakings limiting the volume or type of products available in the market

First Conduct Rule

(4) Bid-rigging

- It is defined in Section 2(2)
- It generally involves two or more undertakings agreeing that they will not compete with one another for particular projects

First Conduct Rule

(4) Bid-rigging

- Bid-rigging can take a number of forms, including undertakings agreeing:
 - **Bid suppression:** certain parties do not submit a bid or withdraw a bid submitted previously;
 - **Bid rotation:** parties take turns at being the winning bidder;
 - **Cover bidding:** certain bidders submit higher bid prices or less attractive terms; and
 - **Other actions** that reduce the competitive tension in the bidding process (e.g. agreeing minimum bidding prices or agreeing that the winning bidder will reimburse other bidders' bid costs)

First Conduct Rule

(4) Bid-rigging

Bid-rigging vs. Joint tendering

- Joint tendering – undertakings cooperating openly to make a joint bid
- Where joint tendering is carried out in an open manner and is made known to the party organizing the tender → pro-competitive
 - Allows participation by companies which would not have been able to make a stand-alone bid
 - Enables companies to submit more competitive bids
- Joint tendering will not generally be considered to have the object of harming competition



First Conduct Rule

Other Conducts (1) - Joint Buying

- Undertakings often agree to jointly purchase products including inputs used for the production of other products
- Joint buying can be carried out in a number of ways-
 - through a jointly controlled legal entity
 - through an association
 - by a contractual arrangement between undertakings

In general, joint buying is unlikely to give rise to concerns under the FCR

First Conduct Rule

Other Conducts (2) – Exchange of Information

- Businesses often share information, and this is often legitimate commercial behavior
- However, sharing **commercial secrets** with a competitor such as information concerning future prices, quantities and customers can harm competition
 - E.g. information on prices, pricing strategy, customers, production costs, quantities, turnover, sales, product quality, marketing plans, technologies and innovations
 - Exchange of information between competitors in private on their future individual intentions or plans with respect to price and quantities etc. → likely to be regarded as having the object of harming competition

First Conduct Rule

Other Conducts (2) – Exchange of Information

- **Indirect exchange of competitively sensitive information** through the use of a third party supplier or distributor as a “conduit” → likely to be considered a form of price fixing with the object of harming competition

First Conduct Rule

Other Conducts (2) – Exchange of Information

- **Publicly available information:** information that is equally accessible in terms of the cost of access to all competitors and customers
- In general, the exchange of publicly available information is unlikely to involve a contravention of the FCR

First Conduct Rule

Other Conducts (3) – Group Boycotts

- In general, an undertaking is free to choose with whom it will or will not do business
- However, an agreement to engage in a group boycott may have the object of harming competition, when a group of competitors agrees to exclude an actual or potential competitor

First Conduct Rule

Other Conducts (4) – Activities of Trade Associations and Industry Bodies

- Where members of an association of undertakings make or give effect to a decision of the association which has the object or effect of harming competition, the undertakings and the association may both incur liability under the CO
- When membership of an association is an essential pre-condition for competing in a market, exclusion from membership can significantly impact an undertaking's effectiveness as a competitor and might be equivalent in terms of effect to an anti-competitive boycott

First Conduct Rule

Other Conducts (5) – Vertical Price Restrictions

- VPR are restrictions imposed or recommended by an undertaking which affect the prices at which another undertaking operating at a different level of the production or distribution chain sells products
- E.g. **resale price maintenance (“RPM”)** – a supplier imposes or recommends prices or price range at which another undertaking sells the products it purchases from the supplier

First Conduct Rule

Other Conducts (5) – Vertical Price Restrictions

- RPM restricts competition in various ways, e.g.-
 - Undermines suppliers' incentives to lower prices to distributors and distributors' incentives to negotiate lower wholesale prices
 - Prevents emergence of new market participants at distributor level
 - Limits “intra-brand” price competition by restricting the ability of distributors to offer lower sales prices for the affected brand as compared with prices offered by competing distributors of the same brand

First Conduct Rule

Other Conducts (5) – Vertical Price Restrictions

- RPM can be also achieved **indirectly** by the supplier—
 - fixing the distributor's margin or the maximum level of discount which the distributor can grant from a prescribed price level
 - using threats, intimidation, warnings, penalties or delays in deliveries

First Conduct Rule

Other Conducts (5) – Vertical Price Restrictions

Efficiency justifications for RPM

- When the RPM in question leads to efficiencies of the type detailed in section 1 of Schedule 1 to the CO
 - RPM may help address free rider problems at the distribution level where the extra margin guaranteed by the RPM structure encourages parties to provide certain sales services for the benefit of consumers
 - In the case of maximum resale prices, the resale price restriction may help to ensure that the brand in question competes more effectively with other brands notably when it avoids “double marginalisation”

First Conduct Rule

Other Conducts (6) – Exclusive Distribution and Exclusive Customer Allocation

- **Exclusive Distribution Agreement:** a supplier assigns exclusivity for the resale of its products in a particular territory to a single distributor (or reseller)
- **Exclusive Customer Allocation Agreement:** the supplier assigns exclusivity to a single distributor for resale to a particular group of customers

In general, EDA and ECAA do not have the object of harming competition, whereas their effects on competition will be assessed in on case by case basis

First Conduct Rule

Other Conducts (7) - Joint ventures

- JV refers to cooperative arrangement between undertakings, e.g.-
 - joint production arrangements
 - joint buying arrangements
 - joint selling, distribution and marketing arrangements
 - joint R&D ventures

Joint ventures, particularly those between SMEs to jointly provide a product or service they could not provide individually, are often good for competition

First Conduct Rule

Other Conducts (8) - Franchise Arrangements

- A common business model for the production and distribution of products in Hong Kong
- A franchise agreement typically contains provisions to
 - Maintain the identity and reputation of a franchise network
 - Protect the franchisor's branding, trademarks and know-how

Do these provisions raise concerns under FCR?

First Conduct Rule

Other Conducts (8) - Franchise Arrangements

Franchise arrangements – maintain the identity and reputation of the franchise network

- Typical franchisee's obligations under a franchise agreement include
 - To apply the franchisor's business method
 - To use the franchisor's trademarks, trade names only at the agreed franchise location
 - Not to change location without the franchisor's consent
 - Not to sell competing goods apart from those supplied or selected by the franchisor
 - To only sell products in a manner consistent with the franchisor's instructions (e.g. follow a particular recipe, use particular promotional materials)
 - To decorate the franchise premises in specified manner

First Conduct Rule

Other Conducts (8) - Franchise Arrangements

Franchise arrangements – maintain the identity and reputation of the franchise network

- Although the restrictions limit a franchisee's commercial freedom, CC considers that where they **relate directly to** and are **necessary for the implementation of the franchise arrangement** → unlikely to give rise to concerns under FCR

First Conduct Rule

Other Conducts (8) - Franchise Arrangements

Franchise arrangements – protect branding and know-how

- Typical franchisee's obligations under a franchise agreement include
 - To protect confidential information and know-how
 - Non-competition (e.g. not to open the same kind of shop in an area where it might compete with another franchisee during the term, not to carry on competing businesses during the term, not to compete with other franchisees for a reasonable period after termination of franchise)
- CC considers the above provisions are inherent in the nature of franchising → ancillary to a legitimate commercial purpose → unlikely to give rise to concerns under FCR

First Conduct Rule

General exclusions and specific exemptions

- 5 categories of general exclusions in Schedule 1 CO
- 2 specific exemption grounds

First Conduct Rule - General exclusions

1. Agreements enhancing overall economic efficiency (**S1 of Schedule 1**);
2. Agreements for compliance with legal requirements (**S2 of Schedule 1**);
3. Services of general economic interest (**S3 of Schedule 1**);
4. Mergers (**S4 of Schedule 1**); and
5. Agreements of lesser significance (**S5 of Schedule 1**)

First Conduct Rule - General exclusions

(1) Agreements enhancing overall economic efficiency

- Section 1 of Schedule 1 only applies where certain cumulative conditions are met, namely where the relevant agreement:-

“(a) contributes to–

- (i) improving production or distribution; or*
- (ii) promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit;*

(b) does not impose on the undertakings concerned restrictions that are not indispensable to the attainment of the objectives stated in paragraph (a); and

(c) does not afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the goods or services in question.”

First Conduct Rule - General exclusions

(1) Agreements enhancing overall economic efficiency

4 cumulative conditions

(1) The agreement contributes to improving production or distribution or promoting technical or economic progress

- An undertaking relying on the efficiency exclusion must provide convincing evidence of each of the following:
 - the efficiencies, which must be objective in nature;
 - a direct causal link between the efficiencies and the agreement;
 - the likelihood and magnitude of each efficiency;
 - how each efficiency will be achieved; and
 - when the efficiencies will be achieved

First Conduct Rule - General exclusions

(1) Agreements enhancing overall economic efficiency

4 cumulative conditions

(2) Consumers receive a fair share of the efficiencies

- The notion of a “**fair share**” means that the benefits accruing to consumers must at a minimum compensate them for the actual or likely harm to competition associated with the relevant restrictive agreement
- **Key consideration:** the overall impact on consumers of the products within the relevant market as a whole (**NOT** the impact on individual consumers or individual consumer groups within that market)

First Conduct Rule - General exclusions

(1) Agreements enhancing overall economic efficiency

4 cumulative conditions

(3) The agreement does not impose on the undertakings concerned restrictions that are not indispensable to the attainment of the relevant efficiencies

- the agreement itself, and each of the individual restrictions contained in the agreement, must be reasonably necessary to attain the efficiencies

First Conduct Rule - General exclusions

(2) Agreements for compliance with legal requirements

- Agreements are excluded from FCR to the extent that they are made to comply with a legal requirement that is any requirement imposed by or under any written law in Hong Kong
- The legal requirement must **eliminate any margin of autonomy** of the undertakings concerned → undertakings are compelled to enter into or engage in the agreement
- Exclusion does not apply if the undertaking has some scope to exercise its independent judgment

First Conduct Rule - General exclusions

(3) Services of general economic interest

- FCR does not apply to an undertaking **entrusted by the Government** with the **operation of services of general economic interest** in so far as FCR would **obstruct** the performance of the particular tasks assigned to it

First Conduct Rule - General exclusions

(3) Services of general economic interest

- Entrustment
 - By legislative measures (e.g. regulation, grant of a licence governed by public law)
 - By an act of the Government
 - Mere approval by the Government of activities carried out by the undertaking will not suffice

First Conduct Rule - General exclusions

(3) Services of general economic interest

- Services – include distribution of goods and provision of services
- Services of general economic interest
 - Services which should be provided to the public whether or not the private sector would supply the relevant services
 - e.g. activities in cultural, social and public health fields which aim to make profit

First Conduct Rule - General exclusions

(4) Mergers

- Agreements to implement a merger are not caught under FCR

First Conduct Rule - General exclusions

(5) Agreements of lesser significance

- Certain agreements, concerted practices and decisions of trade associations involving SMEs are excluded from the scope of application of the First Conduct Rule
- 2 conditions:
 1. The combined aggregate worldwide annual turnover of the undertakings involved do not exceed HK\$200m
 2. No involvement of “serious anti-competitive conduct”

First Conduct Rule - General exclusions

Block Exemption Orders

- Section 15 provides that if the Commission is satisfied that a particular category of agreement is excluded from the application of the FCR by or as a result of Section I of Schedule 1, the Commission may issue a Block Exemption Order in respect of that category of agreement
- Where an agreement falls within scope of a Block Exemption Order issued by the Commission, the agreement is exempt from application of the FCR under Section 17

First Conduct Rule - Specific exemption grounds

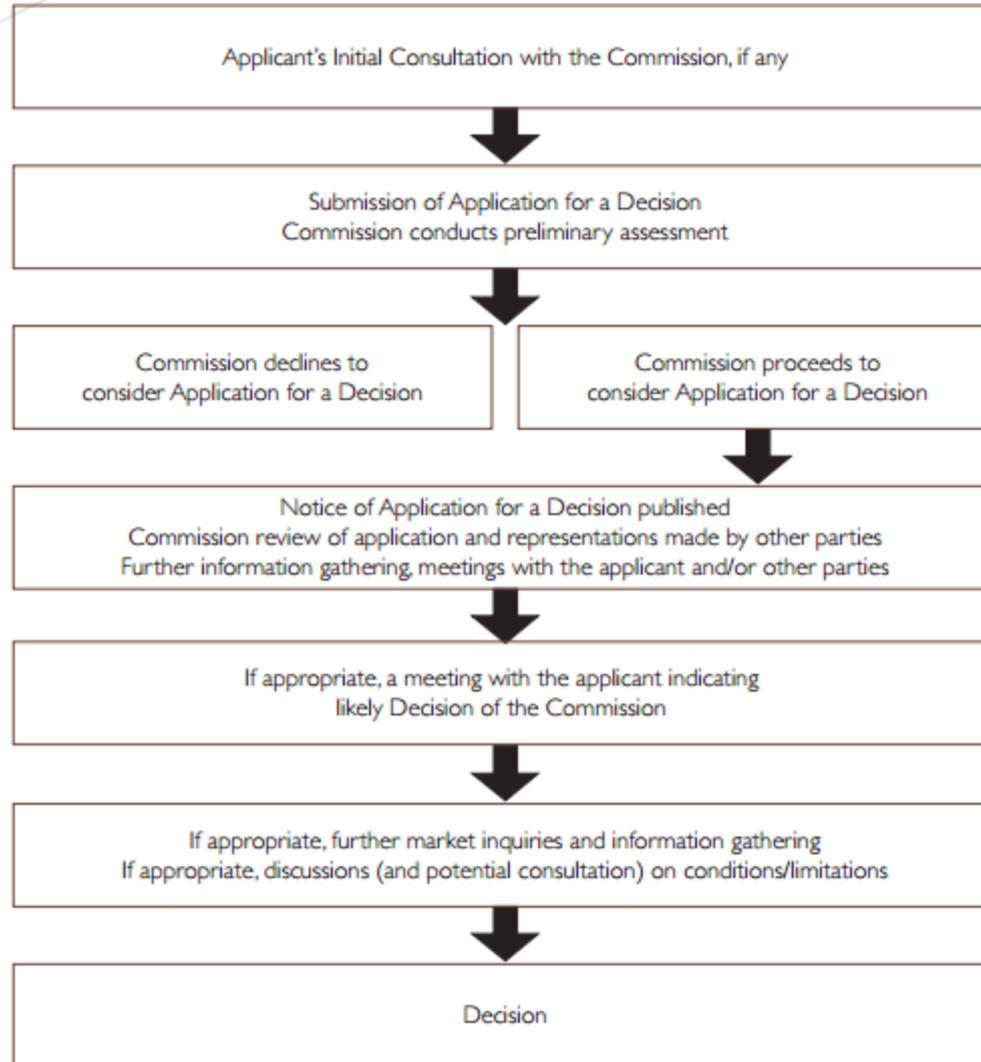
- 2 exemption grounds:
 1. **Public policy exemption** – exceptional and compelling reasons of public policy (s31)
 2. **International obligations exemption** – to avoid a conflict with an international obligation that directly or indirectly relates to Hong Kong (s32)
- Unlike the Schedule 1 exclusions which are listed in the Ordinance, these two exemptions require that the Chief Executive in Council make an order specifying that a particular agreement or conduct or a particular class of agreement or conduct is exempt from the Conduct Rules

First Conduct Rule

How to benefit from the exclusions or exemptions?

- Self-assessment by parties
- Application for decision or block exemption order from CC whether an agreement is excluded or exempted from the application of FCR
- Note: no requirement that there be a decision or block exemption order before undertakings may rely on applicable exclusions or exemptions

Figure 2. Key steps for an Application for a Decision



First Conduct Rule

Initial consultation

- Potential applicants may approach CC for initial consultation before submitting an application for decision
- Information provided to CC during initial consultation (including information protected by legal professional privilege) will not be accepted on a without prejudice basis or for sole purpose of the initial consultation and/or subsequent application
- CC may use such information, with or without notice to interested parties, for other purposes (e.g. enforcement)

First Conduct Rule

Preliminary assessment

- CC will conduct preliminary assessment to determine whether it should decline or proceed with the application for decision
- Relevant factors
 - Whether the application poses novel or unresolved questions of wider importance or public interest in relation to the application for exclusions or exemptions
 - Whether the application raises a question of an exclusion or exemption for which there is no clarification in existing case law or CC's decisions
 - Whether it is possible to make a decision based on the information provided

First Conduct Rule

Preliminary assessment

- If CC declines to consider the application, such outcome is not indicative of CC's position on whether the relevant agreement or conduct
 - Raises a concern under the FCR; or
 - Is or is not excluded or exempt from FCR

First Conduct Rule

Decision of CC

- CC may decide that the agreement or conduct
 - Is not excluded or exempted from FCR
 - Is excluded or exempted from FCR
 - Is excluded or exempted from FCR, subject to conditions or limitations
- Decision that the agreement or conduct is not excluded or exempted from FCR does not necessarily mean that CC has formed a view on whether it has reasonable cause to believe that the agreement or conduct has contravened FCR

First Conduct Rule

Confidentiality

- CC has a general obligation to preserve confidentiality of any confidential information provided to or obtained by it
- BUT CC is permitted to make disclosure in certain circumstances; e.g.
 - With the complainant's consent
 - In the performance of its functions or carrying out in effect or doing anything authorized by the CO
 - In accordance with an order of the CT or any other court
- CC may disclose confidential information without the consent of relevant parties!

First Conduct Rule

Confidentiality

- An applicant may make a claim for confidentiality in respect of information provided to CC in an application
 - Identify relevant information
 - Provide a written statement as to why the applicant considers such information is confidential

First Conduct Rule

Any immunity?

- CO does not provide for any immunity from enforcement action during CC's review of application for decision
- CC may use the information provided in an application and may initiate enforcement action in respect of any agreement or conduct which is the subject of an application
- Unlike Hong Kong, Singapore's application regime provides for temporary immunity → no investigation when application is being reviewed
- Applicants should seek legal advice before making an application for decision

Second Conduct Rule

Section 21 of the Ordinance provides:

“(1) An undertaking that has a substantial degree of market power in a market must not abuse that power by engaging in conduct that has as its object or effect the prevention, restriction or distortion of competition in Hong Kong

(2) For the purpose of subsection (1), conduct may, in particular, constitute such an abuse if it involves-

- a) predatory behavior towards competitors; or*
- b) limiting production, markets or technical development to the prejudice of consumers”*

Second Conduct Rule

- 2-part test to assess whether the Second Conduct Rule applies
 - Whether an undertaking has a substantial degree of market power in a market;
 - If it does, whether it abuses that market power by engaging in conduct that has the object or effect of preventing, restricting or distorting the competition of Hong Kong

Second Conduct Rule

Territorial Application

- SCR applies irrespective of place of the undertaking involved or the place of conduct so long as the conduct has the object or effect of preventing, restricting or distorting competition in Hong Kong

Second Conduct Rule

What is the relevant market?

- Purpose of defining the relevant market – identify the competitive constraints which undertakings face when operating in a market
- 2 dimensions – **product dimension** and **geographic dimension**

Second Conduct Rule

Substantial market power (“SMP”) – market share factor

- Market share analysis → initial screening device in SMP assessment
- Undertakings are more likely to have SMP where they have high market share BUT this is not a definite rule
- Relevant data for market share analysis include:
 - Turnover
 - Sales volume
 - Capacity to supply the relevant market

Second Conduct Rule

Substantial market power (“SMP”) – entry / expansion barrier factor

- Entry/ expansion barriers prevent prospective new entrants from entering the relevant market
- Examples of barriers include:
 - Regulatory and legal barriers (e.g. licensing requirements)
 - Structural barriers
 - Sunk costs (e.g. R&D investment, marketing and ongoing advertising expenses)
 - Scarce important inputs or distribution channels
 - Economies of scale
 - Economies of scope

Second Conduct Rule

Abusive conduct

- Whether the undertaking abuses its substantial degree of market power by engaging in conduct that has the object or effect of preventing, restricting or distorting the competition of Hong Kong
- Whether the undertaking can demonstrate that the conduct is **indispensable** and **proportionate** to the pursuit of some **legitimate objective** unconnected with harming competition; e.g.
 - Refusal to deal may not be abusive where the undertaking with SMP refuses to supply a particular input to a customer because of the customer's poor creditworthiness
 - Below cost pricing may not be abusive where it is a genuine promotional offer of limited duration relating to launch of new product or entry into new market

Second Conduct Rule

Object or effect

- Same interpretation as under the FCR



Second Conduct Rule

Exclusions and exemptions

Relevant exclusion or exemption		Exclusion or exemption from First Conduct Rule	Exclusion or exemption from Second Conduct Rule
General Exclusions	Agreements enhancing overall economic efficiency	✓	
	Compliance with legal requirements	✓	✓
	Services of general economic interest	✓	✓
	Mergers	✓	✓
	Agreements of lesser significance	✓	
	Conduct of lesser significance		✓
Block Exemption Orders		✓	
Public Policy Exemption		✓	✓
International Obligations Exemption		✓	✓
Statutory Body and Specified Person or Activities Exclusions		✓	✓



Making a Complaint to the Competition Commission

- Any person who suspects that an undertaking has contravened, is contravening, or is about to contravene a competition rule may make a complaint to the CC
- Complaints can be in made
 - Directly
 - Anonymously
 - Through an intermediary (e.g. a legal advisor)

Making a Complaint to the Competition Commission

- What information should a complainant include in a complaint?
 - Relevant facts regarding the conduct the complainant is concerned about
 - Documents that relate to the conduct in question
 - Parties involved in the conduct and their contact information
 - Impact of the conduct on the complainant
 - Other parties affected by the conduct – Who are they? How are they affected?
 - Contact details of the complainant

Making a Complaint to the Competition Commission

- Confidentiality of complaints
 - CC has a general obligation to preserve confidentiality of any confidential information provided to or obtained by CC, including the identity of the complainant
 - CC is permitted to make disclosure in certain circumstances; e.g.
 - With the complainant's consent
 - In the performance of its functions or carrying out in effect or doing anything authorized by the CO
 - In accordance with an order of the CT or any other court
 - Complainant should also keep complaint confidential

Making a Complaint to the Competition Commission

- Discretion to decide which complaints warrant investigation
 - Not required to investigate if the CC does not consider it reasonable to do so (e.g. where the complaint is misconceived or lacking in substance)
 - May investigate a complaint even where the complainant no longer wishes to cooperate with the CC
- Possible outcomes after preliminary review of complaint by CC
 - No further action
 - No action but recommend complainant to refer the complaint to another agency
 - Review the matter further by conducting an Initial Assessment (to be further explained later)

Investigation by the Competition Commission

- CC may only conduct an investigation where it has **reasonable cause** to suspect that a contravention of a competition rule has occurred
- “reasonable cause”
 - No statutory definition under the CO
 - Guideline on Investigations
 - Requires the CC to be satisfied, at least beyond mere speculation, that there may have been a contravention of a competition rule
 - Does not require evidence to a standard that, on balance, tends to suggest that a contravention has occurred

Investigation by the Competition Commission

- 2 phases of investigation

- Initial Assessment Phase

- Investigation Phase

Investigation by the Competition Commission

Initial Assessment Phase

- CC has not yet formed a view on whether there is reasonable cause to suspect contravention → seek information on a voluntary basis
 - Contact relevant parties by telephone or in writing
 - Interview persons who may have knowledge of the conduct
 - Review publicly available information; e.g. market surveys and industry reports
- Identify whether
 - It is reasonable to conduct an investigation
 - There is sufficient evidence to establish a reasonable cause to suspect that a contravention of a competition rule has occurred

Investigation by the Competition Commission

Initial Assessment Phase

- Possible outcomes of the Initial Assessment Phase include
 - No further action
 - Commencement of the Investigation Phase
 - Alternative course – refer to another agency
 - Voluntary resolution of the matter (e.g. s.60 Commitment)

Investigation by the Competition Commission

Investigation Phase

- CC will proceed to the Investigation Phase where it has reasonable cause to suspect a contravention of a competition rule
- CC's investigation powers
 - Written request for documents and information (“**s.41 Notice**”)
 - Request for attendance before CC to answer questions (“**s.42 Notice**”)
 - Search warrant (“**s.48 Warrant**”)

Investigation by the Competition Commission

S.41 Notices – Request for documents and information

- CC may issue written notices to any person whom it has reasonable cause to suspect that such person has or may have **possession or control of relevant documents or information** or may otherwise be able to **assist in its investigation**
 - To produce any **document**
 - To provide any **specified information**
- CC may also
 - **Make copies** of or **take extracts** from documents
 - Require an **explanation** of the document
 - Where a document is not produced, require the person to state the location of such document

Investigation by the Competition Commission

S.42 Notices – Request for attendance before CC to answer questions

- CC may issue written notice to require any person to appear before it to answer questions relating to any matter which CC reasonably believes to be relevant to an investigation
- To whom s.42 Notices may be issued?
 - Current or former employees, competitors, customers, distributors or suppliers of the parties under investigation
 - Representatives of relevant trade associations
 - Complainants
- Any person appearing before CC may be accompanied and represented by a legal advisor admitted to practise law in Hong Kong

Investigation by the Competition Commission

S.48 Warrant

- Upon application by CC, the Court may issue a warrant to allow CC to **enter and search** any premises to obtain documents, information and other items relevant to its investigation
- When will CC apply for a warrant?
 - **Secretive conduct** is involved
 - Relevant documents or information may be **destroyed or interfered with** if CC seeks them through other means
 - CC has been **unsuccessful in obtaining documents or information** or suspects **non-compliance with an earlier request** for such documents or information

Investigation by the Competition Commission

S.48 Warrant

- What are the powers conferred by a warrant?
 - **Use of reasonable force** to gain entry and/or access evidence on the premises
 - **Removal of obstructions** to the execution of warrant
 - Taking of necessary action and steps to **preserve** relevant documents or information
- CC may retain evidence found during the search for as long as necessary for its investigation and/or any ensuing legal proceedings

Investigation by the Competition Commission

Sanctions for non-compliance

- Failure to comply without reasonable excuse with any requirement under CC's investigation powers → criminal offence
 - Maximum fine: HK\$200,000
 - Imprisonment: 1 year
- Other relevant criminal offences include:
 - Provision of false or misleading information
 - Destruction, falsification or concealment of documents
 - Obstruction of search
 - Disclosure of confidential information received from CC

Maximum fine: HK\$1 million; imprisonment: 2 years

Investigation by the Competition Commission

Confidentiality and disclosure

- Same confidentiality obligations as handling complaints
- Information obtained by CC in one matter may be used in another matter → information or documents **cannot be provided to the CC on a without prejudice or limited waiver basis** unless the CC expressly agrees to do so

Investigation by the Competition Commission

Possible outcomes of Investigation Phase

- Enforcement action to be taken by CC depends on
 - Responses of the undertakings subject to investigation
 - Nature of violation

Investigation by the Competition Commission

Possible outcomes of Investigation Phase

- **No further action** (e.g. where parties alter any conduct of concern in response to CC's enquiries)
- **Accept a s.60 Commitment**
 - CC may accept a commitment to take/ refrain from taking any action from parties under investigation and agree to terminate investigation and not to bring proceedings in the CT
 - Commitment will be published in a register
 - Withdrawal of acceptance of commitment
 - Material change of circumstances
 - Reasonable grounds to suspect (i) non-compliance with commitment or (ii) commitment based on incomplete, false or misleading information

Investigation by the Competition Commission

Possible outcomes of Investigation Phase

- **Violations of FCR which involve serious anti-competitive conducts or violations of SCR**
 - CC may issue an **infringement notice**
 - Sets out conditions in compliance of which CC will not bring proceedings in CT
 - Failure to comply with conditions → CC may commence proceedings in CT
 - CC may bring **infringement proceedings** in CT
 - Note: infringement notice is NOT a pre-requisite to the commencement of proceedings in CT

Investigation by the Competition Commission

Possible outcomes of Investigation Phase

- **Violations of FCR which do NOT involve serious anti-competitive conduct**
 - CC **must** issue a **warning notice** to the undertaking before bringing proceedings in CT
 - The warning notice requires the undertaking to cease the contravening conducts within a warning period
 - CC may bring proceedings in CT if undertaking continues contravening conducts after the warning period

Enforcement and Sanction

- CC: Remedial goals:
 - Swift end to illegal conduct
 - Undo any harm caused
 - Encourage effective compliance
 - Deterrence
 - Consistency
 - Proportionality

Enforcement and Sanction

- CC will target anti-competitive conduct that is clearly harmful
- Enforcement Priorities
 - Cartel conduct
 - Other agreements contravening FCR causing significant harm to competition in HK and
 - Abuses of substantial market power involving exclusionary behaviour by incumbents
- CC may also prioritize taking action against:
 - Associations of undertakings; and/or
 - Officers (as defined in CO). Including directors and managers of undertakings

Enforcement and Sanction

Public enforcement – leniency regime

- CC: Leniency policy – for individuals and corporations
 - S80 of CO: CC may make a leniency agreement with a person that it will not bring or continue proceedings in the Competition Tribunal for a pecuniary penalty in exchange for the person's cooperation in an investigation or in proceedings under the CO.

Enforcement and Sanction

- Cartel leniency policy
 - In the public interest that leniency should be accorded to an undertaking which is willing to terminate its participation in cartel conduct, report that conduct to CC and cooperate, at that undertaking's own cost, in the bringing of proceedings against other parties to the cartel.
 - Incentive for a cartel member to stop the cartel conduct and report the cartel to CC
 - Only in respect of cartel conduct (FCR)
 - Available only for the first cartel member who reports and meet all the requirements for receiving leniency
 - The only way to apply for leniency under the Cartel Leniency Policy is to call the Leniency Hotline

Enforcement and Sanction

- CC is responsible for the application and enforcement of the CO
- CC may become aware of potential contraventions of the CO in various ways; e.g.
 - Receiving complaints from the public
 - Research and market intelligence gathering by CC
 - Referral by the Government, the courts or other statutory bodies of potentially anti-competitive conduct

Enforcement and Sanction

Private enforcement

- “Follow-on actions”
 - Persons who have suffered loss or damage as a result of contravention of the conduct rules will have a right of action against any person who has contravened or involved in the contravention of the conduct rules
- Applicable to
 - Beneficiaries of leniency agreements
 - Parties who have admitted to an infringement as part of settlement procedure

Enforcement and Sanctions

The Competition Tribunal (競爭事務審裁處)

- Extensive sanction powers, e.g.:-
 - To impose sanctions, order redress
 - To hear appeals against CC's decisions regarding exemptions, exclusions, commitments and leniency
 - To adjudicate private follow-on damages actions and make compensation orders

Enforcement and Sanction

Fines

- If CT is satisfied of the contravention of a competition rule, it may order pecuniary penalty
- Relevant factors in determining the amount of pecuniary penalty:
 - The nature and extent of the contravening conduct
 - The loss or damage caused by the conduct
 - The circumstances in which the conduct took place
 - Whether the person has previously been found by CT to have contravened CO

Enforcement and Sanction

Fines

- Maximum penalty for a “single contravention” – 10% of the turnover of the undertaking concerned in HK for each year the infringement lasted; maximum 3 years
- For contravention > 3 years – 10% of the turnover of the undertaking concerned for the 3 years in which the contravention occurred that saw the highest, 2nd highest and 3rd highest turnover

Enforcement and Sanction

Other orders include

- Disqualification of responsible directors for up to 5 years
- Award injunctions
- Declaration that agreement to be void
- Award damages
- Confiscation of illegal profits
- Order to pay costs of CC's investigation



Complying with the CO

- Different business and industries will face different competition law risks. All business should be aware of the risk of serious anti-competitive conduct:
 - Price fixing
 - Output restriction
 - Market sharing
 - Bid-rigging
- Does information sharing raises competition law concerns. Is competitively sensitive information shared between competitors?
- Vertical agreements - risks arising from resale price restrictions or where one party to the vertical agreement has market power.

Complying with the CO

- Identify risks
 - Review business practices to identify and classify competition law risks
- Mitigate risks
 - Develop and adopt appropriate controls (protocol, training) to mitigate and manage the identified risks.
- Regular review
 - Monitor and review business practices on an on-going basis, accounting for changes in the market.

Hong Kong's First Competition Law case to the CT

- CTEA1/2017
- 23 March 2017
- Originating Notice of application - 24 pages, 81 paragraphs
- Against 5 IT companies
 - Supplier of IT products (one)
 - Distributor and re-seller of the Supplier's IT products (the other four)
- CC has reasonable cause to believe that the 5 respondents have contravened the FCR by engaging in bid-rigging in a tender conducted by an NGO in July 2016 for the supply and installation of an information technology server system (a "hyper-converged system" based on Nutanix technology)

Hong Kong's First Competition Law case to the CT

- Reliefs sought
 - Pecuniary penalty
 - Declaration that each of the 5 respondents has contravened the FCR
 - Legal costs
 - Further or other relief as the CT may consider appropriate
- Still on going

Hong Kong's First Competition Law case to the CT

- Tendering process
 - The expectation on the part of the body conducting the tender that it will receive, as a response to its tender, a number of independently articulated bids formulated by contractors wholly independent of each other.
 - Concentration by bidders regarding the manner in which they intend responding to an invitation to tender is anti-competitive.
 - The competitive tendering process may be interfered with if the tenders submitted are not the result of individual economic calculation but of knowledge of the tenders by other participants or concentration between participants.

Hong Kong's First Competition Law case to the CT

- Cover bid
 - Anti-competitive bidding
 - Not intended to win the contract but gives the impression to the body conducting the tender that it is a genuine competitive tender.
 - Submission of a cover bid restricts competition because it reduces the number of competitive bids submitted in respect of that particular tender.
- As a selective tendering process by its nature has a restricted number of bidders, any interference with the selected bidders' independence can result in significant distortions of competition.

Hong Kong's First Competition Law case to the CT

- Allegations
 - NGO wants to procure IT server system
 - Procurement policy requires that goods, services or works exceeding certain financial thresholds must be conducted through a tender with a minimum requirement of 5 tenders.
 - If less than 5 tenders are received, the award of contract must be approved by both the NGO's finance and administration committee and the Tender board.
 - NGO invited 12 companies to tender, including 2 of the 5 respondents. But there was only 1 bid (one of the 5 respondents).

Hong Kong's First Competition Law case to the CT

- Allegations
 - Dissatisfied with receiving only 1 bid for the first tender, NGO conducted a 2nd tender, again on a selective basis.
 - NGO invited 9 companies to tender, including 4 of the 5 Respondents and one other company.
 - Some of the mandatory terms included in the list of core project items of the First tender were changed to optional terms in the 2nd tender.
 - This time, NGO received 4 bids from 4 of the 5 Respondents.
 - The same respondent from the First Tender submitted the lowest bid for the mandatory items and was the only bid to include a quote for optional items.

Hong Kong's First Competition Law case to the CT

- Allegations
 - The 4 bids have unusual features:
 - A high degree of consistency in the substance and format of the bids including common mistakes and omission of key information
 - Identical responses, typographical errors and common alterations made to the original forms and documents in the submitted bids.
 - Breach of FCR:
 - Anti-competitive vertical bilateral arrangements between the supplier respondent and the respective other respondents as reseller or distributor of the supplier's products.
 - An anti-competitive trilateral arrangement between the supplier respondent and 2 re-seller respondents.
 - There were interviews
 - Emails and Whatsapp messages were obtained
 - There were arrangements between the respondents for NGO to obtain 4 "dummy bids" i.e. not genuine bids to fulfil NGO's requirement for 5 tenders for the 2nd Tender.

Hong Kong's First Competition Law case to the CT

Takeaways:

- Bid rigging – one of the top priorities
- CC exercised its investigation powers:
 - Search and seizure
 - Imaging of computers for emails and smartphones for instant messages
 - Interviewing people and taking of statements
- Act on complaints

Hong Kong's First Competition Law case to the CT

Takeaways:

- S.6 of the Prevention of Bribery Ordinance (Cap 201) – Bribery for procuring withdrawal of tenders

(1) Any person who, without lawful authority or reasonable excuse, offers any advantage to any other person as an inducement to or a reward for or otherwise on account of the withdrawal of a tender, or the refraining from the making of a tender, for any contract with a public body for the performance of any work, the providing of any service, the doing of any thing or the supplying of any article, material or substance, shall be guilty of an offence.

(2) Any person who, without lawful authority or reasonable excuse, solicits or accepts any advantage as an inducement to or a reward for or otherwise on account of the withdrawal of a tender, or the refraining from the making of a tender, for such a contract as is referred to in subsection (1), shall be guilty of an offence.

Hong Kong's First Competition Law case to the CT

Takeaways:

- S.7 of the Prevention of Bribery Ordinance (Cap 201) – Bribery in relation to auctions
- (1) Any person who, without lawful authority or reasonable excuse, offers any advantage to any other person as an inducement to or reward for or otherwise on account of that other person's refraining or having refrained from bidding at any auction conducted by or on behalf of any public body, shall be guilty of an offence.
 - (2) Any person who, without lawful authority or reasonable excuse, solicits or accepts any advantage as an inducement to or reward for or otherwise on account of his refraining or having refrained from bidding at any auction conducted by or on behalf of any public body, shall be guilty of an offence.



Q & A



Thank you!



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