

Draft Hong Kong Competition Guidelines Released for Public Comment

Industry has an opportunity to comment on the Competition Commission's proposed Guidelines on how it intends to interpret and enforce the conduct rules in Hong Kong's Competition Ordinance.

Introduction

Hong Kong's Competition Ordinance (Chapter 619 of the Laws of Hong Kong) (the Ordinance) was enacted in June 2012, but is still not yet fully in force. The objective of the Ordinance is to prohibit conduct that prevents, restricts or distorts competition, and mergers (in the telecommunications market only) that substantially lessen competition in Hong Kong. The Ordinance also sets out how anti-competitive conduct will be investigated, enforced and sanctioned by the Competition Commission (Commission), the independent statutory body established to enforce the Ordinance.

Before the Ordinance comes into full force, the Ordinance expressly requires that the Commission issue guidelines indicating the manner in which it expects to interpret and give effect to the conduct rules; the manner and form in which it will receive applications for a decision or block exemption order; and indicating how it expects to exercise its power to make a decision or grant block exemptions (Section 35 of the Ordinance).

On 9 October 2014, the Commission took this next step in the process which will ultimately lead to the introduction of broad, industry-wide competition laws in Hong Kong and released, jointly with the Communications Authority (Authority) (the independent statutory body regulating the telecommunications and broadcasting industry sectors), six draft competition guidelines (Draft Guidelines) for public comment. In drafting the Guidelines, the Commission aims to assist businesses operating in Hong Kong to familiarize themselves with competition law and its underlying policies, as embodied in the Ordinance.

The Draft Guidelines are divided into two categories:

- Substantive Guidelines on (i) the First Conduct Rule; (ii) the Second Conduct Rule; and (iii) the Merger Rule
- Procedural Guidelines on (i) Complaints; (ii) Investigations; and (iii) Applications for a Decision under Sections 9 and 24 of the Ordinance (Exclusions and Exemptions) and for a Block Exemption Order under Section 15 of the Ordinance (Block Exemption)

The Draft Guidelines are intended to provide general guidance on how the Commission and/or the Authority propose to interpret and administer the Ordinance. When finalized, the Guidelines will not represent the law — the Competition Tribunal (Tribunal) and other courts will not be bound by the Guidelines and will, ultimately, be responsible for deciding on the meaning of the Ordinance's

provisions and the approach to enforcing those provisions. The Commission and the Authority may revisit the Guidelines in time having regard to decisions of the Tribunal and other courts, developments in international best practice, and the Commission's and the Authority's experience in enforcing the Ordinance in specific cases.

The Draft Guidelines

Draft Guideline on the First Conduct Rule

The First Conduct Rule applies to anti-competitive arrangements between two or more different parties (including parties who are not competitors) that have or are likely to have the object or effect of preventing, restricting or distorting competition (*i.e.*, harming competition) in Hong Kong. The First Conduct Rule captures both horizontal and vertical arrangements with (or likely to have) such object or effect.

The Draft Guideline on the First Conduct Rule sets out the manner in which the Commission expects to interpret and give effect to the First Conduct Rule and outlines the implications where an agreement that has the object or effect of preventing, restricting or distorting competition is also found to amount to serious anti-competitive conduct (SAC).

The Draft Guideline sets out the Commission's view that vertical agreements (*i.e.*, those between buyers and sellers) are inherently less likely to harm competition than horizontal agreements (*i.e.*, arrangements between competitors). Both forms of agreement, the Commission suggests, would be covered by the anti-competition provisions of the Ordinance, but vertical agreements are only likely to be found to harm competition where the parties to the arrangement have some measure of market power (which is addressed under the Second Conduct Rule).

However, the Commission notes that it generally views one specific group of vertical arrangements — resale price maintenance (RPM) arrangements — as being, by their nature, harmful to competition. An RPM agreement is an arrangement whereby a supplier requires a retailer (or distributor) not to sell its products below a certain price or an arrangement that fixes the price at which the retailer may sell. The Commission notes that it will take it that undertakings engaging in such conduct which cannot defend their RPM practices on efficiency grounds are engaging in anti-competitive conduct in breach of the Ordinance. In certain cases, RPM arrangements may also amount to SAC. Recommended resale price or maximum resale price arrangements are, however, less likely to give rise to concerns.

In addition, the Draft Guideline on the First Conduct Rule also:

- Provides examples to illustrate how information exchanges, trade association price recommendations and fee scales set by professional bodies may contravene the First Conduct Rule
- Outlines the Commission's approach to interpreting the provisions of the Ordinance relating to exclusions and exemptions

Draft Guideline on the Second Conduct Rule

The Second Conduct Rule applies where an undertaking, with a substantial degree of power in a market, abuses its market power by engaging in conduct that has as its object or effect the prevention, restriction or distortion of competition in Hong Kong.

The Draft Guideline on the Second Conduct Rule explains the Commission's proposed approach to (i) defining the relevant market; and (ii) assessing substantial market power.

With respect to market definition, the Commission's proposed approach follows international best practice and is consistent with the Ordinance, incorporating factors such as product and geographic market boundaries. The definition of the market will depend on the specific facts of the conduct in question, and may in a particular instance be global, regional or smaller than Hong Kong.

With respect to the definition of substantial market power, the Commission proposes taking an economic approach, and does not identify any thresholds above (or below) which substantial market power will be presumed (or not). Rather, the Commission proposes to adopt the internationally recognized test for ascertaining whether an undertaking has substantial market power, by looking to that undertaking's ability to act with minimal regard to competitive constraint. In considering that test, market share is a relevant factor, but will not be conclusive. Other factors will include ease of entry or expansion, and buyer power.

Undertakings with turnover not exceeding HK\$40 million are exempt from the operation of the Second Conduct Rule.

The Draft Guideline provides guidance on what the Commission may consider when investigating cases of alleged abuse of substantial market power, and sets out examples of the types of conduct that the Commission may consider to be an abuse of a substantial degree of market power. The Draft Guideline also discusses the general exclusions and other statutory exclusions and exemptions which are applicable in relation to the Second Conduct Rule.

The Commission notes that, if an undertaking with substantial market power abuses that power through an arrangement such as a vertical restraint, the undertaking may contravene both the First and Second Conduct Rules, depending on the facts of the case.

Draft Guideline on the Merger Rule

The Merger Rule prohibits mergers that have, or are likely to have, the effect of substantially lessening competition in Hong Kong. The Merger Rule only applies to mergers involving, directly or indirectly, holders of carrier licences under the Telecommunications Ordinance.

The Draft Guideline on the Merger Rule sets out the Commission's and the Authority's interpretation of the Merger Rule and related provisions under the Ordinance, and their proposed approach in applying the same. In this regard, the Draft Guideline discusses:

- The scope of the Merger Rule
- The proposed approach for conducting a competition assessment, with indicative safe harbours to enable parties to self-assess whether a proposed transaction may raise competition concerns under the Merger Rule

The Draft Guideline on the Merger Rule also explains how undertakings can seek informal, confidential advice from the Commission on a proposed merger transaction, the formal processes by which the Commission may review merger transactions, as well as the Commission's powers to formally investigate anticipated and completed mergers.

Draft Guideline on Complaints and Draft Guideline on Investigations

The Draft Guideline on Complaints is largely procedural, providing guidance on the manner and form in which complaints are to be made to the Commission and incorporating information on the processes the Commission will use for determining what action to take in relation to a complaint or a query received from the public.

The Draft Guideline on Investigations provides an outline of how the Commission will gather evidence to assess whether it has reasonable cause to suspect that certain conduct contravenes the Ordinance. If the Commission determines that there is “reasonable cause”, it may exercise its compulsory evidence gathering powers under the Ordinance. The Draft Investigations Guideline supplements the detailed provisions contained in the Ordinance on the exercise of the Commission’s investigatory powers. These include powers to request documents and information, to request attendance before the Commission to answer questions and to enter and search premises under warrant.

Together, the two Draft Guidelines provide an outline of the proposed three-stage investigative process:

- (1) Receiving and assessing a complaint
- (2) An initial assessment phase
- (3) An investigation phase

The Draft Guidelines do not outline how the Commission will prioritise enforcement or select which enforcement tool is appropriate in a given circumstance. This, the Commission indicates, will be the subject of a separate policy, to be released subsequently.

Draft Guideline on Applications for a Decision under Sections 9 and 24 (Exclusions and Exemptions) and Section 15 Block Exemption Orders (the Applications Guideline)

The Ordinance contains a number of exclusions and exemptions. Once the Ordinance comes into full operation, the Commission will be empowered to:

- Make decisions as to whether a specific agreement or conduct is excluded or exempt from the Conduct Rules upon the application to the Commission for a decision in respect of the same by an undertaking (Decisions)
- Issue Block Exemption Orders, exempting categories of agreements that enhance overall economic efficiency from the operation of the Conduct Rules

The Commission indicates that it will only exercise such powers (in particular, block exemption powers) in limited circumstances.

The Draft Applications Guideline provides general guidance on the:

- Procedure to follow in applying for a Decision or a Block Exemption Order
- Process that the Commission will follow in making Decisions and issuing Block Exemption Orders, including how the Commission intends to (i) apply its discretion on whether to accept an application; and (ii) exercise its power to issue Block Exemption Orders of its own volition

The way forward

Businesses and members of the public have been invited to submit their comments on (i) the Procedural Guidelines by 10 November 2014; and (ii) the Substantive Guidelines by 10 December 2014.

Following the public consultation, the Commission will refine the current Draft Guidelines and produce final draft Guidelines for consultation with the Legislative Council and other appropriate persons. The Commission will then adopt and issue the Guidelines. This will pave the way for full implementation of

the Ordinance. Currently, full implementation is not anticipated until the second half of 2015 at the earliest.

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