Hong Kong Competition Commission publishes revised draft guidelines

In October 2014, the Hong Kong Competition Commission (the “Commission”) published, for public comment, draft procedural and substantive guidelines on its interpretation of the Competition Ordinance (the “Draft Guidelines”). Forty-nine interested parties, including Slaughter and May, submitted comments on these to the Commission.

On 30 March 2015, the Commission published revised draft guidelines (the “Revised Guidelines”). Overall, the changes provide further clarification and hypothetical examples to assist in the practical application of the First Conduct Rule ("FCR") and Second Conduct Rule ("SCR"), most of which are uncontroversial. While the Commission has not changed its position on some fundamental questions (such as providing an indicative market share threshold for a substantial degree of market power), it has generally given careful consideration to the comments it received, as reflected in the Revised Guidelines.

The Commission has invited comments before 20 April 2015 and currently plans to present the Revised Guidelines to the Legislative Council for consultation on 27 April 2015.

The Commission has not as yet published guidelines on its leniency policy or enforcement priorities. It is understood that these will be released in the coming months prior to the implementation of the Competition Ordinance.

SUBSTANTIVE GUIDELINES

1. Guideline on FCR

The Commission has made several important changes to the guideline concerning the FCR. The key amendments are discussed below.

1.1 Definition of “concerted practice”

A number of interested parties informed the Commission that the definition provided for a “concerted practice” in the Draft Guideline on the FCR was not clearly distinguishable from that of “agreement”.

The Revised Guideline on the FCR reaffirms that a concerted practice is a form of cooperation “falling short of an agreement” and clarifies that it generally involves the exchange of competitively sensitive information, which may have an anti-competitive object or effect.
The Revised Guideline states that, similar to the rules on information exchange (discussed below), a concerted practice involving future prices or pricing strategy ("pricing information") will amount to an object infringement of the FCR where:

– it is disclosed with the expectation/intention that the recipient will act on the information when determining their market conduct; and

– the recipient does act/intends to act on the information.¹

1.2 Agreements that have the effect of harming competition

The Draft Guideline stated that whether a horizontal or vertical agreement has anti-competitive effects will depend on a number of factors, including the "extent to which the parties individually or jointly have or obtain some degree of market power" (emphasis added).

A number of interested parties asked the Commission for further guidance on this point and, in particular, for indicative safe harbours (which are common in other jurisdictions) to be included in the Revised Guideline.

This, however, has not been included in the Revised Guideline. Therefore in order to establish if a particular agreement has anti-competitive effects, businesses will have to conduct a more detailed assessment including factors such as the parties' market shares, market concentration, market barriers to entry or expansion and whether there is any countervailing buyer/supplier power.

1.3 Agreements must have an appreciable effect on competition

Whilst the Commission notes that the Competition Ordinance does not include an "appreciability" or "materiality" test², it was willing to include in the Revised Guideline that agreements that do not amount to object infringements of the FCR will only infringe it where their effect on competition is "more than minimal". As part of its assessment, the Commission will take into consideration the cumulative effect on competition of similar agreements in the market as well as the agreement’s contribution to the cumulative effect.³

1.4 Serious Anti-competitive Conduct ("SAC")

The Commission has clarified in the Revised Guideline that whether an agreement amounts to SAC is not part of its assessment on whether the agreement infringes the FCR: it is only relevant once the Commission has established that the FCR has been infringed.

Importantly, the Commission has explicitly stated that SAC includes agreements that are either the object or effect of harming competition.⁴

---

¹ Paragraph 2.28.
³ Paragraph 3.27 – 3.28.
⁴ Paragraph 5.7.
1.5  **Resale price maintenance ("RPM")**

While the Commission has retained its position on RPM, it appears to have softened the wording of its guidance in light of comments received from interested parties. Importantly, the Revised Guideline states that:

- Such agreements “may” amount to an object restriction. Whether this is the case will depend on the content of the agreement, how it has been implemented as well as the relevant context.

- All RPM arrangements (i.e. both those that have an anti-competitive object or effect) do not automatically contravene the FCR and can benefit from the efficiencies exclusion.

- RPM can amount to SAC in certain circumstances. The Commission has provided some clarity on this point through Hypothetical Example 16.

1.6  **Information exchange**

The Revised Guideline has clarified how information exchanges will be assessed by the Commission in several ways.

- The Commission, in response to comments received, has explicitly recognised that information exchanges can be pro-competitive. The Revised Guideline notes that "competition is often enhanced through the sharing of information, for example, in relation to best practices or exchanges of information which allow firms to better predict how demand is likely to evolve."

- The Commission has clarified that an information exchange between competitors will amount to an object infringement where it occurs "in private" and it concerns pricing information.

Further, a number of interested parties requested that the Commission clarify when an indirect information exchange (i.e. an exchange which is effected by a third party) could give rise to competition concerns so as not to unfairly inhibit legitimate commercial dealings between suppliers and distributors. The Revised Guideline clarifies that, consistent with the position in the UK, such an indirect information exchange can amount to an agreement or might form part of a concerted practice, if:

i. Company A provides the information to a third party intending for the third party to make use of the information to "influence market conditions" by passing it to a competitor;

ii. the third party shares the information with Company B (a competitor of Company A); and

iii. Company B uses the information to determine its conduct in the market.

---

5 The Draft Guideline said that such agreements would amount to Revised Guidelines provides several examples of when RPM will amount to a restriction by object including when it is instigated by a distributor who seeks to persuade its supplier to impose RPM on the distributor’s competitors.

6 If this is not the case the arrangement’s effects are considered. See Paragraph 6.76 et seq.

7 Paragraph 6.84.

8 Paragraph 5.6.

9 Paragraph 6.38.

10 Paragraph 6.40.

11 Such an agreement may amount to an object infringement if it concerns the sharing of pricing information.

12 Paragraph 6.43.
1.7 Vertical agreements

The Draft Guideline provided limited guidance in relation to only two vertical agreements: exclusive distribution and exclusive customer allocation.

As a welcome response to public comments, the Revised Guideline now contains additional guidance on franchise and selective distribution arrangements, both of which are common in Hong Kong. In short, the Revised Guideline notes that:

- franchise agreements will not raise concerns to the extent that they contain measures either to maintain the identity and reputation of the franchise network or to protect the franchisor’s branding and know how. Other restrictions, however, may infringe the FCR if they have the object or effect of harming competition;\(^{13}\) and

- selective distribution agreements will not raise concerns where the supplier selects retailers based purely on qualitative criteria. The use of other conditions (e.g. quantitative criteria such as sales targets) may however have anti-competitive effects.\(^ {14}\)

1.8 Joint ventures

Similar to the above, the Draft Guideline provided guidance only in relation to production joint ventures.

The Revised Guideline provides businesses with useful additional guidance on joint tendering and joint selling, distribution and marketing agreements. In short, the Revised Guideline notes that:

- joint tendering agreements will not generally be considered to have an anti-competitive object but may have an anti-competitive effect where the parties could have made independent bids;\(^ {15}\) and

- sales-related joint ventures can have the object of harming competition, particularly where they lead to price fixing, output restriction or market sharing. Even where this is not the case, such arrangements can have an anti-competitive effect, for example if competitively sensitive information is shared which goes beyond what is necessary to implement the agreement.\(^ {16}\)

1.9 Principal/Agent relationship

The Commission has further clarified what constitutes a “genuine” agency agreement in the Revised Guideline which states that a distributor acts as a true agent of the supplier if it “does not bear any, or bears only insignificant, risks in relation to the contract concluded on behalf of the principal”. This may be the case where the title to the contract products is not transferred to the distributor and the distributor does not bear any, or only an insignificant proportion of, costs or risks (e.g. distribution (i.e. transport) costs, advertising/promotional costs, risks associated with customer non-performance etc.).\(^ {17}\)
1.10 **Collective bargaining**

The Revised Guideline clarifies that discussions and arrangements between employees (or their trade unions) and employers concerning their employment terms (e.g. salary and other working conditions) fall outside the scope of the FCR.\(^{18}\)

2. **Guideline on SCR**

The Commission has made several important clarifications to the guideline concerning the SCR, which are discussed below.

2.1 **Definition of “substantial degree of market power” (“SDMP”)**

One of the key comments almost unanimously made by interested parties was for an indicative market share threshold to be included in the Revised Guideline on the SCR, which would enable businesses to carry out effective risk assessments of their business(es).

The Commission however has not included an indicative market share threshold in the Revised Guideline given that other factors, such as the ease of entry and expansion in the relevant market, supply-side substitution and buyer power, also need to be taken into account by the Commission.\(^{19}\)

2.2 **The Commission’s approach to SCR cases**

The Commission has clarified that, in line with the wording of the Competition Ordinance, abusive conduct can have an anti-competitive object or effect. The Commission therefore has rejected the request of certain interested parties to assess all conduct by reference to its effects on competition. To illustrate this, the Commission has included exclusive dealing arrangements as an additional example of conduct (together with predatory pricing) which would mount to a restriction by object in the Revised Guideline.\(^{20}\)

We do not necessarily expect that this suggests the Commission will adopt the form-based approach of the European Courts.\(^{21}\) However, this is only the interpretation of the Commission and does not bind the Competition Tribunal, who will ultimately decide whether an infringement has occurred.

2.3 **Clarity on whether the SCR covers “exploitative” conduct**

A number of interested parties sought clarity in relation to whether the SCR covered “exploitative” abuses (conduct which exploits consumers, such as excessive pricing) as well as “exclusionary” abuses (conduct that excludes or forecloses actual or potential competitors, such as predatory pricing etc.).

The Commission has indicated that it will focus on exclusionary conduct which may harm the “process of competition”.\(^{22}\)

---

\(^{18}\) Paragraphs 2.18 – 2.19.

\(^{19}\) The Commission’s reasons are set out in paragraph 31 of the Commission’s Guide to the Revised Draft Guidelines.

\(^{20}\) See Paragraph 4.15.

\(^{21}\) For example, paragraph 4.7 notes that when considering whether conduct has the object of harming competition regard will be had to the nature of the conduct as well as the economic and legal context.

\(^{22}\) Paragraph 4.20.
2.4 **Objective justification ‘defence’**

The Commission recognised the availability of this defence in the Draft Guideline which stated that "the Commission may consider whether the undertaking is able to demonstrate that the concerned conduct is indispensable and proportionate to the pursuit of some legitimate objective" (emphasis added).

In response to comments for further clarification, the Revised Guideline:

- provides an extra example, which states that an undertaking with a SDMP may not infringe the SCR where it refuses to supply a particular input to a customer because the customer is, as an objective matter, insufficiently creditworthy,\(^\text{23}\) and

- despite the fact that the efficiencies exclusion\(^\text{24}\) only applies to the FCR, it has opened the door to undertakings to argue that there has been no infringement of the SCR where the conduct entails efficiencies sufficient to guarantee no net harm to consumers.\(^\text{25}\)

3. **Guideline on Merger Rule**

The Commission has made minor changes to the guidelines on the Merger Rule, which only applies to companies that hold a carrier licence.\(^\text{26}\)

3.1 **Transactions subject to the Merger Rule**

The Commission has adopted the following definition of “decisive influence” – which mirrors that used for purposes of the EU Merger Regulation – in the Revised Guideline:

“Decisive influence” … refers to the power to determine decisions (including the making or vetoing of such decisions) relating to the strategic commercial behaviour of an undertaking, such as the budget, the business plan, major investments or the appointment of senior management.”\(^\text{27}\)

**PROCEDURAL GUIDELINES**

4. **Guideline on Complaints**

The Revised Guideline continues to include very few restrictions on the manner in which complaints can be made. For policy reasons, the Commission did not wish to reduce the possible sources of information about possible anti-competitive conduct. For example, complainants need not have a "legitimate interest" in the complaint, may make complaints anonymously and are not required to follow any “checklist” of information that must be provided in support of a complaint.

\(^{23}\) Paragraph 4.4.  
\(^{24}\) Section 1 of Schedule 1 to the Competition Ordinance.  
\(^{25}\) Paragraph 4.5.  
\(^{26}\) Section 4 of Schedule 7 to the Competition Ordinance.  
\(^{27}\) Paragraph 2.7.
5. Guideline on Investigations

5.1 Claims of confidentiality

The Commission emphasises in the Revised Guideline that it will not look kindly upon a broad brush approach to claims of confidentiality, referring numerous times to the need for parties to clearly specify their reasons for claiming confidentiality.28

5.2 Changes for greater transparency

To some extent, the Commission has responded to calls to increase transparency in the investigations process. The Revised Guideline specifies, for example, that the Commission will generally endeavour to keep both companies under investigation29 and complainants30 informed of the progress of the investigation. The Commission also committed to establishing and publishing a procedure for dealing with disputes in respect to claims to legal professional privilege.31

6. Applications for a Decision under Sections 9 and 24 (Exclusions and Exemptions) and Section 15 Block Exemption Orders

6.1 Timing of the decisions / block exemptions process

The Commission chose not to include indicative timeframes for the applications / block exemptions process despite many calls to do so. Its justification was that although it will "endeavour to work efficiently", the timeframe will depend on factors such as "the complexity of the issues raised, the number of parties who have an interest in the decision and who also need to be consulted, and the resources available to be devoted to the review".32 Whilst this is perhaps understandable, as the Commission does not yet have an established practice as to its review process, it means that potential applicants will have to make their application without any indication as to how long the review may take.

6.2 Information provided to the Commission may be used in an investigation

The Commission refused to soften its stance that information provided in the context of an application for a decision or a block exemption (including during an initial consultation with the Commission) may be used by the Commission for investigative or enforcement purposes.33 Companies would therefore be well advised to consider whether they are willing to take this risk before voluntarily providing information to the Commission.

28 Paragraphs 6.7 and 6.12.
29 Paragraph 3.5.
30 Paragraph 4.4.
31 Paragraph 5.40.
33 Paragraph 4.1.
7. **Links to the Revised Guidelines**

A link to each of the Commission’s Revised Guidelines is set out below:


