The Link Management Limited 領匯管理有限公司

Manager of The Link REIT

9 December 2014

THE COMPETITION COMMISSION
36/F., Wu Chung House,
197-213 Queen's Road East,
Wanchai,
Hong Kong.

By post and also
by email: submissions@compcomm.hk

Dear Sirs,

Response to Market Consultations on Draft Guidelines on the First Conduct Rule and Draft Guidelines on the Second Conduct Rule

The Guidelines are welcome steps for businesses to get to understand the approach of the Commission on the key prohibitions under Competition Ordinance. The generous use of illustrations makes the competition laws digestible and easier for cascading the technical concepts to frontline staff members who are laymen and non-legally trained.

1. GENERAL COMMENTS

1.1. The Guidelines contains little industry-specific guidance. While we can understand that the Competition Ordinance and the Guidelines are meant for cross-sectors application, we believe the Commission agrees that different industry is operating in different economic environment and market structure. Property industry, for example, faces competition constraints different from the retail or manufacturing sector. The landscape of conventional retail and trades are being reshaped in the big era of e-commerce. Consumer behavior changes with mobile data and online-shopping getting increasing popularity.

1.2. Trades and industries are operating in a landscape different from what they were before and are fast evolving with globalization and quantum leap of technologies break-through. Competition authorities of established jurisdictions survey from time to time key product markets and publish the results of their findings to enable businesses to understand their responsibilities and the competition authorities' expectation of them. We note, for example, the Singapore Competition Commission published market studies (see hyperlinks below), which are helpful materials for the industry.

- Retail malls market of Singapore (copy enclosed in particular) http://www.ccs.gov.sg/content/dam/ccs/PDFs/MarketStudies/SummaryReportforRetailSpaceMarketStudyFinal.pdf
- Industrial property market of Singapore http://www.ccs.gov.sg/content/dam/ccs/PDFs/MarketStudies/Industrial%20Property%20Market%20Study%20-%20For%20Publication%20040213.pdf
- Retail petrol market of Singapore http://www.ccs.gov.sg/content/dam/ccs/PDFs/MarketStudies/Inquiry%20into%20Retail%20Petrol%20Market%20in%20Singapore%20(May%2023).pdf

1.3. It is hoped that the Commission can similarly conduct and publish market studies helping industry players to understand the competition landscape in which they are operating and the expectation of the Commission on them in the context of the market structure in Hong

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2. DRAFT GUIDELINES ON THE SECOND CONDUCT RULE

2.1. The glaring absence of a threshold on what constitutes "substantial degree" of market power is disturbing.

2.2. Other jurisdictions set market share indications. For the EU and Mainland China, it is 50% and Singapore Competition Commission sets 60% as indicative of market dominance (see http://www.ccs.gov.sg/content/dam/ccs/PDFs/CCSGuidelines/s47_Jul07FINAL.pdf). This leaves the Hong Kong competition laws regime at odds with the other more established anti-trust regimes from which the Commission borrows inspirations, case law reference, and anti-trust market practice. Within the Hong Kong competition law regime, we note that telecom carriers have a safe-harbor with a 40% market share threshold, below which the Competition Commission indicates that it may not even investigate (see paragraphs 3.12 & 3.14 of the draft Guidelines on Merger Rule). Telecom carriers have a safe harbor to work out the boundary of their business. It is hard to understand why other industries are denied with one.

2.3. During the legislative process, the Government indicated that it would consider a market share of 25% as indicative of the substantial degree of power a business had in the relevant market. And whether it should be 25% or some other higher threshold gained traction in the legislative debate on whether the concept to adopt was "significant market power" or "dominance"[1]. The Guidelines do not explain what led the Commission to deviate from the original policy intent of a 25% market share threshold (which in our view is already quite low).

2.4. The elaborate discussions in the Guidelines on "market power" are qualitative and do not help businesses to figure out where do they stand in the grand scheme of things under the Second Conduct Rule. The defense of *conduct-of-lesser significance* is only HK$40 Million[2] and the defense of "*economic efficiency*" is not available on a Second Conduct Rule violation. Uncertainty is unhelpful. Businesses cannot screen whether or not their business is, and when will their businesses become, vulnerable under the Second Conduct Rule. It will be difficult for businesses to plan industry merger/acquisition if there is no certainty whether they will be trapped by the pitfalls of the Second Conduct Rule. We note that the absence of a threshold for Second Conduct Rule also creates issue in interpreting some parts of the First Conduct Rule.

2.5. We hope the Commission can re-consider the position to provide (or at the least, indicate) a market share threshold for the public and businesses to understand whether they have already had and if not, when will they be considered as having substantial degree of market power.

3. DRAFT GUIDELINES ON THE FIRST CONDUCT RULE

What "degree" of market power for the First Conduct Rule"

3.1. Paragraph 3.13 (page 13) of the Guidelines of First Conduct Rule says when considering whether an agreement has anti-competitive effect, the Competition Commission will take into account whether the parties (individually or jointly) have "*some* degree" of market power, and it suggests that the degree of market power under the First Conduct Rule is less than the "*substantial* degree" of market power under the Second Conduct Rule[3]. Given the

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[1] See also the paragraphs 6.2.9 & 6.2.10 (page 91 & 92) in Research Paper "Competition Policies in Selected Jurisdictions" dated 25 June 2010.

[2] HK$200 Million for First Conduct Rule.

[3] See paragraph 3.16 & 3.17 of the Guidelines of the First Conduct Rule.

lack of a figure on what amounts to substantial degree of market power under Second Conduct Rule, how can one work out what is this lesser degree of market power under First Conduct Rule? It serves only to reinforce our view that the degree of market power – whether it is under the First Conduct Rule or Second Conduct Rule – needs to be quantitatively clarified. We hope the Guidelines can also illustrate how this "some degree of market power" works by hypothetical example.

3.2. We support the views of the Commission that vertical agreements are less harmful to competition while offering greater scope for efficiencies. However, after stating that this is the general approach of the Commission, paragraph 6.8 (on page 21) of the Guidelines of the First Conduct Rule said competition concerns will arise (in relation to vertical agreements) where there is "*some degree*" of market power at either the level of the supplier, the buyer or at the level of both. Is this the same degree of market power as mentioned in paragraph 3.13 of the Guidelines? If so, we maintain the same view that a *threshold* (i.e. *how much* market power) is necessary. Otherwise, it is hard for businesses to understand, with certainty, whether their vertical arrangements will violate the First Conduct Rule.

Output limitation

3.3. We disagree with the view set forth in paragraph 6.19 of the draft Guidelines of the First Conduct Rule that "crisis cartel" carries, *per se*, the object of harming competition. In a structural over-capacity situation, the natural force of supply-demand eliminates inefficient operators leaving only the fittest to survive. In Hypothetical Example 7 of the Guidelines of the First Conduct Rule, the salted fish producers are structuring an orderly exit to avoid cut-throat competition and massive close-down affecting the entire industry. We consider that over-capacity should be left for resolution by normal market force.

Exchange of information

3.4. We do not quite agree with the broad statement [4]that exchanging information between undertakings harms competition where it results in undertakings becoming aware of the pricing strategies of their competitors.

3.5. Industry mergers/acquisitions are common activities. It is normal that sensitive and confidential information (such as forecast of turnovers, profit margins, market share, etc which are information of future intent) will be supplied by the target/vendor to the potential buyer in the course of deal negotiation and due diligence process. What is the competition harm if one gets to know the pricing strategy of his competitor in such circumstances?

3.6. Perhaps, the Guidelines may want to clarify that it is not every exchange of information *per se* offends. It is only when the sharing of information is done with a view to restrict, distort or prevent competition offends the Conduct Rules.

3.7. Paragraphs 6.36 and 6.37 of the Guidelines of the First Conduct Rule said exchanging information via a third party may violate the First Conduct Rule. If sensitive information is exchanged by parties knowingly via a third party with a view to bring about competition harm, the concern of the Commission is valid. However, third party/intermediaries (such as estate agents or travel agents) commonly get to know information such as pricing, supply/availability schedules, discounts, rebates etc of landlords/airlines, and often they feed their customers and among them competitors with such information to match deals. These are normal market activities. Landlords frequently go to estate agents for intelligence on what their competitors are about to roll out in order to plan their response strategies. This is, technically, information flow among competitors via a third party. We hope the Competition Commission can elaborate on how the behavior of such as this can become unlawful.

[4] Paragraph 6.32 of the Guidelines of First Conduct Rule.

3.8. The Guidelines may perhaps want to clarify that information obtained by one another via a third party does not *per se* offend the Conduct Rules. It is only when information is knowingly exchanged among competitors using a third party as conduit *with the object or an intended effect of foreclosing competition* offends the Conduct Rules.

The defense of compliance of legal requirement – S. 2, Schedule 1

3.9. Land owner is bound by the restrictions in the land lease, often with very few exceptions for the entire life of the land grant. For example, the land lease may require that the parking spaces of a car-park can only be used by residents of a particular housing estate. Non-resident cannot park their cars at that car-park and the supply of available car-parks in that locality is limited.

3.10. Land leases are contracts in nature (between the Government as lessor and the land owner as lessee). The land owner must, however, observe all the positive as well as restrictive conditions (termed "covenants") in his land lease. A failure to do so enables the Government to forfeit the land or impose fines/charges. Land lease covenants (such as the car-park users restriction in our example above) is being enforced by the Lands Department which is a Government authority being charged with land administration and enforcement matters. There is no "margin of autonomy" or judgmental scope[5] on the part of the land owner as to comply or not and when and how to comply with terms and covenants of his land lease. In our example above, no judgment call is there for the land owner to determine who will and who will not be allowed to park his car at that car-park. If the car-parker is not an Estate resident or his visitor, he can not be allowed to park his vehicle at the car-park in question.

3.11. We hope the Guidelines can clarify that complying with the terms of the land lease is equivalent to complying with a legal requirement; alternatively, agreement/conduct carried out in complying with the land lease will be favorably considered as suitable exemption upon an application under S.9 of the Competition Ordinance.

The defense of agreement of lesser significance – S.5, Schedule 1

3.12. A company may operate separate businesses and have separate income from different activities. A media company may have out-board as well as online advertising. A landlord may run office, retail shops, and hotels. A business conglomerate may have banks, logistics, property, and manufacturing within its group. Different businesses generate different income streams and are being run by separate teams each operating in different economic and competition environment.

3.13. If the activity of one business offends the Conduct Rule, the Commission will investigate the activities of that business line. The other business lines of the company are irrelevant and no personnel of those other divisions should be penalized.

3.14. Suppose the aggregate turnover of Company A from its office, retail and hotels is, respectively, HK$200 Million, HK$200 Million and HK$40 Million. Company B is a hotel operator. Company B's turnover is HK$170 Million. One of the hotels of Company A had cartel practice with Company B. The turnover of that hotel is HK$10 Million. For the purpose of considering whether the defense of agreement of lesser significance under S. 5 of Schedule 1 is available, the aggregation should concern the turnover of the offending elements. The innocent elements should not be penalized. Therefore, the aggregation should concern neither the consolidated turnover of Company A and Company B, nor the consolidated turnover of the hotels of Company A and Company B but rather only (i) that offending hotel and (ii) Company B, which is HK$180 Million and within the defense threshold of HK$200 Million under S.5, Schedule 1.

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[5] See paragraph 3.2 and 3.3 on page 54 and page 55 of the Guidelines of the First Conduct Rule.

3.15. We suggest Competition Commission should clarify that only the business line or division which is tainted with competition-harmful conduct is relevant for considering the defense/exclusion under S.5 of Schedule 1 to (and also for the purpose of the pecuniary penalty under S. 93 of) the Competition Ordinance.

We hope our views are of use to the Competition Commission in its market consultation process. Should the Commission appreciate a discussion, or require us to deliberate further, please do not hesitate to contact me or Mr. Ricky Chan (Director (Legal) & Company Secretary) at

Yours faithfully,

Andy Cheung, CFO & Executive Director
The Link Management Limited
(as Manager of The Link REIT)