Submission by the Hong Kong General Chamber of Commerce on the Draft Guidelines Issued for Public Consultation by the Hong Kong Competition Commission and the Communications Authority Pursuant to the Competition Ordinance (Cap. 619)[1]

INTRODUCTION

The Chamber welcomes this opportunity to provide comments on the draft guidelines to the Competition Ordinance ("**Ordinance**"). The Ordinance is an important piece of legislation which has the potential to have significant ramifications for the competitiveness of the Hong Kong economy and the interests of both businesses and consumers.

The Chamber commends the efforts of the Commission and the Authority to provide guidance in the draft guidelines that have been issued and the opportunity that has been provided for the public to comment on them. The consultation exercise provides an important opportunity for the business community and other stakeholders to share their views on areas in which the guidelines are clear and areas in which there is uncertainty and more clarity is required.

This submission starts by providing some important preliminary comments on competition law implementation and then contains three sections, respectively addressing:

1. the Chamber's detailed submissions on the draft guidelines on complaints, investigations and applications for decisions;
2. the Chamber's detailed submissions on the draft guidelines on the First Conduct Rule ("CR1");
3. the Chamber's detailed submissions on the draft guidelines on the Second Conduct Rule ("CR2").

PRELIMINARY COMMENTS

At the outset, the Chamber would make the following preliminary points about competition law implementation in Hong Kong:

Clarity and proportionate enforcement is essential: Competition policy experts have long understood and appreciated the dangers inherent in competition law implementation. There are two fundamental errors that may be made when addressing competition matters which represent a very complex mixture of economics and law: Type I errors (over-enforcement errors) and Type II errors (under-enforcement errors).

Over-enforcement errors come from seeking to over-apply competition laws. This may occur by applying rigid tests that fail to look in each case at whether the conduct was in fact competition restrictive (*per se* prohibitions or other presumptions) or in leaving the prohibitions very general in nature and not providing clear safe-harbours or guidance on conduct that clearly falls within the 'permissible' category. *Per se* rules are often adopted because competition authorities recognise and have concerns about the time and resources required to prove conduct has an anticompetitive effect. Safe-harbours may not be provided because competition authorities wish to preserve "flexibility" going forward or because they consider that time and experience is required before they can commit to a position on the permissibility of more complex commercial arrangements.

[1] This document reflects solely the view of HKGCC. It does not represent the views of individual members of HKGCC.

Under-enforcement errors come from not applying the law broadly enough. The consequence of under-enforcement error is that the competition authorities potentially do not catch some anticompetitive conduct.

There is an interplay between Type I and Type II errors in that as competition authorities seek to apply the law more broadly to avoid Type II error they necessarily increase the risk of Type I error.

Implementation of competition law, especially when being introduced for the first time in a developed economy, is a complex task. The United States, which has the longest experience of any jurisdiction in competition law enforcement and a market philosophy similar to Hong Kong's, clearly comes down on the side of wanting to avoid over-enforcement (i.e. preferring to avoid Type I error), even if this risks some degree of under-enforcement (i.e. Type II error at least in the short term). In this regard, the US Supreme Court has repeatedly insisted on rules that give more weight to avoiding over-deterrence of pro-competitive conduct. This is not surprising. Type I errors have serious consequences. Type I errors, by deterring pro-competitive conduct, fundamentally undermines the very objective that the law set out to achieve. To use a football analogy, Type I over-enforcement error is tantamount to scoring an own goal. It is particularly important to avoid such errors when introducing a cross-sector competition law for the first time in a jurisdiction with a free market philosophy such as Hong Kong.

In fact, the preference for avoiding over-enforcement is merely a reflection of the principle of proportionality (government/regulatory intervention should only take place if and to the extent necessary) and is consistent with Hong Kong's tradition and preference for light-touch regulation, as exemplified by the "Be the Smart Regulator" initiative.

The dangers of over-enforcement are not limited to potentially punishing pro-competitive conduct. Such rules also create uncertainty, resulting in constructive Type I errors, where businesses, fearful of breaching unclear rules, refrain from competing as aggressively as they otherwise would, thereby depriving consumers of the benefits that flow from vibrant and intense competition.

Without any enforcement history in Hong Kong outside the existing sectoral (and very limited) competition laws, there is a need for clear and detailed guidelines. Without clarity, businesses will struggle to understand what is prohibited, they will then have difficulty complying, business costs (which ultimately affect the cost to consumers) will increase and there is a high probability of competition being reduced as businesses hold back their competitive punches for fear of breaching unclear rules. The burden will fall heavily on SMEs, which have very limited financial resources to apply to trying to determine, where there is uncertainty, what they can and cannot do under the new law.

The Chamber appreciates that there have been calls from various commentators to keep the potential scope of the prohibitions as broad as possible and to wait and gain enforcement experience before expressing views on what, outside of the most obvious serious anticompetitive conduct, is and is not prohibited. The concern with this approach is that it leaves businesses guessing what is prohibited and tips the risk heavily towards over enforcement, leading to a high likelihood the law will reduce, rather than increase competition in Hong Kong. The brunt of this will, ultimately, fall on consumers as they see reduced quality, less choice, higher costs and a less vibrant and innovative economy that is unable to maintain the competitive edge that it has, for many decades, enjoyed in the region.

The Chamber would respectfully suggest the following to reduce the risk of Type I error:

a) **Introduce safe harbours at the outset**: at present, there are, apart from the *de minimis* exemptions, no safe harbours under either CR1 or CR2. The vast majority of agreements and conducts that are engaged in by businesses on a daily basis are not competition restrictive. Other jurisdictions provide clear safe harbours to avoid Type I error and so that businesses can focus their compliance and risk assessment efforts on the small subset of agreements and conducts that are potentially competition restrictive. To give an example, vertical agreements (including vertical restraints that businesses use to ensure their supply chains are appropriately managed to deliver consumer value) are subject to a safe harbour in Singapore which provides that vertical agreements may only be problematic if the undertaking imposing the restraint(s) has a market share of 60% or more. The EU, likewise, lays down a safe harbour in its vertical block exemption regulations, for companies with market shares of up to 30%. In contrast, companies in Hong Kong presently have no guidance as to safe harbours.

   It has been suggested that no safe harbour is required because warning notices will be issued for any conduct that is not serious anticompetitive conduct and that most vertical agreements will not be regarded by the Commission and Authority as serious anticompetitive conduct. With the greatest of respect, the warning notice mechanism will not adequately resolve the issue and prevent Type I error. Companies in Hong Kong, if adopting a prudent approach to compliance, will seek to avoid situations that might give rise to warning notices (which are in effect statutory notices of breach). Even an allegation of anticompetitive conduct carries with it the prospect of reputational damage and prudent companies will therefore prefer to refrain from conduct that they consider might give rise to a warning notice. Without safe harbours, this necessarily means that companies are likely to be overly cautious about the vertical supply chain and other arrangements that they put in place.

   It will be evident that such an approach significantly increases the prospect of actual and constructive Type I error as companies that are unclear about the boundaries of permissible conduct refrain from competing as aggressively as they otherwise would.

   Such safe harbours are also clearly consistent with the policy intent as evidenced in the draft guidelines that were tabled by the Administration during the Bills Committee stage of enactment of the Ordinance, which, for example, stated:

   > "In respect of "vertical agreement", it is expected that the first conduct rule will be applied in a much more limited fashion. A vertical agreement is an agreement made by two or more undertakings, each operating (for the purposes of the agreement) at a different level of the production or distribution chain. For instance, where undertaking A produces raw material, and undertaking B uses raw material acquired from A as an input, A and B are in a vertical supply relationship. Generally, a vertical agreement should be viewed simply as a legitimate way of influencing how a supplier's product is distributed and marketed. A supplier competing with other suppliers generally has no incentive to use a distribution or marketing strategy that makes its product less attractive to consumers than its competitors' products. Restricting a supplier's vertical supply chain (restrictions on intra-brand competition) can have positive benefits for competition between

different brands (inter-brand competition) by promoting inter-brand competition, for example, improved quality of service."

The above is consistent with world best practice competition policy and the prevailing view internationally in competition economics as to the pro-competitive benefits of restraints designed to assist in implementing distribution and marketing strategies.

b) **Recognise that waiting on decisions from the Tribunal is not the answer to lack of clarity and Type I error:** The Chamber recognises that ultimately it will be for the Tribunal to interpret the Ordinance in cases that come before it. However, safe harbours in the guidelines will very meaningfully assist in reducing Type I error and increasing certainty (and competition). It will take many years to build up a body of case law covering the various areas of current uncertainty in the Ordinance. In the meantime, safe harbours will give comfort to businesses as to the conducts that the Commission will take enforcement action against and those it will not. In the absence of stand alone rights of action at this early stage in competition law implementation in Hong Kong the Commission will have a discretion to decide which cases will come before the Tribunal and can give useful guidance on how it will exercise that discretion in the guidelines. It is respectfully submitted that the legislature has been alive to the risk of Type I error and risk of the law unwittingly reducing Hong Kong's competitiveness to the detriment of consumers and that this concern needs to be accommodated in the guidelines with appropriate safe harbours.

c) **Revisit issues as enforcement experience grows**: The Chamber is not suggesting in the above that safe harbours that are put in place in the early days of implementation should be fixed in stone forever. Serious anticompetitive conduct should be the focus of enforcement efforts from the outset and the Commission and Authority can revisit safe harbours that have been provided for in the guidelines as they gain enforcement experience and as and when needed, or when consultations arise in relation to block exemption applications. All safe harbours do is to ensure that early enforcement efforts are focused on the conducts that are most obviously of concern, giving business the comfort to continue to compete vigorously for the benefit of the Hong Kong economy while allowing the regulators time to develop enforcement experience and more considered views as to the finer boundaries between permissible and prohibited conduct in more complex areas of potential enforcement.

d) **Approach *per se* breaches or presumptions that certain conducts are anti-competitive with extreme caution**: The Ordinance does not provide that any conduct will be presumed to be anti-competitive and overseas experience over the decades shows that *per se* prohibitions (or such presumptions) significantly increase the prospects of Type I error. A simple example of this is resale price maintenance ("RPM"). It is stated in the guidelines that RPM will be presumed to be anti-competitive. This is at odds with the approach in, for example, Singapore, which is only concerned about potential restrictive effects of RPM where markets shares are in excess of 60%. There are very valid reasons why businesses might seek to impose RPM restraints e.g. to prevent free-riding which undermines anchor stores that invest to bring new products to market, promote the brand, educate consumers and display a wide range of products when they are undercut by stores that do not provide these services, depriving the anchor store of the economic incentive to bring these benefits to consumers. Such restraints could only be a potential competition law problem where they are being used to mask a horizontal cartel or where there is a serious

deficiency in inter-brand competition. Furthermore, if the product concerned is a new product in Hong Kong which the supplier wishes to be sold above a certain price for image reasons, e.g. a luxury product, the supplier may not be prepared to supply in Hong Kong at all (being a small market) unless the distributor/retailer agrees to RPM. It cannot be said that this harms competition, when the consequence of no RPM may be no product at all for Hong Kong consumers.

It may be suggested that companies should, if they see such benefits in RPM arrangements, be prepared to justify them by putting on an efficiency defence under the First Schedule to the Ordinance. However, the cost and risk of running such defences is significant and the reality is that prudent businesses will often opt instead simply not to bring some new products to market in Hong Kong or to refrain from trying to encourage distributors to establish anchor stores to avoid the significant risks that are impose by a presumption that RPM is inherently anticompetitive.

e) **Focus early enforcement on serious anti-competitive conduct and make it clear in the guidelines that this is the enforcement priority**: The concept of 'serious anti-competitive conduct' is not, as is being suggested in the draft guidelines, simply a procedural issue about whether or not a warning notice will issue. The Legislative Council debate during the Bills stage was clear that the concept of serious anti-competitive conduct was being introduced into the Ordinance to make clear the potentially most serious categories of infringement under CR1.

It is respectfully submitted that the clear legislative intent was that the four conducts that have been categorised as serious anti-competitive conduct are so categorised because they are the most capable of having a serious effect on market competition and should be the focus of CR1 enforcement activity. The four conducts are: price fixing, market sharing, output restrictions and bid rigging. It is not apparent to the Chamber what statutory or policy basis there could be for assuming that conducts outside of those four conducts might be regarded as serious anti-competitive conduct as defined by the statute or subjected to a presumption that they are inherently anticompetitive. Necessarily, if the legislature had considered other conducts to be inherently or manifestly anti-competitive, they would have been included within the list of serious anti-competitive conduct. If the legislature had intended that conduct should be presumed anti-competitive and the burden pushed to business to justify the conduct, then this would have been clearly spelt out in the Ordinance. This is all the more so given the long-standing economic policy of Hong Kong which places faith in markets and presumes (recognising the risks and costs of intervention) that markets get it right more often than regulators.

The draft guidelines refer to, and seek to adopt, the EU concept of 'by object' infringements. However, this fails to recognise that EU law does not have a concept of serious anti-competitive conduct and further that Hong Kong's prohibitions, although using the expression 'object or effect' are otherwise in substantially quite different terms to the EU provisions (Articles 101 and 102). Importantly, CR2 also contains the words 'object or effect', but it cannot be presumed that the legislature's intention was thereby to introduce 'by object' infringements under CR2. Abuse of market power cases require assessment of whether there has been an exclusionary effect. Conduct cannot be presumed by its very nature to be an abuse of a substantial degree of market power. Conduct that might otherwise be at risk under CR2 can perfectly legitimately be engaged in by companies without a substantial degree of

market power. Such conduct can even be engaged in by a company that has a substantial degree of market power so long as it is not considered an abuse of that market power. The Chamber had always understood, during the passage of the Bill through LegCo, and from the Government's initial proposals, that the focus would be on the anti-competitive effects of conduct, and that no types of conduct would automatically or always deemed to be anti-competitive.

The Chamber would make two further points.

Measuring market power: the concept of market power is obviously very important in assessing potential infringements under both CR1 and CR2. Section 3.2 of the draft CR2 guideline states that "Substantial market power can be thought of as the ability profitably to charge prices above competitive levels, or to restrict output or quality below competitive levels, for a sustained period of time."[2] A similar definition is provided at paragraph 3.15 of the draft CR1 guideline. If this is to be the benchmark for such a critical test under the Ordinance, the Chamber would respectfully suggest that more guidance needs to be given as to how the Commission will determine a 'competitive' price or 'competitive' levels of quality/output. In this regard, the Chamber would note that it is now universally accepted that perfect competition is not an appropriate benchmark for antitrust analysis and that the benchmark should be workable competition in the industry under consideration. Reference should be made to this in the guidelines and it should be explained in this context how the Commission would assess 'competitive' price levels, output and quality.

Approach controversial doctrines such as the essential facilities doctrine with extreme care: While the draft CR2 guidelines recognise that as a general matter undertakings should be free to decide with whom they will do business[3], they go on to say that a refusal to deal by an undertaking with market power is likely to be abusive in very limited or exceptional circumstances and that a refusal to licence an intellectual property right could be a violation in exceptional circumstances.[4] Such an approach could significantly undermine incentives to innovate (which are the single most important engine of competition), particularly if applied to intellectual property rights. The United States Supreme Court, in its 2004 Verizon Communications decision[5] cautioned against imposing obligations to deal with competitors, in the following terms:

> *"Firms may acquire monopoly power by establishing an infrastructure that renders them uniquely suited to serve their customers. Compelling such firms to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities. Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing–a role for which they are ill-suited. Moreover, compelling negotiation between competitors may facilitate the supreme evil of antitrust: collusion. Thus, as a general matter, the Sherman Act "does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal." United States v. Colgate & Co., 250 U.S. 300, 307 (1919)."*

[2] See also Draft Second Conduct Rule Guideline ¶¶1.4, 3.4 and 3.6.
[3] Draft CR2 guidelines, para 5.15.
[4] Draft CR2 guidelines, para
[5] Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, Llp (02-682) 540 U.S. 398 (2004) 305 F.3d 89.

Given Hong Kong's long-standing market policy and its antipathy towards central planning, the Chamber respectfully submits that such doctrines have no place in Hong Kong law.

COMMENTS ON THE DRAFT GUIDELINES ON COMPLAINTS, INVESTIGATIONS AND APPLICATIONS FOR DECISIONS

A. INTRODUCTION

Our comments below will specifically address the Commission's guidance on how it will interpret and carry out its obligation of confidentiality, and the appropriateness and sufficiency of each of the procedural guidelines.

B. CONFIDENTIALITY UNDER SECTIONS 123-126 OF THE ORDINANCE

The Commission's obligation of confidentiality and treatment of confidential information are areas of key concern to the Chamber. As the Commission envisages complaints and information from the public will be an important source of information, the assurance of confidentiality goes hand in hand with the efficacy of the competition regime in Hong Kong. Accordingly, while we comment on each Guideline separately below, we consider it important to separately outline our comments with respect to confidentiality because it is an overarching issue that runs throughout the procedural guidelines.

The submission and/or disclosure of confidential information give rise to complex and often litigated issues in developed competition regimes. We consider the Guidelines in their present form do not sufficiently elucidate the Commission's intended approach and would urge the Commission to clarify and elaborate upon its obligations and powers under sections 123-126 of the Ordinance.

Section 124 of the Ordinance states as follows:

> "*The Commission and the Communications Authority must establish and maintain adequate procedural safeguards to prevent the unauthorized disclosure of confidential information.*"

We submit this necessitates substantive guidance on the submission and treatment of confidential information. We note further that unlike substantive issues relating to the interpretation of the Conduct Rules, the Commission should find confidentiality a familiar concept on which prior local enforcement experience is not required to formulate detailed guidance. Looking to developed competition law jurisdictions, DG Competition of the European Commission, the Australian Competition and Consumer Commission, and the Competition and Markets Authority of the United Kingdom have each issued specific guidance on confidentiality claims.

Having regard to its mandate under the Ordinance, and, in line with international best practice, we strongly recommend the Commission to issue separate, detailed guidance on the submission and treatment of confidential information under the Ordinance. Failure to do so could detract from the certainty of the enforcement regime and risk undermining transparency, at the same time undermining incentives to report suspected contraventions of the Conduct Rules, and cooperate with the Commission.

1. Submission of confidential information to the Commission

The Commission has power under section 41 of the Ordinance to require production of information or documents ***relating to any matter it reasonably believes to be relevant to the investigation***. This qualification is an important line of defence and protection to undertakings involved or assisting in an investigation against potential overreaching of the Commission's powers of investigation.

To place the issue beyond doubt, it would be helpful if the Commission would expressly state that undertakings do not have to submit to the Commission information, whether or not confidential, that is not relevant to the subject matter of an investigation. This should include the right to redact irrelevant information from documents to be submitted to the Commission.

2. Confidential treatment of information submitted to the Commission

It would be most instructive if the Commission could categorise the types of confidential information it expects to receive and how its treatment of each category may differ, particularly in applying the exceptions for disclosure under section 126 of the Ordinance.

The case for disclosure and justifiable extent of disclosure under section 126(3) of the Ordinance should involve a balancing exercise taking into account (i) the exception sought to be invoked under section 126(1), (ii) the potential consequences of disclosure to the Complainant and the undertakings under investigation (whose interests may be diametrically opposed), (iii) the context in which the Commission received the information (whether a complaint, investigation or Application); (iv) the circumstances, including sensitivity, of the case; (v) the party who submitted the information (whether undertaking under investigation or a third party) and (vi) the nature of the confidential information.

By way of example, distinction should be made between information which is by its nature confidential (e.g. competitively sensitive information, commercial secrets and intellectual property), information on which an obligation of confidentiality is imposed by the Ordinance, and information which is not in and of itself confidential but, if disclosed, may amount to a de facto disclosure of matters the Commission is otherwise obliged to keep confidential (e.g. the fact and circumstances of an investigation in a concentrated market which de facto identifies the parties). Properly categorising the nature of confidential information should produce a sliding scale that would better inform the Commission's practice on the scope, extent and form of disclosure.

3. Transparency

It is a fundamental principle of natural justice and due process that an undertaking under investigation is entitled to meet its accuser and the case made against it. It follows that the need for clear guidance on confidentiality also promotes transparency, in that where confidentiality claims are not justified or properly articulated in accordance with published guidance, the scales tip towards disclosure.

While we take the view confidential information the Commission requests from parties under investigation does warrant protection, we do not consider appropriate the Commission's default position that the identity of Complainants be kept secret. The default position should

be transparency; with robust safeguards for genuine confidential information and the interests of Complainants, undertakings under investigation and other third parties where disclosure would cause undue prejudice to them.

C. INDICATIVE TIMETABLES

Although the Ordinance does not prescribe any deadline for assessing complaints, completing an investigation or making a decision, it would be useful (and, we submit, feasible) to specify indicative target periods to assist businesses in their commercial planning.

As the Commission builds its enforcement experience, the expectations of those involved may be managed by regular engagement and indicative timetables for each stage of a case. Needless to say, indicative timetables may change as a case progresses. Having indicative timetables would give all those involved, including the Commission, greater certainty and control over the process.

We submit the Guidelines should provide for (i) general target periods for assessing complaints, each stage of an investigation, making a decision or issuing a Block Exemption and (ii) indicative timetables for each case. In this regard we note the stringent standards provided for in OFCA's "Guide on How Complaints Relating to Anti-Competitive Practices … are Handled" ("OFCA's Guide to Complaints").

D. ENFORCEMENT POLICY AND LENIENCY POLICY

The Commission is expected to publish an Enforcement Policy and a Leniency Policy later in 2014/ early 2015, which should be complementary to the Investigations Guideline. As such, it remains to be seen whether gaps in the Investigations Guideline will be filled by the Enforcement Policy. More importantly, the Guideline should provide that the Enforcement Policy and Leniency Policy will be published before the Conduct Rules become operational.

E. COMPLAINTS

The Commission is expected to establish an internal complaints-handling mechanism with designated independent officers to handle disputes regarding the conduct of a case.

The procedure for submitting and handling complaints should be set out in detail and separately published to ensure public accountability. Good complaint handling would also strengthen public confidence in the Commission and enable the Commission to resolve disputes in an efficient and cost-effective manner.

F. COMMENTS ON THE GUIDELINES

Para / Ref.	**Issue**	**Comment**
Complaints Guideline		
The Complaints Guideline largely summarises existing provisions in the Ordinance. There are certain overlaps between the Complaints Guideline and the Investigations Guideline, as the process of assessing a complaint is similar to an Initial Assessment. The main issues identified below relate to the lack of clearly stated timeframes, low transparency and lack of		

consultation between the Commission and the parties relevant to a complaint.		
1.2, 2.2, 2.4	Evidentiary standard of complaints	Given the general wording of the Conduct Rules, there is a very real prospect that the Commission will be flooded with unmeritorious and vexatious complaints. It is thus vital that the Commission requires complaints to be "well-informed" (as stated in para. 1.2) and to be accompanied by evidence, including at least the information listed in paragraph 2.4. In other words, the Commission should not pursue any complaints which are not accompanied by proper evidence and information: it should not be for the Commission to request the information (as para. 2.4 currently suggests). Equally, a mere telephone call by a Complainant should not be sufficient (contrary to what para. 2.2 currently states). These arguments are supported by OFCA's Guide to Complaints, which imposes stringent standards for the submission of complaints: we recommend that the Commission follows a similarly rigorous approach.
2.3	Acknowledgment of complaints	To avoid creating confusion over whether a complaint has been received or received as complete, the Commission should make clear in the Guideline a written confirmation of receipt will be given to the Complainant within a specific timeframe, confirming the status of the complaint as received and/or received as complete.
2.5	Response to requests for information	We support the Commission's view that complaints should be well-substantiated in order to form the basis of an investigation. It is suggested the Commission maintain an open dialogue with the Complainant in order to better understand the Complainant's circumstances and reasons for reservation (if any) and that no adverse inference be drawn solely from a failure to respond within any timeframe that may have been unilaterally imposed. Despite assurances of confidentiality, a Complainant may have legitimate concerns regarding their response to requests for information. It should be emphasized that Complainants may seek assurance that information or parts of information provided to the Commission will be kept strictly confidential (subject to the observation\ made in Section B(1)-(3) above). Complainants should be reminded that requests for information at the complaint stage are entirely voluntary, but failure to provide sufficient evidence may lead to the Commission's decision not to pursue an investigation. Whether or not to submit further information at this stage should be the Complainant's decision and Complainants will have sufficient incentive to substantiate a meritorious and genuine complaint.
3.1	Commenting on	Although it is clear the Commission owes a duty in

	matters under consideration or investigation	respect of confidential information, a blanket statement that the Commission will not normally comment on matters it is considering or investigating is unhelpful. We strongly urge the Commission to formulate a clearer set of guidance on the circumstances where it may be justifiable for the Commission to: a. give comments or make disclosure in relation to ongoing complaints or investigations; b. the nature of the comments/ extent of disclosure; and c. to whom comments/ disclosure will be made. Section 124 of the Ordinance mandates establishment of clear procedural safeguards to prevent the disclosure of confidential information. There should be substantive guidance on the treatment of confidential information in the context of any guidance from the Commission on circumstances in which it might comment on matters under investigation.
3.4 – 3.5	Disclosure of Complainant's identity	As stated in section B3 above, promoting transparency should be the starting point. This paragraph restates section 126 of the Ordinance and does not add any explanation or clear guidance as to when the Commission will or will not disclose a Complainant's identity. Additionally it is not clear whether the Commission will, prior to disclosing a Complainant's identity, adopt certain procedural measures such as to notify the Complainant of the impending disclosure and/or give the Complainant an opportunity to be heard. Where the Commission indicates it may depart from usual practice it would be helpful to specify in the Guideline when and in accordance with what principles the Commission will decide to do so.
3.6	Cooperation between competition authorities	This paragraph is a restatement of section 126(1)(h) and does not add guidance on how and when confidential information will be exchanged between the Commission and OFCA. The Guidelines should specify the circumstances under which the Commission intends to share information with OFCA and indicate how the Commission will control/ ensure the confidentiality of information shared.
4.1	Assessment of Complaints and Queries	This paragraph largely restates section 37(2) of the Ordinance. The latter half of the last sentence states that the Commission enjoys the discretion to investigate a complaint even where the Complainant no longer wishes to cooperate with the Commission. This manner of exercising the discretion to investigate is new and involves potentially the Commission's use of confidential information provided by a Complainant after consent is revoked. Further clarification is required

		as to: • when the Commission may exercise its discretion to investigate despite a Complainant's withdrawal of the complaint; • whether the Commission will return proprietary or confidential documents to the Complainant; • whether, and how the Commission may use confidential information provided by the Complainant to the Commission.
4.2-4.4	Assessment of Complaints and Queries	We welcome the Commission's clarification that it will adopt a principled approach in the exercise of its discretion in the selection of cases. In the interests of providing legal certainty to Complainants and subjects of investigation, we look forward to the publication of further guidance on how the Commission intends to apply each of the factors listed under paragraph 4.3, and the Commission's enforcement strategy, priorities and objectives. We submit the Guideline should provide that the Commission should consult on its enforcement strategy, priorities and objectives and publish the same before the Conduct Rules take effect. In addition to paragraph 5.3, please clarify: • whether and in what circumstances the Commission may be prepared to revisit a decision of no further action; and • whether a Complainant will be given the opportunity to request additional explanation, or submit additional information or make submissions.
5	Next steps	The Commission's decisions to take no further action may be open to challenge in certain circumstances. In the interests of judicial economy, and in light of section 5.3 in which the Commission sets out circumstances under which it may reconsider the issues raised in a complaint despite an initial decision of no further action, we recommend the Commission give clearer and more extensive guidance on grounds it may be prepared to accept as warranting reconsideration of an initial decision to take no further action. The Guideline does not include any timeline or performance pledge. It would be helpful if the Guideline could provide indicative timescales, extendable if necessary, in which the Commission may be expected to complete its assessment of a complaint. Again we invite the Commission to consider adopting a similar approach to that found in OFCA's Guide to Complaints. Even if the Commission does not wish to commit to a prescribed deadline for completion of an investigation, it should recognise in certain circumstances where consumer

		interests are significantly harmed, Complainants and the affected consumers should be entitled to expect swift enforcement action.
5.4	Status updates	Unless there are specific circumstances that warrant confidentiality, as a matter of legitimate expectation and to ensure diligent prosecution, a Complainant should be entitled to be informed of the status of the Commission's assessment. There has been a recent and unfortunate example of the Communications Authority being heavily criticised by the Telecommunications (Competition Provisions) Appeal Board for the Communications Authority's handling of an Initial Assessment of a competition complaint, which extended to well over a year without satisfactory resolution. Best practice would generally require investigations, including Initial Assessments, to be conducted in a manner that ensures that the Commission remains accountable for how it is discharging its statutory powers.
Investigations Guideline		
The Investigations Guideline largely summarises existing provisions in the Ordinance. The main issues identified relate to the absence of timeframes and lack of transparency. In relation to the Commission's exercise of significant enforcement powers further provision is required to safeguard undertakings' right of defence.		
3.2	Timeframe for Initial Assessment Phase	There is no long stop deadline or performance pledge in relation to the Commission's conduct of the Initial Assessment. It would be helpful if the Commission could provide indicative timescales for both the Initial Assessment Phase and Investigation Phase, as in OFCA's Guide to Complaints, to enable Complainants and undertakings under investigation to assess and make appropriate plans/ provision.
3.4	Whether matter warrants investigation	The criteria listed here should apply not just to whether the matter warrants further investigation, but whether an Initial Assessment Phase should be commenced in the first place. This is consistent with paragraph 4.3 of the Complaints Guideline.
4.2	Explanation to the Complainant only if a decision is made to take no further action	We submit the Commission should also explain other outcomes listed at 4.1(a)-(d).
4.4	Case updates	It is not clear how, save in exceptional circumstances, informing parties of the ongoing status of the investigation may prejudice the investigation. Not informing parties of case status as a blanket policy goes against principles of transparency and accountability. Please provide guidance on: • whether and if so how and how often the

		Commission intends to update subjects of investigation and Complainants of the status of an assessment/ investigation; • whether the subjects of investigation and Complainants will have opportunities to meet with and make representations to the relevant the Commission case team; and • whether the Commission case team will, subject to any prejudicial effect on an investigation, share its preliminary thinking and working plan with the subjects of investigation and Complainants.
5.1	Reasonable cause to suspect	It is unclear how the standard of reasonable cause of suspicion will be applied. It appears that "beyond mere speculation" is a lower standard than a "suspicion based on relevant facts and any other information". We submit that paragraph (b) should be replaced by the following: "such facts and information would, if proved, establish a breach of a Competition Rule".
5.9	Section 41 notices	Although this list is non-exhaustive, it would be useful to add to the list "why the Commission has reasonable cause to suspect that a contravention of a Competition Rule has occurred".
5.15-5.16	Written requests for documents and information	Section 41 only empowers the Commission to collect relevant documents and information. The Guidelines ought to make it clear that the scope of section 41 notices and the subject matter of the investigation a notice relates to must be identified with sufficient precision in order for persons served with it to identify the relevant documents in compliance with the notice. The scope of the section 41 notice is significant as the Commission may use evidence gathered in one investigation for other purposes, e.g. in other investigations or to conduct a market study. It is important that the section 41 notice does not infringe upon an undertaking's right of defence not to be forced to facilitate a fishing expedition by the Commission. Accordingly where the scope of a section 41 notice is unduly wide or unclear, whether it should be amended should not be determined by whether it would impede the Commission's investigation, but whether it is accurate and relevant to the investigation.
5.20	Legal assistance	We suggest, in the interests of clarity, that this paragraph be adjusted to read "Any person required by the Commission to appear may be accompanied by one or more in-house and/or external legal advisers".
5.22	Recordings, transcripts and documents	Where a person gives information in compliance with a section 42 notice, that person should always be provided a copy of the record of interview for verification,

		immediately after the interview is conducted. Such record should also be signed off by that person after he/she is given an opportunity to review and amend the record.
5.26-27	Search warrants	The situations under which the Commission may seek a section 48 warrant do not offer assurance that the Commission will use its power responsibly. For example, there may be many reasons for "secretive" conduct or non-compliance with the Commission's requests, particularly where the requests are voluntary. A person/ undertaking may be unable to respond promptly where legal advice is being sought, records are incomplete, or resources are insufficient to prepare a timely response. The Guideline should make clear that the Commission will seek a section 48 warrant only where there is unjustifiable secretive conduct or non-compliance with requests. Further, even though the Ordinance does not require the Commission to have first used other investigation powers, a section 48 warrant, being a rather draconian enforcement tool, should in most cases be used only as a measure of last resort.
5.31	Waiting for legal advisers	It is important for businesses to know that the Commission will (not "may") wait a reasonable period for legal advisers to arrive, whether in-house or external, and to give an approximate indication of what they would consider a reasonable period to be. Where there are in-house lawyers already on the premises, that period could be shorter than where in-house lawyers or external lawyers have to travel from other places to attend.
5.32	Oral explanations	Individuals questioned on the spot are entitled to separate legal representation if they so elect. It would be helpful for the Guidelines to provide that the Commission will where individual representation is requested wait a reasonable amount of time for separate legal advisers to arrive.
5.34	Return of documents	We suggest the Commission's right of search/access should be restricted to only those documents/equipment which are relevant to the investigation but no others, and as mentioned in relation to 5.38 below there should be a mechanism to ensure the documents/equipment accessed/taken possession of for inspection do not contain private/confidential information which is not relevant to the investigation or is privileged. Please confirm that returned documents will not form part of the investigation file and all copies made thereof would be returned or destroyed.
5.35	Retention of evidence	We suggest the word "reasonably" is inserted before "necessary" in the first sentence of this paragraph.

5.36-37	Statutory declarations regarding evidence	This ties in with our comments on paragraph 5.22 above, that a person being asked to give a statutory declaration should be given the opportunity to review and amend the record of evidence.
5.38	Privilege	The Guidelines lack a procedure for dealing with disputed evidence. Where there is a difference in opinion between the Commission official and the undertaking/ person under investigation regarding whether certain evidence is privileged, the disputed item of evidence should be sealed for safekeeping pending further determination by an independent arbiter.
5.45	Timeframe for completion of investigation	The lack of a timeframe casts significant uncertainty on undertakings under investigation and their ongoing business relationships. The Commission should commit to providing an indicative timeframe, which may be extended if required.
6.7	Disclosure of information	Before making disclosure of confidential information to a third party, the Commission should notify and consult the affected party.
7.5-7.7	No further action	Please state whether the Commission will issue no-action/ comfort letters in cases where it decides not to pursue an investigation upon a change of conduct/ acceptance of a commitment.
7.8	Interim Orders	Please clarify under what circumstances the Commission may seek an interim order from the Tribunal.
7.11	Press release	Please confirm that the Commission will consult the parties on a draft press release before it is issued.
7.12	Acceptance of Commitments	Please clarify whether it is intended that Complainants will be given the opportunity to comment on the appropriateness or adequacy of a proposed commitment, before it is accepted, rejected or published by the Commission.
7.16-7.21	Warning/ Infringement Notices	We note the Ordinance does not state that Warning Notices will be published, but that, despite this, the Commission is proposing to do so. We would respectfully suggest that this be reconsidered. The purpose of a Warning Notice is to give the undertaking in question notice that the Commission might have concerns about non-SAC conduct. At such an early stage, where an undertaking has not had an opportunity to respond to the allegations, publication risks causing unjustified reputational damage and, in the case of listed companies, could involve a price sensitive event, which could cause significant disruption to the company and ramifications for investors. Please further state whether Warning or Infringement Notices will contain the Commission's legal and economic assessment of the relevant facts/ conduct and

		the action(s) it proposes to take (in addition to proposed directions/commitments). Please clarify whether, prior to publication on the Commission's website, Warning or Infringement Notices will be provided to the relevant parties in draft, to allow them to: • make submissions for redaction of confidential/ sensitive information; and • prepare their responses.
Decision and Exemption Guideline		
The Decision and Exemption Guideline largely summarises the relevant provisions in the Ordinance. Where the Guideline provides further elaboration, the new content is uncontroversial and in line with international practice, save as set out below. The Guideline gives a good overview of the procedural flow of the Application process and confirms the Commission will consult relevant parties and the public during the process. In line with international practice, the Commission also encourages Applicant(s) to approach it for a preliminary consultation for guidance prior to making an Application.		
1.17	Issuing of Block Exemptions on the Commission's initiative	This paragraph points out (correctly) that the Commission may issue a Block Exemption Order not just in response to an Application, but also on its own initiative. Vertical agreements are generally regarded as only potentially problematic where there is substantial market power, and otherwise are considered to deliver efficiencies which outweigh any harm to competition. The Guideline, however, turns the presumption on its head by generally saying that vertical agreements may be justified on efficiency grounds. The presumption should be the other way: that agreements are generally pro-competitive, unless there is evidence to suggest to the contrary. There is also no clarity provided by saying that it is only where undertakings have a degree of market power that there might be a concern. Necessarily, most healthy competitive markets exhibit a degree of market power. The question is at what threshold levels businesses need to start to be concerned that their conduct could be infringing the law. The Commission should exercise its power to issue a Block Exemption order for vertical agreements as soon as possible after the Conduct Rules take effect. The Commission has sufficient time to do the necessary preparatory work before that date, so that it can commence the consultation process in section 16 of the Ordinance as soon as the Conduct Rules take effect. Pending clarification in a block exemption, it should be made clear that, while the Commission may initiate enforcement actions under the Second Conduct Rule against vertical restraints that are regarded as an abuse of a substantial degree of market power, it will refrain from enforcement action under the First Conduct Rule

		pending conclusion of the block exemption consultation and issuance of a block exemption to the market which gives adequate clarity. More generally, although the focus in this guideline is on Applications for a Block Exemption, the Commission should commit to proactively identifying types of agreement which may be suitable for Block Exemption.
3.6(b)	Scope of confidentiality claims	While we agree that unduly broad confidentiality claims should be critically assessed, we submit subsection (b), which is worded as a sanction, is not appropriate in the context of Applications. Unlike in complaints and investigations, Applicants of a decision or Block Exemption provide information to the Commission on their own volition and are likely to be more forthcoming in comparison. Understandably, unduly broad claims for confidentiality may be rejected and revised following appropriate discussions, however, we do not consider it appropriate for the Commission to disclose such information without the Applicant's consent.
4.1	Use of information received for other purpose	It is not clear to us the statutory basis on which the Commission has the power to use information received in an Application for other purposes. This is a significant power which may curb an Applicant's incentive to approach the Commission. We submit the Guideline should provide clearly the source of the Commission's power and how the Commission intends to exercise this power.
5.1	Who may apply	We submit eligibility to apply for an Application should not be limited to undertakings engaging in economic activity. The Commission should be open to receiving Applications from parties that satisfy the Suitability Factors, such as statutory bodies and non-profit organisations.
5.3	Eligibility of Applicant	It is not clear whether the Commission intends to apply wider industry interest and cooperation from undertakings, which this paragraph states it expects, as eligibility requirements on top of the Suitability Factors set out at paragraph 6.4. We would invite the Commission to clarify the source of its authority to do so. We submit Application should merit consideration where the Applicant clearly satisfies the Suitability Factors. We suggest the Commission remove the additional "expectation" under this paragraph, or apply them as factors relevant to the determination of whether a decision or a Block Exemption would be more appropriate. In any event the Commission should clarify how it

		expects an Applicant to demonstrate it is "representative of a wider industry interest", particularly in the context of cross-sector Block Exemption Applications, such as an Application for exemption for vertical agreements. While the Commission may request cooperation from all undertakings that are party to the agreements in question, this should not be a prerequisite to the Commission's consideration of an Application. Whether or not other undertakings will be cooperative is often out of the Applicant's control and should have little bearing on the worthiness of the Commission's decision on the issues raised.
5.8	Whether to apply for a decision or Block Exemption order	Where the Commission receives Applications for decisions for similar agreements, the Commission should exercise its case management powers and consider making a Block Exemption order of its own volition.
5.10	Application Forms	We would suggest the Commission attach specimen Forms AD and BE to the Guideline.
5.15	No immunity	We appreciate the Commission may not wish to grant immunity to undertakings with respect to anti-competitive agreement or conduct notified to it by way of an Application or Block Exemption Application. However except in the most clear-cut cases of violation of a Competition Rule, we recommend the Commission take a mutually constructive approach (instead of initiating enforcement action) of entering into discussions with the Applicant and other affected parties to identify (i) appropriate modifications to the subject agreement or conduct and (ii) limitations or conditions, which may improve the Applicant's chances of obtaining a favourable Decision. Where the Commission is not prepared to make a favourable Decision in any form, it should explore the possibility of accepting certain commitments from the Applicant and other affected parties as appropriate.
6.2	Timeframe for review of an Application	Although the Ordinance does not prescribe any deadline for making a Decision, it would be useful (and, we submit, feasible) to specify a target period within which the Commission will make a Decision, at least in respect of individual agreements or conduct, to assist businesses in their commercial planning, and thereby increase the attractiveness of the Applications procedure. We suggest the maximum target period should be six months, although in simple cases the actual period for making the Decision could be considerably shorter.
6.4	Consideration of Applications	Although the Commission is only <u>required</u> to consider an Application if three criteria are satisfied, the Commission should exercise its <u>discretion</u> to accept as many Applications as possible, particularly in the first

		few years of the Conduct Rules taking effect. This is because the Conduct Rules are drafted in relatively general terms, and published Decisions will greatly assist in providing clarity as to the Commission's approach to particular types of agreements and conduct.
6.11	Hypothetical question	Although it may not be appropriate to consider hypothetical questions, the Commission should acknowledge that, as undertakings are encouraged to obtain approval prior to executing and implementing an agreement, an Application in relation to an intended agreement or conduct may be fairly conceptual at the time the Applicant(s) approach(es) the Commission, albeit not hypothetical.
6.14, 6.16	Initial consultation/ Conduct that does not harm competition	Businesses may wish to have an Initial Consultation to obtain comfort that particular agreements or conduct do not raise competition concerns, i.e. an Application would not need to be made. It would be helpful if this paragraph could make clear that the Initial Consultation would also serve this purpose. It should also be made clear that it would be open for businesses to submit reasons (whether in an Initial Consultation or Application) why the agreement or conduct do not harm competition.
7.3	Denial of Application	It should be made clear that it would be open for businesses to submit in the Application reasons why the agreement or conduct <u>do not</u> harm competition, and to submit arguments for an exclusion only in the event that the Commission disagrees and believes that there is harm to competition.
8.6-8.8	Engagement with the Applicant	During the process of engagement with the Applicant, it would be useful to state that the Commission will update the Applicant from time to time as to the timescale within which the Decision will be reached.
8.10	Draft decision	The Commission may consider providing the Applicant(s) with a draft of the decision where it does not publish a draft for public comment.
10.1	Completeness of Application	It is inevitable given the broad implications of a decision/ Block Exemption Application that there will be a plurality of views regarding key issues such as market definition and theories of harm, which by their nature permit a certain margin for argumentation. The Commission should expressly recognise in the Guideline that it will not require an Application to cover arguments from every perspective in order to be considered "complete". The process of engagement with parties likely to be affected (paragraphs 8.3-8.5) ensures different perspectives of relevant stakeholders will be considered and the burden should not fall solely on the Applicant to present an entire case. The Commission should base the requirement of

		"completeness" on factual information submitted in the Application and whether the Applicant has given well-substantiated explanations.
11.4	Self assessment	We submit further guidance is required to ensure greater certainty. Otherwise: 1. the Commission will be inundated with Applications for decisions as parties seek more clarity; and 2. businesses will refrain from conduct for fear of breaching uncertain rules, with the effect that the law actually reduces competition in Hong Kong to the detriment of consumers (Type I error). The net is being cast too wide given that there is no enforcement history or other avenue for guidance.
11.5	Issuance of Block Exemption orders	It is a matter of great concern that the Commission suggests (citing experience in other jurisdictions) that it may take several years before a Block Exemption order is made. As submitted above, it is important that vertical agreements be excluded from the First Conduct Rule by means of a Block Exemption order as soon as legally permissible after the Conduct Rules take effect. Prior preparatory work can be done to ensure that the consultation process on such an Order can be commenced as soon as the Conduct Rules take effect.
11.8	Timeframe for review of Block Exemption Application	As above, the Commission should commit to an indicative timeframe, to be extended if necessary. Although it may be difficult for the Commission to initially estimate the length of time it may require to process a Block Exemption Application, some indication of an approximate timeframe would nonetheless accord greater certainty to businesses.

COMMENTS ON THE DRAFT GUIDELINE ON THE FIRST CONDUCT RULE

A. INTRODUCTION

In this section the Chamber submits its comments on the draft Guideline on the First Conduct Rule.

We have comments on four major issues, namely: the meaning of "object"; treatment of vertical agreements; resale price maintenance ("RPM"); and the exclusion on grounds of overall economic efficiency.

B. THE MEANING OF "OBJECT"

The draft guideline is ambiguous as to meaning of this term. In some places it suggests that there are certain types of agreements which always harm competition and that these are agreements which harm competition "by object". In other places it suggests that every agreement has to be looked at on a case-by-case basis, and if it is clear that the provisions of the agreement, considered in their legal and economic context, harm competition, then they harm competition "by object" and no detailed assessment of the agreement's effects on competition is required. The latter is the correct approach, and this should be clarified. As noted in our Preliminary Comments above, the Chamber had always understood, during the passage of the Bill through LegCo, that the focus would be on the anti-competitive effects of conduct, and that no types of conduct would automatically or always deemed to be anti-competitive.

C. THE TREATMENT OF VERTICAL AGREEMENTS

The draft guideline (correctly) states that vertical agreements are generally less harmful to competition than horizontal agreements. In fact, it is generally recognised that they are only potentially harmful to competition if one of both parties have substantial market power or dominance, in which case the Second Conduct Rule is sufficient to deal with any problems which may arise. Both the EU and Singapore provide clear safe harbours for verticals, and it is unclear why an appropriate safe harbor is not being proposed in Hong Kong, especially with its traditionally free market, non-interventionist approach.

The Guideline should state that vertical agreements will only be tackled under the Second Conduct Rule, pending a block exemption order for vertical agreements, which should be consulted on and issued at the earliest possible date after the Conduct Rules take effect.

D. RESALE PRICE MAINTENANCE

The draft guideline states that resale price maintenance restricts competition "by object" (see the table at 6.9 and 6.64). However, it is generally considered that a detailed case-by-case examination of the economic effects of RPM is needed before it can be concluded that it harms competition. Paragraph 6.62 implies that this is the case. The references to RPM having the object of harming competition should therefore be deleted.

E. EXCLUSION ON GROUNDS OF OVERALL ECONOMIC EFFICIENCY

While it is appropriate that agreements which produce overall economic efficiencies outweighing the harm to competition should be allowed, greater guidance should be given on how this balancing exercise is to be conducted.

F. COMMENTS ON THE GUIDELINES

Para / Ref.	**Issue**	**Comment**
2.16 and 2.17	Restriction on contact with competitors	Since any arrangement between competitors (such as a supply arrangement or joint venture) will result in different conditions of competition than would otherwise prevail, and influence each business's conduct on the market, these paragraphs appear to suggest that any such arrangement will be prohibited. We presume this is not the intention, and competition laws in other jurisdictions do not prohibit any such contact. These paragraphs need to be altered to reflect the correct extent of permissible contact between competitors.
3.4 to 3.9	The "object" of harming competition	3.4, table at 6.9 and 6.10 indicate that "object" means certain types of agreement (i.e. those listed in the left-hand column of the table) will always (i.e. *per se*) harm competition, without the need for assessing their actual effects. However, 3.5, 3.6 and 3.8 contradict this, by stating that each agreement has to be considered individually against (among other things) its economic context to assess whether it has the object of harming competition. In fact, it is the second proposition which correctly reflects EU law, from which the concept of "object" is derived. This interpretation is also consistent with comments made by the Government during the passage of the Bill through LegCo and its earlier proposals, to the effect that there would be no conduct which would be automatically deemed harmful to competition and that a case-by-case assessment of effects on competition is always necessary. Those statements which suggest that there are certain types of agreement which always harm competition should therefore be deleted.
3.5, 3.6 and 3.8	Distinction between "object" and "effect"	Given that the "economic context" and "surrounding circumstances" of each agreement need to be assessed to determine whether it has the "object" of harming competition, how is this different from examining its effects? The question is one of degree and standard of proof: if it is obvious from the agreement's provisions, assessed in the light of its legal and economic context, that the agreement harms competition, it will have the "object" of harming competition. If it is not obvious, a

Para / Ref.	Issue	Comment
		full examination of the agreement's effects is required. This should be stated in the guideline. In our view there should be no objection to this more 'visceral' approach to identifying 'by object' infringements. This approach is effectively the one endorsed by the Court of Justice of the EU in its most recent ruling on the issue[6]. Nor should it prove to be too limiting in practice for the HKCC. After all, if there is a strongly held belief that an arrangement is anticompetitive 'by object', then it should not be too onerous for that authority to demonstrate likely or actual anticompetitive effects.
3.12 to 3.18	The "effect" of harming competition	"Anti-competitive" effects are defined as occurring where, due to the agreement, the parties can profitably raise prices or reduce output, product quality, etc. This is similar to the definition of "substantial degree of market power" ("SMP") under the Second Conduct Rule guideline. Moreover, in 3.17, the series of factors that will be taken into account in assessing where the parties can exercise such power as a result of the agreement are the same as those used in assessing SMP under the Second Conduct Rule. Therefore, to simplify matters, and in the interests of consistency, we recommend that the concept of SMP be used for both conduct rules, and that agreements will only have the object or effect of harming competition if they result in SMP. This would avoid the necessity of distinguishing between "market power" and "substantial market power", which is a very subjective and arbitrary assessment. Moreover, it should be made clear that for an agreement to be found to have harmful effects on competition, those effects have to be proved by means of a robust and detailed economic analysis.
4.3	Burden of proof as to whether Schedule 1 paragraph 1 exclusion (overall economic efficiency) applies to an agreement	We can see nothing in the Ordinance which suggests that this burden should rest on the businesses concerned, contrary to what this paragraph currently states. The Commission should be (and in our view is) obliged to prove to the requisite standard before the Tribunal not only that the agreement prevents, restricts or distorts competition but also that it is not excluded from the First Conduct Rule. It is true that a party seeking a decision under section 9 will have to produce reasons as to why an exclusion applies, but this does not alter the fact that the overall burden of proving a contravention rests on the Commission.
5.2	Relevance of	This paragraph states that the definition of Serious Anti-

[6] See *Groupement des cartes bancaires (CB)* v *European Commission*, Judgment of 11 September 2014: CB / Commission (C-67/13 P) ECLI:EU:C:2014:2204.

Para / Ref.	Issue	Comment
	"Serious Anti-Competitive Conduct"	Competitive Conduct ("SAC") is "largely" of procedural relevance. In fact, under the Ordinance, SAC is only relevant insofar as it does not qualify for (a) the Warning Notice procedure, or (b) the exclusion for "agreements of lesser significance" in Schedule 1 paragraph 5. SAC should not be confused with agreements which have the "object" harming competition (see comments on 3.4 to 3.9 above) which is a totally separate issue. In the interests of clarity, this sentence should be deleted.
6.5 to 6.8	Vertical Agreements	These paragraphs recognise (correctly) that vertical agreements are generally less harmful to competition than horizontal agreements. This is why in Singapore and the EU (for example) they have been excluded from the First Conduct Rule equivalents – in the former by means of an exclusion in the law itself, and in the latter by means of a block exemption. The Commission should adopt a block exemption for vertical agreements at the earliest possible date following the entry into force of the Conduct Rules, as advocated in our response to the draft guideline on Applications. In the meantime, the first sentence of 6.8 should be elaborated, by stating that vertical agreements will not be regarded as a priority for enforcement under the First Conduct Rule, and will normally only be tackled under the Second Conduct Rule, with the possible exception of RPM (see below).
6.9	Resale price maintenance ("RPM")	RPM should not be regarded as having the "object" of restricting competition, as indicated in the table, because a full assessment of its economic effects in any given case must be conducted before it can be concluded whether it harms competition. Similarly, it should be made clear that RPM does not constitute price-fixing under the definition of SAC, since SAC is only intended to catch horizontal conduct between competitors (contrary to what 5.6 currently states). 6.10 to 6.14 correctly regard price-fixing as horizontal conduct. In fact, 6.62 itself indicates that a case-by-case assessment of economic effects is required. Further comments on RPM are given in relation to paragraphs 6.61 to 6.75 below.
6.10	"Price-fixing"	6.10 is inconsistent with 3.5. Whereas 6.10 implies that price-fixing and other certain types of agreement will be regarded automatically ("in themselves") as harming competition, 3.5 states that a case-by-case assessment of each agreement must be made in the light of "the content of its provisions, its objectives and the economic and legal context of which it forms part …" etc. As

Para / Ref.	Issue	Comment
		noted in our comments on 3.4 to 3.9, the latter is an accurate reflection of EU law (from which the concept of "object" is derived) and is consistent with the Government's previous proposals and comments to LegCo. 6.10 therefore needs to be amended or deleted to reflect this.
6.14	"Price-fixing"	The last sentence of this paragraph appears to equate "intention" with "object", whereas 3.6 suggests that the two concepts are different. This should be clarified. Moreover, Hypothetical Example 5 raises a number of problems: (a) It suggests that the mere fact that "a number" of new car dealers enter into the agreement in question means that the agreement has the "object" of harming competition. But as the agreement has to be looked at in its economic context before it can be concluded that it has the "object" of harming competition (see comments on 3.5, 3.6 and 3.8 above), the number of dealers which are party to the arrangement, as well as their size and market position, are highly relevant for this purpose. As noted above, price-fixing is not *per se* harmful to competition under EU law. If 2 out of 20 dealers entered into the agreement, it is not clear from the economic context that it would harm competition in the market (in fact it might increase competition by enabling them to compete more effectively with the other 18) and therefore the agreement would not have the "object" of harming competition. But the opposite might apply if all 20 did. (b) What if the operators in question went a step further and formed a joint venture to sell cars, by definition at a uniform price. (Joint selling ventures do not appear to be covered in the draft guideline) Would this be regarded as price-fixing? Cartel conduct does present very real definitional and coverage problems. To assist in bringing essential clarity to this area, the guideline could usefully explain the common characteristics of price-fixing and the other three SAC conducts that constitute cartel behaviour: e.g. no integration of operation, no sharing of risk and reward from respective transactions, typically covert, etc.
6.16	Market-sharing	The first sentence suggests, as in the case of price-fixing, that market-sharing is regarded as *per se* harmful to competition and therefore having the object of harming competition – as noted above, this is not a correct reflection of EU law. See further our comments above in relation to 'by object' infringements.

Para / Ref.	Issue	Comment
		It is noted that legitimate JVs can involve market sharing. The differentiating factors between this and a potentially anticompetitive market-sharing agreement include the wider context, customer knowledge, etc. It would also help if the guideline again made it clear that what is of concern under this head is secret arrangements between rivals. As with other SAC conduct, it would assist if there could be more definitional analysis of scope and characteristics the market sharing arrangements that will be considered SAC/cartel condcut so that they can be distinguished from legitimate commercial arrangements e.g. no integration of operation, no sharing of risk and reward from respective transactions, typically covert, etc.
6.61 to 6.75	Resale Price Maintenance ("RPM")	As noted above, the factors listed in 6.62 indicate that a case-by-case assessment of *inter alia* the economic context is necessary before concluding that RPM harms competition, and paragraph 6.64 is incorrect in stating that direct or indirect RPM will be considered automatically as having the object of harming competition, without regard to its economic context. There are very valid reasons why businesses might seek to impose RPM restraints e.g. to prevent free-riding which undermines anchor stores that invest to bring new products to market, promote the brand, educate consumers and display a wide range of products when they are undercut by stores that do not provide these services, depriving the anchor store of the economic incentive to bring these benefits to consumers. Such restraints could only be a potential competition law problem where they are being used to mask a horizontal cartel or where there is a serious deficiency in inter-brand competition. Furthermore, if the product concerned is a new product in Hong Kong which the supplier wishes to be sold above a certain price for image reasons, e.g. a luxury product, the supplier may not be prepared to supply in Hong Kong at all (being a small market) unless the distributor/retailer agrees to RPM. It cannot be said that this harms competition, when the consequence of no RPM may be no product at all for Hong Kong consumers. The above examples demonstrate that, far from the harming competition, RPM can <u>increase</u> competition in certain common situations. Instead of just giving examples of where RPM may harm competition, the guideline should also give examples of where RPM increases competition, such as in the situations described above. This shows that there is certainly no

Para / Ref.	Issue	Comment
		justification for treating for regarding RPM as harming competition "by object". In 6.65 to 6.70, recommended or maximum prices are more likely to promote competition than hinder competition. Again, it would be useful to emphasise this and to give examples of where they promote competition, not just where they might conceivably hinder competition, such as to move old stock, sell new products, short term promotions, enable market entry etc. It may be suggested that companies should, if they see such benefits in RPM arrangements, be prepared to justify them by putting on an efficiency defence under the First Schedule to the Ordinance. However, the cost and risk of running such defences is significant and the reality is that prudent businesses will often opt instead simply not to bring some new products to market in Hong Kong or to refrain from trying to encourage distributors to establish anchor stores to avoid the significant risks that are impose by a presumption that RPM is inherently anticompetitive. Finally, it would be useful to move the definition of RPM from 6.61 to the paragraph where RPM is first-mentioned, so that the reader is clear from the outset what the term means.
6.75	RPM	The last paragraph of Hypothetical Example 16 causes concern. It suggests that a mere restriction on the ability of independent retailers to set prices in itself is deemed to harm competition, without regard to the market context or effects. The last sentence should therefore be supplemented by the words "… and as a result market competition, depending on the economic context, may be harmed", or words to that effect.
6.76 to 6.80	Exclusive Distribution or Exclusive Customer Allocation	These fall within the category of vertical agreements, on which our views are set out in relation to 6.5 to 6.8 above.
6.85	Joint ventures	The second sentence of this paragraph is unclear. Is it suggesting that, if a joint venture is simply an attempt to "disguise" price-fixing which has a negative impact on market competition, it will also be regarded as having the "object" of harming competition? If so, this should be stated.
Annex 2.1 to 2.23	Exclusion for agreements enhancing overall economic efficiency	The confirmation that agreements which produce overall economic efficiencies outweighing the harm to competition is welcome, and reflects the "total welfare" standard which applies in other relatively small, open

Para / Ref.	Issue	Comment
		economies such as Singapore, New Zealand, South Africa, Canada and Australia[7]. Nevertheless, this section of the guideline raises a number of issues which would benefit from further clarification. For example, how are businesses to assess whether the efficiencies are "sufficient to compensate for the harm to competition" (2.8(c))? Especially where the efficiencies are qualitative rather than quantitative (2.10 to 2.14)?

[7] M. Gal *Competition Policy for Small Market Economies*, Harvard University Press 2003, 51-53

COMMENTS ON THE DRAFT GUIDELINE ON THE SECOND CONDUCT RULE

A. INTRODUCTION

In this Section, the Chamber addresses the draft Guideline on the Second Conduct Rule.

B. COMMENTS ON THE GUIDELINES

Para / Ref.	Issue	Comment
2.14	Geographic scope of market	The Chamber would suggest that it should be made clearer that in some industries, the relevant market could be much wider than Hong Kong plus the Pearl River Delta, eg. Asia-Pacific or even the world.
2.17	Hypothetical example	It would be worth adding in hypothetical example 3 the fact that a customer's willingness to travel will depend to a large extent on the value of a product and its availability. For high value products such as computers, furniture etc. the consumer may well be prepared to shop around over fairly wide distances, perhaps even the whole of HKSAR. Also, online ordering may be another possibility, and if so, should be included in the relevant market.
3.2	Market power	Guidance should be given as to how the Commission proposes to determine 'competitive' price for the purpose of assessing market power. If this is to be the benchmark for such a critical test under the Ordinance, the Chamber would respectfully suggest that more guidance needs to be given as to how the Commission will determine a 'competitive' price or 'competitive' levels of quality/output. In this regard, the Chamber would note that it is now universally accepted that perfect competition is not an appropriate benchmark for antitrust analysis and that the benchmark should be workable competition in the industry under consideration. Reference should be made to this in the guidelines and it should be explained in this context how the Commission would assess 'competitive' price levels, output and quality.
3.3	Efficiencies	There is no reference in the guideline as to the relevance of efficiencies under the CR2. If overall economic efficiencies can justify agreements which restrict competition, the same should logically apply to unilateral conduct, whether or not the business has SMP. This should be clearly stated in the guideline.
4.5	Objective purpose	Purpose / object is not a subjective concept. It is respectfully submitted that paragraph 4.5 of the guideline (and the equivalent CR1 guideline) should make it clearer that the 'object' of the conduct in question requires (inter alia) an objective assessment of

		the aims of the conduct, and that, even assuming it is possible, it is unnecessary (and perhaps unhelpful) to investigate the parties' subjective intentions.
4.7	Where conduct has the object of harming competition it is not necessary to show effect	Abuse of market power cases requires assessment of whether there has been, or is likely to be, an exclusionary effect. Conduct cannot be presumed by its very nature to be an abuse of a substantial degree of market power. Conduct that might otherwise be at risk under CR2 can perfectly legitimately be engaged in by companies without a substantial degree of market power. Such conduct can even be engaged in by a company that has a substantial degree of market power so long as it is not considered an abuse of that market power. Para 5.4 is noted in this regard, which makes clear reference to the relevance of demonstrating anticompetitive foreclosure effect in predatory pricing cases. The Chamber respectfully suggests that paragraph 4.7 of the draft guideline should be deleted. The word "object" in CR2 is being used in a similar way to the word "purpose" in the New Zealand equivalent, section 36 of the Commerce Act, which requires three elements to be established: 1. a person or business has a substantial degree of power in a market; 2. that person or business takes advantage of that power; and 3. the *purpose* of the behaviour is to restrict the entry of any person or business into that or any other market, prevent or deter a person or business from engaging in competitive behaviour in that or any other market, or eliminate any person or business from that or any other market. See also the similar approach taken in Australian law. The guideline should also make it clear that the Commission will consider objective justification of the conduct as a valid defence.
4.8	Pricing below average variable cost is an object infringement	Treating pricing below average variable cost as a *per se* (or by object) breach is, with respect, inconsistent with best practice in other jurisdictions. Even in the EU, selling below average variable cost is only presumed to be anticompetitive and this presumption can be rebutted where there is an objective justification. As the Commission notes at para 5.3, charging lower prices is the essence of competition. A *per se* approach to pricing below average variable cost risks sending a chilling effect through the market and dampening aggressive price competition to the detriment of consumers. We predict a great many pricing related complaints which will unnecessarily consume HKCC resources and

		ultimately have a chilling effect of businesses that would find it difficult and expensive to identify and evaluate their internal costs. The Chamber respectfully suggests that para 4.8 needs to be deleted.
4.11	Exploitative effects	CR2 is drafted in substantially different terms to Article 102. Importantly, it does not seek to regulate prices (i.e. it is focused on exclusionary conduct).[8] The list of factors at para 4.11 appears to have been transposed from EU law without consideration for this important difference in drafting and scope. The Chamber respectfully submits that para 4.11 should be amended to make it clear that the law regulates exclusionary abuses i.e. conduct that has the economic effect of impeding effective competition on the relevant market (by forcing out or marginalising existing as efficient competitors and/or raising barriers to entry for potential new competitors) and that, insofar as reference is being made to prices, what will be considered are exclusionary pricing practices (i.e. predatory pricing, price discrimination).
5.6	Recoupment	Predatory pricing can only be economically and commercially rational if the undertaking engaged in the conduct can anticipate being a reasonable prospect of being able to subsequently recoup the losses. The Chamber would respectfully submit that more emphasis needs to be placed on demonstrating recoupment as an essential element of determining that conduct is predatory.
5.15-5.21	"Essential" facilities	While the draft CR2 guidelines recognise that as a general matter undertakings should be free to decide with whom they will do business[9], they go on to say that a refusal to deal by an undertaking with market power could be abusive (albeit in very limited or exceptional circumstances) and that a refusal to licence an intellectual property right could also be a violation in certain circumstances. [10] Such an approach could significantly undermine incentives to innovate (which are the single most important engine of competition), particularly if applied to intellectual property rights. The United States Supreme Court, in its 2004 Verizon Communications decision[11] cautioned against imposing obligations to deal with competitors, in the following terms: *"Firms may acquire monopoly power by*

[8] This is in contrast to the amendments that were made to the Telecommunications Ordinance to introduce a provision, section 7Q, expressly prohibiting exploitative conduct by dominant telecommunications licensees.
[9] Draft CR2 guidelines, para 5.15.
[10] Draft CR2 guidelines, para
[11] Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, Llp (02-682) 540 U.S. 398 (2004) 305 F.3d 89.

		establishing an infrastructure that renders them uniquely suited to serve their customers. Compelling such firms to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities. Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing–a role for which they are ill-suited. Moreover, compelling negotiation between competitors may facilitate the supreme evil of antitrust: collusion. Thus, as a general matter, the Sherman Act "does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal." United States v. Colgate & Co., 250 U.S. 300, 307 (1919)." Given Hong Kong's long-standing market policy and its antipathy towards central planning, the Chamber respectfully submits that such doctrines have no place in Hong Kong law. To the extent that the concern is as to potential "hold up" abuse of patent rights related to standard essential patents, such patents are usually subjected *ex ante* to commitments by the patent holder to licence on Reasonable and Non-Discriminatory (RAND) terms. A refusal to honour RAND commitments can be addressed under the usual prohibitions on exclusionary abuse (e.g. discriminatory pricing) without the need to introduce the controversial concept of "essential facilities" into Hong Kong law.

HKGCC Secretariat

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