Draft Guidelines under the Competition Ordinance

Comments by Hong Kong Cable Television Limited

Two overarching points

The Hong Kong Competition Commission ("Commission")'s draft guidelines ("Guidelines") should be reviewed with two overarching points in mind.

First, important pieces of the jigsaw are not yet in place. These include the guidance on leniency procedures, enforcement policy and institutional cooperation between the Commission and the Communications Authority ("CA").

Second, the picture needs more clarity. Multi-national companies familiar with competition laws may view the draft Guidelines as rather high level. The Commission retains a wide margin of discretion in its future enforcement activities. This approach has resulted in the omission of some important policy areas and a degree of imprecision in respect of certain business critical issues. The consultation process should be used as an opportunity to seek clarification of some of these issues in order to provide greater legal certainty for businesses.

Resale price maintenance automatically illegal?

Resale price maintenance ("RPM") occurs whenever a supplier establishes a fixed or minimum resale price to be observed by its distributor when the product is re-sold. The draft Guidelines treat RPM as a restriction of competition by object and it may amount to "Serious Anti-competitive Conduct". Its mere existence is a serious infringement of the Competition Ordinance ("Ordinance"): the Commission does not need to show the practice leads to anti-competitive effects. However, the Commission has recognised that RPM can sometimes lead to efficiencies that could outweigh any anti-competitive effects. Undertakings replying on this exemption must demonstrate efficiencies and fulfillment of all the conditions listed out in the Ordinance. Does it mean that the chance of the Commission granting such exemption will be very low? So what should companies draw from this guidance?

The Commission's guidance closely resembles that of the European Commission ("EC"). But, the EC's practice is instructive: RPM is more or less prohibited *per se* in Europe – there is no example of the EC deciding that efficiency outweighs the

competitive harm arising from RPM.

There is no single common thread on the treatment of RPM between established competition law regimes. For example, the US Supreme Court has ruled that RPM should not be prohibited *per se* (as had been the case up until the late 90s) and an assessment is necessary as to whether the benefit outweigh the competitive harm. Meanwhile in China, the National Development and Reform Commission of the Government of the People's Republic of China has to date treated RPM as a *per se* restriction of competition and imposed significant fines on the parties involved in such conduct.

Exclusive distribution – the need for a "safe harbour"

The draft Guidelines mention that exclusive distribution agreements may present risks to competition and the effects of such agreements will need to be assessed in order to determine whether they infringe the law.

The draft Guidelines provide very little guidance, however, as to how such agreements are to be assessed, it would seem that companies should undertake their own full competitive effects analysis for every distribution agreement. This is unrealistic: it is both time-consuming and costly. The present guidance risks creating an environment where businesses have to adopt an overly cautious approach to the negotiation of distribution agreements which are broadly recognized in other regimes not to create competition concerns in many situations.

Given the prevalence of such exclusive distribution agreements in supplier/distributor relationships, the Commission could usefully provide a market share threshold below which such agreements would be presumed exempted from the First Conduct Rule – in effect a "safe harbour".

Information exchanged via customers and suppliers – clarifying "hub and spoke"

Anti-competitive exchange of information can take place between competitors (A + B) through the intermediary of a common supplier or customer (S). In such a scenario, S might be considered to be a "hub", collating and relaying commercially sensitive information between the spokes (A+B).

The draft Guidelines provide no guidance on the elements needed for a breach of the Ordinance. The Commission could remedy this by setting out the test established by, for example, the leading UK case law regarding intention and use of the relevant information. Without this additional guidance, the draft Guidelines risk capturing conduct which should be considered as legitimate cross supplier/customer relationships.

Substantial degree of market power: no market share threshold

The Second Conduct Rule prohibits the abuse of substantial degree of market power. Business with a "substantial degree of market power" will have "special responsibilities", a concept borrowed from the EU. However, the draft Guidelines do not provide any indication of the level of market share at which a company might be viewed as holding such power.

This silence confers discretion on the Commission. It also creates business uncertainty as a market share threshold of 25% (possibly even lower) was debated during the legislative passage of the Ordinance and gained some traction. So, the 25% figure remains in play. This would leave the Commission at odds with most established and mature antitrust regimes, which typically provide a higher indicative market share threshold.

A reasonable indicative market share threshold would serve as a useful screening device for companies to determine whether or not they are more or less likely to be subject to the "special responsibilities" imposed by the Second Conduct Rule.

While a clearly defined market share threshold would create certainty in determining whether there is "substantial degree of market power", for certain industries such as power and transport sectors, companies will have to own relatively large market share in order to achieve economies of scale. To balance the interests of different industries, would the Commission consider setting a fixed market share threshold to determine "substantial degree of market power" and at the same time, grant exemptions to certain industries like power and transport sectors?

An emphasis on exclusionary abuses of market power?

The draft Guidelines address exclusionary abuses of the market power. These include:

- Predatory pricing
- Tying
- Bundling
- Margin squeeze
- Refusal to deal
- Exclusive dealing

These abuses are considered to be exclusionary in nature as the relevant conduct aims unjustifiably to exclude competitors from the market. The Commission has not discussed exploitative conduct (e.g. excessive pricing) in the draft Guidelines. Nor was exploitative conduct a feature of the legislative discussions on the Ordinance. This may suggest a keen enforcement focus on exclusionary abuses.

This focus mirrors other established competition authorities, such as the EC. But even without guidance, it is premature to conclude that the Commission will not concern itself at all with exploitative abuses as a matter of policy. It will then be up to the Commission to consider further and decide whether such exploitative conduct also falls under the second conduct rule?

When can the Commission refuse to investigate complaints?

Complaints will be a key source of business for the Commission. Along with leniency applications (for which draft Guidelines are yet to be produced), complaints are a straightforward way for the Commission to identify possible infringements of the Ordinance. The draft Guidelines encourage the making of complaints by "any person", and in 'any form', including anonymously. This is broader than the approach in the EU, for example, where the complainant must demonstrate a "legitimate interest" in relation to the subject matter of the complaint.

Despite this apparent encouragement, the draft Guidelines stress that the Commission retains the discretion not to investigate complaints. The ability for the Commission to prioritise is sensible from a policy perspective, and in keeping with the position in the EU. However, the Hong Kong regime is structurally different from the EC's regime and the guidance on this discretion is likely to prove contentious.

Further, given the likelihood of opening a floodgate of frivolous and vexatious complaints, are there any practical and effective procedural safeguards to filter out unwarranted cases to avoid abuse of process?

Cooperation with foreign authorities

As a new competition authority in a global economic hub, it is likely that the Commission will be keen to cooperate with overseas competition agencies, and companies will be keen to understand the extent to which the Commission intends to cooperate with other agencies. Both the Ordinance and the draft Guidelines are silent on this issue.

The Commission is a member of the International Competition Network (ICN). The critical issue is sharing confidential case material in international investigations. The draft Guidelines are silent even as to whether this is possible, and give rise to uncertainty on some key issues. More specifically, it is unclear how and when contact between the Commission and overseas agencies will take place, what type of information may be exchanged and how the Commission will treat confidential information it may receive from those overseas agencies. Further guidance would be welcomed.

The circularity of applying for exemptions

Various exclusions and exemptions from the Conduct Rules are provided for in the Ordinance, notably for agreements that generate economic efficiencies. According to the draft Guidelines, companies can either self-assess the legality of their conduct according to this test or they can apply to the Commission to that effect if they require "greater legal certainty", i.e. to confirm the application of the general exclusion.

Can the Commission rely on information and evidence received during the course of a company's application for a decision to initiate enforcement action against any company?

The draft Guidelines provide no explanation on how will the Commission charge the companies for making application for exemptions. By hourly rate?

We are grateful for being given the opportunity to offer our comments on the draft guidelines. We hope they will be useful.

Hong Kong Cable Television Limited