Grasping the nettle – Your Role in Shaping our Guidance

Keynote Speech by Ms Rose Webb
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Thank you David and good morning ladies and gentlemen, and for some of you, if I may say this as a resident for just two months now, welcome to Hong Kong.

My thanks go to Kluwer Law International for the invitation to be your keynote speaker. It's great to see some already familiar faces around the room and I look forward to meeting with more of you in the course of today. As you might imagine, over the past few weeks I've been on an enormous learning curve about Asian competition law. I look forward to progressing up that curve a little further today..

This morning I would like to use this opportunity to outline two areas of the Commission's work.

- First, an update of where we are at in our Engagement process and our path to full commencement of the Competition Ordinance.
- Second, I want to raise a number of some of the trickier unsettled issues in the Ordinance that we are currently grappling with. I hope the topics I've chosen will provoke further debate today and beyond.

Engagement Update
First, what has happened in the past year and what's next.

Many of you here today will be aware of our recent activities so let me just provide a brief recap.

As you will know the Competition Ordinance was passed in June 2012 and, in May 2013, Anna Wu, our Chairperson and 13 Commission Members were appointed. Since then a lot of work has been done to build up the infrastructure of the Commission. We now have an office and a dedicated team of about 35 staff in place from both Hong Kong and overseas, with more to come.

A month ago, following a briefing to the Economic Development Panel of LegCo, we launched an "Engagement" process as a prelude to consulting on our guidelines. Before the Ordinance comes into effect, we are tasked to develop guidance that will set out:

- how the Commission expects to interpret the Conduct Rules;
- what type of processes we will have in place for exclusion and exemption applications; and
- how we will deal with complaints and investigations.

We expect to publish the draft guidelines in September for formal public and LegCo consultation. Based on the comments and feedback we receive, we will then publish the final version of the Guidelines.

We are actively working to ensure that what we produce is practical, understandable and useable for all the relevant stakeholders. However, recognising that the guidelines will inevitably be technical we also propose to publish a number of other publications that will help businesses and the public understand the Ordinance and how the Commission intends to approach its enforcement role.

The Commission's target is to complete all its preparatory work by the first half of 2015. The government and the Tribunal will also be undertaking preparatory work in parallel including making necessary regulations. It will be then for the Government to set the commencement date for the Ordinance.

Engagement is an on-going role

I should emphasise that the end of the initial Engagement phase next month is not the end to our wider role in advocacy and education. In the last month, as we have met with a range of business and professional organisations, we have often heard that there is a lack of knowledge about competition law and that, companies are struggling to work out how to comply.

Clearly, there remains further work, by the Commission, but also by lawyers and businesses, to ensure everyone understands why competitive markets are important and appreciates the impact of the Ordinance.

In fact, earlier this week we held our first SME Seminar at the Commission. With a good range of SME associations and individual SMEs attending, we provided them with an overview of the key provisions and a series of clear "dos" and "do not's". We will be holding another seminar at the end of July and would encourage you to flag this event to any potential attendees (details are available on our website).

While the key messages of the Ordinance for SME's are relatively straight forward, more generally we acknowledge that at present there are question marks over the likely approach of the Commission to a number of issues, and I will come to some of those shortly. Our Guidelines will provide the roadmap for our interpretation on a range of agreements, practices and conduct – giving companies and their advisors an indication of our enforcement direction and a sufficient basis for self-assessment.

However, in the end no matter how effective the Commission's engagement and advocacy work is, businesses must be the ones to put themselves into a compliant position.

What I have taken away from discussions so far, is that in many companies with activities in Hong Kong there is the need for a culture change. One of the stakeholders we were talking to described it as a need for "realignment" in his industry sector. I thought this was a nice way of putting it.

The introduction of the Ordinance is not going to undermine the essential operations of existing businesses in Hong Kong. But there a shift is needed in the future business model for Hong Kong, it must be competition, not collusion.

This leads me onto the second part of my comments today.

Themes for discussion

As we move closer to publishing our draft Guidelines there are a number of more difficult substantive topics that we will need to give some firm views on to form a proper basis for discussion.

Our Discussion Note published at the end of May included three themes that I will explore a little more now:

- Vertical agreements
- Information exchange and
- Substantial market power.

Vertical agreements

In preparing for today, I was reminded of the volume of ink that was spilled on the topic of vertical agreements during the Bill stage. There were many calls for verticals to be entirely exempted from the Ordinance following the approach taken in Singapore. Failing that, the alternative was that they should only be assessed under the Second Conduct Rule. Both of those options were resisted by the Government and thus we now have before us the question of how to best deal with vertical restraints under the First Conduct Rule.

We are aware that this is a topic that businesses and enforcement agencies across Asia and beyond are recognising as one of the more thorny issues to address. Indeed, I'm sure we will be hearing more on this topic today.

Unlike what I see as a global consensus and convergence on cartels, vertical restraints prompt varying reactions and policies from antitrust authorities. Here in Asia particularly, there is no uniform approach in spite of the fact that certain categories of vertical restraints have prompted a string of recent enforcement actions.

For example, in China, we are all aware of the NDRC's investigations in a range of industries in the past couple of years including baby milk and, optical lenses. Similarly, a brief review of agency websites and reports in Taiwan, South Korea and Malaysia all reveal verticals to be a topic of recent investigations.

And beyond Asia, we can see in the UK, OFT/CMA closely examining RPM and other vertical arrangements in sectors as diverse as hotel booking websites, mobility scooters and until recently sports bras.

Similarly, in Australia, a number of companies have been investigated and as recently as last December a fine of $2.2 million being imposed by the Federal Court for RPM in the air-conditioning sector.

Indeed, if you'll allow me a small indulgence the Australian court report contains one of my favourite paragraphs in a recent judgment. In outlining the evidence before him the judge said:

Following his discussion with the employees of (the target company), Mr X sent an email to Mr Y which stated:

"*They will make an adjustment.*
I have told them they are somewhere around $200 off the current market recognised sell price. Of course this has all been of a verbal nature as we cannot be seen to be price fixing ($500k personal fine)."

So what about verticals here in Hong Kong?

In casting around the world for their respective approaches to vertical agreements including RPM, there is clearly a wide spectrum of approaches.

I don't want to prejudge our on-going discussions in relation to the manner in which the Commission expects to interpret and give effect to the First Conduct Rule. However, it is unlikely that the Commission will end up at either extreme of the spectrum. This is because:

- First, one size does not fit all. Not all vertical restraints bring the same inherent risks of being found to be anti-competitive. Indeed, in the Hong Kong context, some may be entirely benign., There may be more likely to be a problem when the companies involved have some market power.
- Second, we recognise, in line with antitrust economics and international best practices, vertical agreements are, in general, much less likely to have adverse impact on competition compared to, for example, a price fixing cartel. However, I stress that is a generalisation and of course, there will be circumstances when vertical restraints damage intrabrand competition and have an impact on other business and consumers in terms of higher prices and restricting choice for products or services.

- Third, we recognise that there may be genuine efficiency justifications for certain vertical restraints. For example, overseas experience shows RPM can be justified where it is seen as a temporary measure to foster market entry or in the introduction of a new product or service. Likewise, such practices can be seen as a solution to prevent the so called issue of "free-riding".

Information exchange
The second theme I'd like to explore is information exchange.

Purely based on what we read and see in the media, today, there are companies or trade associations that seem to regularly discuss, formally or informally, competitively sensitive information.

We know that information sharing is an area in which our guidance will need to

distinguish between illegal and the innocent or even pro-competitive forms of information sharing. In this area too, Commission discussions are on-going as to the type of information exchanges that we would view with suspicion.

I think what is already clear, and this is not unsurprising, is that if competitors exchange information that enables them to engage in price fixing, market sharing, output restrictions or bid rigging, such activities are serious forms of anti-competitive conduct. Exchanging, for example, future price intentions with a competitor is highly likely to be of concern.

Whether this is done bilaterally or through a well-meaning trade association, in the board room or on the golf course, information exchanges that facilitate cartels or remove the inherent uncertainty of competitive markets are at risk under the Ordinance.

At the same time, we also are recognising that there are completely innocent information exchanges occurring across many industries and some may even generate synergies and be pro-competitive. For example, regular benchmarking, R&D projects or discussions on achieving common technical standards for a new product/service all may be credible efficiency enhancing explanations.

Again, we welcome your input as to how we ought to interpret and give effect to the First Conduct Rule in this regard. We must be able to strike a balance between cracking down on cartels and giving sufficient guidance to allow companies to engage in innocent activities which may even develop the Hong Kong economy.

Substantial market power

The third aspect I wanted to raise was just how substantial is substantial market power.

As you will know, there was a conscious decision for the Ordinance to not have a dominance test, but to rely on a different standard of substantial market power. Across the world there are many different levels justifying intervention for purely unilateral conduct. Whilst those with a European background may be more at home in the language of dominance, jurisdictions such as Australia or New Zealand have long relied on substantial market power as the relevant test. In those jurisdictions, we have been able to provide robust and practical guidance for businesses.

I am aware that during the legislative process, the Government indicated a safe harbour of 25% market share by which an undertaking was unlikely to be found to have substantial market power. However, I would like to avoid the 25% or indeed any figure as the focus of our discussions.

Section 21 of the Ordinance requires the Commission to consider a "range of factors" in making its assessment. Indeed, I think it would be quite misplaced, for any agency, including the Commission, to solely rely on a market share alone to be sole evidence of substantial market power.

Perhaps my past three years doing merger regulation in Australia has left me jaundiced and cynical. But in my experience any number an authority sets as an indicator can somehow be worked towards by the parties with a bit of imaginative manipulation of the data. I think most antitrust authorities have a natural fear of market share indicators turning into a permanent line in the sand.

I thus think it is important that any market share threshold is put in context. An indicator remains just that and an assessment of substantial market power must be taken in the round.

Some of the topics we may seek to address in the guidance include,

- **Barriers to entry and expansion** that is, to what extent do existing market structures suggest that future entry or expansion is going to be likely, timely and of sufficient scale that would serve as credible competitive constraints on an undertaking. Indeed, I will be interested to hear from Miguel later today on the IPR/antitrust interface. I hope he may address how IPR can be a barrier or worse, an insurmountable hurdle, for entry in certain markets.
- Also, we will need to reflect on to what extent being **conferred a role or power by government** would amount to market power. For example, there can often be complicated relationships between undertakings and government entities or statutory bodies here or elsewhere. We would be interested to hear what issues you think that raises in the Hong Kong context.
- Similarly, we may need to consider how the **size of the Hong Kong economy** and its role as an import/export hub may impact on the assessment of market power.

Conclusion

I'm conscious that in concluding today I have probably raised more questions than provided you with a set of definitive positions of the Commission. We've appreciated the feedback we've received so far, so I hope I have prompted a bit more.

However, I hope you understand that we are in a position now where policy is being formulated and shaped around the views we hear and the submissions we receive from you and others.

As Anna Wu our Chairperson said yesterday, and I will repeat today, in the coming months we look forward to hearing from you in business and the legal community in helping us ensure the Guidelines are fit for purpose. We want to work with you to create an environment that ensures companies are ready, willing, and able to comply with the Ordinance upon commencement.

I look forward to hearing what I am sure will be very interesting discussions for the rest of the day.

Thank you.

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