

Hong Kong Enacts Competition Law

July 2012

After years of debate, on 14 June 2012 and in its last days of office, the Legislative Council finally enacted Hong Kong's first cross-sector competition law. Although the Competition Ordinance provides a framework for what is generally agreed to be a controversial new area of regulatory control for Hong Kong, much work is yet to be done before the law can be implemented, which is not expected to be before 2014. During the transitional period, the Government will take steps to establish a new Competition Commission and Competition Tribunal under subsidiary legislation subject to negative vetting by the Legislative Council.

Once established, the Commission will have an important role educating the public on the implications of the new law and must (again in consultation with the Legislative Council) issue guidelines setting out its policy on the scope of the competition rules and any exemptions, as well as procedures for such matters as enforcement, handling complaints and conducting investigations. Although there is much to be done before the law comes into effect there will be no grace period. Any activities or arrangements which are not now compliant with the law will be affected if they continue to have effect after it comes into force. Companies and individuals should now undertake a review of their agreements and practices to assess whether they may be held to be anti-competitive.

Scope of the Ordinance – Anti-Competitive Conduct

With 177 Sections and nine Schedules, the Ordinance is a substantial piece of legislation. Anyone looking for a definition of "competition" will find none, though four kinds of "serious anti-competitive conduct" are broadly defined, namely price fixing, market partitioning, fixing the production of goods or services and bid-rigging (itself defined to include bidding or not bidding by agreement). Consistent with international practice, the following two types of anti-competitive conduct are prohibited, unless otherwise exempted under the Ordinance.

The "first conduct rule" prohibits agreements and concerted practices by businesses the object or effect of which is to prevent, restrict or distort competition in Hong Kong. This targets both anti-competitive agreements between competitors and between non-competitors (for example, a company and its distributor or customer). Serious anti-competitive conduct will be the main focus of enforcement. Other types of arrangements – both between

competitors (such as cooperation agreements) and non-competitors (such as distribution contracts) – are less exposed to future enforcement activity; if such types of agreements are found to be anti-competitive, the parties will be given a "warning notice" first and only be proceeded against if they refuse to change the conduct or repeat it.

The "second conduct rule" prohibits businesses with a "substantial degree of market power" from abusing that power by engaging in conduct that has the effect or object to prevent, restrict, or distort competition in Hong Kong. Though not defined, having substantial market power implies a lower threshold than being in a dominant position. Specifically mentioned in this category are predatory behaviour towards competitors (for example driving them out of the market by undercutting) and limiting production, markets or technical development to the prejudice of consumers.

Unlike in most other jurisdictions, cross-sector merger control is not governed under the Ordinance except as regards holders of telecommunications carrier licenses in Hong Kong, as already reflected under the Telecommunications Ordinance.

Exemptions

Exemptions from some or all of these provisions apply notably to "statutory bodies," being bodies established under an Ordinance (other than the Companies Ordinance), unless otherwise specified by regulation (in practice a very limited number are expected to be so specified).

Exemptions aimed at SMEs apply in the case of the first conduct rule to "agreements of lesser significance," where the combined annual turnover of the businesses concerned does not exceed HK\$200 million and in the case of the second conduct rule to "conduct of lesser significance" where the turnover of the business does not exceed HK\$40 million.

Other exemptions which will require particular economic analysis extend to agreements which are indispensable to improving production or distribution or which promote technical or economic progress. Activities strictly required to comply with the law are likewise exempt, as are those relating to public services and others (yet to be determined by the Chief Executive in Council) based on public policy or international obligations.

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Institutions and Procedures

While the substance of competition regime under the Ordinance largely follows the European model, enforcement of its provisions is more inspired by the US model, in particular by providing for a system of judicial enforcement.

In the interim period before the Ordinance enters into force, a Competition Commission ("Commission") and Competition Tribunal ("Tribunal") will be established. The Commission will be an administrative body whose main task is to investigate suspected conduct and, if it believes the conduct is anti-competitive, bring proceedings in the Tribunal.

The Tribunal will consist of judges from the Court of First Instance. If it finds the Commission's case to be sound, the Tribunal can make a variety of decisions including imposing a fine of up to 10% of the perpetrator's annual turnover in Hong Kong (for a maximum of three years).

During the administrative process, the Commission has various means to "settle" a case by accepting a commitment from a party under investigation. However, if the party resists settlement, the Commission has no direct enforcement powers – for example, it cannot directly impose sanctions – but must instead initiate proceedings in the Tribunal.

The Ordinance does not enable entities or persons other than the Commission to bring actions before the Tribunal or other courts in Hong Kong. Nevertheless, "follow-on actions" are possible under which a third party is entitled to bring proceedings in the Tribunal to seek compensation for damages as a result of conduct held (or admitted in a commitment) to be anti-competitive by the Tribunal (or on appeal) in prior proceedings initiated by the Commission.

In the telecommunications and broadcasting sectors, the Communications Authority has the same enforcement powers under the Ordinance as the Commission. The Ordinance requires the two agencies to issue a memorandum of understanding explaining how they plan to exercise their concurrent jurisdiction in these sectors.

Impact on business

During the interim period, businesses should review the extent to which they may or may not be compliant under the Ordinance when it comes into force.

Clearly, cartel conduct will be the key focus of enforcement under the Ordinance. Businesses should therefore make sure their key personnel, including management, sales and marketing staff (and legal department) are familiar with the restrictions when communicating and dealing with competitors. Experience in other jurisdictions shows that it

can take a while before compliance training and other preparatory measures start to yield results.

In addition, as guidelines on the various types of anti-competitive conduct will be developed over time, businesses should get a sense of their obligations under the Ordinance. A review of cooperation, distribution and sales agreements, as well as other types of agreements and practices such as information sharing will lay the basis for assessing whether a company is compliant under the first conduct rule and/or has a substantial degree of market power, triggering the application of the second conduct rule.

Although having to focus attention on potentially anti-competitive practices under the Ordinance may be a burden for some companies doing business in Hong Kong, any company engaged in international activity may or should already be familiar with such obligations elsewhere. Hong Kong finally accepting the need to curb anti-competitive activity should not only encourage a more level playing field for businesses, but also have the concurrent benefit of reducing the risk that agreements or practices in Hong Kong breach antitrust rules in other jurisdictions.

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