For discussion
on 24 April 2012

Bills Committee on Competition Bill

Responses to follow-up questions arising from previous meetings

Purpose

This paper responds to questions raised by Members at previous meetings.

Responses to submissions

2. Our response to the submissions made by the Hong Kong General Chamber of Commerce, PCCW Limited and HKT Limited, and the Hong Kong Association of Banks in March/ April 2012 concerning the Competition Bill (the Bill) is set out at **Annex A**.

Responses to questions related to market power threshold and conduct of lesser significance arrangement

(a) Market power threshold

3. At the meeting on 10 April 2012, some Members considered that the proposed minimum market share threshold of 25% for the second conduct rule might be too low to address the concerns of the small and medium enterprises (SMEs). On the other hand, some Members were concerned that further increase in the minimum market share threshold might seriously affect the effectiveness of the Bill.

4. It should be noted that the market share threshold of 25% proposed to the Bills Committee (see LC Paper No. CB(1)1506/11-12(02)) aims to provide an indicator of the minimum market share threshold **below** which an undertaking would unlikely possess a substantial degree of market power. It should be distinguished from a market share threshold of "*presumed market power*" **above** which a substantial degree

of market power is presumed. For the latter, we have indicated in the public consultation document "*Detailed Proposals for a Competition Law – A Public Consultation Paper*" in 2008 that it should be about 40% given Hong Kong's circumstances (vis-à-vis the market share threshold of presumed market power of 50% proposed by some sectors of the business community and 30% by the Consumer Council).

5. Raising the minimum market share threshold further to 30% or 35% as suggested by some Members might have the effect of excluding certain oligopolies altogether from the application of the second conduct rule, since these undertakings might each have a market share of around 30% only but they may have significant market power and influence over a market. This would significantly affect the effectiveness of the Bill in dealing with the conduct of oligopolies which are not uncommon in many sectors in Hong Kong.

6. To provide more certainty to SMEs, we have already provided in the Bill a statutory conduct of lesser significance arrangement. As suggested in our paper for the Bills Committee meeting on 10 April 2012 (see LC Paper No. CB(1)1506/11-12(02)), the turnover threshold for the conduct of lesser significance would be increased from HKD 11 million to HKD 40 million. As a result, nearly 95% of all SMEs would be excluded from the application of the second conduct rule. For SMEs with turnover over HKD 40 million, they would also not be regarded as having a substantial degree of market power if their market share is below 25%, unless there is other strong evidence suggesting otherwise.

7. Taking account of the above, we consider that the proposed minimum market share threshold of 25% combined with the conduct of lesser significance arrangement have already struck a balance between the interests of SMEs and the need to maintain the overall effectiveness of the Bill. We therefore do not suggest further adjustment to the minimum market share threshold.

8. This notwithstanding, we note Members' suggestions that other factors apart from market share percentage might need to be taken into account in assessing market power of an undertaking, and that consideration should also be given to the specific conditions of different markets. Overseas experience also suggests that factors other than market share such as the undertaking's power to make pricing decisions and barriers to entry to a market may also be relevant to the assessment of market power. Taking account of overseas experience and Members' suggestions, we propose to include in the Bill the relevant factors that

may be taken into account in determining whether an undertaking has a substantial degree of market power. We propose to amend clause 21 of the Bill, by adding a new sub-clause, as follows –

*"21. **Abuse of market power***

(2A) Without limiting the matters that may be taken into account in determining whether an undertaking has a substantial degree of market power in a market, the following matters may be taken into consideration in any such determination –

(a) the market share of the undertaking;

(b) the undertaking's power to make pricing and other decisions;

(c) any barriers to entry to competitors into the relevant market; and

(d) any other relevant matters specified in the guidelines issued under section 35 for the purposes of this paragraph."

(b) Threshold for conduct of lesser significance arrangement under the second conduct rule

9. In response to Member's request, the thresholds proposed by different parties for exclusion from the application of the second conduct rule under the conduct of lesser significance arrangement are set out in the table at **Annex B**. Our responses to these suggestions have been presented to the Bills Committee at the meeting of 10 April 2012 (see Paper No. CB(1)1506/11-12(02)).

Responses to other issues

(a) Clause 2 (supplementary note)

10. We have reconsidered the desirability of adding the proposed note to the definition of "*serious anti-competitive conduct*" in clause 2(1) of the Bill in light of Members' comments. We remain of the view that the note would be useful in reminding readers that provisions

supplementing the definition are contained in clause 2(2). Given that *"serious anti-competitive conduct"* is an important concept in the Bill, the note would assist readers to more quickly understand the concept and gain a complete picture of the meaning of the expression. In addition, clause 2(3) of the Bill clarifies that the note is not intended to have legislative effect in the same way as a clause in the Bill. The note is provided for information only and plays no interpretative role.[1]

(b) Clause 118

11. Clause 118(2) provides that the Court of First Instance (CFI) or the Competition Tribunal (CT) is bound by any earlier decision of the CFI or the CT that certain act is a contravention or involvement in a contravention of the conduct rule, subject to the expiry of certain periods for appeal set out in clause 118(3). Some Members were concerned that the term *"any earlier decision"* could be construed to include a decision that is overruled by an appeal.

12. It is our policy intent that the CFI or the CT should be bound by an earlier decision of the CFI or the CT. If an appeal is made against such decision, the decision should bind the CFI or the CT only if the decision is not set aside during the appeal process. To put things beyond doubt, we suggest adding a sub-clause to clause 118 as follows -

> *"(4) To avoid doubt, subsection (2) only applies to a decision of the Court of First Instance or the Tribunal that has not been set aside on appeal."*

(c) Section 28B(7) of Schedule 5

13. In the English text of section 28B(7) of Schedule 5, we will amend the phrase *"to a member a committee"* to read as *"to a member of a committee"* so as to rectify the typing error.

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[1] In this regard, Members may wish to note the following extract from the information paper (LegCo Paper No. CB(2)512/09-10(04)) on the drafting of legislation submitted by the Department of Justice for the meeting of the Panel on Administration of Justice and Legal Services on 15 December 2009 –

> *"20. Reader aids – The use, where appropriate, of reader aids such as notes and examples will be encouraged. An ordinance-specific interpretation provision to clarify their status will be included in contexts in which clarification is required, while the question of a provision of general application is being considered."*

Advice sought

14. Members are invited to note the contents of the paper.

Commerce and Economic Development Bureau
April 2012

Annex A

The Administration's consolidated response to submissions made by the Hong Kong General Chamber of Commerce (HKGCC)[1], PCCW Limited and HKT Limited (PCCW)[2] and The Hong Kong Association of Banks (HKAB)[3] in March/ April 2012 concerning the Competition Bill

Formulation of the conduct rules and exclusions *HKGCC (paras. 2-5, 10 of the submission), HKAB (part B of the submission)*
● The proposed conduct rules as well as the exclusions in the Competition Bill (the Bill) model on the corresponding competition provisions in the EU, Singapore and the UK. There is plenty of case law and a wealth of jurisprudence in these overseas jurisdictions which suggest that only conduct that has an appreciable adverse effect on competition would be prohibited. Our previous responses to the Bills Committee of the Legislative Council (LegCo), including papers CB(1)2420/10-11(02) on 21 June 2011 and CB(1)1450/11-12(02) on 2 April 2012, have set out in detail the reasons for adopting the current formulation.
● We have proposed the de minimis arrangements providing for exclusions of certain agreements or conduct of lesser significance of undertakings the turnover of which does not exceed the prescribed thresholds (see LegCo Paper No. CB(1)1506/11-12(02) on 10 April 2012). Coupled with the introduction of the warning notice for alleged contravention of the first conduct rule for agreements not involving serious anti-competitive conduct (which are defined in the Bill), the concerns over legal certainty in the application of the conduct rules should have been addressed.
● On the proposal to replace the test of "abuse" in the second conduct rule, it is noted that "abuse" is commonly adopted for general prohibitions against unilateral anti-competitive conduct of an undertaking with a substantial degree of market power in overseas competition jurisdictions. It is a well-known concept and term in the competition jurisprudence. Only conduct having the object or effect of affecting competition appreciably in a market would be regarded as "abuse" and be caught under the Bill. The future Competition Commission (Commission) will issue regulatory guidelines to give guidance on the interpretation of the second conduct rule, including what may constitute an abuse. Moreover, the introduction of the conduct of lesser significance arrangement for the second conduct rule, together with the Government's stated policy intent on the market share thresholds

[1] HKGCC's submission to the Bills Committee dated 5 April 2012 (CB(1)1519/11-12(02)) refers.

[2] PCCW's submission to the Bills Committee in March 2012 (CB(1)1371/11-12(01)) refers.

[3] HKAB's submission to the Bills Committee dated 30 March 2012 (CB(1)1496/11-12(01)) refers.

should to a large extent alleviate the concerns of the small and medium enterprises (SMEs) that they would be subject to investigations under the second conduct rule.

Substantial degree of market power / dominance

HKGCC (paras. 7-9 of the submission), HKAB (part B of the submission)

- Our views on adopting the test of substantial degree of market power for the second conduct rule instead of applying the test of dominance have been set out in detail in our submissions to the Bills Committee in CB(1)389/11-12(02) on 22 November 2011 and CB(1)1450/11-12(02) on 2 April 2012. To enhance clarity of the policy intent in respect of "substantial degree of market power", we have also proposed a minimum market share threshold in Paper CB(1) 1506/11-12(02) on 10 April 2012. The policy intent and the minimum market share threshold will be set out again by the Secretary for Commerce and Economic Development when the Bill resumes Second Reading.

Thresholds for agreements / conduct of lesser significance

HKGCC (para. 6 of the submission)

- Our recent submission to the Bills Committee on 10 April 2012 (CB(1) 1506/11-12(02)) have responded to the various suggestions on adjusting the thresholds for agreements / conduct of lesser significance.

Sector-specific exemption/ arrangement

HKAB (part A of the submission)

- The exclusion of an agreement or conduct engaged in for complying with a legal requirement as currently drafted under the Bill (section 2 of Schedule 1) is in line with similar provisions in competition law in overseas jurisdictions. Adhering to the current wording would enable the competition authorities to draw reference from a large pool of overseas case law and guidelines, thereby providing more certainty.

- Whether a particular arrangement or sectoral practice falls within the legal requirement exclusion would need to be examined on a case-by-case basis. If necessary, the Commission may give a decision, in response to an application from the relevant undertakings, on whether an agreement/ conduct is excluded for compliance with a legal requirement. The Commission will also issue guidelines to indicate how it is expected to interpret and apply the general prohibitions, including the exclusions, after consultation.

- The Commission is an independent body for implementing the competition law. Within the legal framework provided under the Bill, the Commission will prepare the regulatory guidelines, grant block exemption, and initiate market study. The effectiveness of the Bill lies in the Commission's ability to carry out its investigation and enforcement independently and the Commission should be given the flexibility to decide whether, and to what extent, the relevant parties (e.g. regulatory bodies overseeing the undertaking/ sector under investigation or study) should be consulted and involved in an individual case. As a statutory body, the work of the Commission will be subject to the scrutiny of LegCo and the public.

Enforcement (including imposition of penalties) *HKGCC (para. 12 of the submission), HKAB (part B of submission)*
● The penalties and enforcement options for the Competition Tribunal (Tribunal) proposed under the Bill are on par with those available to overseas competition jurisdictions such as the UK and Singapore, as well as those under the Securities & Futures Ordinance (Cap. 571). It would be the Tribunal's judicial decision to decide what and to what extent penalties should be applied to persons found to have contravened or involved in the contravention of the competition rules on a case-by-case basis. As for the proposal of limiting the turnover to relevant products or services to which a contravention relates, we consider it not acceptable and our views have been set out in the submission to the Bills Committee on 25 October 2011 (Paper No. CB(1)91/11-12(01)).
Vertical Agreement *HKGCC (para. 11 of the submission), HKAB (part B of submission)*
● Our view remains that it is more prudent not to exempt vertical agreements across-the-board and upfront from the Bill, but to allow the future Commission to consult the stakeholders and the public on whether block exemption for a particular class of vertical agreements is appropriate for Hong Kong. Our detailed analysis is set out in our submissions to the Bills Committee on 5 July 2011 (CB(1)2631/10-11(02)), 11 October 2011 (CB(1)3079/10-11(03), and 8 November 2011 (CB(1)257/11-12(02)).
Telecommunications sector *PCCW's submission, HKGCC (para. 15 of the submission)*
● Part 11 of the Bill provides the legal framework for the effective and transparent operation of the concurrent jurisdiction regime in the telecommunications sector by the Commission and the Communications Authority (CA) (see our submission to the Bills Committee on 31 May 2011 (CB(1)2283/10-11(02)). Given a common set of competition rules and regulatory guidelines, as well as the judicial enforcement model under which the power to adjudicate a competition case will rest with the Tribunal, the concern over inconsistent application of the law or regulatory arbitrage should not arise. It is also our policy intent to have one competition authority for all competition matters in the long run.
● As regards merger regulation, noting the views of the Competition Policy Review Committee and the public, we consider it pragmatic and sensible not to regulate cross-sectoral merger activities under the Bill at its infancy stage, except for carrier licences which is already subject to such regulation under the Telecommunications Ordinance (Cap. 106) (see Bills Committee Paper No. CB(1)320/10-11(02) on 9 November 2010).
● On the proposed new section 7Q of the Telecommunications Ordinance (Cap. 106) to be inserted by way of consequential amendment under the Bill, it seeks to maintain the status quo to enable the CA (formerly the Telecommunications Authority) to regulate exploitative conduct of telecommunications licencees which

abuse their dominance. The proposed new section merely maintains the existing control of the CA, as a sectoral regulator, over exploitative conduct of telecommunications licencees in general, and does not represent a separate or different second conduct rule.
Others *HKGCC (paras. 16-17 of the submission), HKAB (part B of the submission)*
● There is suggestion that ancillary restraints related to and necessary for the implementation of a merger should be carved out from the application of the conduct rules under the new section 4 of Schedule 1 to the Bill. The crux of the matter is whether the ancillary restraint is in contravention of the conduct rules. Carving out ancillary restraint related to a merger (e.g. non-compete provision) from the application of the conduct rules might leave certain anti-competitive conduct un-regulated in the absence of a cross-sectoral merger control regime.
● Our responses to the proposed exemption for statutory bodies have been set out in Bills Committee papers issued on 14 and 28 February 2012 (CB(1)1031/11-12(02) and CB(1)1523/10-11(02)).
● On whether intra-group agreements would be subject to the first conduct rule which regulates anti-competitive agreements between undertakings, in almost all overseas jurisdictions the issue will be considered in the context of applying the concept of "undertaking". Specifically, the concept of "undertaking" suggests that intra-group entities having no independent economic freedom to make their own decisions would be regarded as one single undertaking, and thus the first conduct rule does not apply to such intra-group agreements.

Annex B

Summary of proposals on thresholds for conduct of lesser significance arrangement under the second conduct rule

	Parties	Views/proposals
1.	Chinese Manufacturers' Association of Hong Kong / Environmental Services Contractors Alliance (Hong Kong)/	The threshold for the second conduct rule should be on par with the listing requirements for listing on the Main Board of the Hong Kong Exchanges, i.e. an annual turnover of HK$500 million.
2.	Federation of Hong Kong Industries	The threshold for the second conduct rule should make reference to the listing requirements. Suggested that the threshold be set at half of the listing requirement, i.e. an annual turnover of HK$ 250 million, which is similar to the small agreement threshold in the UK.
3.	Institute of Dining Art	There should be different thresholds for different industries, taking account of their different market circumstances. Suggested using market share as the basis for calculating the threshold.
4.	Economic Synergy	Considered the originally proposed threshold of HK$ 11 million too low when compared with those adopted in other jurisdiction, e.g. Singapore, EU and UK. Suggested excluding "micro companies" from the calculation of the turnover threshold as their inclusion in the calculation might distort the resultant threshold.
5.	The Toys Manufacturers Association of Hong Kong	The threshold should be set at HK$500 million for both the first and second rules.
6.	Hong Kong Far Infrared Rays Association	The threshold should be sufficiently high to address the concerns of small and medium enterprises about the inadvertent contravention of the Bill.