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11 July 2011

By email: [mjylee@legco.gov.hk](mailto:mjylee@legco.gov.hk)

Clerk to Bills Committee on Competition Bill  
 Legislative Council Building  
 8 Jackson Road, Central  
 Hong Kong

Attention: Ms Lilian Mok

Dear Sirs

**COMPETITION BILL**

Thank you for your letter which we received on 30 June 2011. The letter (which was undated) extends an invitation to HKAB to give views on three guidelines relating to the proposed conduct rules in the Competition Bill (the Bill), namely, Guidelines on the First Conduct Rule, Guidelines on the Second Conduct Rule and Guidelines on Market Definition, all of which were prepared by the Commerce and Economic Development Bureau to facilitate the Bills Committee's scrutiny of the Bill.

We understand that these guidelines are indicative only and the proposed new Competition Commission (the Commission) would be tasked with developing its own set of guidelines explaining its enforcement priorities and methodology. While clause 35 of the Bill obliges the Commission to consult relevant persons before issuing the guidelines, given the importance of the matters to be covered in these guidelines, we consider that it should be provided in the law that there should be a public consultation process with sufficient time allowed for a proper review of the draft guidelines before they are given effect. At this stage, we would therefore defer our comments on these draft guidelines pending the full consultation process.

Taking this opportunity, we would also like to reiterate our earlier request for the Bill to be amended so as to require the Commission to consult with relevant regulatory / supervisory / representative bodies when developing guidelines specially relating to the relevant sectors including the banking industry. Please refer to recommendations 2 and 5 in the HKAB submission to the Bills Committee dated 23 November 2010 (copy re-enclosed for ease of reference by the Bills Committee).

*Chairman* Bank of China (Hong Kong) Ltd  
*Vice Chairmen* The Hongkong and Shanghai Banking Corporation Ltd  
 Standard Chartered Bank (Hong Kong) Ltd  
*Secretary* Eva Wong Mei Seong

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 渣打銀行（香港）有限公司  
 秘書 黃美嫦



There are other pressing issues that we feel compelled to address in this response previously raised in our submission dated 23 November 2010. It is our understanding that the Administration is still to address many of these issues, and we are concerned that the most common response of the Administration to these issues is that they are considered appropriate to leave for handling by the Commission in due course (as opposed to steps being taken to deal with these issues now, such as by amendments to the Bill).

Accordingly, as a major representative body of the banking sector in Hong Kong, HKAB would again draw the attention of the Bills Committee to the various other matters (including amendments to the Bill) set out in our previous submission. That submission contains a total of 11 recommendations, with Recommendation 1 being the issue that we believe is of most immediate concern to our members. As distinct from the other issues we have raised, the Administration has provided a form of substantive response to our comments in relation to this issue, but as we explain below we consider this response is neither well reasoned nor sufficient. Pursuant to Recommendation 1, HKAB recommends that the Bills Committee seek an amendment to the definition of “legal requirement” in section 2 of Schedule 1 of the Bill, so that conduct engaged in or agreements made in compliance with any requirements applicable under codes of practice, circulars, guidelines or other directions or guidance in any form issued or endorsed by a Government-approved regulatory or supervisory authority in Hong Kong (or a relevant supranational body) are excluded from challenge under the Conduct Rules. Additionally, HKAB recommends that the Bills Committee highlight to the Government the importance of ensuring that the Commission takes appropriate steps, in consultation with the banking sector, to effectively exempt from the Conduct Rules conduct in compliance with directives or guidance issued by relevant supranational bodies or any other foreign regulatory or supervisory bodies outside Hong Kong (e.g. the Basel Committee on Banking Supervision) having jurisdiction over the undertaking concerned.

We understand that the Administration has indicated that it considers broadening the definition of “legal requirement” might cast the net too wide, rendering the exclusion a norm rather than an exception. Further, the Administration has made a distinction that, according to case laws in overseas jurisdictions, the exclusion for compliance with legal requirements applies only where the regulated undertaking *is required* to act in a certain way; it does not apply to the discretionary behaviour of that undertaking (e.g. making reference to a guideline or circulars of no particular legal effect). We consider this to be unhelpful. Currently, there are many regulatory requirements that do not have the force of law but which financial entities need to treat as binding and therefore of a quasi-legal status to ensure their prudent operation at both a local and international level. As we believe both the Administration and general public would expect Hong Kong's banking sector to be conducted in accordance with such requirements, which are in place for the protection of the global financial system and all those who engage with that system, we believe it is improper and arbitrary to distinguish between local laws and important international



requirements in the context of section 2 of Schedule 1 of the Bill. Indeed, in our submission we provide an example of how governmental authorities in Hong Kong currently supervise banks to ensure they are complying with such requirements, and may be penalised if they fail to do so.

We recognise that some careful drafting and consultation may be required in order to ensure that any amendment to the Bill to address this issue do not result in an overreach of the relevant exemption, and we would be pleased to work with the Administration to achieve this. For now, however, we are concerned that the only response from the Administration has been to reinforce the limited scope of the existing exemption in its comments on this issue and refer to the difficulties that may be encountered in attempting a redraft. The Administration has not provided our members with any comfort on the issue or explained whether or why it considers the concern we have expressed is unfounded. Accordingly, given the significance of the banking sector to the continued growth and prosperity of Hong Kong and its economy, we hope that appropriate attention would be given by the Bills Committee in addressing the continuing concerns of HKAB members highlighted above.

Once again, thank you for consulting HKAB again on this important legislation for Hong Kong.

Yours faithfully

A handwritten signature in black ink, appearing to be "Eva Wong", written in a cursive style.

Eva Wong  
Secretary

Enc.



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23 November 2010

By email: [hysiu@legco.gov.hk](mailto:hysiu@legco.gov.hk)

Ms. Debbie Siu  
Clerk to Bills Committee on Competition Bill  
Legislative Council Building  
8 Jackson Road, Central  
Hong Kong

Dear Ms. Siu

### COMPETITION BILL

The Hong Kong Association of Banks (HKAB) is pleased to present this submission to the Bills Committee regarding the Competition Bill presently before Hong Kong's Legislative Council. HKAB hopes this submission will assist the Bills Committee to work to secure appropriate refinements to the Bill, so that if enacted the Bill will support the continued growth of the Hong Kong economy and provide maximum benefit to the community.

In particular, the submission includes recommendations that are aimed at ensuring that any new competition law in Hong Kong is implemented in a manner that balances the interests of safeguarding competition in Hong Kong with the benefits of facilitating the free play of market forces and continuing to promote a business-friendly environment in the region.

Reflecting the sectoral focus of HKAB, the submission also includes recommendations intended to ensure any new competition law aligns with, and appropriately complements, the existing regulatory framework applicable to Hong Kong's banking sector.

In addition to the detailed content of the submission, an Executive Summary focussing on the primary recommendations of HKAB is included in Annex A. Please note that this submission is confidential and not for publication. However, the Executive Summary in Annex A is not confidential and may be published for public review.

HKAB trusts the Bills Committee will give due consideration to the issues and recommendations set out in the submission, and would be pleased to discuss the submission further with Bills Committee representatives.

*Chairman* Standard Chartered Bank (Hong Kong) Ltd  
*Vice Chairmen* Bank of China (Hong Kong) Ltd  
The Hongkong and Shanghai Banking Corporation Ltd  
*Secretary* Rita Liu

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HKAB looks forward to working with the Government and relevant parties to progress consideration and refinement of the Competition Bill.

Yours sincerely



Rita Liu  
Secretary

Enc.

## **Submission to the Bills Committee of the Legislative Council regarding the Competition Bill**

**Prepared by The Hong Kong Association of Banks and submitted on 23 November 2010**

Please note that capitalised terms used in this submission have the meaning given to those terms in the Hong Kong Competition Bill unless it is indicated otherwise.

### **1. Introduction**

#### **1.1 About The Hong Kong Association of Banks**

The Hong Kong Association of Banks ("**HKAB**") was created by The Hong Kong Association of Banks Ordinance, Cap.364 ("**Ordinance**") in 1981 to replace the Exchange Banks' Association. The Ordinance provides a framework for the Government to exchange views with the banking sector for the further development of the industry. The key roles of HKAB include:

- promotion of the interests of fully licensed banks in Hong Kong;
- being a focal point for consultation on law reform, new legislation and regulatory matters; and
- forming a sounding-board for the Government and other relevant bodies on general business and banking issues.

#### **1.2 HKAB and Hong Kong's proposed competition law**

1.2.1 HKAB has been monitoring developments in relation to the proposed Hong Kong competition ("**Proposed Law**") for a number of years, in accordance with its responsibility to members and to the broader community to play an active role in consultation on new legislation and regulatory matters.

1.2.2 As part of this process, HKAB has:

- written to the then Economic Development and Labour Bureau on 2 February 2007, in response to the Government's *A Public Discussion Document on the Way Forward for Competition Policy in Hong Kong*; and
- written to the Commerce, Industry and Tourism Branch of the Commerce and Economic Development Bureau on 1 August 2008, in response to the Government's *Public Consultation Paper on Detailed Proposals for a Competition Law*.

1.2.3 Following introduction of the Competition Bill into the Legislative Council in July 2010 and formation of the Bills Committee in October 2010, HKAB is pleased to provide this submission, outlining HKAB's comments and recommendations with respect to the Bill.

### 1.3 Confidentiality

This submission is confidential and not for publication. However, the Executive Summary extract provided in Annex A is not confidential and may be published for public review.

## 2. Executive Summary

Annex A to this submission contains a high-level summary of the key issues and recommendations of HKAB in relation to this Bill, which issues and recommendations are also referenced (in the boxed text) and explained more fully in sections 3.1 to 3.9 below.

## 3. Substantive submission comments

Explained in sections 3.1 to 3.9 below are HKAB's primary observations and recommendations in relation to the Bill:

### 3.1 Immunity for agreements and conduct required by relevant codes of practice, circulars, guidelines, etc

**Recommendation 1:** HKAB recommends that the Bills Committee seek an amendment to the definition of "legal requirements" in section 2 of Schedule 1 of the Bill, so that conduct engaged in or agreements made in compliance with any requirements applicable under codes of practice, circulars, guidelines or other directions or guidance in any form issued or endorsed by a Government-approved regulatory or supervisory authority in Hong Kong (or a relevant supranational body) are excluded from challenge under the Conduct Rules. Additionally, HKAB recommends that the Bills Committee highlight to the Government the importance of ensuring that the Competition Commission ("**Commission**") takes appropriate steps (in consultation with the banking sector) to effectively exempt from the Conduct Rules conduct in compliance with directives or guidance issued by relevant supranational bodies or any other foreign regulatory or supervisory bodies outside Hong Kong having jurisdiction over the undertaking concerned.

#### 3.1.1 Section 2 of Schedule 1 of the Bill effectively provides that:

- the First Conduct Rule does not apply to an agreement to the extent that it is made for the purpose of complying with a legal requirement;
- the Second Conduct Rule does not apply to conduct to the extent that it is engaged in for the purposes of complying with a legal requirement; and
- in this context, "legal requirement" means a requirement imposed by or under any enactment in force in Hong Kong, or imposed by any national law applying in Hong Kong.

#### 3.1.2 HKAB is concerned that these exclusions will not extend to agreements made (in the context of the First Conduct Rule) or conduct engaged in (in the context of the Second Conduct Rule) for the purposes of complying with all of the important codes of practice, circulars and regulatory guidance or directives applicable to the banking sector in Hong Kong.

- 3.1.3 For example, HKAB members are committed to complying with the Code of Banking Practice ("**Code**"), which aims to promote good banking practices by setting out minimum service standards that HKAB member banks and authorized institutions should meet when providing services to personal customers. The Code is issued on a voluntary basis by HKAB and the DTC Association. Accordingly, HKAB understands that compliance with the Code may not be a "legal requirement" in the context of section 2 of Schedule 1 of the Bill.
- 3.1.4 However all HKAB member banks and other relevant authorized institutions are expected to comply with the Code, which has been endorsed by the Hong Kong Monetary Authority ("**HKMA**"). Indeed, in section 1.4 of the Code it is noted that "HKMA expects all institutions to comply with the Code and will monitor compliance as part of its regular supervision". Any authorized institution that fails to comply with the Code may be viewed by the HKMA as failing in its duty to conduct business in the fit and proper manner required of authorized institutions.
- 3.1.5 As the Code aims to promote good banking practice and a fair and cordial relationship between authorized institutions and their customers, HKAB does not expect that conduct undertaken in compliance with the Code would commonly raise competition-related concerns. However, it is also clear that this cannot be determined with precision until the scope of application of the Conduct Rules is more fully explained by regulations and guidance documents that the Bill indicates would be issued in due course by the Commission - and which may be amended from time to time.
- 3.1.6 In this context, HKAB believes that it would be improper for banks to be placed in a position where they would need to assess the legality under the Proposed Law of agreements made (in the context of the First Conduct Rule) or conduct engaged in (in the context of the Second Conduct Rule) for the purposes of complying with the Code. Instead, HKAB believes that requirements under the Code should be treated as "legal requirements" to which the existing Conduct Rules exclusion would extend.
- 3.1.7 Similarly, the HKMA regularly issues circulars, guidelines and other forms of guidance or directives to authorized institutions on matters aimed at ensuring best banking practice and the stability of the banking sector in Hong Kong. For example, in August 2010, HKMA issued a circular concerning prudential measures for residential mortgage loans. Similar instruments impacting the banking and financial sector are also issued from time to time by other regulatory bodies such as the Securities and Futures Commission ("**SFC**"). It is not always clear on the face of instruments of this or a similar nature whether they will be characterised as subsidiary legislation in the context of the Interpretation and General Clauses Ordinance and thus "legal requirements" in the context of section 2 of Schedule 1 of the Competition Bill.
- 3.1.8 For reasons analogous to those stated in paragraph 3.16 in the context of the Code, HKAB also believes that these forms of guidance or directives should be treated as "legal requirements" given that relevant institutions are expected to comply with them in the same way that they are expected to comply with applicable Ordinances and regulations, etc.
- 3.1.9 Beyond these examples, there are a range of other circumstances and modes in which bodies such as the HKMA may provide directions or guidance to banks regarding the manner in which they conduct their business which may not qualify as "legal requirements" in the relevant context. Additionally, banks in Hong Kong may from time to time be required to comply with directives or guidance issued by supranational bodies such as the Basel Committee on Banking Supervision.



- 3.1.10 Although the examples mentioned above are specific to the banking sector, it is clear that the same concern may arise in relation to other industry sectors in Hong Kong.
- 3.1.11 Accordingly, HKAB recommends that the Bills Committee seek an amendment to the definition of the term "legal requirements" in section 2 of Schedule 1 of the Bill, so that conduct engaged in or agreements made in compliance with any requirements applying under codes of practice, circulars, guidelines or other directions or guidance in any form issued or endorsed by a Government-approved regulatory or supervisory authority in Hong Kong are excluded from challenge under the Conduct Rules.
- 3.1.12 HKAB recognises that in contrast to the position regarding Government-approved regulatory or supervisory authorities in Hong Kong, it may be difficult to define with precision in the Bill the scope of supranational or other foreign bodies whose directions or guidance to Hong Kong banks should be treated as "legal requirements" in the context of section 2 of Schedule 1 of the Bill. Accordingly, HKAB recommends that the Bills Committee also highlight to the Government the importance of ensuring that the Commission takes appropriate steps (such as through the drafting of relevant enforcement guidelines in consultation with the banking sector) to effectively exempt from the Conduct Rules conduct in compliance with directives or guidance issued by relevant supranational bodies or any other foreign regulatory or supervisory bodies outside Hong Kong having jurisdiction over the undertaking concerned.

## 3.2 Banking-specific guidelines

**Recommendation 2:** HKAB recommends that the Bills Committee highlight to the Government the importance of ensuring competition-orientated guidelines relating to relevant banking practices are developed by the Commission as a priority, in consultation with relevant sector representatives, and published well prior to commencement of the Conduct Rules. This could be done by amending section 35 of the Bill (Guidelines) to include references to the banking and other sectors in the text that requires the Commission to issue guidelines on its interpretation and enforcement approach, or by the Government liaising with the Commission after it is established to emphasize the benefit of developing and prioritising such guidance.

- 3.2.1 According to section 35 of the Bill (Guidelines), the Commission is required to issue guidelines explaining, amongst other things, the manner in which it intends to interpret and give effect to the Conduct Rules.
- 3.2.2 In addition to more general cross-sector guidelines, HKAB submits that the Government should require the Commission to issue guidelines specifically applicable to industry sectors whose structure or regulatory environment may raise particularly complex or challenging competition issues in respect of which additional clarity regarding the Commission's interpretation and enforcement approach will be appropriate. In particular, HKAB submits that the banking sector should be amongst the industry sectors that are the subject of such guidelines, for reasons such as those referenced in paragraph 3.1.12 above and in the remainder of this section 3.2.
- 3.2.3 There is international precedent for such approach. By way of example, it is noted that the European Commission has existing and forthcoming regulations incorporating guidance on the application of competition laws to cross-border banking payments and direct debit schemes<sup>1</sup>. There are also many further examples of competition-related

<sup>1</sup> For example, refer to Regulation (EC) No 924/2009 of the European Parliament and of the Council of 16 September 2009.

guidance being issued in Europe and elsewhere specific to the banking and/or financial services sectors<sup>2</sup>.

- 3.2.4 There can be no doubt that the development of guidance for specific industry sectors will promote understanding and compliance with the Proposed Law, and enhance legal fairness. With particular reference to the banking sector, it is also clear that there are relatively unique structural and regulatory features in this sector that lead to business arrangements and activities in respect of which guidance is especially warranted.
- 3.2.5 For example, banks are commonly required by regulation or business necessity to enter into co-operative arrangements with other banks, for reasons such as to ensure the efficient and secure operation of inter-bank networks and systems. Examples include networks relating to automatic teller machines, international credit card or national debit transfer systems, payments clearing systems, and credit history databases. Prudent administration of these arrangements requires a level of information exchange and inter-bank coordination that it is recognised may need to be managed carefully to ensure strict compliance with competition laws. Accordingly, banks will benefit from guidance from the Commission regarding how they can best ensure such compliance whilst fulfilling other regulatory requirements and maximising the efficient and secure operation of the relevant networks and systems.
- 3.2.6 Accordingly, HKAB recommends that the Bills Committee highlight to the Government the importance of ensuring competition-orientated guidelines relating to relevant banking practices are developed by the Commission as a priority, and published well prior to commencement of the Conduct Rules. HKAB also submits that development of such guidelines by the Commission should occur in consultation with banking sector representatives, to ensure the guidelines address an appropriate range of banking practices and that the Commission is furnished with appropriate information regarding the rationale for and benefits from relevant practices, etc.
- 3.2.7 This could be done by amending section 35 of the Bill to include references to the banking and other sectors in the text that requires the Commission to issue guidelines on its interpretation and enforcement approach, and by expressly linking this section with the consultation requirement discussed in section 3.5 of this submission. Alternatively, the Government should liaise with the Commission after it is established to emphasise the benefit of developing and prioritising guidance in this manner.

### 3.3 Appropriate market definition guidance:

**Recommendation 3:** HKAB recommends that the Bills Committee seek an amendment to the Bill to introduce a definition of the term 'market', and that this definition expressly reflect the fact that the geographic scope of many product and service markets contested by undertakings in Hong Kong extends beyond the territorial boundaries of the Hong Kong S.A.R. and will commonly encompass mainland China and beyond.

<sup>2</sup> For example, Canada's Competition Bureau has issued guidelines regarding merger control enforcement in relation to the financial services sector (refer to the Bureau publication *The Merger Enforcement Guidelines as applies to a Bank Merger*, available at [www.competitionbureau.gc.ca](http://www.competitionbureau.gc.ca)), and the Norwegian Competition Authority has reportedly circulated guidance on the appropriate definition of relevant financial markets.

- 3.3.1 HKAB notes that many key sections of the Bill use the term 'market', such as:
- section 21, which prohibits an undertaking that has "a substantial degree of market power in a market" from engaging in certain conduct;
  - section 129, which empowers the Commission to "conduct market studies into matters affecting competition in markets in Hong Kong"; and
  - section 6, which effectively prohibits undertakings from entering into agreements or arrangements pursuant to which they will "share markets" with competitors in certain circumstances.
- 3.3.2 Additionally, HKAB understands that the process of defining the relevant markets in which undertakings participate will be a key step in identifying whether their conduct prevents, restricts or distorts competition in those (or related) markets in Hong Kong and thereby violates the Conduct Rules. Put simply, the narrower the definition of such a market, the more scope there will be to discern that certain conduct by an undertaking participating in the relevant market prevents, restricts or distorts competition.
- 3.3.3 Despite its significance, and in contrast to the approach taken by legislators in many jurisdictions with developed or influential competition law regimes<sup>3</sup>, the term 'market' is not defined in the Bill.
- 3.3.4 HKAB understands that it is likely some form of definition and guiding principles relating to the term would be provided in the guidelines that section 35 of the Bill requires the Commission to issue after the Bill is enacted.
- 3.3.5 However, as it is clearly integral to the effective and just application of the Proposed Law that proper principles of market definition are employed, and to ensure a proper understanding of the scope of the Proposed Law at this Bill consideration stage, HKAB believes it is appropriate to include in the Bill specific wording explaining the intended meaning of the term 'market' and embodying some key principles relevant to market definition. This definitional wording could be supplemented, but not contradicted, by later Commission guidelines.
- 3.3.6 HKAB believes that this issue is of particular importance given that the Bill now provides for a judicial enforcement model. Specifically, as any guidelines issued by the Commission will not be binding on the judiciary, HKAB submits that it is proper for certain integral issues such as the appropriate process for (and relevant fundamental aspects of) market definition to be set out in the Bill itself.
- 3.3.7 This approach would have the additional benefit of aiding the Government's stated intention of reducing the risk of ill founded complaints and private actions based on a misconception about market definition (and, in particular, the misconception that all 'markets' referenced in the Bill should be assumed to have a geographic scope encompassing just the territory of Hong Kong). The importance of this can be underlined by recent litigation experience in China, where the vast majority of reported private actions brought by plaintiffs under China's Anti-Monopoly Law have been rejected by China's courts for reasons that include incorrect or unsupported market

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<sup>3</sup> For example, the legislators in Australia, China, and Taiwan all incorporated definitions for the term 'market' (or the related term 'relevant market') in their primary competition laws. Refer to section 4E of Australia's *Trade Practices Act 1974* (Cth), Article 12 of China's *Anti-Monopoly Law of the People's Republic of China*, and Article 5 of Taiwan's *Fair Trade Act*.

definition and market power allegations<sup>4</sup>. As the Bill does not limit private litigation to 'follow on' actions after determination of a claim brought by the Commission, it is important that steps such as this be taken to reduce the potential for misconceived stand alone actions.

3.3.8 Reflecting the geographic principle mentioned in paragraph 3.3.7, HKAB is of the view that any new definition of the term 'market' included in the Bill should be tailored to reflect certain unique aspects of the Hong Kong economy.

3.3.9 In particular, and in addition to ensuring any new definitional wording reflects international best practice, HKAB believes it is essential that such wording expressly reflect the fact that:

- Hong Kong's open economy and the increasingly porous nature of trade and general business activity between Hong Kong and mainland China allows a very high degree of competition in Hong Kong from firms outside of the region<sup>5</sup>; and
- this aspect of Hong Kong's economy will mean that many markets in which businesses participate in Hong Kong will have a geographic scope that is properly defined as extending beyond the region.

3.3.10 Indeed, it is well recognised that many Hong Kong companies that may be substantial players in the domestic economy are (in the context of competition laws) properly viewed as competitors in a global or broad regional market place where they are just one of many businesses operating in an intensely competitive environment. This was even touched upon in the Government's May 2008 *Detailed Proposals for a Competition Law* consultation paper ("**May 2008 Consultation Paper**")<sup>6</sup>.

3.3.11 With specific regard to the banking sector, HKAB notes that there are a broad range of banking-related services that take place in markets that are properly characterised as being highly competitive regional or international markets, clear examples of which include (but are not limited to) provision of wholesale banking services, corporate banking services, investment management services, and forms of insurance and private equity services. International jurisprudence supports this view<sup>7</sup>, and it is also clear that the scope of banking service examples will continue to expand as more steps are taken to facilitate greater banking integration between Hong Kong and mainland China.

3.3.12 Express recognition of the unique cross-border market integration between Hong Kong and mainland China in the Proposed Law would assist to ensure that, at a minimum, a competition regulator in Hong Kong considers this issue when determining the appropriate geographic scope of markets, and identifying the boundaries of competitor pressure for the purpose of reviewing conduct under the law.

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<sup>4</sup> For an in-depth discussion of this issue, refer the Mayer Brown JSM legal update dated 8 February 2010, *Civil Actions Under China's Anti-Monopoly Law - Five Major Cases, Five Major Lessons*.

<sup>5</sup> Refer, for example, paragraph 20 of the May 2008 Consultation Paper (as defined in paragraph 3.3.11).

<sup>6</sup> Refer to paragraph 20 of Chapter III of the May 2008 Consultation Paper.

<sup>7</sup> See, for example, the 2001 decision of the U.K. Competition Commission in respect of the merger of *Lloyds/Abbey*, where the Competition Commission considered that the market for financial products sold to customers larger than SMEs is global. Decision available at: [http://www.competition-commission.org.uk/rep\\_pub/reports/2001/458lloyds.htm](http://www.competition-commission.org.uk/rep_pub/reports/2001/458lloyds.htm)

- 3.3.13 There is precedent for such a step. For example, Australia's Trade Practices Act includes express recognition that there will be "Trans-Tasman" markets (that is, markets geographically encompassing a region at least as broad as both Australia and New Zealand)<sup>8</sup>.
- 3.3.14 Accordingly, in summary, HKAB recommends that the Bill Committee seek an amendment to the Bill to introduce a definition of the term 'market', and that this definition expressly reflect that the geographic scope of many product and service markets contested by undertakings in Hong Kong extends beyond the territorial boundaries of Hong Kong and will commonly encompass mainland China and beyond.

#### 3.4 Exclusion of vertical agreements & 'M&A' from the First Conduct Rule

**Recommendation 4:** HKAB recommends that the Bills Committee seek an amendment to the Bill to expressly exempt vertical agreements and M&A agreements from the scope of the First Conduct Rule. In the alternative, if M&A agreements are to be subject to challenge, then HKAB submits that this should be in accordance with specific merger review provisions that will ensure there are appropriate procedural safeguards and review thresholds.

- 3.4.1 Prior to publication of the Bill, HKAB had assumed that vertical agreements and M&A agreements (relevant to sectors other than telecommunications) would be exempt from challenge under the Proposed Law. However, as explained below, this is not the case.
- Potential application of the Proposed Law to challenge vertical agreements*
- 3.4.2 Section 6(1) of the Bill, referred to as the First Conduct Rule, can be summarised as prohibiting business operators from entering into agreements or arrangements that have the purpose or effect of preventing, restricting or distorting competition in Hong Kong.
- 3.4.3 Section 6(2) of the Bill provides a non-exhaustive list of examples of the types of agreements that may be deemed to violate the First Conduct Rule. Each of these examples is a 'horizontal agreement' (i.e. an agreement between competitors, such as a price-fixing agreement).
- 3.4.4 However, notwithstanding that these examples are confined to horizontal agreements, it is clear that the First Conduct Rule is worded broadly enough to apply to 'vertical agreements' (that is, agreements or arrangements between business operators at different levels of the supply chain, such as suppliers and customers or manufacturers and distributors). There is no wording in the Bill exempting these types of agreements from the First Conduct Rule.
- 3.4.5 This development has the potential to be inconsistent with previous Government proposals, pursuant to which it was suggested that the Government favoured a broad exclusion from the First Conduct Rule for vertical agreements that met relevant conditions. For example, in 'Proposal 26' in the May 2008 Consultation Paper, the Commerce and Economic Development Bureau stated in relation to the then-proposed First Conduct Rule that - "The focus of the prohibition on agreements should be on horizontal agreements. Vertical agreements should only be addressed in the context of abuse of substantial market power."
- 3.4.6 For substantially the same reasons as those referenced in paragraph 9 of Chapter II of the May 2008 Consultation Paper, HKAB holds the view that vertical agreements should only

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<sup>8</sup> Refer to section 46A of Australia's *Trade Practices Act 1974* (Cth), which utilises and defines the term "trans-Tasman market".

be subject to challenge under the Proposed Law in the context of abuse of substantial market power.

*Potential application of the Proposed Law to challenge M&A deals in any sector*

- 3.4.7 The Bill contains what is commonly referred to as a 'merger regime', pursuant to which certain mergers and acquisitions ("M&As") will be unlawful if they substantially lessen competition in Hong Kong. However, the merger regime will apply only to transactions involving telecommunications licensees. HKAB notes that this is consistent with options set out in previous Government proposal documents, and supports the approach that has been adopted.
- 3.4.8 Notwithstanding this, it is clear that M&As conducted by business operators in other industry sectors may also be challenged as anti-competitive and unlawful. This is on the basis that the First Conduct Rule applies to any form of 'agreement' which has the purpose or effect of preventing, restricting or distorting competition in Hong Kong. There is no exclusion for M&A agreements.
- 3.4.9 For substantially the same reasons as set out in paragraphs 20 and 21 of Chapter III of the May 2008 Consultation Paper, HKAB holds the view that M&A agreements unrelated to the telecommunications sector in Hong Kong should be excluded from challenge under the Proposed Law. In the alternative, if M&A agreements are to be subject to challenge, then HKAB submits that this should be in accordance with a specific merger control regime analogous to that which will apply in respect of the telecommunications sector under the Bill. That will ensure there are appropriate procedural safeguards (i.e. a specific timeframe in which challenges may occur, and mechanisms via which parties can seek advance clearance) and appropriate review thresholds (i.e. violations only for relevant deals that prevent or *substantially* restrict or distort competition) for M&A agreements, which do not exist in relation to the First Conduct Rule as it is currently framed.

*Role of regulations and guidelines*

- 3.4.10 HKAB recognises that it may be possible for the Commission to wholly or partially exempt vertical agreements and M&A agreements from the First Conduct Rule after the Bill is passed in its current form, through later Block Exemption Orders or enforcement guidelines. Indeed, the May 2008 Consultation Paper indicated that this may be a mechanism utilised by the Government to exempt vertical agreements from the Proposed Law. However, for the reasons set out below, HKAB believes that this would not be an appropriate way forward on this issue if it is indeed still the intention of the Government to provide such exemptions.
- 3.4.11 Firstly, HKAB notes that the Commission will be an independent statutory body, and not a servant or agent of the Government<sup>9</sup>, and therefore will presumably not be bound to follow the preferences of Government officials when it comes to drafting and implementing later regulations or guidelines. Accordingly, HKAB believes that it is important that such fundamental exemptions be provided in the Bill itself - for the purposes of certainty (both regarding the intended operation of the Proposed Law going forward, and current debate about the merits of the Bill more generally).
- 3.4.12 Secondly, and with specific reference to the possible use of Block Exemption Orders to exempt vertical agreements and/or M&A agreements from the application of the First Conduct Rule, HKAB notes that section 16 of the Bill sets out detailed procedures that

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<sup>9</sup> Refer to section 130 of the Bill.

must be followed by the Commission before such orders can be issued, including a form of consultation with interested parties. Given the significant workload that will be borne by the Commission once established, it is suggested that the burden of dealing with exemption of vertical agreements and/or M&A agreements from the application of the First Conduct Rule should not be added to its responsibilities when it can be dealt with in the text of the Bill.

- 3.4.13 In relation to the potential for the Commission to use guidelines to effectively exempt vertical agreements and/or M&A agreements, then as noted in paragraph 3.3.6, any guidelines issued by the Commission will not be binding on the judiciary. Accordingly, it is not clear how the Commission could exclude private litigants from challenging vertical agreements and/or M&A agreements in 'stand alone' actions before the Competition Tribunal.
- 3.4.14 In light of the above matters, HKAB recommends that the Bills Committee seek an amendment to the Bill to expressly exempt vertical agreements and M&A agreements from the scope of the First Conduct Rule.

### 3.5 Consultation between the Commission and banking sector representatives

**Recommendation 5:** HKAB believes that the Bills Committee should highlight to the Government the importance of ensuring the Commission consults with banking regulators and other key banking sector representatives before conducting investigations and enforcement actions in relation to the sector or when developing guidelines specifically relating to the sector. More particularly, HKAB recommends the Bills Committee:

- seek an amendment to section 35 of the Bill (Guidelines) to require that when the Commission is drafting or amending relevant guidelines in relation to the bill it must, at a minimum, consult with any body or association in Hong Kong that, under a Hong Kong Ordinance, is provided with regulatory, supervisory or representative functions or responsibilities in relation to an industry sector to which the relevant guidelines wholly or substantially relate; and
- seek an amendment to section 129 of the Bill (Functions of the Commission) so that the Commission is required to consult with any body or association in Hong Kong that, under a Hong Kong Ordinance, is provided with regulatory, supervisory or representative functions or responsibilities in relation to an industry sector before commencing any investigation or enforcement action in fulfilment of its function under paragraph (a) of that section ("to investigate conduct that may contravene the competition rules and enforce the provisions of this Ordinance").

- 3.5.1 Under the Bill, the existing role of the Telecommunications Authority and Broadcasting Authority as the primary competition regulator in relation to their respective sectors is retained. According to paragraph 7 of Chapter VI of the May 2008 Consultation Paper, this is for reasons that include the merit of retaining this "specialist knowledge" of the sector.
- 3.5.2 HKAB supports this approach, and also believes that it is appropriate to ensure that the expertise of existing banking regulators such as HKMA and other key banking sector representatives is appropriately utilised by the competition regulator.

3.5.3 In particular, HKAB recommends that the Government take steps to ensure that the banking regulators and other key banking sector representatives are consulted by the Commission in respect of key activities that it is required or may seek to undertake, such as:

- undertaking relevant investigations and enforcement actions; and
- developing relevant guidelines,

specifically relating to the banking sector.

*Consultation before undertaking relevant investigations and enforcement actions*

3.5.4 HKAB believes consultation between banking sector representatives and the Commission should occur prior to the Commission seeking to open any investigations or enforcement action pertaining to the sector. Open dialogue between competition regulators and sectoral regulators for the purposes of ensuring informed decision is common in many mature competition law jurisdictions, and has even been formalised in some areas<sup>10</sup>.

3.5.5 For example, HKMA responsibilities extend beyond prudential supervision of the banking sector and include monitoring the conduct of banks to ensure they act in a manner which is not detrimental to the interests of customers. HKMA also works with other regulators such as the SFC to ensure that there is an open market and level playing field for service providers in their relevant sectors. These functions and duties provide HKMA with special knowledge of Hong Kong's banking industry and the optimum competition environment for the sector.

3.5.6 Accordingly, HKAB believes it will be appropriate for the Commission to liaise closely with HKMA and obtain its input in relation to issues such as appropriate market definition, and the market effect and public policy benefits of common industry practices.

3.5.7 Dialogue with banking regulators will also be prudent to ensure that any remedies sought by the Commission are appropriate with regard to the prudential operation of the banking sector.

3.5.8 For example, under section 1 of Schedule 3 to the Bill, the Competition Tribunal has very broad powers to make orders with respect to a contravention of the competition rules, including orders requiring a person to dispose of assets and operations, and orders mandating the provision of services or access to facilities. It is expected that such orders would most commonly be considered upon application by the Commission in the context of a particular enforcement action.

3.5.9 To the extent that such cases may concern participants in the banking and financial sectors, it will be important that the Commission works closely with the banking regulators to ensure that any enforcement orders are not inconsistent with the obligations relevant instructions may have under sectoral regulations, such as line-of-business restrictions or restrictions on the portfolio of assets that banks can hold.

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<sup>10</sup> For example, in Norway the Competition Authority and The Financial Supervisory Authority have entered into supervisory cooperation arrangements.



*Consultation before development of relevant guidelines*

- 3.5.10 As noted in section 3.2 of this submission, HKAB believes that competition-orientated guidelines relating to relevant banking practices should be developed by the Commission as a priority, and published well prior to commencement of the Conduct Rules.
- 3.5.11 HKAB believes that these guidelines should be developed in consultation with banking regulators and other key banking sector representatives, to ensure (for example) that the guidelines address an appropriate range of banking practices and that the Commission is furnished with appropriate information regarding the rationale for and benefits from such practices.

*How the consultation requirement should be integrated into the Bill*

- 3.5.12 It is common practice for regulatory bodies to be required by law to consult with appropriate persons and institutions before engaging in key activities. For example, in the banking and financial sector, section 60A of the Banking Ordinance requires the HKMA to consult with bodies such as The DTC Association and HKAB when fulfilling key functions such as the drafting of rules prescribing information to be disclosed to the general public by authorized institutions (regarding financial affairs) and when calculating the capital adequacy ratio.
- 3.5.13 Accordingly, HKAB considers that relevant consultation requirements may be most appropriately incorporated into the Competition Bill via:
- an amendment to the existing section 35 (Guidelines), which provides that the Commission must consult any persons "it considers appropriate" when issuing or amending relevant guidelines relating to the Bill. Specifically, HKAB recommends that the Bills Committee seek an amendment to this section so that the consultation requirement is extended to require the Commission to, at a minimum, consult with any body or association in Hong Kong that, under a Hong Kong Ordinance, is provided with regulatory, supervisory or representative functions or responsibilities in relation to an industry sector to which the relevant guidelines wholly or substantially relate; and
  - an amendment to the existing section 129 (Functions of Commission), which lists the primary functions of the Commission. Specifically, HKAB recommends that the Bills Committee seek an amendment to this section so that the Commission is required to consult with any body or association in Hong Kong that, under a Hong Kong Ordinance, is provided with regulatory, supervisory or representative functions or responsibilities in relation to an industry sector before commencing any investigation or enforcement action in fulfilment of its function under paragraph (a) of that section ("to investigate conduct that may contravene the competition rules and enforce the provisions of this Ordinance").

**3.6 Preserving the role and authority of existing sectoral regulators**

**Recommendation 6:** HKAB recommends that the Bills Committee seek an amendment to section 129 of the Bill (Functions of Commission) so that the Commission will be precluded from conducting market studies in respect of industry sectors that are already supervised by a sectoral regulator empowered to review and respond to instances of market failure.

- 3.6.1 Section 129 (Functions of Commission) of the Bill empowers the Commission to conduct market studies into matters affecting competition in markets in Hong Kong.
- 3.6.2 No further details are provided in the Bill regarding the nature of such market studies, and their implications. However, it is recognised by HKAB that the Government may intend the market study powers of the Commission to be exercised in a similar manner to the market investigation powers that the Office of Fair Trading has in the United Kingdom under that jurisdiction's Enterprise Act 2002.
- 3.6.3 In this context, HKAB believes it is appropriate to ensure that mechanisms are built into the Bill to avoid unnecessary overlap in the functions of the Commission and existing sectoral regulators, particularly in the context of examining instances of market failure and how these may be best addressed.
- 3.6.4 With regard to the banking sector, HKAB notes that there is already significant regulatory oversight of banking markets in Hong Kong, through bodies such as the HKMA. As mentioned previously in this submission, the HKMA's supervisory role extends beyond mere prudential supervision of the sector to include reviewing and addressing a broad range of issues relating to malpractice and market failure.
- 3.6.5 For example, under the Banking Ordinance, the HKMA is required to promote proper standards of conduct and sound business practices by banks (section 7(c)), suppress or aid in suppressing illegal or improper practices in the sector (section 7(d)), and take steps to ensure banking business is carried on with integrity and in a manner not detrimental to the interests of depositors or potential depositors (section 7(g)).
- 3.6.6 Additionally, the HKMA scrutinizes the overall operation of the banking sector and may from time to time issue directives to banks aimed at ensuring they operate in a manner that enhances efficiency and serves the interests of customers. The HKMA may also liaise with Government representatives such as the Financial Secretary to recommend regulatory or structural changes as it deems appropriate.
- 3.6.7 HKAB therefore believes the HKMA's legislative responsibilities and the scope of its supervisory role is sufficient to ensure appropriate ongoing review of banking markets, and the HKMA's special knowledge of the banking sector also positions it as the most appropriate body to conduct any intensive assessment of specific banking structures or practices whenever this may be necessary. Accordingly, HKAB believes that it is appropriate for the scope of the Commission's market study powers to exclude review of the banking sector.
- 3.6.8 HKAB therefore recommends that the Bills Committee seek an amendment to section 129 of the Bill (Functions of Commission) to clarify that market studies should be restricted to sectors in which there is no existing sectoral regulator already in a position to review and if necessary act on any instances of market failure.

### **3.7 Appropriate Block Exemption Regulations:**

**Recommendation 7:** HKAB recommends that the Bills Committee highlight to the Government the importance of the Commission introducing Block Exemption Orders or other exemptions and exclusions relating to relevant aspects of banking and financial sector practice, and for the Commission to consult foreign competition regimes and liaise with Hong Kong's banking sector representatives in order to achieve this end.

- 3.7.1 Many countries around the world have introduced competition law exemptions or other forms of sector-specific treatment for banks and/or other types of financial institutions, most commonly granted so as to reduce risk and uncertainty and ensure systemic stability.
- 3.7.2 In this context, HKAB believes that it is important for the Government to ensure that, once established, the Commission gives priority to considering the banking and financial sector and what types of exemptions and exclusions it is appropriate to adopt in respect of the sector.
- 3.7.3 The importance of this is well recognised around the world. For example, in Europe, the insurance sector benefits from a Block Exemption Regulation that allows European insurers to collaborate in certain specified circumstances that may otherwise be subject to challenge under Europe's equivalent to the First Conduct Rule ("**the EU Insurance BER**").
- 3.7.4 Exemptions have previously existed in other jurisdictions for selected activities of financial institutions such as consortium lending and implementation of certain restrictive agreements, for reasons such as ensuring the stability of the banking system. Additionally, many merger regimes have incorporated special arrangements or provisions applicable to the banking and/or financial sector<sup>11</sup>.
- 3.7.5 Importantly, even where exemptions or special arrangements of the type mentioned in clause 3.7.4 have been removed after a period of application, this has commonly occurred as part of broader steps to streamline administration of the relevant competition law regime and facilitate more 'self assessment' by businesses subject to the regime, rather than necessarily as a result of a change in perspective regarding whether the relevant business practices warrant clearance or some form of special treatment. Moreover, such steps are usually pursued only after the regime has been in place for a sufficient period of time to afford the business sector a high level of understanding regarding how the regime operates in practice and how broadly worded provisions and prohibitions will be interpreted and applied by the competition regulator(s) and courts. Obviously it will take some time to reach this point in Hong Kong, given that participants in most domestic industry sectors have not previously had to deal with the application of competition laws. Accordingly, in the lead-up to introduction of the Proposed Law in Hong Kong, it will be more appropriate to focus on ensuring clarity when it comes to implementing relevant guidelines and exemptions in the initial phase of regime implementation.

*The EU Insurance BER as an illustration of why sector-specific issues require special treatment*

- 3.7.6 The EU Insurance BER is a helpful case study in the context of this submission. The EU Insurance BER recognises that many forms of cooperation between insurers are necessary and appropriate in order for the insurance system to operate in a way that is both prudent and works best for customers, such as:

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<sup>11</sup> For example: (a) Prior to 1998, Finnish legislation included special provisions applicable to competition review of bank mergers; (b) the French Authorities have been required to consult with the banking regulator before taking a decision and to provide a full explanation, should they decide to deviate; and (c) prior to 1986, interbank agreements and mergers involving banks were exempted from Canada's competition law.

- the sharing of information to make prudent premium calculation possible and limits the risk of vigorous market-based competition proving ruinous in insurance markets; and
- certain insurance pooling arrangements to assist the industry to properly accommodate insurance risks.

3.7.7 The European Commission recently reviewed the scope of the EU Insurance BER and decided to continue these aforementioned exemptions for a further 7 years.

3.7.8 HKAB believes that there are a number of areas where issues broadly analogous to those referenced in paragraph 3.7.6 arise in relation to the banking and financial sector, such as in respect of the activities mentioned in paragraph 3.2.5 of this submission.

3.7.9 Accordingly, the HKAB believes it will be appropriate for the Hong Kong Government to ensure the Commission makes it a priority to:

- (a) identify areas of business activity that are properly excluded from, or specially dealt with under, the Conduct Rules; and
- (b) more generally liaise with representatives of the banking sector to determine where existing industry arrangements are already subject to appropriate regulation and control or should otherwise properly fall outside of the proper ambit of competition review.

3.7.10 HKAB recognises that, given the existing mechanisms in the Bill for the Commission to consider and introduce Block Exemption Orders after it has been established, it may be unnecessary or extraneous to include a specific reference in the Bill to the need for such orders or other exclusions specific to the banking sector. Accordingly, at this stage HKAB recommends that the Bills Committee focus on highlighting to the Government the importance of ensuring that the Commission introduces Block Exemption Orders or other exemptions and exclusions covering relevant aspects of banking and financial sector practice, and for the Commission to consult foreign competition regimes and liaise with Hong Kong's banking sector representatives in order to achieve this end.

### 3.8 A level playing field where banks compete with statutory bodies:

**Recommendation 8:** HKAB recommends that the Bills Committee seek amendments to the Bill to remove any specific form of exemption for statutory bodies. Alternatively, if this recommendation is not adopted, or the Government continues to resist this form of amendment to the proposed competition law regime, then HKAB recommends that the Bills Committee:

- request that, as soon as possible, the Government should publish a preliminary list of those statutory bodies (and the scope of their activities) that the Government favours making subject to the Conduct Rules in accordance with section 3 of the Bill, and should then allow submissions to be made by interested parties regarding the list before it is finalised; and
- highlight to the Government the importance of ensuring that any statutory body which provides goods or services in competition with private sector entities should be required to comply with the Conduct Rules when providing those goods or services (subject to the application of other relevant exemptions and exclusions), including the Hong Kong Export Credit Insurance Corporation ("HKECIC").

- 3.8.1 Section 3 of the Bill effectively excludes statutory bodies from the scope of the Conduct Rules, except and to the extent that one or more particular statutory bodies (or certain activities of one or more statutory bodies) are specified in regulations made by the Chief Executive in Council.
- 3.8.2 Based on statements made by the Secretary for Commerce and Economic Development in June 2010, HKAB understands that the Government is reviewing the activities and functions of all statutory bodies in Hong Kong, and will announce in due course which of these bodies will be (or have certain of their activities) specified in a regulation made by the Chief Executive in Council under section 5 of the Bill with the effect that those bodies/activities will be subject to the Conduct Rules.
- 3.8.3 HKAB does not believe that a compelling case has been made for the introduction of a specific exemption for statutory bodies (or certain activities of statutory bodies) from the Proposed Law, and believes that inclusion of such an exemption undermines principles of fairness and promotion of a 'level playing field' for businesses in Hong Kong.
- 3.8.4 As noted in previous consultation papers, many (but by no means all) statutory bodies engage in activities that are not economic in nature, or provide services that may be considered essential public services, and thus may benefit from separate forms of exclusion or exemption from the law. However, HKAB strongly believes that activities of statutory bodies that do not fall into these categories should be subject to the Conduct Rules, particularly where undertaken in competition with private sector entities.
- 3.8.5 To date, HKAB is aware of only two main arguments that the Government has raised in support of the proposed exemption for statutory bodies, being<sup>12</sup>:
- to shield such bodies from unfounded and misconceived complaints; and
  - anti-competitive conduct in the private sector is the main competition-related concern of the public.
- 3.8.6 HKAB believes that these arguments are obviously flawed, for reasons that include the following:
- In relation to the issue of unfounded and misconceived complaints, it is noted that section 37 of the Bill provides that the Commission is not required to investigate a complaint if it is satisfied that the complaint is "trivial, frivolous or vexatious" or "is misconceived or lacking in substance", and this safeguard against such complaints would automatically apply in relation to any complaints relating to statutory bodies. In any case, it is difficult to see why any concern about statutory bodies being required to deal with such complaints is not equally a concern in relation to the private sector.
  - In relation to the issue of the 'main' concerns of the public, it is not clear how the Government has reached this view. Even if it is correct that submissions made by the general public during consultation on the Proposed Law focussed on conduct by the private sector (and this is unclear), this could not reasonably be viewed as

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<sup>12</sup>

Refer paragraph 16 of Chapter VII of the May 2008 Consultation Paper, where it is stated that "This approach [of exempting statutory bodies] should help ensure that the operation of ... statutory bodies would not be affected by unfounded and misconceived complaints" and "Feedback from the previous consultation exercise and subsequent discussion with stakeholders indicated that the main concern of the public is anti-competitive conduct in the private sector".

indicating that the public accepted or was unconcerned by anti-competitive practices by statutory bodies. Rather, HKAB submits that it is reasonable to expect that the public interest demands that the Bill be framed in a manner that reflects the aim of fairness and a level playing field, and thus should be capable of addressing anti-competitive practices in all areas of Hong Kong's economy.

3.8.7 Accordingly, HKAB's primary recommendation to the Bills Committee in relation to this issue is that the Bills Committee seeks to amend the Bill to remove any specific form of exemption for statutory bodies.

3.8.8 However, if this recommendation is not adopted, or the Government continues to resist this form of amendment to the proposed competition law regime, then HKAB suggests that it will be important for the Bills Committee to highlight to the Government the need for greater transparency and consultation in relation to its ongoing review of statutory bodies in the context of section 3 of the Bill, as well as reinforce to the Government the need to ensure that any statutory body that acts wholly or partly as a commercial entity in competition with private sector entities is specified to be a non-exempt body in the context of the aforementioned section.

3.8.9 In this context, HKAB welcomes the inclusion in section 5(2) of the Bill of a list of criteria that the Chief Executive should have regard to before deciding to specify a particular statutory bodies or certain of its activities in accordance with section 3, namely that:-

- the statutory body is engaging in an economic activity in direct competition with another undertaking;
- the economic activity of the statutory body is affecting the economic efficiency of a specific market;
- the economic activity of the statutory body is not directly related to the provision of an essential public service or the implementation of public policy; and
- there are no other exceptional and compelling reasons of public policy against making such a regulation.

3.8.10 In particular, HKAB welcomes the implicit recognition of the Government by inclusion of the aforementioned wording in the Bill that some statutory bodies compete against the private sector in certain markets, and in doing so may engage in activities that detrimentally affect the economic efficiency of those markets.

3.8.11 Indeed, HKAB notes that there are several key examples of entities that have been formed under an Ordinance, or are given certain monopoly or significant rights under an Ordinance, and who compete with member banks and other financial institutions or may be seen to engage in activities which materially affect the markets in which banks and financial institutions compete, such as:

- the Hong Kong Mortgage Corporation ("HKMC"), which competes with the private sector in providing mortgage guarantee and fixed adjustable rate mortgage programs;
- the HKECIC, which offers certain insurance services to Hong Kong exporters; and

- Hong Kong Exchanges and Clearing Ltd ("**HKEx**"), which provides a trading venue that competes with the private sector "dark pools" which provide trading capabilities for Hong Kong listed equities.

3.8.12 If the broad exemption for statutory bodies is retained in the Bill, then HKAB understands:

- the exclusion of 'companies' from the definition of the term 'statutory body' in the Bill means that HKMC (which was incorporated in Hong Kong as a limited liability company under the Companies Ordinance on 3 March 1997) and HKEx would not benefit from the exemption, which position is supported by HKAB; but
- HKECIC would benefit from the exemption on the basis that it was formed under the Hong Kong Export Credit Insurance Corporation Ordinance, which position is not supported by HKAB on the basis that HKECIC clearly operates in competition with private sector entities.

3.8.13 HKAB submits that it is clear any failure to subject bodies such as the HKECIC to the Proposed Law would put them at a significant competitive and regulatory advantage over private organisations that were subject to such a law and the burdens it necessarily entails.

3.8.14 Accordingly, if the HKAB's primary recommendation to the Bills Committee in relation to this issue (that the Bills Committee seek to amend the Bill to remove any specific form of exemption for statutory bodies) is not adopted or able to be implemented, then HKAB recommends that the Bills Committee:

- request that, as soon as possible, the Government should publish a preliminary list of those statutory bodies (and the scope of their activities) that the Government favours making subject to the Conduct Rules in accordance with section 3 of the Bill, and should then allow submissions to be made by interested parties regarding the list before it is finalised; and
- highlight to the Government the importance of ensuring that, at a minimum, economic activities of statutory bodies such as the HKECIC should be made subject to the Conduct Rules, along with any other body that acts wholly or partly as a commercial entity in competition with private sector entities.

### 3.9 Other matters:

**Recommendations 9 - 11:** HKAB recommends that the Bills Committee consider seeking:

- removal of some of the restrictions on the process set out in Subdivision 2 of Part 2 of the Bill pursuant to which undertakings may apply to the Commission for a decision as to whether or not an agreement that they have entered into (or propose to enter into) would benefit from a relevant exemption or exclusion from the Conduct Rules;
- the introduction of a substantiality requirement into the Conduct Rules so as to ensure that conduct which exerts an insignificant or unappreciable effect on a market will not be subject to unnecessary regulatory intervention; and

- the introduction of certain 'de minimus' thresholds into the Bill to automatically exclude from challenge under the First Conduct Rule agreements of minor importance.

3.9.1 Paragraphs 3.1 to 3.8 of this submission address the priority concerns of HKAB members in relation to the Bill as at the date of this submission. However, HKAB would also like to briefly supplement the comments in those paragraphs with three further recommendations explained below.

*Broadening the 'Application Process'*

3.9.2 Clause 9 of the Bill provides that an undertaking may apply to the Commission for a decision as to whether or not an agreement that they have entered into (or propose to enter into) would benefit from a relevant exemption or exclusion (hereafter, the "**Application Process**") - including the exclusion under Schedule 1 of the Bill for agreements that enhance overall economic efficiency.

3.9.3 However, the Bill provides that the Commission is only required to consider such an application in certain specific circumstances, which include if the application "poses novel or unresolved questions of wider importance or public interest in relation to the application of exclusions or exemptions". Further, section 10 of the Bill provides that the Commission must publish notice of the application and accept representations from third parties in relation to it before any decision on the application can be made.

3.9.4 HKAB is concerned that these restrictions on the Application Process will in most cases deprive undertakings of any useful process for consulting with the Commission to receive comfort on the legality of their agreements.

3.9.5 In this context, HKAB notes that a much broader form of Application Process applied for many years in jurisdictions such as Europe. Although businesses operating under the European regime are now required to 'self assess' the legality of their agreements under Europe's primary competition law as mentioned in paragraph 3.7.5, the move away from having a broad form of Application Process only occurred after it has been in existence for many years, ensuring that the business sector had sufficient enforcement experience to draw on for reference and sufficient time in which to ascertain the interpretation and enforcement approach of the European regulators and courts.

3.9.6 In this context, HKAB considers that it is especially appropriate for businesses in Hong Kong to have access to an Application Process of broad scope, given that many such businesses will have never previously been exposed to competition laws and will require time to fully understand the nuances of its application.

3.9.7 Accordingly, HKAB recommends that the Bills Committee give consideration to seeking removal of some of the restrictions on the Application Process, so as to broaden its utility at least in the initial years of enforcement of the Proposed Law. In the same way that the Government has indicated that the need for cross-sector merger control provisions is something that can be further considered only after a period of review of the effect of the Proposed Law, it is submitted that the Government (and Commission) should only consider narrowing the scope of an initially broad Application Process after an initial period from which its ongoing utility can be assessed.



### *Threshold of harm*

- 3.9.8 The First Conduct Rule effectively prohibits agreements or arrangements that have the purpose or effect of preventing, restricting or distorting competition in Hong Kong. The Bill does not specify that a certain 'threshold of harm' (such as an 'appreciable' or 'substantial' restriction or distortion of competition) must be achieved - or be the purpose - of a relevant agreement or arrangement before the First Conduct Rule is reached. Indeed, on its face the First Conduct Rule could be breached even by conduct that caused an extremely minimal restriction of competition - notwithstanding that such conduct would not normally be subject to challenge in most mature competition law regimes.
- 3.9.9 This can be contrasted with the prohibition that applies to relevant 'M&A' transactions involving telecommunications licensees - which is only breached if the relevant transactions "*substantially* lessen competition" in a relevant market.
- 3.9.10 In many other jurisdictions, similar thresholds of harm are specified in prohibitions that are broadly equivalent to the First Conduct Rule. For example, in Australia most anti-competitive conduct is not actionable unless it results in (or has the purpose of) substantially lessening competition.
- 3.9.11 HKAB supports the amendment of the First Conduct Rule to incorporate a substantiality requirement, to ensure that conduct which exerts an insignificant or unappreciable effect on a market will not be subject to unnecessary regulatory intervention.
- 3.9.12 HKAB recognises that a form of substantiality requirement could conceivably be introduced via Commission guidelines outlining its enforcement priorities. However, it is again noted that any guidelines issued by the Commission will not be binding on the judiciary. Accordingly, HKAB submits that the matter is best dealt with by amendment of the Bill, and encourages the Bills Committee to seek such amendment.

### *De minimis rule*

- 3.9.13 Finally, and as a follow-on to the matters discussed in paragraphs 3.9.8 to 3.9.12 of this submission, HKAB supports the adoption of an appropriately framed 'de minimis' rule as part of the enforcement framework for the Proposed Law. Such a rule aims to take conduct that does not relate to a 'substantial part' of a relevant market (such as agreements between small and medium sized businesses) outside of the purview of the relevant competition law.
- 3.9.14 A useful example of such a 'de minimis' rule is found in the 'Guidelines on the Major Provisions' (of Singapore's Competition Act) published by the Competition Commission of Singapore, which state that:

*"As Singapore is a small and open economy, an agreement will generally have no appreciable adverse effect on competition:*

- if the aggregate market share of the parties to the agreement does not exceed 20 per cent on any of the relevant markets affected by the agreement where the arrangement made is between competing undertakings (i.e. undertakings which are actual or potential competitors on any of the markets concerned);*

- *if the market share of each of the parties to the agreement does not exceed 25 per cent on any of the relevant markets affected by the agreement, where the agreement is made between non-competing undertakings (i.e. undertakings which are neither actual nor potential competitors on any of the markets concerned);*
- *in the case of an agreement between undertakings where each undertaking is a small or medium enterprise ('SME')."*

3.9.15 As the equivalent prohibitions to the Hong Kong Bill's Conduct Rules in Singapore's Competition Act only apply where the relevant conduct has the effect of *appreciably* preventing, restricting or distorting competition within Singapore, the above 'de minimis' rule has the effect of ensuring that agreements that fall within the 3 stated categories will not (subject to relevant exceptions stated elsewhere in the Guidelines) be subject to review under relevant anti-competitive conduct prohibitions.

3.9.16 It is submitted that provisions or guidelines of this nature would be appropriate for inclusion in the Bill or subsequent enforcement guidelines, and HKAB encourages the Bills Committee to seek this outcome. This would assist to provide comfort to smaller businesses or participants in strongly contested markets regarding the potential impact of the Proposed Law, and relieve those businesses of some of the administrative and economic burden that may otherwise arise relating to legal review of all agreements.

#### **4. Conclusion**

HKAB requests that the Bills Committee give due consideration to the comments and recommendations set out in the submission, which are provided in the interests of ensuring that any new competition law in Hong Kong is implemented in a manner that balances the interests of safeguarding competition in Hong Kong with the benefits of facilitating the free play of market forces and continuing to promote a business-friendly environment in the region.

HKAB would be pleased to discuss or supplement this submission in any manner that may be useful for the Bills Committee, and any enquiries in this regard may be directed to:

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## ANNEX A

### EXECUTIVE SUMMARY (RECOMMENDATIONS)

For the reasons set out in the attached submission, HKAB makes the following recommendations to the Bills Committee regarding the Competition Bill:

- **Recommendation 1:** HKAB recommends that the Bills Committee seek an amendment to the definition of "legal requirements" in section 2 of Schedule 1 of the Bill, so that conduct engaged in or agreements made in compliance with any requirements applicable under codes of practice, circulars, guidelines or other directions or guidance in any form issued or endorsed by a Government-approved regulatory or supervisory authority in Hong Kong (or a relevant supranational body) are excluded from challenge under the Conduct Rules. Additionally, HKAB recommends that the Bills Committee highlight to the Government the importance of ensuring that the Competition Commission takes appropriate steps (in consultation with the banking sector) to effectively exempt from the Conduct Rules conduct in compliance with directives or guidance issued by relevant supranational bodies or any other foreign regulatory or supervisory bodies outside Hong Kong having jurisdiction over the undertaking concerned.
- **Recommendation 2:** HKAB recommends that the Bills Committee highlight to the Government the importance of ensuring competition-orientated guidelines relating to relevant banking practices are developed by the Competition Commission as a priority, in consultation with relevant sector representatives, and published well prior to commencement of the Conduct Rules. This could be done by amending section 35 of the Bill to include references to the banking and other sectors in the text that requires the Competition Commission to issue guidelines on its interpretation and enforcement approach, or by the Government liaising with the Competition Commission after it is established to emphasize the benefit of developing and prioritising such guidance.
- **Recommendation 3:** HKAB recommends that the Bills Committee seek an amendment to the Bill to introduce a definition of the term 'market', and that this definition expressly reflect the fact that the geographic scope of many product and service markets contested by undertakings in Hong Kong extends beyond the territorial boundaries of the Hong Kong S.A.R. and will commonly encompass mainland China and beyond.
- **Recommendation 4:** HKAB recommends that the Bills Committee seek an amendment to the Bill to expressly exempt vertical agreements and M&A agreements from the scope

of the First Conduct Rule. In the alternative, if M&A agreements are to be subject to challenge, then HKAB submits that this should be in accordance with specific merger review provisions that will ensure there are appropriate procedural safeguards and review thresholds.

- **Recommendation 5:** HKAB believes that the Bills Committee should highlight to the Government the importance of ensuring the Competition Commission consults with banking regulators and other key banking sector representatives before conducting investigations and enforcement actions in relation to the sector or when developing guidelines specifically relating to the sector. More particularly, HKAB recommends the Bills Committee:
  - (a) seek an amendment to section 35 of the Bill (Guidelines) to require that when the Competition Commission is drafting or amending relevant guidelines in relation to the bill it must, at a minimum, consult with any body or association in Hong Kong that, under a Hong Kong Ordinance, is provided with regulatory, supervisory or representative functions or responsibilities in relation to an industry sector to which the relevant guidelines wholly or substantially relate; and
  - (b) seek an amendment to section 129 of the Bill (Functions of Commission) so that the Competition Commission is required to consult with any body or association in Hong Kong that, under a Hong Kong Ordinance, is provided with regulatory, supervisory or representative functions or responsibilities in relation to an industry sector before commencing any investigation or enforcement action in fulfilment of its function under paragraph (a) of that section ("to investigate conduct that may contravene the competition rules and enforce the provisions of this Ordinance").
- **Recommendation 6:** HKAB recommends that the Bills Committee seek an amendment to section 129 of the Bill (Functions of Commission) so that the Commission will be precluded from conducting market studies in respect of industry sectors that are already supervised by a sectoral regulator empowered to review and respond to instances of market failure.
- **Recommendation 7:** HKAB recommends that the Bills Committee highlight to the Government the importance of the Competition Commission introducing Block Exemption Orders or other exemptions and exclusions relating to relevant aspects of banking and financial sector practice, and for the Competition Commission to consult

foreign competition regimes and liaise with Hong Kong's banking sector representatives in order to achieve this end.

- **Recommendation 8:** HKAB recommends that the Bills Committee seek amendments to the Bill to remove any specific form of exemption for statutory bodies. Alternatively, if this recommendation is not adopted, or the Government continues to resist this form of amendment to the proposed competition law regime, then HKAB recommends that the Bills Committee:
  - (a) request that, as soon as possible, the Government should publish a preliminary list of those statutory bodies (and the scope of their activities) that the Government favours making subject to the Conduct Rules in accordance with section 3 of the Bill, and should then allow submissions to be made by interested parties regarding the list before it is finalised; and
  - (b) highlight to the Government the importance of ensuring that any statutory body which provides goods or services in competition with private sector entities should be required to comply with the Conduct Rules when providing those goods or services (subject to the application of other relevant exemptions and exclusions), including the Hong Kong Export Credit Insurance Corporation.
- **Recommendation 9:** HKAB recommends that the Bills Committee consider seeking removal of some of the restrictions on the process set out in Subdivision 2 of Part 2 of the Bill pursuant to which undertakings may apply to the Competition Commission for a decision as to whether or not an agreement that they have entered in to (or propose to enter into) would benefit from a relevant exemption or exclusion from the Conduct Rules.
- **Recommendation 10:** HKAB recommends that the Bills Committee consider seeking the introduction of a substantiality requirement into the Conduct Rules so as to ensure that conduct which exerts an insignificant or unappreciable effect on a market will not be subject to unnecessary regulatory intervention.
- **Recommendation 11:** HKAB recommends that the Bills Committee consider seeking the introduction of certain 'de minimus' thresholds into the Bill to automatically exclude from challenge under the First Conduct Rule agreements of minor importance.