For discussion
on 22 November 2011

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, including those relating to the proposed amendments to the Competition Bill ("Bill") set out in Paper No. CB(1)91/11-12(01).

A. Thresholds for the de minimis arrangements

Basis for determining the threshold for the second conduct rule

2. The Administration has proposed that the de minimis threshold for the second conduct rule should be HK$11 million, being the turnover of an undertaking in the preceding financial year. According to the statistics of the Census and Statistics Department (C&SD), the average annual business turnover of small and medium enterprises (SMEs) in Hong Kong has been steady through 2005 to 2009 at about HK$ 11 million. The rationale of the proposed threshold is that a smaller-than-average-sized SME is unlikely to have a substantial degree of market power in a market and its conduct would unlikely constitute an abuse of market power causing an appreciable effect on competition.

3. While an undertaking with an annual turnover above HK$ 11 million is not excluded from the application of the second conduct rule, it does not automatically mean that it will possess a substantial degree of market power. For undertakings with an annual turnover above the threshold, it is a question of fact as to whether or not the undertaking possesses a substantial degree of market power, taking account of the circumstances of each case. Even if the undertaking possesses a substantial degree of market power, the second conduct rule would not apply unless the undertaking abuses that power by engaging in conduct that has as its object or effect the prevention, restriction or distortion of competition in Hong Kong.

4. Other overseas jurisdictions such as the EU, Singapore and Canada do not provide any de minimis arrangement for their prohibition against abuse of market power. In the UK, a "conduct of minor significance" approach is stipulated in section 40 of the UK Competition Act 1998 which provides that conduct of an undertaking with a turnover not exceeding GBP 50 million is considered to be conduct of minor significance, and such undertaking is immune from financial penalties. The Office of Fair Trading may still take other enforcement actions, and can withdraw the immunity from financial penalties if, having investigated the conduct, it considers the conduct is likely to infringe the competition law.

Statistics for deriving the threshold

5. The methodology in compiling the statistics on the average annual turnover of SMEs is set out at **Appendix A**. The breakdown by turnover level and by number of establishments is set out at **Appendix B**.

Other benchmarks of business turnover

6. It is noted that under the Companies Bill, a private company (except for certain exceptions) would be regarded as a "small private company" if it satisfies any two of the following conditions: (i) total annual revenue of not more than HK$50 million; (ii) total assets of not more than HK$ 50 million; and (iii) no more than 50 employees. We understand that the qualifying criteria have been formulated, on the advice of the Hong Kong Institute of Certified Public Accountants (HKICPA), to enable small companies to prepare simplified financial and directors' reports. Such criteria of small private company only concern which entity could opt for a simplified reporting framework under the Companies Bill for the sake of business facilitation. They are of limited relevance to our Bill in the context of assessing the likely effect of restrictive agreements between undertakings or conduct of an undertaking on market competition under the de minimis framework.

7. As regards the request for aggregate data on the level of turnover of companies paying profits tax in Hong Kong, we are checking with the Inland Revenue Department on the availability of the data and will provide a reply to the Bills Committee in our next submission.

B. Abuse of market power

Factors for assessing market power

8. Members asked about the relevant factors for assessing the degree of market power of an undertaking. As we have explained on earlier occasions, market power arises where an undertaking does not face sufficiently strong competitive pressure and can be thought of as the ability to profitably sustain prices above competitive levels or to restrict output or quality below competitive levels.

9. Market power is a matter of degree and is assessed on a case-by-case basis. While an undertaking's market share over time is an important factor to assess whether market power exists, market share does not on its own determine whether an undertaking possesses market power. To assess the degree of market power, competition authorities would take into account other factors such as the existing competition in the market, the ease of entry into the market, and the bargaining power of the buyers. Hence, it would be inappropriate to indicate a level of market share in the law for the purpose of assessing market power, which would limit the Competition Commission (the Commission)'s flexibility in enforcing the second conduct rule against powerful firms amidst changing market circumstances without regard to the characteristics of individual sector. It is international best practices for the competition authorities to explain the relevant factors in the assessment of market power in the regulatory guidelines. To this end, we have provided a set of template guidelines on the second conduct rule, vide Paper No. CB(1)2618/10-11(01), which sets out some of the key topics and contents that may be covered in the future guidelines to be issued by the Commission for Members' reference.

Dominance Vs substantial degree of market power

10. As regards the suggestion to replace the standard of "substantial degree of market power" with "dominance" for the second conduct rule, it is noted from overseas case law and regulatory guidelines that a firm would normally be considered as dominant only if it possesses a market share of at least 50% to 60%. While market share is only one of the determinants of market power, overseas jurisprudence of at least 50% presumption for "dominance" would inevitably be relevant to Hong Kong if we adopt the same legal language in the Bill. As explained in previous submissions, given Hong Kong's small and geographically concentrated economy, it is not unusual for certain economic sectors to have an oligopolistic structure involving few big companies, each

constituting a significant, albeit short of 50%, market share. Should we adopt the description of "dominance" for the second conduct rule, the future Commission's ability to address public concerns over exclusionary conduct of oligopolies would be affected. We therefore consider it appropriate for Hong Kong to adopt the threshold of "substantial market power".

Examples of abuse of market power

11. At Members' request, **Appendix C** summarises two overseas competition cases concerning the abuse of dominance/ substantial degree of market power.

C. Review of the Competition Ordinance

12. The Administration has undertaken to conduct a review of the competition law in a few years' time after its enactment. The purpose of such review is to critically examine the operational experience of the competition authorities in implementing the law, and to gauge public feedback on the effectiveness of the competition regime. The review findings would enable the Administration and the competition authorities to identify room for improvement, including necessary amendments to the law. Subject to the passage of the Bill and our proposed amendments, we envisage the review on the competition law would cover, but not limited to, the differential treatment of hardcore and non-hardcore conduct; the cap on pecuniary penalty; the de minimis arrangements; private action rights; and merger control. We consider that the exact timing of the review should be determined after the coming into effect of the law, when the institutional framework is in place and as Hong Kong builds up its own case law.

D. Clause 141(1)(c)

13. With the proposed amendments to take out the right of standalone private action from the Bill, the legal advisor to the Bills Committee has suggested that clause 141(1)(c) of the Bill be amended to clarify that the "private actions" mentioned therein referred to follow-on actions. Given clause 106 which provides that no proceedings may be brought independently of the Bill, it is clear that the "private actions" referred to in clause 141(1)(c) are private actions under Part 7 of the Bill, which would be left with follow-on actions only. Hence, from the drafting point of view, we consider it not necessary to change the reference in clause 141(1)(c) from "private actions" to "follow-on actions".

E. Questions raised by Hon Jeffrey Lam

14. Our response to questions raised by Hon Jeffrey Lam in his letter to the Bills Committee dated 25 October 2011 is set out at **Appendix D**.

Advice sought

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

Commerce and Economic Development Bureau
November 2011

Appendix A

Methodology of the Annual Survey of Economic Activities of the Census and Statistics Department

Survey Background

The Census and Statistics Department (C&SD) introduced the Annual Survey of Economic Activities (ASEA) starting from the reference year of 2009 as an integrated survey to replace the annual economic surveys[1] on major economic sectors conducted in past years, with a view to achieving further harmonisation and streamlining of survey processes. Survey results in respect of the different major economic sectors are published in the respective survey reports annually.

Survey Objectives

2. The ASEA aims to provide statistical information for gauging the business performance and operating characteristics of different economic sectors and for evaluating their contribution to Hong Kong's Gross Domestic Product. The survey results are useful to both the Government and the private sector in formulating policies and making decisions.

Legislation

3. The ASEA is conducted under Part III of the Census and Statistics Ordinance (Chapter 316 of the Laws of Hong Kong). It was notified as a mandatory statistical survey in Legal Notice 218 of 2009 in the Government of the HKSAR Gazette of November 6, 2009. The Ordinance also stipulates that all collected information which may enable identification of individual establishments should be kept in strict confidence and be used solely for statistical purposes. Only aggregate information, which does not reveal details of individual establishments, will be released.

Classification of Industries

4. The Hong Kong Standard Industrial Classification (HSIC) has been adopted in the survey for sample selection, data collection and dissemination of survey results. The HSIC is devised by using the United Nations' International Standard Industrial Classification as the framework, with local adaptation to reflect the structural characteristics of the Hong Kong economy.

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[1] The Annual Economic Surveys include：

(a) Annual Survey of Industrial Production (first conducted for 1973 round and then for each of the years from 1976 to 2008)

(b) Annual Survey of Building, Construction and Real Estate Sectors (first conducted for 1979 round and then for each of the years from 1981 to 2008)

(c) Annual Survey of Transport and Related Services (conducted for each of the years from 1980 to 2008)

(d) Annual Survey of Wholesale, Retail and Import and Export Trades, Restaurants and Hotels (first conducted for 1977 round and then for each of the years from 1979 to 2008)

(e) Annual Survey of Storage, Communication, Financing, Insurance and Business Services (first conducted for 1980 round and then for each of the years from 1982 to 2008)

(f) Annual Survey of Banks, Deposit-taking Companies, Restricted Licence Banks and Representative Offices of Foreign Banks (first conducted for 1980 round and then for each of the years from 1982 to 2008)

5. HSIC Version 2.0 has been used in ASEA starting from the reference year of 2009, to replace HSIC Version 1.1 which was used in previous rounds of annual economic surveys. To maintain data continuity and comparability before and after the implementation of HSIC Version 2.0, the C&SD has re-compiled survey results dating back to 2005 in accordance with HSIC Version 2.0.

Survey Reference Period

6. For the survey reference year of 2009, data collected in the survey referred to the calendar year 2009, or any consecutive 12-month period between 1 January 2009 and 31 March 2010 according to the accounting practice of individual establishments. For establishments which commenced or ceased operation within their respective accounting periods which fall within the survey reference period, data collected were for that part of the period during which the establishments were in operation.

Data Collection

7. The survey questionnaire comprises two parts: the main part collects basic data and the supplementary part collects more detailed data on specific topics. Survey questionnaires are sent out by post and/or via electronic mails starting from January every year to the selected establishments requesting them to return the completed questionnaires by the end of May. In March, staff of the C&SD start to make telephone contacts with or visit individual establishments to assist respondents in completing the questionnaires or to collect completed ones. Reminder letters are issued during different stages of the survey to urge respondents for an early response.

Data Processing

8. Completed questionnaires received are subject to thorough checking by statistical staff and detailed computer-based validation checks before tabulation. Such checkings cover completeness of entries, consistency among data items and credibility of reported data. Where dubious entries or inconsistencies in the reported data are observed, clarification is made with respondents by telephone or field verification visits. Reporting errors are rectified with information provided by respondents as far as possible.

Statistics Coverage and Dissemination Schedule

9. ASEA statistics cover establishments engaged in a number of different economic sectors in Hong Kong, including manufacturing, import and export trades, food services and financial activities, etc.. ASEA statistics are usually published within around 11-12 months after the end of the reference year.

Sample Design

10. The sampling frame is mainly based on the Central Register of Establishments maintained by the C&SD and updated by reference to records of the Business Registration Office. The sampling frame is first stratified by industry and, within each industry stratum, by employment size of establishments to form a number of industry/employment size strata. The sample size for each industry /employment size stratum is determined by Neyman's

allocation according to a desired level of precision for the estimated value added for individual industries. Individual establishments are systematically selected at a uniform interval after an establishment is randomly selected as a start.

Sample Size and Response Rate

11. The sample size for the aforementioned coverage of statistics in the survey reference year of 2009 was around 18 000 establishments of which about 80% were SMEs. The response rates for all establishments and SMEs in the 2009 round were both 85%.

Census & Statistics Department
November 2011

Appendix B

Table 1: SME statistics by employment size, 2005-2009

Year	Level of employment size	Number of establishments
2005	<10	230 294
	10-49[1]	27 968
	Total	**258 262**
2006	<10	234 491
	10-49[1]	28 329
	Total	**262 820**
2007	<10	229 476
	10-49[1]	27 761
	Total	**257 237**
2008	<10	231 926
	10-49[1]	27 997
	Total	**259 923**
2009	<10	243 787
	10-49[1]	27 496
	Total	**271 283**

Notes:

1 Following the current definition of SME adopted by TID, a SME is defined as "a manufacturing business which engages fewer than 100 persons in Hong Kong; or a non-manufacturing business which engages fewer than 50 persons in Hong Kong". In this class, manufacturing businesses which engage 50-99 are also included.

2 The above statistics do not cover the following economic activities under the Hong Kong Standard Industrial Classification Version 2.0:

(i) Agriculture, forestry and fishing

(ii) Mining and quarrying

(iii) Community, social and personal services

3 *Establishment* is ideally an economic unit which engages, under a single ownership or control, in one or predominantly one kind of economic activity at a single physical location. Where separate figures relating to different activities or different locations under the same management are not available, a combined return is accepted and in this case, the reporting unit is treated as an establishment.

Data Source:

Annual Survey of Economic Activities (or the Programme of Annual Economic Surveys for 2008 or before)

Appendix B

Table 2: SME statistics by level of business receipts, 2005-2009

Year	Level of business receipts	Number of establishments
2005	<1 million	127 395
	1 million - <5 million	72 685
	5 million - <10 million	18 854
	10 million - <20 million	18 142
	20 million - <50 million	12 558
	>= 50 million	8 628
	Total	**258 262**
2006	<1 million	126 845
	1 million - <5 million	73 794
	5 million - <10 million	22 549
	10 million - <20 million	16 042
	20 million - <50 million	13 020
	>= 50 million	10 569
	Total	**262 820**
2007	<1 million	123 718
	1 million - <5 million	69 704
	5 million - <10 million	23 850
	10 million - <20 million	18 185
	20 million - <50 million	11 129
	>= 50 million	10 650
	Total	**257 237**
2008	<1 million	117 608
	1 million - <5 million	77 316
	5 million - <10 million	20 573
	10 million - <20 million	19 564
	20 million - <50 million	13 489
	>= 50 million	11 372
	Total	**259 923**
2009	<1 million	130 069
	1 million - <5 million	75 656
	5 million - <10 million	24 059
	10 million - <20 million	16 788
	20 million - <50 million	13 739
	>= 50 million	10 970
	Total	**271 283**

Notes:

1 Following the current definition of SME adopted by TID, a SME is defined as "a manufacturing business which engages fewer than 100 persons in Hong Kong; or a non-manufacturing business which engages fewer than 50 persons in Hong Kong".

2 The above statistics do not cover the following economic activities under the Hong Kong Standard Industrial Classification Version 2.0:

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Data Source:

Annual Survey of Economic Activities (or the Programme of Annual Economic Surveys for 2008 or before)

Appendix C

Examples of abuse of dominance or substantial degree of market power as determined by overseas competition authorities

A. Predatory pricing

AKZO Chemie BV *- Judgment of the European Court of Justice (ECJ) ([1991] ECR I-3359)*

- AKZO, a large Dutch multinational firm, and ECS (Engineering and Chemical Supplies Ltd.), a small United Kingdom (UK) firm, both manufactured organic peroxides. AKZO had a 50% market share in the market for organic peroxide.

- AKZO and ECS competed in the market for benzoyl peroxide, which is the most important organic peroxide and can be used as a bleaching agent in the production of flour and as an initiator of the polymer production process in the production of plastics.

- ECS originally only operated in the flour market, but later moved into the plastics market and solicited some of AKZO's customers. AKZO threatened to take punitive action against ECS in the flour market unless the latter withdrew from the plastics market. ECS refused and AKZO began selective price cutting against certain of ECS's customers in the flour market.

- From the end of 1980 for about four years, AKZO took the following three courses of action –

  (i) selling benzoyl peroxide to ECS's customers in the flour segment at below cost and substantially below the prevailing market price. Meanwhile, AKZO charged its own loyal customers about 60% more than the targeted customers of ECS;

  (ii) selling the targeted customers flour milling complements at below AKZO's average cost; and

  (iii) selling the targeted customers vitamin mixes, which it had bought specifically to resell to these customers, at below its own purchase prices.

- The issue for the ECJ was whether AKZO's price cutting constituted predatory pricing and violated Article 82 of the EC Treaty, as found by the European Commission (EC). The ECJ held that a 50% market share created a presumption of dominance, and also pointed to AKZO's superior marketing organization and technical knowledge regarding safety and toxicology to support its conclusion. Having ascertained AKZO's dominant position, the ECJ affirmed that AKZO had committed an abuse under Article 82 "*through recourse to methods which, different from those which condition normal competition in products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing in the market or the growth of that competition*".

B. Refusal to supply

Microsoft Corporation *– Decision of the EC (2004) – official journal of the European Union (2007/53/EC)*

- Microsoft is a software company that holds a dominant position in the Client Personal Computers (PC) operating system market as a result of the popularity of its product, Windows. The dominant position is characterized by market shares that have remained very high at least since 1996 (as high as 90%+ in the early 21st century), and by the presence of very high barriers to entry. These barriers to entry are in particular linked to the presence of indirect network effects, as the popularity of a PC operating system among users derives from its popularity among vendors of PC applications, which in turn choose to focus their development efforts towards the PC operating system which is most popular among users.

- Microsoft also develops work group server operating systems (work server system), which are used by offices as the core part of corporate IT networks (e.g. sharing of files and printers, network user administration, etc.). The EC considered that Microsoft has achieved a dominant position in the work server system market, as it held the leading market share which, under every measure, is above 50% and for most measures, is in the 60%-75% range.

- There are strong commercial and technical associative links between the PC operating system market and the work server system market. As a result, Microsoft's dominance over the PC operating system market has a significant impact on the adjacent market for work server systems.

- The EC took a decision in March 2004 finding that Microsoft has violated the EU Treaty's competition rules by abusing its near monopoly (Article 82) in the PC operating system. Specifically, the EC found that Microsoft abused its market power by refusing to provide Sun, its competitor, with information enabling the latter to design competitive work server systems to the extent that Microsoft restricts inter-operability between Windows PCs and non-Microsoft work group servers. Microsoft's refusal risks eliminating competition in the relevant market for work server systems because the refused input is indispensable for competitors operating in that market. Such refusal limits technical development to the prejudice of consumers, in contradiction of Article 82(b).

C. Tying

Microsoft Corporation *– Decision of the EC (2004) – official journal of the European Union (2007/53/EC)*

- Same case and facts as (B). The EC also found Microsoft abusing its dominant position in the PC operating system market by tying Windows Media Player (WMP), a product where Microsoft faced competition, with its Windows operating system. The EC based its finding of a tying abuse on four elements:

(i) Microsoft holds a dominant position in the PC operating system market;

(ii) The Windows PC operating system and WMP are two separate products;

(iii) Microsoft does not give customers a choice to obtain Windows without WMP, as PC manufacturers must license Windows with WMP, or if they want to install an alternative media player on Windows, they can only do so in addition to WMP;

(iv) The tying by Microsoft forecloses competition. The tying affords Microsoft unmatched ubiquity of its media player on PCs worldwide, as it induces content providers and software developers to rely primarily on WMP technology to reach almost all PC users worldwide. With a wider array of complementary software and content, consumers will in turn prefer to use WMP. As a result, Microsoft's tying of its media player has the effect of foreclosing the media player market to competitors, and hence ultimately reducing consumer choice.

Appendix D

Responses to questions raised by Hon Jeffrey Lam
concerning the Administration's proposed amendments to the Competition Bill to address major concerns

	Questions [1]	Administration's Response
De minimis arrangement for the first conduct rule		
1.	Why the de minimis arrangements do not apply to four specified types of serious anti-competitive conduct?	The four types of serious anti-competitive conduct are considered hardcore contravention of competition rules, because such conduct restricts competition and will almost always have an appreciable adverse impact on competition. These conduct are commonly prohibited by competition laws in other jurisdictions and excluded from their de minimis arrangements.
2.	Whether two local stores with no market power would contravene the law if they agree to a price cut in face of competition from big players in the vicinity?	Pricing strategy is a common means of individual firms to compete in a market and it is legitimate for individual stores to cut their prices to compete with big players in their vicinity. However, an agreement between stores on price level would raise competition concern as it distorts the competitive process and deprives the consumers the possible benefits of lower prices resulting from competition.
3.	Whether conduct of the two local stores in (2) would be considered as serious anti-competitive conduct which has the effect of restricting competition?	As competition law is meant to regulate those agreements which have an appreciable adverse effect on market, it would be a question of fact to determine whether the agreement between two local stores is anti-competitive.

[1] The incoming letter was in Chinese only. For the original wordings of the questions, please refer to Hon Jeffrey Lam's letter to the Bills Committee dated 25 October 2011.

	Questions [1]	Administration's Response
4. 5.	Would the four specified types of serious anti-competitive conduct be made per se illegal as they are by their very nature be regarded as restricting competition appreciably?	As we have explained in our letter to the Hong Kong General Chamber of Commerce dated 25 July (copied to the Bills Committee), the Bill does not propose automatic breaches of conduct rules (i.e. no per se infringement of competition rules). The crux of the general prohibitions in the first and the second conduct rules is that the Competition Commission (the Commission) must show that an agreement or any conduct has the object, or the effect, of preventing, restricting or distorting competition in Hong Kong. That the four types of serious anti-competitive conduct are commonly regarded as agreements restricting competition does not alleviate the onus of the Commission to establish, as a matter of fact, that a particular conduct has contravened the general prohibitions.
6.	How many one-man establishments or shell companies were included in the statistics compiled by the Census & Statistics Department (C&SD) relating to the average turnover of SMEs at $11 million? How the threshold of $100 million was derived? Why the Administration decided to set a threshold that would cover only 8-9 average-sized SMEs, and not more or less?	Regarding the statistics compiled from the Annual Survey of Economic Activities (the Survey) from which the average turnover of $11 million was derived, information in respect of inactive establishments or shell companies **was not included**. As regards one-man establishments, they ranged from 85 000 to 90 000 during 2005-2009, accounting for about one-third of the total number of SMEs covered in the Survey. In devising the turnover threshold for the first conduct rule, we have made reference to the turnover of an average-sized SME and consider that an agreement between undertakings the combined turnover of which does not exceed $100 million should not have a significant impact on competition in Hong Kong. There is no restriction that the participating undertakings must be average-sized SMEs but in terms of turnover amount, the proposed threshold is equivalent to the sum of the turnover of 8-9 average-sized SMEs.

	Questions [1]	Administration's Response
De minimis arrangement for the second conduct rule		
7.	How the threshold of $11 million for the second conduct rule was derived? Even for a small trading company with an annual turnover beyond $11 million, the net profit is very negligible.	We have also drawn reference from the turnover of an average-sized SME in proposing the threshold of $11 million for the second conduct rule. According to statistics compiled from the Survey, the average annual turnover of SMEs during 2005-2009 was $11 million. The rationale of adopting this threshold for the second conduct rule is that a smaller-than-average-sized SME is unlikely to have a substantial degree of market power in a market, and its conduct would unlikely constitute an abuse of market power under the second conduct rule.
8.	Does the Administration take the view that an undertaking with an annual turnover above $11 million possesses a substantial degree of market power under the Bill?	The de minimis arrangement is aimed at providing exclusion and as such, we need to have a level of certainty that the conduct of the undertaking is unlikely to restrict competition in a market appreciably. While an undertaking with an annual turnover above this threshold is not excluded from the application of the second conduct rule, it does not automatically mean that it will possess a substantial degree of market power or has breached the law. Conversely, the competition authority will have no enforcement power over an undertaking below the threshold even when it is involved in a conduct which restricts competition in a market appreciably. A prudent approach on setting the threshold is necessary to preserve the effectiveness of the law.
Warning notice and non-serious anti-competitive conduct		
9.	How to ensure that the Commission follows a due process in issuing the warning notice?	The Commission is required to discharge its statutory duty to issue warning notice to undertakings in respect of an agreement involving non-serious anti-competitive conduct under the Bill. As with other independent statutory bodies, the Commission will exercise its power impartially and reasonably in accordance with the provisions of the law.

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<tr><th></th><th>Questions [1]</th><th>Administration's Response</th></tr>
<tr><td>10.</td><td>What's the difference between warning notice, commitment and infringement notice after the removal of the payment requirement under the infringement notice regime? To which case do these arrangements apply?</td><td>A comparison of the warning notice, commitment and infringement notice is as follows –
<table>
<tr><th></th><th>Warning Notice</th><th>Commitment</th><th>Infringement Notice</th></tr>
<tr><td>Scope of application</td><td>Agreements involving non-serious anti-competitive conduct under the first conduct rule (new clause 80A)</td><td>Agreements or conduct to which the Commission has reasonable cause to believe that a competition rule has been contravened (clause 59)</td><td>Agreements or conduct to which the Commission has reasonable cause to believe that a contravention of the first conduct rule involving serious anti-competitive conduct or a contravention of the second conduct rule has occurred, before the Commission brings proceedings in the Tribunal. (newly amended clause 66)</td></tr>
<tr><td>Issued/ Made by whom</td><td>Commission (mandatory)</td><td>Made by a person to the Commission</td><td>Commission (discretionary)</td></tr>
<tr><td>Purpose</td><td>Undertakings are put on notice of the suspected contravention of the first conduct rule and be asked to cease the contravening act before expiry of the prescribed warning period.</td><td>To address the Commission's concerns about a possible contravention. It works on a consensual basis and the Commission may choose to accept it or not.</td><td>The Commission may issue an infringement notice to a person against whom the Commission proposes to bring proceedings, offering not to bring those proceedings on condition that the person makes a commitment to comply with the requirements of the notice, including to take or refrain from taking certain action, or admit a</td></tr>
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<tr><th></th><th>Questions [1]</th><th>Administration's Response</th></tr>
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<tr><td></td><td></td><td></td><td>contravention. It works on a consensual basis and the person may choose to accept it or not.</td></tr>
<tr><td>Effect</td><td>The Commission may bring proceedings in the Tribunal against the undertaking in respect of the contravening conduct if it is continued or repeated after the expiry of the warning period.</td><td>The Commission may not commence an investigation; may terminate an investigation; may agree not to bring proceedings in the Tribunal; or may terminate a proceeding if the commitment is accepted.</td><td>If a person makes a commitment to comply with the requirements of an infringement notice, the Commission may not bring proceedings against that person in respect of the contravention referred to in the notice.</td></tr>
<tr><td>Failure to comply</td><td>The Commission may bring proceedings in the Tribunal; liability is limited to the contravention starting from the commencement of the warning period.</td><td>The Commission may apply to the Tribunal for an order to enforce the commitment (clause 62).</td><td>The Commission may bring proceedings in the Tribunal or apply to the Tribunal for an order to enforce the commitment to comply with the requirements of the infringement notice.</td></tr>
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<tr><td>11.</td><td>There is only a commitment system in the EU. Does Hong Kong need three different systems to settle a case in lieu of bringing proceeding before the court?</td><td>The proposed infringement notice and warning notice have been put forward mainly in response to the concerns expressed by the local business community that more lenient enforcement options are required for certain circumstances. We note that the warning notice is not adopted in other major jurisdictions and will review the arrangements after we gain experience in enforcing the law.</td></tr>
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	Questions [1]	Administration's Response
12.	Whether the Commission "must" or "may" issue a warning notice under the new clause 80A in respect of non-serious anti-competitive conduct?	The Commission must issue a warning notice before taking out enforcement action in respect of non-serious anti-competitive agreement. For clarity sake, we would amend the heading of the new clause 80A to "Warning notice".
13.	Why the Commission is given the power to issue warning notice, bypassing the Tribunal?	We disagree that the power of issuing a warning notice by the Commission is quasi-judicial. Refusal to comply with a warning notice carries no adverse consequences to the undertaking since it is neither punishable nor will it create an adverse inference against that undertaking. In the event that the concerned undertaking fails to cease or repeats the anti-competitive activities, the Commission may institute legal proceedings in the Competition Tribunal and only the Tribunal can adjudicate on alleged contravention of the competition law.
14.	The power to issue warning notice by the Commission is quasi-judicial. Why the Commission is so empowered under the judicial model?	
Warning notice and the second conduct rule		
15.	Why the warning notice mechanism only applies to the first conduct rule?	The warning notice is aimed at addressing concerns that SMEs may inadvertently engage in non-serious anti-competitive conduct since it cannot be written into the law whether such conduct may give rise to competition concerns, and SMEs lack the means to carry out competition analysis for each of their activities. The warning notice would help undertakings concerned to rectify any non-serious anti-competitive behaviour, on the advice of the Commission, without breaching the law unknowingly. As regards contravention of the second conduct rule, it concerns abusive behaviour by powerful undertakings to foreclose competition in the market. Such unilateral conduct would otherwise have no appreciable adverse effect on competition if they are engaged in by a market player without a substantial degree of market power. Undertakings with market power will
16.	In respect of the conduct to be regulated under the second conduct rule, is there a differentiation between "serious" or "non-serious" conduct? Is there hard-and-fast rules to determine whether certain conduct is antic-competitive of a non-serious nature? Is there hard-and-fast rules	

	Questions [1]	Administration's Response
	to determine what constitutes abuse of market power, and if so, why the term "abuse" is not defined in the Bill?	have the necessary resources to follow the competition rules and they would unlikely be engaging in abusive conduct to foreclose competitors unwittingly. The warning notice system therefore does not apply to the second conduct rule.
Vertical agreements		
17.	Why the latest proposal does not cover the issue of vertical agreement?	On vertical agreements, while some of them would raise no competition concerns, there can be vertical agreements containing constraints which may lessen competition, as reflected in recent allegations that suppliers refused to supply certain products to retailers when the latter sold at prices lower than those required by the suppliers. In the light of the complexity involved and the prevalence of vertical agreements in Hong Kong, our view as elucidated in previous responses remains that in line with international best practices, it would be more appropriate for the Commission to consider issuing block exemption order to exempt certain types of vertical agreements having regard to the circumstances of Hong Kong after the enactment of the Bill. At the request of the Bills Committee, we have provided some overseas examples of block exemption orders which were granted to specified types of vertical agreements that would enhance overall economic efficiency. Moreover, since we have introduced the warning notice mechanism, businesses no longer need to worry about unknowingly breaching the law.
18.	Is the Administration aware that many of the sales and distribution arrangements entered into by SMEs are vertical agreements which could enhance overall economic efficiency?	