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Hutchison Telecom
Hong Kong

**RESPONSE OF HUTCHISON TELEPHONE COMPANY LIMITED AND HUTCHISON GLOBAL COMMUNICATIONS LIMITED TO THE DRAFT COMPETITION BILL**

**Date: 19 November 2010**

Hutchison Telecommunications (Hong Kong) Limited welcomes this opportunity to present the views of Hutchison Global Communications Limited and Hutchison Telephone Company Limited to the Bills Committee on the Competition Bill. As the Committee will be aware, similar competition provisions have been in force in the telecommunications and broadcasting sectors for a number of years. Our comments are based on our experience with these existing rules, and we hope our comments will assist the Committee in considering the Bill.

Objective of the Bill

The Government stated in its May 2008 Consultation Document that the objective of the Bill is economic efficiency, and in its report on the consultation it stated that most respondents endorsed this objective. Indeed, the Government itself has said that mergers and other agreements will be permitted if they result in economic efficiencies which outweigh any harm to competition. We are surprised therefore to note that there is no reference to economic efficiency in the objects clause of the Bill. This needs to be amended to make it consistent with the Government's policy objective, and the text of the Bill itself. We suggest that the object be amended to read 'to promote economic efficiency, where appropriate through prohibiting conduct and mergers which substantially lessen competition…'. It is very important that the objective is set out clearly in the objects clause, since this will affect how the conduct rules are drafted, and ultimately interpreted by the Commission and the courts.

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<u>First Conduct Rule: the Need to Distinguish Offensive Arrangements from Beneficial Arrangements in Framing the Prohibition</u>

In designing a new law, we believe that a clear distinction needs to be made between arrangements which almost always restrict competition substantially and rarely have redeeming economic benefits – namely price-fixing, market-sharing and bid-rigging – and those whose effects on competition may be more arguable, and which may have overall economic efficiencies which exceed any harm to competition. One example of the latter is arrangements between competing telecommunications operators to share their network infrastructure – the European Commission has permitted several such arrangements under competition law. This is because they generate efficiencies which outweigh any harm to competition at the wholesale level, while keeping competition at the retail level intact. These arrangements are of a fundamentally different nature from arrangement between competitors to fix prices, share markets, or rig bids.

However, we note that, in framing the First Conduct Rule, the Government has not made this distinction: *all* arrangements between businesses are assessed according to whether they 'prevent, restrict or distort' competition. This concept is derived from EU law, and has been interpreted very broadly by the European Courts to cover virtually any constraint on an operator's freedom of movement in the market place – including beneficial network-sharing agreements of the type discussed above. Indeed, one of the examples set out in the Bill – 'limit or **control** production, markets, **technical development or investment**' (emphasis added)– could cover such arrangements.

We appreciate that the Government may have designed the exclusion for 'agreements enhancing overall economic efficiencies' (Schedule 1, paragraph 1) with these sorts of arrangements in mind. However, we do not believe this is a satisfactory solution for a number of reasons:

1. We believe it is wrong to classify these kinds of arrangements alongside price-fixing cartels as prohibited in principle, albeit subject to possible exclusion under Schedule 1 on grounds of economic efficiency. This is particularly the case since the parties to such beneficial arrangements would inevitably carry the burden of proof in demonstrating, if challenged, that the criteria for exclusion were satisfied, which is not an easy task.

2. It is not clear what sort of analysis will justify the application of the exclusion. The Government said in its brief to Legco of 28 June 2010 that the rules would not apply to any merger <u>or other agreement</u> 'which enhances or would be likely to enhance economic efficiency'. The Merger Rule states that a merger will be permitted if 'the economic efficiencies that arise or may arise from the merger outweigh the adverse effects caused by the lessening of competition in Hong Kong' (Schedule 7 Part 4 paragraph 8(1)). However, the economic efficiency exclusion for other agreements is framed in entirely different terms, requiring three separate criteria to be satisfied (Schedule 1 paragraph 1). It is not clear what the reason for this difference is. The Explanatory Memorandum does not explain this (nor does it explain why the competition test 'substantially lessening competition' used for mergers is not used for other agreements). It seems from the Government's stated policy that the economic exclusion test used for mergers should also apply to other agreements.

3. However, in any event, we think it is wrong in principle, and inconsistent with the rule of law, that legal liability should depend on the results of such economic balancing exercises. Businesses are not equipped to conduct such assessments, even with legal advice, and even economists may reach different views on such matters. In addition, the requirement to engage specialist lawyers and economists unnecessarily raises compliance costs.

4. While the Bill provides for the possibility for businesses to apply the Commission for a decision as to whether the exclusion applies, this is not an adequate solution to the problem, we do not believe this is a workable solution because:

(a) The wide nature of the prohibition, combined with the uncertainty as to whether the exclusion applies, means parties to a large number of commercial arrangements would feel reluctant to proceed in the absence of official approval from the Commission. This would have a chilling effect on Hong Kong commerce, and even the Hong Kong economy, which would be exactly the opposite of the Government's objective of promoting competition. Businesses (as well as individuals) in Hong Kong should generally be able to carry on their affairs freely on the assumption that what they are doing is lawful, unless the law itself clearly states otherwise. Administrative approval should be the exception rather than the rule.

(b) In any event, even if such an approval system existed, the same factors would mean that the Commission would be over-burdened with applications, and would only be able to deal with a small fraction of the applications submitted. Indeed, the Bill itself strictly restricts the circumstances in which the Commission is obliged to make a decision on applications, perhaps in order to stem the potential tide of applications (see Clause 9(2)). This means that parties to a large number of potential transactions will be left without guidance. (This was the experience in the EU, where such applications have now been abolished).

(c) Even if a decision from the Commission can be obtained, it is not binding on the Tribunal, and so is of limited reliability.

We note that Canada has recently addressed this problem by removing from the prohibition all agreements except the 'hardcore' ones (price-fixing, market-sharing, bid-rigging). Businesses are therefore free to proceed with their commercial arrangements in the safe knowledge that they are acting legally. If at some stage in the future any such agreement causes harm to competition which is not outweighed by its economic efficiencies, the Commission can intervene, and if no voluntary settlement is achieved, can ultimately apply to the Tribunal for a cease and desist order. We believe that this solution is much fairer and more consistent with the rule of law in Hong

Kong. It also makes more sense from the point of view of economic efficiency, which the Government has said is the objective of the competition law. The Canadian Competition Bureau has explained the rationale for this amendment as follows:

"Canadian firms face increasing pressure to adopt flexible business strategies to remain competitive in an economy that is continually changing due to globalization, technological innovation and advancements in production processes. Strategic alliances can permit Canadian firms to capture the benefits of rapid technological changes and dynamic competitive conditions. They can permit firms to combine capabilities and resources so as to lower the costs of production, enhance product quality, and reduce the time required to bring new products to market. Such pro-competitive collaborations, even when they involve competitors, can often benefit Canadians by allowing firms to make more efficient use of resources and accelerate the pace of innovation".[1]

We believe this reasoning should also apply in Hong Kong, and is entirely consistent with the Government's position that the primary objective of the law should be to promote economic efficiency.

<u>Merger Control in the Telecommunications Sector should be withdrawn</u>

We note that the Government's stated policy is not to introduce cross-sector merger control, at least in the early years of the new law being in effect. We have seen no proper explanation as to why the Government believes that merger control is appropriate for the telecommunications sector but not for other sectors. In order to remove this anomalous, and indeed discriminatory, situation, we recommend that, pending a Government decision to introduce merger control across all sectors (a) the Merger Rule should be withdrawn from the Bill, or at least provision made that it shall not take effect in respect of <u>any</u> mergers until a commencement date is set by the Chief Executive in Council, a date which is later than that on which the other parts of the Bill take effect and (b) section 7P of the Telecommunications Ordinance, under which mergers in the telecommunications sector are currently regulated, should be revoked.

[1] Canada Competition Bureau, 'Competitor Collaboration Guidelines', December 2009 (preface).

<u>The new proposed section 7Q of the Telecommunications Ordinance (see Schedule 8 of the Bill) should be withdrawn</u>

We were very surprised to note that the Government is proposing to insert a major new provision into the Competition Provisions of the Telecommunications Ordinance, without any prior consultation with telecommunications operators or the public generally. In any event this proposal is flawed, and should be withdrawn, for the following reasons:

1. It is generally accepted nowadays by competition experts that such rules on 'exploitative abuse' are not appropriate in competition laws, because these laws should be addressed at protecting the competitive process.[2]

2. The difficulties of assessing what is 'exploitative conduct' (such as 'excessive pricing) are widely-recognised. These difficulties mainly arise from the fact that there are no reliable objective benchmarks against which to measure these matters, so that decisions are inevitably subjective. Although EU competition law has such provisions, they have become effectively a 'dead letter' in terms of enforcement for these reasons. The EU Commission's enforcement policy focuses on anti-competitive abuses, not exploitative abuses.

3. For these reasons, the Government has correctly (like Singapore) restricted the Second Conduct Rule to anti-competitive abuses. It is therefore anomalous (and indeed discriminatory) to subject the telecommunications operators to additional provisions on exploitative abuse. In any event, the telecommunications regime already provides sufficient safeguards against conduct which is regarded as unfair to consumers, as well as for the ability of the Telecommunications Authority to impose price controls. The proposed Section 7Q should therefore be withdrawn.

[2] The arguments against prohibition of abuse are set out in R.Whish Competition Law, 6th ed 2009, 709-711.

## Concurrent jurisdiction

The terms of the memorandum of understanding pursuant to which, the Telecommunications Authority and the Competition Commission will share concurrent jurisdiction over telecommunication licensee will have to be make available for public consultation in order to ensure that there is the necessary degree of transparency of how competition investigations in the telecommunications sector are to be coordinated and carried out.

## The proposed penalties are grossly excessive

The proposed penalty cap of 10% of consolidated worldwide turnover for each year of the infringement is grossly excessive, compared not just to the existing penalties under the Telecommunications Ordinance, but also other cross-sector competition regimes such as the EU. The cap should be at most 10% of turnover in the relevant service or product market in Hong Kong, since the law would only address conduct which has effects in Hong Kong.