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**Subcommittee on Four Subsidiary Legislation Related to Competition
Ordinance Gazetted on 18 February 2015**

**Background brief for
Meeting on 16 March 2015**

Purpose

This paper summarizes some of the major concerns raised by Members on the four pieces of subsidiary legislation related to the Competition Ordinance (Cap. 619) Gazetted on 18 February 2015.

Background

2. Cap. 619 was passed by the Legislative Council ("LegCo") on 14 June 2012 and published in the Gazette on 22 June 2012. The objective of Cap. 619 is to prohibit and deter undertakings¹ in all sectors from adopting abusive or other anti-competitive conduct which has the object or effect of preventing, restricting and distorting competition in Hong Kong. Cap. 619 provides for general prohibitions in three major areas of anti-competitive conduct (described as the first conduct rule², the second conduct rule³ and the merger rule⁴, which

¹ "Undertaking" is defined under section 2(1) of Cap. 619 to mean "any entity, regardless of its legal status or the way in which it is financed, engaged in economic activity, and includes a natural person engaged in economic activity".

² The first conduct rule under section 6 prohibits undertakings from making or giving effect to arrangements or decisions or engaging in concerted practices that have as their object or effect the prevention, restriction or distortion of competition in Hong Kong.

³ The second conduct rule under section 21 prohibits undertakings that have a substantial degree of market power in a market from engaging in conduct that has as its object or effect the prevention, restriction or distortion of competition in Hong Kong.

⁴ The merger rule under section 3 of Schedule 7 prohibits mergers that have or are likely to have the effect of substantially lessening competition in Hong Kong. This rule only applies to mergers involving undertakings directly or indirectly holding carrier licences issued under the Telecommunications Ordinance (Cap. 106).

are collectively known as the "Competition Rules" in Cap. 619) as well as the institutional arrangements and penalty provisions for their enforcement.

3. The Administration implements Cap. 619 in phases after its enactment to allow sufficient time for setting up the Competition Commission ("the Commission") and the Competition Tribunal ("the Tribunal") and preparing the guidelines⁵ ("the Guidelines") before the Competition Rules come into force. The provisions relating to the establishment and operation of the Commission and the Tribunal had come into force in January and August 2013 respectively. According to the Administration, such arrangements would enable the public and the business sector to familiarize themselves with the new legal requirements during the transitional period and make the necessary adjustments to their business practices.

4. The rest of Cap. 619 including the Competition Rules and the relevant penalty provisions will come into operation only when all the relevant preparatory work has been completed. Such preparatory work includes the issue of the Guidelines⁶ by the Commission (which are not subsidiary legislation) regarding the Competition Rules, block exemption orders, lodging of complaints as well as investigations, and the making of rules by the Chief Judge of the High Court regulating and prescribing the practice and procedure to be followed in the Tribunal.⁷

The Subsidiary Legislation

5. Four pieces of subsidiary legislation were gazetted and tabled at LegCo on 18 and 25 February 2015 respectively.

⁵ Under sections 35(1) of Cap. 619, the Commission must issue guidelines: (a) indicating the manner in which it expects to interpret and give effect to the conduct rules; (b) regarding the manner and form in which it will receive applications for a decision or block exemption order; and (c) indicating how it expects to exercise its power to make a decision or grant block exemptions. Under section 35(8), guidelines issued under section 35 and amendments made to them are not subsidiary legislation.

⁶ Under sections 35(4) and 59(3) of and section 17(4) of Schedule 7 to Cap. 619, before issuing any guidelines or amendments to them, the Commission must consult LegCo and any persons the Commission considers appropriate. At the meeting on 24 November 2014, the Panel on Economic Development was briefed on the preparation and consultation of the draft Guidelines. Members may wish to refer to LC Paper No. CB(4)370/14-15 for the minutes of the meeting for further information.

⁷ Under section 158(1) of Cap. 619, the Chief Judge of the High Court may, after consulting the President of the Tribunal, make rules regulating and prescribing the practice and procedure to be followed in the Tribunal. At the meeting on 16 February 2015, the Panel on Administration of Justice and Legal Services was consulted on four sets of draft rules. Members may refer to LC Paper No. CB(4)493/14-15(03) for further details.

Competition (Application of Provisions) Regulation

6. Section 3(1) of Cap. 619 provides that the provisions referred to in section 3(1) ("the Key Provisions") do not apply to a statutory body⁸. The Key Provisions are Part 2 (The conduct rules), Part 4 (Enforcement powers of Commission), Part 6 (Enforcement before Tribunal) and Schedule 7 (Mergers).

7. Activities of many statutory bodies are considered non-economic and regulatory in nature or involve provision of essential public services. To ensure efficient implementation of public policies as well as measures which are required to respond swiftly to the needs of the community, Cap. 619 provides for the exemption arrangements for statutory bodies, specified persons and persons engaged in specified activities. On this basis, 575 statutory bodies are exempted in their entirety. Among them, 415 do not engage in economic activities or have insignificant amount of economic activities. Most of them are advisory, regulatory, adjudicative/quasi-judicial/appellate or administrative/governing bodies. The remaining 160 are statutory bodies engaging in economic activities that are directly related to the provision of essential public services or the implementation of Government policy in such areas as education, healthcare, social welfare, public housing and trade promotion.

8. Section 5(1)(a) of Cap. 619 provides that the Chief Executive in Council ("CE-in-Council") may, by regulation, apply the Key Provisions to (i) any statutory body; or (ii) any statutory body, to the extent that it is engaged in an activity specified in the regulation only if he or she is satisfied that all of the four criteria set out in section 5(2) of Cap. 619 are met. The criteria are –

- (a) the statutory body is engaging in an economic activity in direct competition with another undertaking;
- (b) the economic activity of the statutory body is affecting the economic efficiency of a specific market;
- (c) 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
- (d) there are no other exceptional and compelling reasons of public policy against making such a regulation.

⁸ "Statutory body" is defined in section 2(1) of Cap. 619 to mean "a body of persons, corporate or unincorporate, established or constituted by or under an Ordinance or appointed under an Ordinance, but does not include (a) a company; (b) a corporation of trustees incorporated under the Registered Trustees Incorporation Ordinance (Cap. 306); (c) a society registered under the Societies Ordinance (Cap.151); (d) a co-operative society registered under the Co-operative Societies Ordinance (Cap. 33); or (e) a trade union registered under the Trade Unions Ordinance (Cap. 332)".

9. The Competition (Application of Provisions) Regulation ("C(AP)R") is made to apply the Key Provisions to the following six statutory bodies –

- (a) Ocean Park Corporation (established under the Ocean Park Corporation Ordinance (Cap. 388));
- (b) Federation of Hong Kong Industries (established under the Federation of Hong Kong Industries Ordinance (Cap. 321));
- (c) The general committee of the Federation of Hong Kong Industries (established under the Federation of Hong Kong Industries Ordinance (Cap. 321));
- (d) Matilda and War Memorial Hospital (incorporated under the Matilda and War Memorial Hospital Ordinance (Cap. 1035));
- (e) Kadoorie Farm and Botanic Garden Corporation (established under the Kadoorie Farm and Botanic Garden Corporation Ordinance (Cap. 1156)); and
- (f) The Helena May (incorporated under The Helena May Incorporation Ordinance (Cap. 1021)).

Competition (Disapplication of Provisions) Regulation

10. Section 5(1)(b) of Cap. 619 provides that the CE-in-Council may, by regulation, disapply the Key Provisions to (i) any person, or (ii) any person, to the extent that the person is engaged in an activity specified in the regulation.

11. The Competition (Disapplication of Provisions) Regulation ("C(DP)R") is made to disapply the Key Provisions to the following seven non-statutory bodies, which are all market or platform operators regulated under the Securities and Futures Ordinance (Cap. 571) –

- (a) recognized exchange companies ("RECs"):
 - (i) The Stock Exchange of Hong Kong Limited ("SEHK") and
 - (ii) Hong Kong Futures Exchange Limited ("HKFE").
- (b) recognized clearing houses ("RCHs"):
 - (i) Hong Kong Securities Clearing Company Limited;
 - (ii) HKFE Clearing Corporation Limited;
 - (iii) The SEHK Options Clearing House Limited; and
 - (iv) OTC Clearing Hong Kong Limited.

- (c) recognized exchange controller ("RXC"):
 - (i) Hong Kong Exchanges and Clearing Limited.

12. According to paragraphs 7 to 10 of the Legislative Council Brief on C(AP)R and C(DP)R (File Ref: CITB CR 05/62/25/14), the above non-statutory bodies are regulated under Cap. 571 which provides a specially calibrated regime for regulating them. As they play a key role in maintaining Hong Kong's position as an international financial centre, the Administration is satisfied that they should continue to be regulated under the framework of Cap. 571. According to the Administration, this will prevent any regulatory ambiguity that might otherwise arise as a result of their activities being subject to regulation under both Cap. 571 and Cap. 619.

Competition (Turnover) Regulation

13. The Competition (Turnover) Regulation ("C(T)R") is made by the Secretary for Commerce and Economic Development ("SCED") under section 163 of Cap. 619 to provide for the determination of the turnover of an undertaking.

14. Turnover of an undertaking over a turnover period is the measurement of eligibility for the exclusions of "agreements of lesser significance" and "conduct of lesser significance" under sections 5 and 6 of Schedule 1 to Cap. 619. Section 5 of Schedule 1 provides that the first conduct rule does not apply to an agreement or a concerted practice between undertakings which does not involve serious anti-competitive conduct if their combined turnover for the relevant turnover period does not exceed \$200 million⁹. Section 6 of Schedule 1 provides that the second conduct rule does not apply to conduct of an undertaking the turnover of which does not exceed \$40 million for the relevant turnover period.

15. Turnover is also the measurement for determining the cap on pecuniary penalties under section 93 of Cap. 619. The maximum amount of pecuniary penalty imposed in relation to conduct that constitutes a single contravention may not exceed in total 10% of the turnover obtained in Hong Kong by the undertaking concerned for each year in which the contravention occurred for up to three years.

16. C(T)R specifies how turnover is to be determined, what the turnover period would be under specific circumstances set out in sections 5(4) and 6(3) of Schedule 1 to Cap. 619, and other related issues such as the determination of turnover of undertakings that consist of two or more undertakings and each prepares accounts, and undertakings that receive any sum from a public body by

⁹ If a decision of an association of undertakings is involved, the relevant criteria are that the total gross revenues of all the members of the association for the relevant turnover period do not exceed \$200 million.

way of grant, subsidy or similar financial assistance. The said regulation will come into operation on 17 April 2015.

Competition Ordinance (Commencement) Notice 2015

17. The Competition Ordinance (Commencement) Notice 2015 ("the Notice") is made by SCED under section 1(2) of Cap. 619 to provide for the commencement of the empowering and related provisions relating to the making of C(AP)R and C(DP)R (i.e. section 3 (Application to statutory bodies), section 4 (Application to specified persons and persons engaged in specified activities) and section 5 (Regulations) of Cap. 619) on 17 April 2015.

Views and concerns expressed by Members

18. The Bills Committee on Competition Bill ("the Bills Committee) held a total of 38 meetings between 2010 and 2012 during which members expressed concerns on the three regulations. The Panel on Economic Development ("the Panel") was briefed on the subsidiary legislation except the Notice at the meeting on 24 November 2014. Members' views, including a LegCo question raised at a Council meeting, are summarized in ensuing paragraphs.

Competition (Application of Provisions) Regulation

19. Some of the Bills Committee members expressed concern about exempting nearly all statutory bodies from the Competition Bill ("the Bill") and considered that such a broad exemption was unfair to the private sector. They urged that the list of exempted bodies should be reviewed after implementation of Cap. 619 for a certain period of time. The Administration advised that the majority of statutory bodies in Hong Kong did not engage in economic activities or engaged in economic activities that had insignificant effect on the market or the economic activities were directly related to the provision of an essential public service/implementation of public policy.

20. Views of the Bills Committee members on exemption of the Hong Kong Trade Development Council ("TDC") from the Bill varied. Those indicating support considered that if TDC was made subject to the Bill, its performance of the role of promoting trade for Hong Kong and providing essential non-profit making trade services to small and medium enterprises ("SMEs") might be hampered. Members who did not support opined that while TDC's conduct relating to the discharge of its statutory functions could be exempted, its profit-making economic activities should be subject to regulation of the Bill. In response, the Administration advised that the proposed exemption would help eliminate any uncertainties in organizing trade promotion activities that might be alleged as anti-competitive to ensure TDC's uninterrupted support to local

industries and SMEs. Despite the exemption, TDC would be requested to adhere to the competition principles and to rectify any of its anti-competitive behaviour.

21. At the Council meeting on 9 April 2014, a Member raised a question on the implementation of Cap. 619 enquiring, among others, whether the Commission would monitor any anti-competitive phenomenon caused by the economic activities of exempted statutory bodies, so as to ensure that these bodies did not abuse the exemption arrangement. In reply, the Administration advised that the statutory bodies exempted from Cap. 619 should adhere to the Competition Rules despite that they did not come under the regulatory preview of the Commission. The Government would seek to ensure that unless there were justifiable causes, the exempted statutory bodies would not engage in anti-competitive activities.

22. Some Panel members enquired about the circumstance under which the Administration would consider applying the Key Provisions of Cap. 619 to statutory bodies to which they did not originally apply. The Administration advised that according to a comprehensive review of all statutory bodies amounting over 500 in total, it was concluded that the Key Provisions should only apply to the six statutory bodies stated in C(AP)R. The Panel also noted that these bodies were included because they satisfied the four criteria set out in section 5(2) of Cap. 619 (please see paragraph 8 above). In this connection, members noted the objection of the Federation of Hong Kong Industries ("FHKI") as well as its general committee to being included in C(AP)R because both of them considered themselves not meeting all the four criteria. The Administration advised that after reviewing the grounds put forth by FHKI, it still considered that the conditions for applying the Key Provisions to FHKI and its general committee continue to be valid. In particular, the facilitation, training and counselling services provided by FHKI to the trade were trade facilitation services but not the "essential public service" as stipulated in section 5(2)(c) of Cap. 619.

23. Some Panel members pointed out that in case a private company collaborated with a statutory body in carrying out certain activities which were considered contrary to Cap. 619, the private company might be liable to penalty but the statutory body concerned would be immune. The Administration advised that statutory bodies should adhere to the competition principle and rectify any of its anti-competitive behaviour despite that the Key Provisions of Cap. 619 did not apply to them. The Competition Policy Advisory Group ("COMPAG")¹⁰, chaired by the Financial Secretary, was responsible for investigating into competition-related complaints relating to those parties not

¹⁰ The weblink to COMPAG's annual reports is <http://www.compag.gov.hk>.

subject to the Key Provisions of Cap. 619, including those made against the statutory bodies.

Competition (Disapplication of Provisions)

24. During the scrutiny of the Bill, some members suggested that the criterion for granting exemption on public policy grounds (i.e. exceptional and compelling reasons of public policy) should also apply and be incorporated into proposed section 5(1)(b) as a criterion for the CE-in-Council in exercising the power to exempt non-statutory bodies.

25. The Administration advised that unlike statutory bodies where their services or activities were usually regulated by the ordinances by or under which they were established or constituted, the types and functions of non-statutory bodies as well as the nature of their activities could vary widely. As it would not be practicable to provide a common set of general criteria in the provision for determining exemption, in particular given the vast number of non-statutory bodies in Hong Kong, the Administration considered that proposed section 5(1)(b) provided the necessary flexibility for catering for unforeseen circumstances under which non-statutory bodies might warrant exemption.

26. Noting the legislative proposal on disapplication of the Key Provisions of Cap. 619 to the seven non-statutory bodies regulated under Cap. 571, some Panel members considered it necessary to tighten the regulation and control of these bodies through Cap. 571 to ensure that they would not abuse their dominant market power. Some other members even considered it unnecessary to make C(DP)R as the seven bodies were required to comply with the requirements of Cap. 571 which had already incorporated the competition principle. In response, the Administration advised that the Securities and Futures Commission ("SFC") would continue its enhanced communication with the Commission in order to strengthen monitoring of the fulfilment of requirements concerning competition under Cap. 571. As regards strengthening the competition principle under Cap. 571, the Administration referred to its sections 5 and 6 of which had been made in line with the competition principle.

27. Noting that C(DP)R was made on the basis of public interest, some Panel members enquired about the relevant considerations. According to the Administration, it made C(DP)R for the seven bodies because they played important roles in developing and maintaining a safe and efficient financial infrastructure in Hong Kong. Consideration had also been given to the long term development of the financial market as well as the overall economy of Hong Kong.

28. Noting that the Hong Kong Monetary Authority and SFC had signed a memorandum of understanding ("MOU") to set out their respective roles in regulating the sale process for securities and futures products offered by banks and non-bank intermediaries, a member enquired if the Commission and SFC would also sign a MOU with a view to authorizing SFC to enforce Cap. 619. The Administration clarified that SFC did not have jurisdiction under Cap. 619 and it regulated the competition aspect of RECs, RCHs and RXC under Cap. 571. A MOU between SFC and the Commission for SFC to enforce Cap. 619 therefore would not be necessary.

Competition (Turnover) Regulation

29. Addressing the view of the Bills Committee members that it was necessary to clarify the turnover calculation for newly established undertakings, the Administration advised that their turnover (e.g. those established in the current calendar year or those without a financial year of 12 months ended in the preceding calendar year) should be specified by way of subsidiary legislation to be made by SCED.

30. In reply to Panel members' enquiries, the Administration advised that the thresholds of turnover under C(T)R were determined based on the statistics of average turnovers of SMEs reported by the Census and Statistics Department, and such thresholds would be reviewed from time to time.

31. In respect of members' concern on the ways to tackle the situation where an undertaking entered into an agreement through its shell companies or virtual companies with very low turnovers but the conduct of the undertaking breached Cap. 619, the Administration advised that the Commission would consider the undertaking(s) (i.e. the parent company and/or its subsidiaries) actually involved in the suspected illegal acts based on the facts of each case. Similarly, when determining the penalty level of a convicted case, it might vary on a case-by-case basis depending on the involvement of the parent company and/or its subsidiaries in question.

Latest position

32. At the meeting of the House Committee held on 27 February 2015, Members agreed that a subcommittee should be formed to study the four pieces of subsidiary legislation in details.

Relevant papers

33. A list of relevant papers is given below –

<http://www.legco.gov.hk/yr09-10/english/bc/bc12/reports/bc120530cb1-1919-e.pdf>

<http://www.legco.gov.hk/yr14-15/english/panels/edev/papers/edev20141124cb4-166-4-e.pdf>

<http://www.legco.gov.hk/yr14-15/english/panels/edev/minutes/edev20141124.pdf>

http://www.legco.gov.hk/yr14-15/english/subleg/brief/36_37_brf.pdf

http://www.legco.gov.hk/yr14-15/english/subleg/brief/38_39_brf.pdf

<http://www.legco.gov.hk/yr14-15/english/hc/papers/hc20150227ls-41-e.pdf>

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