A public discussion document on the way forward for competition policy in Hong Kong

Promoting Competition - Maintaining our Economic Drive

Table of Contents

Table of Contents

Printed by the Government Logistics Department

Introduction

Competition serves Hong Kong well. It drives our economy by providing opportunities for entrepreneurs to enter and trade freely in markets. It encourages businesses to provide good quality products and services at prices that are attractive to consumers. It also enhances the choices available to consumers, and promotes innovation and creativity, thereby helping to make Hong Kong competitive vis-à-vis other economies.

Our competition policy emphasises the need for competition in order to enhance economic efficiency and the free flow of trade, thereby also providing benefits to consumers. It also stresses that we discourage anti-competitive conduct, such as price-fixing or abuses by companies enjoying a dominant position in the market.

Given the importance of free and fair competition to Hong Kong's economy, the Government considers that high priority should be given to ensuring that our competition policy keeps pace with the times and continues both to serve the public interest and to facilitate a business-friendly environment.

In the interests of maintaining a high level of efficiency in our economy and promoting market discipline, we consider that this is an opportune time for us to re-examine how best to safeguard competition in Hong Kong. In so doing, we must take care that our response to any perceived weakness in the current arrangements strikes an appropriate balance between allowing the free play of market forces and putting in place the level of regulation necessary to ensure that fair competition can thrive in our city. Important questions that the community as a whole will need to take a view on include whether the time is ripe for the introduction of a cross-sector competition law, and how we can assure our business community, particularly our small and medium enterprises, that this will not impose on them onerous compliance costs.

This document sets out the main areas for consideration when determining the direction for Hong Kong's competition policy, and seeks your views on a number of key questions. I hope that you will take time to read this document and provide us with your input, so that we can ensure that Hong Kong has an effective competition policy that will help safeguard our continued economic development.

Henry Tang, Financial Secretary

Chapter 1
Competition and the Hong Kong Approach

This Chapter looks at how we might define competition and assess its benefits, and summarises developments in Hong Kong's competition policy over the past decade. In later chapters of this document we will look at how other economies tackle the issue of competition, and we will set out the various considerations that we might take into account when charting a course for Hong Kong's future competition policy.

Defining Competition and Assessing its Benefits

The Nature of Competition

2. In a paper[1] published in 1998, the World Bank and the Organisation for Economic Cooperation and Development (OECD) defined competition in market-based economies as follows –

> *"a situation in which firms or sellers independently strive for buyers' patronage in order to achieve a particular business objective, for example, profits, sales or market share."*

3. The paper further noted that competition: "forces firms to become efficient and to offer a greater choice of products and services at lower prices." The presence of competition in a market is beneficial for the economy as a whole, as it can help maximise efficiency in the allocation of resources, provide for a clear indication of market preferences and maintain costs at viable levels whilst providing a range of choices.

1 *"A Framework for the Design and Implementation of Competition Law and Policy": World Bank and OECD, November 1998*

"The Key to Hong Kong's Economic Success"

4. Between 1993 and 1996, the Government commissioned the Consumer Council to undertake a series of studies on competition in Hong Kong. In its final report, entitled "Competition Policy: The Key to Hong Kong's Economic Success"[2], the Council observed that the benefits of competition in any given market could be expressed in the following terms –

> *"when there are many firms with freedom of entry and exit, market forces will result in productive and allocative efficiency."*

5. The report also noted that in practice competition was not a perfect state, but that markets operate in an environment of what might be termed "workable competition". In such an environment, competition depends on factors such as ease of market entry and exit, availability of sources of supply and outlets for distribution, and access to information, expertise and financial resources – and does not necessarily depend on the number of participants in the market.

6. In 1997, in its response[3] to the Consumer Council report, the Government acknowledged that the presence of only a few firms in a given market does not necessarily mean that there is inadequate competition. The government response suggested that a more important indicator of competition is the *contestability* of a market – in particular, whether the behaviour of firms in the market restricts market access, thereby leading to an inefficient economic performance (in terms of, for example, allocation of resources, technological progress and the stability of the market).

Measuring the Benefits

7. Although competition is accepted as having a positive impact on markets, it is not always easy to demonstrate this impact in concrete terms. However, it is possible to compare the range and cost of products available in a market before and after a process of "opening up" of the market to competition, as a possible indicator of the effects of enhanced competition in the market.

8. One example of such "opening up" is the deregulation processes in many economies which have often led to increased competition in the supply of products and services. The result has generally been significantly lower costs and greater ranges of products and services for businesses and consumers, as well as rapid innovation in the

2 Consumer Council, November 1996
3 "Competition Policy for Hong Kong": Trade and Industry Bureau, November 1997

development of technology. According to a research report by the Brookings Institute in 2003, prices in many industries including air transport, rail and road cargo transport, natural gas and long distance telephone services, in the United States of America fell substantially following deregulation. Although additional costs to the community may be incurred in developing and maintaining an effective regulatory mechanism to safeguard competition, such costs can be more than mitigated by the overall benefits to consumers of a free and competitive market.

9. In Hong Kong, competition has also brought substantial benefits to the economy. In the telecommunications sector, deregulation has resulted in a significant fall in telephone call charges, and a substantial increase in telephone call volume and fixed asset investment. There have also been huge gains in technological innovation and management efficiency. Improved telecommunications services have promoted the use of information technology in a wide range of sectors in their bid to improve efficiency, thereby also helping Hong Kong maintain its international competitiveness. In the banking sector, the phasing out of rules on bank interest rates in 2001 created competition that has led to greater choice for businesses and consumers when considering their options for depositing their savings. At the same time it has prompted innovation in the banking sector itself, both in terms of products and services offered to customers, and in the application of technology and management practices.

Promoting Competition

10. Competition benefits businesses and consumers and can help ensure the efficient allocation of resources within the economy. In the right market environment – which does not necessarily depend on the number of participants in the market – both the suppliers of products and services and the people and the firms who buy these products and services can enjoy the benefits of competition. Recognising that competition is good for the economy, for business and for the wider community, the Government has adopted a policy aimed at promoting competition in all sectors. The following paragraphs outline the way in which government policy has developed in recent years.

Development of Competition Policy in Hong Kong

11. As noted earlier, in the mid-1990s, the Government commissioned the Consumer Council to undertake a number of studies on various aspects of competition in Hong Kong, and in 1997 published its own response to the Council's recommendations.

Policy Objectives

12. In its response to the Consumer Council, the Government described the ultimate objective of competition policy as: "to promote economic efficiency or the best use of resources from the society's perspective." In stating this objective, the Government noted that the concept of economic efficiency carried a number of dimensions, for example –

    - Increasing the output obtained from a given input;
    - Improving the allocation of resources between different uses;
    - Improving managerial or other kinds of efficiency; and
    - Improving responsiveness to changing demand and supply conditions.

13. The response document also looked at ways in which the existence of competition could be assessed, whether by market structure, market performance or the behaviour of market participants. In doing so it noted that, provided that a market was accessible and contestable[4], the presence of one dominant participant or of only a small number of firms did not necessarily indicate that there was inadequate competition.

14. Finally, the government response acknowledged that a number of other policy objectives were linked to those of competition policy, including trade, industrial and consumer protection policies. It concluded that where there were conflicting objectives, the final judgment on how to proceed would be made on the basis of what was considered to be best for the economy as a whole.

Implementation of Competition Policy

15. Having set out the policy objectives for competition, the government response outlined the steps that would be taken to implement a comprehensive policy for Hong Kong. These included the following –

    - Issuing a clear policy statement on the objectives of promoting competition and discouraging various forms of restrictive business practices;
    - Requiring all government bureaux to give due regard to the competition angle in setting new policies or reviewing existing policies;

4 In layman's term, a market is more contestable when it is easier for a new entrant to enter that market and to compete therein than is the case with another market.

- Establishing a high-level Competition Policy Advisory Group (COMPAG) under the chairmanship of the Financial Secretary to take a proactive role in vetting existing government policies and practices to ensure that they were not anti-competitive, and to review other competition policy matters; and

- Requesting the Consumer Council to continue to monitor and review trade practices in sectors prone to "unfair" trading activities.

16. The response document further noted that the Government had reviewed the arguments for and against a general competition law for Hong Kong, and had concluded that a non-legislative approach was more appropriate.

Establishment of COMPAG

17. In line with the proposals set out above, COMPAG was established in December 1997, and the Group took on the responsibility of issuing the statement on competition policy, which was published in May 1998[5]. The statement further clarified the objective of the Government's competition policy as being –

> *"to enhance economic efficiency and free flow of trade, thereby also benefiting consumer welfare."*

18. In the COMPAG Statement, the Government called on businesses voluntarily to cease or to refrain from introducing restrictive practices that impair economic efficiency or free trade, adding that it would take administrative or legal steps to remove such practices as necessary. Restrictive practices were defined in the statement as the following –

- Price-fixing;

- Bid-rigging, market allocation, sales and production quotas;

- Joint boycotts; and

- Unfair or discriminatory standards.

A fuller description of these terms, as set out in the COMPAG Statement (and illustrated by examples), is set out in paragraphs 63 to 70 below.

5 "Statement on Competition Policy": Competition Policy Advisory Group, May 1998

19. The Statement also addressed the issue of market dominance, albeit noting that even if a business had a dominant position in a market, this did not necessarily mean that the business was anti-competitive. The determining factor would be whether the business was limiting market accessibility and contestability, giving rise to economic inefficiency or obstructing free trade. Examples of behaviour that could constitute abuse of a market position were quoted as being –

    - Predatory behaviour, particularly in relation to pricing;
    - Setting retail price minimums for products or services with no ready substitutes; and
    - Conditioning the supply of specified products or services to the purchase of other specified products or services or to the acceptance of certain restrictions.

    A fuller discussion of the concept of abuse of a dominant market position is set out in paragraphs 71 and 72 below, and a wider discussion of the issue of defining what might constitute anti-competitive conduct is at paragraphs 74 to 79.

Further Development of Competition Policy – Sector Specific Approach

20. In its 1997 response to the Consumer Council, the Government concluded that there was no compelling case for a general competition law. However, in 2000 and 2001, legislative proposals were passed to specifically prohibit certain types of anti-competitive conduct and the abuse of a dominant position in the telecommunications[6] and the broadcasting[7] markets respectively.

21. The enactment of these laws was consistent with the Government's policy of legislating on competition issues on a sector by sector basis. In the specific sectors concerned, the laws reflected the need to ensure that new and existing licensees in the telecommunications and broadcasting sectors would be able to compete on a level playing-field in markets that were undergoing a process of deregulation. For other sectors of the economy, COMPAG continued to look at complaints of anti-competitive conduct and to investigate possible abuses of dominance as they arose.

6 Including sections 7K and 7L of the Telecommunications Ordinance (Chapter 106, Laws of Hong Kong)
7 Including sections 13 and 14 of the Broadcasting Ordinance (Chapter 562, ibid)

22. The provisions in the Telecommunications and Broadcasting Ordinances are still the only laws governing competition in Hong Kong - although competition related provisions have recently been written into the individual contracts for the Government Electronic Trading Services. Sector specific competition legislation has now been in place in Hong Kong for more than five years, and this has allowed for the development of legal, economic and accounting expertise in this area.

Work of the Competition Policy Review Committee

23. Having taken note of the continuing interest in the community in the issue of whether or not Hong Kong should introduce a broader competition law, in June 2005, COMPAG appointed the Competition Policy Review Committee (CPRC), with a Chairman and membership drawn almost entirely from business, academic and other non-government backgrounds, to review the effectiveness of Hong Kong's competition policy and to report to COMPAG on its findings.

24. In the course of its review, the CPRC conducted extensive research into the competition policy and legislation of other administrations and how these were implemented in practice. The committee was also able to draw first-hand on the knowledge of a number of experts from other countries, several of whom were invited to Hong Kong to brief CPRC members on their experience in dealing with competition regulation in their own respective economies.

25. The CPRC completed its review and delivered its findings and recommendations in June 2006. These were published in a report[8] that was made public in July 2006. The findings of the CPRC form the basis for the issues, options and key questions that are set out in Chapters 3 to 6 of this discussion document.

8 *"Report on the Review of Hong Kong's Competition Policy": CPRC, June 2006*

The Need for a Policy Review Now

26. The sector specific approach to enacting competition law has so far resulted in the development of a regulatory framework for competition in the broadcasting and telecommunications sectors that allows for full investigation and, where appropriate, the sanctioning of anti-competitive conduct. However, in other sectors of the economy, in the absence of supporting legislation, COMPAG has been unable to determine the extent to which complaints of anti-competitive conduct might be justified. This not only results in an unsatisfactory outcome for complainants, but can also leave a question mark against the practices of companies that have been the subject of complaints, even though these companies may not have engaged in anti-competitive conduct.

27. From a broader perspective, in order for Hong Kong to maintain our high degree of competitiveness in relation to other major cities, it is important that we show a clear commitment to high standards of market discipline, backed up where appropriate by robust regulatory frameworks. Our current competition policy is concisely articulated in the COMPAG Statement and subsequent guidelines issued in 2003. Nonetheless, with the exception of the broadcasting and telecommunications industries, there is no legal framework for the implementation of the policy.

28. Given that our current competition policy has been in place for a number of years, and in the light of experience gained in the process of legislating to regulate competition in the broadcasting and telecommunications sectors, we believe that this would be an appropriate juncture at which to review the effectiveness of the policy and, in view of the CPRC's clear recommendations, to consider critically whether a general competition law should be introduced in Hong Kong.

29. We note that although Hong Kong's free-market and pro-enterprise culture in itself provides a fair degree of safeguard for competition, competition law of a general nature has already been implemented in most advanced overseas economies. We also accept that the introduction of a cross-sector, as opposed to sector specific, competition law in Hong Kong could have the following benefits –

    a) It would allow us to implement the current competition policy more effectively by providing a legal basis for the investigation and sanctioning of anti-competitive conduct. While the guidelines issued by the COMPAG in 2003 set out the types of conduct that we regard as anti-competitive, there is currently no overall legal mechanism to support the effective enforcement of these guidelines. Collection of evidence, for example, is often difficult;

    b) It would strengthen our institutional framework for regulating competition and for its advocacy, thereby promoting market discipline in Hong Kong;

    c) It would improve the business environment and promote a level playing-field for business in Hong Kong by barring conduct that upsets the normal processes of competitive markets; and

    d) Without such a regulatory regime, in the long term there might be an adverse effect on our relative competitiveness, especially in sectors with high entry barriers.

30. Importantly, to help ensure that any new competition law would benefit the overall business environment in Hong Kong, it should be consistent with the existing policy on competition, which is to enhance economic efficiency and free flow of trade, thereby also benefiting consumers. It should also have the aim of reinforcing business and consumer confidence and enhancing our pro-market environment, and should not impose an unnecessary regulatory burden on the community.

31. The following chapter, largely drawn from the CPRC report, outlines the main features of competition regulation in a number of major economies that are familiar to Hong Kong, by virtue of being well established trading partners, and in some cases having legal systems similar to Hong Kong's.

Chapter 2
Competition Regulation in Selected Major Economies

32. Given that over 80 economies worldwide have competition laws in place, there are plenty of examples to choose from when seeking to understand how competition regulation works. This Chapter gives a brief overview of the competition law and regulatory framework in Australia, Canada, the European Union (EU), Singapore, the United Kingdom (UK) and the United States of America (USA). In particular it looks at –

- The scope of the relevant laws;
- The types of behaviour that are prohibited by the laws; and
- Other important provisions, such as exemptions.

Examples of Regulatory Provisions in Other Economies

33. A summary of the main areas covered by the laws in the jurisdictions mentioned above is shown in Table 1 below. The table indicates that competition laws in other jurisdictions have many common general elements. However, there is no single "mainstream" or "set formula" approach to the detailed provisions of the relevant legislation. Rather, the actual legal and regulatory frameworks adopted in different jurisdictions reflect their specific characteristics, such as the size of the economy, market structure and political and historical context.

Table 1: Main Areas Covered by Competition Laws

	Australia	Canada	European Union	Singapore	United Kingdom	USA
Law	Trade Practices Act 1974	1985 Competition Act	EC Treaty, Articles 81and 82	Competition Act 2004	Competition Act 1998, Enterprise Act 2002	Sherman Act, Clayton Act and Hart-Scott-Rodino Anti-trust Improvements Act
Scope	Restrictive agreements, abuse of dominance, anti-competitive mergers and acquisitions, unfair trade practices	Restrictive agreements, abuse of dominance, anti-competitive mergers and acquisitions and unfair trade practices	Restrictive agreements (Article 81), abuse of dominant market position (Article 82); separate merger provisions	Restrictive agreements, abuse of dominance and anti-competitive mergers and acquisitions	Restrictive agreements, abuse of dominance and anti-competitive mergers and acquisitions	Monopolies, unreasonable restraint of trade and anti-competitive mergers and acquisitions
Types of conduct covered	Price-fixing, sales and production quotas, joint boycotts, price discrimination, exclusive dealing, resale price maintenance	Price-fixing, predatory pricing, market allocation, group boycotts, bid-rigging, sales and production quotas	Agreements and practices that have the object or effect of restricting or distorting competition	Price-fixing, predatory behaviour, market allocation, sales and production quotas, application of discriminatory conditions	Price-fixing, bid-rigging, resale price restriction, market sharing, limiting or controlling output, application of discriminatory conditions	Monopolising or attempting to monopolise, mergers and acquisitions, price-fixing, bid-rigging
Other provisions	Amendments introduced in recent years to protect small businesses against larger players; exemptions may be granted on public policy or economic grounds	Ensuring small and medium-sized enterprises have "an equitable opportunity to participate in the economy" is one of the law's main purposes; certain public interest or economic grounds could be used as a defence	Exemptions may be granted on an individual basis or by block exemption by the European Commission	Exemptions may be granted on public policy or economic grounds	Exemptions may be granted on public policy or economic grounds	Scope of the law tends to be defined by the interpretations of the courts; the law provides for exemptions in specific circumstances

34. Although the various economies listed above have shaped their laws to suit their own particular political, economic and legal situations, there are features that appear to be commonly accepted as indispensable to an effective competition law –

- An indication of the broad scope of the conduct that is considered to be anti-competitive;
- A description of the specific types of conduct that are to be prohibited under the law; and
- Provision to be made for exemptions from the law in cases where public interest or economic grounds are paramount.

35. In considering the way forward for Hong Kong's competition policy, it is important that the actual situation of Hong Kong should be taken into account. This notwithstanding, the experience of other jurisdictions provides useful pointers. For example, in many jurisdictions, the regulation of mergers and acquisitions and the breaking up of monopolies are priority issues for the regulatory authorities. It needs to be considered whether such an approach would be suitable for Hong Kong's situation, or whether we should be more concerned with other aspects of competition regulation.

36. Furthermore, when assessing an appropriate response to conditions in Hong Kong, it is important that we acknowledge that there may be divergent views in the local community as to the most appropriate way of ensuring that our markets remain competitive.

Chapter 3
Maintaining a Competitive Environment: Considerations for Hong Kong

Introduction - Hong Kong's Economic Environment

37. Hong Kong is a free and open economy, with few restraints to trade in goods and services and foreign direct investment (FDI), and no significant entry barriers to most industries. In common with many other developed economies, a high proportion (some 98%) of local registered businesses are Small and Medium-sized Enterprises (SMEs). Companies are free to compete in terms of price, including the use of discount and loyalty schemes, and in terms of differentiated goods and services.

38. Some sectors characterised by significant economies of scale are dominated by a few big companies, with or without a large number of smaller companies at the periphery. These sectors usually involve large fixed asset investment with long payback periods. The domination of certain sectors by a small number of companies is not anti-competitive per se. In certain sectors, this is simply a result of market forces. Nonetheless, in some sectors such domination is combined with other factors, with the result that the possibility of anti-competitive behaviour exists. These factors include high market entry barriers, price inelastic demand, limited product differentiation with competition mainly on price, predictable demand and market share, and vertical integration. Nonetheless, even though the market structure might have elements that could allow for anti-competitive conduct, it does not necessarily follow that such conduct is present.

39. Hong Kong has a vibrant market in many goods and services. With enhanced public education on consumer protection and heightened awareness in the community, the public has developed a keen sense of consumer rights. In recent years, there has been increasing demand for greater consumer protection and more competition in sectors such as transport and utilities, where there are perceived to be limited opportunities for new market entrants. There have also been allegations of a lack of competition or of anti-competitive behaviour in some sectors. Bundling of services across sectors has also raised concerns.

40. The international community recognises Hong Kong's free and favourable business environment. In a peer review of Hong Kong conducted in 2005, APEC remarked that Hong Kong's market oriented and sector specific approach to competition had much merit, whilst noting that there was a need for constant surveillance and evaluation of the situation.

41. Nonetheless, some international organisations have expressed concern that there is little regulation of anti-competitive conduct in Hong Kong. The World Trade Organisation (WTO) Secretariat's report on the 2002 Trade Policy Review on Hong Kong expressed the opinion that "the seeming lack of coherent measures to address anti-competitive practices in all but a few sectors could constitute an obstacle to greater competition" – although this view was later balanced by a comment from the Chair of the WTO Trade Policy Review to the effect that it generally appreciated Hong Kong's efforts to maintain a competitive market. Earlier this year, the International Monetary Fund welcomed the establishment of the CPRC to review competition policy in Hong Kong and the possible role of a general competition law.

42. The report of the CPRC highlighted the specific characteristics of Hong Kong's economy, and concluded that competition is best nurtured and sustained by allowing the free play of market forces. It further commented that any new approach to competition policy, including legislation should serve the purpose of enhancing economic efficiency and the free flow of trade, thereby also benefiting consumer welfare. The aim should not be to benefit or to target specific sectors, nor to stimulate or introduce competition artificially. Rather, the key objectives should be to reinforce business and consumer confidence, enhance Hong Kong's pro-enterprise, pro-market environment and to provide a level playing-field for all by combating anti-competitive behaviour.

Need for a New Competition Law

Key Question 1:
Does Hong Kong need a new competition law?

43. In setting out its plans to implement the competition policy embodied in the COMPAG Statement of May 1998, the Government called upon all businesses: "to cease existing, and refrain from introducing, restrictive practices that impair economic efficiency or free trade on a voluntary basis." The COMPAG Statement continued:

"Where justified, the Government will take administrative or legal steps as appropriate to remove such practices if necessary."

44. In practice, outside of the telecommunications and broadcasting sectors, there are no statutory procedures that the Government can take to reign in businesses that are engaged in restrictive practices that might impair Hong Kong's economic efficiency. Currently, where possible cases of anti-competitive conduct are brought to the attention of COMPAG, it generally asks the government bureau responsible for the sector concerned to investigate whether such conduct has in fact taken place. However, such investigations, and by extension, the effective implementation of the competition policy are constrained by two factors, namely –

- The government bureau tasked with investigating a complaint of possible anti-competitive conduct can only request cooperation from the party under investigation – it has no statutory power to require the provision of information that might be relevant to the case; and

- Even if a complaint of anti-competitive conduct is substantiated, COMPAG has no power to sanction the party or parties concerned or to require them to desist from the restrictive practice in question.

Specific Considerations (For and against introducing a new competition law)

45. Bearing in mind the current situation in Hong Kong, in addition to the benefits set out in paragraph 29 above, arguments that might be put forward in support of introducing a competition law include –

- A new law would improve transparency through delineating what constitutes anti-competitive conduct throughout the economy, and would send a clear signal as to the standards of business conduct that we would wish to promote in Hong Kong, thereby encouraging self discipline by undertakings; and

- A new law that targets anti-competitive conduct but not the size and number of competitors would not disturb market structure, which is often the result of free play of market forces in Hong Kong.

46. Nonetheless, there are also arguments that may be advanced in support of maintaining the current framework for implementing competition policy, for example –

- Introducing a new cross-sector law could increase the cost of doing business locally, particularly for SMEs, and could affect Hong Kong's regional competitiveness;
- Hong Kong is already a free and competitive market and there is no need to interfere with normal business operations in a market place that already works well; and
- There are other ways to enhance competition in local markets without introducing a new competition law.

47. Two further points might be considered when assessing the need for new legislation, that is –

- Without a new competition law there will be a need to strengthen the current mechanisms for investigating and publicising cases of anti-competitive conduct, if we intend to take stronger steps to deter such conduct and to educate the community as to the standards of business practice that are appropriate for an advanced economy such as Hong Kong's; and
- If there is to be *a new competition law* it should not create a significant additional burden on local business, nor encourage interference with normal business practices or economically efficient market structures.

Following publication of the CPRC report, concerns were raised, especially by representatives of SMEs, that the introduction of a new law could lead to higher business costs, and that larger firms could use such a law to put pressure on small companies through unfounded complaints or legal action. However, evidence from other jurisdictions suggests that SMEs have little to fear from a carefully framed competition law.

Big and Small

When overseas jurisdictions first started passing competition laws, one of the key objectives was often to address the undue concentration of market power. The focus was therefore on the regulation of market structures and big companies.

A more recent approach to regulating competition has been to prohibit anti-competitive conduct rather than to address market structures or monopoly power. The law thus applies equally to big and small companies that engage in such conduct. In practice, given their lack of market power, the actions of SMEs are unlikely to have the effect of significantly preventing, restricting or distorting competition. It is relatively uncommon for SMEs to be prosecuted in overseas jurisdictions, unless the law provides for "per se" offences, i.e., conduct that is always assumed to cause harm to competition and to have little economic benefit. Such conduct typically includes price-fixing, bid-rigging and market allocation. Competition authorities understand that some cooperative arrangements common among SMEs, for example information sharing and joint purchasing, may actually have pro-competitive benefits when certain conditions are met. Regulation of SME conduct is not normally a priority for competition authorities.

In order to keep SMEs informed, and recognising that small companies have limited resources in handling compliance issues, it is common for overseas competition authorities to issue guidelines on the regulation of SME conduct. For example, in the USA, the Anti-trust Guidelines for Collaborations among Competitors issued jointly by the Federal Trade Commission and the US Department of Justice (DOJ) state that, other than in extraordinary circumstances, the authorities do not challenge a collaboration between competitors when the market shares of the participants and the collaboration involved collectively account for no more than 20% of each market in which competition may be affected.

There have been cases where the US DOJ concludes that a joint purchasing association established by SMEs has pro-competitive benefits through reducing costs and has no anti-competitive harm. In Singapore, the guidelines published by the Competition Commission state that 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%. The guidelines also state explicitly that agreements between SMEs are rarely capable of distorting competition appreciably, and recognise that competition may be enhanced by, for example, sharing of information on new technologies or market opportunities.

48. The remaining key considerations in this Chapter are based on the assumption that some form of new competition law is required to ensure the effective implementation of competition policy. In such deliberations, it is important to have regard to the Hong Kong context, and to ask ourselves what legal and institutional set up would best suit the circumstances of Hong Kong.

Extent of a New Competition Law: Sector Specific or Cross-Sector

Key Question 2:
Should any new competition law extend to all sectors of the economy, or should it only target a limited number of sectors, leaving the remaining sectors purely to administrative oversight?

49. Competition laws in the jurisdictions surveyed in Chapter 2 apply in principle to all sectors of the economy – although the laws do allow for exemptions in certain circumstances (see paragraphs 80 to 84 in this Chapter for a discussion of the issue of exclusions and exemptions). Under our current arrangements, the telecommunications and broadcasting sectors have legislation containing competition provisions, whilst for other sectors, complaints of anti-competitive conduct are handled on a case-by-case basis.

50. If the Government were to introduce a new competition law for Hong Kong, one of the first considerations would be whether such a law should be "cross-sector" in nature, i.e., covering all sectors of the economy, or should just target sectors where the risk of anti-competitive conduct was felt to be particularly acute.

Specific Considerations with regard to a "Cross-sector" Approach

51. There is the view that extending competition law across all sectors of the economy might adversely affect business confidence by creating uncertainty as to which industries might be targeted by the regulator. One might also argue that the current sector specific approach to legislating for competition in Hong Kong is well understood by business and consumers, and that it would be more prudent to extend this to cover only those markets where competition was felt to be an issue of concern, rather than to introduce a cross-sector law.

52. Another argument that might be made against having a cross-sector competition law is that each sector has its own characteristics that could not be satisfactorily addressed by a single, across-the-board piece of legislation. It could also be argued that a sector specific approach is consistent with the approach to date, given that the telecommunications and broadcasting industries are subject to separate competition legislation and regulatory control.

53. On the other hand, as anti-competitive conduct could occur in any sector, many commentators have pointed out that there are no strong grounds for targeting only certain individual sectors or industries for regulation. Whilst there might be a common perception that certain specific sectors are particularly vulnerable to anti-competitive behaviour, the profile of complaints to COMPAG in recent years – appended at the Attachment to this document – indicates that there is a concern that anti-competitive conduct exists in a large number of sectors. In addition, it is clear that the current policy set out in the COMPAG Statement does not discriminate between sectors, but applies equally to all.

54. Were the Government to extend competition regulation only on a sector specific basis, it would be difficult to define clearly the exact scope of the many individual market sectors in Hong Kong, and therefore to put effective regulatory mechanisms in place. In the case of the broadcasting and telecommunications industries, the sectors are clearly defined by the licensing regimes under which the relevant authorities regulate these sectors.

55. One further point in favour of making any new competition law cross-sector in nature is that under sector specific laws it could be difficult to deal with cross-sector anti-competitive conduct, an example being the "bundling" of services across different sectors. (Whilst "bundling" might not necessarily be anti-competitive per se – and indeed might even provide economic efficiency and benefits to consumers in certain cases – should such a practice be suspected to be distorting the market, there would be a case for action by the regulator.)

Scope of Behaviour to be Covered by Competition Law

Key Question 3:
Should the scope of any new competition law cover only specific types of anti-competitive conduct, or should it also include the regulation of market structures, including monopolies and mergers and acquisitions?

56. Regardless of whether any new competition law extends to all sectors of the economy or just to a limited number of sectors, there is a need to consider carefully the scope of the behaviour that such a law might cover. Legislation in other jurisdictions generally addresses the following types of conduct –

- Restrictive agreements;
- Abuse of market dominance;
- Monopolies; and
- Mergers and acquisitions.

If Hong Kong were to adopt an approach consistent with that taken in most other developed economies, provisions governing the above areas would appear in local competition law.

57. However, introducing a broad competition law would be a new approach for Hong Kong. With this in mind, the CPRC in its report on the competition policy review considered that the Government should take an incremental approach to any new legislation, so as to help build broad understanding and acceptance of new measures and to allow the law to develop gradually in response to actual circumstances. The CPRC also noted that to ensure broad consistency with the existing competition policy, the scope of any new competition legislation should focus on preventing anti-competitive conduct – rather than seek to "open up" markets to competition. The CPRC proposed that competition law should cover seven specific types of such conduct, which are described in paragraphs 62 to 72 below.

Monopolies and Mergers and Acquisitions

58. The CPRC in its report recommended against targeting market structures or seeking to regulate "natural" monopolies, proposing instead that the focus of a new competition law should be on the actual conduct of firms within the markets concerned. It also observed that in Hong Kong, there was no clear indication that merger and acquisition activity was currently a threat to competition. Whilst some commentators have pointed out that market structure is addressed by many overseas competition regimes, others suggest that a competition law for Hong Kong should not, at least at the initial stage, target monopolies, taking the view that current market structures are generally the result of normal free market forces.

59. It has also been suggested that the presence of a monopoly in a given economic sector does not necessarily reduce economic efficiency. In a relatively compact geographical area, such as Hong Kong, there may be limited business scope for multiple providers of certain products or services to co-exist, particularly those that require high levels of "sunk" investment. In such cases, the provision of products or services by one or a few companies might be the most economically efficient situation. One further consideration is that as long as there are effective safeguards against anti-competitive conduct, it might well be superfluous to devise a regime to target market structures, since an undertaking enjoying market dominance and engaging in anti-competitive conduct to protect its market position would in any event be caught under the law.

60. The submissions received by the CPRC generally indicated that there was no clear justification at this time for the regulation of mergers and acquisitions (M&A) outside the legal provisions governing ownership in the broadcasting and telecommunications sectors. Furthermore, it might be argued that at the initial stage of bringing in a new competition law, it would be preferable to focus regulatory resources on areas where there are perceived to be the greatest problems, rather than to try to cover all possible areas of the law as it applies in other jurisdictions.

61. Nonetheless, even though M&A activity might not currently pose a threat to competition in Hong Kong, there is the possibility that without regulation of M&A, companies could simply merge in order to circumvent new laws against anti-competitive cartel conduct or other prohibited practices. There may therefore be an argument for sending a signal to the business sector that anti-competitive M&A activities would not be tolerated, for example, by including in the new competition law provisions regulating M&A activities that are to come into effect not immediately upon enactment but at an appropriate time in future. Indeed, the timing for the M&A provisions to

take effect could be subject to a further review so that experience with the new law can be fully taken into account.

Types of Behaviour to be Regarded as "Anti-competitive Conduct" and the Approach to be Adopted in Defining Such Conduct

Key Question 4:
Should a new competition law define in detail the specific types of anti-competitive conduct to be covered, or should it simply set out a general prohibition against anti-competitive conduct with examples of such conduct?

Key Question 5:
Should a new competition law aim to address only the seven types of conduct identified by the CPRC, or should additional types of conduct also be included, and should the legislation be supported by the issue of guidelines by the regulatory authority?

62. In its report on the review of competition policy, the CPRC recommended that a new cross-sector competition law should address seven types of anti-competitive conduct. These are discussed in detail in the following paragraphs. The first six types of conduct (i.e., all except abuse of a dominant market position, which is usually treated as a category in its own right) are often grouped under the broad category referred to as "restrictive agreements".

Price-fixing

63. Price-fixing often refers to an agreement among competitors to raise, fix or otherwise maintain the price at which their goods or services are sold. Such an agreement may involve fixing either the price itself or the components of a price, establishing the amount or percentage by which prices are to be increased, or establishing a range outside which prices are not to move.

64. Price-fixing may also take the form of an agreement to restrict price competition. This can include, for example, an agreement to adhere to published price lists or not to quote a price without consulting potential competitors, or not to charge less than any other price in the market. An agreement may restrict price competition even if it does not entirely eliminate it.

Petrol prices in Victoria, Australia

In 2002, the Australian Competition and Consumer Commission (ACCC) instituted court proceedings against seven companies and seven individuals involved in the distribution and retail of petrol in the state of Victoria, on the grounds that these companies and individuals had entered into and given effect to arrangements to fix retail petrol prices.

Specifically, the ACCC alleged that the companies had first arranged to raise petrol prices by telephoning one another and agreeing on the amount and timing of the price rise, and had then contacted the individual petrol filling stations in the area to ask them to implement the rise. The Commission further alleged that when one of the parties to the arrangement became aware that a petrol station had not raised its price in accordance with the arrangement, further calls were made to try to have the station raise its price.

In 2004, the courts found that the parties in question were guilty of breaching the Trade Practice Act 1974. Fines of a total of A$23.3 million (approximately HK$140 million) were imposed on the guilty parties.

Bid-rigging

65. Tendering procedures are designed to promote competition between potential suppliers of products or services. Bid-rigging involves an agreement between competitors as to which of them will submit the winning bid on a contract being let through the tendering process[9].

9 *Under sections 6 and 7 of the Prevention of Bribery Ordinance (Chapter 201), certain bid-rigging activities, to the extent that they relate to public bodies, are criminal offences.*

66. Bid-rigging agreements usually fall into one or more of the following categories –

- Bid suppression: One or more competitors who otherwise would be expected to bid, or who has previously made a bid, agrees to refrain from bidding or withdraws a previously submitted bid so that the designated winning competitor's bid will be accepted.

- Complementary bidding: Some competitors agree to submit bids that are either too high to be accepted or contain terms that they know will not be acceptable to the buyers. Such bids are made merely to give the appearance of genuine competitive bidding.

- Bid rotation: Parties to the agreement submit bids but take turns at being the lowest bidder. The terms of rotation may vary; for example, competitors may take turns in bidding for contracts according to the size of the contract sum, allocate equal amounts of the contract sum to each party or allocate amounts that correspond to the size of each company involved in the agreement.

Collusive tendering for flat roof and car park surfacing contracts in England and Scotland

From 2000 to 2002, thirteen roofing contractors colluded in bidding for flat roof and car park surfacing contracts in England and Scotland.

Owners requiring the surfacing of their roofs or car parks typically invited a number of suitably qualified contractors to submit tender bids in order to ensure competition between contractors and thereby obtain a competitive price. The contractors in question cooperated and coordinated with each other in relation to the setting of tender prices with the object of preventing, restricting or distorting competition. In some cases the winning contractor paid losing contractors compensation for not bidding for the contract or for submitting a bid that they knew would be too high to win the contract.

Having been found guilty of collusion, the contractors were fined a total of around £2.3 million (approximately HK$33.5 million). In line with the policy to give lenient treatment to parties that give information with regard to cartel cases, a number of contractors were granted 25% to full immunity from these penalties.

Market Allocation

67. Companies may agree to share markets, whether on the basis of geographical area, market type, size of customer or in some other way. Such agreements may reduce or eliminate competition and may lead to consumers paying higher prices than if there was genuine competition in the market.

Wholesale distribution of magazines, other periodicals, and books in Western New York State and at Pittsburgh International Airport

In 2003, the Empire State News Corporation Inc. (Empire), of Buffalo, New York in the USA was prosecuted for allegedly –

a) participating in a conspiracy to suppress and eliminate competition in the wholesale distribution of magazines, other periodicals, and books in Western New York State from January 1999 to mid-2000; and

b) eliminating competition for the contract to supply magazines, other periodicals, and books at Pittsburgh International Airport between March 1999 and mid-2000.

Empire and another wholesale distributor agreed to allocate markets for the wholesale distribution of magazines, other periodicals, and books in Western New York State. Empire also agreed to refrain from the wholesale distribution of magazines, other periodicals, and books at Pittsburgh International Airport in exchange for another wholesale distributor agreeing not to expand its market share in Buffalo, the home territory of Empire.

Empire pleaded guilty to the charges and was fined US$200,000 (about HK$1.6 million).

Sales and Production Quotas

68. An agreement between competitors to limit production will almost inevitably lead to price increases. Such an agreement may relate to the way in which prices are fixed, or it may be intended to deal with structural overcapacity. In some cases, it may be linked to other anti-competitive agreements.

Cement cartel in the Slovak Republic

In 1991, a number of cement producers in the Slovak Republic entered into agreements restricting competition.

The producers agreed to a regular exchange of basic information about their firms on matters such as production output, costs, export volumes, inventories, profits, numbers of employees, and average wages and salaries. They reported this information monthly to a consulting firm, which consolidated the information and distributed this to the producers. The consulting firm also prepared documents establishing a geographical division of markets among the producers and suggested a production quota for each producer. These plans were first discussed by the commercial directors of the producers and then agreed to by the managing directors. As a result, customers were restricted to dealing with only one producer in their area.

In 1994, the Anti-monopoly Office issued an order prohibiting all cement producers from engaging in market allocation, setting sales quotas or exchanging information that could facilitate the coordination of such illegal agreements. The Office also imposed fines totaling about US$0.7 million (approximately HK$5.5 million) on the parties to the agreements.

Joint Boycotts

69. An agreement between competitors not to deal with other competitors, suppliers or customers is a joint boycott. Refusing to deal with customers unless they agree to pricing or other terms set by the firms participating in such an agreement may be anti-competitive. If competitors join together to pressure suppliers or customers to stop dealing with another competitor, they may also be engaging in anti-competitive conduct.

Refusal to supply entertainment services in Australia

In 2004, the ACCC instituted proceedings alleging that on three occasions an entertainment group, individual members of the group and affiliated corporations entered into an agreement, arrangement or understanding with one another not to supply services to organisers of events.

One specific allegation related to a county fair to be held in 1998, where executive members of the entertainment group directed certain other members not to supply services to the event, upon threat of suspension or expulsion from the group. It was also alleged that in relation to shows in 2002 and 2003, certain group executives arrived at an agreement, arrangement or understanding not to supply services to those shows.

The Federal Court in Sydney found that the entertainment group had breached s. 45 of the Australian Trade Practices Act and the Competition Code by attempting to induce its members to boycott the county fair in 1998.

Unfair or Discriminatory Standards

70. An agreement between companies on, for example, technical or design standards may have the positive effect of helping to reduce the cost or raise the quality of a product or service. It may also promote technical or economic efficiency by reducing waste and consumers' search costs. However, such an agreement may adversely affect competition, in particular if it includes restrictions on what the parties may produce. It may also have the effect of limiting competition from other sources, for example by raising entry barriers to a market. Agreements that prevent the parties concerned from developing alternative standards or products that do not comply with the agreed standard may also harm competition.

Accreditation of law schools in the USA

The American Bar Association (ABA) conducts the national accreditation process for law schools in the USA. The bar admission rules in most states require that a person graduate from an ABA-approved law school to satisfy the legal education requirement for taking the bar examination.

The ABA prohibited ABA-approved law schools from enroling graduates of a law school accredited by a state, but not by the ABA, in post-graduate programmes. It also prohibited law schools from offering transfer credits for any course successfully completed at a law school accredited by a state, but not by the ABA.

In 1995, the US Department of Justice (DOJ) filed a complaint against the ABA. The two parties entered into a final settlement, under which the ABA refrained from adopting any standard that had the purpose or effect of discriminating against non-ABA accredited schools.

Abuse of Dominant Position

71. A business that has a dominant position in a market can use this position to limit other firms' access to or ability to compete in the market. This type of conduct can give rise to economic inefficiency or the obstruction of free trade. In assessing whether or not the conduct of a company amounts to an abuse of dominance, competition regulators usually employ a two-stage process. First, they establish whether or not the business is indeed in a dominant position. They then assess whether the business has engaged in conduct that is abusive of that position. Such conduct usually falls into one or both of the following categories –

    - Conduct which exploits customers or suppliers (for example, by pressuring the other party into entering a contract with grossly unfair terms in favour of the dominant player); or

    - Conduct which amounts to exclusionary behaviour, because it removes or weakens competition from others in the market, or establishes or strengthens entry barriers, thereby removing or weakening potential competition.

72. The COMPAG Statement lists the following examples of abuse of a market position –

- "Predatory behaviour such as selling below cost for the purpose of driving out competition" ;
- "Setting retail price minimums for products or services where there are no ready substitutes"; and
- "Conditioning the supply of specified products or services to the purchase of other specified products or services" – also known as "bundling" or "tie-in".

Two examples of cases of abuse of dominance are given below, one of which involves the "bundling" of services.

Bread market in Melbourne, Australia

In 1996, the ACCC launched proceedings in the Federal Court in Melbourne against a large retail store, on the grounds that the company had a policy of removing products from sale when the same products were offered at discount prices at nearby smaller independent stores. The ACCC alleged that the conduct of the company involved amongst other things misuse of market power.

The specific allegations concerned the supply of bread by three bakeries to independent stores whose owners discounted the price of the bread. The ACCC alleged that the large retailer took action against each of the bakeries to induce them, or attempt to induce them, to take action to stop the discounting.

It was alleged that the large retail store refused to accept further supplies of bread from a baker who supplied independent stores that were selling the bread at a discount price. The space in the store normally occupied by the affected baker's product was filled with another product. The ACCC alleged that the large retailer again started purchasing bread from the baker concerned once the independent store stopped offering bread at a discount.

In all, pleas were taken in respect of nine similar incidents. The court found that the large retail store operator had misused its market power in four of the incidents.

"Bundling" - Gas meter installation in New Mexico, USA

El Paso Natural Gas Company ("El Paso") was a regulated monopoly which operated the largest gas pipeline system in the San Juan Basin of New Mexico and Colorado.

In 1995, the US DOJ filed a complaint in US District Court in Washington, alleging that El Paso required owners of gas wells that had little choice but to use El Paso's natural gas gathering system also to purchase El Paso's meter installation service. Meter installation was an unregulated business, consisting of the services necessary to connect a well to El Paso's gathering system, including the construction and installation of metering equipment and the line used to connect the well to the gathering system. The complaint also alleged that El Paso's practice had raised the price of each installation by thousands of dollars and slowed the pace of installation by weeks, compared with the situation where there was free competition. El Paso had used the tie-ins to evade the effect of government price control in respect of its regulated activity.

The DOJ and El Paso reached a settlement, under which gas producers in the San Juan Basin would be free to choose their own contractor to construct the well connection rather than pay El Paso for the service. The settlement also ensured that El Paso would not impose standards that gave it an unfair advantage over others who could provide connection services to well owners.

Other Types of Anti-competitive Conduct

73. Some commentators have observed that, if a new competition law were to cover only certain major types of anti-competitive conduct, simply addressing the seven types of conduct discussed above may not provide for sufficiently robust regulation. Specifically, it has been pointed out that the category "restrictive agreements" often also covers the following two types of conduct –

    - Making the conclusion of agreements subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such agreements; and

    - Applying dissimilar conditions to equivalent agreements with other trading parties, thereby placing them at a competitive disadvantage.

Defining Anti-competitive Conduct: General Prohibition or Detailed Definitions

74. Regardless of the extent of the scope of any new competition law for Hong Kong, stakeholders would need to have a clear understanding of the specific types of conduct that would be covered by such a law. Businesses, for example, might feel that a law that only sets out a broad prohibition against anti-competitive conduct could give rise to uncertainty as to how such a law might apply. Such uncertainty could, in turn, lead to constraints on innovation and expansion in the local economy in some circumstances.

75. Providing in a new law a set of detailed and explicit definitions of the types of anti-competitive conduct to be covered would help to remove such uncertainty. However, it would be unrealistic to expect that such an approach could cover all circumstances in which anti-competitive conduct might occur. Furthermore, if the legal definitions were too precise, it is highly likely that frequent legislative amendments would be required to modify these definitions as new types of anti-competitive practice became prevalent. It should be noted that, even were an exhaustive, specific listing approach to be adopted, detailed guidelines would be important in ensuring that prevailing and new market conditions could be taken into account.

76. The approach most commonly used in other jurisdictions is to set out a general prohibition against anti-competitive conduct and to supplement this with guidelines and regular commentaries, including examples of cases that have been investigated, both in local and overseas economies. The advantage of taking this approach in Hong Kong would be that it would be familiar to many in the business and professional sectors, and would also allow us to take reference to jurisprudence in this area in other administrations. As with the administrative guidelines on competition issued by the Telecommunications and Broadcasting Authorities in Hong Kong, such guidelines could also indicate how the regulatory authority proposed to perform its functions. Whilst such guidelines would not in themselves have legal effect, they could clarify the principles that would govern regulatory considerations and decisions, thereby providing some comfort to stakeholders.

77. Whether a general or specific approach to defining anti-competitive conduct is preferred, it would be premature at this stage to try to anticipate precisely how a competition regulator in Hong Kong might decide what would constitute anti-competitive conduct in a particular case. Nonetheless, we recognise that stakeholders may wish to have an early indication of the types of conduct that might be regarded

as anti-competitive. This would help also to ensure that any competition law that might be introduced in the future would adequately address the aspirations of the wider community.

"Purpose" or "Effect" - An Essential Test of Infringement?

Key Question 6:
In determining whether a particular type of anti-competitive conduct constitutes an infringement of the competition law, should the "purpose" or "effect" of the conduct in question be taken into account? Or should such conduct on its own be regarded as sufficient in determining that an infringement has taken place?

78. One further important point to consider when seeking to define anti-competitive conduct is the question of whether certain practices should be considered to be violations of competition law *per se*, that is, whether the very fact of engaging in a certain type of conduct should constitute an infringement. The alternative is that, to constitute an infringement, the conduct must not only be shown to have taken place, but must *also* be shown to have the "purpose" or "effect" of preventing, restricting or distorting competition.

79. For example, if a number of competing firms collude in fixing the price for their product at a certain level, should this automatically be an offence under the law? Or should it only be an offence if the conduct of these firms could be shown to have the purpose or effect of distorting normal market conditions? Although the latter approach might make it more difficult to prove anti-competitive conduct, it could have the advantages of –

- Ensuring that small businesses that share information for legitimate purposes would unlikely face regulatory action unless their conduct could be shown to have wider implications for the market as a whole; and

- Providing continuity with the thrust of the CPRC's proposals, which emphasise an incremental approach and the need to avoid putting an unduly onerous burden on normal business operations.

Exclusions and Exemptions

Key Question 7:
Should any new competition law allow for exclusions or exemptions from the application of some or all aspects of the law, and if so, in what circumstances should such exemptions apply?

80. As Table 1 in Chapter 2 of this document shows, in other jurisdictions, the competition law allows for exclusions or exemptions where there are public policy or economic grounds for not applying the law to certain sectors or in specific cases. For example, in Singapore, agreements that are necessary in order to avoid a conflict with the country's international obligations are excluded. In the following paragraphs, we consider how and in what circumstances exclusions and exemptions might apply if a new competition law were to be introduced in Hong Kong.

A Legal Mechanism for Exclusions or Exemptions

81. In terms of procedure, exclusions or exemptions from competition law could be made in a number of ways, for example –

- Providing within the main body of the law for certain types of firm to be excluded from the application of some or all aspects of the law. For example, firms with fewer than a given number of employees, or in a specified industry could have automatic exclusion.

- Making provision in the law to empower the regulatory body or a designated public officer to exempt one or more category of undertaking from the law. For example, firms in a particular economic sector may seek an exemption on grounds that the unique characteristics of the sector are such that some conduct, although anti-competitive in nature, actually enhances economic efficiency and consumer benefits. Such exemptions could also take the form of subsidiary legislation requiring the vetting of the Legislative Council.

- Allowing undertakings to seek exemptions on a case-by-case basis from the regulatory authority. For example, an undertaking may seek an exemption on the grounds that its conduct, whilst anti-competitive, actually results in a public benefit that outweighs the harm to consumers.

Circumstances in which Exemptions might Apply

82. Providing for too many exclusions or exemptions, particularly at the early stage of introducing a new competition law, would likely dilute the effectiveness of such a law. It could also give the impression that the Government was not wholehearted in addressing the potential problem of anti-competitive conduct in our economy. However, there might well be circumstances in which exemptions could be justified in the public interest.

83. The United Nations Conference on Trade and Development (UNCTAD)[10] has noted that exemptions that have been granted in various jurisdictions fall into a few major categories. For example, many jurisdictions have granted exemptions in respect of actions aimed at balancing unequal economic or bargaining power, such as labour unions' collective bargaining to negotiate wage levels and other employment conditions; joint purchasing by SMEs; and the formation of farmers' and fishermen's cooperatives. Exemptions have also been granted to address information, transaction cost and "collective action" problems, such as the collection and exchange of statistics and information, and professional rules that help ensure the supply of qualified and ethical services.

84. The UNCTAD report also found that for some sectors that had been granted exemptions, developments in technology, organisational methods and applied economics suggested that alternative pro-competition approaches to these sectors had become feasible. The report thus considered it useful to adopt certain basic principles and procedures in the granting of exemptions, namely –

- Exemptions should be granted on a limited-time basis with provision for periodic review;
- Exemptions should be granted after public hearings with the participation of the interested and affected parties;
- The exemptions should place as few restrictions on competition as possible; and
- Exemptions should be generic in nature, relating to types of economic activity or arrangement, rather than being industry or sector specific.

Some examples of how exclusions and exemptions are tackled in some overseas jurisdictions are briefly described in the following box.

10 "Application of Competition Law: Exemptions and Exceptions": UNCTAD, 2002

Exclusions and exemptions – some overseas examples

Australia's Trade Practices Act

The Trade Practices Act of 1974 allows the regulatory authority, the Australian Consumer and Competition Commission (ACCC), to exempt conduct from the relevant provisions of the Act. This may be done on application, provided that the ACCC is satisfied that a violation of the law would result in a public benefit that would outweigh the possible harm that might result from a lessening of competition. In making its decision, the ACCC conducts detailed investigations involving the parties in question, other interested parties, and experts in the field concerned.

United Kingdom Competition Act

In the United Kingdom, certain undertakings and agreements can be excluded from the application of part or all of the Competition Act 1998. These include, for example, an undertaking entrusted with the operation of services of general economic interest while carrying out the particular tasks assigned to the undertaking; an agreement that is made in order to comply with a legal requirement; an agreement that is needed to avoid a conflict with an international obligation; and an agreement in the interest of public policy.

The Competition Act 1998 also provides that the Office of Fair Trade (OFT) may grant an exemption if an agreement –

(i) contributes to improving production or distribution or promoting technical or economic progress;

(ii) allows consumers a fair share of the resulting benefit;

(iii) does not impose on the undertakings concerned restrictions which are not indispensable to the attainment of those objectives; and

(iv) does not afford these undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

In addition, the OFT may recommend to the Secretary of State for Trade and Industry that he make an order exempting a particular category of agreement that is likely to meet the above criteria. Exemptions have been granted to agreements related to public transport ticketing schemes, airline alliances, and collaboration between banks on ATM services.

Singapore's Competition Act

In Singapore, the Competition Act 2004 allows for exclusion of various types of undertaking and agreement similar to those of the UK. The Act also excludes agreements or conduct relating to any "specified activity" regulated under the legislation, which includes the supply of postal services, wastewater management services, scheduled bus services, rail services and cargo terminal operations. The Act also allows for block exemptions, similar to those in the UK.

85. The following chapter deals with how a competition law might be implemented, particularly in terms of the regulatory structure and options available.

Chapter 4
Regulating a Competitive Environment – Options

86. If a new competition law were to be introduced in Hong Kong, an appropriate authority would be required to enforce the law and to ensure that the community was aware of its rights and obligations. Currently, the only body within the Government solely responsible for competition is the Competition Policy Advisory Group (COMPAG), under the Financial Secretary. However, this body has no statutory role or powers, and little in the way of dedicated resources or full-time expertise at its disposal. In its current form, COMPAG is therefore not equipped to enforce new competition laws.

87. In the telecommunications and broadcasting sectors, competition issues are regulated by the Telecommunications Authority (TA) and the Broadcasting Authority (BA) respectively. However, both these authorities have a wide range of industry specific issues other than competition under their purview, and it would not be consistent with their current roles for them individually to take on a broader, cross-sector competition workload.

88. In order to have a successful competition regime, it would be important that enough support and resources would be provided to the authority so that it could fulfill its regulatory, advocacy and other essential functions. In this Chapter, we look at three main options for the establishment of a regulatory mechanism for the enforcement of a new competition law, should this be introduced, as well as the powers that the regulator should have. Initially, however, we look briefly at the regulatory frameworks in the jurisdictions discussed in Chapter 2.

Overseas Regulatory Frameworks

89. For ease of reference, Table 2 below highlights some of the main aspects of the regulatory frameworks in the relevant jurisdictions.

Table 2: Competition Regulatory Regimes in Overseas Jurisdictions

	Australia	Canada	European Union	Singapore	United Kingdom	USA
Enforcement agency	Australian Competition and Consumer Commission (ACCC)	Competition Bureau under the Commissioner of Competition	European Commission – Directorate General for Competition (ECDGC)	Competition Commission of Singapore (CCS)	Office of Fair Trading (OFT)	Federal Trade Commission (FTC)
Hearing and sanctioning power	The courts (civil and criminal cases)	Competition Tribunal (civil cases); the courts (criminal prosecutions)	ECDGC	CCS	OFT – civil sanctions The courts – criminal prosecutions and company disqualification orders	The courts (civil and criminal cases)
Type of sanction for competition related offences	**Civil:** fine of up to A$10 million for companies **Criminal:** individual fines of up to A$40,000	**Civil:** financial penalties **Criminal:** up to five years' imprisonment and C$10 million fine	**Civil** only: fines of up to €20 million or 10% of total turnover in preceding business year (whichever is the greater)	**Civil** only: fine of up to 10% of annual turnover for 3 years	**Civil:** fines of up to 10% of annual turnover for up to three years **Criminal:** prison term of up to 5 years for cartel offences	**Civil:** fines **Criminal:** fines of up to US$1million for individuals or $100million for companies; prison term of 10 years
Appeal or review channels	Competition Tribunal (reviews regulatory decisions) and the courts (appeals)	The appeal courts	European Court of First Instance, European Court of Justice	Competition Appeal Board (further appeals through the courts)	Competition Appeal Tribunal (further appeals through the courts)	The appeal courts

90. As the above table shows, the regulatory mechanisms for enforcing competition law vary between jurisdictions. In some places, the authority responsible for enforcement has wide-ranging powers including investigating potential cases of anti-competitive conduct and sanctioning offenders. Others rely heavily on the courts to adjudicate as to whether an enterprise has sought to hinder competition unfairly and to hand down appropriate sanctions. Sanctions themselves also vary, with different approaches to civil and criminal remedies, and to the penalties that can be handed down to companies and to individuals.

91. Nonetheless, there are certain common features that the various regulatory mechanisms have to ensure effective law enforcement, for example –

- A dedicated regulatory authority that is either independent from or in some way removed from the main body of the government and that has access to sufficient resources and expertise;
- Appropriate powers to enable the regulatory authority to investigate possible cases of anti-competitive conduct – typically such powers would include the right to demand the production of evidence and to enter premises and conduct searches (with the necessary authorisation, usually from the courts); and
- Sanctions, either civil, criminal or both, which are sufficient to deter people from taking the risk of engaging in anti-competitive conduct.

92. Whichever of the regulatory models Hong Kong were to pursue, in the event that a new competition law were to be introduced, it is likely that the system would require similar features to provide for effective enforcement of such a law. In this regard, the powers and functions that might be required to be exercised by a competition regulator are discussed in Chapter 5 of this document. The paragraphs below look at options for an overall regulatory framework for implementing a competition law.

A Regulatory Framework for Implementing Competition Law

Key Question 8:
Which is the most suitable of the three principal options set out below for a regulatory framework for the enforcement of any new competition law for Hong Kong?

Key Question 9:
Regardless of the option you may prefer, should the regulator be self-standing or should a two-tier structure be adopted, whereby a full-time executive is put under the supervision of a management board made up of individuals appointed from different sectors of the community?

Option One – A Single Authority with Power to Investigate and Adjudicate

93. The first option is to adopt a model that resembles the regulatory regimes in the European Union, Singapore and the United Kingdom[11](see Table 2 above), as well as Hong Kong's regimes for telecommunications and broadcasting, under which the TA and the BA not only receive and investigate complaints of anti-competitive behaviour, but also decide whether such behaviour has in fact taken place, and impose penalties as appropriate. A competition authority could act in the same way, as both the enforcement agency and as the body responsible for deciding on whether anti-competitive conduct had taken place.

94. There are a number of arguments for having a single regulatory body investigate, determine the outcome of and hand down penalties for cases of anti-competitive conduct. For example –

- A simple and streamlined institutional structure is consistent with the principle of small government;

11 It should be noted that in the UK, civil sanctions may be imposed by the regulator, whereas if criminal sanctions are to be sought, the case in question goes to the courts.

- It is likely that cases could be dealt with more quickly by a single regulatory body;
- Having separate bodies engaged respectively in the investigation and the adjudication of cases of anti-competitive conduct would require more resources (and quite possibly the duplication of some support functions) than having a single body responsible for all aspects of regulation and enforcement; and
- There is no indication that the competition regimes in place in the European Union and the United Kingdom (as well as the current arrangements in Hong Kong for the broadcasting and telecommunications sectors), where the regulatory authority determines cases and hands down penalties, have led to unfair treatment.

95. On the other hand, there might be a concern that placing both executive and quasi-judicial powers in the hands of a single regulator would limit the scope for checks and balances in the implementation of any new law. To a large extent, this concern could be allayed by putting in place an appropriate appeal mechanism to ensure an effective check on the authority. Appeal mechanisms are discussed in paragraphs 102 to 103 below.

96. A measure of balance could also be provided by providing for a "two-tier" structure for the regulatory body, whereby its full-time executive would be put under the supervision of a management board made up of individuals from within the community. The BA in Hong Kong is an independent statutory industry regulator supported by the Broadcasting Division of the Television and Entertainment Licensing Authority, a government department, as its executive arm. Having a two-tier structure would also allow the regulatory body to project an image of independence and distance from the main body of the government, a factor considered to be important by many supporters of a new regulatory regime for competition. The CPRC also supported a two-tier structure for the regulatory authority.

Option Two – Separation of Enforcement and Adjudication

97. In Australia and the USA – and in the case of criminal sanctions, the UK – the roles of enforcement agency and adjudicator are separate, with the competition regulator investigating possible anti-competitive conduct and then where appropriate, putting the evidence before the courts for a judgment.

98. Arguments in favour of having the adjudication of cases conducted by a body separate from that which enforces the law include the following –

- It would provide for objective judgment of the merits of individual cases at a remove from the day-to-day operation of the regulatory authority;

- It could provide a check against over-zealous regulation by the enforcement body (for example, through the setting of aggressive quantitative targets for investigation and sanctioning of anti-competitive conduct); and

- Given that the Government itself may be involved in certain markets from time to time, placing the power of adjudication outside the ambit of the government-appointed regulator should help reassure the public and the business community that a fair hearing will be given to all parties and without favour.

99. Placing the responsibility for adjudicating cases of suspected anti-competitive conduct on the courts would add to the workload of the Judiciary, and as noted above would require additional time and resources when compared to having a regulator assume the roles of both investigator and judge. However, separating the enforcement and adjudication roles might be seen by many as more likely to lend itself to transparency and accountability.

Option Three – Adjudication by a Specialist Tribunal

100. Of the examples of overseas regulatory regimes set out in Table 2 above, there is one (Canada) in which a specialist Competition Tribunal has been established to adjudicate on cases of suspected anti-competitive conduct brought by the enforcement authority.

101. Similar to Option Two above, a specialist tribunal creates a clear separation of powers of enforcement and adjudication. A specialist tribunal would further provide for a degree of expertise to be built up within one body, which could help ensure consistency of judgments. It should be borne in mind, however, that the establishment of a Competition Tribunal would likely require the allocation of more public resources than that required for the setting up of a single regulatory authority with powers of investigation and adjudication (Option One above). More time may be required to complete the processing of a competition complaint than in the case of Option One.

Appeals

102. In addition to setting up a regulatory authority, it would be necessary to provide for appropriate channels of appeal with regard to the decisions of the authority. To an extent, the actual avenue for appeal would depend on the nature of the adjudicating body. For example, under the option for the courts to adjudicate on and sanction cases of anti-competitive conduct (Option Two), it would be appropriate for any appeal to go to a higher court than that which had made the original decision, as is the case with court judgments generally in Hong Kong. Similar considerations apply to Option Three, given that the specialist tribunal would be quasi-judicial in function.

103. In the case of the regulatory authority itself having the power to adjudicate and hand down sanctions (Option One), rather than appeals go through the courts, one option would be to set up a dedicated appeal board along the lines of the Telecommunications (Competition Provisions) Appeal Board, which handles appeals against the TA's decisions in relation to competition issues in the telecommunications sector. This would create conditions that would help to ensure consistency in judgments and allow the members of the board to develop expertise in the area of competition.

Summary of Options

104. For ease of reference, the three principal options outlined here for the framework for enforcing any new cross-sector competition law can be summarised as follows –

- Option One – a regulatory authority with the power to investigate suspected cases of anti-competitive conduct and to adjudicate and impose sanctions where it considers that a case has been established, with appeals against the decisions of such a body to be heard by the courts or a specially appointed appeal board;

- Option Two – a regulatory authority with enforcement powers, which would bring suspected cases of anti-competitive conduct to the courts for judgment and sanction, as appropriate, with appeals to be made to higher courts; and

- Option Three – a regulatory authority with enforcement powers, which would bring suspected cases of anti-competitive conduct to a specialist tribunal for judgment and sanction, as appropriate, with appeals to be made to higher courts.

105. For each of these options, the regulatory authority could be either a "stand-alone" executive body like the TA, or a body that has an executive overseen by an appointed management board, i.e., a two-tier structure, like the BA. Whichever option might be adopted, the full-time staff of the regulatory authority would require appropriate levels of expertise in disciplines related to competition matters, such as economics, accounting and the law.

106. The authority would require sufficient resources to allow it to enforce the law effectively, as well as to provide guidance and information to business and consumers alike on how the law would apply in practice. It would be difficult at this stage to come up with a firm estimate of the likely resource requirements, as this would depend on which of the regulatory options were to be pursued. Nonetheless, making reference to a number of local and overseas regulatory authorities, and on the assumption that the authority would have a full-time executive including professional legal, accounting and economic expertise, it may require an annual budget in the range of $60 million to $80 million.

Chapter 5
Enforcement and Related Issues

107. The previous two chapters of this document have considered whether Hong Kong needs a competition law – and if so, how such a law might be framed – as well as a possible institutional framework for enforcing such a law. There are also other related aspects that need to be discussed, many of which relate to enforcement and the powers available to the regulatory authority. These include the following –

- The handling of complaints, including those that are trivial, frivolous or malicious;
- The extent of the investigative and enforcement powers that should be granted to the regulatory authority;
- The conduct of investigations, including the issue of confidentiality and disclosure of information;
- The relationship with existing regulatory frameworks and the concurrent application of different laws to regulated industries;
- The level and type of penalties that should apply, as well as the need for a leniency programme;
- Whether the authority or the courts should have the power to order that parties desist from anti-competitive conduct, and to reach settlement with parties suspected of anti-competitive conduct without recourse to formal adjudication; and
- The procedure for civil claims for damages by parties that have suffered losses as a result of anti-competitive conduct.

Handling of Complaints

Key Question 10:
In order to help minimise trivial, frivolous or malicious complaints, should any new competition law provide that only the regulatory authority has the power to conduct formal investigations into possible anti-competitive conduct?

108. Whilst the regulatory authority can act of its own volition, complaints are often an important source of information on which it may act. Whilst some overseas competition authorities will consider anonymous complaints, there may be practical difficulties in doing so when full information is not available and clarification cannot be sought from the complainants. Accordingly, complainants are generally encouraged to provide as much information as possible.

Handling of Trivial, Frivolous or Malicious Complaints and Threshold for Investigation

109. The introduction of a new competition law should not lead to normal business operations being unduly constrained by complaints that are trivial, frivolous or made in bad faith. For this reason, it might be prudent for such a law to stipulate that only the regulatory authority would have the power to investigate possible violations. In other words, whereas any party believing itself to have been the subject of anti-competitive conduct may lodge a complaint with the regulatory authority, the regulatory authority alone would be able to decide whether further action should be taken.

110. Any new competition law could also stipulate the threshold that would have to be met before the regulatory authority might decide to initiate a formal investigation. For example, such a law could provide that the regulatory authority could only use its powers of investigation if it considered that there were reasonable grounds for suspecting that an infringement of the anti-competition law had taken place.

Conduct of Investigations

Formal Powers of Investigation

> ***Key Question 11:***
> **What formal powers of investigation should a regulatory authority have under any new competition law?**

> ***Key Question 12:***
> **Should failure to cooperate with formal investigations by the regulatory authority be a criminal offence?**

111. To enable a regulator to enforce any new competition law effectively, the authority would require investigative powers to facilitate access to relevant information, be it direct from individuals concerned or from records kept by suspected offenders. Without such powers, any investigation would rely largely on the extent to which market players voluntarily provide information to the agency charged with the investigation. The experience of COMPAG suggests that this may not be an effective approach, as it is likely that parties under investigation would cite concerns such as personal privacy or commercial sensitivity as grounds for not allowing access to a full range of data and other related information, thereby severely constraining any investigative process.

112. In the telecommunications and broadcasting sectors in Hong Kong, in relation to the investigation of offences related to competition (as well as to other offences) the law provides the authorities with the powers –

- To require the supply of information relating to the relevant business, regardless of whether or not this might be subject to a confidentiality agreement with a third party;
- To require the production of documents or accounts; and
- To enter premises, inspect and copy relevant documents and accounts, in accordance with the procedures set down in the law.

113. Overseas competition legislation provides for similar powers to be granted to the regulator, although the exercise of these powers may depend on the granting of an order or a warrant by a judicial officer. For example, in Canada, once the Competition Commissioner has begun a formal inquiry into possible anti-competitive conduct, he may apply to a judge for an order to require a person to provide information under oath or to produce specified documents. The Commissioner may also apply to a judge for a warrant to enter premises and to search for and seize documents.

114. In its report on competition policy, the CPRC noted the various investigative powers available to authorities in Hong Kong and competition regulators overseas, and recommended that a competition authority in Hong Kong should have the formal powers of investigation –

- To require a person to give written or oral information;
- To require the production of documents or other records or data; and
- With a warrant issued by the court, to enter and inspect premises and seize relevant documentary evidence.

115. Such powers are commonly regarded as "formal" in the sense that a person who fails to cooperate when these powers of investigation are exercised by the regulatory authority will be deemed to have committed a criminal offence, and may have to face a fine or imprisonment in consequence. Overseas legislation often stipulates that it is an offence for a person to –

- Fail to comply with a requirement imposed under the formal powers of investigation in the relevant competition law;
- Intentionally obstruct an authorised officer carrying out an inspection, either with or without a warrant as the relevant law may specify;
- Intentionally or recklessly destroy or otherwise dispose of or falsify or conceal a document that he or she has been required to produce or cause or permit its destruction, disposal, falsification or concealment; or
- Provide information that is false or misleading particularly if he or she knows, or is reckless as to whether, it is false or misleading, either to the regulatory authority or to another person such as an employee or legal adviser, knowing that it will be used for the purpose of providing information to the regulatory authority.

Confidentiality and Disclosure of Information

> ***Key Question 13:***
> **How might a competition regulatory authority deal with the disclosure of information that comes to its knowledge having regard to the need to protect various categories of confidential information on the one hand, and the need to make appropriate disclosure in order to take forward an investigation when the circumstances so require?**

116. The investigation and detection of infringements of any new competition law would likely rely in many cases on information from individuals working with or close to the parties engaged in such conduct. Such individuals, and possibly their own companies, would need to be assured that, as the source of the information passed to the regulator, they would be protected by appropriate confidentiality provisions in any new competition law. Parties that were the subject of complaints would also be likely to expect protection from the disclosure of information provided by complainants that, even if not substantiated, might be damaging to their personal reputation or business operations. Without strictly observed provisions prohibiting the disclosure of confidential information provided by complainants and other parties, it might be difficult for a competition regulator to function effectively. The box below briefly outlines how the issues of confidentiality and disclosure of information are addressed in Singaporean law.

Disclosure of information – Singapore

Section 89 of the 2004 Competition Act of Singapore provides that all matters –

- relating to the business, commercial or official affairs of any person;
- which have been identified as confidential; or
- relating to the identity of persons furnishing information to the Competition Commission of Singapore (CCS);

coming to the knowledge of the CCS in the course of performance of its functions and duties shall not be disclosed, unless this is necessary for the performance of its function or duties, or unless disclosure is lawfully required or permitted under the Act or any written law.

However, section 89 of the Act sets out a number of exceptions under which disclosure is authorised, including –

- where consent has been obtained from the person to whom the information relates;
- for the purpose of a prosecution under the Act;
- for the purpose of investigating a suspected offence or enforcing a provision under the Act; and
- for the purpose of giving effect to any provision of the Act.

If disclosure is to be made under the last category stipulated in the preceding paragraph, i.e., to give effect to a provision of the Act, the CCS shall have regard to the extent to which disclosure is necessary for the purpose of such disclosure.

The CCS must also have regard to the need for excluding, so far as is practicable –

- information the disclosure of which would, in the CCS' opinion, be contrary to the public interest;
- commercial information the disclosure of which would, in the CCS' opinion, significantly harm the legitimate business interests of the undertaking to which it relates; or
- information relating to the private affairs of an individual, the disclosure of which would, in the CCS' opinion, significantly harm that individual's interest.

Interface with Existing Regulatory Framework and the Issue of Concurrent Powers

Key Question 14:
Should the existing sector specific regulators that also have a competition role continue to play such a role if a cross-sector competition regulatory authority were to be established?

117. The CPRC Report noted that legislation to prohibit anti-competitive conduct already exists in the broadcasting and telecommunications sectors in Hong Kong, each of which has its own regulatory framework. Having made reference to a number of overseas regulatory regimes, the CPRC concluded that during the initial period of operation of a cross-sector competition law in Hong Kong, the current sector specific regimes in broadcasting and telecommunications should be retained for the following main reasons –

- The proposed cross-sector competition law is not as comprehensive in coverage as the existing sector specific regimes;
- The sector specific regimes have been operating for a number of years and the sector regulators have built up a body of procedures and precedents which the new regulatory authority may take some time to develop; and
- There are advantages for the sector specific regulators to continue to administer competition law in their respective sectors because of their detailed knowledge about the operation of these sectors.

118. The CPRC considered that there should be coordination between the new cross-sector competition authority and the sector specific regulators about the administration of competition law to ensure consistent enforcement standards. One way of implementing such coordination might be to empower any new competition authority, in consultation with sector specific regulators, to issue guidance and procedural rules to help identify which regulator should investigate individual cases or categories of case. In addition, a Memorandum of Understanding could be agreed by each of the regulatory authorities to clarify in what circumstances a particular authority would take responsibility for a case of anti-competitive conduct.

Penalties for Anti-competitive Conduct

Civil versus criminal

> ***Key Question 15:***
> **Should breaches of any new competition law be considered civil or criminal infringements? What levels of penalty would be suitable?**

119. Table 2 in Chapter 4 summarises the sanctions that regulatory authorities in other jurisdictions impose in cases of anti-competitive conduct. Many overseas regulators have the option of seeking either civil or criminal judgments in such cases. For civil judgments, penalties are generally handed down in the form of fines, which can be equivalent to a fixed percentage of a company's annual turnover for a period of time, or simply a set maximum level. For criminal cases, fines can be combined with a term of imprisonment for individuals involved in anti-competitive conduct.

120. Penalties for engaging in anti-competitive conduct need to be sufficiently high to have a deterrent effect. In this regard, the risk of imprisonment would undoubtedly help people to resist pressure or the temptation to act in an anti-competitive manner. However, given that the introduction of a cross-sector competition law would be a new step for Hong Kong, it might not be appropriate to provide for custodial sentences from the outset. A sufficiently high level of fines, whether related to a company's turnover or set at a high maximum level, might prove to be a sufficient deterrent. To strengthen the deterrent effect, any new law could also provide for the disqualification of any person found responsible for anti-competitive conduct from holding a directorship of any company for a period of time.

121. For reference, under the Broadcasting Ordinance, the maximum penalty for a first offence is $200,000, rising to $400,000 for a second offence and $1 million for any subsequent offence. Where the Broadcasting Authority considers such a level of fine inadequate for a breach of the law regarding competition, it may apply to Court of First Instance to impose on the party in question a fine of up to 10% of the turnover of the party concerned during the period of the breach. Similar financial penalties exist in legislation regulating competition in the telecommunications sector.

122. One further point to consider with regard to the level of penalties relates to the regulatory framework for enforcing a new competition law. It could be argued that if penalties for anti-competitive conduct were to be restricted to fines, there might not be a need for cases to be determined by the courts or a specialist tribunal. Assuming that sufficient appeal channels were available, it might be acceptable for a regulatory authority itself to adjudicate on cases of anti-competitive conduct and impose fines. However, in cases where individuals had refused to cooperate with investigations into potential infringements of a new competition law, to be consistent with other laws in Hong Kong and overseas, offenders would still have to appear before the courts, where, on conviction, criminal sanctions could apply.

Leniency

> ***Key Question 16:***
> **Should any new competition law include a leniency programme?**

123. Due to the secretive nature of cartels, regulatory authorities often rely on the provision of information by one or more cartel member to assist in investigations conducted under competition law. In other jurisdictions, the offer of leniency to cartel members that come forward with information has frequently been effective in helping to uncover anti-competitive conduct. Under a typical leniency programme, a cartel member that provides relevant information may have any subsequent fine imposed by the authorities substantially reduced or even waived[12]. The extent of the relief given usually depends on factors, such as whether the informant is the first member of the cartel to come forward, whether it cooperates throughout the investigation, and whether it has previously taken steps to encourage other companies to take part in the cartel.

12 In jurisdictions where regulators have authority to impose fines, the extent of leniency programme is usually set out in regulatory guidelines. Where penalties are subject to determination by the courts, the regulator would typically have a stated policy of asking the court to impose lesser penalties on companies that have come forward with information.

Regulatory Orders and Settlements

124. The effective implementation of a new competition law could be constrained if the regulator was required to conduct frequent lengthy investigations into suspected anti-competitive conduct followed by formal hearings. Bearing in mind that the main objective of a competition law would be to enhance economic efficiency and ensure free trade for the benefit of consumers, such an objective might be more effectively met by requiring parties to cease immediately from engaging in anti-competitive practices or by the regulator reaching an early settlement with parties rather than initiating a full-scale investigation with a view to possible punitive action.

"Cease and Desist" Orders

Key Question 17:
Should any new competition regulator be empowered to issue orders to "cease and desist" from anti-competitive conduct?

125. In its review, the CPRC noted that it was important for a competition regulator to have suitable administrative tools at its disposal to help in the effective enforcement of the law. One such tool could be the power to make an order - or to seek an order from an appropriate judicial authority - to require parties to "cease and desist" from anti-competitive conduct, in order to minimise harm to markets as soon as possible after such conduct had been detected. Currently, the BA is empowered to issue directions to licensees to cease and desist from the action prohibited.

126. In considering the procedure for issuing "cease and desist" orders, the CPRC noted that the process of securing such an order from the courts could lead to delay, and that it might be more effective for the regulator itself to be empowered to issue such orders.

Settlements

Key Question 18:
As an alternative to formal proceedings, might any new competition regulator have the authority to reach a binding settlement with parties suspected of anti-competitive conduct?

127. Where a competition regulator had good cause to believe that anti-competitive conduct had taken place, rather than initiate formal judicial proceedings, it might be equally effective for the regulator to reach a settlement with the party under investigation. Such a settlement could be in the form of a payment, or of an undertaking to stop the conduct in question, or both.

128. A settlement might not be appropriate in every case. In order to show that breaching competition law would be regarded as a serious matter, a regulator would need to judge carefully whether to take punitive action against a party suspected to be engaged in anti-competitive conduct, or whether reaching a settlement would be a more efficient and effective course of action. The regulator would also need to take into account the interest of parties that might have been affected by anti-competitive conduct when deciding whether or not it might be appropriate to reach a settlement.

Rights of Private Civil Action

Key Question 19:
Should any new competition law allow parties to make civil claims for damages arising from anti-competitive conduct by another party?

Key Question 20:
How should any new competition law address the concerns that our businesses, especially our SMEs, may face an onerous legal burden as a result of such civil claims?

129. Many laws contain provision for a person who has committed an infringement to be liable to pay compensation by way of damages for financial losses sustained by any other person as a result of such infringement. The CPRC in its report concluded that regardless of the outcome of cases of anti-competitive conduct, parties that considered that they had been affected by such conduct should be entitled to take civil action in the courts for the recovery of damages suffered. The CPRC added that proven anti-competitive conduct could be cited as grounds for claiming damages.

130. There may well be concerns that adopting such an approach could lead to extensive litigation between parties accusing one another of anti-competitive conduct, and that this might be used as a ploy to require business rivals to incur heavy legal costs and discourage them from pursuing valid business objectives. In particular, small businesses may be concerned that larger corporations would use the threat or exercise of civil action to prevent them entering certain markets or to constrain their business activities. Smaller firms may also be concerned at the potential costs involved in defending themselves against such action or in seeking to pursue their own claims for redress.

131. To address this concern, one approach adopted in jurisdictions overseas is to limit the right to private action so that it could be pursued only after the regulator had made a decision that the conduct in question constitutes an infringement of competition law. Where that decision was subject to appeal, the right to private civil action could only be exercised upon expiry of the appeal period, or upon the determination of any appeal that confirms the earlier finding of the competition regulator that an infringement has occurred. A time limit for taking such private actions (for example, within two years of the decision or the determination of any appeal with regard to that decision) could also be imposed.

132. It should, however, be noted that even without such a limit, SMEs and large firms alike are unlikely to incur significant litigation costs as a result of trivial, frivolous or malicious complaints. Without the support of a finding of infringement by the competition regulator (or the tribunal) it will in reality be very difficult for a private party to initiate or sustain legal actions that rely heavily on proven anti-competitive conduct to succeed. The nature of cartel type behaviour, which involves collusion between two or more consenting parties, is such that, without the benefit of formal investigative powers or information provided by "insiders", it is often difficult for a private party to adequately discharge the burden of proof that will be required in the court to establish that anti-competitive conduct has taken place.

133. In reality, before instituting any civil claim for damages, an aggrieved party will likely lodge a complaint with the competition regulator in the first place, and wait until it (or the tribunal) has made a finding of infringement of competition law. Most trivial, frivolous or malicious complaints will thus have been filtered out by the competition regulator at a very early stage, as noted in paragraphs 109 and 110 above.

134. It should be noted that at the initial stage where the regulatory authority is only making informal enquiries, it is generally not necessary for a firm which is the subject of a complaint to engage legal advice in preparing its response, although it would be free to do so if it so wishes. The firm might feel a greater need to engage legal advice if formal powers of investigation are subsequently invoked by the regulatory authority, but this would only happen if, in the eyes of the authority (not the complainant), there are reasonable grounds for suspicion after the evidence gathered from the informal enquiry has been fully taken into account.

Allaying concerns of SMEs

It has already been noted in the Box on "Big and Small" after paragraph 47 that SMEs have little to fear from a competition law as it is relatively uncommon for SMEs to be targeted by a competition regulator. SMEs do not have market power almost by definition. On the contrary, SMEs stand to gain as the potential of the bigger players to adopt abusive or other anti-competitive practice is checked by competition law. SMEs might enter and trade more freely in the various markets as it would then be difficult for the bigger players to impose artificial entry barriers. They might also benefit from lower costs of inputs amidst a more competitive environment.

The new competition regulator in Hong Kong could play a strong advocacy role and let SMEs know how a competition law may benefit them. Subject to resources, the competition regulator may also provide appropriate advisory services to SMEs so as to help them better meet any challenges that may arise in the compliance process.

135. It has been suggested by some commentators that a complainant whose complaint turns out to be unsubstantiated should be required to bear the legal and administrative cost incurred by the undertaking that is the subject of the complaint in dealing with any enquiries or formal proceedings that may be undertaken by the competition regulator. Whilst it is reasonable to consider different options, it should be noted that such a requirement is not a common feature in the overseas competition law we have studied.

An overseas example

In the United Kingdom, albeit in the different context of the alternative dispute resolution (ADR) mechanism under the Consumer Credit Act 1974, the Office of Fair Trade (OFT), when responding to the question of whether consumers should be charged a fee for bringing a case to the ADR, points out that a fee to consumers would hinder their access to the mechanism and would likely deter people from using it. The OFT notes that making a complaint is not without cost to a consumer, and that whilst some consumers may pursue frivolous or vexatious complaints, these could be screened out at an early stage. The OFT's view is that, on balance, charging a fee could deter a significant number of consumers with legitimate concerns from seeking redress, and could also undermine confidence in the ADR regime.

Chapter 6
Conclusion and Key Questions

136. This document has outlined a number of ways in which Hong Kong's competition policy might move forward in order to achieve the objective of enhancing economic efficiency, protecting free trade and thereby bringing benefits to consumers.

137. Chapters 1 and 2 respectively set out the local background to the development of competition policy and briefly review the approach taken by certain other jurisdictions. Chapter 3 introduces several important considerations that we need to discuss when deciding whether or not Hong Kong needs its own competition law. Chapter 4 looks at possible models for a regulatory framework for enforcing a new competition law, whilst Chapter 5 reviews a number of issues that might be of concern in the detailed preparation of such a law.

138. It is the intention that this document should provide an objective basis for an informed discussion in the community of the appropriate way forward for Hong Kong's competition policy – in particular, whether a new law needs to be introduced in order to ensure the effective implementation of this policy, and if so, what the scope and the key provisions of such a law might be.

139. With these points in mind, and in order to help focus the discussion clearly on the issues that have been covered in these pages, we have identified the following key questions for you to consider and respond to.

Twenty Key Questions

The Need for a New Competition Law - Considerations

1. **Does Hong Kong need a new competition law?**
   (In considering this question you may wish to refer back to the considerations set out in paragraphs 43 to 47 in Chapter 3 above)

2. **Should any new competition law extend to all sectors of the economy, or should it only target a limited number of sectors, leaving the remaining sectors purely to administrative oversight?**
   (Paragraphs 49 to 55 in Chapter 3)

3. **Should the scope of any new competition law cover only specific types of anti-competitive conduct, or should it also include the regulation of market structures, including monopolies and mergers and acquisitions?**
(Paragraphs 56 to 61 in Chapter 3)

4. **Should a new competition law define in detail the specific types of anti-competitive conduct to be covered, or should it simply set out a general prohibition against anti-competitive conduct with examples of such conduct?**
(Paragraphs 74 to 77 in Chapter 3)

5. **Should a new competition law aim to address only the seven types of conduct identified by the CPRC, or should additional types of conduct also be included, and should the legislation be supported by the issue of guidelines by the regulatory authority?**
(Paragraphs 74 to 77 in Chapter 3)

6. **In determining whether a particular anti-competitive conduct constitutes an infringement of the competition law, should the "purpose" or "effect" of the conduct in question be taken into account? Or should such conduct on its own be regarded as sufficient in determining that an infringement has taken place?**
(Paragraphs 78 and 79 in Chapter 3)

7. **Should any new competition law allow for exclusions or exemptions from the application of some or all aspects of the law, and if so, in what circumstances should such exemptions apply?**
(Paragraphs 80 to 84 in Chapter 3)

The Regulatory Framework for Competition Law – Options

8. **Which would be the most suitable of the three principal options set out in Chapter 4 for a regulatory framework for the enforcement of any new competition law for Hong Kong? The options are –**

   - **Option One: A single authority with power to investigate and adjudicate**
   (Paragraphs 93 to 96 in Chapter 4)

- **Option Two: Separation of enforcement and adjudication**
  (Paragraphs 97 to 99 in Chapter 4)

- **Option Three: Adjudication by a specialist tribunal**
  (Paragraphs 100 and 101 in Chapter 4)

9. **Regardless of the option you may prefer, should the regulator be self-standing or should a two-tier structure be adopted, whereby a full-time executive is put under the supervision of a management board made up of individuals appointed from different sectors of the community?**
   (Paragraph 105 in Chapter 4)

Enforcement and Other Regulatory Issues

10. **In order to help minimise trivial, frivolous or malicious complaints, should any new competition law provide that only the regulatory authority has the power to conduct formal investigations into possible anti-competitive conduct?**
    (Paragraphs 109 to 110 in Chapter 5)

11. **What formal powers of investigation should a regulatory authority have under any new competition law?**
    (Paragraphs 111 to 114 in Chapter 5)

12. **Should failure to co-operate with formal investigations by the regulatory authority be made a criminal offence?**
    (Paragraph 115 in Chapter 5)

13. **How might a competition regulatory authority deal with the disclosure of information that comes to its knowledge having regard to the need to protect various categories of confidential information on the one hand, and the need to make appropriate disclosure in order to take forward an investigation when the circumstances so require?**
    (Paragraph 116 in Chapter 5)

14. **Should the existing sector specific regulators that also have a competition role continue to play such a role if a cross-sector competition regulatory authority were to be established?**
    (Paragraphs 117 and 118 and Chapter 5)

15. **Should breaches of any new competition law be considered civil or criminal infringements? What levels of penalty would be suitable?**
(Paragraphs 119 to 122 in Chapter 5)

16. **Should any new competition law include a leniency programme?**
(Paragraph 123 in Chapter 5)

17. **Should any new competition regulator be empowered to issue orders to "cease and desist" from anti-competitive conduct?**
(Paragraphs 125 and 126 in Chapter 5)

18. **As an alternative to formal proceedings, might any new competition regulator have the authority to reach a binding settlement with parties suspected of anti-competitive conduct?**
(Paragraphs 127 and 128 in Chapter 5)

19. **Should any new competition law allow parties to make civil claims for damages arising from anti-competitive conduct by another party?**
(Paragraphs 129 to 135 in Chapter 5)

20. **How should any new competition law address the concerns that our businesses, especially our SMEs, may face an onerous legal burden as a result of such civil claims?**
(Paragraphs 129 to 135 in Chapter 5)

Responding to these Questions

Written Responses

140. You may respond directly in writing on the issues set out in this document to the address below. The deadline for the submission of views is 5 February 2007. You should be advised that unless you specifically request otherwise, the views that you put forward may be published and attributed to you.

Economic Development Branch (Division A)

Economic Development and Labour Bureau

2/F, Main Wing, Central Government Offices

Lower Albert Road

Central, Hong Kong

Fax: 2868 4679

E-mail: competition@edlb.gov.hk

Other Channels for Response

141. We shall also organise and attend public events that will enable us to exchange views with other stakeholders. We shall publish the details of these events on our website at www.edlb.gov.hk.

Chapter 7
What Next?

142. The purpose of issuing this document is to provide a basis for a public discussion of how best to implement an effective competition policy in Hong Kong.

143. During the discussion process, we shall collect and analyse views expressed by stakeholders, with a view to compiling a report on the feedback from the community. This report, which we will make available to the public, will help the Government in considering the measures that we need to take in order to ensure the effectiveness of our competition policy.

144. It would be premature at this stage to draw up a firm timetable for further action. Nonetheless, we recognise the need to respond in good time to the outcome of the process, so as to maintain the momentum of this exercise and to meet public expectations for further progress.

145. We look forward in the coming months to receiving your views on the way forward for an effective competition policy for Hong Kong.

Economic Development and Labour Bureau
November 2006

References

A Framework for the Design and Implementation of Competition Law and Policy, World Bank and OECD, 1998.

ACCC Settles Case against Showmen's Guild, Press Release of the Australian Competition and Consumer Commission (ACCC), 10 May 2006.

Guidelines issued by the UK Office of Fair Trading (OFT) (2004).

Antitrust Guidelines for Collaborations Among Competitors, US Federal Trade Commission and Department of Justice (DOJ), 2000.

Collusive Tendering for Flat Roof and Car Park Surfacing Contracts in England and Scotland, Decision of the UK OFT No. CA98/01/2006, 22 February 2006.

Guidelines issued by Competition Commission of Singapore (December 2005).

Federal Court Orders $23.3 million in Penalties for Petrol Price-fixing, Press Release of ACCC, 17 March 2005.

Justice Department Settles Case Against El Paso Natural Gas Co., Press Release of the US DOJ, 12 January 1995.

New York State Periodical Distributor Pleads Guilty to Market Allocation Charges, Press Release of the US DOJ, 26 September 2003.

The Provision of Alternative Dispute Resolution for Disputes Arising under the Consumer Credit Act 1974, a Response by the UK OFT to the DTIs Consultation Paper, 17 March 2004.

United States of America v. American Bar Association, Final Judgement of the United States District Court for the District of Columbia, 1995.

$8.9 million Penalty on Safeway for Price Fixing and Misuse of Market Power in Bread Market, ACCC, 31 January 2006.

Attachment

Profile of Complaints to COMPAG from 2001-02 to 2004-05

A. Broad Areas of the Economy Involved

Broad Area	No. of cases
Telecommunications	14
Professional services[1]	12
Trading & Retailing	9
Catering & Food supply	7
Transportation & Logistics	6
Real estate & Property management	5
Broadcasting & Media	3
Health care	3
Personal services[2]	3
IT	2
Airline & Hotel	2
Miscellaneous	1
Total :	**67**

B. Nature of Complaints

Alleged Anti-competitive Conduct	No. of cases
Unfair or restrictive government practices	21
Abuse of dominant market position (including predatory pricing)	15
Miscellaneous restrictive practices[3]	9
Price-fixing	7
Bundling of services	3
Unfair or discriminatory standards	3
Market allocation	1
Exclusive arrangement	1
Joint boycott	1
Others[4]	6
Total :	**67**

C. Profile of Complainants

Sector	No. of cases
NGOs	15
Individuals (traders)	13
Large corporations	11
SMEs	11
Individual consumers/others	11
Total :	**61**[5]

1. *Professional services include accounting & finance, consultancy services, insurance, security services and maintenance of equipment.*
2. *Personal services include interior decoration and car washing.*
3. *Includes obstructing market entry, providing inferior service or charging competitors unreasonably high prices and creating artificial barriers to discourage customers from switching to competitors.*
4. *Studies initiated by COMPAG on the situation in certain sectors and alleged conflict of interest of publicly-funded organisations.*
5. *Excludes 6 cases that were initiated by COMPAG.*

Economic Development and Labour Bureau

November 2006