

# Clients & Friends Memo

## What you need to know about Hong Kong Competition Law (Part 2) The First Conduct Rule

28 October 2015

The implementation of the new Competition Ordinance (Chapter 619 of the Laws of Hong Kong) (the **Competition Ordinance**) on 14 December 2015 will mark the first time that Hong Kong has a general and cross-sector competition law.

### Background

The Competition Ordinance was enacted on 14 June 2012 as a general and cross-sector competition law to curb anti-competitive conduct and will come into full effect on 14 December 2015.

Three major forms of anti-competitive conduct are prohibited under the First Conduct Rule, the Second Conduct Rule (collectively referred to as the **Conduct Rules**) and the Merger Rule respectively. In this issue, we will discuss the First Conduct Rule.

### What is the First Conduct Rule?

The First Conduct Rule<sup>1</sup> concerns **agreements, decisions and concerted practices** among **undertakings** which have **the object or effect of preventing, restricting or distorting competition** in Hong Kong. It applies to both horizontal and vertical agreements, and even if the impugned conduct occurs outside Hong Kong or if any party to the conduct is outside Hong Kong.

A flowchart illustrating how the First Conduct Rule works is set out in Appendix 1.

---

<sup>1</sup> Section 6(1) of the Competition Ordinance provides that "an undertaking must not (a) make or give effect to an agreement; (b) engage in a concerted practice; or (c) as a member of an association of undertakings, make or give effect to a decision of the association, if the object or effect of the agreement, concerted practice or decision is to prevent, restrict or distort competition in Hong Kong."

**Key terms used in the First Conduct Rule**

<p><b>Undertaking</b></p>	<ul style="list-style-type: none"> <li>▪ Any entity (including a natural person), regardless of its legal status or the way in which it is financed, which is engaged in economic activity is considered an undertaking.</li> <li>▪ The First Conduct Rule does not apply to conduct involving two or more entities if the relevant entities are part of the same undertaking or corporate group.</li> <li>▪ Employees and trade unions are not considered as undertakings within the scope of the First Conduct Rule.</li> </ul>
<p><b>Agreement</b></p>	<ul style="list-style-type: none"> <li>▪ “Agreement” is broadly defined in the Competition Ordinance and is considered to exist once there is a “meeting of minds” between the parties concerned. For example, an exchange of letters, emails, telephone calls and instant messages would be sufficient.</li> <li>▪ An undertaking may be found to be a party to an anti-competitive agreement if it can be shown that it knew, or should have known, that the collusion in which it participated was part of an overall plan intended to harm competition.</li> <li>▪ Both horizontal and vertical agreements are subject to the First Conduct Rule.</li> </ul>
<p><b>Concerted practice</b></p>	<ul style="list-style-type: none"> <li>▪ A concerted practice is a form of cooperation, falling short of an agreement, where undertakings knowingly substitute practical cooperation for the risks of competition.</li> <li>▪ It typically involves an exchange of commercially sensitive information between competitors without a legitimate business reason.</li> </ul>
<p><b>Decision of an association of undertakings</b></p>	<ul style="list-style-type: none"> <li>▪ Trade associations, cooperatives, professional associations or bodies, societies, associations without legal personalities, associations of associations, etc. are examples of associations.</li> <li>▪ A decision of an association includes its constitution, rules, resolutions, rulings, decisions, guidelines, recommendations, etc., even if it is non-binding.</li> </ul>

<b>Anti-competitive object or effect</b>	<ul style="list-style-type: none"> <li>▪ Where an agreement has an anti-competitive object, it is not necessary for the Competition Commission to also demonstrate that the agreement has an anti-competitive effect.</li> <li>▪ Determining the object of an agreement requires an objective assessment of its aims/purposes viewed in context and in light of the way it is implemented. The parties' intention may also be taken into account. Examples include cartel agreements and, possibly, resale price maintenance agreements.</li> <li>▪ For an agreement to have an anti-competitive effect, it must have, or be likely to have, an adverse impact on one or more parameters of competition in the market (for example price, output, product quality, product variety or innovation).</li> <li>▪ Restrictions contained in an agreement (which is not in itself harmful to competition) that are necessary for the agreement to be workable (<i>i.e.</i>, ancillary restrictions) fall outside the prohibition of the First Conduct Rule.</li> </ul>
--	---

### **Serious Anti-competitive Conduct – the "hard core" infringements**

Where the Competition Commission has reasonable cause to believe that a contravention of the First Conduct Rule has occurred, in general, it must issue a warning notice to the undertaking concerned before bringing proceedings in the Competition Tribunal.

However, this procedure may be bypassed in cases of serious anti-competitive conduct (**Serious Anti-Competitive Conduct**), which is defined as "conduct that consists of any of the following or any combination of the following:

- a) fixing, maintaining, increasing or controlling the price for the supply of goods or services (*i.e.*, price fixing);
- b) allocating sales, territories, customers or markets for the production or supply of goods or services (*i.e.*, market sharing);
- c) fixing, maintaining, controlling, preventing, limiting or eliminating the production or supply of goods or services (*i.e.*, output limitation);
- d) bid-rigging".<sup>2</sup>

<sup>2</sup> Section 2(1) of the Competition Ordinance.

Further, the general exclusion for agreements of lesser significance<sup>3</sup> does not apply to cases of Serious Anti-Competitive Conduct.

### **Exclusions and exemptions from the First Conduct Rule**

The First Conduct Rule does not apply to statutory bodies unless they are specifically brought within the scope of this Rule, nor does it apply to persons or activities specified in a regulation made by the Chief Executive in Council.

Further, schedule 1 to the Competition Ordinance sets out the following general exclusions in respect of the First Conduct Rule:

- e) agreements enhancing overall economic efficiency;
- f) compliance with legal requirements;
- g) services of general economic interest;
- h) mergers; and
- i) agreements of lesser significance.

The Competition Ordinance also provides for block exemption orders and public policy and international obligations exemptions.

Undertakings are not required to apply to the Competition Commission in order to secure the benefit of a particular exclusion or exemption. Nevertheless, they may elect to apply to the Commission for a decision as to whether an exclusion or exemption applies.

### **What's next?**

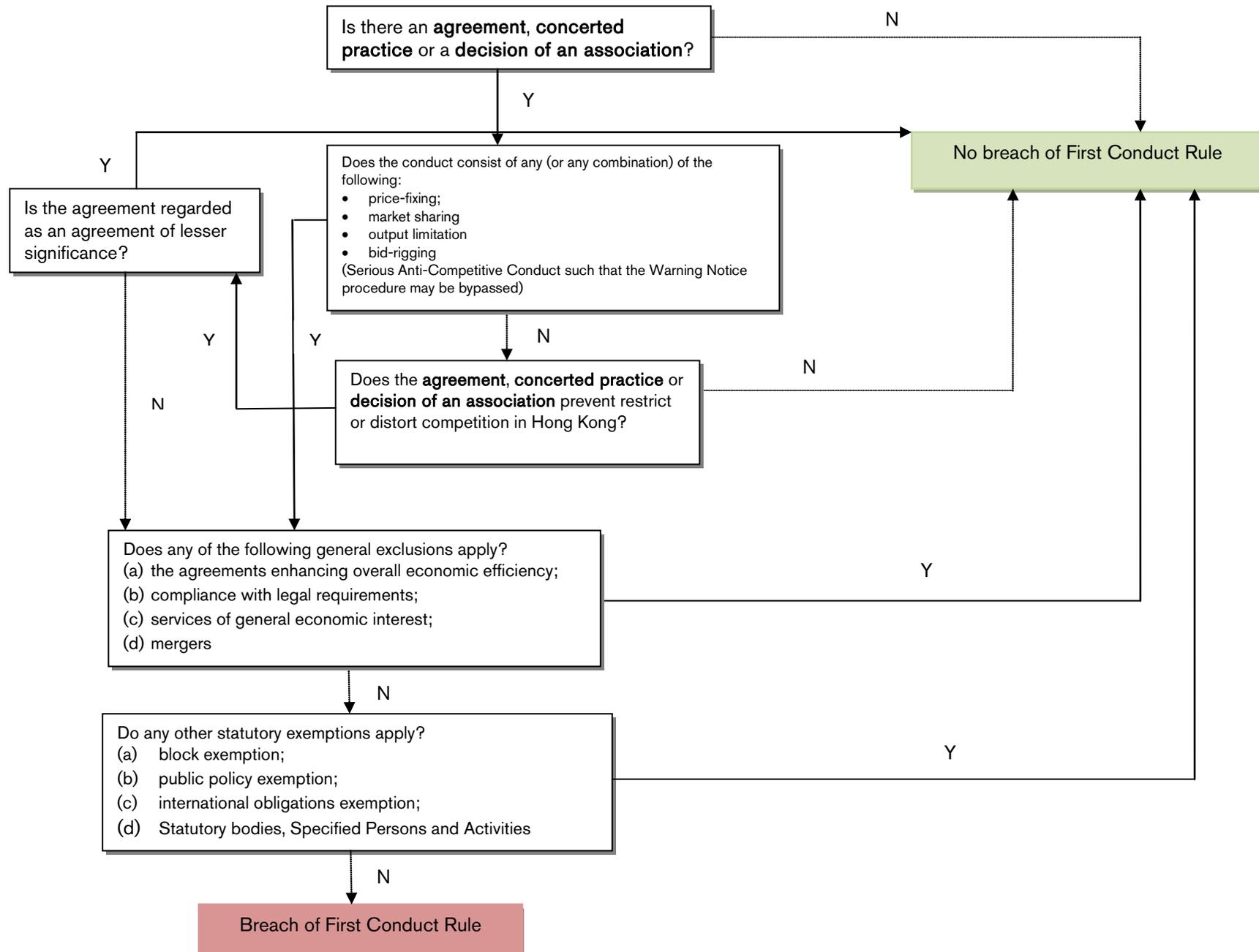
The imminent implementation of the Competition Ordinance is a significant step in the evolution of Hong Kong's fledgling antitrust regime and puts Hong Kong on a similar footing to many other jurisdictions, such as the European Union, the United States and Australia.

Multinational enterprises doing business in Hong Kong can no longer afford to ignore the Special Administrative Region as a jurisdiction that has no competition regime or antitrust enforcement. In the next issue, we will discuss the Second Conduct Rule in greater detail.

---

<sup>3</sup> Pursuant to section 5, Schedule 1 to the Competition Ordinance, the First Conduct Rule does not apply to (a) an agreement between undertakings in any calendar year if the combined turnover of the undertakings for the turnover period does not exceed HK\$200 million; (b) a concerted practice engaged in by undertakings in any calendar year if the combined turnover of the undertakings for the turnover period does not exceed HK\$200 million; or (c) a decision of an association of undertakings in any calendar year if the turnover of the association for the turnover period does not exceed HK\$200 million.

**Appendix  
First Conduct Rule – How it works**



Please feel free to contact any of the following Cadwalader lawyers if you have any questions about this Clients & Friends Memo.

Charles F. (Rick) Rule <i>Head of the firm's Antitrust Group – Washington</i>	+1 202 862 2420	<a href="mailto:rick.rule@cwt.com">rick.rule@cwt.com</a>
Alec J. Burnside <i>Partner – Brussels</i>	+32 (0)2 891 81 81	<a href="mailto:alec.burnside@cwt.com">alec.burnside@cwt.com</a>
Michael Liu <i>Partner – Hong Kong</i>	+852 2946 1235	<a href="mailto:michael.liu@cwt.com">michael.liu@cwt.com</a>
Jane Ng <i>Partner – Hong Kong</i>	+852 2946 1245	<a href="mailto:jane.ng@cwt.com">jane.ng@cwt.com</a>
Simon Berry <i>Counsel – Hong Kong</i>	+852 2946 1266	<a href="mailto:simon.berry@cwt.com">simon.berry@cwt.com</a>
Viola Jing <i>Senior Associate – Hong Kong</i>	+852 2946 1237	<a href="mailto:viola.jing@cwt.com">viola.jing@cwt.com</a>

*"Cadwalader's lawyers are frequently invited to address the ever-changing competition environment throughout Asia."* – Legal 500

*"Very smart"* work on competition issues in Asia – Legal 500

*"Cadwalader's antitrust leaders are hailed as 'incredibly accomplished and bright' and provide 'U.S. and international antitrust advice to major corporations on bet-the-company matters.'"*  
– Chambers USA

*Antitrust Practice of the Year Award 2014* – Benchmark Litigation