

The 2012 Hong Kong Competition Ordinance

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Introduction and Background

On 22 June 2012, Hong Kong's Competition Ordinance (the Ordinance) was published following approval by the Legislative Council of Hong Kong. The Ordinance introduces a number of important rules and regulations affecting companies operating in the same market or with a significant presence in a market as well as certain business combinations, and provides for significant potential penalties for noncompliance. The Ordinance also creates a Competition Commission (Commission) and a Competition Tribunal (Tribunal) to police those new rules and formulate guidelines regarding their interpretation and enforcement. The Ordinance grants those bodies investigative and enforcement powers.

The Ordinance has three primary areas of focus. The so-called First Conduct Rule regulates agreements that restrict competition in Hong Kong (regardless of where those agreements are negotiated or executed). The Second Conduct Rule (together with the First Conduct Rule, the Conduct Rules) prohibits abusing a substantial degree of market power to restrict competition in Hong Kong (again, regardless of where the conduct itself occurs). In addition, the very limited Merger Rule, at least initially, regulates only those mergers, acquisitions and joint ventures affecting the telecommunications sector in Hong Kong.

Despite its publication, the Ordinance is not yet in full effect. Indications from the secretary for Commerce and Economic Development who is responsible for the initial implementation, suggest that its provisions will enter into force through a staged approach, with the Conduct Rules and Merger Rule becoming effective in the next several months.

Key Aspects of the Ordinance

First Conduct Rule

The First Conduct Rule prohibits agreements that have the intent or effect of preventing, restricting or distorting competition in Hong Kong. The first category of agreements that fall under this rule are "hard-core" restrictions, which are recognized as being harmful in nearly every jurisdiction worldwide. Most prominently, these include agreements among competitors to: (i) agree on prices, rebates or similar contract terms offered to customers; (ii) divide up customers or territories; (iii) reduce output or supply; or (iv) collaborate to rig public bids (for example, through agreements on when to bid or what prices to offer). Hard-core restrictions are subject to a blanket prohibition (and may expose parties to criminal and/or civil sanctions in other jurisdictions as well).

Other types of agreements also will be evaluated under the First Conduct Rule on a case-by-case basis, including ordinary business agreements such as exclusive or selective distribution arrangements, noncompetition provisions, or joint cooperation arrangements for R&D or specialised production. These agreements often will be justifiable on the grounds of pro-competitive efficiencies or lack of harmful impact, but a careful assessment should be undertaken beforehand to evaluate their competitive effects. In addition, where the parties involved have combined total gross worldwide

revenues of less than HK\$200 million (approximately US\$25.8 million), these agreements will be exempted from review entirely.

Second Conduct Rule

The Second Conduct Rule applies to businesses with a powerful presence in a particular market or business sector and prohibits such firms from unfairly excluding other rivals or foreclosing competition. The Second Conduct Rule only applies to businesses with total gross worldwide revenues of more than HK\$40 million (approximately US\$5.15 million) and requires the company to have a “substantial degree” of market power. While the Competition Commission has not yet indicated specific market shares that would indicate a “substantial degree” of market power, the undertaking must be able to operate in a manner essentially independently of its competitors. In particular, the Competition Commission is concerned about “predatory” pricing (that is, pricing below cost to eliminate competitors) and taking measures to reduce innovation or supply in the market.

Merger Control

The Merger Rule establishes a voluntary notification regime that, at least initially, will be limited to mergers, acquisitions and joint ventures involving a business with a telecommunications “carrier licence” issued under Hong Kong’s Telecommunications Ordinance. As part of ordinary regulatory due diligence and evaluation, any such transactions should now also be given a full competition analysis to ensure compatibility with the new Merger Rule.

Penalties and Enforcement Powers

The Ordinance provides the Commission with broad investigatory powers and provides for serious penalties for violations of the Rules. In addition, obstruction of investigations (through, for example, providing misinformation to the Commission or destroying evidence) can expose individuals or businesses to criminal sanctions.

The Commission may apply to the Tribunal to impose a fine for violations of the Conduct Rules. If the Tribunal finds that the Commission has substantiated its case, it may levy fines of up to 10 percent of an infringing firm’s total gross Hong Kong revenues from each year in which the conduct occurred (capped at a maximum of three years).

The Tribunal may make other orders as well, including, among other things: (i) disqualification of individuals from future service as directors, (ii) cease and desist orders; (iii) payment of damages and/or disgorgement of profits; (iv) divestiture orders; (v) rescission orders; and (vi) compulsory supply orders. The Ordinance also introduces the possibility of private damages actions, although these will be limited to actions “following on” a successful prosecution by the Commission.

Under the Merger Rule, the Commission has the power to apply to the Tribunal to block an anticipated telecommunications merger in whole or in part, or even to order the unwinding of a completed merger.

The Commission will also be supported by significant investigative powers. Under the Ordinance, the Commission has the ability not only to compel production of documents, but also to compel individuals to answer questions and, when accompanied by a warrant, to enter into premises to search and seize relevant information (including computer systems and data). Moreover, failure to comply with an investigation, destruction or falsification of evidence, obstruction of a search, and provision of misleading information to the Commission can be prosecuted as criminal offences, carrying fines up to HK\$1 million (approximately US\$130,000) and up to two years imprisonment.

Timing

In order for the Ordinance to enter into force, the Secretary for Commerce and Economic Development must give further notice, which will likely set forth a phased implementation approach. The first provisions likely to enter into force are those regarding the creation of the Commission and the Tribunal. The substantive provisions should follow thereafter, once the Commission has been formed and has had an opportunity to draft relevant implementing and enforcement guidelines. Given this timetable, the substantive provisions of the Ordinance are not expected to come into force until late 2013 or 2014.

Conclusion

It will still take some time before the Ordinance comes into force and before official guidelines, decisional practice and case law clarify exactly how it will be applied. Businesses should take advantage of the current transitional period to refresh (or introduce) effective competition compliance programmes to be prepared as this new competition regime develops.