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COMPETITION TRIBUNAL'S FIRST DECISIONS: SIX KEY TAKEAWAYS

On 17 May 2019, the Competition Tribunal (Tribunal) handed down its judgments in Hong Kong's first two competition cases involving bid-rigging, market sharing and price fixing. As the President of the Tribunal laid down important principles in respect of the interpretation and application of the Competition Ordinance (Cap. 619) (Ordinance), Hong Kong is beginning to build its own body of precedents in competition law.

BACKGROUND

The judgments cover the first two cases brought by the Competition Commission (Commission) under the Ordinance. In both cases, the Commission was alleging an infringement of the First Conduct Rule which prohibits businesses from "*making or giving effect to an agreement, engaging in a concerted practice, or making or giving effect to a decision of an association, if the object or effect is to harm competition in Hong Kong*". In both cases, the Commission was seeking a declaration of contravention; a pecuniary penalty and costs.

The judgments do not address the issues of penalties or costs (which will be dealt with subsequently), but do uphold the Commission's contention that the various respondents in the two cases (with one exception) participated in conduct that infringed the First Conduct Rule.

Competition Commission v. Nutanix Hong Kong Ltd and Others [2019] HKCT 2 concerns a tender issued by the Hong Kong Young Women's Christian Association (YWCA) relating to the installation of a Nutanix server system. Nutanix agreed with BT Hong Kong Limited (BT) that it would assist BT by obtaining dummy bids from other IT companies, so as to satisfy YWCA's procurement policy which required a minimum of five bids for a tender. As a result, SiS, Innovix and Tech-21 each submitted a bid with substantially higher bid prices than BT's. The Tribunal found that all respondents (with the exception of SiS) acted in contravention of the First Conduct Rule under the Ordinance. Further, the agreements among them fell within the definition of bid-rigging and constituted "serious anti-competitive conduct". Accordingly, the Commission was not required to issue a warning notice to any of the respondents before issuing the proceedings.

Competition Commission v. W. Hing Construction Co Ltd and Others [2019] HKCT 3 concerns decoration works undertaken in a public housing estate. Ten companies, which were decoration contractors approved by the Hong Kong

Key issues

- The criminal standard, i.e. proof beyond reasonable doubt, is to be applied to Tribunal proceedings where the Commission seeks to impose a fine.
- An undertaking can be held liable for the infringing conduct of its employees, provided that there is a sufficient connection between the acts of the employee in question and the undertaking.
- Under the "by object" test, the question is whether an agreement entails such a sufficient degree of harm to competition that no additional examination needs to be made on whether it has anti-competitive effects.
- A respondent that seeks to invoke the efficiency defence bears the burden to prove such defence on the balance of probabilities.
- A company and its sub-contractors could be considered as a single undertaking, both of which could be held liable for contraventions of the Ordinance.
- The Commission is not required to issue a warning notice if it has reasonable cause to believe that the contravention involves "serious anti-competitive conduct".

Housing Authority (HKHA), allocated among themselves designated floors in the buildings and jointly produced a flyer setting out the package prices offered. The Tribunal found that the conduct of the respondents consisted of allocation of market for the supply of services and price-fixing, and accordingly they acted in contravention of the First Conduct Rule, notwithstanding the respondents' arguments that this conduct was justifiable on efficiency grounds.

In this briefing we set out the six key takeaways from the two decisions.

1. STANDARD OF PROOF

It was accepted by the parties in the *Nutanix* case that these proceedings involved the determination of a criminal charge for the purposes of Art 11 of the Bill of Rights. The Tribunal considered that it was bound by the Court of Final Appeal's decision in *Koon Wing Yee v Insider Dealing Tribunal* (2008) 11 HKCFAR 170 and confirmed that the criminal standard, i.e. proof beyond reasonable doubt, is applicable, at least where the Commission is seeking a pecuniary penalty.

Although the higher standard of proof adopted may impact on the Commission's future enforcement actions, the success of the Commission in these two actions helps to demonstrate that this obstacle is not insurmountable. The various investigation tools of the Commission, in particular the ability to obtain evidence from a leniency applicant, would also assist it in proving its case before the Tribunal. At the time of writing, the Commission is still able to appeal this point.

2. ATTRIBUTION OF CONDUCT AND KNOWLEDGE OF EMPLOYEES

In the *Nutanix* case, SiS contended that it was a junior employee who privately agreed to and did submit a bid in its name, and that his conduct was outside his scope of work and authority. The Tribunal held that the junior employee's conduct was not attributable to SiS.

The President of the Tribunal rejected the strict approach advanced by the Commission that an undertaking is responsible for the acts of its employees carried out during their employment, irrespective of the responsibilities and authority normally conferred on such employees. On the other hand, he was of the view that the policy of the statute would be undermined if an undertaking is only liable for an employee's acts that are specifically authorised by or known to senior management. It would be easy to bypass the restrictions if an employer could be exonerated simply on the basis that an employee's conduct is contrary to or prohibited by the employer's policies or instructions.

It follows that there must be a sufficient connection between the acts of the employee in question and the undertaking so that the former can properly be regarded as part of the latter in the relevant context. Where the employer has put the employee in a position to do the kind of acts in question, it will be fair to conclude that the employer has engaged in economic activity through the employee and is answerable for the manner in which the employee has conducted himself in that appointment.

After all, the obligation is placed on the undertaking to provide effective preventive measures and to organise its affairs in such a way as to avoid infringements. Although providing adequate trainings and guidance to employees is not itself an answer to potential infringement actions, such measures would be necessary to raise the awareness of competition law issues

within an undertaking. In addition, adopting a clear delineation of authority and effective reporting functions within an undertaking may help to mitigate the risks arising from opportunistic actions of individual employees.

3. APPLICATION OF THE "BY OBJECT" TEST

The First Conduct Rule prohibits conduct where "*the object or effect is to harm competition in Hong Kong".* It is well established that under the "by object" test, the question is whether an agreement entails such a sufficient degree of harm to competition that no additional examination needs to be made on whether it has anti-competitive effects.

In the *Nutanix* case, the respondents (who were mainly resellers or distributors of Nutanix) other than BT had apparently agreed to submit "dummy" bids to YWCA simply as a favour to Nutanix given that YWCA's first tender did not generate enough bids to allow it to proceed. Also, BT had apparently not increased its bid after YWCA's first (unsuccessful) tender. In light of this, Nutanix argued that the agreements in question did not contain the "typical features" of bid-rigging, such as (i) increased or controlled price; and (ii) a trade-off or *quid pro quo* for the other participants who would not win the tender in question. The President of the Tribunal held that these features were not necessary ingredients of a restriction by object or bid-rigging.

In the *W. Hing Construction* case, the Tribunal confirmed that both market sharing and price fixing behaviour are properly characterised as agreements that restricted competition by their object.

The decisions serve as a useful reminder to businesses as to which types of conduct are considered to have the object of preventing, restricting or distorting competition. In addition to bid-rigging, price fixing and market sharing, the practice of cover pricing[1] is also generally regarded as an infringement of competition law and should be avoided. The Tribunal emphasised that a company running a tender process has the right to expect that those participating in the tender are bona fide bidders who have not sought to influence the outcome of the tender through direct or indirect contact.

4. APPLICATION OF THE EFFICIENCY DEFENCE

The *W. Hing Construction* case provides important guidance on the application of the efficiency defence, as the contractors argued that there were savings in labour costs and raw material delivery costs and efficiencies had been gained from focused marketing efforts.

The Tribunal held that the respondents bear the persuasive burden to bring themselves within the exclusion in the form of the efficiency defence. The standard of proof of such defence is on the balance of probabilities.

The test of the efficiency defence consists of four conditions: (i) the agreement generates efficiencies; (ii) it allows consumers a fair share of the resulting benefit; (iii) it does not impose restrictions that are not indispensable to the attainment of the objectives; and (iv) it does not afford the undertakings concerned the possibility of eliminating competition. On the evidence adduced by the respondents, none of these four conditions was satisfied.

[1] Cover pricing refers to a practice that occurs where a company wishes to be seen to tender for a particular contract but in fact does not wish to win the tender. The company then seeks a cover price from another company such that the price it submits will be sufficiently high to ensure that it does not win.

The proof of an efficiency defence has always been notoriously difficult in other jurisdictions. The present case has highlighted the difficulty in advancing a coherent version of facts where the respondents first denied that there was a price fixing agreement, then sought to make an alternative argument on the basis that such agreement was necessary to deliver efficiencies from which their customers benefited. The reliability of the expert's analysis in this case has also been put into question. It seems that economic experts within the city would have to familiarise themselves with the Tribunal's expectation and be prepared to provide a well-reasoned opinion to assist the Tribunal's analysis in the future.

5. LIABILITY FOR THE SUB-CONTRACTOR'S ACTIONS

In the *W. Hing Construction* case, two of the respondents contended that the renovation business in question was carried out by a separate undertaking; they only let their names be used by their respective sub-contractors.

The Tribunal considered various factual matters, including that the licence granted by HKHA was offered to and signed by the respondents, the terms of the licence made clear that it was the respondents who would be carrying out the decoration works, the decoration works were promoted in the name of the respondents etc. Although the sub-contractors bore the risk of profit and loss on the decoration business, the respondents were the contracting parties *vis-à-vis* HKHA and the tenants of the housing estate; they assumed the risks externally. Accordingly, the respondents were comprised in the undertakings that were engaged in the provision of decoration services.

The decision sends an important warning to businesses. The definition of "undertaking" and the operation of "single economic unit" concept mean that companies would have difficulties availing themselves of the usual shield of separate legal entity. One may wish to consider putting in safeguards to ensure compliance with the Ordinance by sub-contractors and agents, and to introduce indemnities where such third parties' unauthorised actions attract investigation or prosecution by the Commission.

6. ISSUANCE OF WARNING NOTICE

The requirement of warning notice only arises if the Commission has reasonable cause to believe that the contravention does *not* involve "serious anti-competitive conduct". As defined in the Ordinance, bid-rigging is a type of "serious anti-competitive conduct".

In the *Nutanix* case, the Tribunal accepted that definition of bid-rigging entails that the agreement in question had to be one that was not made known to YWCA before those bids were submitted. It found that although a staff member of YWCA did understand BT contacted Nutanix who would help and try to get in some bids, he had no knowledge that the bids being procured were deliberately prepared to ensure they would be unsuccessful. On the facts of the case, there was no reasonable cause for the Commission, as at the date of commencement of proceedings, to believe that the agreements in question had been made known to YWCA. Accordingly, the Commission was not required to issue a warning notice to any of the respondents before issuing the proceedings.

The Tribunal's decision has helped to clarify the operation of the warning notice, which is a unique feature of the Hong Kong competition law regime.

CONCLUSION

The judgments in Hong Kong's first two competition cases represent an important milestone in combatting anti-competitive conduct in Hong Kong. The Commission's success in these two actions is likely to mark the beginning of further enforcement actions.

We wait to see the penalties to be imposed in these actions, as such matters are to be determined after a further hearing. It will be interesting to see what mitigating factors may be submitted by the respondents, and how the Tribunal approach the penalty issue, so as to strike a right balance between the individual circumstances of the respondents and the need to uphold the deterrence effect of the local regime.

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