

## HONG KONG COMPETITION TRIBUNAL FINES CONTRACTORS FOR PRICE FIXING AND MARKET SHARING

The Competition Tribunal recently handed down its first decision on pecuniary penalties under the Competition Ordinance. Total penalties of almost HK\$4 million were imposed on ten contractors for making and giving effect to a market sharing arrangement and a price fixing arrangement while providing decoration services to tenants at a public housing estate.

### BACKGROUND

The detailed background of this case and the Competition Tribunal's (**Tribunal**) analysis of the respondents' conduct were set out in our previous [client briefing](#) discussing Hong Kong's first competition cases determined by the Tribunal.

On 17 May 2019, the Tribunal found that the ten respondents in question contravened the First Conduct Rule, as they allocated among themselves designated floors in the buildings of a public housing estate and jointly produced a flyer setting out the package prices offered. The orders sought by the Competition Commission (**Commission**) included a pecuniary penalty under section 93 of the Competition Ordinance (Cap 619) (**Ordinance**) in respect of each contravention; an order under section 96 of the Ordinance for the respondents to pay the costs of and incidental to the investigation into their conduct, and costs of the proceedings in the Tribunal. These matters were heard by the Tribunal on 14 to 16 January 2020.

In the latest judgment [\[2020\] HKCT 1](#), handed down on 29 April 2020, the Tribunal set out important guidance for assessing the pecuniary penalties to be imposed under the Ordinance as well as principles applicable to the determination of costs orders.

### THE USE OF A STRUCTURED AND METHODOLOGICAL APPROACH

The Ordinance does not spell out the specific approach or methodology for assessing pecuniary penalties; section 93(2) simply sets out the general factors the Tribunal must have regard to, namely: (a) the nature and extent of the conduct that constitutes the contravention; (b) the loss or damage, if any, caused by the conduct; (c) the circumstance in which the conduct took place, and (d) whether the person has previously been found by the Tribunal to have contravened the Ordinance.

#### Key issues

- The Hong Kong Competition Tribunal has set down a four-step structured and methodological approach in assessing pecuniary penalties for anti-competitive conduct.
- The approach to costs orders used in civil court proceedings is applicable to proceedings commenced by the Competition Commission.
- Undertakings may be ordered to pay for the Commission's investigation costs if the Commission provides sufficient evidential basis to justify why such order should be made.

The Tribunal considers that the Ordinance's object of deterrence is best served in Hong Kong by a structured and methodological approach for the determination of pecuniary penalties. The Tribunal accordingly developed four main steps for such determination, simplifying the approach proposed by the Commission, which is based very closely on the EU and UK approaches:

Step 1: Determining the base amount;

Step 2: Making adjustments for aggravating, mitigating and other factors;

Step 3: Applying the statutory cap; and

Step 4: Applying cooperation reduction and considering plea of inability to pay, if any.

## **STEP 1: DETERMINING THE BASE AMOUNT**

The base amount, is intended to reflect one of the mandatory considerations set out in section 93(2) of the Ordinance, namely the nature and extent of the conduct which constitutes the contravention. It is calculated as:

Value of Sales x Gravity Percentage x Duration Multiplier

The Value of Sales is the value of the undertaking's sales directly or indirectly related to the contravention in the relevant geographic area within Hong Kong in the financial year in question. In this case, the Value of Sales was calculated by the Commission based on each Respondent's work orders and invoices issued for the renovation works at the public housing estate in question.

A Gravity Percentage provides a broad scale to reflect the gravity and blameworthiness of the conduct. For serious anti-competitive conduct (which includes conduct such as price fixing, market sharing and bid-rigging), the range of 15% to 30% is applicable. In this case, the Tribunal adopted a gravity percentage of 24%, taking into consideration that these cartel arrangements represented some of the most serious kinds of collusive conduct; the decoration works carried out by the respondents represented a substantial market share; the contractors involved were primary contravenors as opposed to persons involved in contravention by others; the conduct in question targeted and affected low income tenants from public rental housing estates, and that the Hong Kong Housing Authority had expressly warned the respondents not to engage in "pie sharing".

The Duration Multiplier is to reflect the temporal extent of the conduct in question. This is intended to provide an incentive for an infringing undertaking to cease its contravention as soon as possible. In this case, a Duration Multiplier of 1 was adopted, although the conduct in question only lasted for 5 months. The Tribunal, however, did not consider it necessary to decide, as a matter of principle, whether it is possible to have a Duration Multiplier of less than 1 where the total duration of an infringement is less than one year.

## **STEP 2: MAKING ADJUSTMENTS FOR AGGRAVATING, MITIGATING AND OTHER FACTORS**

Encompassed within this stage are the section 93 mandatory considerations of (i) the circumstances in which the conduct took place (including aggravating and mitigating factors); (ii) the loss or damage, if any, caused by the conduct, and (iii) whether the person in question has previously been found to have contravened the Ordinance.

The Commission submitted that there were two aggravating factors present: (1) in respect of two of the respondents, there were directors and senior management involved in the contravention, and (2) there was evidence that the anti-competitive arrangements found in this case reflect long-running and widespread industry practice. However, the Commission did not invite the Tribunal to make upward adjustments for these factors.

As for mitigating circumstances, some of the respondents submitted that they did not directly participate in the conduct impugned, but that each of them became liable only as a result of letting their "licence" to a "subcontractor" who was found to have engaged in the infringing conduct. To reflect the more limited role of these respondents, the Tribunal allowed a reduction of the Base Amount by one-third.

However, the Tribunal did not accept as mitigating factors that the respondents were undertakings that were small in size and turnover, or that the Ordinance was a new law and there was genuine uncertainty about its application to the arrangement in question.

### **STEP 3: APPLYING THE STATUTORY CAP**

A statutory cap is provided for in section 93(3) of the Ordinance. A pecuniary penalty may not exceed 10% of the turnover of the undertaking concerned for each year in which the contravention occurred or, if the contravention occurred for more than 3 years, 10% of the turnover of the undertaking concerned for the 3 years in which the contravention occurred that saw the highest, second highest and third highest turnover.

The term "turnover" is defined to mean the total gross revenues of an undertaking obtained in Hong Kong, and "year" means the financial year of an undertaking.

The Tribunal reminded that the statutory cap is calculated by reference to overall turnover of an undertaking, not the value of the kind of sales affected by the infringement.

The application of the statutory cap had an effect on seven of the ten respondents upon which the maximum pecuniary penalty allowed under the Ordinance was imposed. This was mainly because these respondents were small companies, as the statutory cap is calculated by reference to overall turnover. For each of the three larger companies, the penalty ultimately imposed represented 2 to 31% of the statutory cap. Overall, without the cap, the Commission was seeking HK\$8,117,744, whereas the Tribunal would have ordered HK\$6,366,000. With the cap, the pecuniary penalty ultimately ordered was HK\$3,970,000.

### **STEP 4: APPLYING COOPERATION REDUCTION AND CONSIDERING PLEA OF INABILITY TO PAY**

The final step involves the application of a reduction to reflect any cooperation with the Commission. The cooperation reduction that the Commission will recommend is the sum of discounts determined in accordance with the Commission's [Cooperation and Settlement Policy for Undertakings Engaged in Cartel Conduct](#) (April 2019). Although there was no claim for reduction for cooperation in the present case, the Tribunal set out the following general principles:

1. The Tribunal, as an independent tribunal, is not bound by any such recommendation of the Commission.

2. The Tribunal may, however, properly have regard to the Commission's recommendation bearing in mind the policy justifications.
3. It is appropriate that the cooperation reduction is dealt with after applying the statutory cap, to ensure that there is still a real benefit to offer cooperation even if the pecuniary penalty is already limited by the statutory cap.

In terms of pleading inability to pay, one of the respondents asked for a 40% discount to the proposed penalty on the basis that the level of penalty recommended by the Commission would cause it financial hardship. To make out a case of financial hardship, the Tribunal considered it necessary for the respondent in question to produce clear and comprehensive evidence of its financial position. The audited financial statements relied on by the respondent in this case was insufficient to justify a reduction of the penalty on account of inability to pay.

## **COSTS ORDERS**

The Tribunal considered that the general rule in civil proceedings, namely that costs follow the event or the unsuccessful party pays, should apply. Mindful that this was one of the first cases in the Tribunal, and that more costs were incurred because of the novelty of the law, the Tribunal considered it appropriate to apply a 20% reduction to the costs payable by the contractors to the Commission. Apart from the costs attributable to the efficiency defence (which only fell on the contractors who had run such defence), the ten respondents were each to pay one-tenth of 80% of the Commission's costs of this action.

Whilst under section 96 of the Ordinance, the Tribunal may order a person contravening competition rules to pay the investigation costs incurred by the Commission, the Tribunal expressed that it is for the Commission to justify why such order should be made. There ought to be some materials provided in advance of the hearing to show the heads of investigation costs claimed, what activities they cover, their very approximate amounts, how they constitute costs of and incidental to the investigation into the conduct or affairs of the respondents, and why they should be regarded as having been reasonably incurred. In the absence of such evidential basis for the exercise of the Tribunal's discretionary power, the Tribunal refused to award the Commission's investigation costs in the present action.

## **CONCLUSION**

This judgment has offered certainty, clarity and transparency in respect of the assessment of the pecuniary penalty in Tribunal proceedings and explained in detail the matters that will be taken into consideration by the Tribunal.

It is relevant to note that the fact that the Tribunal imposed the maximum amount on seven respondents is mainly because those respondents were small companies. For the three larger companies, the Tribunal declined to follow the Commission's recommendation and the eventual fines were significantly lower (by over HK\$1 million across the three companies) than the Commission had sought. Nevertheless, the judgment reflects the importance of compliance with the competition law regime in Hong Kong and the punishment that may result from a contravention of the First Conduct Rule.

Apart from pecuniary penalties, there are still a wide range of tools that the Tribunal and the Commission may employ to deter wrongdoers. Although the

respondents were not ordered to pay the Commission's investigation costs in this case, the Tribunal made it clear that the threshold for the Commission to justify such a costs order may not be very high so long as it is supported by some evidential basis. It will also be interesting to see how the Tribunal will apply other types of non-pecuniary penalties, such as a director disqualification order or an order that a respondent adopt certain compliance measures, in other enforcement proceedings that are going to come before the Tribunal in the near future.

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