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On the Competition Law Regime and Conglomerates in Hong Kong

Introduction

One of the most notable features of the economy of Hong Kong is the dominance of a small number of large conglomerates that is seen across various industries, such as food, real estate, transport, and telecommunications.[1] As conglomerates may distort competition in many ways,[2] it is important to examine the ways in which competition law regulates conglomerates in Hong Kong. This paper embarks on such examination and further proposes dwsirable changes to the competition regime.

This paper is divided into three parts. First, it discusses the available tools the HKCC currently has under the Competition Ordinance ("the Ordinance") to address anticompetitive behaviours of conglomerates. Second, it analyses the ways in which the conglomerates are not subject to competition laws and proposes changes to the current competition law regime of Hong Kong. Third, this paper asserts that while changes should be made, there remains a balance that needs to be struck between the domestic and the international competition concerns.

A. Available Tools

I. Anticompetitive Agreements, Concerted Practices and Decisions

As Thomas K. Cheng notes, 'existing competition law is well equipped to tackle [the multifirm conducts of conglomerates]'.[3] The multifirm conducts that are regulated under the competition law regime of Hong Kong include anticompetitive agreements, concerted

[1] Williams, Mark *Competition Policy and Law in China, Hong Kong and Taiwan* Cambridge: Cambridge University Press 2009 p. 237.
[2] Cheng, Thomas K. "Sherman vs. Goliath?: Tackling the Conglomerate Dominance Problem in Emerging and Small Economies—Hong Kong as a Case Study" 37(1) Northwestern Journal of International Law & Business 2017, p. 35. Note that this paper does not to suggest that all conglomerates distort competition. However, as Cheng points out, 'conglomerates are better positioned than other firms to perpetrate [distortion of competition]'. Ibid., p. 58.
[3] Cheng, p. 58.

practices and decisions that have the object or the effect of preventing, restricting or distorting competition in Hong Kong, subject to the general exclusions from conduct rules listed in Schedule 1 of the Ordinance.[4] For instance, if a conglomerate engages in anticompetitive agreements such as price fixing, market sharing, output restrictions, or bid-rigging, it may amount to a contravention of s. 6 subject to the relevant exclusions.

It is worth noting that s. 6 of the Ordinance 'prohibits relevant agreements between undertakings rather than between persons.'[5] If, for instance, a conglomerate consists of subsidiaries that engage in serious anti-competitive agreement with each other such as price fixing, market sharing, output restrictions, and bid-rigging, they are not subject to s. 6 of the Ordinance as they are within an undertaking, or, using the European terminology, a single economic unit. In this sense, then, the concept of single economic unit can be said to be a shield for conglomerates that conduct anticompetitively *within* themselves.

II. Abuse of Market Power

The HKCC may also address the anti-competitive behaviours of conglomerates with substantial market power that result in foreclosure by relying on s. 21 of the Ordinance, which addresses abuse of market power. S. 21 of the Ordinance applies to any conduct that has the object or effect of preventing, restricting or distorting competition in Hong Kong even if the conglomerate engage in the conduct is outside Hong Kong or the conduct is engaged in outside Hong Kong. This is subject to certain general exclusions listed in Schedule 1.[6]

[4] Section 1 of the Schedule excludes agreements that enhance overall economic efficiency, allow consumers a fair share of the benefits, are reasonably necessary and give no possibility of eliminating competition the benefits; s. 2 concerns agreements that are for the purposes of compliance with legal requirements; s. 3 excludes services of general economic trust as entrusted by the Government; s. 4 excludes agreements under the first conduct rule and conducts under the second conduct rule that result in mergers; s. 5 excludes agreements between undertakings with a combined turnover of not exceeding $200 million that do not involve serious anti-competitive conduct.

[5] *Competition Commission v W. Hing & Ors* CTEA 2/2017 at [302].

[6] This is with the exception of s. 1, which cannot be relied on for abuse of market power. Additionally, instead of s. 5 of Schedule 1, the relevant section here is s. 6, which excludes conduct engaged in by an undertaking with a turnover of not exceeding $40 million.

Conglomerates with substantial market power in Hong Kong may raise anticompetitive concerns specifically in the area of abuse of dominance due to the range of products offered that strengthen their incentives to conduct tying. In contrast to firms that only have related products in a few markets, conglomerates that are in a wide range of markets have more opportunities to tie their products such that they are subject to s. 21 of the Ordinance.[7]

Moreover, conglomerates also have strong incentives to pursue predatory pricing. Given its financial resources, conglomerates can cross-subsidise their businesses in other markets and therefore cope with the predation period of predatory pricing better than equally efficient targets with weaker financial strengths.[8]

Such concerns are more than a theoretical possibility. In Hong Kong, the two dominant players in the food retail industry, Park'N Shop and Wellcome, are each controlled by a conglomerate that also has businesses in housing developments that include supermarket sites.[9] When adMart, a new entrant, operated without a store and started to provide free home delivery in 1999, Park'N Shop and Wellcome responded by offering the same services and reducing the prices of certain goods.[10] Within eighteen months, adMart left the market,[11] and Park'N Shop and Wellcome then reduced the scale of the free home delivery services before starting to charge for it.[12] Though it remains debatable as to whether such conduct has amounted to predatory pricing,[13] it nonetheless has demonstrated how conglomerates are better financially equipped than their competitors.

[7] Cheng, p. 68.
[8] Ibid., p. 58. Williams, p. 241. For criticisms and further discussions of the conglomerates' having more financial resources, see Cheng p. 67.
[9] Williams, p. 247.
[10] Ibid, p. 248.
[11] It is worth noting that while the Guideline on the Second Conduct Rule has suggested that anticompetitive foreclosure may be found even where competitors have not actually exited the market, whether the Tribunal accepts this approach remains unclear.
[12] Williams, p. 248.
[13] Ibid.

Furthermore, by pursuing predatory pricing in one market, conglomerates may gain itself the reputation as a strong competitor in other markets they are in, which may in turn disincentivise their competitors from competing with them and potential entrants from entering into the market.[14] Conglomerates therefore have the incentives to pursue predatory pricing as they not only are better equipped to cope with the loss during the predation period, but also can they benefit from their reputation as a predator.

III. The Merger Rule

Conglomerates may be subject to s. 177, Schedule 7 of the Ordinance where they are involved in anticompetitive mergers in the telecommunications industry. The Merger Rule in Hong Kong currently only applies to mergers involving an undertaking that, directly or indirectly, hold a carrier licence issued under the Telecommunications Ordinance.

B. Gaps and Desirable Changes

While HKCC has certain available tools to address the anticompetitive concerns caused by the conglomerates in Hong Kong, there are ways in which conglomerates are not subject to the competition law regime and changes that may be desirable. Such is what this paper now turns to.

I. Superior Bargaining Positions

First and foremost, it may be desirable to put in place rules that regulate abuse of superior bargaining position like Korea.[15] Conglomerates that do not have substantial market power may nonetheless have superior bargaining positions that could raise anticompetitive concerns. When a firm works with several businesses of a conglomerate, the conglomerate may abuse its strong bargaining power and impose exploitative contractual terms on the firm.[16] The enforcements of such regulation on conglomerates in Korea, such as the LG Group and Lotte.com which is part of the Lotte Conglomerate, suggest that it would be an

[14] Cheng p. 68. For debates on the extent to which conglomerates may deter new entry, see Cheng p. 71-72.
[15] Article 23 of the South Korean Monopoly Regulation and Fair Trade Act (MRFTA).
[16] Cheng, p. 69.

effective tool to prevent competition from being distorted by the contractual terms imposed by conglomerates in Hong Kong that, while not having substantial power, may act anticompetitively through their superior bargaining positions.

II. Cross-Subsidisations

Second, as previously noted, conglomerates may cross-subsidise their businesses in other markets. While HKCC may address the anticompetitive effects through s. 21 of the Ordinance if the cross-subsidisation results in abuse of dominance, cross-subsidisation itself is not regulated. Whereas cross-subsidisation may be procompetitive where it allows a conglomerate to enter into a new market more efficiently,[17] at the same time, its potential anticompetitive effects should not be overlooked. As analysed, it may allow the conglomerates to abuse their dominance in various markets, and it is clearly more than a theoretical possibility that an inefficient conglomerate would be able to stay in a market due to cross-subsidisation, which arguably not only distorts competition but also misallocates resources.[18]

Therefore, it may be desirable to regulate the internal transactions of the conglomerates. Just as Korea,[19] it may be possible to regulate the area of debt guarantees. The businesses within conglomerates may obtain credit more easily because their affiliates would be able to provide guarantee, thereby unfairly placed at a better position than their competitors.[20] Whether debt guarantees by conglomerates should be per se illegal remains debatable, and further assessment needs to be conducted in order to determine the proper level of such intervention in Hong Kong. As this would be a relatively radical intervention in the competition law regime of HK, incremental steps should be taken.

III. Formation of Conglomerates through Mergers

[17] Cheng, p. 73.
[18] Ibid.
[19] Articles 10-2 of The Monopoly Regulation and Fair Trade Act.
[20] Cheng, p. 78.

Third, there is a lack of tools in the area of the formation of conglomerates through mergers where telecommunication industry is not involved. Currently, if a merger leads to the formation of a conglomerate but it does not involve the telecommunications industry, HKCC has no jurisdiction over it whatsoever even if the formation of the conglomerate through mergers will substantially lessen competition in Hong Kong.[21] Rather than addressing the anticompetitive conducts of the conglomerates, it is perhaps more effective to address the anticompetitive concerns that may arise as soon as a conglomerate is formed. Therefore, in order to effectively regulate the formation of conglomerates, it is strongly desirable to have a merger control regime that expands beyond the telecommunication industry.

IV. Parental Liability

Fourth, it is desirable to introduce the European concept of parental liability, which can be a powerful tool to regulate conglomerates. Under the concept of parental liability, the parental undertaking can be held jointly and severally liable for the anticompetitive conducts of any business within the conglomerate.[22] As a result, penalty is calculated according to the turnover of the parental undertaking rather than the subsidiary within a conglomerate. Introduction of such concept would transform 'single economic unit' from a shield in the context of first conduct rule to a sword directed at conglomerate's liability in Hong Kong in general. The huge penalties that result from parental liability can encourage conglomerates to implement effective compliance programmes to ensure none of the business would engage in anticompetitive conducts that the parental undertakings would be liable for.

[21] It is worth noting that it is impossible for the HKCC to rely on s. 21 to prevent the conglomerates from being formed through mergers in the first place. s. 21 is the equivalent of Art. 102 of the TFEU that addresses the abuse of dominance. Whereas Art. 102 has been held to apply to mergers before EU Merger Regulation emerged and it has been noted that an alteration of the competitive structure of a market where the dominant undertaking already weakens the market may amount to an abuse under Article 102, s. 4 of Schedule 1 of the Ordinance has clearly indicated that a conduct is excluded from the second conduct rule if it results in mergers. Therefore, while it is the case in EU that a merger may amount to an abuse of dominance, such is not the case in Hong Kong, where s. 21 cannot be used to bar the formation of conglomerates. For the European approach see *Continental Can v Commission*. Such approach has also been seen be seen in *Tetra Pak I (BTG Licence)* and *Servier*. Whish, Richard and Bailey, David *Competition Law* Oxford, Oxford University Press 2018 p. 729

[22] "European Court of Justice confirms Commission's approach on parental liability" 1 Competition Policy Newsletter 2010.

C. Domestic and International Competition Concerns

Through an examination of the tools the HKCC has to address conglomerates in Hong Kong as well as the desirable changes, this paper has demonstrated that while certain tools are available, they are rather limited. Indeed, there is room for more regulations to come into play in order to regulate the conglomerates more effectively. However, far from suggesting that the changes should be made immediately without taking any other factor into account, this paper only suggests that they are desirable. The close tie between various conglomerates in Hong Kong and the international market begs the following question: should changes be made if the conglomerates would no longer be able to compete on the international level and Hong Kong would be less internationally economically competitive as a result?

The hint – if not the answer – can perhaps be found in the Singaporean practice. Setting out the functions and duties of the Competition and Consumer Commission of Singapore, s. 6 of the Singaporean Competition Act prioritises the maintenance and enhancement of 'overall productivity, innovation and competitiveness of markets in Singapore'[23] over domestic competition concerns. Such emphasis on the international competitiveness provides a different anchor of competition law. This is, of course, not to suggest Hong Kong can necessarily be more internationally economically competitive by imposing less regulations on conglomerates.[24] Rather, where the conglomerates in Hong Kong can maintain or even enhance the overall competitiveness of Hong Kong, they should not, perhaps, be subject to further restrictions in light of the Singaporean perspective.

While it is not necessarily ideal for Hong Kong to adopt the exact same practice as Singapore, it nonetheless brings the significance of striking a balance between domestic and international competition concerns to light. When bringing about changes to regulate conglomerates in Hong Kong, the suitability of the changes should be holistically assessed,

[23] s. 6 of the Competition Act.
[24] See, for instance, the negative impact that the lower level of domestic competition can have on Hong Kong's overall competitiveness in Williams, p. 243, p. 281-283.

steps should be taken incrementally, and the balance between domestic and international competition concerns should be struck.

Conclusion

This paper has shown that currently, the HKCC have certain tools to address the anticompetitive conducts of the conglomerates, such as ss. 6 and 21 of the Ordinance. Yet there are anticompetitive concerns that remain unaddressed by these tools, including the superior bargaining positions, the cross-subsidisations, formation of conglomerates through mergers and parental liability. This paper has proposed changes that are desirable if these anticompetitive concerns are to be addressed. However, the changes are not necessary per se. While they are desirable, the exact way of implementing these changes should strike a balance between the domestic and international competition concerns.