

Hong Kong Liner Shipping Association

Supplementary Submission to Hong Kong Competition Commission

Case Number: BE/0004

NON-CONFIDENTIAL VERSION

1. Introduction

1.1 Having considered the Preliminary Statement of Views of the Competition Commission (the “**Commission**”) dated 14 September 2016 (the “**Statement**”), the Hong Kong Liner Shipping Association (the “**Applicant**”) believes that, as demonstrated in its response to the Statement, dated 14 December 2016 (the “**Consultation Response**”), both vessel sharing agreements (“**VSAs**”) and voluntary discussion agreements (“**VDAs**”) meet the standards for an exemption under the Competition Ordinance (Cap. 619 of the Laws of Hong Kong) (the “**Ordinance**”). Nonetheless, in the event that the Commission remains of the view that VDAs in their current form do not meet the standards for an exemption under the Applicant’s suggested broader approach, the Applicant hereby requests that the Commission consider granting a block exemption order for VDAs under a revised scope (the “**Revised VDA Scope**”) specifically by:

- (A) expressly carving-out any Hong Kong-specific pricing (including rates and surcharges) discussions and voluntary agreements within VDAs, but
- (B) permitting the discussion and sharing of certain types of information among VDA members relating to the shipping industry, including supply and demand forecasts, vessel utilisation and capacity levels, carrier costs, trade growth and development and international cargo flows (discussed in more detail in section 2 below).

1.2 The Applicant understands that the Commission’s greatest concerns regarding VDAs relate to discussions and voluntary agreements on pricing (including rates and surcharges). Notwithstanding the Applicant’s position that such activities meet the four conditions in section 1 of Schedule 1 to the Ordinance (the “**Efficiencies Exclusion**”), [...] the Revised VDA Scope would exclude pricing discussions, whilst continuing to allow non-pricing information relevant to Hong Kong to be discussed and exchanged between VDA members, thus helping to keep Hong Kong competitive vis-à-vis competing regional ports. It would also provide an exemption for a portion of the VDA authority that is common and permitted by other regulatory regimes around the world.

1.3 In this submission, we explain in detail:

- (A) how each of the four conditions of the Efficiencies Exclusion are met by the Revised VDA Scope; and
- (B) how the Revised VDA Scope falls within the Applicant’s original application for a block exemption order for liner shipping agreements, submitted on 17 December 2015 (the “**Application**”),¹ albeit that by adopting the approach in the Revised VDA Scope, the block exemption order would cover VSAs and only selected elements of VDAs, rather than liner shipping agreements in their entirety.

1.4 The Applicant therefore requests that the Commission re-consider its position in the Statement, in view of the additional arguments in this submission, to grant a block exemption order for VDAs under the Revised VDA Scope.

2. What the Revised VDA Scope would cover

¹ For examples, please refer to paragraphs 4.27(A), 7.3(B) and 8.42-8.48 of the Application

- 2.1 The Commission proposed in the Statement to provide a block exemption order for VSAs, but suggested certain safeguards in the form of conditions to its proposed order. Similarly, the Applicant envisages that the Revised VDA Scope would cover VDA activities generally, with a carve-out for Hong Kong-specific rate discussions or recommendations, which would fall outside the scope of any exemption granted by the Commission. For the avoidance of doubt, discussions on the rates for cargo that is merely transhipped through Hong Kong would not fall within the meaning of “Hong Kong-specific rate discussions”. This is because the cargo rates are determined by reference to the origin and destination ports, and not the port through which the cargo is transhipped.
- 2.2 [...]
- 2.3 The particular items that would be specifically authorised for discussion and information exchange under the Revised VDA Scope would include the following: supply and demand trends; carrier costs (general and Hong Kong specific); vessel utilisation and capacity levels; general industry issues; general economic issues/trends; regulatory developments and compliance issues; best practices (general and Hong Kong specific), including service contract rules, terms, conditions; and revenue/rate indices based on aggregated historical data.
- 2.4 The requested exemption under the Revised VDA Scope relates only to the authority to discuss and exchange information with respect to the categories above. The exceptions to this would be the categories for general industry issues, regulatory developments and compliance issues and best practices, for which topics the Applicant also requests that any block exemption order should cover the authority to reach voluntary agreements (for the avoidance of doubt, in no case would any such agreements relate to setting rates or charges). This represents the broad position which we expect to be adopted for the large majority of the VDAs covering Hong Kong. We are currently conducting a detailed review of whether particular VDAs may request additional voluntary agreement authority to be included under the Revised VDA Scope and will discuss this in due course with the Commission if necessary.
- 2.5 A more complete description of all the categories of information proposed to be exchanged and discussed among VDA members under the Revised VDA Scope is provided in paragraphs (A) to (H) below, in order to give the Commission a fuller understanding of what the proposal would involve and why these discussions are beneficial and promote efficiencies. Except where otherwise noted, the categories below would include past, current, and forward-looking data, as well as both individual and aggregated data. As discussed at section 3, because certain of these categories contain potentially competitively-sensitive information, the Applicant sets out further in that section why it would be necessary for the Commission to grant a block exemption order to give carriers the legal certainty they require to continue to discuss these issues without risking any potential contravention of the Ordinance.

(A) *Supply and demand trends*

- (i) As explained at paragraph 4.4 below, at VDA meetings, carriers discuss specific cargo flows and exchange statistics on which port ranges and trade lanes have declining or increasing cargo throughput, both current and forecast. These discussions lead to better individual carrier operational and commercial decisions that reflect true market trends. This avoids waste and inefficiency, and ultimately leads to lower costs and better service to shippers.

- (ii) There are a number of types of data that provide information on supply and demand trends, all of which may be discussed within a VDA, including:
 - (a) Summaries of carriers' existing fleets, including service and vessel information;
 - (b) Carrier data on trade growth and cargo flows;
 - (c) Carrier market share summaries;
 - (d) Expected individual carrier deployments;
 - (e) Expected demand forecasts in the trade; and
 - (f) Carrier summaries of seasonal deployments and/or temporary voided or blank sailings.
- (iii) There are various sources of information that carriers use to make their operational and commercial decisions. Data derived from VDAs are one important source. VDAs may also, for example, circulate information such as third party market analyses, news articles and internal statistics to its members. However, to the extent that the relevant market information is available from such third party sources, the data is often not up-to-date, and is generally less accurate. For this reason, to be most useful, data of these types generally must come from the carriers themselves, and are often only collected and exchanged through VDAs. The information is helpful to carriers because it provides a single and reliable source for these important types of detailed market information.

(B) *Costs (general and Hong Kong specific)*

- (i) The ability to discuss common vessel operating costs is critical to ocean carriers. Because the liner shipping industry provides scheduled transport on specified and fixed trade routes, once a schedule has been agreed upon, numerous cost items such as fuel, documentation, Customs costs, crew wages, equipment, cargo handling, and maintenance and repair become fixed and cannot be avoided. In many cases, the costs are common among carriers serving a particular trade. VDAs provide an important forum to discuss these costs.
- (ii) To use the sharing of information on bunker costs as an example, this is an important component of a carrier's costs and therefore a key input factor in determining pricing. There are generally no other sources that have real-time data on a per container basis in the same way that VDAs do. VDAs will often publish the posted weekly average bunker fuel prices over several weeks. The carrier industry relies to a large extent on the VDAs' collection and distribution of bunker data to formulate their own reasonable and fact-based bunker recovery plans. Moreover, the carriers' customers benefit from this information, as it provides them a single source for the information, as opposed to having to check with numerous individual carriers and reconcile multiple bunker recovery formulas.
- (iii) VDAs often provide cost studies on behalf of their members on issues such as round trip economics, impact of commercial items such as equipment free

time/demurrage extensions, intermodal cost challenges, and which particular costs are rising due to trade conditions. Based on these cost studies, VDAs may make recommendations on how carriers could improve efficiency and reduce certain costs.

- (iv) Another resource that VDAs provide to carriers are “break even” studies, which provide a bottom line revenue figure for a given trade lane based on average vessel operating costs among the VDA members. In light of the economic challenges that carriers have faced over the years, these types of studies have become increasingly important to carriers in terms of ensuring the short and long term sustainability of their businesses.

(C) *Vessel utilisation and capacity levels*

- (i) Vessel utilisation and capacity data is a reflection of supply and demand trends in the trade, and is a key indicator of where the market is currently, and where it is going. Utilisation and capacity data is critically important to carriers in allowing them to better understand the overall market in order to understand and forecast market demand and make necessary decisions to efficiently meet demand at any given time. Utilisation and capacity statistics are more useful the more broadly they are sourced. By allowing exchange of vessel utilisation and capacity information between carriers in the market, VDAs provide carriers with a better and more accurate picture of the supply and demand trends in that trade than would otherwise have been available based on their own data alone. In making strategic investment decisions or, more frequently, routine operational decisions such as slot arrangements, it is helpful for carriers to have access to such information, which is generally not available outside of VDAs.
- (ii) Utilisation statistics are also more useful where they reflect recent or current levels in the market. This information goes out of date quickly, which is another reason why VDAs represent a greatly superior information-sharing resource to any other forms of public data on this subject area.²

(D) *General industry issues*

- (i) VDAs are used as a forum for discussion of industry issues generally, and how specific carriers are handling those issues. Examples of these types of issues include port congestion, equipment repositioning, piracy, and container weighing. This type of information exchange can often lead to better education of the industry on a particular issue, and ideas on how to address the issues efficiently, which has positive benefits for many stakeholders.
- (ii) The shipping industry in particular needs to be able to discuss general industry issues freely, quickly and directly, given the significant degree of cooperation between carriers and the common use of port facilities and infrastructure. It is beneficial to customers that any industry issues are resolved between carriers as

² For more information on utilisation and capacity data, please refer to the Applicant’s response to question 2 of the Commission’s Request for Further Information dated 15 April 2016

quickly as possible, and the most efficient way of doing so is to discuss these issues within a VDA meeting.

- (iii) As previously mentioned by the Applicant in meetings with the Commission, a recent example arose at the height of the piracy cases off the Horn of Africa. Through the framework of the VDA, carriers started exchanging information about what could be done to protect their vessels. As a direct result of the information exchange facilitated by VDAs, the risk in the Indian Ocean was mitigated by vessels commencing operations in convoys under protection of (mostly Chinese) naval ships when transiting those areas. This example highlights how VDAs are used for much more than just the discussion of rates and charges; they serve a much greater purpose in allowing industry dialogue and innovation. Without a block exemption for VDAs, there would be no other forum to allow carriers to discuss these types of issues that may arise in Hong Kong.

(E) *General economic issues/trends*

- (i) VDAs study a broad range of economic indicators to assist the carriers in better understanding the various markets which they serve, such as GDP growth, macro-economic trends, manufacturing and retail inventory levels, fuel prices, wholesale prices, retail sales, consumer confidence and spending, exchange rates, and trade and manufacturing investment patterns.

(F) *Regulatory developments and compliance issues*

- (ii) VDA meetings often include a summary of the legal and regulatory positions in relevant jurisdictions, touching on pertinent developments and compliance issues for the VDAs and their carrier members. Having a collection of lines gathered together in a VDA forum facilitates a better understanding of these issues, as know-how is shared and common questions can be answered to the benefit of all present. This understanding can thereby enhance compliance with applicable laws and regulations.
- (iii) Issues that are discussed within VDAs include competition law developments, shipping regulatory developments and requirements, Customs and documentation issues, anti-boycott regulations, import/export trade restrictions, and export control and economic sanctions issues.

(G) *Industry outreach and best practices (general and Hong Kong specific), including service contract rules, terms, conditions*

- (i) Within VDAs, carriers will often discuss general industry best practices and potential model service contract terms and conditions in an effort to make the contracting and transportation processes more efficient and effective for all parties, including their customers. The focus of these discussions is on process and structure. Specific commercial terms and conditions between individual carriers and shippers are never discussed. Discussions would not relate to specific carriers, customers or contracts, individual rates or charges, or other similar commercial issues.

- (ii) VDAs also serve as an important forum for outreach to the carriers' customers, including shipper organisations on trade issues. Representatives of the VDAs will meet with shipper groups to provide educational seminars and forums, or to discuss shipper questions or concerns.

(H) *Rate and Revenue Indices Based on Aggregated and Historical Data*

- (i) There are some rate indices currently available from third party sources, such as the Shanghai Shipping Exchange's Shanghai Containerized Freight Index and China Containerized Freight Index. However, there is a particular benefit in having VDAs collect this historical information directly from their members and then distribute summaries in an aggregated format. Such information is tailored to the specifications and methodologies that the carriers will find most useful, as opposed to the data being imposed on them in a particular format by a third party source. In addition, many of the outside sources of this information do not cover all the carriers in the trade, or obtain the rate information from intermediaries, making the data less reliable.
- (ii) One example of such an index is the Transpacific Stabilization Agreement ("TSA") Revenue Index, which tracks average revenue per 40 foot container ("FEU") across TSA's member carriers. [...] TSA has maintained a Revenue Index for several years in an effort to track market rate trends. The Revenue Index, which is available to the public on TSA's website, is comprised of monthly average revenue data provided by the carriers to TSA. Individual carrier data is kept confidential by TSA, and then aggregated to develop the index. The Index shows how revenue per FEU has evolved over a period of time using an index of relative values based on a formula, rather than focusing on specific dollar amounts. The Revenue Index is intended to provide carriers and the shipping public with one more piece of information that helps show a more complete picture of long-term market trends in a complex and highly competitive trade.

3. Why carriers need a VDA exemption, even if reduced in scope

- 3.1 The Commission acknowledges in the Statement that in addition to currently discussing freight rates, VDAs "*provide for the exchange of other, more general information in relation to trades, such as statistics, reports or other information relating to market trends, economic forecasts, operational or technological developments, and policy or legal issues*".³ The Commission states that the exchange of more general information through VDAs may or may not amount to a contravention of the Ordinance, depending on the nature of the information concerned, and states that certain of the information currently exchanged between carriers through VDAs can thus be exchanged without risk of contravening the Ordinance.⁴ The Commission references public data, and historical, aggregated data in particular. The Applicant accepts that some data exchange could fall under the self-assessment regime, but submits that not all of the information exchanged through VDAs and listed in section 2 above falls into these categories, thus necessitating a block exemption order.

³ Paragraph 2.33 of the Statement

⁴ Paragraph 4.76 of the Statement

- 3.2 [...] VDAs are used as a platform to discuss many issues that go beyond what can usefully be treated under the self-assessment regime. The Applicant's previous arguments for legal certainty for the industry continue to apply here, namely that some may take the view that liner shipping agreements may be restrictive of competition and the Applicant therefore wishes to obtain legal certainty that the Efficiencies Exclusion applies and therefore that there is no compliance risk associated with such discussions.
- 3.3 The Commission's Guideline to the First Conduct Rule (the "**FCR Guideline**") includes only a high level discussion on the subject of information exchange and its explanation of what can and cannot be exchanged does not sufficiently provide carriers with the clarity needed to ensure compliance with the Ordinance, without having a block exemption order in place. The Revised VDA Scope would not cover pricing, but even so, the FCR Guideline states that information relating to quantities (information concerning sales, market shares, sales to particular customer groups or territories) is likely to be considered by the Commission as having the object of harming competition.⁵ [...]
- 3.4 [...] The FCR Guideline mentions certain benefits arising from information exchange, for example: "*competition is often enhanced through the sharing of information, for example, in relation to best practices or exchanges of information which allow firms to better predict how demand is likely to evolve*", but also discusses the potential competition concerns from the exchange of information which relates to: "*customers, production, costs, quantities, turnover, sales, capacity, product quality, marketing plans, risks, investments, technologies and innovations*".⁶ [...], for the reasons discussed at section 4 below, discussion and information exchange in liner shipping VDAs give rise to significant efficiencies that meet the conditions for the granting of a block exemption order pursuant to the Ordinance.
- 3.5 In order for carriers to have sufficient confidence to allow VDAs to continue to cover Hong Kong, they require legal certainty that the issues that are discussed within VDA meetings, some of which could include potentially competitively sensitive information (albeit not related to rates or charges), fall within a block exemption order. The self-assessment model does not give sufficient certainty to carriers, who by the nature of their international business operate with great emphasis on compliance and are unwilling to risk potential breaches of competition law.
- 3.6 The Applicant understands the generally-applicable self-assessment regime under the Ordinance, but there are nonetheless certain information exchanges and discussions (as listed above) which take place within VDAs that are specific to the shipping industry and which warrant a block exemption.
- 3.7 Having conducted a lengthy and detailed review of VDAs, the Commission should be in a position to provide this clarity. Without such specific guidance from the Commission, carriers cannot be sufficiently certain of what information can be exchanged under the First Conduct Rule, which in turn means that carriers will struggle to discuss the industry and exchange information at all. Against this backdrop, it is simply not possible to rely on self-assessment for the exchange of information within a VDA. This will mean that, should the Commission not grant a block exemption order for the Revised VDA Scope, the industry will lose the benefit of the information exchanges, which in turn will harm the industry in Hong Kong and have adverse effects on competition and consumers.

⁵ Paragraph 6.39 of the FCR Guideline

⁶ Paragraph 4.125 of the Statement

4. Application of the Efficiencies Exclusion criteria to information exchanged under VDAs

- 4.1 At paragraph 4.75 of the Statement, the Commission states that given that certain aspects of VDAs may give rise to significant competition concerns, the Commission considers that “*any efficiencies in this context must be particularly clear cut and that the evidence of consumer benefit would need to be compelling*”. By proposing to remove Hong Kong-specific pricing discussions and voluntary price agreements from VDAs, the Applicant has eliminated the Commission’s key competition concerns and any concerns over information exchange activities should be less significant. Accordingly, the Revised VDA Scope should allow the Commission to accept the broader efficiencies of VDAs outlined in the Applicant’s Consultation Response.

First condition: efficiency gains

- 4.2 As set out in the Consultation Response, even excluding the pricing discussion element, VDAs give rise to broad cost efficiencies for consumers in Hong Kong by promoting Hong Kong: (i) as a transshipment hub, with benefits to all consumers; and (ii) as an international maritime centre and “super-connector” with an impact on the broader Hong Kong economy. This increases the volume of vessels routed through the port and consequently results in economies of scale and reduced costs per TEU. This in turn lowers the costs and thus the retail prices for all consumer products that are transported to Hong Kong in this way. We explain these efficiencies in further detail in this section.

Broad efficiency to the Hong Kong economy of VDAs promoting transshipment services in Hong Kong

- 4.3 As set out in paragraphs 5.25 to 5.33 of the Consultation Response, VDAs, provide an important information sharing platform for Hong Kong carriers to make decisions on whether to transport their transshipment cargo through Hong Kong or any other port. Through VDAs, carriers discuss specific cargo flows and weekly statistics, outlining which ports and port ranges have declining or increasing cargo throughput, both currently and forecast. This enables carriers on an individual basis to have the relevant information to hand in order to calculate, with a forward-looking perspective, how many ships should be allocated to serve a particular port at any given time and how much space should be allotted on each vessel for goods to be picked up at that port.
- 4.4 A carrier has many decisions to make with respect to Hong Kong. It must decide whether to serve Hong Kong at all, either in a direct service or as a port in a transshipment service. It must then decide how many vessels to deploy in Hong Kong and the extent, size, and nature of its vessel services. It must decide (independently) what rates to charge to its Hong Kong-based customers. The discussion and exchange of information as proposed under the Revised VDA Scope will ultimately lead to better overall carrier decisions in these areas. This means that carriers can have access to timely and accurate information about the market, which will help them to make well-informed and efficient decisions. Broader, more accurate market knowledge will help carriers make those decisions in a more educated manner. As they do, they operate more efficiently and reduce the risk of financial distress or failure.

- 4.5 These decisions have important impacts on both the carrier and its customers, as well as to Hong Kong consumers. They impact the carrier because, if it makes uninformed (or ill-informed) decisions, it risks losing money, being unprofitable, or even facing bankruptcy or acquisition by another carrier. Because of the unique economics and extremely competitive nature of the shipping industry, as explained in the Application, these decisions are particularly important. Carrier decisions also impact customers and consumers. If carriers, because of lack of market information, reduce the number of vessels calling at Hong Kong, there will be fewer competitors and less competition. Less competition is not beneficial to customers or consumers. The inability of carriers to access complete market information in Hong Kong also risks a decline in the service provided to Hong Kong customers and consumers. This would have negative effects on the Hong Kong economy and its ability to lead and effectuate the One Belt One Road initiative.
- 4.6 Of course, carriers ultimately have to make decisions independently. A VDA will not decide or coordinate whether a carrier will serve Hong Kong, nor will a VDA decide what rates the carrier will charge its customers. Under the Revised VDA Scope discussed in this paper, VDAs would no longer even discuss rates or issue recommended rate increases or levels. However, the information exchange provided in VDAs provides carriers with an important tool as they make those individual decisions. That tool, which has been recognised as deserving of a competition law exemption in most countries in the world, should also be recognised and permitted in Hong Kong.
- 4.7 The broader benefits of VDAs in facilitating transshipment result in a greater number of vessels calling at the port of Hong Kong, which in turn results in increased options and higher shipment frequencies for customers that need to transport goods to Hong Kong. This leads to clear benefits to the Hong Kong economy and consumers, which is evidence of “*improving production or distribution*” or “*promoting technical or economic progress*”.

Broad efficiency to the Hong Kong economy of VDAs promoting a super-connector maritime shipping centre and Hong Kong role in One Belt One Road

- 4.8 As set out in paragraphs 5.20 to 5.25 of the Consultation Response, VDAs provide the forum necessary for the exchange and review of market data, supply and demand forecasts, international trade flows and industry trends, which feed into the various industries that survive on the back of shipping in any maritime centre. The choice of maritime centre is discretionary. In order for stakeholders to choose and commit to Hong Kong as a maritime centre, they need to be confident that there is a sufficient and credible flow of information and market intelligence across the shipping industry (as there is in most other countries) to allow their respective businesses to succeed. VDAs are the only platform for this kind of information exchange in the industry and the absence of any form of block exemption order covering VDAs would harm the wider industries that rely on VDA operation, e.g. banks, insurers, lawyers, retailers, consumers.
- 4.9 The role that VDAs play in allowing Hong Kong to fully achieve its potential as a super-connector shipping hub and maritime centre is an efficiency which gives rise to quality improvements and other benefits of a qualitative nature by facilitating and enhancing Hong Kong’s ability to provide maritime services, which would otherwise struggle to exist, without the Hong Kong-specific data exchange function carried out through VDAs. VDAs also enhance Hong Kong’s ability to play a key role in the One Belt One Road initiative, which relies heavily on the flow of information (past, current and forecast) between carriers to efficiently connect vessels with cargo emanating from southern China, providing carriers with intelligence on current or expected/forecasted movements in cargo demand between different port locations. In other words, the information efficiencies to which even the

Revised VDA Scope gives rise, promoting Hong Kong as a maritime centre, can be seen as “*improving production or distribution*” or “*promoting technical or economic progress*”.

Second condition: consumers receive a fair share of the efficiencies

- 4.10 As set out in the Consultation Response, the Applicant submits that the Commission should take a broader definition of consumers than it has in the Statement and submits that the Revised VDA Scope gives rise to broad cost efficiencies for consumers in Hong Kong by allowing Hong Kong to compete against other regional ports as a transshipment hub.
- 4.11 The shipping industry, by its nature, impacts consumers in virtually every sector by transporting a very high proportion of all cargo into Hong Kong. End or “final” consumers in Hong Kong are direct beneficiaries and will receive a fair share of the broad efficiencies resulting from VDAs. For example, the high service levels passing through Hong Kong reduce the unit cost of shipping individual containers to Hong Kong, thereby reducing the transportation costs of cargo imported to Hong Kong and resulting in the scope for retailers to charge lower prices for consumer products. Other, more intangible, benefits such as promoting Hong Kong abroad and increasing employment, are passed through the supply chain to consumers across Hong Kong in general.
- 4.12 As explained at paragraphs 5.26 to 5.33 of the Consultation Response, it is only through ensuring a high volume of throughput and connectivity that Hong Kong remains competitive as a transshipment hub. Information exchange through VDAs gives carriers the data they need in order to make informed decisions to route vessels through Hong Kong, keeping service levels high. This allows the trade, infrastructure, and employment currently brought about by Hong Kong’s maritime industry, to be retained. In turn, this allows Hong Kong to benefit from a lower cost of goods and higher employment etc.
- 4.13 Also, both VDAs and VSAs facilitate investment in vessels, equipment, and vessel services, which in turn provide more and higher quality service options for Hong Kong stakeholders. Again, consumers benefit in the form of cheaper goods as the cost of importing cargo to Hong Kong is reduced. Without a block exemption for VDAs, Hong Kong’s shipping industry will ultimately suffer and consumers will be faced with higher costs for everyday items.
- 4.14 Finally, there are also significant “flow-through benefits” to consumers, industry and the whole Hong Kong economy of building a centre of concentrated support services and activity around the operations of carriers and shippers, as outlined in the Consultation Response. The related infrastructure accompanying a maritime centre in Hong Kong also supports expanded and more efficient shipping services that will ultimately be pro-competitive for Hong Kong.

Third condition: indispensability to the attainment of efficiencies

- 4.15 VDAs and, in particular, the discussion of market information are reasonably necessary to achieve the efficiencies discussed at paragraphs 4.2 to 4.6 above. The Applicant submits that there are no other economically practicable and less restrictive means of achieving the claimed efficiencies.

Alternative sources are not as useful as VDAs

- 4.16 For the reasons outlined above, both VDAs and VSAs are necessary together to provide carriers with the certainty needed to make efficient individual investment decisions to ensure demand matches supply, and thereby ensure reliability of services. They are the standard business model

of the industry worldwide and are fundamental to the continued promotion of service to Hong Kong. Further, as explained in the Consultation Response at paragraph 5.10 and elsewhere, there are no substitutes for the quality and relevance of VDA data on which carriers place by far the most weight; Government and publicly-available sources are not as reliable or useful as VDA data.

- 4.17 In response to the Commission's statement at paragraph 4.99 of the Statement that "*some of the relevant information can be exchanged regardless of whether VDAs meet the conditions of the efficiency exclusion and/or regardless of whether the Commission issues a block exemption order for VDAs*", as set out above, these discussions are not able to fall under the self-assessment regime as they give rise to potential anti-competitive concerns in so far as they relate to sensitive topics, such as supply and demand trends, costs, and vessel utilisation and capacity levels.
- 4.18 For these reasons, information exchanged through VDAs is needed for carriers to effectively operate on the market and is of a markedly different quality to publicly available information. Carriers, particularly the smaller players on the market, would struggle to deploy operations efficiently if they had to base movements only on publicly available sources of information, making these discussions an indispensable tool to the achievement of the efficiencies described above.

Alternative solutions are not practicable

- 4.19 The Commission has asked for more information regarding the distinction between Hong Kong and the EU as regards the need for VDAs as an information sharing platform. Following the removal of an exemption for conferences in the EU, carriers could only exchange data that was historical and aggregated in certain forums. As a result, these data have been of more limited value, both to the carriers and ultimately to their customers. As noted above, VDAs provide accurate, up-to-date market data to the carriers in a single, reliable source and are therefore the best possible structure for continuing to facilitate information exchange between carriers in Hong Kong in order to achieve the above-outlined efficiencies.
- 4.20 In any event, the EU approach would not be practicable for Hong Kong because the EU is a large and cohesive regulatory block, in which carriers have been limited to the same general types of aggregated and historical information for all ports (following the withdrawal of the EU block exemption). The same is not true for Hong Kong, in the context of Asia generally, where the vast majority of jurisdictions permit VDAs. If Hong Kong adopted the EU approach, carriers would continue to discuss and exchange trade information as it relates to other neighbouring ports where such activities are permitted. That would mean that carriers would have better, more reliable and more up-to-date information about other port ranges than they would for Hong Kong. Hong Kong would be at a competitive disadvantage vis-à-vis other countries.
- 4.21 Since, as discussed above, service and investment decisions are based in large part on these types of information, absent an exemption for the Revised VDA Scope, service could ultimately diminish in Hong Kong in favour of other neighbouring ports where better market information was available to the carriers. In terms of achieving the above-outlined efficiencies, it is crucial to appreciate that – in the context of Hong Kong – VDA information on other regional ports will continue be available, which means that carriers would have much better visibility over these other ports than for Hong Kong. Given the very discretionary nature of transshipment traffic in particular, there would be a clear commercial incentive to call at these other ports, where VDAs have more market intelligence to support a business case for that routing, instead of Hong Kong.

- 4.22 It does not make business sense for a carrier to choose a transshipment hub that involves a greater degree of risk (due to a lack of the credible market intelligence that VDAs provide) and therefore carriers would find it more difficult to route vessels through Hong Kong if the Commission were not to grant a block exemption order for VDAs. The most likely result without any block exemption for VDAs and considering that potential enforcement action could carry heavy fines, is that the carrier community will gravitate towards jurisdictions where they can be more certain of compliance with the relevant regulatory framework; Hong Kong would likely be carved out of discussions altogether. For these reasons, there would be significant risk of harm to consumers in Hong Kong if carriers were limited to an EU model of information exchange and shifted towards the ports of VDA-compatible jurisdictions, ultimately losing Hong Kong the critical mass of shipping frequency necessary to operate as a transshipment hub, let alone a maritime centre.
- 4.23 Finally, it should be noted that the provisions of VDAs do not go beyond what is required to attain the efficiencies. Indeed, by removing pricing discussions and voluntary price agreements, the Revised VDA Scope further tailors VDA activities to make them even more limited; discussions on market trends would merely provide an informational platform. They are purely to enable carriers to be better informed on market conditions. They are necessary to attain the efficiencies, improving service stability (e.g. by improved vessel deployment and promotion of investment).

Fourth condition: No possibility of eliminating competition

- 4.24 As noted in the Consultation Response, the Commission appears to accept that the fourth condition of the Efficiencies Exclusion criteria is met, or at least does not state that it would not be met.⁷ In any event, however, the Revised VDA Scope proposal to remove Hong Kong-specific pricing discussions and voluntary agreements from the scope of VDAs should mean that this is even more clearly demonstrated.
- 4.25 In the Statement, the Commission references the general assertion from the FCR Guideline that “*the more an agreement causes harm to competition, the greater the likelihood that the undertakings concerned are afforded the possibility of eliminating competition*”.⁸ Given that it is proposed that VDAs will only discuss and exchange non-pricing information in relation to Hong Kong, it seems implausible that the Revised VDA Scope could ever give parties the possibility of eliminating effective competition in the market for liner shipping services. Carriers, as now, would remain completely autonomous in making their own business decisions – save that they now have information which allows them to make better and more efficient decisions.

Further, as mentioned at paragraph 5.74 of the Consultation Response and as demonstrated in the capacity share chart below, the market is highly fragmented and there is a strong degree of existing competition between carriers, as evidenced by historically low rates (which are forecast to continue for the coming years).

Capacity share of the world liner fleet in TEU terms (January 2017)

Carrier	TEU Slots	Slot Share
APM-Maersk	3,292,309	15.9%

⁷ Paragraph 4.125 of the Statement

⁸ Commission’s guideline on the First Conduct Rule, paragraph 2.19

MSC	2,837,462	13.7%
CMA CGM Group	2,133,114	10.3%
COSCO	1,622,547	7.8%
Evergreen	992,905	4.8%
Hapag-Lloyd	950,212	4.6%
Hamburg Sud	603,051	2.9%
OOCL	575,563	2.8%
Yang Ming Marine Transport	570,018	2.8%
UASC	526,858	2.5%
NYK Line	518,897	2.5%
MOL	493,775	2.4%
Hyundai M.M.	455,859	2.2%
PIL	364,600	1.8%
K Line	350,937	1.7%
Zim	299,225	1.4%
Wan Hai Lines	220,067	1.1%

Source: Alphaliner

5. Conclusion

- 5.1 The Applicant recognises the Commission's concerns regarding the pricing discussions within VDAs and is seeking to arrive at a pragmatic conclusion in line with the Government's wider policy to promote the maritime industry. The Revised VDA Scope would allow Hong Kong to remain generally aligned with other jurisdictions in terms of regulatory approach and network structure, whilst removing the elements of VDAs which the Commission most objects to from a competition perspective.
- 5.2 This can be achieved without any substantiated theory of harm to competition. A large number of VDAs (including with rate discussion and agreement authority) have operated openly in the Hong Kong trades for decades. During that time, freight rates have not been inflated by VDAs and recently have been sitting at all-time lows. There has been no demonstration of harm to consumers through VDAs. Even if the Commission is not comfortable with the operation of pricing discussions touching on Hong Kong, that should not prevent the granting of a block exemption order covering the Revised VDA Scope to allow the continued operation of discussion of other subjects through VDAs.
- 5.3 A sudden removal of VDAs in their entirety will have a much more immediate damaging effect on Hong Kong's role as a transshipment hub than a removal of the exemption for pricing discussions alone. Given that the Commission can review, vary and revoke its decision at any time if it considers it appropriate to do so, e.g. following a material change in circumstances, and in any event must commence a review of its decision within 5 years from the date of granting a block exemption order,⁹ it is clear that a step-by-step approach to making such a fundamental decision is the preferable

⁹ Ordinance, sections 15(4), 18(2) and 20

course of action. The Applicant would welcome the Commission adopting the Revised VDA Scope approach, rather than simply proposing not to issue a block exemption order for VDAs at all.

- 5.4 The Applicant would like to thank the Commission for taking the time to review this supplementary submission. Should the Commission require any further information, in particular on the practical means by which the Revised VDA Scope would work in practice, the Applicant would be glad to provide it, either in written submissions or in the meeting with the Commission to discuss the finalisation of a decision.

ANNEXES

[...]