The Hong Kong Competition Ordinance and the maritime industry

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Hong Kong's first-ever competition legislation came into force less than a year ago, on 14 December 2015. Anti-trust regulations have existed in many countries for quite some time, and it might seem that Hong Kong is rather late to the party. Be that as it may, the Competition Ordinance (CO) has arrived and it is important that businesses that have dealings in Hong Kong learn to adapt to the new regulatory landscape. In this article, we provide a brief introduction to the CO and its impact on the maritime sector, with a particular emphasis on the container liner business.

Who and what is subject to regulation by the CO?

The CO consists of three key rules: the First Conduct Rule, the Second Conduct Rule and the Merger Rule. Currently, the Merger Rule only applies to the telecommunications industry, so we will focus on the First and Second Conduct Rules in this article.

The First Conduct Rule

This prohibits agreements, concerted practices and decisions by undertakings that have the effect of preventing, restricting or distorting competition in Hong Kong. The most obvious example of prohibited conduct is cartel behaviour by means of price-fixing, market sharing and output limitation, amongst others.

It is important to note that the CO defines 'agreement' much more broadly than the strict legal understanding of the word. Here, an 'agreement' can include any 'meeting of minds', arrangement, understanding or promise, whether express or implied, written or oral, and whether legally enforceable or not.

A 'concerted practice' may also fall foul of the CO. This is a form of cooperation that is not quite an 'agreement'. An example is if a group of competitors do not expressly agree to fix prices, yet knowingly exchange sensitive information that can influence each other's market strategies or pricing policies.

The Second Conduct Rule

This prohibits an undertaking that has a substantial degree of market power from abusing this power to engage in conduct that has the object or effect of preventing, restricting or distorting competition in Hong Kong. The difficulty is that the CO does not define 'substantial degree of market power', which will be determined on a case-by-case basis.

It is important to note that the First and Second Conduct Rules apply to non-Hong Kong undertakings and conduct that takes place outside of Hong Kong.

Both the First and Second Conduct Rules apply to 'undertakings' that are 'engaged in business activity', which is defined very widely under the CO. Practically, 'undertakings' include individuals and virtually every conceivable business-related entity (ie companies, partnerships, groups of companies, sole traders, etc). It is therefore almost certain that any shipowner, operator or charterer would be considered an 'undertaking' by the Competition Commission (the competition regulatory authority in Hong Kong).

Impact of the CO on the maritime shipping industry

Liner cooperation agreements and block exemptions

The Commission has announced that in the initial years of the CO, one of the Commission's top priorities is to target cartel behaviour and Serious Anti-competitive Conduct[1] such as price-fixing, market sharing, output limitation and bid-rigging agreements.

During the drafting and public consultation stages of the CO, the Hong Kong Liner Shipping Association (HKLSA) informed the Competition Commission that enforcement of the First Conduct Rule would pose a serious threat to the viability of Hong Kong as a shipping hub. Hong Kong is the fifth-largest container port in the

The Hong Kong Competition Ordinance and the maritime industry continued

The phenomenon of cooperative liner agreements is by no means unique to Hong Kong and has existed since 1875. In modern times, such cooperation commonly takes the form of liner consortia, VSAs, strategic/global alliances, capacity stabilisation agreements and VDAs.

world by volume, and roughly 70% of its throughput comes from transhipment. More than 95% of the container liner shipping business in Hong Kong operates under liner agreements such as vessel-sharing agreements (VSAs) and voluntary discussions agreements (VDAs) that may well be considered Serious Anti-competitive Conduct under the First Conduct Rule. Industry experts and participants have expressed concerns that if the liner trade were no longer allowed to operate using liner agreements in Hong Kong, ship liners could, and would, abandon Hong Kong in favour of a new transhipment hub, such as Shenzhen.

At first glance, such cooperative agreements could easily fall foul of the competition regulations of many developed countries, including the CO in Hong Kong. However, the liner industry has always defended such practices on the basis that cooperation between liners actually produces pro-competitive effects which achieve economies of scale and improve the quality of services for consumers.

Liners in Australia, China, the EU, India, Israel, Japan, Malaysia, Singapore and the USA have successfully relied on similar arguments to obtain block exemptions for certain types of liner agreements from competition authorities, although the exact criteria of what is or is not exempt differs from country to country. Looking across these other countries as a whole, technical and operational arrangements tend to be allowed, such as joint use of vessels and port installations. Rate-fixing and price discussions are allowed in some jurisdictions but prohibited in others.

Three days after the CO came into force, the HKLSA lodged an application with the Competition Commission for a block exemption for certain liner shipping agreements, specifically VSAs and VDAs. While the Commission has yet to publicly issue a final decision, it has indicated that it is unlikely to initiate enforcement action against ship liners in respect of these types of agreements while the application is under consideration.

Mergers and alliances
There are also possible contraventions of the Second Conduct Rule. In particular, the failed P3 alliance is a prime example of Second Conduct Rule issues. In June 2014, the would-be alliance of Maersk, MSC and CMA CGM was rejected by China's competition authorities despite having already been approved by the EU and US authorities. The Chinese authorities stated that the alliance's market share in the Asia-Europe trade would be 46.7%, which was too strong.

The past few years have seen a spate of actual or planned container line mergers, as well as the breaking apart and regrouping of various container shipping alliances: Hapag-Lloyd and United Arab Shipping Co; CMA CGM and NOL; the 2M, THE and Ocean Alliances. If this trend of consolidation continues, vessel owners, operators and charterers doing business in Hong Kong could, in principle, find themselves in a position where they are considered to be a 'powerful undertaking' that has 'abused' its dominant position under the Second Conduct Rule.

Learning to live with the CO

In the past years, we have seen major investigations by the Chinese, Russian and EU competition authorities against box carriers for purported anti-competitive conduct, some of which have resulted in fines. While the CO is still in its early days and it remains to be seen how block exemptions and related case law will develop in Hong Kong, it would be wise for vessel owners, operators and charterers to educate themselves on the CO and adapt to the new regulatory landscape in order to avoid fines and criminal prosecutions.

1 The First Conduct Rule of the CO distinguishes between Serious Anti-competitive Conduct (listed above) and other conduct (eg exchange of information, group boycotts, joint purchasing agreements, standard terms and standardisation agreements, etc)

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