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Submissions on Draft Leniency Policy
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Dear Sirs,

Consultation on Draft Leniency Policy: Response of Slaughter and May

This letter sets out the views of the Slaughter and May Competition Group on the Draft Leniency Policy published by the Competition Commission (the "**Commission**") on 23 September 2015.

As a general comment, the Draft Leniency Policy provides useful insight into how the Commission proposes to incentivise and process applications for leniency in respect of cartel conduct. The Draft Leniency Policy also sets out practical guidance as to how the Commission will apply sections 80 and 81 of the Competition Ordinance (Cap. 619) (the "**Ordinance**") and is a helpful starting point on this important subject.

We welcome the opportunity to comment on the Draft Leniency Policy. In particular, we fully support the Commission's stated aim of providing a "*strong and transparent incentive*" for a cartel member to report the cartel to the Commission.[1] Whether a cartel member decides to apply for leniency is an extremely important decision from the perspective of both the cartel member (for whom the decision carries economic and legal implications), and the Commission (whose detection and investigation of the cartel is thereby facilitated), and the Leniency Policy must provide sufficiently clear guidance and the requisite incentives to do so.

For the Commission's aim to be realised, it is vital that the Leniency Policy addresses, at a minimum, the following questions:

- **What is the scope of the conduct covered by the leniency policy?**
- **How will cases falling outside the policy be assessed?**
- **What will be the scope of leniency granted under the policy?**
- **Who can benefit from the policy?**
- **How to apply for leniency under the policy?**

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[1] See paragraph 1.3 of the Draft Leniency Policy.

- **What happens if the leniency agreement is terminated?**

Addressing each of the above questions fully in the Leniency Policy will help to ensure that: (i) undertakings have the information they require to decide whether or not to apply for leniency; and (ii) the Commission adopts a consistent general approach towards all cases.

Whilst the Draft Leniency Policy already contains some useful guidance on each of the above questions, we believe that these issues should be more fully addressed by the Commission. Our recommendations are set out below.

1. What is the scope of the conduct covered by the leniency policy?

The need for greater clarity as to what is covered by the Draft Leniency Policy

1.1 Paragraphs 2.1(a) and 2.3 of the Draft Leniency Policy specify that the policy applies only to "cartel conduct" in contravention of the First Conduct Rule.

1.2 Paragraph 2.4 of the Draft Leniency Policy then provides, in essence, that "cartel conduct" refers to horizontal agreements "*that seek to do one or any combination of [the activities listed in sub-paragraph (i) to (iv) of that paragraph] which have as their object the harming of competition*". Paragraph 2.5 notes that "cartel conduct" is considered Serious Anti-Competitive Conduct under section 2(1) of the Ordinance.

1.3 The relationship between "cartel conduct", "object" infringements and Serious Anti-Competitive Conduct introduces unnecessary complexity to the issue of the conduct covered by the Draft Leniency Policy.

1.4 For example, paragraph 2.4 of the Draft Leniency Policy refers to activities "*which have as their object the harming of competition*". This wording could be interpreted as either:

(A) imposing a requirement (in addition to the requirement that the activity must fall within sub-paragraphs (i) to (iv)) that the conduct must have the object of harming competition; or

(B) intending to be descriptive only, i.e. it is explaining that the Commission considers the activities listed in sub-paragraphs (i) to (iv) of paragraph 2.4 to have the object of harming competition.

1.5 The dual requirements under the first interpretation above appear redundant in light of the Commission's Guideline to the First Conduct Rule, which expressly provides that those four types of conduct constitute object infringements if they occur between competitors.[2]

1.6 We would therefore recommend deleting the wording "*which have as their object the harming of competition*" from Paragraph 2.4 of the Draft Leniency Policy.

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[2] See paragraphs 6.10, 6.18, 6.24, and 6.29 of the guideline.

1.7 In addition, the Draft Leniency Policy notes that "cartel conduct" would be considered Serious Anti-Competitive Conduct, but does not clarify whether the converse would be true, i.e. whether Serious Anti-Competitive Conduct involving competitors would necessarily constitute "cartel conduct". The fact that sub-paragraphs (i) to (iv) of paragraph 2.4 closely follow, but do not exactly correspond to, the definition of "serious anti-competitive conduct" in the Ordinance, further confuses matters.[3]

1.8 Given the apparent similarities between the two concepts – save for the fact that "cartel conduct" currently only refers to horizontal agreements (see further our submission below) – it would arguably make sense to rely on the concept of Serious Anti-Competitive Conduct in the Leniency Policy, rather than introduce a new, separate concept of "cartel conduct". Otherwise, it may introduce unnecessary complexities if undertakings have to assess separately whether their conduct is Serious Anti-Competitive Conduct and "cartel conduct".

1.9 We therefore recommend that the Commission either:

(A) define the scope of the Leniency Policy by reference to the concept of Serious Anti-Competitive Conduct; or

(B) if the Commission intends for the concept of Serious Anti-Competitive Conduct to be separate from that of "cartel conduct", clarify why this is necessary.

The applicability of the Draft Leniency Policy to vertical agreements

1.10 As mentioned above, paragraph 2.4 of the Draft Leniency Policy specifies that "cartel conduct" involves horizontal agreements, i.e. the conduct must occur "*among undertakings that are, or otherwise would be if not for the cartel conduct, in competition with each other*".

1.11 We understand that in limiting the Draft Leniency Policy to "cartel conduct", the Commission considered that cartels are universally condemned as economically harmful, and that they are more difficult to detect compared to other forms of anti-competitive conduct because they are usually organised or implemented in secret.[4] We note that, whilst not universally condemned as economically harmful, certain types of vertical agreements – particularly resale price maintenance - may constitute an object infringement[5] and/or Serious Anti-Competitive Conduct in certain circumstances.[6]

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[3] For example, sub-paragraph (ii) specifies that seeking to "*share markets*" would constitute cartel conduct; whereas sub-paragraph (b) in the definition of "serious anti-competitive conduct" is broader and refers to "*allocating sales, territories, customers or markets for the production or supply of goods or services*".

[4] See e.g. paragraph 1.1 of the Draft Leniency Policy.

[5] See e.g. paragraph 6.74 of the Guideline on the First Conduct Rule.

[6] See paragraph 5.6 of the Guideline on the First Conduct Rule.

1.12 Given that resale price maintenance could constitute Serious Anti-Competitive Conduct and may not always be easily detectable (e.g. if it is imposed on the wholesale level of the supply chain), it would be beneficial to both the Commission and undertakings to have the option to apply for leniency, and for a clear set of procedures to be applicable to such an application. This would be consistent with the position in the United Kingdom, where the relevant leniency regime provides for leniency in relation to vertical agreements involving price fixing (e.g. resale price maintenance cases).[7]

1.13 We therefore recommend removing the requirement that the conduct must involve a horizontal agreement in order to be covered by the Leniency Policy.

2. How will cases falling outside the policy be assessed?

2.1 As mentioned above, as currently drafted, the Draft Leniency Policy applies only to undertakings who have engaged in "cartel conduct". Paragraph 2.12 also limits the scope of the Draft Leniency Policy by providing that leniency will not be available if the Commission has "*decided to issue an infringement notice under section 67 of the Ordinance or to commence proceedings in the Tribunal in respect of the cartel conduct reported by the undertaking*".

2.2 The following situations would therefore appear to fall outside the scope of the Draft Leniency Policy:

(A) applications in respect of non-cartel conduct (e.g. information exchange, resale price maintenance (see above) and infringements of the Second Conduct Rule); and

(B) applications made after the Commission has decided to issue an infringement notice or to commence proceedings.[8]

2.3 Applications falling outside the scope of the Draft Leniency Policy are addressed primarily at page one of the Draft Leniency Policy, which notes that the Commission is not precluded from entering into a leniency agreement in respect of non-cartel conduct, or with persons who are not undertakings.[9] We note that, whilst section 4 of the Draft Leniency Policy briefly discusses non-cartel conduct, such

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[7] See paragraph 2.3, Applications for leniency and no-action in cartel cases. OFT's detailed guidance on the principles and process ("**CMA Leniency Guidance**") July 2013. Available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/284417/OFT1495.pdf.

[8] Section 80(2) envisages that leniency agreements may be entered into after proceedings for a pecuniary penalty have already been brought – it states that the Commission must not, while a leniency agreement is in force, "*bring or continue proceedings under Part 6*" (emphasis added).

[9] As to applications made after the Commission has decided to issue an infringement notice or to commence proceedings, paragraph 2.12 of the Draft Leniency Policy only provides that leniency would not be possible "*under [the] policy*" in such circumstances, which suggests such an application could be made outside the scope of the policy.

guidance is very limited[10] and the remainder of the section addresses only the situation where an undertaking does not qualify for leniency in respect of cartel conduct.

2.4 We recognise that it would be difficult for the Commission to provide full procedural and substantive guidance on the situations above, but we believe that it is important for the Leniency Policy to indicate, at a minimum, the Commission's general approach towards such cases. In order to ensure fairness, there must be some measure of consistency and transparency in how the Commission decides whether or not to grant leniency under such circumstances. Such guidance is particularly vital in light of the framework set out in section 80 of the Ordinance which envisages leniency being available in circumstances outside the current scope of the Draft Leniency Policy. The Commission has not provided any reasons for this narrowed scope of leniency.

2.5 We therefore recommend that the Commission provides further guidance on situations falling outside the scope of the Draft Leniency Policy.

3. What will be the scope of leniency granted under the policy?

Whether the scope of protection will extend to orders of the Competition Tribunal

3.1 Paragraphs 1.3, 2.1(d) and 2.24 of the Draft Leniency Policy provide that the Commission will undertake not to commence proceedings for a pecuniary penalty against the cartel member who enters into a leniency agreement with the Commission. This is consistent with section 80(2) of the Ordinance.

3.2 The main text of the Draft Leniency Policy is silent as to whether the Commission will apply to the Competition Tribunal (**"Tribunal"**) for an order under section 94 of the Ordinance to be made against the successful leniency applicant. However, clause 2.1 of Annex A to the Draft Leniency Policy (the Template for a Leniency Agreement with an Undertaking Engaged in Cartel Conduct) ("**Annex A**") states that, in addition to not seeking a pecuniary penalty under section 93 of the Ordinance, the Commission agrees not to bring "*any other Proceedings (other than Proceedings for an order under section 94 of the Ordinance as mentioned in clause 4.1c) below declaring that [Party] has contravened the First Conduct Rule…*".

3.3 Annex A therefore indicates that the Commission will not seek any other order from the Tribunal, other than a declaration that the undertaking in question has contravened the First Conduct Rule. We agree that this is the right approach and suggest, for the sake of clarity, that this be reflected in the main body of the Leniency Policy as well. As mentioned above, it is important that the Leniency Policy is sufficiently clear and certain if it is to incentivise potential applicants to apply for leniency.

3.4 We therefore recommend the Commission clarifies in the main text of the Leniency Policy that it will not seek any other order from the Tribunal against a successful leniency applicant, other

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[10] Paragraph 4.2 provides that the Commission may provide favourable treatment in respect of "*contraventions of the First Conduct Rule*".

than a declaration that the undertaking in question has contravened the First Conduct Rule (consistent with Annex A).

Undertakings who do not qualify for leniency under the Draft Leniency Policy

3.5 Paragraphs 1.3 and 2.1(c) of the Draft Leniency Policy state that leniency is available only for the first undertaking that reports the cartel conduct to the Commission and meets all the requirements for receiving leniency. Section 4 of the Draft Leniency Policy then provides that an undertaking who does not qualify for leniency but who cooperates with the Commission may receive "*favourable treatment*". This may take the form of a joint submission between the undertaking and the Commission on the pecuniary penalty to be imposed.

3.6 For the effective detection of, and investigation into, cartels, it is important that cartel members be incentivised to cooperate with the Commission – even if they are not the first in the queue and therefore do not qualify for leniency. The first cartel member who reports the conduct may not necessarily be the one with the most probative evidence regarding the cartel, and the Commission should ensure that the leniency framework encourages the subsequent undertakings in the queue to come forward with all available evidence.

3.7 Under the Draft Leniency Policy, however, it is questionable whether undertakings would have sufficient incentive to do so. The Commission has committed only to "*consider*" whether to grant favourable treatment to undertakings who do not qualify for leniency, and the Draft Leniency Policy provides only limited explanation as to what "*favourable treatment*" could entail. It would be helpful, for example, if the Commission could clarify whether favourable treatment may include a decision not to bring proceedings against an undertaking. This would provide a strong incentive for an undertaking to cooperate fully, and would not affect the impetus to be the first applicant for leniency (as the first applicant would be the only undertaking that is *guaranteed* not to be subject to proceedings for a pecuniary penalty).

3.8 It would be therefore helpful if the Commission could clarify:

(A) what forms and level of "*cooperation*" will be expected of undertakings who do not qualify for leniency but wish to benefit from favourable treatment – for example, if the undertaking were able to provide corroborating evidence, etc;

(B) what other forms of "*favourable treatment*" may be granted to the undertaking – including whether the Commission may decide not to commence proceedings against the undertaking; and

(C) an indication as to what the Commission would include in its joint submission on the pecuniary penalty to the Tribunal – for example whether it would propose a percentage reduction in the penalty, and if so, the possible range of such reduction.

3.9 As to paragraph 3.8(C) above, whilst the decision to impose a pecuniary penalty (and the level of the penalty) is ultimately a question for the Tribunal, it is entirely within the discretion of the Commission to include in the Leniency Policy an indication of the submissions (including proposed percentage reductions in penalty) it may make to the Tribunal. If the Commission is concerned that the content of

such submissions may change over time (e.g. once there is case law on the level of penalty), the Commission could make clear that the content of such submissions may in the future be amended to reflect decisions of the Tribunal.

3.10 **We therefore recommend providing further guidance on the position of undertakings which do not qualify for leniency under the Leniency Policy.**

4. Who can benefit from leniency?

Directors, officers, employees and agents

4.1 Paragraph 2.2 of the Draft Leniency Policy provides, among other things, that leniency will:

(A) "*ordinarily*" extend to any current director, officer or employee of the undertaking; and

(B) extend to any agent, former director, former officer, former partner, or former employee of the undertaking specifically named in the leniency agreement,[11]

provided the relevant individuals provide complete, truthful and continuous cooperation with the Commission throughout its investigation and any ensuing proceedings.

4.2 We assume that leniency would be withheld from such persons only if there is some wrongdoing or failure to cooperate on their part – if this is the case, then more detailed guidance would assist the director, individual or employee in avoiding such conduct or omission. The fact that leniency would not extend to certain individuals would also be relevant to the undertaking, who may wish to take this into account in deciding whether or not to apply for leniency.

4.3 **We therefore recommend clarifying the meaning of "*ordinarily*" and providing guidance as to when leniency will not extend to current directors, individuals or employees of the undertaking.**

4.4 Furthermore, we suggest that paragraph 2.2 of the Draft Leniency Policy and Clause 3 of Annex A be amended so that agents and former directors, partners, officers and employees do not need to be specifically named in the leniency agreement in order to benefit from leniency. There may be practical obstacles to identifying all such persons who were involved in a cartel activity at the time the leniency agreement is entered into, particularly in complex cases where the involvement of certain individuals may become clear only as the investigation progresses. We recognise and appreciate that the Commission's policy allows undertakings to benefit from a signed leniency agreement early on in the leniency process, but it is important that individuals and/or undertakings are not prejudiced as a result.

4.5 We note, for example, that the approach taken by the Competition and Markets Authority in the United Kingdom is to commit not to apply for a disqualification order against any current or former director of

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[11] The fact that such persons must be specifically named is also reflected in Clause 2 of Annex A.

a company which benefits from leniency in respect of the activities to which the grant of leniency relates.[12]

4.6 We therefore recommend deleting the requirement that such persons be "*specifically named*".

5. How do you apply for leniency?

Information required to obtain a marker

5.1 Paragraph 2.7 of the Draft Leniency Policy provides that when a caller contacts the Commission to apply for a marker, the caller "*will be asked to provide sufficient details to identify the conduct for which leniency is sought*", and "*may*" subsequently receive a marker which identifies the time and date of the call.

5.2 However, it is unclear:

(A) what level of detail would be considered "*sufficient*" for the purposes of qualifying for a marker; and

(B) whether such information may be provided on a no-names or hypothetical basis.

5.3 Given the importance of being the first undertaking in the queue, potential callers will likely be under substantial time pressure to apply for a marker. It is therefore critical that they are made aware of the level of detail which the Commission expects them to include in their request for a marker.

5.4 As to (B), we note that the proffer may be made on a no-names basis (see paragraph 2.15 of the Draft Leniency Policy), so we expect the same should apply in relation to the marker. We understand this is the Commission's intended approach and therefore suggest this be made explicit in the Leniency Policy.

5.5 We therefore recommend amending the Draft Leniency Policy so that it provides further information as to when the level of detail provided in a request for a marker would be considered "*sufficient*", and whether the request can be made on a no-names or hypothetical basis.

Information required to enter into a leniency agreement

5.6 Paragraph 2.18 of the Draft Leniency Policy states that the Commission will decide whether or not to make an offer to enter into a leniency agreement "*[b]ased on the proffer and any additional information requested and provided by the applicant*".

5.7 It would be helpful if the Commission could clarify how it will assess the proffer and additional information, i.e. what standard the submitted information would have to reach in order for the

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[12] Paragraph 2.10, CMA Leniency Guidance.

Commission to offer to enter into a leniency agreement (e.g. sufficient to give the Commission reasonable cause to suspect that a contravention of the First Conduct Rule has occurred and to commence an investigation pursuant to section 39 of the Ordinance). The Commission should also clarify that it will assess only the completeness of the information provided to it for the purposes of assessing whether this standard has been met and not, for example, the usefulness of the information to its investigation (which may not be apparent until much later in the process).

5.8 We therefore recommend that the Commission clarifies how it will assess the proffer and additional information provided by the applicant in deciding whether or not to grant leniency.

6. What happens if the leniency agreement is terminated?

Opportunity to make representations prior to the termination of a leniency agreement

6.1 Section 81(5) of the Ordinance requires that, prior to the termination of a leniency agreement, the Commission must consider any representations about the proposed termination that are made to it.

6.2 Whilst Section 3 of the Draft Leniency Policy notes that termination of a leniency agreement is governed by section 81 of the Ordinance, it does not refer to the fact that the Commission will allow an opportunity to make representations or consider such representations before terminating an agreement.

6.3 The opportunity to make representations to the Commission in these circumstances is of utmost importance to the leniency applicant, given that termination will give rise to the possibility of the Commission commencing proceedings against the undertaking and/or any persons previously covered by the agreement. As such, it is critical that the Commission's policy provides for sufficient procedural safeguards to ensure that the undertaking is given full opportunity to make representations, and that the undertaking has the opportunity to respond to the Commission's arguments, before the agreement is terminated.

6.4 We therefore suggest including further details in the Leniency Policy as to the process for making and considering representations under section 81(5) of the Ordinance. To this end, the approach of the Australian Competition & Consumer Commission (the "**ACCC**") may be instructive – the ACCC provides for a procedure whereby it will, if it considers that the leniency applicant has breached its conditions of leniency:

(A) engage in informal discussions with the applicant;

(B) issue a written caution to the applicant;

(C) if the ACCC does not receive a satisfactory response to the above, issue a further letter to the applicant requiring an explanation as to why the ACCC should not revoke leniency; and

(D) If the ACCC does not receive a satisfactory response to the second letter, only then may it advise the applicant in writing that they no longer qualify for leniency.[13]

6.5 We note that the Commission is required to give notice in writing of the termination to the applicant under section 81(2) of the Ordinance, after which there must be a period of at least 30 days for the representations to be made. We propose that issuance of this notice should be preceded by informal discussions with the applicant and a written caution (i.e. paragraphs 6.4(A) and (B) discussed above).

6.6 We therefore recommend amending the Draft Leniency Policy to explain the procedure for making and considering representations under section 81 of the Ordinance.

Whether leniency will transfer to the next undertaking in the queue if a leniency agreement is terminated

6.7 As mentioned above at paragraph 3.5 of this letter, the Draft Leniency Policy currently provides that leniency is available only for the first undertaking that reports the cartel conduct to the Commission and meets all the requirements for receiving leniency. It is unclear what the position would be where a leniency agreement is terminated – in particular whether the undertaking who was party to that agreement would be considered as having failed to meet all the requirements for receiving leniency, such that leniency may be available to the next undertaking in the queue.

6.8 It is important to clarify the circumstances under which the subsequent undertakings in the queue may receive leniency as this could serve as a strong incentive for undertakings to come forward and put forward a marker even where they are not the first in the queue.

6.9 We therefore recommend that section 3 of the Draft Leniency Policy (on termination of leniency agreements) be amended to clarify whether leniency will transfer to the next undertaking in the queue if a leniency agreement is terminated.

We appreciate the opportunity to participate in this important milestone in the development of Hong Kong's competition law. We are available to discuss our views further if this would be useful to the Commission.

Yours faithfully,

Slaughter and May

Slaughter and May

[13] See Section F, ACCC immunity and cooperation policy for cartel conduct (September 2014). Available at: http://www.accc.gov.au/system/files/884_ACCC%20immunity%20and%20cooperation%20policy%20for%20cartel%20conduct_FA2.pdf