

## Global Shipper Forum Submission to the Hong Kong Competition Commission

**Response to the Hong Kong Liner Shipping Association Supplementary Submission of 27 February 2017 requesting that the Commission reconsider its position in its Statement of Preliminary Views of 16 September 2016 and grant a block exemption order for voluntary discussion agreements (VDAs) falling within the Revised VDA Scope defined by the Applicant**

### Introduction

1. The Global Shippers' Forum (GSF) welcomes the opportunity offered by the Hong Kong Competition Commission (the Commission), in an email from its CEO dated 1 March 2017, to respond to the Hong Kong Liner Shipping Association (the Applicant) Supplementary Submission of 27 February 2017.
2. The GSF was formally incorporated and registered as a non-governmental organisation in the United Kingdom in June 2011. The GSF was created in 2006 as a successor to the informal Tripartite Shippers' Group established in 1994. The GSF is the international shippers' organisation that represents thousands of shippers internationally through GSF member associations in Asia, Africa, Europe and North and South America. The main focus of the GSF is to promote the interests of shippers as users on international transportation services across a broad spectrum of issues, including policy, commercial and technical matters.
3. The Applicant requests that the Commission reconsider its position in its Statement of Preliminary Views of 16 September 2016 and grant a block exemption order for voluntary discussion agreements (VDAs) falling within the Revised VDA Scope defined by the Applicant. The request is said to be made 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 as requested in its original application for a block exemption order for liner shipping agreements under section 15 of the Competition Ordinance.
4. The GSF endorses the submission of the Hong Kong Shippers' Council dated 9 March 2017. In particular, the GSF fully supports the Commission's proposal in the Preliminary Statement of Views (the Statement) to exclude carrier discussion

agreements from the exemption. Such VDAs are prohibited under EU competition law and excluded from the scope of the EU Consortia Block Exemption Regulation. These agreements are considered by the European Commission and the OECD 2002 report on liner conferences to be 'hard core' competition restrictions which provide no benefit to shippers in the form of enhanced maritime services or reduced costs. The 2002 OECD report also questions whether the historic anti-competitive practices of international carriers, such as liner conferences and discussion agreements are relevant to market stability, whether in the form of alleged rate stability or service stability, as relied upon by the Applicant in the present context.<sup>1</sup>

5. This Submission is divided into three main sections:
  - (1) General observations
  - (2) Specific comments on the Applicant's Supplementary Submission on VDAs
  - (3) Some Conclusions on VSAs and VDAs.

## General Observations

6. In this section of the Submission, the GSF outlines the main general criticisms of the competition law analysis in the Applicant's supplementary Submission.

### No evidence of efficiencies or causal link between Revised VDA Scope and efficiencies

7. VSAs already cover much of the non-price information exchanged. However, they do not allow discussion or recommendations/voluntary agreements except where required for operational purposes under the VSA.
8. The first Condition for the efficiency exclusion under Section 1 of Schedule 1 of the Competition Ordinance requires convincing evidence of each of the following, according to paragraph 2.6 to 2.12, and in particular 2.7, of the First Conduct Rule Guideline:
  - (a) The efficiencies, which must be objective in nature;
  - (b) A direct causal link between the efficiencies and the agreement;
  - (c) The likelihood and magnitude of each efficiency;
  - (d) How each efficiency will be achieved; and
  - (e) When the efficiencies will be achieved.
9. Section 4 of the Supplementary Submission seeks to demonstrate how the Efficiencies Exclusion criteria apply to information exchanged under VDAs. Not only does it not refer at this stage to justifying the discussion and recommendation aspects of VDAs, but the arguments about the need to make decisions about

choosing to provide Hong Kong with a transshipment service or direct service, “reducing the risk of financial distress or failure” by the carriers (paragraph 4.4), on the basis of “information efficiencies to which even the Revised VDA scope gives rise” (paragraph 4.9), do not satisfy the criteria set out in paragraph 2.7 of the First Conduct Rule Guideline (paragraph 8 above).

**The application for a Block Exemption Order for the Revised VDA Scope is hypothetical as it does not identify any specific restrictions of competition requiring exemption**

10. Section 3 of the Applicant’s Supplementary Submission fails to explain adequately why carriers need a VDA exemption, even if reduced in scope. While the carriers appear to admit that some elements of their Revised VDA Scope infringe the First Conduct Rule of the Competition Ordinance, they fail to identify the actual infringements that they say should be exempted.
11. Their attempt to claim that the Commission identified certain infringements in the Statement is unsubstantiated. The consequence of the Commission’s rejection of the Applicant’s Application for a Block Exemption Order for VDAs is that the carriers need to follow the process for self-assessment if they wish to continue to enter into VDAs. There is no reason why self - assessment should not apply to the shipping industry which is not “unique, including to the information and discussions that take place within VDAs and are specific to the shipping industry, just as the carriers do on the Europe trades under EU competition law. They do not “warrant a block exemption” (paragraph 3.6).

**Applicant’s reliance on Singapore Competition law undermines claims for exemption since there is no requirement that consumers share the benefit of efficiencies**

12. The Applicant has failed to satisfy the four conditions for exemption in Schedule 1 Section 1 of the Competition Ordinance. In particular, it has failed to show that any alleged efficiencies are shared with customers, whether direct or indirect, because it has overlooked in its reliance on Singapore Competition law that it is different when it comes to the conditions for exemption. Unlike Hong Kong and the EU, Singapore does not require a fair share of the efficiencies to be enjoyed by the consumer. This is crucial to understanding why the Applicant’s new (and previous submissions) on VDAs are fundamentally flawed, especially as they have to be seen in the context of VSAs, and in particular the business model of three Global Alliances in an international market dominated by mega ships where there have been no new entrants for 20 years.

13. The main argument of the Applicant appears to be political in the form of a thinly veiled threat to reduce the number of ships calling at Hong Kong, especially for transshipment, because the Hong Kong Competition Ordinance, or its present application by the Commission, does not favour carriers in the way that the Singapore equivalents do so, according to the Applicant. According to industry sources at the Intermodal Asia conference in Shanghai on 20-21<sup>st</sup> March 2017, it is understood that the three main Alliances have already determined for operational and commercial reasons that Singapore is likely to be the main winner in the selection of transshipment ports in reduced main Europe-Asia port pairs, which is a direct consequence of the introduction of mega-ships and the three mega-alliances.
14. In the original application for a Block exemption under Section 15 of the Ordinance, the Applicant claimed that it could not maintain the volume and level of services at the port of Hong Kong, without the rate and surcharge transparency provided by VDAs through their discussion of individual carrier rates and recommendations/voluntary agreements.
15. The Commission has rightly rejected the Applicant's submissions relating to rate stability, service stability and rate/surcharge transparency. In particular, the Commission has pointed out that the only instruments that can be said to contribute to stability are confidential service contracts (introduced by the Ocean Shipping Reform Act amendments to the US shipping Act) and required to be available in the EU (even at the time liner conference cartels still enjoyed a block exemption) , in paragraphs 4.122 and 4.123 of the Statement); that the Shanghai Shipping Exchange provides the most accurate index of prices with there being no need for VDAs (paragraph 4.111 of the Statement); that rate and surcharge transparency facilitate the levying or the introduction of rate increases and surcharges by carriers, in paragraph 4.107 of the Statement and footnote 63 referring to the Transpacific Stabilisation Agreement. In addition, these restrictions of competition were claimed to be reasonably necessary for the so-called efficiencies constituted by the provision of transshipment, as well as direct, services to Hong Kong. The Commission again noted the lack of any evidence and any causal link between such efficiencies and the competition restrictions, to show that VDAs ensure the benefits of transshipment for the Hong Kong economy generally, in paragraphs 4.113 to 4.117 of the Statement.
16. Any suggestion that the current low level of rates were a benefit shared with customers caused by the efficiencies resulting from VSAs or VDAs was exposed in the Statement as overlooking the reality that overcapacity prevents higher rates in the current market conditions. The Commission rightly recognised that this might not be the case in the future, concluding that there was no convincing evidence of a direct link between VDAs and the claimed efficiencies, as required by paragraph 2.7 of the First Conduct Rule Guidelines, in paragraph 4.121 of the Statement. In reality, it is

only VSAs that are capable of providing operational efficiencies. Not only do VDAs not contribute to rate or service stability but they include in their rate escalation armoury the practice of General Rate Increases (GRIs) which the carriers have recently committed to cease on the trades serving Europe, where the European commission says that GRIs, and therefore, GSF submits it also follows that VDAs, facilitate price signalling.

17. Moreover, publicly available information on the topics covered by VDAs meant that there were alternative sources of information less restrictive of competition according to the Commission in paragraph 4.124 of the Statement. This is consistent with the First Conduct Rule Guideline which says that “for the purposes of satisfying the indispensability test of Section 1 of Schedule 1, the parties must demonstrate that the agreement itself, and each of the individual restrictions contained in the agreement, are reasonably necessary to attain the efficiencies. The determinative factor in this context will be whether the restrictive agreement and the individual restrictions in it make it possible to perform the activity in question more efficiently than would likely have been the case in the absence of the agreement or the restrictions.” (paragraph 2.16, the First Conduct Rule Guideline, Third condition).
18. Now, the Applicant argues that the same efficiencies currently enjoyed by Hong Kong will be lost to Singapore unless the “information efficiencies”, said to result from VDAs, are recognised by the Commission as agreements enhancing overall efficiency. By carving out any pricing discussions or voluntary agreements for Hong Kong, the Applicant wrongly claims that the four conditions for exemption in Section 1 of Schedule 1 will be satisfied, justifying the exclusion of VDAs under Section 30 from the First Conduct Rule in Section 6 of the Ordinance, and the issuing of a Block Exemption Order under Section 15 of the Ordinance.
19. According to the Applicant, the Hong Kong Competition Commission should follow Singapore competition law as applied to VSAs and VDAs and accept the past practice of the shipping industry as being in the “broader consumer interest” of the port industry and the wider economy. The simple fallacy in this argument is that the four conditions for the Schedule 1 Section 1 exclusion for agreements enhancing overall economic efficiency are modelled on the EU equivalent exemption provisions. Some other Asian jurisdictions, such as Singapore and Malaysia are different, and in particular do not require that a fair share of the benefits accrue to consumers. This alone undermines the entire approach to the Block Exemption proposal taken by the Applicant. Indeed, it would be welcomed by the GSF if the Commission were to persuade their colleagues in Singapore to recognise that the EU approach is more likely to result in a competition law system that improves competitiveness and consumer choice, rather than simply providing an easier life for the carriers which ultimately will suffer from their own elimination of effective competition.

## VDA's must be assessed in economic context of any VSA's

20. The interplay between VSA's and VDA's on the same trades must be taken into account by the Commission and the Applicant. For this reason, the Commission may not wish to issue a Block Exemption Order as proposed authorising VSA's with market shares based on capacity of up to 45% and based on freight tonnes or teus carried of up to 40%.
21. First, where there is a VDA operating on the same trade as a VSA, its carrier members are likely to account for a much higher share of the overall market than the VSA members, for example, the TSA VDA.
22. Second, in the context of Global Alliances, where there may be only two alliances on a specific trade in future, each with 40% or 45% market share, there is likely to be a duopoly with 80% or 90% market share which will be capable of eliminating effective competition on the trade concerned as there will be no incentive for one alliance (or its members) to compete with the other alliance (or its members), if they are sharing commercially sensitive information and discussing that data with competitors, and even making recommendations/voluntary agreements, under the authority of a VDA which includes members from both alliances.
23. In this context, it is pertinent to recall the significant potential for elimination of effective competition in oligopolistic markets. Albeit in the area of merger control, the European Commission has warned of the non-coordinated (or unilateral) effects of a merger in oligopolistic markets where the merger may result in a significant elimination of competition (paragraph 25, Commission Notice (Guidelines on assessment of horizontal mergers, 2004)). By analogy with the analysis of mergers in oligopolistic markets, the simultaneous operation of Alliances and VDA's in oligopolistic markets could involve: "the elimination of important competitive constraints that the [merging] parties previously exerted upon each other together with a reduction of competitive pressure on the remaining competitors which may, even where there is little likelihood of coordination between the members of the oligopoly, also result in a significant impediment to competition" (or the elimination of effective competition).

## Specific Comments on the Supplementary Submission

24. This Section of the GSF submission provides specific but non-exhaustive comments on the body of the Applicant's Supplementary Submission forming Sections 2, 3 and 4 of that Submission. In particular, the GSF endorses the specific criticisms made by the Hong Kong Shippers' Council (HKSC) in its submission dated 7 March 2017, at paragraph 2.2 a. to j.
25. The main criticisms of these sections in the Supplementary Submission is that they do not provide evidence of the terms in the VDAs in sufficient detail to identify the restrictions of competition which they are alleged to contain. They, therefore, also fail to provide evidence of a causal link between any such restrictions in the agreements and the economic benefits which are claimed to justify exclusion of VDAs from the First Conduct Rule, and to satisfy the efficiency condition (and other three conditions) required for exclusion under Schedule 1 Section 1. Each of the three sections is considered briefly in turn.

#### What the Revised VDA Scope would cover

26. Section 2 of the Supplementary Submission explains what the revised VDA Scope would cover in terms of pricing (paragraph 2.1, 2.2 ...[confidential?]). It does so by listing the particular categories of items that would be specifically authorised for discussion and information exchange (paragraph 2.3). It states that the requested exemption relates only to the authority to discuss and exchange information with respect to these categories (paragraph 2.4:

"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 (emphasis added by GSF).

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 (emphasis added by GSF).”
27. As the HKSC point out in paragraph 2.1 of their Submission, it will be impossible to know whether the carriers will comply with a carve-out for Hong-Kong specific rate discussions or recommendations (described in the Applicant’s Submission at paragraph 2.1). This is because the VDA discussions are in private behind closed doors and not subject to any policing or safeguard mechanism.
28. The exclusion from the Revised VDA Scope, in the underlined sentences of paragraph 2.1 above, of transshipment rates for cargo that is merely transhipped from Hong Kong directly contradicts the Commission’s approach in the Statement, and that avowed by the Applicant, to the effect on competition of including pricing in VDAs. In particular, transshipment rates affect competition in Hong Kong because of the impact on competition between Hong Kong and other regional ports.
29. It is clear from the following criticisms of the proposed revised VDA Scope as described under the categories of information exchange and discussion listed from (A) to (H) below, that they are merely a description of the categories of information to be exchanged and discussed, providing no evidence of a causal link between the alleged efficiencies and restrictions of competition in the agreements. The competition law infringements identified by the GSF are supported by paragraph 2.2 a. to j. of the HKSC Submission:
- “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 (emphasis added by GSF).

...

- (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.. The information is helpful to carriers because it provides a single and reliable source for these important types of detailed market information (emphasis added by GSF).
30. It is not clear what are the carriers costs that are lower, or services to shippers which are better, as a result of their discussing specific cargo flows and exchanging statistics on which port ranges and trade lanes have declining or increasing cargo throughput, both current and forecast (category (A) subparagraph (i)). In reality, the Applicant is asking for a block exemption for capacity management and supply manipulation as contended by the HKSC (paragraph 2.2 a.).
31. Category (A) subparagraph (iii) indicates that alternative information and data is publicly available. This is sufficient for independent individual decision making by the carriers. Discussing this data and sharing individual commercially sensitive information can only have the purpose of removing competition and giving the VDA carriers an unfair negotiating advantage over their shipper customers (see paragraph 2.2 b. of the HKSC Submission).

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

32. There can be no explanation as to why carriers wish to discuss common costs, or carry out break-even studies, other than that they seek to keep prices above price floors or minimum prices, see paragraph 2.2 c. of the HKSC Submission. Competition law requires them to make individual independent decisions on rates including surcharges such as the bunker adjustment factor.

(C) *Vessel utilisation and capacity levels*

33. The benefits of exchange of information on individual utilisation and capacity levels are considered by the Applicant only from the point of view of how helpful this is to carriers. Consistent with the general approach, no consideration is given to the needs of the customer shipper.

(D) *General industry issues*

34. As explained by the HKSC in paragraph 2.2 d. of its Submission, there are many open and public forums and conferences dealing with industry issues such as port congestion, equipment repositioning, piracy and container weighing, so there is no justification for discussing these issues in private. To the extent these issues are operational, including the first two issues, they are covered by VSAs. It is notable that the only example provided by the Applicant relates to piracy and has nothing to do with Hong Kong.

(E) *General economic issues/trends*

35. According to the Applicant, 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, macroeconomic trends, manufacturing and retail inventory levels, fuel prices, wholesale prices, retail sales, consumer confidence and spending, exchange rates, and trade and manufacturing investment patterns

36. This category of information exchange and discussion is a good example of where the information is readily available in the public domain and trade associations and general industry bodies involving all stakeholders are more appropriate venues than a private VDA meeting.

(F) *Regulatory developments and compliance issues*

37. No reasons are given by the Applicant as to why sharing information on regulation will lead to greater compliance by carriers acting together as opposed to adopting individual independent decisions.

(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 (emphasis added by GSF).

(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.

38. There is a contradiction in subparagraph (G) (i) between discussing potential model service contract terms and conditions and never discussing specific commercial terms since it must be intended that model terms are used in specific service contracts. As submitted by the HKSC in paragraph 2.2.e., this sort of discussion will facilitate aligned adoption and practice.

39. Not only is the "outreach" referred to in subparagraph (G) (ii) unnecessary, it is unhelpful to shippers who benefit from individual negotiations as explained by the HKSC in paragraph 2.2 f. of their Submission. The surcharge notice imposed by the Intra-Asia Discussion Agreement attached as Appendix 1 to the HKSC Submission demonstrates how VDAs eliminate negotiation on surcharges. This notice also indicates what might be seen as discrimination between Hong Kong and Singapore where the rates are much lower.

40. This category also provides insufficient evidence to identify the relevant restrictions and any efficiencies justifying their exclusion. There are not even any examples provided.

(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 (emphasis added by GSF).
- (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.

41. Paragraph (H) (i) above indicates that the main purpose of VDAs, and their price indices such as the Transpacific Stabilization Agreement (TSA) Revenue Index referred to in paragraph (H) (ii) above, is to cover all the carriers in the trade. The purpose of VDAs is to eliminate effective competition in this way which is why discussion agreements are considered hard core competition restrictions in certain jurisdictions such as the EU. A single VSA may not cover the whole trade and must demonstrate that its market power is limited.

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

42. Section 3 of the Applicant's Supplementary Submission explains why the carriers say that they need a VDA exemption, even if it is reduced in scope. However, the Applicant's new application is not only technically inadmissible (see HKSC Submission paragraph 1) but also hypothetical. While the carriers admit that some of the non-

price information exchange and recommendations/voluntary agreements in their VDAs infringe the First Conduct Rule of the Hong Kong Ordinance, they do not identify any of the restrictions (see paragraph 3.1, despite the attempts to claim that only the Commission or others say that there are any infringements once the pricing terms are removed). This precludes any consideration of the application by the Commission of the Efficiency Exclusion (see paragraphs 10 and 11 above).

43. In any event, self-assessment should enable the Applicant to determine whether the VDAs restrict competition and qualify for the Efficiency Exclusion in the light of the First Conduct Rule Guideline, just as they do in the EU and every other industry must in Hong Kong (see HKSC Submission paragraph 2.2 g.), contrary to paragraphs 3.3 to 3.5 of the Supplementary Submission.
44. In particular, suggestions that the shipping industry is different or even unique are completely unsupported, contrary to paragraph 3.6 of the Supplementary Submission.

#### **Application of the Efficiencies Exclusion criteria to information exchanged under VDAs**

45. Section 4 unsuccessfully seeks to show that the four conditions required to qualify for the Efficiencies Exclusion are met. In particular, the Applicant has failed sufficiently to identify any relevant efficiencies and their causal link to specific restrictions of competition in the agreements (see paragraph 9 above).

##### ***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 (emphasis added by GSF).”

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

*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”*

46. None of the arguments set out in paragraphs 4.2 to 4.9 under the two above headings explain why VDAs produce efficiencies which benefit shippers and end consumers in Hong Kong trades. The carriers suggest that the VDAs are designed to comply with the competition rules in other jurisdictions such as Singapore, which the Applicant appears to favour, over Hong Kong. There is no evidence that the VDAs choose Hong Kong as a transshipment port rather than choose to reduce the services, as planned in future. On the contrary, the negative effect of VDAs on competition drive shippers away from Hong Kong (see HKSC Submission paragraph 2.2 h.). In any

event, it is not clear why competition law could permit VDAs to influence the choice of Hong Kong as a transshipment super-connector maritime centre or promote the One Belt One Road policy.

47. In particular, there is no evidence as to how the VDAs (as opposed to market forces) result in economies of scale and reduced costs per teu that lowers the costs and thus retail prices for all consumer products that are transported to Hong Kong, contrary to paragraph 4.2 of the Supplementary Submission (set out above).

***Second condition: consumers receive a fair share of the efficiencies***

48. No evidence is provided of the alleged benefits to shippers or end consumers of the lower cost of goods and higher employment said to result from the Revised VDA Scope allowing Hong Kong to compete against other regional ports as a transshipment hub, contrary to paragraphs 4.10 to 4.12 of the Supplementary Submission. There is certainly no evidence that the carriers have a normal commercial dialogue with shippers as to their requirements rather than dictating the nature of the services available.

49. As the HKSC Submission paragraph 2.2 i. indicates, while carriers claim that VDAs allow them to deploy vessels more efficiently, in reality the purpose of VDA meetings is to discuss market features that will enable them to increase rates. The HKSC illustrates this issue by attaching at Appendix 2 to its Submission the transpacific trade freight index which shows that current low season rates are three times higher than those of the 2016 peak season. This evidence tends to contradict paragraphs 4.13 and 4.14 of the Supplementary Submission.

***Third condition: indispensability to the attainment of efficiencies***

50. It is very difficult to see how the restrictions of competition in the Revised VDA Scope could be claimed to be indispensable to the efficiencies alleged to be created by them. If the test referred to in paragraph 17 above is applied, it is clear that there are alternative sources which are as useful as VDAs and alternative solutions which are practicable, contrary to paragraphs 4.15 to 4,23.

51. In particular, as the HKSC points out at paragraph 2.2 j. of its Submission, the Revised VDAs Scope will still allow the carriers to exploit an unfair playing field against the shippers. In this connection, it is not clear why the VSAs to which the Commission proposes to apply a Block Exemption Order would not perform the legitimate objectives of the Applicant's desired information exchange without the discussion aspects of VDAs.

***Fourth condition: No possibility of eliminating competition***

52. The claims in paragraphs 4.24 to 4.25 of the Supplementary Submission that the market is highly fragmented with a strong degree of existing competition between carriers, as evidenced by historically low rates (which are forecast to continue for the coming years), ignores the increased consolidation in the relevant trades resulting from Global Alliances and the increasing merger trend.

53. If the Commission were to permit VDAs as well as VSAs on the Hong Kong trades, the Supplementary Submission itself demonstrates that effective competition will be eliminated.

## Conclusions

54. There are three main points which the GSF submits demonstrate that no form of VDA may justify exclusion from the First Competition Rule.

55. First, the main instrument that is capable of providing stability in international shipping markets is the confidential individual service contract. However, there is a serious risk that carriers are using the current VDAs and Global Alliances to agree limits on the volume of containers that carriers will agree to transport under a service contract since they can command much higher spot prices.

56. Second, at no point in the Applicant's Supplementary Submission do they show any interest in understanding their customers' needs. This is symptomatic of the carriers take it or leave it approach to their customers which explains their failure to understand that VDAs are contrary to the interests of their customers. It also reflects their attempt to make the Commission follow Singapore Competition law and ignore the requirement that efficiencies must be shared with shippers and end consumers before any restriction of competition may be excluded under the Efficiency Exclusion in Schedule 1 Section 1 of the Hong Kong Ordinance.<sup>μ</sup>

57. Finally, this GSF submission, and that of the HKSC dated 7 March 2017, support the rejection of the Applicant's original application for a Block Exemption Order and that for the Revised VDA Scope. It is also submitted that the Commission needs to carefully review the market for Global Alliances before adopting such a high market share threshold for any VSA Block Exemption Order as the proposed 40% and 45%. With VDAs operating on neighbouring trades to Hong Kong covering the whole trade and the likelihood of only two Alliances on the same trade, there is a serious risk that competition will be eliminated on Hong Kong trades to the detriment of shippers and end consumers.

27 March 2017

31. <sup>1</sup> See <http://www.oecd.org/dataoecd/13/46/2553902.pdf>