

## Hong Kong's Competition Bill - Implications for Directors & Senior Executives

As most readers will be aware, a comprehensive cross-sector Competition Bill (the "Proposed Law") is currently before Hong Kong's Legislative Council. A Bills Committee is currently reviewing the Proposed Law, which according to the current legislative schedule may be enacted in the first half of 2012.

The Proposed Law aims to prohibit conduct that prevents, restricts or distorts competition in Hong Kong, and contains three key prohibitions. In addition to prohibiting certain M&A transactions that restrict competition in Hong Kong, the Proposed Law contains a generally worded prohibition of anti-competitive agreements and a prohibition against unilateral conduct that constitutes abuse of substantial market power. These latter two prohibitions are collectively referred to as the 'conduct rules'.

According to the Proposed Law, any contravention of the conduct rules will expose the concerned company to penalties amounting up to 10 percent of global turnover - one of the broadest pecuniary penalty formulas under any competition law regime around the world. Additionally, the relevant enforcement body (a proposed new Competition Tribunal) will be empowered to impose a wide range of orders against the company, including orders requiring that it divest assets or exit markets as punishment for transgressions.

These penalties are obviously significant enough to demand the Proposed Law be given the full attention of boardrooms across Hong Kong. However, in addition to threats to a company's finances and permitted scope of operations, company directors and senior executives need to be aware that they may also face significant financial and other risks *as individuals* if they are involved in the operation or management of a company that contravenes the law.

In this update, we summarise these risks and explain how the Proposed Law may impact the rights and responsibilities of company directors and senior executives.

### Pecuniary penalty

According to section 91 of the Proposed Law, the Competition Tribunal's power to impose pecuniary penalties in response to identified contraventions of the conduct rules extends to fining any person 'involved' in such a contravention. This clearly includes company directors and executives.

In particular, directors and executives may be at risk where they aid or abet, or are knowingly concerned in (directly or indirectly), a contravention. This may include, for example, where a director personally oversees, takes part in, or signs off on an arrangement that the Competition Tribunal later deems to be contrary to the conduct rules, or perhaps

even wilfully ignores information that suggests a contravention is occurring.

While it can be expected that such risks will usually be higher for individuals directly involved in the day-to-day management or supervision of a company, this does not mean that individuals holding roles such as non-executive directorships can assume that their risk of personal liability is negligible. The experience of foreign competition regimes shows that while such individuals may not be expected to have an intimate knowledge of the company's day-to-day activities and transactions, they are expected to challenge the decisions and actions of the executive directors where appropriate. They may also be responsible for internal audit within a company. As part of such functions, competition regulators may reasonably expect individuals holding positions such as non-executive directorships to ask appropriate questions of the company's executives, and to ensure that appropriate compliance methods have been adopted to prevent and detect breaches of competition law.

Importantly, directors and senior executives will not be able to receive indemnification from their employers in respect of any liability they may incur to pay a pecuniary penalty for violations of the competition law - or the costs of defending an action in relation to the law where such a penalty is imposed or conviction recorded. This is expressly stipulated in section 167 of the Proposed Law, and applies in respect of both regulatory and private action enforcement of the Proposed Law.

## Disqualification orders

Section 99 of the Proposed Law empowers the Competition Tribunal to make an order disqualifying a person from being a director of a company or from otherwise being concerned in the affairs of a

company, if the company has contravened a conduct rule and the Competition Tribunal considers that the person's conduct as a director makes the person unfit to be concerned in the management of the company. In determining whether such an order is appropriate, the Tribunal is required to have regard to matters such as whether the person contributed to the contravention, or should have known or suspected that a contravention would occur but did not take steps to prevent it. Such an order will effectively preclude the person from being (or continuing to be) in any way concerned in the management of a company for a period of up to five years.

Disqualification powers are not new to Hong Kong's regulatory environment, with bodies such as the Securities and Futures Commission already empowered to seek similar orders against directors and senior executives involved in serious breaches of the Securities and Futures Ordinance ("SFO"). However, it is arguable that the broad nature of the Proposed Law's conduct rules may give rise to a greater level of compliance uncertainty than will usually be the case with legislation such as the SFO, and this will make many directors and executives nervous about their capacity to mitigate risk in this area.

For example, although it may be reasonably straightforward to take steps to identify and eradicate blatant company participation in so-called 'hardcore' cartel activity (such as price-fixing and market-sharing), it can be much more difficult to determine the legality under a competition law of other common business activities such as information or equipment sharing between rivals or aggressive pricing strategies by companies with a strong degree of market power. Whether or not such activities are permitted will usually require consideration of a broad range of economic and

market factors. Indeed, the experience of many foreign competition regimes shows that regulatory and judicial views on such issues regularly shift - meaning risk management can be a very challenging task for a business and relevant management personnel.

It is expected that further guidance on the intended application of the Proposed Law's disqualification power would be provided after enactment, perhaps drawing on existing guidance relating to similar powers vested in competition law regulators in other jurisdictions. For example, the UK Office of Fair Trading ("OFT") recently issued revised guidelines relating to the director disqualification orders that may be issued in response to a contravention of UK competition laws, which guidelines include helpful information on issues such as when the OFT will consider that a director "ought to have known" that a contravention was occurring and thus ought to have taken steps to try and bring the contravention to an end.

### Risks of being sued by the company?

Directors also potentially face the risks of being sued by their company if they are relevantly involved in a breach of law that exposes the company to penalty or loss. However, a recent English decision suggests this risk may be narrowed in a competition law context. In *Safeway Stores v Twigger & Ors* [2010] EWHC 11 (Comm), England's Court of Appeal ruled that the company Safeway could not recover from certain former directors and other former employees amounts (more than £10 million) that Safeway had agreed to pay as part of settlement of an investigation by the UK Office of Fair Trading into competition law contraventions in which those persons were said to have been relevantly involved. Safeway argued that the former directors and employees had

breached their contracts of employment, had breached fiduciary duties they owed to Safeway, and had been negligent - but the UK Court of Appeal ruled that Safeway's liability was personal and could not be passed to its employees (even if they were largely responsible for the infringement).

The court noted that the aim of the UK competition law was to protect consumers and the general public from anti-competitive trade practices, and suggested that this aim would be undermined if a company that was fined for a contravention could pass on its liability to individual employees.

Of course, it remains to be seen how this issue would be dealt with in Hong Kong in the context of the Proposed Law.

### How should directors and executives be preparing?

The most important steps directors and executives should take to prepare for the Proposed Law is ensuring they - and their companies - are properly educated on all aspects of the law. Although the conduct rules in particular are framed very broadly, and crucial further guidance on the scope of those rules will be provided only after the Proposed Law is enacted, reviewing how similarly worded rules have been applied in foreign regimes can assist business operators to undertake an immediate assessment of their likely impact in Hong Kong.

Directors and executives should also ensure they understand their rights as individuals in the context of the Proposed Law. Apart from the issues dealt with above, such as when directors and senior executives may face serious penalty or disqualification risks as individuals, and the scope of permissible company indemnities, this includes

matters such as when they may benefit from seeking ‘leniency’ deals with the proposed new Competition Commission (which will investigate suspected or alleged contraventions of the Proposed Law, and prosecute relevant cases before the Competition Tribunal).

According to section 79 of the Proposed Law, the Competition Commission will be empowered to enter into leniency agreements with persons who co-operate in an investigation or court proceedings relating to a suspected contravention of the conduct rules, pursuant to which those persons will receive immunity from prosecution or a guaranteed reduction in penalty. These types of arrangements are common to many competition law jurisdictions, and encourage persons who have participated in a contravention (such as an unlawful cartel) to confess to the existence of the unlawful arrangement and provide evidence that facilitates successful prosecution. The Bill contemplates that such leniency arrangements may be entered into with a business concerned in relevant conduct rule contraventions, or with individuals such as directors and officers. Accordingly, where a director or senior executive has concerns about the potential ramifications they and their business may face for a contravention of a conduct rule, it will be appropriate to consider making an application for leniency.

Additionally, directors and executives should ensure their companies implement comprehensive compliance policies and compliance programs, specifically tailored to reflect the major risks likely to arise in their industry sector and with regard to the structure of their business.

Consideration should also be given to active participation in the debates that are currently taking place in Hong Kong regarding key aspects of the Proposed Law, and in the context of ongoing review of the Proposed Law by a Legislative Council Bills Committee. Interestingly, the Bills Committee’s review has already included a significant focus on how the Bill will impact directors, and a number of business operators have made submissions to the Bills Committee raising concerns relating to this area.

There is no doubt that the Proposed Law will continue to be a lightning rod for debate and discussion in Hong Kong in the months ahead, as its enactment will lead to significant changes to the regulatory landscape affecting nearly all Hong Kong businesses. Additionally, as this article has explained, the Proposed Law will raise a number of new issues and concerns for directors and senior executives within companies doing business in Hong Kong.

By empowering the Competition Tribunal to penalise and disqualify directors and senior executives for their role in competition law contraventions, the Proposed Law clearly sends a signal to such individuals about the importance of their role in ensuring appropriate conduct of, and influencing the compliance cultures within, their companies. It is crucial that this signal is heeded, and that the task of risk management and compliance preparation is made a high priority for such individuals.

## Contact Us

### **John Hickin**

Partner, Mayer Brown JSM

**T:** +852 2843 2576

**E:** [john.hickin@mayerbrownjism.com](mailto:john.hickin@mayerbrownjism.com)

### **Hannah Ha**

Partner, Mayer Brown JSM

**T:** +852 2843 4378

**E:** [hannah.ha@mayerbrownjism.com](mailto:hannah.ha@mayerbrownjism.com)

### **Gerry O'Brien**

Senior Associate, Mayer Brown JSM

**T:** +852 2843 4355

**E:** [gerry.obrien@mayerbrownjism.com](mailto:gerry.obrien@mayerbrownjism.com)

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