Journal of Antitrust Enforcement, 2020, 0, 1–7
doi: 10.1093/jaenfo/jnaa004
Contemporary Critique

The Nutanix judgment—practical implications for competition law in Hong Kong

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I. INTRODUCTION

The Hong Kong Competition Tribunal ('Tribunal') handed down two landmark judgments in May 2019. As the first substantive competition law enforcement decisions since the Competition came into full effect in December 2015, these decisions laid the foundations for future competition law enforcement in Hong Kong and paved the way for legal interpretation of some key provisions of the Competition Ordinance.

One judgment concerned a market sharing and price-fixing case (the decoration works case),[1] while the other involved a 'vertical bid-rigging' scheme (the Nutanix case).[2] Both judgments made extensive reference to competition case law from the European Union (EU), UK, USA, Australia, and Canada. While such references give reassurance to practitioners that the Tribunal will adhere to internationally accepted principles and interpretations of competition law (as was widely expected), the Tribunal's application of those overseas principles to the facts, particularly in Nutanix judgment, demonstrated that the interpretation of the Competition Ordinance will not necessarily follow the approach taken in other jurisdictions.

This short commentary will look at the Nutanix judgment and highlight some of the distinctive points that practitioners should be mindful of when advising on the Competition Ordinance in Hong Kong.[3]

II. BRIEF BACKGROUND AND THE TRIBUNAL'S KEY FINDINGS

In July 2016, a tender was issued by the Hong Kong Young Women's Christian Association (YWCA), a social services organization. The tender related to the supply and installation of a new information technology (IT) server system based on Nutanix Technology. Four IT companies, namely BT Hong Kong Limited ('BT'),

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1 *Competition Commission v W Hing Construction Co Ltd & ors* (No 2) [2019] HKCT 3.

2 *Competition Commission v Nutanix Hong Kong Ltd & ors* (No 3) [2019] HKCT 2 [hereafter, 'Judgment'].

3 Appeals have been lodged against both judgments.

SiS International Limited ('SiS'), Innovix Distribution Limited ('Innovix') and Tech-21 Systems Limited ('Tech-21'), submitted bids in response to the tender.

Noting multiple similarities and common mistakes found in the bid documents of these companies, YWCA made a complaint to the Hong Kong Competition Commission ('Commission'). It transpired that a sales manager from the supplier of the technology for the IT server system, Nutanix Hong Kong Limited ('Nutanix'), had entered into bilateral agreements (and one trilateral agreement) with the IT companies to put in 'dummy bids' for the same tender.

In its judgment, the Tribunal found all but one of the respondent companies to be guilty of bid-rigging in contravention of the First Conduct Rule, being the prohibition against anti-competitive agreements in the Competition Ordinance.[4] In summary, the Tribunal's findings were as follows:

a. In cases where the Commission asks the Tribunal to impose pecuniary penalties, the requisite standard to which the Commission must prove its case before the Tribunal is the criminal standard of proof, ie proof beyond reasonable doubt, due to the application of human rights protections in Hong Kong.[5,6]
b. Nutanix and BT entered into an agreement to procure the submission of four dummy bids from SiS, Innovix, Tech-21, and a fourth company called iCON Business Systems Ltd ('iCON').[7] Pursuant to such agreement, Nutanix entered into separate bilateral agreements with those companies to put in dummy bids and used tender documents provided by BT to prepare documents for those companies. As between Nutanix, BT, and Innovix, there was also a trilateral agreement to the same effect.[8]
c. With the exception of the agreement between Nutanix and SiS, the Commission had proved beyond reasonable doubt that each of the bilateral and trilateral agreements vis-à-vis Nutanix, BT, Innovix, and Tech-21 had been reached on the facts, and each of those agreements had the object of preventing, restricting, or distorting competition in Hong Kong (referred to as 'harming competition').[9]
d. Procedurally, as such conduct fell within the definition of 'bid-rigging' in the Competition Ordinance, it constituted 'serious anti-competitive conduct' under the Ordinance. As the Commission had no reasonable cause to believe that this was not the case at the time of commencing enforcement proceedings, the Commission was under no obligation to issue a 'warning notice' to the respondents before commencing proceedings.[10]

4 Section 6 of the Competition Ordinance.
5 The Commission is not required to prove every element to a criminal standard and the Tribunal is entitled to consider the evidence 'as a whole'.
6 See paras 71–72 of the Judgment.
7 Interestingly, the Commission did not bring proceedings against iCON because iCON decided not to make good its bilateral agreement with Nutanix by not submitting its bid.
8 See paras 266 and 417 of the Judgment.
9 See para 437 of the Judgment.
10 See para 522 of the Judgment.

e. With respect to SiS, the acts of the SiS employee in reaching an agreement with Nutanix and submitting the bid in question were not attributable to the employer company. This was because the SiS employee had 'gone rogue' and acted on his own in doing so, such that the Commission failed to show that there was a sufficient connection between the acts of the SiS employee and the company.[11]

The Tribunal therefore concluded that Nutanix, BT, Innovix, and Tech-21 contravened the First Conduct Rule and were liable to have orders made against them accordingly.[12] The application as against SiS (and as against Nutanix in relation to the alleged agreement with SiS) was dismissed. The orders that should be made consequent upon the Tribunal's findings and conclusions are to be dealt with in a subsequent hearing.[13]

The legal principles enunciated in the Nutanix decision, particularly the principles relating to the standard of proof, the object of harming competition, and the requirement for the Commission to issue a warning notice, were also applied to the decoration works judgment,[14] which was issued by the same judge on the same day.

Observers quickly pointed out that both judgments cited extensively overseas jurisprudence and lauded the Tribunal's alignment with competition law principles that are generally recognized internationally. The natural inclination for practitioners would be to assume that overseas principles, particularly EU jurisprudence, are now recognized as generally applicable in Hong Kong. However, upon a closer look, the picture is not so straightforward. Practitioners should be aware that there remain a few distinctive points arising from the Tribunal's judgment such that overseas principles should not necessarily be assumed to apply in Hong Kong. In particular, the criminal standard of proof of beyond reasonable doubt in a regime involving only civil liability is specific to Hong Kong. We discuss three additional—perhaps less obvious—points below.

III. DISTINCTIVE POINTS ARISING FROM THE TRIBUNAL'S JUDGMENT

Tribunal is willing to recognize atypical cartels

The Tribunal has demonstrated that it is ready and willing, at the very outset of the competition law regime in Hong Kong, to recognize atypical cartels as 'object restrictions', even in the absence of case precedent in competition law jurisdictions across the world.

The striking feature of the facts in the Nutanix case is that it was not a typical horizontal bid-rigging cartel or the typical cover pricing case that usually spans a

11 See paras 555–556 of the Judgment.

12 See para 562 of the Judgment.

13 As of the time of writing, these hearings are fixed to be heard in Q1 2020, potentially almost one year from the Judgment.

14 See *Competition Commission v W Hing Construction Co Ltd & ors* (No 2) [2019] HKCT 3, paras 39, 125, 330–332.

series of tenders as the bidders 'take turns'. Instead, it was a one-off, tender-specific arrangement between a supplier and a reseller, in which the supplier agreed to procure other resellers into putting in other bids for purposes of satisfying a 'five bid minimum' rule in the end-user's procurement rules. There was no agreement amongst competitors for the purposes of artificially inflating prices.

However, this did not stop the Tribunal from categorizing the arrangement in question as one that had the object of harming competition. In doing so, the Tribunal cited the leading EU case of *Groupement des cartes bancaires v European Commission*[15] as the basis for the interpretation of the concept of an 'anti-competitive object' for the purposes of the First Conduct Rule.[16] This came as no surprise to practitioners, as the First Conduct Rule is modelled on Article 101 of the TFEU.[17]

The Tribunal noted that the key holdings of the Court of Justice of the European Union ('CJEU') in that case, including the finding that the General Court in *Cartes Bancaires* was wrong to find that the concept of a 'by object' restriction must not be interpreted 'restrictively'.[18] However, the Tribunal went on to consider that the object box could nevertheless be expanded, in that '[a]greements not of a kind considered before may yet be found to be restrictive by object upon a proper assessment in light of their own content and context.'[19] This is interesting, as the CJEU's ruling in *Cartes Bancaires* has since been hailed as putting an end to the ever more expansive approach of the European Commission and the General Court to expand the concept of the 'object box'.[20]

Although no case cited in the judgment expressly supported the notion of a vertical bid-rigging cartel, in the Tribunal's assessment, an anti-competitive object was nevertheless found in the legal and economic context of this case. In particular, despite the respondents' disputes on the facts during trial, the Tribunal found that each of the following agreements had the object of harming competition: (i) the bilateral agreement between Nutanix and BT; (ii) the trilateral agreement between Nutanix, BT, and Innovix; and (iii) the bilateral agreement between Nutanix and Tech-21. In particular, Nutanix and BT were found to have agreed to procure four 'dummy bids' (explained as 'non-genuine' bids in the judgment), whereas Innovix and Tech-21 were each found to have agreed with Nutanix to submit a bid which was not intended to win but to help someone else's bid.

On the basis of these findings, the Tribunal did not have to consider the legal submissions raised by the respondents during trial on the relevance of reasonable foreseeability of the conduct of other parties[21] and focused on the principles concerning tender processes and bid-rigging enunciated in *Apex Asphalt and Paving Co Ltd v*

15 Case C-67/13P *Groupement des cartes bancaires v European Commission* [2014] EU:C:2014:2204.

16 See paras 35–39, 382–390 of the Judgment.

17 See para 24 of the Judgment.

18 See para 384 of the Judgment.

19 See para 386 of the Judgment.

20 Richard Whish and David Bailey, *Competition Law* (9th edn, OUP 2018) 123–27. See also Grant Murray, 'In Search of the Obvious: Groupement des cartes bancaires and 'By Object' Infringements under EU Competition Law' (2015) 36 (2) ECLR, 47; David Bailey and Laura Elizabeth John (ed), *Bellamy & Child: European Union Law of Competition* (8th edn, OUP 2019) 166–67.

21 For example, see paras 45–49 of the Judgment.

Office of Fair Trading[22] and *SPO v Commission*.[23] While the Tribunal conceded that both cases concerned horizontal cartels, it considered the principles articulated in those cases to be equally applicable in the context of vertical agreements or concerted practices.[24]

As discussed further below, the Tribunal essentially reasoned that the arrangements in question impugned upon YWCA's expectation for competition in its tender, in that the arrangement of dummy bids for purposes of making up the numbers required in YWCA's procurement rules gave YWCA the false impression of competition. The mischief was to deceive the tenderee into thinking that a bid was genuine when it was not. This allowed the Tribunal to find that the 'vertical bilateral arrangements' had the object of harming competition.

The Tribunal's approach to the economic context is a broad one

A notable fact in the Nutanix case is the context in which the 'dummy bids' arose. In the first tender, only one company (BT) submitted a bid, which suggested that only one company was interested in this contract. However, this did not comply with the YMCA's rules (which required a minimum of five bidders) and thus led to the various bilateral and trilateral agreements such that BT could win the second tender. The respondents argued that there was little competition in the first place and that the respondents did not find this contract a particularly attractive opportunity. An argument could be made, therefore, that the proper interpretation of the relevant economic context was that neither Innovix nor Tech-21 (or SiS) would have competed for the contract in any case. In other words, in the context of the second tender, the 'dummy bids' could be argued to have no impact on competition.

The Tribunal was not swayed by these arguments. It briefly considered what would have happened had the respondents not entered into the bilateral and trilateral agreements, and noted that YWCA would have made decisions on its next steps based on the 'true conditions of the market',[25] which reflects a very broad approach to considering the economic context. The Commission also noted that the objective purpose of the relevant agreements 'was to interfere with that process, and to lead YWCA to believe it had received additional genuine bids and to award the tender on that mistaken basis'.[26] The Tribunal seems to have placed importance on the authenticity of the bids rather than consider the conditions of competition in the second tender.

In any case, the Tribunal simply reasoned that, on its interpretation of the relevant context, the relevant agreements had the object of harming competition because the 'dummy bids' would 'result in the tender being awarded by the procurer in the false belief that it had in fact received the necessary number of genuine bids' and thereby '[distort] the competitive process and [prevent] any further potential competition'.[27]

22 [2005] CAT 4.
23 Case T-29/92 *SPO and others v Commission* [1995].
24 See para 395 of the Judgment.
25 See para 397 of the Judgment.
26 ibid.
27 See para 427 of the Judgment.

In the end, notwithstanding the arrangement between the parties, there were only four bids (because iCON did not submit a bid) and thus YWCA's requirement was again not met. In the third tender, only one bid (from IT Channel (Asia) Ltd) was received. Finally, YWCA did not conduct another tender and awarded the contract directly. It is understood that the prices YWCA paid in the end were actually higher than even some of the 'dummy bids' in the second tender. Although there were some differences in the specifications, YWCA may have been better off accepting even a 'dummy bid' than direct procurement.

From a practitioner's perspective, this is a stark reminder that the Tribunal will take a fairly formalistic approach towards cartel cases, even for atypical cartel conduct and it would be difficult to win any argument suggesting the agreement in question had no impact on competition due to the broad interpretation of the economic context by the Tribunal.

Successful 'rogue employee' defence

A third area that is specific to the Hong Kong competition law regime is the availability of the rogue employee defence.

Competition laws typically render companies responsible for acts of its employees carried out during their employment which give rise to infringements of competition law.[28] The Tribunal, however, applied common law canons of interpretation to the First Conduct Rule, taking into account its language, content, and policy, to identify a special rule of attribution that allowed one of the respondents (SiS) to escape liability by demonstrating that its employee's conduct was not attributable to the employer company.

The Tribunal considered that there must be a 'sufficient connection' between the acts of the employee in question and the undertaking so that the former can properly be regarded as part of the latter in the relevant context.[29] That sufficient connection is often established if the employer has put the employee in his position to do the kind of acts in question. However, in certain circumstances where an employee has 'gone rogue' in carrying out the contravening acts in question, that connection may not be sufficient.

The facts in which this rogue employee defence arose are considered to be case specific. SiS was a distributor of IT products and sold only to resellers, not end-users such as YWCA. SiS does not bid in tenders at the invitation of end-users as part of its business. Tendering is not within the job description of anyone in SiS. There had been at least two competition law compliance training sessions since the employee in question started his employment with SiS.

The SiS employee in question was a junior employee who did not have the responsibility or authority to deal with end-users or to submit tenders to them or to anyone else. He had no authority to sign any outgoing documents for SiS. SiS had in place a Code of Conduct for its employees prohibiting anti-competitive conduct. The Commission failed to show that the SiS employee's supervisors were cognizant

28 For instance, in the EU and the UK, acts of employees are generally regarded as part of the undertaking. See para 323–340 of the Judgment.

29 See para 372 of the Judgment.

of his arrangements with the representative of Nutanix. In these circumstances, the Tribunal held that there was no sufficient connection between the acts of the employee in question and SiS for purposes of attributing liability to the employer.

It is unclear whether the success of the defence hinges on whether the employee had 'gone rogue' in the sense that: (i) the employee acts outside his/her scope of work; (ii) the employee acts without authority; or (iii) the employee acts outside the business practices of the employer company, or whether other or further circumstances may 'break' the connection between the acts of the employee and the employer.

Nevertheless, the availability of this defence could prove to be an important defence in future cases. Importantly, it will be an important consideration to take into account at early stages of determining a company's defence strategy—whether to keep its employees on the company's side or to argue that they have gone rogue. This will not be an easy task for practitioners, especially when the employee in question is yet to tell the company of relevant facts in an investigation.

IV. CONCLUSION

On the whole, the Tribunal's interpretation of the Competition Ordinance in the Nutanix judgment is consistent with internationally accepted principles of competition law. However, it is to be expected that each jurisdiction will have its own approach to certain issues, and Hong Kong is no exception. This article discussed three key points in which the approach taken in Nutanix might not be expected to a seasoned competition practitioner outside of Hong Kong. No doubt practitioners will uncover more challenges as they consider the significance of the Nutanix judgment in future cases and as the competition law in Hong Kong continues to develop.