

China in focus

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ANTITRUST ALERT

China's Antitrust Enforcement Authority shows its teeth

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When China announced that it would divide responsibility for enforcement of its first ever Anti-Monopoly Law (the "AML") between three separate governmental bodies (the State Administration of Industry and Commerce, or "SAIC", the Ministry of Commerce, or MOC, and the National Development and Reform Commission or, "NDRC"), many were concerned that this would lead to dilution of the power that one single enforcement authority may have been able to wield. Now, with the publication for public comment of its draft Guidance on Monopoly Agreements and Abuse of A Dominant Position, one of the three agencies – the SAIC – is beginning to show how it will meet the challenges of implementation of the AML.

The two papers published by China's SAIC on 27 April 2009 clarify the meaning of "Dominant Markets" and "Monopoly Agreements" and thus how SAIC intends to wield its new powers. A deadline of 31 May 2009 has been set for the submission of any public comments.

SAIC was empowered by the AML to handle cases relating to the abuse of dominance and administrative monopolies, as well as non price-related anti-trust cases. These two draft public consultation papers are the first papers to be published by SAIC since the AML became effective in August 2008.

1. Abuse of a Dominant Market Position

The first consultation paper – entitled Rules on the Prohibition of Abuse of a Dominant Market Position (the "Draft Dominant Position Rules") – defines what is considered to be a dominant market position and those activities that may constitute an abuse of a dominant market position.

Dominant Market Position

Under the Draft Dominant Position Rules, a party is said to have a dominant market position if it is able to:

- control the price or quantity or other factors that affect market transactions, or
- prevent the entry of new companies into the market within a reasonable time by setting barriers to that market or increasing the cost of entry.

In deciding whether a dominant market position exists, SAIC will consider factors such as the market share and status of the competition, the ability of a business operator to control the market, the financial and technological circumstances of an operator, the level of reliance placed upon the operator by other business operators and the degree of difficulty of another business operator entering the relevant market. Compared with previous guidance issued under the AML, the Draft Dominant Position Rules provide a more comprehensive guide on the technical assessment of how a dominant market decision is made, and they are broadly consistent with international practice.

Presumed Position of Dominance

In keeping with the provisions of the AML, SAIC will presume a dominant market position to exist in cases where a company controls half of the relevant market. When partnered with another firm this threshold rises to two-thirds and when there are three companies involved it increases again to a market share of three quarters of the relevant market. However the Draft Dominant Position Rules allow a company to rebut this presumption if it is able to show that it is relatively easy for a new party to enter the market, that there is substantial competition between firms in a dominant position and that they have no ability to control the price and quantity of commodities.

According to these draft rules, any company with a market share below one tenth of the relevant market will not be presumed to have a dominant market position.

Abuse of a Dominant Position

The Draft Dominant Position Rules state that businesses with a dominant position in the relevant market shall not “without fair reason”:

- refuse to enter into a transaction with a party;
- refuse to let other business operators use their networks or other necessary facilities under reasonable conditions;
- require parties to transact only with them or with selected counterparties;
- enter into tying arrangements in relation to two commodities; or
- impose differing terms discriminating between counterparties in like transactions.

The caveat that a business may conduct not these activities “without fair reason” means that the activities are not wholly prohibited and that a business in a dominant position may conduct such activities where a legitimate “fair reason” exists. No definition of “fair reason” has been proposed by the SAIC in the Draft Dominant Position Rules but they do state that businesses suspected of abusing a dominant market position may justify their actions by providing evidence to SAIC.

Compared with AML, the Draft Dominant Position Rules provide more a comprehensive guidance on how abusive behaviour should be determined. For example, the draft rules make it clear that factors such as transaction volume, quality grade, payment terms, delivery terms and after-sales services, etc., must be considered before discriminatory treatment can established. However, the draft rules do not provide any guidance on predatory pricing issues, which are specified by the AML as one of the abusive behaviours. Many observers hope that these issues can be clarified by NDRC who is in charge of pricing related antitrust issues.

Investigation and Penalties

The Draft Dominant Position Rules authorise SAIC to handle investigations on abusive activities that have significant nationwide impact, and any other cases that SAIC consider fall within its jurisdiction. The draft rules also authorise SAIC to delegate its power to its local branches to handle cases that occur at a local level. There are many concerns that the local branches of SAIC, who have in the past taken an aggressive approach in applying penalties and fines, may need time to familiarise themselves more with the technical aspects of competition law. The Draft Dominant Position Rules do not provide details on the procedural rules in dawn raid scenarios; these may have been reserved for further AML implementing guidance.

Under the Draft Dominant Position Rules SAIC may order any business operator found to be in breach of the rules to stop the violating activity, confiscate any illegal earnings and impose a fine ranging between one and ten per cent of the prior year's turnover of the breaching company.

2. Monopoly Agreements

The second draft consultation published by SAIC is entitled Relevant Provisions on the Provision of Acts involving Monopolistic Agreements (the "Draft Monopoly Rules"). In these rules SAIC set out what monopoly agreements are, which type of agreements are prohibited and SAIC's authority to punish such agreements.

What are Monopoly Agreements?

The Draft Monopoly Rules explain that monopoly agreements may be written or oral agreements and decisions, or even a "tacit understanding" or "concerted act" between two parties without an express agreement being in place. In order to decide whether a "concerted act" has occurred, the SAIC will look at the behaviour of the parties, whether there is any justification for such action in the market, and whether there are any market structure issues or changing market conditions that must be considered.

What Monopoly Agreements are prohibited?

Relating to horizontal agreements, the Draft Monopoly Rules confirm that competing companies are prohibited from entering into the monopoly agreements that:

- restrict the production or sales volume of commodities;
- divide up the market, sales territory or customer base;
- restrict technological development or the application of new technologies;
- contain collective boycotts, including refusals to buy from, sell to or supply a specific supplier; or
- include evidence of "bid-rigging" between businesses that amounts to collusion on who among them will be the successful bidder in particular tender.

Relating to vertical agreements, business entities and their partners in transactions are prohibited from entering into the agreements that:

- provide preferred bidders with access to information relating to the tender during a tendering process which may amount to "bid-rigging";
- contain, without valid reason, vertical arrangements that require counterparties to trade with specified business entities or third parties or within a specified geographical market;

For both categories there is also a "catch all" clause which gives the SAIC power to determine whether there are any other monopoly agreements that are not specified by the draft rules. This means that firms should be vigilant in ensuring that they are aware of any future action by the SAIC that may impact on their contracting practices.

Trade associations

Trade associations are also prohibited from organising business entities to participate in monopoly agreements. The Draft Monopoly Agreement Rules state that trade associations should not make any rules or decisions that restrict competition, should not convene meetings to discuss and reach monopoly agreements or provide conditions that facilitate business entities to enter monopoly agreements. Once again SAIC have inserted a "catch all" that prohibits any other methods that it determines may encourage or facilitate monopoly agreements.

Exemptions

Certain monopoly agreements may be exempt under Article 15 of the AML. Agreements that develop new products or standards, improve technology and quality of products, improve the operational efficiency or competitiveness of small and medium undertakings or protect the public interests of China will not be subject to the restrictions of the Draft Monopoly Rules. In order to qualify for the exemption a business must prove that the agreement does not substantially restrict competition and that consumers will benefit from the agreement.

Penalties

As with under the Draft Dominant Position Rules, SAIC may require that any company engaging in a monopoly agreement ceases operating such an agreement and may impose a fine ranging between 1 per cent and 10 per cent of the company's sales turnover for the previous year. Where a monopoly agreement has been agreed but not yet implemented by the parties, a maximum fine of RMB500,000 may be imposed on the businesses.

The Draft Monopoly rules allow businesses that do not accept a penalty imposed by SAIC to apply for administrative review or to take legal action through the courts.

Leniency

The Draft Dominant Position Rules look to bridge the gap with the AML on leniency. If a participating business, other than the organiser or initiator of the monopoly agreement, provides SAIC with "relevant information" and "material evidence" relating to the existence of monopoly agreements, then SAIC has the discretion to reduce the administrative penalties imposed upon such party. "Material evidence" is defined as enough to spur SAIC to initiate an investigation or evidence which plays a crucial role in determining the existence of a monopoly agreement and details such as the products involved and the type of agreement.

The exercise of such leniency by SAIC is dependant on the timing of any report by a business operator and the importance of any information it provides, and if the informant is the first to report the existence of a monopoly agreement it may receive a complete immunity from the penalty.

SAIC will use the following tariff for applying discounts to the penalties imposed on businesses who report monopoly agreements:

When Informant reports to SAIC	Discount of Penalty Imposed
First to report a monopoly agreement on its own initiative	100 per cent
Second to report a monopoly agreement on its own initiative	50 per cent
Third to report a monopoly agreement on its own initiative	30 percent

It is important to note that the leniency scheme does not apply to the organiser or initiator of a monopoly agreement or a company who compel others to reach a monopoly agreement.

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