

Chinese pharma company fined for refusal to supply downstream competitors

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On 22 December 2015, the State Administration for Industry and Commerce ("**SAIC**") published [the decision](#) of its local branch in Chongqing ("**Chongqing AIC**") against pharma company Chongqing Qingyang Pharmaceutical Co., Ltd. ("**Qingyang**") for refusal to deal in breach of China's Anti-Monopoly Law ("**AML**").

The background

Qingyang is a manufacturer of both allopurinol active pharmaceutical ingredients ("**API**") and allopurinol drugs. Allopurinol API is an essential ingredient for the production of allopurinol drugs. Allopurinol drugs are used to treat gout, a type of arthritis disease.

Before September 2013, Qingyang used around 10% of its allopurinol API production to manufacture allopurinol drugs itself, while the remaining 90% were sold on the market to seven competing allopurinol drug manufacturers.

The conduct targeted in the antitrust enforcement action started in September 2013, when Qingyang entered into a five-year distribution arrangement with Xiangbaihe, a pharmaceuticals distributor. The agreement was to take effect from December 2013 when Xiangbaihe would become Qingyang's exclusive distributor in China. The agreement also stipulated that, during a "buffer period" from October to December 2013, Qingyang would not supply any allopurinol API to third parties without Xiangbaihe's approval.

As a result of the agreement with Xiangbaihe, Qingyang stopped supplying allopurinol drug manufacturers with allopurinol API from October 2013, until March 2014, and rejected various purchase orders. Instead, Qingyang ramped up its own production of allopurinol drugs, increasing its market share to close to 60%.

The investigation into Qingyang's activities started after the company itself approached the Chongqing AIC to check whether the practices are compliant with the AML. The Chongqing AIC found they were not.

The ruling

In its decision of 28 October 2015 – but which was only made public on 22 December – the Chongqing AIC held that Qingyang had committed an abuse of dominance by way of "refusing to deal." The refusal to deal consisted of Qingyang's refusal to supply allopurinol API, as an indispensable input, for the production of allopurinol drugs. In reaching that conclusion, the authority followed the standard steps in abuse of dominance cases: relevant market; dominance; abuse; justifications; and effects.

In terms of market definition, the authority conducted a relatively detailed analysis into the pharmacology and prices of allopurinol drugs and other drugs used in the treatment of gout, and found them not to be sufficiently substitutable with each other. Allopurinol API was found to be an indispensable input for the production of allopurinol drugs. As a result, the Chongqing AIC concluded that the Chinese allopurinol API market was the relevant market in this case. The dominance analysis of the authority showed that Qingyang did not have any domestic competitors, in part due to the lack of governmental authorization for the import of foreign allopurinol API. On the basis of a 100% market share and other factors, the Chongqing AIC found Qingyang to have a dominant position.

Analyzing Qingyang's conduct, the Chongqing AIC held that the company had abused its dominance in the upstream market (allopurinol API) to exclude competition in the downstream market (allopurinol drugs). During the six months of the contested conduct, four out of the seven competing allopurinol drug producers stopped production or switched to other products as a result of Qingyang's refusal to supply the required input. In contrast, Qingyang's downstream market share was estimated to rise from around 10% before the conduct to around 57% within one year after.

The authority also spent some time analyzing the actual effects of the abusive conduct, and held Qingyang's behavior to have caused significant harm to the market, the industry and customers. The regulators found that prices for allopurinol API had increased from 240/kg to 535/kg, and were eventually passed on to end customers purchasing allopurinol drugs.

As a result, the Chongqing AIC imposed a fine of approximately RMB 440,000 on Qingyang, representing 3% of the company's aggregate sales revenues in the upstream and downstream markets in 2013.

Impact

The Chongqing AIC's decision is important from several aspects. First, the pharma sector continues to be under spotlight for antitrust enforcement in China. In August 2015, another Chinese antitrust authority – the National Development and Reform Commission ("**NDRC**") – challenged the anti-competitive conduct by a local government body in Anhui in the course of the government drug procurement process (see [here](#)). Later on, in November 2015, NDRC took antitrust actions against similar conduct by government branches in Sichuan and Zhejiang.

From these developments it becomes clear that the pharma sector continues to be under close scrutiny by antitrust regulators. The background is, in part, that in May 2015 the Chinese government started to liberalize drug prices and may view antitrust as a tool to intervene in the event of unwanted price increases as the reform takes pace.

Second, the *Qingyang* case is the first published decision by SAIC or its local offices finding a refusal to deal in breach of the AML, and one of the very few refusal to deal decisions by antitrust authorities and courts in China more generally.

Refusal to deal is a hotly debated issue in antitrust circles, not least in the pharma industry with its extensive R&D efforts and intellectual property rights. The future will tell whether the *Qingyang* decision remains an isolated case, or herald a more frequent use by antitrust authorities of the AML's refusal to deal provision.

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