

## ANTITRUST LAW

### China's Anti-Monopoly Law

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On Aug. 30, the Standing Committee of the 10th National People's Congress adopted the Anti-Monopoly Law of the People's Republic of China. The AML will become effective on Aug. 1, 2008, to guard against monopolistic conduct, safeguard competition, improve economic efficiency, protect public and consumer interests, and promote the healthy development of the socialist market economy. After 13 years of debate, the final adoption of the AML marks an important step toward an effective competition regime in China's move toward a market economy. The AML's main outline is similar to competition laws in other countries because the drafting committee conducted extensive studies of foreign laws and had many discussions with foreign experts, but it also maintains some "Chinese-specific" provisions.

The AML legislative process began in 1994. Prior to the adoption of the AML, several regulations addressing competition issues already existed. For example, the Anti-Unfair Competition Law prohibits utility companies or companies that hold a lawful monopoly from requiring their trade partners to use certain designated suppliers. The Interim Provisions on Prohibition of Acts of Price Monopoly bans price-fixing, dumping and price discrimination. The Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors requires foreign investors to notify proposed transactions to the Ministry of Commerce (MOFCOM) and other agencies, and guidelines clarify the procedures and filings required by MOFCOM when implementing the M&A provisions. Also, a number of local regulations supplement national legislation. Yet no comprehensive competition law existed.

After its accession to the World Trade Organization, China stepped up its efforts to create a competition law. In early 2004, a draft AML was submitted to the State Council. Chinese authorities have attached great importance to this project, and have been receptive to suggestions by both foreign and domestic experts.

The AML is comprised of eight chapters and 57 articles. It applies not only to conduct in China, but also to conduct outside China that affects competition within China. Conduct covered by the AML includes monopoly agreements, abuse of dominant market position and transactions that may restrict competition.

#### **Both horizontal and vertical agreements are covered**

"Monopoly agreements" under the AML include both horizontal and vertical agreements. Prohibited horizontal agreements include price-fixing; output or sales volume restrictions; market division; restricting the purchase or development of new technology, equipment or products; and boycotts. Vertical monopoly agreements include minimum resale price-fixing. The law in most jurisdictions recognizes that vertical agreements are less likely to be anti-competitive. It is uncertain whether that distinction exists in the AML. This needs to be further clarified in the implementation rules. The AML also sets out a list of activities that are exempt from the prohibition on monopoly agreements, such as agreements to improve technology and develop new products.

- *Dominant position.* Under the AML, an undertaking has a dominant market position if it is able to control the price or quantity of goods, or if it can block or affect other undertakings' access to the relevant market. Relevant factors include market share and entry barriers — a dominant position is presumed from a 50% market share. Article 19 of the AML also applies to joint dominance. Abuses of dominant market position include sales at an unfairly high price or below cost, purchases at an unfairly low price, refusing to trade, tie-in sales, exclusive dealing and other discriminatory treatment.

The AML specifically states that it does not apply to efforts by undertakings to protect their legitimate intellectual property rights in accordance with IP laws and regulations, although it does apply to abuses of IP rights to eliminate or restrict market competition. But it is uncertain how these provisions will be interpreted.

- *Concentrations.* Concentrations under the AML, which must be notified prior to closing, include mergers, acquisitions of shares or assets, and contracts to acquire control over other firms. Under Article 21, undertakings involved in such transactions must make advance filings and await clearance prior to closing. All filings are subject to an initial 30-day review period and a possible additional 90-day investigation (extendable by a further 60 days under certain circumstances). The factors to be considered include the market shares of the involved parties, entry barriers and the effect of the concentration on consumers. The AML makes it clear that foreign transactions would be subject to review if they involve national security.

When the AML takes effect, it will replace the low thresholds in the current M&A provisions — which can trigger a filing even if the transactions have minimal impact on the Chinese market — with higher thresholds to be set later. Unlike the existing M&A provisions, the AML clearly sets out the penalties for failure to file. Unlike the current "negative approval" mechanism, under the AML, authorities must make a decision whether to investigate within 30 days after filing and they must notify the undertakings of their decision.

The Anti-Monopoly Commission will be in charge of general policy under the AML, while it will be enforced by enforcement authorities designated by the State Council. It has long been assumed that the agencies that have existing anti-monopoly functions, such as MOFCOM, the State Administration of Industry and the Commerce and National Development and Reform Committee, will jointly form such agencies. But such a multiagency regime without a court supervision is unlikely to be effective, so it would be preferable to designate one authority. It is highly advisable to clarify the power, scope and relationships among the agencies.

Antitrust authorities are granted extensive powers to conduct on-site examination; review contracts, correspondence, and financial data; and question the parties. But the AML also establishes protective procedures, providing, e.g., that at least two law enforcement officials must be present and take written minutes of the investigation. Targets also have the right to submit their position, and presumptively dominant firms can submit rebuttal evidence. The anti-monopoly authorities can suspend the investigation if the undertakings admit to the alleged monopolistic conduct and accept adequate remedies supervised by the authorities.

The AML establishes civil and administrative liabilities for violations, but does not adopt criminal penalties. Remedies include cease-and-desist orders, confiscation of illegal gains and fines of 1% to 10% of the total sales volume in the previous year. In the case of a transaction, the authorities can prohibit the transaction, require sale of stock or assets or impose other remedies to restore competition and may also impose a fine of less than 500,000 yuan. Individuals and

companies that do not cooperate with the anti-monopoly authorities are subject to administrative penalties and criminal liabilities.

### **The AML will regulate administrative monopolies**

Chapter 5 of the AML applies to administrative monopolies, which indicates that the Chinese government intends to try to create a level playing field. They are prohibited from limiting or restricting competition, such as requiring consumers to purchase or use products from certain designated enterprises, or imposing discriminatory measures that unfairly favor local businesses. Because of China's planned economy, administrative monopolies have been regarded as a serious obstacle to competition in China. It is uncertain how effectively the AML can control administrative monopolies and state-owned enterprises (SOEs). The AML offers protection to industries dominated by SOEs viewed as critical to China's national economy and national security. However, the AML also states that SOEs shall not abuse their position to harm consumers. How these provisions will be harmonized and implemented is far from clear. There is also concern that the AML will not have "real teeth" in industries in which SOEs have a dominant position. Historically, trade associations have controlled the prices of some commodities, but the AML prohibits them from organizing monopoly agreements, with penalties of up to 500,000 yuan and de-registration.

AML Article 11 is the first time that a national security review has been specifically authorized by statute, which clearly spells out that such a review is separate from anti-monopoly review. Yet it is uncertain which authority will conduct such a review, what would trigger one and how one will be conducted. This uncertainty increases the risk for foreign investors.

In sum, the AML will have significant implications for foreign investment and business operations in China. On the one hand, it may assist foreign investors by providing uniform and comprehensive guidelines on competition. The regulation of administrative monopolies law could help multinational companies compete fairly with local companies. On the other hand, it may subject multinational companies to uncertain enforcement and harsh penalties, and there are concerns that Chinese firms may be favored. Special attention should be paid to the competitive impact of proposed deals by foreign firms in China. The extra-jurisdictional aspect of the AML also could be important. Foreign companies in China should review their Chinese operations for compliance with the AML and consider the AML in planning deals, and it is especially important that they monitor the development of the AML and its implementation rules.

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