Two steps forward, one step back

The proposed amendments to China's Anti-Unfair Competition Law

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On 25 February 2016, the Legislative Affairs Office of the State Council – China's "cabinet" – published a draft (the Draft) of the proposed amendments to the Anti-Unfair Competition Law (AUCL) and invited comments by stakeholders.

Draft in a nutshell

The AUCL contains a potpourri of provisions aimed at protecting fair competition, and covering legal fields such as intellectual property and commercial bribery, as well as antitrust. It was enacted in 1993, at the initial stages of China's economic reform under Deng Xiaoping. After more than 20 years of implementation, the market practice has evolved and new rules – for example, the Trademark Law and the Anti-Monopoly Law (AML) – have been enacted to regulate the areas covered in the AUCL.

The Draft proposes an important overhaul of the current law, especially in the fields of antitrust, intellectual property and anti-bribery. It aims to bring the AUCL more in line with recent domestic legislation and more in sync with international legal standards, and to codify existing case law and practice.

The proposed AUCL amendments have implications far beyond the antitrust arena. For instance, in the IP field, the Draft improves the AUCL's protection over those rights that cannot benefit from registration with the authorities, such as unregistered marks, trade dress, product packaging and trade secrets.

In the anti-bribery field, the Draft brings the Chinese anti-bribery laws into line with well-recognised international standards. For example, while the AUCL currently prohibits bribe payments made in order to "sell or purchase products," the Draft expands the definition of "commercial bribery" to conduct whereby "economic advantages" are provided or promised to third parties, in order to secure opportunities or competitive advantages.

In the antitrust arena, the Draft also promises to bring substantial changes, as set out below.

Alignment with the AML

As mentioned, the AUCL was enacted long before the enactment in 2007 of the AML, which is generally more in line with up-to-date international antitrust practices. It is against this background that the Draft proposes to delete a few antitrust provisions from the AUCL to avoid overlap and inconsistency with the AML.

In particular, while there are subtle textual differences between the two laws, both the AUCL and the AML ban predatory pricing, tying and the imposition of unreasonable transaction conditions. But unlike the AML, the AUCL does not require demonstration that the company at issue has a dominant position for such types of conduct to be illegal. Hence, at this point in time, predatory pricing, tying and the imposition of unreasonable conditions can be illegal under the AUCL for any company, irrespective of its market position. By deleting the AUCL provisions, the Draft proposes to give the AML's text full meaning as the only applicable legal framework for these types of conduct.

The AUCL also singles out public utilities and other monopolies – mainly state-owned enterprises – by prohibiting them from engaging in exclusive dealing and tying. The background of this prohibition is that, back in 1993, the radical transformation of the Chinese economy within the framework of Deng Xiaoping's "reform and opening-up policy" was going ahead full steam. At that moment in China's reform process, the economy was largely dominated by state-owned companies, and specific regulation of their behaviour seemed appropriate.

In today's China, private enterprises play a much more important role than in 1993, and the legislator today may feel that it is no longer necessary to single out public utilities and state monopolies, as the AML should apply to companies irrespective of their ownership. As a result, the Draft also proposes to delete this provision from the AUCL.

Another set of overlapping provisions between the AUCL and the AML is in the area of "administrative monopoly" conduct, a term used in China to describe government's anti-competitive interference in the marketplace.

The current AUCL has a relatively high-level provision banning government bodies and assimilated agencies from abusing administrative powers to restrict competition, such as appointing exclusive suppliers or discriminating against non-local companies.

In turn, the AML contains an entire chapter on administrative monopoly, outlawing specific manifestations in quite some detail. As with the other above-mentioned provisions, the Draft resolves the discrepancies across laws by proposing to delete the AUCL provision on administrative monopoly, leaving the field to the more specialised provisions of the AML.

Overall, therefore, the Draft's deletions cut overlaps, ensure a higher degree of consistency between the AUCL and AML provisions and may thereby reduce uncertainty for businesses.

"Relatively advantageous position"

While the above deletions may bring more comfort to market players, article 6 of the Draft goes in the opposite direction.

Essentially, article 6 attempts to address situations where a company is not dominant, but has a "relatively advantageous position" vis-a-vis counterparties in the course of trade, and engages in certain activities deemed anticompetitive or unfair.

The threshold for the relatively advantageous position is clearly meant to be lower than that of "dominance." The Draft proposes to look at factors such as financial strength, technology, market access, sales channel or raw materials procurement to check if they create a relationship of dependence on the company by its trading partners. If so, the company may be deemed to have a relatively advantageous position.

Similar to the AML's abuse of dominance rules, the Draft does not prohibit companies from having or obtaining a relatively advantageous position as such. Only certain abuses of such position can be illegal.

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According to article 6, an abuse may take the shape of (for example) restrictions on the trading partners' business dealings with third parties; exclusive purchasing; abusive charges on (or requiring unreasonable economic benefits from) trading partners; or the imposition of unreasonable conditions.

The "relatively advantageous position" concept is fairly – though not completely – new in China. In the past, there were a limited number of similar rules in other pieces of legislation.

In particular, in 2006, the Chinese antitrust authorities – the Ministry of Commerce, the National Development and Reform Commission, and the State Administration for Industry and Commerce – and two other ministries jointly issued the Administrative Measures for Fair Transactions between Retailers and Suppliers. These measures aim to regulate the relationship between retailers – basically, large shops, supermarkets and chain stores – and individual suppliers. They contain a broad range of rules including the prohibition of unfair transaction practices by retailers vis-a-vis their suppliers by "abusing an advantageous position". In *Wumei v Lifeng*, a court applied this prohibition, holding that a big supermarket chain abused such an advantageous position by forcing "unconditional rebates" on its supplier.

Internationally, China is not completely isolated with the proposed relatively advantageous position draft: Germany, Japan and Korea have similar rules. In fact, article 6 in the proposed AUCL amendment draws heavily on German – and to a lesser extent – Japanese and Korean competition laws.

From an enforcement perspective, the experience in these jurisdictions suggests that proving a relatively advantageous position (or similar concept) is often easier than proving a dominant position. Broadly speaking, the former often only requires a comparison between the relative positions of the trading parties involved, while the latter typically demands an overall market assessment.

Among the jurisdictions with rules similar to the Chinese relatively advantageous position concept, some enforce the rules more actively than others – for example, in Korea, the Korean Fair Trade Commission (KFTC) reportedly prosecuted over 3,000 cases from 1981 to 2014. The 2007 *Posco* judgment by the Supreme Court, overturning a KFTC abuse of dominance decision, may have led to a further shift of focus on abuse of "superior position" cases with their relatively lighter burden of proof (as opposed to abuse of dominance cases).

If the Draft's proposals remain in the final amendment of the AUCL and are enforced vigorously in practice, the impact of article 6 on companies doing business in or with China could be far-reaching. While the relatively advantageous position concept may potentially be beneficial to small(er) companies, it risks creating a new level of rather opaque compliance obligations on larger companies. Moreover, the penalties for breaching article 6 can be high. The Draft provides for fines of up to five times the "illegal revenues," a concept not explained in the Draft. If those revenues cannot be determined, a statutory fine ranging between RMB100,000 and RMB3m can be imposed.

Unfair competition in the internet sector

Other antitrust reforms can be found in the Draft's new rules on unfair competition between internet companies.

Over the past few years, many of China's largest internet and ecommerce companies were entangled in legal disputes with each other. Most of these disputes were channelled through the Chinese court system. The disputes involved new types of unfair competition conduct such as adblocking; enabling users free access to others' non-free content; and inducing users of other products to use one's own products.

Given the lack of specific rules on internet-based conduct in the AUCL, the Chinese courts dealt with these cases on the basis of article 2 of the AUCL, a provision referring to high-level principles such as voluntariness, equality, fairness, honesty and good faith. From these principles, the courts developed other, more concrete principles – such as "non-interference" with the legitimate operations of competitors – though the case law is uneven across different courts in China.

Now the Draft attempts to codify some of the existing case law on unfair competition in the internet arena – drawing on the courts' experience from (among others) the *Qihoo 360 v Tencent* and *Tencent v Sogou* cases – by inserting a specific provision applicable to internet disputes.

In particular, article 13 of the Draft incorporates the non-interference principle into the AUCL, prohibiting companies from "interfering" with users' options or other companies' normal business operations by using network technology or app services. Without prior consent, companies are prohibited from using technical methods to stop users from using other companies' online services; inserting links in others' online services to force skipping to targeted content; misleading, cheating or forcing users to revise, close, uninstall or stop the normal use of online services legally provided by others; or interfering with, or destroying, the regular operations of online services legally provided by others.

In general, the insertion of article 13 is an understandable attempt to make sure the rules are applied consistently among courts and authorities. At the same time, the internet industry is a vibrant sector with fast-moving technologies and business practices and the provision in the Draft risks becoming outdated quickly.

Conclusions

The Draft may be seen as an attempt by the Chinese government to modernise Chinese unfair competition rules. If the proposals in the Draft are enacted, the AUCL's rules would be brought more in line with other Chinese legal texts, such as the Trademark Law or the AML, and – to an extent – international practices.

From an antitrust perspective, seeking to align the AUCL and the AML is surely laudable, and the abrogation of prohibitions of predatory pricing, tying and imposition of unreasonable conditions by companies irrespective of their market position appears to make sense. At the same time, the introduction of the new concept of a "relatively advantageous position" may add significant compliance obligations for companies and hence risks significantly reducing the benefits of the AUCL reform.

The new provision on unfair competition conduct in the internet space provides the benefit of codifying – and thus streamlining – existing case law, but its static nature may freeze developments at a particular moment in time.

Looking ahead, the State Council has already collected stakeholder feedback on the Draft. As a next step, the Draft may either be further amended (and potentially circulated for comment again) or be directly sent to the Standing Committee of the National People's Congress for enactment.