NDRC's Antitrust Crackdown Continues and its Scope Broadens

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On September 4, 2013, the Guangdong Price Bureau issued its decision to fine two river sand companies for antitrust-related offenses. The Price Bureau acts as the local office of the National Development and Reform Commission ("**NDRC**").

The offenses found – abuse of dominance in violation of the *Anti-Monopoly Law* ("**AML**") by way of 'excessive pricing,' and 'hoarding' supplies in violation of the *Regulation on Administrative Penalties for Illegal Pricing Conduct* ("**Illegal Pricing Regulation**") – shows the way in which the scope of NDRC's antitrust investigations seems to be widening.

The facts

The actions that led to the case occurred in Shaoguan, a city with around 2.8 million inhabitants that is geographically parcelled into sub-divisions (that is, districts or counties) including Qujiang District. Two companies in Shaoguan were found to have stockpiled supplies of river sand – a material that is extracted from river beds and typically processed near the river to serve as construction material – during the period from 2011 to 2013 and to have raised prices sharply. The two companies were reported to belong to the same individual, and hence NDRC seems to have treated them for regulatory purposes as a single 'business operator.'

The investigation was initiated under the instructions of the governor and the deputy governor of Guangdong Province. The press release issued by the Price Bureau indicates that over the past two years, the construction of expressways and other key construction projects were delayed due to the scarcity and high prices of river sand. Following the high-level instructions, the Price Bureau initiated an industry-wide investigation into the pricing of river sand in Guangdong. The alleged antitrust violations and the companies were targeted as part of the investigation.

The decision

The Guangdong Price Bureau found that the companies had committed two separate offenses. First, they had infringed the prohibition under the AML on companies with a dominant market position charging "unfairly high prices."

The Price Bureau first looked at the specificity of river sand, finding that long-distance transportation was not economical and that the relevant geographical market for sales of river sand would be in the area located within a certain distance from the sand processing plant. Without further explanation, the Price Bureau looked at Qujiang District, within the city of Shaoguan, and concluded that the two companies had an aggregate market share of over 75% and hence held a dominant market position in that (very small and specific) geographical market.

Then, the Price Bureau compared the companies' price rise (54.4%) with the increase in costs (over 20%), as well as the companies' price levels with those prevalent in other river sand markets. The Price Bureau found that the differences demonstrated the excessiveness of the price charged. In the authority's view, this conduct amounted to an abuse of dominance in violation of the AML, and imposed a fine on the companies equivalent to 2% of their annual sales revenues.

Second, the Price Bureau also objected to the 'hoarding' of supplies of river sand. The authority found that there was a scarcity in supply due to quota controls and licensing requirements of the government. As a result, river sand was normally sold shortly after extraction, and the storage cycle was generally shorter than two years. The companies' hoarding reportedly led to an artificially exacerbated scarcity in supply, and strong price fluctuations. The authority held this to be a violation of the Illegal Pricing Regulation, which was issued to implement the Price Law – another statute with antitrust and antitrust-related provisions. The remedy against this offense was to order the companies to sell off the excess stock at capped prices within six months.

Analysis

As the Guangdong Price Bureau's press release points out, the decision was adopted following consultations with NDRC in Beijing. Hence, to a large extent, this decision can be interpreted as reflecting NDRC's own thinking and approach.

This case is important in many respects. First, it illustrates the increasing breadth of the investigations launched by NDRC and its local offices. In the first few years after the AML came into effect, NDRC's main focus was clearly on curbing cartel activities. This has been changing gradually; the record fine imposed on six baby milk formula suppliers for resale price maintenance – a vertical restraint – on August 7, 2013 is a clear sign of that change.

The *River sand* case is the first decision in the public domain where NDRC directly relied on the AML's 'excessive pricing' prohibition. So far, this much-commented-on prohibition has not played a major role in AML enforcement actions – with the exception of the *Huawei v. InterDigital* case, where a Shenzhen court ruled that the US patent holding company had made excessive demands for royalties and other licensing conditions and thereby breached the prohibition.

It is clear, however, that the 'excessive pricing' provision in the AML could be a very powerful weapon for antitrust regulators to intervene in the market. Companies will no doubt be following carefully how Chinese regulators and courts will use this provision going forward – for example, if the provision will be invoked in cases involving allegedly excessive royalties in the intellectual property rights licensing context.

A second interesting point in the *River sand* case is that, as noted above, the relevant geographic market was defined extremely narrowly – Qujiang District in the city of Shaoguan. Qujiang District, one of the 10 sub-divisions of Shaoguan, is an area of around 1,600 square kilometers that is not clearly (for example, topographically) separated from Shaoguan's other districts. There appear to be other river sand extraction and processing sites in Shaoguan.

If future enforcement activities show that NDRC and/or its local branches are prone to define markets very narrowly, then the thresholds for them to apply the abuse of dominance rules in the AML will be significantly lower. Leading on from this, many companies may find themselves in the line of sight from NDRC in the future even if they have a high market share only in a relatively circumscribed geographical area: they will need to step up their compliance efforts to screen whether their business conduct complies with those rules, even when they have never previously thought of themselves as being 'dominant.'

Third, this case shows that political considerations may be an important driver of antitrust enforcement. In China, infrastructure projects are widely favored by local governments as a convenient tool to boost the growth of local GDP. As a result, antitrust authorities have frequently targeted suppliers of building materials to drive down prices or otherwise ensure steady supplies of building materials. As noted, this case was launched 'from on high,' as the governor and deputy governor of Guangdong Province themselves called for the investigation into the river sand industry. In that way, it is similar to the NDRC investigation into sea sand suppliers, which also started upon the initiative of the governor of Guangdong Province.

More generally, the general sentiment in China is that targeted law enforcement in many key, sensitive areas – ranging from transfer pricing and anti-corruption to antitrust law – has now moved to near the top of the political agenda.

A final takeaway from the *River sand* case is that the decision once more confirms that the Price Law continues to apply in parallel to the AML. Five years down the road, it remains clear that Chinese antitrust enforcement does not simply revolve around the AML. This in practice enables NDRC to choose to apply the AML, the Price Law – or both – as it deems appropriate in particular cases to achieve its own regulatory goals.

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