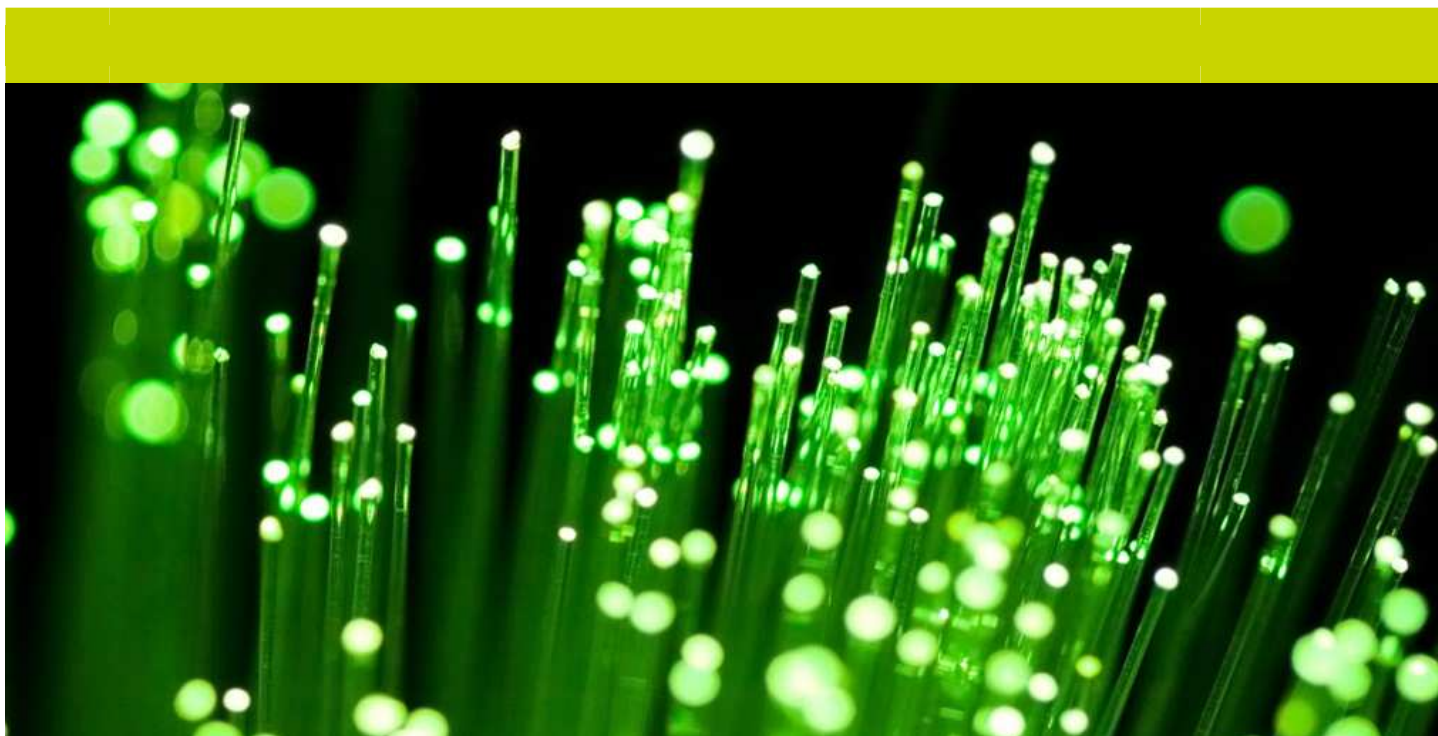


## **Antitrust Issues Continue Flaring up in China's IT Sector**

February 2013



**Further information**

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This note is written as a general guide only. It should not be relied upon as a substitute for specific legal advice.

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## Antitrust Issues Continue Flaring up in China's IT Sector

On 30 and 31 January 2013, the State Administration for Industry and Commerce ("**SAIC**") posted a press release and a brief question-and-answer protocol ("**Q&A**") on its website to inform of a recent enforcement action. According to these documents, SAIC's local branches in Beijing had issued a notice to the Chinese software company Qihoo 360 a week earlier, warning the company about its allegedly unfair competition practices.

While the immediate implications of this "warning" notice are not entirely clear, the case is symptomatic for the current state of the Chinese IT sector. SAIC's "warning" notice may not be the last word in this case.

### The "warning" notice

According to the press release and the Q&A, Qihoo 360 has a market share of over 80% in the "security software market" in China. The local SAIC branches in Beijing –the Administration for Industry and Commerce ("**AIC**") of Beijing and a district of Beijing– found that Qihoo 360 had used this "monopolistic market advantage" to induce users of its security software (such as anti-virus software) to use its own browser, and to impede security software competitors by making its own security software incompatible and difficult to uninstall.

According to the press release, the Qihoo 360 security software issues pop-ups when users rely on competing software –likely indicating that the competing software is unsafe. In addition, Qihoo 360 was allegedly sending software patches to install its browser and set a specific webpage created by it as the default home page on users' computers without seeking the users' consent. According to the press release, Qihoo 360 even disguised the software patches as being from Microsoft, which a spokesperson from Microsoft denied.

### In the footsteps of the European Commission?

The press release and the Q&A are brief, and contain only sparse information on the legal aspects of the case. As such, neither of the two documents states the exact legal basis for the authorities' action or the specific legal characterization of the conduct under scrutiny. An unnamed SAIC enforcement official mentioned the Anti-Unfair Competition Law, the Anti-Monopoly Law and the Law on Protection of Consumers' Rights by name –as falling under SAIC's jurisdiction– but no specific provisions in those laws were identified.

However, despite this general lack of information, it may still be possible draw some inferences from the published documents. In particular, it appears that one of the main issues in this case is that Qihoo 360 was found to have engaged in "tying." The authorities seem to allege that Qihoo 360 leveraged its market power in one market – security software, where the company reportedly has a market share over 80%– into other markets –such as web browsers.

On this aspect, the investigation against Qihoo 360 resembles the European Commission's cases against Microsoft. In those cases, the European Commission objected to Microsoft tying its Windows operating system with other products, namely its media player and its browser. The methods Qihoo 360 allegedly employed in its tying practice are similar to those in the *Microsoft* cases –for example, technical tying through default installations, at no charge to users.

Another allegation in the SAIC press release is also similar to the European Commission's cases against Microsoft –namely, that Qihoo 360's security software is not compatible with competing products. In *Microsoft I*, one of the main issues was whether Microsoft was obliged to release data allowing companies offering competing work group server operating systems to ensure interoperability with its Windows operating systems.

SAIC did not explicitly mention the possibility of Qihoo 360 arguing an objective justification for the design of its products.

### **SAIC assumes enforcement**

SAIC is the body responsible for implementing the Anti-Unfair Competition Law. It is also one of the three authorities with jurisdiction to enforce the Anti-Monopoly Law (in addition to the Ministry of Commerce and the National Development and Reform Commission). Under the Anti-Monopoly Law, SAIC and its local offices have powers to investigate and sanction anti-competitive agreements between market players and abuses of a dominant market positions, as long as the practices do not directly relate to pricing conduct.

"Tying" can be an offense under both the Anti-Unfair Competition Law and the Anti-Monopoly Law.

### **Soft enforcement in a rapidly changing environment**

One of the most interesting aspects of the investigation against Qihoo 360 is that the Beijing AIC issued an "administrative warning" (行政告诫). This is not equivalent to a formal sanction. The main applicable laws –*i.e.*, the Anti-Unfair Competition Law, the Anti-Monopoly Law and the Administrative Penalties Law– do not mention this feature. The rules by the Beijing AIC, which provide information on the "administrative warning" concept, indicate that this is a form of administrative guidance, and is not binding upon the companies concerned. The rules also state that the authorities should resort to "administrative warnings" in case of violations of the market order which no law explicitly governs, or minor violations of the market order where no express penalty provisions can be found in the law.

This background shows that SAIC and its local offices are following a "soft approach" in enforcing antitrust and unfair competition rules in the IT sector. The approach here somewhat resembles that in the antitrust/unfair competition dispute between Qihoo 360 and Tencent, another major Chinese software company. In that case, SAIC was reported not to take action after receiving a complaint by Qihoo 360. The result was that the two parties took their dispute to the Chinese courts.

Antitrust enforcement in the IT sector is challenging, as the underlying issues can be very technical and –perhaps more importantly– technological change can be very fast, hence adding to the complexity of the enforcement task.

Still, irrespective of the challenges for administrative enforcement, it becomes increasingly clear that the disputes in the Chinese IT/high technology space may continue and that the companies involved may need to seek other ways to solve such disputes. Hence, litigation in courts –in China and, perhaps, beyond China– may become a possible way for IT companies to air, and solve, their differences in the antitrust and unfair competition field.

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